

DIARY

Book 566.

September 2 - 4, 1942

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September 2, 1942

During the meeting last night, I asked Harold Graves to go into Mrs. Klotz's room with me as I wanted to have a quiet talk as to whether or not we should give up that part of the volunteer War Bond program which has to do with payroll deduction.

I started the discussion by saying, "Harold, I got a memo today showing that only about 1,400,000 to 1,500,000 workers in approximately 14,000 concerns are having 10% deducted from their pay. Is that correct?" He said, "Yes." I said, "Aren't you having a great deal of difficulty getting the bulk of the workmen in this country up to 10%?" and he said, "Yes." I said, "With the constantly increasing amount we have to pay out for the war, isn't it a fact that under the volunteer plan we haven't been able to keep up with it?" and he said, "Yes."

I then said, "Would you object very much if we abandoned the volunteer plan and go into either compulsory savings or post-war credit?" He said, "No, I have no objections. I only want you to be sure to get a good swap for what you are giving up." I said, "If I can get \$4,000,000,000 of non-negotiable, non-interest bearing securities through this tax on spending which would be refundable, isn't that a pretty good swap?" and he said, "Yes, it is."

I said, "Harold, I want to tell you now that nobody could have done any more than you have done on this, and I appreciate enormously what you have done." I said, "Furthermore, during this year the Treasury has been practically the only agency that has done anything to build up the civilian morale, and that you can never measure in dollars." Graves answered me by saying, "You have been more than kind to me all through this thing."

Naturally, I felt very badly about having to make this decision, but I felt the time had come inasmuch as I promised both the President and Congress that if we didn't make good I would be the first to say so, and I think it is up to me to do so now.

NOTE: This memorandum was dictated on the dictaphone by the Secretary at 6:30 a. m. this morning, Sept. 2.

Herbert Gaston
Ferdinand Kuhn

September 2, 1942

Secretary Morgenthau

In my statement for tomorrow, I'd like to say something like this:

"Gentlemen, I told you if at any time that I was worried about the financing, I'd come before you and say so. I am here today. I also told you that if I wasn't satisfied with the volunteer plan, I'd come before you and say so. I am here today. I can assure you and through you the country that I can continue to raise the stupendous sums necessary to finance the war for the balance of the year, but after the first of the year I will need additional revenue in order to carry out my responsibility. I also feel that the present bill as it passed the House ~~now~~ does not sufficiently reach the mass of the purchasing power, and that we in the Treasury must carry out our share of the responsibility to close this gap. Therefore, I have asked to come before you today to make the following suggestions" - and then go ahead and make the suggestions, and give them (1) the figure, how much additional revenue will be raised, and (2) how much of an inflationary gap can be closed through this suggestion. Close by saying that the situation is extremely serious and I feel that in order to keep the country on a sound financial basis this coming year, I've pretty much got to have what I'm asking for today. If Congress will give me this, I feel that I can carry on in the coming year.

Something along that line I think will do the trick. I wish that Kuhn and Gaston would drop everything that they are doing this morning in order to get this draft ready, and get somebody like Blough and Friedman to help them. Also, before I see it I'd like both Walter Stewart and Jake Viner to see it. I'll be ready for the last look at the first draft immediately after lunch. If possible, I'd like to have it before lunch to show it to Walter George. I think that that would be very helpful.

September 2, 1942
10:12 a.m.

Operator: Go ahead.

HMJr: Hello.

Randolph Paul: Hello.

HMJr: Yes.

P: This is Randolph Paul.

HMJr: Henry Morgenthau.

P: I'm with Senator George....

HMJr: Yeah.

P:and we've been discussing the situation, and the particular point I called you about at the moment was that he is tied up for lunch....

HMJr: Yes.

P:and he doesn't know how to get hold of the people that are going to meet him, and he wondered if he could come down after the hearing and see you about five o'clock.

HMJr: Surely.

P: Is that all right?

HMJr: Surely.

P: Well, all right, let's leave it that way then.

HMJr: At five o'clock?

P: We'll be there then at five o'clock.

HMJr: That's all right.

P: All right.

HMJr: Incidentally, I've cleared it with the President.

P: Oh, swell.

HMJr: Yeah.

P: Oh, fine. I'll tell the Senator that.

HMJr: Five o'clock.

P: Okay.

September 2, 1942.
10:23 a.m.

HMJr: Hello.

Claude
Wickard: Yes.

HMJr: Claude.

W: Yes, Henry.

HMJr: For your own ear only....

W: What?

HMJr: For your - confidentially.

W: Oh, yes, I get it.

HMJr: I feel quite encouraged after seeing the President....

W: Uh huh.

HMJr:that - I think he's going to listen to you
fellows and listen to the plan - hello....

W: Yes.

HMJr: But I think that there's - I - oh, I think there's
a 75 per cent chance. that he will go all out Monday
night.

W: He hasn't made up his mind yet?

HMJr: No, I said a 75 per cent chance.

W: Yes.

HMJr: But that's only for you. For God's sake, don't
tell anybody else.

W: I won't.

HMJr: But I thought I'd help you in your fight.

W: (Laughs) Well, thanks very much.

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HMJr: But I came out quite encouraged.

W: I see.

HMJr: Yeah.

W: Well, thanks for calling.

HMJr: Okay.

W: You bet.

September 2, 1942
10:52 a.m.

HMJr: Hello.
Operator: Judge Rosenman is in a conference now.
HMJr: Oh. Well, he left word he wanted to call me.
Operator: Yes, I know, and now Miss Hack says he's gone into a conference.
HMJr: Well, tell them to send a note in.
Operator: All right.
HMJr: Tell them to send a note in, please.
Operator: Right.

10:56 a.m.

HMJr: Hello.
Operator: Judge Rosenman.
HMJr: Hello.
Operator: Go ahead.
HMJr: Hello, hello.
Judge Rosenman: Henry?
HMJr: I'm holding butter. What are you holding?
R: What?
HMJr: I'm holding butter. What are you holding?
R: In my mind's eye - ah - you know, Hedy.
HMJr: Okay. (Laughs)

- 2 -

R: Hey, two things, first of all, I stayed behind and talked and I think you made quite a dent. I think he's pretty well convinced.

HMJr: Oh, wonderful.

R: It may change when that thing comes in, and (2) if you're going to be up there, you'd better be prepared some time or other to go over this tax portion of it.

HMJr: Well, I'd like to very much.

R: I don't know whether you'll need Paul up there or not, but....

HMJr: Well - well, I - I....

R:he has - he said it's too long now and he wants to talk about it generally. Well, you know he gets some general over-all stuff that may disagree with what you fellows are doing.

HMJr: Now this isn't a bribe, see? But it's corn time at Fishkill Farms.

R: (Laughs) Yeah, well - well, I'm more interested in that than in Hedy Lamarr, I'll tell you that.

HMJr: (Laughs) Sez you.

R: Yeah. (Laughs) Okay.

HMJr: I'm not trying to butter you with corn, see?

R: Yeah, well, I hope - I hope you are.

HMJr: Well, now let's leave it this way, if there's any change you'll let me know, maybe I could put in my two bits again?

R: Yeah, yeah.

HMJr: Because I - I think if the President could get this behind him....

R: Well, that - I think - I think he....

HMJr: God, I - I almost....

R:and I stayed behind to put in a couple of cents,
and I - I think....

HMJr: Yeah.

R:I think unless they get at him again, he's all
right.

HMJr: I almost went down on my knes.

R: Did you?

HMJr: Almost.

R: Okay.

HMJr: Yeah.

R: All right. (Laughs)

HMJr: Thank you.

R: Goodbye.

1st draft I saw
3.45 P.M. Sept 2,

I have come before you today in response to your standing invitation and in fulfillment of my promise to come up here at any time when I am seriously concerned as to the state of the nation's finances.

When I appeared before this Committee on July 23rd, I expressed my strong conviction that the revenue bill then before you was inadequate to meet the Government's needs for additional wartime revenue. Since then, the obvious need for new revenue and new sources of revenue has grown far greater. Our original minimum recommendation of \$8.7 billion of additional taxes now appears not only inadequate, from the revenue standpoint, but insufficient to give us the safeguards we need against inflation.

Accordingly, I have come here today to propose additional taxes which will increase Treasury receipts out of current

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income by an amount far in excess of the Treasury's previous recommendations, and will in addition exercise a strong restraining influence on consumer spending and therefore furnish an effective weapon for combatting inflationary increases in prices.

My primary recommendation is for a new form of tax, a tax on spending. The tax would be divided into two parts. The first part, which might be called the normal spendings tax, would apply to all who spend for consumption goods more than \$500 a year for a single person, \$1,000 a year for a man and wife without dependents, and \$250 a year additional for each minor dependent. This tax would be at the rate of ten percent -- not upon incomes, for incomes by themselves do not lead to inflation -- but upon actual expenditures on goods and services, and it would be

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completely repayable after the war. For each taxpayer there would be established a post-war credit, without interest, for the entire amount of the tax paid. Thus this levy, in form a tax, would be in effect a compulsory saving provision affecting all consumers whose expenditures exceeded a minimum subsistence level.

The second part of the proposal is for taxation at steeply progressive rates for persons spending over \$1,000 for an individual, \$2,000 for a married couple, and \$500 for each minor dependent. The rates would be designed not primarily for revenue but for restricting expenditures and inducing true saving. For this purpose, the taxpayer would deduct expenditures for debt repayment, purchases of War Bonds and other forms of investment which are in themselves forms of saving and which should be encouraged in every way.

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In addition to this primary proposal I should like to recommend a further reduction of exemptions from the income tax to the level of \$500 for a single person, \$1,000 for a married taxpayer, and \$250 for each dependent. These reductions are directly linked to our whole program for taxation designed to check inflation and to prevent a further rise in the cost of living. Together with the spending tax they would broaden the tax base so as to include \$65,000,000,000 of individual incomes, or about two-thirds of all the consumer income in the country.

The details of these proposals will be outlined to you by Mr. Paul and the members of his staff. We at the Treasury have been discussing them together, and Mr. Paul and his assistants will be speaking for me completely.

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I should like to comment on only two aspects of these new proposals before I leave the floor to Mr. Paul. One concerns their relation to the War Bond program. I have remarked that the proposed normal spendings tax of ten percent, with full repayment after the war, is in effect a compulsory savings plan. We foresee that it will probably reduce in many individual instances the amounts which workers can afford to set aside for War Bonds under voluntary payroll deduction plans, but the proposal is intended to supplement and not to supplant the voluntary purchase program.

It is our belief that the voluntary War Bond program has produced and will continue to produce a great contribution to the nation's war effort, not measured by the amount of funds raised. This is due almost wholly to the unselfish service that hundreds of thousands of men and

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women throughout the country have given to it. It has enlisted the patriotic support of working people, of the leaders of their unions, of great industrialists, of bankers, of editors and publishers, of the motion picture and radio industries, including their star performers as well as their executives -- in fact, of representatives of all groups of the American people in all walks of life.

They have responded as individuals and as patriots, and their work has been tremendously effective in selling more than \$8 billion worth of Bonds since May 1, 1941, to about 25 million individuals. More than that, it has helped to arouse the people of the country to see clearly the crisis that confronts us, and particularly to cut down their spending and to save so that their fighting men may have enough. Reliable estimates by two Government

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agencies show that the rate of saving of the whole country has doubled in the past year. I believe that the voluntary War Savings program has greatly contributed to that result. It will, of course, be continued.

The results, however, have been uneven, especially in the so-called payroll savings plan under which 20 million working men and women are already authorizing their employers to deduct a portion of their pay for the regular purchase of War Bonds. The employees of some companies have made enviable records, setting aside far more than ten percent of their pay; great Government departments, including the Treasury, can show almost 100 percent of their personnel deducting over ten percent of the entire department's payroll; but other groups have not done nearly as well.

In these circumstances, I feel that the spendings tax is necessary as a supplement to the War Savings program, designed not only to add substantially to current Treasury receipts but to have a powerful effect in restricting spending. The rates at higher levels of spending are especially designed to cut into luxury spending and other expenditures for consumer goods that are not positively essential to the immediate well-being of the individual and the family.

As I suggested a few moments ago, the danger we face is not produced directly by the rising national income. The evil we must control is the spending of that income in ways that compete with war production and drive prices upward. Our effort, therefore, must be to attack spending directly and at its root, not

only by withdrawing spending power from the individual
but by imposing what is in effect a penalty on unnecessary
spending.

Handwritten notes on the right margin, including a large '1' and some illegible scribbles.

As the rate of war production mounts, the national income mounts and the funds available for consumer spending are increasing day by day while the supply of goods is dwindling. We must adjust buying to the goods actually being produced to meet the demand. The reason for this lies as much in the Government fiscal field as in the field of the prices which consumers pay. With all the amounts we have recommended for new taxes, including these present recommendations, there is still a great gap to be closed to meet our fiscal needs. We must borrow very large additional sums. Our problem -- my problem -- is to borrow these amounts in such a way that they will not contribute to inflation. Inflationary pressure is created by consumer demand exceeding the supply of goods available. We are seeking in this proposal before you to attack the problem at the seat

of potential difficulty and to attack it drastically.

It is generally conceded by those with whom I have talked that the approach through price regulation, rationing and other devices to control supply is not enough. I think we shall be doing very much less than our full duty if we do not deal with the problem effectively in the fiscal field. What I have presented is a method -- and the best method we have been able to devise -- for accomplishing this result.

Sept 2, 1942

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~~11~~ 4 o'clock

Agenda for Secretary's Advisory Group

I. Treasury Bills

- A. Should the weekly issue of bills be increased to \$400 millions commencing with the September 16 issue?

II. Tax Notes

- A. Should the changes in tax notes listed in the attached telegram be adopted?
- B. Should the rate of interest on tax notes be flat or graduated? If graduated, what should be the graduations?

III. September Financing

- A. What issues should be employed for the financing?
- B. Should the amount to be sought by each issue be set in advance or determined by the proportion of subscriptions?
- C. Should subscriptions from non-banking subscribers be allotted in full?
- D. Should the issue be open for a longer time than usual? If so, should it be open to banks for the full period?

Q Q P X

Exp. Loans

August 27, 1942

To Presidents, Federal Reserve Banks:

Boston, Mass.
 New York, N. Y.
 Philadelphia, Pa.
 Cleveland, Ohio
 Richmond, Va.
 Atlanta, Ga.

Chicago, Ill.
 St. Louis, Mo.
 Minneapolis, Minn.
 Kansas City, Mo.
 Dallas, Texas
 San Francisco, Calif.

BECAUSE OF POSSIBLE EFFECT ON CURRENT SALES FOLLOWING INQUIRY SHOULD BE TREATED IN STRICT CONFIDENCE BY YOU AND OFFICIALS OF YOUR BANK STOP WOULD YOU PLEASE ADVISE ME BY WIRE NOT LATER THAN SATURDAY OF YOUR REACTIONS TO THE FOLLOWING PROPOSED CHANGES WHICH HAVE BEEN SUGGESTED AS IMPROVEMENTS IN PRESENT SERIES OF TAX NOTES STOP SERIES A NOTES CHANGE AMOUNT WHICH MAY BE TENDERED FOR TAXES FROM TWELVE HUNDRED DOLLARS TO FIVE THOUSAND DOLLARS A YEAR AND INCREASE MATURITY TO THREE YEARS STOP SERIES B NOTES INCREASE INTEREST RATE FROM FOUR CENTS TO SIX CENTS PER MONTH PER HUNDRED DOLLARS STOP PERMIT REDEMPTION FOR CASH WITH INTEREST ON THIRTY DAYS' NOTICE AFTER SIX MONTHS FROM DATE OF ISSUE STOP PERMIT NOTES TO BE PLEDGED AS COLLATERAL SOMEWHAT ALONG THE LINES PERMITTED IN THE CASE OF THE RESTRICTED 2-1/2'S OF 1962-67 STOP INCREASE MATURITY TO THREE YEARS STOP CASH REDEMPTION WITH INTEREST WOULD NOT APPLY TO BANKS ACCEPTING DEMAND DEPOSITS STOP THESE CHANGES WILL BRING RATE IN LINE WITH PRESENT MARKET CONDITIONS AND PROVIDE INCREASED FLEXIBILITY STOP ALSO THEY WILL PERMIT HOLDERS OF SERIES B NOTES TO PAY TAX INSTALLMENTS ENTIRELY IN CASH IF THEY SO PREFER WHICH WILL FACILITATE WORK IN COLLECTORS' OFFICES.

MORGENTHAU

23

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE September 2, 1942.

TO Secretary Morgenthau
FROM George Buffington *G.B.*

In reply to your request, there follows a summary of telephone and telegraph communications from the various District Chairmen and Executive Managers of the Victory Fund Committees, regarding your wire of August 27.

- I. Boston. Agree that the segregation of the two functions would be desirable. (Telephone from Mr. Stubbs, Executive Manager.)
- II. New York. Still feel that the Victory Fund Committee should have full responsibility for the sale of F and G Bonds and do not consider the present arrangement either detracts or adds to the general confusion. (Telegram from Mr. Sproul and telephone from Messrs. Sproul and Payson, Assistant Executive Manager.)
- III. Philadelphia. Expressed an opinion favoring the segregation. (Telephone from Messrs. Williams and Bendere, Executive Manager.)
- IV. Cleveland. Mr. Fleming believes the decision desirable, while Mr. MacBain, Executive Manager, feels the decision needs further clarification. (Telephone calls.)
- V. Richmond. Mr. Anderson, Executive Manager, says their district was set up primarily to sell F and G Bonds and believes the decision will require drastic changes in their organization setup. (Telephone.)
- VI. Atlanta. No comment.
- VII. Chicago. Look with favor on the decision, although have the impression the State Administrators are not in favor of the segregation because they have, without exception, received considerable help from the Victory Fund Committees. Believe some uniform explanation should be sent to organization. (Telegrams from Young and Patton, Executive Manager, and telephone from Mr. Patton.)
- VIII. St. Louis. Concur in the decision, but feel a uniform notice should be sent to Victory Fund organization. (Telegrams and telephone from Mr. Davis.)
- IX. Minneapolis. Favorably disposed toward the clarification arrangement. (Telephone from Mr. Loudon, Executive Manager.)

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- X. Kansas City. Principal function seems to be in the sale of F and G Bonds and believe the decision will somewhat restrict their efforts, but when situation was explained over the telephone to Mr. Leedy, he seemed to view it favorably. (Telegram and telephone from Mr. Leedy.)
- XI. Dallas. Reaction favorable, but believe some uniform explanation should be sent to organization. (Telephone from Messrs. Gilbert and James, Executive Manager.)
- XII. San Francisco. This district had not organized particularly to assist the War Savings Staff in the sale of F and G bonds; therefore decision will have little affect. (Telephone from Mr. Grunigen, Executive Manager.)

W08G86WASH H51 STL 291202

MORGENTHAU

1942 AUG 29 PM 1 20

AFTER DISCUSSING WITH BUFFINGTON YOUR WIRE YESTERDAY AND IN VIEW OF PROPOSED ~~CHANGES~~ CHANGES IN TAX ANTICIPATION NOTES, FEEL THAT THE DECISION TO DROP EFFORT OF VICTORY FUND ON F AND G BONDS IS ACCEPTABLE COURSE TO PURSUE. HOWEVER BELIEVE THAT FORM OF NOTICE TO VICTORY FUND COMMITTEES AND WORKERS SHOULD BE UNIFORM AND PROVIDED BY YOUR OFFICE IN EXPLANATION OF THIS CHANGE.

CHESTER C DAVIS

PRES., FRB OF STLOUIS.

NOTED
BUFFINGTON

NOTED
G. BUFFINGTON

1942 AUG 29 PM 12 03

V

W63G97WASH GX49 CGO 29-1034

GEORGE BUFFINGTON, ASSISTANT TO THE SECRETARY
TREASURY

IN THE CIRCUMSTANCES BELIEVE IT ADVISABLE FOR YOU TO SEND
PROMPTLY TO EACH EXECUTIVE MANAGER SUGGESTION FOR A LETTER
WHICH THEY COULD SEND TO ALL VICTORY FUND COMMITTEEMEN
COMMENTING ON SECRETARY'S WIRE REGARDING FUTURE WORK ON F
AND G BONDS. IF EACH EXECUTIVE MANAGER MAKES HIS
OWN EXPLANATION LACK OF UNIFORMITY MAY RESULT IN REPERCUSSIONS.
PERHAPS LETTER SHOULD GO DIRECT FROM YOU TO ALL
COMMITTEEMEN.



NOTED
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MORGENTHAU

REFERENCE YOUR WIRE TODAY CONCERNING FUTURE ACTIVITIES VICTORY FUND COMMITTEES, I URGENTLY REQUEST THAT ACTION BE DEFERRED WITH RESPECT TO REMOVAL OF F AND G BONDS FROM FIELD OF ACTIVITY OF THESE COMMITTEES ~~DEFERRED~~ PENDING CONFERENCE BETWEEN YOU AND DISTRICT CHAIRMEN. ORGANIZATION THIS DISTRICT HAS BEEN FORMED ON BASIS OF ~~MEMBERSHIP~~ ACTIVITY COVERING F AND G BONDS AND EXCEPT FOR METROPOLITAN AREAS THE FAR GAR GREATER PART OF THE WORK OF OUR COMMITTEES IS IN THAT FIELD. SUBSTANTIALLY ALL BANKS IN THIS DISTRICT ARE REPRESENTED BY MEMBERSHIP ON COMMITTEES AND FINEST POSSIBLE SPIRIT BEING EVIDENCED BY ALL. SPLENDID COOPERATION EXISTS WITH ALL STATE ADMINISTRATORS OF WAR SAVINGS STAFF, ALL OF WHOM HAVE EXPRESSED ENTHUSIASTIC APPROVAL OF ASSISTANCE BEING RENDERED. MEETING OF PRESIDENTS OF FEDERAL RESERVE BANKS NOW SCHEDULED FOR SEPTEMBER 25-26 WHEN CONFERENCE OF THE KIND SUGGESTED COULD BE HAD. FEEL MATTER IS OF GREATEST IMPORTANCE BOTH TO TREASURY AND TO ORGANIZATION SO FAR AS THIS ~~DISTRICT~~ DISTRICT IS CONCERNED.

NOTED
BUFFINGTON

LEEDY PRESIDENT FRB OF KANSASCITY

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1942 AUG 28 PM 5 41

YOUR WIRE TODAY. APPRECIATE DIFFICULTIES DIVIDED OPERATION WAR SAVINGS STAFF AND VICTORY FUND COMMITTEES IN SALE SERIES F AND G WAR SAVINGS BONDS, BUT DO NOT THINK THESE DIFFICULTIES WILL BE RESOLVED BY SUSPENSION OF JOINT EFFORTS IN THIS FIELD. PROBLEMS OF DIVIDED AUTHORITY WITH RESPECT TO PERSONNEL AS DISTINGUISHED FROM KINDS OF SECURITIES WILL STILL EXIST TO DETRIMENT OF TREASURY'S SELLING EFFORT. NO CONSIDERATIONS OF RE PAST POLICY OR PRACTISE SHOULD BE PERMITTED TO ACCOMPLISH THIS RESULT. I RENEW MY RECOMMENDATION, THEREFORE, THAT EFFECTIVE AND WORKABLE DIVISION IS ONLY TO BE FOUND IF SERIES E WAR SAVINGS BONDS ARE PUT IN ONE CATEGORY UNDER WAR SAVINGS STAFF AND ALL OTHER SECURITIES IN ANOTHER CATEGORY UNDER VICTORY FUND COMMITTEES. THESE ARE TWO SEPARATE SELLING JOBS, EACH ONE BIG ENOUGH TO OCCUPY THE TIME AND ENERGY OF YOUR TWO SEPARATE COMMITTEES, AND DISTINCT ENOUGH TO EMPLOY, WITHOUT CONFUSION OR DUPLICATION OF EFFORT, TWO DIFFERENT KINDS OF SELLING ORGANIZATIONS. TO MOVE IN THE OTHER DIRECTION NOW SEEMS TO ME TO BE A STEP BACKWARD

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BUFFINGTON

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HON HENRY MORGENTHAU

1942 AUG 28 PM 3 03

SECY OF TREAS

REPLYING YOUR TELEGRAM THIS DATE FEEL STRONGLY IT WOULD BE MISTAKE TO NOTIFY VICTORY FUND COMMITTEE OR REGIONAL COMMITTEES WITHOUT FULL AND SATISFACTORY EXPLANATION OF REASONS FOR REVERSAL OF POLICY. SO FAR AS I KNOW NO FRICTION WHATEVER EXISTS AT PRESENT TIME BETWEEN VICTORY FUND COMMITTEES AND THE STATE WAR SAVINGS BOND ADMINISTRATORS AND THEIR STAFFS IN THIS DISTRICT. ON CONTRARY STATE ADMINISTATORS ASSURE US ~~COOPERATIVE~~ COOPERATIVE EFFORT OF VICTORY FUND COMMITTEES HAS HELPED GREATLY IN F AND G VOLUME. HOPE YOU WILL SUPPLY ~~RESERVE~~ RESERVE BANKS WITH MORE COMPLETE STATEMENT OF TREASURY POLICY AND REASONS FOR CHANGE IN ORDER THAT WE MAY KNOW HOW TO INSTRUCT COMMITTEES AND PLAN COURSE FOR FUTURE.

CHESTER C DAVIS, PRES.,

FEDERAL RESERVE BANK OF STLOUIS.

NOTED
BUFFINGTON

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W77G25WASH M37 DLS 29-1106A

MORGENTHAU

1942 AUG 29 PM 12 29

REPLYING YOUR TELEGRAM AUGUST 28 THINK THAT THE ACTIVITIES OF BOTH THE VICTORY FUND COMMITTEE AND THE WAR SAVINGS STAFF SHOULD BE CLARIFIED. SUGGEST, HOWEVER, THAT ACTIVITIES OF BOTH GROUPS BE CONTINUED ALONG PRESENT LINES UNTIL PRESIDENTS OF VARIOUS FEDERAL RESERVE BANKS HAVE AN OPPORTUNITY TO FULLY DISCUSS MATTER WITH YOU. PRESIDENTS ARE PLANNING TO MEET IN WASHINGTON ON SEPTEMBER 28 AT WHICH TIME THE PROPOSED CLARIFICATION COULD BE CONSIDERED. IF THAT SUGGESTION IS SATISFACTORY TO YOU, PLEASE ADVISE; OTHERWISE WILL NOTIFY MEMBERS OF VICTORY FUND COMMITTEE IN THIS DISTRICT THAT THE COMMITTEE AS SUCH WILL NOT BE EXPECTED TO CONCERN ITSELF AFTER SEPTEMBER 1 WITH THE SALE OF WAR SAVINGS BONDS



NOTED
G. BUFFINGTON

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W85G42WASH GX67 CGO 29-1120

HON HENRY MORGENTHAU, JR

SECY OF THE TREASURY

WITH FURTHER REFERENCE TO YOUR WIRE REGARDING FUTURE VICTORY
FUND ACTIVITY IN SALE OF F AND G BONDS, I BELIEVE IN SEPTEMBER
THESE COMMITTEES COULD DO EFFECTIVE WORK IF THEY WERE GIVEN OPPORT-
UNITY TO WORK CONTINUOUSLY ON TAX NOTES IN SUGGESTED REVISED FORM

YOUNG.

NOTED

S. BUFFINGTON

W93G62WASH (LONG) H48 STL 29-1143

1942 AUG 29 PM 12 57

MORGENTHAU

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RETEL AUGUST 27 TAX NOTE CHANGES. APPROVE SERIES A CHANGES. INCREASE OF LIMIT TO FIVE THOUSAND DOLLARS A YEAR APPEARS ESPECIALLY DESIRABLE IN VIEW OF MUCH HEAVIER NXXX INDIVIDUAL INCOME TAX LIABILITY IN PENDING TAX LEGISLATION. APPROVE AND WELCOME SERIES B SUGGESTED CHANGES AS BEING IN RIGHT DIRECTION. INCREASE IN RATE NECESSARY UNDER PRESENT MARKET CONDITIONS. IF IT IS ANTICIPATED THAT CORPORATIONS WILL BUY NOTES ON MONTHLY BASIS IN THE AMOUNT OF THEIR CURRENT NET INCOME THE NOTES WOULD BE TURNED OVER ON AVERAGE OF ABOUT ONE YEAR AT QUARTERLY TAX DATES AND CONSEQUENTLY SEVEN OR EIGHT CENTS PER MONTH PER ONE HUNDRED DOLLARS WOULD APPEAR TO PUT RATE MORE IN LINE WITH RRSEX PRESENT MARKET FOR ONE YEAR SECURITIES. IF RATE WAS THUS INCREASED, HOWEVER, IT WOULD APPEAR ADVISABLE TO REDUCE THE AMOUNT OF INTEREST PAID IF REDEEMED FOR CASH BETWEEN SIX MONTHS AND ONE YEAR. PERMISSION TO PLEDGE NOTES AS COLLATERAL SHOULD DO MUCH TO STIMULATE SALES ESPECIALLY AMONG SMALLER CORPORATIONS BECAUSE OF UNCERTAINTIES REGARDING CASH NEEDS IN THESE TIMES. PROVISION FOR CASH REDEMPTION WITH INTEREST WOULD SEEM TO ELIMINATE ANY OBJECTION TO INCREASING MATURITY TO THREE YEARS. SINCE AGREEING ON ABOVE AS POSITION OF THIS BANK, WE HAVE RECEIVED COPIES OF TELEGRAMS OF BOARD AND EXECUTIVE COMMITTEE OF OPEN MARKET COMMITTEE COMMENTING UPON PROPOSED CHANGES SENT YOU AUG 28. BELIEVE INTRODUCTION OF A GRADUATED SCALE OF RATES ON TAX NOTES WOULD GREATLY BROADEN MARKET FOR THEM IN THIS DISTRICT AND VICTORY FUND COMMITTEE WOULD WELCOME OPPORTUNITY TO PROMOTE WIDE DISTRIBUTION.

DAVIS.

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1942 AUG 29 PM 12 49

91WASH B131 BOS 29-1243P

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ORGENTHAU

REPLYING YOUR WIRE AUG 27 CONCERNING TAX NOTES BELIEVE
PROPOSED CHANGES VERY DESIRABLE. AGREE WITH SUGGESTIONS IN
LETTER BOARD OF GOVERNORS TO YOU AUG 28 RELATIVE MORE
ATTRACTIVE AND GRADUATED SCALE OF RATES FOR SERIES B

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September 2, 1942
4:10 p.m.

FINANCING

Present: Mr. Haas
Mr. Heffelfinger
Mr. Murphy
Mr. Viner
Mr. Harrison
Mr. Burgess
Mr. Smith
Mr. Spencer
Mr. Brown
Mr. Stewart

H.M.JR: Who is the mouthpiece?

MR. HARRISON: Mr. Murphy, I think.

MR. MURPHY: I am the secretary, Mr. Chairman.
I merely recorded these decisions.

On the first point it was the unanimous opinion of the group that the bill issue should be increased to four hundred millions on September 15.

On the matter of the tax notes it was the opinion of the group, and I believe also unanimous, that the A note should be increased to five thousand dollars and should mature in three years.

On the B note it was the opinion of the group that the rate should be increased to seventy-two hundredths percent; that the maturity should be increased to three years; and that the notes should be allowable as collateral. The group was opposed to graduating the rate on the notes and was opposed to paying interest on the notes tendered for any purpose other than the actual payment of taxes.

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With respect to the September financing, the group believed that the financing should consist of an approximately two-year and an approximately four-year note, priced in accordance with the rate pattern; that the proportion should be two billion dollars for the shorter note and one billion dollars for the longer note.

H.M.JR: One billion for the shorter?

MR. MURPHY: Two billion for the shorter, and one billion for the longer. Allotment in full should be given to subscribers up to twenty-five thousand dollars and to all non-banking subscribers; but such subscribers receiving allotment in full should be required to hold the notes sixty days - this to be supported by an appropriate sanction; such as delayed delivery.

The group felt that the remainder of the subscriptions not taken by such full allotment should be allotted to banking subscriptions; and that if perchance either note was oversubscribed by non-banking subscribers and parties subscribing up to twenty-five thousand dollars, that the allotment on banking subscriptions over twenty-five thousand dollars would be zero.

H.M.JR: If it were oversubscribed, would it be prorated down?

MR. MURPHY: No. The allotment in full would be guaranteed.

MR. VINER: To preserve the right to close the books before, I think that was the suggestion - to get control on that.

MR. MURPHY: The contemplation was that the issue would be open somewhat longer than two days.

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H.M.JR: Is that the story?

MR. MURPHY: Yes, Mr. Secretary.

MR. STEWART: And delivered with more clearness than was the case during the discussion, I might say. (Laughter)

H.M.JR: It is very nice to have several hours as a filter.

MR. HARRISON: There was some little compromising here and there, you know.

H.M.JR: Have you gentlemen been in contact with the Fed?

MR. HARRISON: Yes.

H.M.JR: Did they give you lunch?

MR. SMITH: They invited us for lunch the next time.

MR. HARRISON: That was our fault. I called five minutes to one and got Ransom, who was at lunch at the time, and arranged an appointment for two-fifteen. We were there almost an hour with them.

H.M.JR: Who financed the lunch today?

MR. HARRISON: I think Walter Stewart financed much of it.

MR. STEWART: To be collected out of highballs before these bankers get away. (Laughter)

MR. HARRISON: I think it is fair to say that as a result of our meeting with the Board, the Board itself put up a pretty strong argument for the

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certificates, May certificates, rather than two issues of notes.

One point was that it was an opportunity to fill out this quarterly cycle of certificates; that if you delayed much longer in putting out a May certificate it would become so short that you would have to reduce the rate too low to make it attractive or to become competitive with the bills.

H.M.JR: Were you men at all impressed with the fact that they want to make this thing short so they can make it a bond issue in October?

MR. BURGESS: Yes. We discussed that bond issue proposition at some length this morning, and I think we all have the feeling that very considerable efforts need to be taken to sell more bonds outside the banking system and that the Victory Fund Committee and others ought to be geared up to do that job.

Now, we recognize that it is going to be hard to do the job October 1 in the style that it ought to be done; but a decision probably ought to be reached on that pretty promptly because it takes a month to get the wheels moving and get the lists ready, and so on. While there is a conflict with the date of the Community Chest drive, I think most of us felt you ought to go ahead on October 1 and have a bond issue. It cannot be the all-out one that we would like to have, but we will do the best we can.

Make it a two-percent bond or a two and a quarter. We do not think that the four-year note would interfere with that, and it would tend to distribute this financing a little more outside the banks than the certificate and short note would.

MR. SMITH: The Board, in suggesting the May 1 certificate, urged the fact that you need to fill

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that place now or face a short certificate. I was in favor of that because of the desire to have something open of a short-term nature that would be easy to finance in October. I do not agree with what Dr. Burgess has said about the preparation for a campaign because I do not believe that you can prepare for any campaign in thirty days. I think the campaign in October must be a meager effort and will take sixty days or ninety days to make proper preparation; and of course during the month of October there will be about four hundred community fund drives for a total quota of about a hundred million dollars.

H.M.JR: You are a Community Chest fellow, aren't you? (Laughter) You are the head of it, aren't you, for the country?

MR. SMITH: No, I am not the head of it.

H.M.JR: Just the brains?

MR. SMITH: Well, over the man power of the country.

H.M.JR: He doesn't deny it, gentlemen. (Laughter)

MR. HARRISON: Not yet. (Laughter)

MR. SMITH: Just on the question of man power during October, because the other fellows will have to do the work.

H.M.JR: He doesn't deny it. What do you know about that? (Laughter)

I don't know. I am for doing everything that is humanly possible to get every dollar we can get out of people outside of the banks; but I don't know about this getting five or six billion dollars in a month, and so forth. The thing that I am afraid of is you work up all this enthusiasm and then you go

- 6 -

into sort of a calm afterward and let down, and then you have to hit them again the following month. I don't know about the amount of energy. One says thirty days, the other says sixty days, to get ready for it. Then you do it, and let's say it is successful; then you skip a month and you are right back again.

MR. SMITH: That is what is ahead of us.

H.M.JR: I would just as soon do it every month.

MR. SMITH: When I said sixty days or ninety days, it is because we have not set up the organization that is necessary to do that work. Once you get it set up you can keep it going.

H.M.JR: Let me ask you fellows, the bank presidents - you happen to be grouped there together - how I am going to go to your customers, the fellows that have a lot, depending upon the community, from twenty-five thousand dollars up to a million dollars - Mr. Brown mentioned a man who was sitting there with that money who, for reasons in his own mind, does not want to do anything about it. Now, how am I going to get that fellow to lend it to the Government?

MR. SPENCER: These Victory Fund Committee fellows have got to go right up against him. I was talking to a fellow the other day, and he says, "The last time I had to subscribe to a hundred thousand. Nobody has told me I had to subscribe to anything yet."

H.M.JR: You mean in the last war?

MR. SPENCER: Yes.

H.M.JR: Let me ask you this. Is it a Victory Fund fellow or is it the head of the institution?

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Let's get personal and take your own institution. Let's say a fellow has a hundred thousand, and you know who it is and you can name him. There is this fellow. Now, who is the man who should approach him? Is it you, somebody from your board of directors, or an outside salesman?

MR. SPENCER: It is all going to depend upon who he is. Our investment bond fellows have their lists. They are the fellows that have sold securities to the great majority of the people with money. To be sure, we have got money on our books that the investment fellow does not know anything about. Now, it is going to be up to us to handle that. I don't doubt but what we are going to make some people a little bit mad in going after them, but I think it has got to be done.

H.M.JR: You haven't answered my question.

MR. SPENCER: It will be either myself or one of my officers, who know that account, who is going to go after him.

H.M.JR: That is what I think. Now, let's be a little bit more - let's be frank with each other. Now, let's say that you say, "All right, I am willing to do that", with the result--

MR. SPENCER: That somebody gets mad.

H.M.JR: No. The deposits in your bank for one month go off two, three, four, or five percent. That would be a lot, wouldn't it?

MR. SPENCER: Yes.

H.M.JR: But I mean, say, from one to five percent. Now, are you and your board of directors - I am just talking to you because you happen to be in my line of vision - I mean you as a man and you

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being connected with the American Bankers, do you think the temper of the American bankers has arrived to that point that the presidents of these institutions are willing to go to these fellows?

MR. SPENCER: A very large percentage.

H.M.JR: Now, the savings banks have done it, and they have lost deposits steadily. They have done it through selling war bonds. But let's be frank, the national banks have not.

MR. SMITH: Absolutely, Mr. Secretary.

H.M.JR: If you have, you have kept it a dark secret.

MR. SMITH: What is necessary to disclose that fact, except that we have sold in our little shop in E bonds ten thousand separate bonds?

H.M.JR: That is not what I am talking about.

MR. SMITH: Well, we sold--

H.M.JR: Have your deposits gone off?

MR. SMITH: Our savings deposits have.

H.M.JR: Well, the total?

MR. SMITH: No, because we are a commercial bank. The individual deposits have.

H.M.JR: Have they?

MR. SMITH: The corporate deposits.

H.M.JR: Tom, I am not conscious - maybe it is because nobody has explained it. Maybe the mutual

- 9 -

savings banks have done a better job in explaining what they have done. We are talking - I am not conscious of the fact. If you want, I will look at this fellow here.

MR. BURGESS: Our savings deposits are off.

H.M.JR: All right, now, I'm not conscious of the fact that the presidents of the national banks or the heads of the boards of directors have yet arrived at that point that they are willing to, if necessary, to get some of their very best depositors mad at them because they say to them, "Look, Jim, you have a hundred thousand dollars; by gosh, you have got to pay ten percent of it this time and buy Government securities and do ten percent a month."

MR. SMITH: That is because you have not been informed correctly. Now, how do you know that the savings banks have? I just wonder how that information gets in here.

H.M.JR: Well, very simple. They have had one of their men with us constantly, and Henry Bruere happens to have been here yesterday. They have one of their men with us all the time. He is right here in Washington with us, a man by the name of Sparks.

MR. SMITH: Take the Victory Fund Committees all over the country, take our district in St. Louis--

MR. EDWARDS: Mr. Secretary, those savings banks did not tell you the whole story. Their deposits have been going off for five years.

H.M.JR: Not in New York.

MR. EDWARDS: They are less. The deposits of the mutual savings banks have been declining for five years.

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Now, as to what the national banks are doing, of course I have been in touch with a good many of them, trying to help you as much as I could in this work up here. If you will pardon a personal illustration, you take our bank; we have discontinued paying interest on any savings deposits above a thousand dollars. We only pay one percent on that first thousand dollars. We have advised all savings depositors to put that money into defense bonds, and during the last sixteen months we have sold in the neighborhood of nine million dollars of Government securities to the public, F's and G's and other market securities. During that same period we bought for our own account seven million; so we have at least sold the public more than we have had to buy.

H.M.JR: But that man Mr. Brown mentioned to me a couple of months ago - is it all right to tell this story?

MR. BROWN: Certainly.

H.M.JR: He didn't tell me the name. I didn't want to know his name. It was some individual who had a couple of million dollars in his bank, as I remember it, wasn't it?

MR. BROWN: Yes.

H.M.JR: And that man just didn't want to invest it, didn't want to do anything. And there he has one man with a couple of million dollars in that bank. Now, what are we going to do with a fellow like that?

MR. BROWN: For one thing you ought to have available in the market a supply of one, two, and three-year Government obligations. It does not make any difference in the over-all picture whether he buys them out of a new issue which you are going to put out next month or whether he buys on the market bonds or notes that will suit his requirements.

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Now, you have to get up more pressure on the part of the community. It is not only the question on the part of the bank presidents. It is the Victory Fund Committees and all that type of people, that they are failing in patriotism unless they buy some kind of a Government security; but it does not necessarily mean that they have to buy the security which is being currently offered that month and which may not fit their wishes.

H.M.JR: Take this Mr. X and let's say he has a couple of million dollars. Now, how can we reach a man like that and get him to buy either outstanding issues or new issues?

MR. BROWN: Well, it so happens that in the case of this particular man you are thinking of, he decided - I don't know through what process of reasoning - to put most of his money into Government bond issues.

H.M.JR: He did?

MR. BROWN: Yes, but it was probably due to a psychological change and feeling that the war picture was much more desperate today than it was two or three months ago.

H.M.JR: Has that happened to many of your large depositors?

MR. BROWN: I think it has happened to a good many of them.

MR. SPENCER: I think they are more willing to go in. I have one case, for instance, where either a man or a wife died and they had to dig up a million and a half dollars inheritance tax. What hurt would there be from here out if any of the bond issues could be used at par for inheritance tax? That would satisfy that individual right down to the ground.

- 12 -

H.M.JR: We did make a change in that recently, didn't we?

MR. BURGESS: You made a change in the tap issue. It was a very great help.

MR. SPENCER: But it had some strings on it, didn't it?

MR. HARRISON: No, no, not on that aspect.

MR. SPENCER: We sold him about half his requirements on that, but he still did not like the bond, for some reason or other.

H.M.JR: I thought that that did not have any strings on it.

MR. HAAS: The bond had some strings - I mean, it had some restricted negotiability.

MR. SPENCER: That was it, restricted negotiability.

H.M.JR: But the F and G can both be used for debt duties, can't they?

MR. SPENCER: Oh, yes, but you are talking about a hundred thousand dollars. I am talking about the larger amounts. I think that G bond is going to take care of a very large percentage of - well, certainly individuals, from here on.

MR. SMITH: The responsibility for the sale of Government bonds to individuals lies with the selling organizations, of which the banks furnish a substantial part of the personnel.

Now, a man will come into the bank and inquire. They know the men of means and solicit them. They go into the banks and inquire and they stir up the inquiries, and they get pretty full information, too.

- 13 -

All over the country, from one end to the other, the banks are occupying important positions in those selling organizations.

H.M.JR: You people feel, then, that this Victory Fund Committee the way it is set up can do the thing that I am talking about?

MR. SMITH: When it has had time to get organized, to get oiled up.

MR. BURGESS: I confess I am greatly troubled by the fact that two organizations, the Savings and the Victory Fund, are working partly parallel and partly in competition with each other.

H.M.JR: That thing can be worked out. We keep trying all the time. That can be worked out.

MR. SPENCER: I think with us the people that will do the big job on that selling are the investment bank fellows. I think the average commercial bank man is an awfully poor salesman. He has got to spruce up on selling Government bonds from a patriotism standpoint. He never was schooled in selling many securities in the past.

MR. BROWN: Real pressure - what is going to make those people buy bonds is the pressure of public opinion as reflected in the newspapers and social attitudes and club circles.

MR. SMITH: And stirred up by this.

MR. BROWN: Stirred up by continuous agitation.

H.M.JR: Then maybe we had better have a drive.

MR. SMITH: You are going to ultimately come to it.

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MR. BROWN: You have got to.

MR. SMITH: We think you are going to have to have them at regular intervals.

MR. HARRISON: And when you do, the fundamental question that has not been decided by either the Victory Fund Committees or the War Savings is the method of approach or coverage. Are you going to give the bond salesman, or whoever it is that is trying to sell bonds, a list of prospects, to whom he is to go, or are you going to organize by counties so that a group of men will cover everybody in a county? That was really the way they tried to do in the last war. I think, so far as I understand it - and I may be wrong - that most of the approach has been the prospect one rather than the over-all coverage by county. I don't mean this doorbell thing that we had, the pledges; but I mean a serious effort on the part of a group of people assigned to a county or a certain geographical area, to be sure that everybody is seriously approached for the sale of bonds in that area.

I think ultimately the latter will have to happen because I don't know where you are going to get your lists of prospects. It might even cover this million-dollar fellow in Ned Brown's bank. The bankers themselves are not going to give out those names, I presume, except in rare instances. They don't do it. So even if you had the staff of salesmen they would not get that man as a prospect, but they would get him if they had an over-all coverage in the block or area.

MR. EDWARDS: I don't know what the bankers are going to do generally. I have given the names out. I haven't told them how much money they had.

MR. SMITH: If you have the organization they will get the names. They have a mysterious way of

- 15 -

getting them. There is an understanding between the banks and their customers that they will not give out names; but they have a mysterious way of getting names. But that will take time to get that going; however, it must be done.

H.M.JR: Walter, do you want to add anything to this discussion?

MR. STEWART: No. I am convinced--

H.M.JR: I am not talking about this. I am going back to this financing Murphy reported on.

MR. STEWART: I am satisfied with the recommendations.

H.M.JR: The two and the four?

MR. STEWART: Yes.

H.M.JR: Viner?

MR. VINER: I like the recommendations as they are now.

H.M.JR: Haas?

MR. HAAS: I would like, if I may, to think about it a little bit.

H.M.JR: Why not? That is what we are fighting for, aren't we, to give you a chance to think? For freedom?

MR. HARRISON: I would not like to change the unanimous report at all, but to express the hope that the word "approximately" four years will be construed to be as near five as you can make it. (Laughter) That is so it will fit into your rate picture, and everything else.

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MR. BURGESS: That is really a question for the market fellows, to look at the market and see where it fits.

H.M.JR: George, you put your number boys to work again and take a fresh look at it in the morning. Henry looks as though he can stand it. Are you going all right?

MR. MURPHY: I am doing all right.

MR. HARRISON: There is one thing we pointed out to the Federal Reserve Board as to one of the reasons we opposed the certificate. I don't know whether it made much impression on them. The figures that we got this morning from your own staff - they were just rough and not definitely accurate yet - show that you have maturities this next fifteen months of bonds, notes, bills and certificates of over thirteen billions and a half, not including the three billion seven of tax notes which can be called for payment. I think to recommend that you add unnecessarily to that immediate liability is a mistake.

H.M.JR: That is the way I feel.

MR. HARRISON: And I think that had a good deal of influence on most of us in our group.

H.M.JR: That is the way I feel.

Let me ask you gentlemen a question, which you need not answer here unless you want to. You can go into a huddle on it. But take people like Senator Vandenberg, who seem to be under the impression that I have nobody advising me - I wondered whether you people think it would be wise, or not wise, to announce that this group comes down occasionally as informal advisors to the Secretary of the Treasury, and give out the names. You can talk it out among

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yourselves if you want to, and let me know. I am not ashamed to have it known.

MR. SMITH: It is pretty generally known, if for any reason you should decide to announce it. That, I think, should be the governing thing, don't you?

MR. SPENCER: I do.

MR. HARRISON: You do what?

MR. SPENCER: He should announce it if he feels like it.

MR. SMITH: If he sees a reason for it - it is generally known.

MR. HARRISON: I haven't any very definite opinion. I would do whatever you think would cause you the least embarrassment.

H.M.JR: This wouldn't cause - I mean, the two sides are coming here. There is no reason to hide it, that is what I mean to say.

MR. HARRISON: I think, frankly, that the greatest possible criticism - it is already known to the group from which the criticism might come, and that is the Federal Open Market Committee. I think that they might have some feeling on it.

H.M.JR: That doesn't bother me.

MR. HARRISON: They already know it so that you lose nothing by that. The only question is whether it will verify Mr. Berryman's cartoon here. (Laughter)

MR. SPENCER: Call him in next time we are down.

H.M.JR: Well, I was just raising it. What do you think?

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MR. BROWN: Well, I think, certainly, as far as the members here are concerned, they have no objection to it. It is purely a question for you to decide as to which is most politically advantageous. I am using the word "politically" in the sense of public relationship.

H.M.JR: B.M.?

MR. EDWARDS: I agree with Mr. Brown. I think it is just whatever you choose to do about it. As far as we are concerned, I think these other gentlemen feel as I do, that we are very proud to have you ask us to come here and do whatever we can. It is just a question of what you want to do.

MR. BURGESS: That is right.

H.M.JR: What do you think?

MR. BURGESS: I agree with that.

H.M.JR: Well, the way you are coming in, I don't see why not say so, that is all - use the words "coming in on an informal basis to advise."

MR. BURGESS: You can tack it onto the story about the new financing that you are considering, that you have talked it over with the Open Market Committee, with the Board, and also with other fellows.

H.M.JR: Well, I will sleep on it, and if it is agreeable with you, if I decide I want to say something this week, is that all right?

MR. HARRISON: I think the only thing that I would suggest that you consider from your standpoint is it would possibly be interpreted by the press - and I think this you would have to avoid, if you can, in your statement - that you had organized

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another committee or another board or another something. There has been a good deal of talk throughout the country about all the different boards that are organized or different groups that are organized in Washington to do anything. But you can cover that in the form of whatever announcement you make.

MR. SPENCER: Couldn't you make the announcement that this has been going on for some time, that it is nothing new?

H.M.JR: Sure. I have not talked about it to any of our public relations people, but I will talk to them about it tonight. I did have it in mind.

I am very much obliged to all of you. I don't think I need to ask you to stay over another day. I have got what is in your brain in mine. I understand from those people who have come here to visit that Washington is not the most pleasant summer resort.

MR. BURGESS: It is all right today.

MR. HEFFELFINGER: I think there was one point in the picture, that if the announcement was proposed on the tenth of this month - next week - and we carried the payment date over to the twenty-fifth, that is a little longer than our usual period. Is there any objection to that?

H.M.JR: From me, you mean?

MR. HEFFELFINGER: No, from the banking standpoint.

MR. SMITH: Announce the issue on the tenth and not accept payment until the twenty-fifth, isn't that the usual way?

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MR. HEFFELFINGER: That intervening week is the heavy payment tax week.

MR. BURGESS: I think it is more important to get it out of the way for the October job. If you are going to do a job in October I think there is advantage in pushing this one along.

MR. HEFFELFINGER: The beginning instead of near the end of the week.

H.M.JR: That is something you can work out with the Fed. I personally don't care.

MR. BURGESS: I do think it is desirable to reach a decision about that October job pretty promptly because there is a lot of work to be done if they are going to do a job on it.

H.M.JR: Have we got to have another group of movie stars down? (Laughter)

MR. BURGESS: In October, if you want to.

MR. HARRISON: Why didn't you invite us yesterday? (Laughter)

H.M.JR: No, it was Monday. Is that what you fellows all want? (Laughter)

MR. SMITH: We heard about your luncheon today - talk about a luncheon, we heard about it today!

H.M.JR: So that is what you fellows want. Even the President of the United States sent a message over and asked why he wasn't invited. He sent this message, "You bring all these boards around to see me, and when you have somebody good looking you don't bring them around." Well, maybe that is what we need. (Laughter)

9-2-42

CHARLES E. SPENCER JR. " WILL BE WITH YOU NEXT WEDNESDAY AND THURSDAY AS REQUESTED"

W. RANDOLPH BURGESS "SHALL BE HAPPY TO BE WITH YOU IN WASHINGTON NEXT WEDNESDAY AND THURSDAY"

B.M. EDWARDS "WILL TRY TO ATTEND YOUR CONFERENCES WEDNESDAY AND THURSDAY"

E.E. BROWN - accepted by telephone call to Fitzgerald (was in town last week)

TOM K. SMITH - accepted by telephone call to Fitzgerald (was in town last week)

GEORGE L. HARRISON - telephoned Saturday afternoon that he was coming, but was having trouble getting train reservations and he might not be able to get here before 1 P.M. on Wednesday -- Fitzgerald is trying to get earlier accommodations for Harrison.

Draft # 2

10/2/42
6:15
E.P.M.

I have come before you today in response to your standing invitation and in fulfillment of my promise to come up here at any time when I feel that a major decision must be made concerning the Treasury's financing program.

When I appeared before this Committee on July 23rd, I expressed my strong conviction that the revenue bill then before you was inadequate to meet the Government's needs for additional wartime revenue. Since then, the need for new revenue and new sources of revenue has obviously become far greater. Our original minimum recommendation of \$8.7 billion of additional taxes in the light of later developments has become not only inadequate, from the revenue standpoint, but insufficient to give us the safeguards we need against inflation.

Accordingly, I have come here today to propose

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additional taxes which will increase Treasury receipts out of current income by an amount far in excess of the Treasury's previous recommendations, and will furnish an additional effective weapon for combatting inflationary increases in prices.

My primary recommendation is for a new form of tax, a tax on spending, to be divided into two parts. The first part would be a ten percent tax on the spendings of all consumers whose income is above a minimum subsistence level. This tax would be completely refundable after the war, and would therefore be in effect a compulsory ^{lending} saving provision. It would currently bring about \$5 billion annually into the Treasury.

The second part would be a spendings tax at a steeply progressive rate, designed not primarily for revenue but

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for restricting expenditures and inducing true saving. This would produce about \$1-1/2 billion additional revenue, but its effects would be still greater, to an extent that we can only guess, in restraining unnecessary spending and thus checking the greatest single factor making for inflation.

In addition to this double-purpose proposal, I should like also to recommend a further reduction of exemptions from the income tax to the level of \$500 for a single person, \$1,000 for a married taxpayer, and \$250 for each dependent. This would produce \$1-1/2 billion additional revenue, and together with the spending tax it would broaden our tax base so as to include \$65 billion of individual incomes, or about 2/3 of all the consumer income in the country. Taken in their entirety, our new

- 4 -

recommendations today would bring into the Treasury an additional amount about equal to the additional revenue provided by the Bill that is now before you.

The details of these proposals will be outlined to you by Mr. Paul and the members of his staff. We at the Treasury have been discussing them together, and Mr. Paul and his assistants will be speaking for me with full authority.

I should like to comment on only two aspects of these new proposals. One concerns their relation to the War Bond program. We foresee that the new spending tax will probably reduce in many individual instances the amounts which workers can afford to set aside for War Bonds under voluntary payroll deduction plans, but the proposal is intended to supplement and not to supplant the voluntary

- 5 -

purchase program.

It is our belief that the voluntary War Bond program has produced and will continue to produce a great contribution to the nation's war effort, not measured entirely by the amount of funds raised. This is due to the unselfish service that hundreds of thousands of men and women throughout the country have given to it. They deserve the thanks of the nation for the magnificent work they have done, are doing, and will, I hope, continue to do, in encouraging the American people to put their dollars to work for their country.

They have responded as individuals and as patriots, and their work has been tremendously effective in selling more than \$8 billion worth of Bonds since May 1, 1941, to about 25 million individuals. More than that, the program

- 6 -

has helped to arouse the people of the country to the crisis that confronts us all and particularly has led them to cut down their spending and to save so that their fighting men may have enough. Reliable estimates by two Government agencies show that the rate of saving of the whole country has doubled in the past year. I believe that the voluntary War Savings program has greatly contributed to that result. It will, of course, be continued.

The danger we face is not produced directly by the rising national income. The evil we must control is the spending of that income in ways that compete with war production and drive prices upward. Our effort, therefore, must be to attack spending directly and at its root, not only by withdrawing spending power from the individual

- 7 -

but by imposing what is in effect a penalty on unnecessary spending.

The reason for this lies as much in the Government fiscal field as in the field of the prices which consumers pay. With all the amounts we have recommended for new taxes, including these present recommendations, there is still a great gap to be closed to meet our fiscal needs. We must borrow very large additional sums. Our problem -- my problem -- is to borrow these amounts in such a way that they will not contribute to inflation. Inflationary pressure is created by consumer demand exceeding the supply of goods available. We are seeking in this proposal before you to attack the problem at the seat of potential difficulty and to attack it drastically.

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The control of prices is of course not exclusively a fiscal problem. But with full allowance for all that can be done through price regulation, rationing and other devices to control supply, I think we shall be doing very much less than our full duty if we do not deal with the problem as effectively as possible in the fiscal field. What I have presented is a method -- and the best method we have been able to devise -- for accomplishing this result.

If the proposals we make seem drastic, I should like to say with all possible emphasis that I believe nothing less drastic will accomplish the results we must accomplish. This is no time for half-way measures.

I do not merely recommend action on these bold lines, I request it and I urge it most seriously and with the

- 9 -

profound conviction that it must be done.

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September 2, 1942

6:15 pm

Present:

Mr. Paul
Mr. Gaston
Mr. Kuhn
Mr. Stewart
Dr. Haas
Dr. White
Mr. Graves
Mr. Blough
Mrs. Klotz

HM, Jr: (Reading Draft #2.) I don't like the words "compulsory saving".

Mr. Paul: I think you are going to be called evasive if you don't come right out and say it.

HM, Jr: Compulsory lending?

Mr. Gaston: "Compulsory lending" is grand.

Mr. Stewart: I don't think "compulsory lending" is any improvement.

HM, Jr: (Interrupting the reading of the draft.)

You cannot go up and ask for \$6½ billions additional taxes with that kind of statement. You just can't do it. I told the people two things: (1) if it ever came that I was worried about the financing, I would say so. I am worried. I want to say so. Another thing, if I wanted to give up the volunteer plan, I would say so. And those two things I want to say.

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Now, I tried it out on Walter George, who is certainly a conservative man, and his only reaction was "Put it in writing so you would know what you are saying", but he did not say I should not say it.

This is what I wrote at 6:30 this morning:

"Gentlemen, I told you if at any time that I was worried about the financing, I'd come before you and say so. I am here today. I also told you that if I wasn't satisfied with the volunteer plan, I'd come before you and say so. I am here today. I can assure you and, through you, the country that I can continue to raise the stupendous sums necessary to finance the war for the balance of the year, but after the first of the year I will need additional revenue in order to carry out my responsibility. I also feel that the present bill as it passed the House now does not sufficiently reach the mass of the purchasing power, and that we in the Treasury must carry out our share of the responsibility to close this gap. Therefore, I have asked to come before you today to make the following suggestions" -- and then go ahead and make the suggestions, and give them (1) the figure, how much additional revenue will be raised, and (2) how much of an inflationary gap can be closed through this suggestion. Close by saying that the situation is extremely serious and I feel that in order to keep the country on a sound financial basis this coming year, I've pretty much got to have what I'm asking for today. If Congress will give me this, I feel that I can carry on in the coming year."

Mr. Paul: As to one word in that, and that is "worried". "I want to express deep concern," but ...

HM, Jr: But it's the idea, Randolph. I have gone up there. These people -- let me go through it once more again. These people have been more than generous and kind in their confidence in me. They have said to me, "All right, Mr. Morgenthau, all right. If you want to

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try out your volunteer plan, we will let you have your way. I said, "Gentlemen, if the time comes I am not satisfied, I will come up and say so." All right. I want to say so. They have not attacked me on the floor. They have shown that confidence. They have asked me, time and time again, can I finance this war and I said, "Yes. If the time comes I am worried, I will come up and say so." Now, they are entitled to have the straight thing, and the country is entitled to it.

I would like to know, Gaston, senior, and Kuhn, second, why I am not permitted to say that.

Mr. Gaston: As baldly as you have stated it there, it seemed to be the opinion of everybody we consulted it would be a mistake to say it. I realize that we tried it along a different line and I realize, after our conversation with you this morning, that that wasn't going to meet your desires and that we would probably have to do a complete re-write of the thing, but we have been consulting other people and I have had half a dozen people in my office most of the afternoon to get their views and we just have not got at approaching it from the other angle. I think that some modifications must be made in your presentation. I think you can't say you are worried about the situation. I have started to try to work out something. I think it would be perfectly safe for you to say. Jake Viner thought we should go into more detail and your statement should be along the line we drafted. Walter Stewart thinks otherwise.

HM, Jr: For the minute, that does not bother me. Now, look. Maybe you people think that this thing that I am going up there tomorrow to suggest is a pink tea affair. I don't. And what is motivating Henry Morgenthau, Junior, after ten months -- we started this thing last November -- that I suddenly come up and ask for almost double taxes than I have ever asked for before, or revenue, whatever you call it. There must be something. I have been here 9 years. "Don't you know your job?" "Why do you suddenly come up? Why didn't you do it 2 months ago, or 6 months

-4-

ago and why do you come up now with this very drastic suggestion -- as drastic as anybody in Washington can suggest -- at the last minute and say to us 'I want this'?"

Now, you people have not had one advantage which I have had, that Haas and Stewart have had, that I have gone from one meeting to another on how I am going to raise \$3 billions this month and \$4 billions next month and \$5 billions the month afterward. And I am worried. And what's the harm in saying so? I always took the attitude I would be much bluer, much blacker, about the financial situation than anybody else. I don't want to exaggerate the danger, but if we tell the people we face that with the result that -- it is 9 years that the President put me in here when the bond market had gone to Hell; he could not sell any bonds, and from that day the bond market is all right, and I have always told him the worst news in the financial community. I have to have some reason for going up 2 months before election and tell them why. I just can't do it because I suddenly wake up on Saturday morning with a bad taste in my mouth and say "This is a bad day. I am made at the war and I am made at the world, and I am going out and tax everybody to the limit." This is the most drastic suggestion that any member of Mr. Roosevelt's Administration has made. I would like to know of anybody in his Administration who would suggest it. Why am I doing it? There is nothing in that statement.

Mr. Gaston: I thought there was in the original statement.

HM, Jr: I differ with you. I have said

Dr. Haas: I think one word would clear up -- a good deal of your worry is about the method. You haven't any doubt you could finance it through the banks and it would go

HM, Jr: No, you are wrong, George. I think there is a limit to what you can do through the banks.

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Dr. Haas: There is ultimately, but we are nowhere near the time.

HM, Jr: But next year you begin to approach the thing. You can't use this machinery

Dr. Haas: It will upset the whole country.

HM, Jr: You can't pile interest-bearing certificates on interest-bearing certificates in the banks and pay interest. You can't do it in an unlimited way. This thing that I am suggesting tomorrow is. How did I get that way? There has to be justification for it.

Now, just because I am positive, anybody else in the room can be just as positive, if they disagree.

Roy, any energy left?

Mr. Blough: I think you can indicate a great deal of serious concern about the manner in which this war is going to be financed and the effect of that financing on inflation without causing a bad break in the markets and a bad scare all over the country and it seems to me that it is entirely in the way in which it is said and it would not be desirable to indicate worry about your ultimate ability to finance the war, but I think you could indicate the greatest concern about the effect of this financing on the economic operation of the war if something isn't done about it, and that is the line that could be taken and wouldn't cause any cracks in the market and wouldn't cause any serious panic of feeling and at the same time would indicate that something serious was necessary.

HM, Jr: Harry?

Dr. White: Well, I am in thorough agreement with you that the thing ought to be short -- one page or a page and a half. I think the less you say, the better; at the outside, two statements very much like you said with a

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little dressing; (1) that the

HM, Jr: French or Russian?

Dr. White: One, that the future looks more uncertain than ever about the duration of the war; that the amount of financing to be done is increasing in prospect and that sound finance calls for looking ahead and a re-examination of the situation in the light of recent developments, and you think more money must be raised in a way which was not inflationary, and that you promised you would come to them when you felt the prospects were disturbing, and you feel the prospects are disturbing and "I am before you now." I wouldn't make any bones about it. I wouldn't expand it. I would just make that statement. Secondly, you said you would come before them when you felt something more was needed than your voluntary savings plan. It has not done enough and it is necessary to supplement it by others which are drastic, as the times call for. You might add it will cut into your volunteer savings program, but the net result will be an increase from sources needed, namely, sources that make for inflation. The program is drastic; the times are drastic. Period. I wouldn't say anything -- I wouldn't say anything about the success of your bond program or the voluntary savings program or anything about inflation. That could all very -- a good deal of it, could go in Randolph's preliminary statement.

HM, Jr: Harold?

Mr. Graves: While I have not examined this at all except that part which relates to the bond

HM, Jr: But you have heard me read it.

Mr. Graves: I would like to say that I hope nothing will be said that will unnecessarily affect the bond program.

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HM, Jr: You are talking now about War Bonds.

Mr. Graves: And I liked Mr. Kuhn's statement, which I read, because it obviously would be calculated to

HM, Jr: May I interrupt you? I would like to say that part which has to do with War Bonds -- I think the War Bond people, starting with you and from you on down, that's the least I can say for them. They are entitled to an explanation and a pat on the back. I am not arguing about that. You can rest on your oars on that. But as one of my group

Mr. Graves: I like what Mr. Blough had to say.

HM, Jr: May I say this for Kuhn. I think that part on the War Bonds, he said beautifully.

Mr. Kuhn: That was Herbert.

Mr. Gaston: And Ferdie.

HM, Jr: Partnership of Gaston and Kuhn. That part I would like to say.

It gets down to a question, why am I doing so and so and so.

Mr. Graves: I think Blough expressed my opinion about it. It would be best for your concern to relate to methods merely. I think it would be very unfortunate if the thing were said in such a way as to give people the impression that there was any doubt about the ability of the Treasury to finance the war, one way or another.

Dr. White: There is never any problem about financing a war. There isn't any Government in the world that can't finance a war and no Government has ever stopped a war because of lack of finance. Obviously, it is a question of

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how he will finance, and that's what he's concerned about, and we can make it in such a way it will not look panicky at all, but just the prospect of more uncertain -- don't know how much we need to borrow; the interest burden is piling up, and conservative financing makes it necessary to look ahead. Can be said in a reasonable tone, very simple, very briefly. I don't think any panic would arise.

Dr. Stewart: Frankly, I am not very clear on the answer to your question why you appear at this time. It is not self-evident. I think you have to make a case. I think there is tied up in your statement an emotion which is merely your own; that is, you have come to a decision which is very difficult to come to. I see no reason to communicate that emotion to the Committee. That is private to you. You have had a hard time to make the decision and you have waited over a period of two or three months to see if the voluntary would succeed. Any way you phrase it, it involves a lot of courage. You are no longer willing to risk it on the volunteer basis. But that thing which you feel very strongly, there is no point in transferring it to the Committee. You don't want the Committee to share your worry. You want them to take partnership with you in making the decision. Make an emphatic statement. It ought to be clear to them that it is drastic and that you have come to it reluctantly, but you have come to it with finality.

I don't think the details should go in, but the mood should go, and Paul should handle all details. But I don't think the panicky feeling --- you don't feel panicky now, but you want them to share a decision with you, but they are not supposed to be worried. You come to them and tell them you have made up your mind. I would not communicate my worry to them. It's a hard job and a hard responsibility to take.

HM, Jr: Now that we are on the basis of Freud. Let's say that you are right for a minute. Having come to this

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decision through worry -- great worry -- it was, as you say, one of the most difficult decisions I have ever had to make -- let's say for a minute you are right; I should not transfer that worry which went into the making up of the decision to the Committee. How can I answer your question it is not clear why I come up there at this time to do this.

Dr. Stewart: I think that is communicated in a mood rather than in effect. If they cross-examine you, the only answer I have been able to think of is you are passing from one phase of war financing into an entirely different one. The volume of spending power has increased. You have carried out a program by using unused reserves so you can make a case without saying a definite date, one month or two months ago. I think this is an acknowledgment that there are limitations to what you can do in financing the war with peace time economy.

HM, Jr: What I am bringing up is transition from a peacetime method to a war-time method.

Dr. Stewart: That's one way of putting it.

Dr. White: And putting our financing on a real war time basis.

Dr. Stewart: I am not sure that is necessary. I agree with Harry, the briefer you make it, the better.

HM, Jr: You (Stewart) don't mind my repeating something. I liked it. Going home last night at 11 o'clock Walter Stewart said one of the things that pleased him the most was that at last he found himself in complete agreement with Harry White and it made him, Walter Stewart, very happy and he was very sincere, and I am being sincere, and I thought it was a nice remark, and I thought you both would appreciate it.

In view of what you say, do you think what Gaston and Kuhn have written is adequate?

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Dr. Stewart: I think the very last page of what was written is in the mood for it.

HM, Jr.: I have not read it.

Dr. Haas: I think, Mr. Secretary, that your reason for coming up is in terms of the greatly accelerated expenditures and the reason there is because war production has gone up and it is obvious to you, as stated in your letter to Senator Vandenberg in April, which you may have forgotten, that something like this would be necessary later on because of the increased expenditures.

You are going up to Congress. Because of the magnitude of these figures, you can't use peace-time mechanism for financing and prevent inflation. This happens to be a drastic change in the devices you used, because you are taking such a large portion of your national income into the economy, but I would put it on the terms that you are using new equipment, but don't see anything unsound in the Nation's finance, but you need this equipment to continue to keep it on a sound basis. Many letters have come into the Treasury inquiring whether the Government debt will be paid off and I am apprehensive that we would frighten those people in any way.

Mr. Paul: I can say in two sentences what I think. He is right and the effort should be on the method of financing. I think Harry is right that the statement should be very short. I agree completely with Stewart. There is no black and white explanation. You have to communicate a mood. I think the phraseology you used "to transfer from peace time to war time" is a little dangerous because we have been at war 8 or 9 months, but generally I agree with you and I liked your statement of partnership -- that here, from now on, Congress and we are in partnerships on this thing. We have known about these magnitudes for months. They will tear us to pieces there. It was months and months ago that we increase the Budget \$14 billions and they will just tear us to pieces if we

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try to make a case. A case could be made there for the idea that you have been very anxious to be right in your position and you have, perhaps, done a little waiting, but now the time has come when the Finance Committee is in Executive session and there is no more time to be lost. You have not lost any time by not having gone up 2 or 3 months ago, but now the Bill is approaching the place where no more time can be lost. It's the communication, really, of a mood, and the shorter it is the less can be written in editorials which will be very hostile.

HM, Jr.: O. K. Herbert?

Mr. Gaston: I think everything that has been said here indicates a statement of more than one page. I have been worried from the standpoint of your going up there and frightening not only the Committee, but frightening the country on the financial situation. And the other thing was anything that would look like repudiation of the volunteer savings campaign. But I don't think you need the detail of the proposal.

I started and I wrote this under some difficulty and it's just an approach to your idea.

(Reading). "We have come before you today to present a program to raise substantial additional sums to finance the war effort. I intend to leave the details of the presentation to Mr. Paul and his associates and to limit myself to a few words about the gravity of the situation as I see it and the imperative need for legislation along the lines we are suggesting.

"We have financed without disturbance and with what I feel to be a minimum of inflationary effects the huge war expenditures we have been called upon to make. But the very success of the production program in turning out immense quantities of goods for the war effort increases the dimensions of the fiscal problem we have to face. We

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"have to contemplate expenditures of 80 billions in the present fiscal year, while the revenue in sight on the basis of the tax bill now before you is only approximately 24 billions.

"We have sought and will continue to seek funds from those sources where borrowing will have the least inflationary effect, and have done so with what I believe to be most gratifying results. We can foresee with confidence provision for the Government's fiscal needs for the remainder of this calendar year.

"But I come before you today to tell you frankly that I need your help in the form of legislation which will enable me to meet the much greater problem of the next year with the same degree of confidence.

"We come before you with legislation which has a double purpose. The first purpose is to draw into the Treasury substantial additional funds out of the earnings and savings of the people. The second purpose is even more important. It is reduce consumer spending directly by withdrawal of funds otherwise available for expenditure and to reduce it also indirectly by creating a strong tax incentive to saving.

"The measures we propose are two: first a tax on consumer spending which will reach into the lowest income groups above the level of bare subsistence incomes and will provide high penalty rates for luxury spendings; second, a further lowering of the exemptions from the income tax applying to family income.

"The two proposals will touch incomes aggregating some 65 billions of dollars and will draw into the Treasury funds otherwise available for consumer spending in an amount estimated at about seven billion dollars. But of this total some four and a half to five billions, although raised as a tax, will be treated not as revenue but as a debt to the individuals from whom it was collected,

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"to be repaid after the war.

"Revenue is not the sole purpose, nor even the primary purpose, of either of these proposals. Their main purpose is to restrict consumer spending so that we may avoid the perils of inflation in the huge financing program that we have ahead of us in the next year and those to follow."

HM, Jr: I think it is very good.

Dr. White: Two thoughts could be -- but very briefly -- one is that your program is designed not only to raise revenue in ways to prevent inflation, but it is also specifically directed toward reduction of expenditures. The second point is, I don't think you can get away from the statement -- and this is the most dangerous point you are trying to skirt around -- and that is "I have given the program of payroll - voluntary - savings as complete a test as possible and I have come to the point where I feel it is not adequate and needs to be supplemented. Why not state that? There is no harm in that. You say you have given it 8 months' trial. It has not produced adequate results.

Mr. Gaston: We said substantially that.

HM, Jr: Let me say this: I get excited. I naturally was surprised that after asking that the thing be eliminated it still was there. I hope I was not rude to you.

Mr. Gaston: Quite the contrary.

HM, Jr: But I could not understand why, having asked, I did not ask for a condensation; I asked that the thing be eliminated.

Mr. Gaston: We realized that this needed a different approach and a different ending and we just could not get

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to it.

Mr. Kuhn: There were two instructions we went away with and this was the result. And then the third instruction was to consult quite a number of people, all of whom were unanimous in feeling you could not say you were worried about the state of the Nation's finances, and that's why this was brought to you in that form.

HM, Jr.: Let me ask this. We have to put it to bed tonight.

Mr. Gaston: It can be done. I will go ahead and complete a draft.

Mr. Kuhn: It can be done.

HM, Jr.: When can I see you and Kuhn.

Mr. Gaston: If anybody else is going to be around we really ought to check some statements. I imagine it will be about 9 o'clock before we -- 8:30 or 9.

HM, Jr.: I will be sitting home.

Mr. Kuhn: Wouldn't it help if the Secretary looked at the last page?

Mr. Gaston: Page 8.

HM, Jr.: I think if I could have Gaston and Kuhn working on this and then I will be home. Come up to the house. That's all.

Mr. Gaston: All right.

HM, Jr.: We agree, so there can be no misunderstanding, reference to the plan will be out - description.

Mr. Gaston: We will have to say something about what you are proposing.

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HM, Jr: What I can say, Herbert, is (reading) "My primary recommendation is for a new form of tax, a tax on spending, to be divided into two parts. The first part would be a ten percent tax on the spending of all consumers whose income is above a minimum subsistence level." I thought "My primary recommendation" -- wait a minute. Beginning with page 3, "In addition to this double-barrel proposal, I should like also to recommend a further reduction ..." -- do you think that has to go in?

Mr. Gaston: No.

HM, Jr: Or does it?

Mr. Gaston: I think we can say in one short paragraph the three things you are recommending and the purpose to which they are directed. You are proposing two things: a tax on spendings, in two parts, and a reduction of the exemptions. The purpose of these is all directed to the same end -- intended to reach a certain amount of consumer expenditure - restrict spending.

HM, Jr: Well, after this thing, certainly Kuhn and Gaston, who are intelligent fellows....

Mr. Gaston: "Quote".

HM, Jr: What?

Mr. Gaston: "Quote".

HM, Jr: No, how I feel. And I will await peacefully your arrival at the house.

Thank you all very, very much.

oOo-oOo

3d draft.

9-10 P.M.

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Sept 2, 1942

Statement of Secretary Morgenthau before the Senate
Finance Committee, Thursday, September 3, 1942.

We have come before you today with a program to raise substantial additional sums to finance the war effort. I intend to leave the details of the presentation to Mr. Paul and his associates and to limit myself to a few words about the gravity of the situation as I see it and the imperative need for legislation along the lines we are suggesting.

Up to this point we have financed without disturbance and with a minimum of inflationary effects the huge war expenditures we have been called upon to make. But the very success of the production program in turning out immense quantities of goods for the war effort increases the dimensions of the fiscal problem we have to face.

- 2 -

We have to contemplate expenditures of \$80 billion in the present fiscal year, while the revenue in sight on the basis of the tax bill now before you is only approximately 24 billions.

The Treasury has sought and will continue to seek funds from those sources where borrowing will have the least inflationary effect, and we have done so with what I believe to be most gratifying results. We can foresee with confidence provision for the Government's fiscal needs for the remainder of this calendar year.

But I am here today to tell you frankly that I need your help in the form of legislation which will enable me to meet the much greater problem of the next year with the same degree of confidence.

The legislation which we are preparing has a double

- 3 -

purpose. The first purpose is to draw into the Treasury substantial additional funds out of the earnings and savings of the people. The second purpose is even more important. It is to reduce consumer spending directly by withdrawing funds otherwise available for expenditure and to reduce it also indirectly by creating a strong tax incentive to saving.

The measures we propose are two: first a tax on consumer spending which will reach into the lowest income groups above the level of bare subsistence income and will provide high penalty rates for luxury spending; second, a further lowering of the exemptions from the income tax applying to family income.

The two proposals will touch incomes aggregating some 65 billions of dollars and will draw into the Treasury

- 4 -

an estimated seven billion dollars otherwise available for consumer spending. But of this total some four and a half to five billions, although raised as a tax, will be treated not as revenue but as a debt to the individuals from whom it was collected, to be repaid after the war.

Revenue is not the sole purpose, nor even the primary purpose, of either of these proposals. Their main purpose is to restrict consumer spending so that we may avoid the perils of inflation in the huge financing program that we have ahead of us in the next year and those to follow.

It can be expected that the new spending tax will reduce in many individual instances the amounts which workers can afford to set aside for War Bonds under

voluntary payroll deduction plans. In present circumstances we can no longer afford to rely entirely upon voluntary lending. The present proposals are intended, therefore, to supplement the voluntary purchase program.

It is our belief that the voluntary War Bond program has produced and will continue to produce a great contribution to the nation's war effort, not measured entirely by the amount of funds raised. This is due to the unselfish service that hundreds of thousands of men and women throughout the country have given to it. They deserve the thanks of the nation for the magnificent work they have done, are doing, and will, I hope, go on doing, in encouraging the American people to put their dollars to work for their country. The voluntary War Bond program will, of course, be continued.

- 6 -

Our present and urgent problem -- my problem -- is to borrow the great amounts that will be needed to finance the war effort in ways that will not contribute to inflation. Inflationary pressure is created by consumer demand exceeding the supply of goods available. We are seeking in these proposals before you to attack the problem at the seat of potential difficulty and to attack it drastically.

The control of prices is of course not exclusively a fiscal problem. But with full allowance for all that can be done through price regulation, rationing and other devices to control supply, I think we shall be doing very much less than our full duty if we do not deal with the problem as effectively as possible in the fiscal field.

- 7 -

What I have presented is a method -- and the best method we have been able to devise -- for accomplishing this result.

If the proposals we make seem drastic, I should like to say with all possible emphasis that I believe nothing less drastic will accomplish the results we must have. This is no time for half-way measures.

I do not merely recommend action on these bold lines, I request it and I urge it most seriously and with the profound conviction that it must be done.

CONFIDENTIAL

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WAR DEPARTMENT
THE CHIEF OF STAFF
WASHINGTON

September 2, 1942.

The Honorable,

The Secretary of the Treasury.

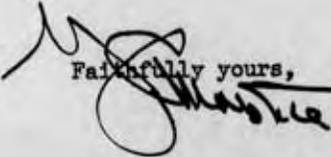
Dear Mr. Secretary:

Thank you for your letter concerning your trip. I hope that it has given you some indication of our Army side of the war effort.

Colonel Phillips informed me, on his return, that you were somewhat concerned about the presence of soldiers of the Japanese race at Fort Riley, Fort Sill, and Fort Bragg. I have had this situation investigated and found that there are about one hundred soldiers of the Japanese race at each of the posts who form part of the station complement and are assigned jobs as truck drivers, laborers, and similar duties. Each individual has been carefully checked as to his loyalty, but at the same time they are kept under surveillance at each post. The Post Commanders are getting good work out of these people and are very desirous to continue the utilization of their services.

In light of the above findings, I am confident you will agree with me that the continued use of these soldiers for the purposes and under the conditions stated is desirable.

With warm regards,

Faithfully yours,


CONFIDENTIAL

September 2, 1942

Dear General Harmon:

The photographs which you so kindly sent me will help to remind me of the deeply impressive day I spent with you and your men at Fort Bragg.

I wrote to General Marshall the other day that I was particularly struck with the fine training and spirit of your command, and that you seemed to have what it will take to defeat the enemy. The more I try to sort out my impressions of a crowded tour, the more I feel that you are entitled to great credit for what you have accomplished.

Let me tell you again how much I appreciate all the courtesy and helpfulness which you and your fellow officers showed to me. My best wishes will go with you and the men of your command wherever you may be serving.

Sincerely,

(Signed) H. Morgenthau, Jr.

Major General E. H. Harmon,
A. P. O. 252,
Fort Bragg, North Carolina.

Photographs given to TM Kubler 9/4/42

m K 96



HEADQUARTERS SECOND ARMORED DIVISION
OFFICE OF THE DIVISION COMMANDER

11 2

A. P. O. 252,
Ft. Bragg, No. Carolina,
August 24, 1942.

Hon. Secretary of the Treasury,
Washington, D. C.

My dear Mr. Secretary:

Enclosed herewith are a few pictures which were taken during your recent visit to the camp of the 2nd Armored Division. The photographs clipped together are pictures of the review which you missed due to a misunderstanding of orders by the Post authorities.

We enjoyed your visit very much and were sorry that you could not be with us a longer period of time. Hope you can call in on us again and stay a little longer.

With kindest personal regards,

E. N. HARMON,
Major General, U. S. Army,
Commanding.

Handwritten notes on the right margin, partially obscured and difficult to read.

September 2, 1942

Dear Mr. Diets:

The motion picture stars' rally here Monday was such a success in every way that I should like to send a special word of thanks to you, as one who helped greatly in arranging it.

I have seldom seen anything here in Washington to equal the enthusiasm and the spirit of the crowd. If each of the stars does as well on the September tour of the country, the industry's drive can hardly fail to be a success.

Sincerely,

(Signed) H. Morgenthau, Jr.

Mr. Howard Diets,
1540 Broadway,
New York City.

FK/ogk

Copies to Thompson

UNITED STATES SAVINGS BONDS

Sales Since May 1, 1941, by months
On Basis of Issue Price

(In thousands of dollars)

Month	Series E			Series F	Series G	Total
	Post Offices	Banks	Total			
July	\$ 42,836	\$ 57,745	\$ 100,581	\$ 37,817	\$ 211,420	\$ 349,818
August	40,788	61,729	102,517	28,876	183,134	314,527
September	50,558	94,717	145,274	27,359	169,498	342,132
October	40,725	76,878	117,603	20,318	127,685	265,606
November	38,117	67,123	105,241	18,099	108,987	232,327
December	41,634	81,250	122,884	22,963	124,866	270,713
January	37,997	71,478	109,475	18,978	105,035	233,487
February	103,154	237,930	341,085	33,272	154,242	528,599
March	158,469	508,942	667,411	77,559	315,576	1,060,546
April	86,938	311,051	397,989	51,820	253,391	703,200
May	86,278	251,321	337,599	41,070	179,223	557,892
June	83,802	242,858	326,660	40,003	163,839	530,502
July	108,005	313,826	421,831	42,465	170,060	634,357
August	105,907	327,316	433,223	41,041	159,681	633,945
September	116,721	391,396	508,118	73,691	319,053	900,861
October	103,951	350,016	453,967	52,268	191,020	697,255
Total	<u>\$1,245,883</u>	<u>\$3,445,575</u>	<u>\$4,691,458</u>	<u>\$ 627,599</u>	<u>\$2,936,710</u>	<u>\$8,255,767</u>

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

September 2, 1942.

Notes: All figures are deposits with the Treasurer of the United States on account of proceeds of sales of United States savings bonds.

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

UNITED STATES SAVINGS BONDS - TOTAL

Comparison of September sales to date with sales during the same number of business days in August and July 1942

(At issue price in thousands of dollars)

Date	: September : daily : sales	Cumulative sales by business days			: September as : percent of August
		: September	: August	: July	
September 1942					
1	\$ 19,162	\$ 19,162	\$ 26,267	\$ 28,418	73.0%

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

September 2, 1942.

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

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

UNITED STATES SAVINGS BONDS - SERIES E

Comparison of September sales to date with sales during the same number of business days in August and July 1942

(At issue price in thousands of dollars)

Date	September daily sales	Cumulative sales by business days			September as percent of August
		September	August	July	
September 1942					
1	\$ 11,634	\$ 11,634	\$ 14,044	\$ 15,821	82.8%

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

September 2, 1942.

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

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

UNITED STATES SAVINGS BONDS - SERIES F AND G COMBINED

Comparison of September sales to date with sales during the same number of business days in August and July 1942

(At issue price in thousands of dollars)

Date	September daily sales	Cumulative sales by business days			September as percent of August
		September	August	July	
September 1942					
1	\$ 7,528	\$ 7,528	\$ 12,222	\$ 12,597	61.6%

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

September 2, 1942.

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

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

Sales of United States savings bonds
September 1, 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
	Daily	Sept. 1 to date	Sept. 1 to date	to date as % of quota	Daily	Sept. 1 to date	Sept. 1 to date	to date as % of quota	Daily	Sept. 1 to date	Sept. 1 to date	to date as % of quota
1	\$ 11.6	\$ 11.6	\$ 14.9	77.9%	\$ 7.5	\$ 7.5	\$ 6.9	108.7%	\$ 19.2	\$ 19.2	\$ 21.8	88.1%
2			34.5				16.6				51.1	
3			55.5				26.4				81.9	
4			81.0				35.6				116.6	
5			98.3				42.2				140.5	
8			143.3				58.1				201.4	
9			168.8				67.8				236.6	
10			193.4				76.7				270.1	
11			220.6				84.4				305.0	
12			239.2				90.1				329.3	
14			272.7				99.7				372.4	
15			288.2				105.0				393.2	
16			307.6				112.1				419.7	
17			327.2				119.2				446.4	
18			350.1				125.7				475.8	
19			365.4				130.5				495.9	
21			399.6				141.0				540.6	
22			415.7				147.0				562.7	
23			436.2				155.2				591.4	
24			457.1				163.4				620.5	
25			481.4				171.0				652.4	
26			497.4				176.6				674.0	
28			532.7				188.7				721.4	
29			549.2				195.5				744.7	
30			570.0				205.0				775.0	

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

September 2, 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.

Note: Quota takes into account both the daily trend during the week and the monthly trend during the month.

TREASURY DEPARTMENT
INTER OFFICE COMMUNICATION

DATE September 2, 1942

TO Secretary Morgenthau
FROM Mr. Thompson

I have looked carefully into the possibility of exchanging your Buick for the Cadillac, but regret that apparently there is no legal way to accomplish this. Under rulings of the legal officers, in an exchange of this nature there must be an appropriation available to pay for the article acquired by exchange, this being so because of a well-established rule under Decisions of the Comptroller General that in the absence of an exchange statute (which is absent in the present case), an appropriation must be charged for the full price of the article acquired, the trade-in value of the article disposed of being covered into Miscellaneous Receipts.

Our appropriation for the car for the Secretary of the Treasury provides only for "maintenance and repair", no purchase authority being included. Specific authority to purchase is included only every three or four years when a new car is authorized.



THE WHITE HOUSE
WASHINGTON

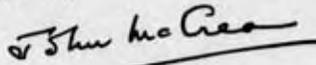
2 September 1942

My dear Mr. Morgenthau:

For your information I am attaching a memorandum which I recently received from Captain Ralph Davison, the Assistant Chief of the Bureau of Aeronautics.

This appears to be the latest information on the New Hackensack airport.

Sincerely yours,



JOHN L. McCREA
Captain, U.S. Navy
Naval Aide to the President

Attachment

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

reply address not the signer of
letter but Bureau of Aeronautics,
War Department, Washington, D.C.

Refer to No. Aer-PL-3-IG
NL-9(1-875)
A2-13(1)

NAVY DEPARTMENT
BUREAU OF AERONAUTICS
WASHINGTON

M E M O R A N D U M

28 August 1942

For: Captain John L. McCrea, USN,
Naval Aide to the President,
The White House.

1. Under date of 22 June 1942, the Commanding Officer, Naval Air Station Anacostia, submitted a memorandum to you relative to the hazardous flight conditions at the New Hackensack, New York, commercial airport. This memorandum you forwarded to the Bureau of Aeronautics to make representations to the Civil Aeronautics Administration for remedial action.

2. The Civil Aeronautics Administration has now advised this bureau by recent letter of its inability to remedy the hazards of the field, but has stated that it believed the War Department would shortly acquire the field.

3. The bureau has verified the fact that the War Department will shortly acquire the field, in connection with flight indoctrination to be given U. S. Military Academy cadets at nearby West Point, and the bureau has been verbally informed that the War Department will improve the field so as to eliminate the dangerous obstructions surrounding the field.

Durison

Copy to:
CO, NAS Anacostia, D.C.

Treasury Department 10
Division of Monetary Research

Date Sept. 2, 1942 19

To: Mr. White

From: Mr. Cass

In further expansion of the last paragraph of this memorandum -- which I have not thought it necessary to include in the memorandum itself -- I am informed by Mr. Neal that he spoke yesterday to both Mr. Randolph Paul and Mr. Roy Blough about the Treasury's spending tax proposal. He says that both Mr. Blough and Mr. Paul made it clear to him that the spending tax would probably have a compulsory saving feature.

TREASURY DEPARTMENT
INTER OFFICE COMMUNICATION

DATE September 2, 1942

TO Mr. White
FROM Mr. Gass

Subject: The Wall Street Journal story of September 2 on the "Spending Tax"

Mr. F. W. Neal, the author of the September 2 story on the spending tax, spoke to me briefly on September 1 about the spending tax. I gave him no information which went beyond what Senator George had already said in public.

Mr. Neal asked what we meant by a spending tax. I indicated that it was a tax on consumption, excluding saving, having exemptions for dependents and with graduation.

He asked how the amount of spending would be calculated. I indicated that account would be taken of income and the net change in capital assets. Spending would therefore be derived as a residual.

He asked whether any part of the spending tax might be treated as compulsory saving. I replied that it had been suggested that part of the tax might be made a post-war rebate and that this suggestion was under consideration.

Mr. Neal asked no questions with regard to the expected yield of the tax or the rate schedule which the Treasury might propose.

He may have received more precise information on the character of Treasury plans from someone in the Treasury. However, his story, as it appears in the Wall Street Journal, may be merely an intelligent reporter's filling-in of the details from such fragments of information as had already been publicly announced. Mr. Neal has been a strong advocate of compulsory saving all along and therefore he readily made forced saving the "hub" of the whole plan.

September 3, 1942

MEMORANDUM FOR THE FILES

Subject: Minutes of meeting in Mr. White's office on the disposition of 5 million ounces of ordinary silver, September 2, 1942.

Present: Mr. White, Mr. De Bols, Mr. Bremer, and E. M. Bernstein for the Treasury; Mr. McGregor and Mr. Murphy for W.P.B.; and Mr. Warfield of Metals Reserve Corporation

Mr. White opened the meeting with a question on the shortage of silver for war purposes. Mr. Murphy said that there would be no shortage now if all domestic silver is made available. Mr. White mentioned the desirability of making sure that low-priced foreign silver went into war production on Government account.

The question arose of whether newly-mined domestic silver would be delivered to the mints or to the market. Mr. Bernstein pointed out that the largest single refinery is already taking advantage of the Treasury's postponement of delivery and is offering silver to the market. The best hope would be that all the refiners would be eager to take care of their commercial customers and would provide them with newly-mined domestic silver instead of delivering such silver to the mint. Mr. Murphy said that some silver might be sent to the mints in order to force a shortage so that the price would be revised upward to 80 or 90 cents. Mr. White said that if any considerable amount of newly-mined domestic silver is delivered to the mints we would look into the reasons.

Mr. White inquired about the possibility that silver held by fabricators with low priority ratings would be made available for essential uses after October 1. Mr. Murphy pointed out that there was no compulsion in the conservation order for them to sell although such compulsion could be applied by the W.P.B. It was hoped that the price of 45 cents may induce fabricators with low priority ratings to dispose of the silver that they were not permitted to use.

Mr. White raised the question of the disposition of the 5 million ounces of ordinary silver. He said that the Treasury had thought that it could be sold through the Metals Reserve Corporation at 45 cents an ounce without any cost or loss to Metals Reserve. Mr. Warfield said that the Metals Reserve Corporation was not ordinarily engaged in selling silver and that it would prefer to have the Treasury do it.

- 2 -

Division of Monetary
Research

Mr. White raised the question of what need there was to have the Metals Reserve do it, and the only reason presented was that it might have a bad psychological effect to have silver coming out of the Treasury as it would encourage silversmiths to put on a drive for more silver from the Treasury. Mr. White said that he did not regard that argument as impressive although it may have merit.

Mr. Murphy expressed a preference for having the Metals Reserve undertake this transaction although he admitted that W.P.B. could provide the Treasury with a list of suppliers holding high priority ratings for war purposes totalling 4.9 million ounces.

Mr. Warfield then pointed out that it would take longer for Metals Reserve to sell than for the Treasury, because they would have to go through the process of setting up on their books the necessary accounts for the purpose. However, if the Treasury or W.P.B. insisted on having Metals Reserve handle it, he would like to have an opinion that the Treasury was empowered to dispose of the silver and he would like to have a statement of the cost of the silver to the Treasury and assurance that no loss would be suffered by Metals Reserve.

Mr. Murphy stated that he would like to reconsider the question with W.P.B. officially, and if necessary have a letter sent from Mr. Nelson to the Secretary indicating a preference, if there is one, for having the transaction go through Metals Reserve.

E. M. Bernstein

EMB

Treasury Department 11
Division of Monetary Research

Date Sept. 2, 1942

To: Miss Chauncey

The Secretary decided that
his letter should not be sent at
his time.

H.D.W.

MR. WHITE
Branch 2058 - Room 214½



TREASURY DEPARTMENT

WASHINGTON

Dear Mr. Chancellor:

During the past 18 months this Government, as you know, has taken many steps to assist the British Treasury in building up a gold and dollar balance and in maintaining that balance at a level deemed necessary for the efficient prosecution of the war. The completion of several arrangements between the Army and the British Supply Council in North America makes this an appropriate time to review the accomplishments of this program.

The total of United States Government purchases of British armament facilities, contracts, and products now amounts to over \$400 million as follows:

Cash refunds or relief
from commitments
(In millions)

Transfers of facilities

1. Tennessee Powder Company	\$21	
2. Machine gun plants	24	
Buffalo Arms Company		
Colts Patent Firearms Company		
High Standard Manufacturing Co.		
Kelsey-Hayes Wheel Company		
3. Todd shipbuilding facilities	12	
Todd-California Shipbuilding Corp.		
Todd-Bath Iron Shipbuilding Corp.		
4. Other facilities for which purchase agreements are being negotiated:	45	
New Jersey Powder Company		
Packard Motor Car Company		
Curtiss-Wright Corporation		
General Motors Corporation		
Pullman Standard Car Mfg. Co.		
Pressed Steel Car Company		
Idms Locomotive Company		
Republic Steel Corporation		
Western Cartridge Company		
Remington Arms Company		\$102



Transfers of contracts

1. Machine guns	\$ 28	
Buffalo Arms Company		
Colts Patent Firearms Company		
High Standard Manufacturing Co.		
Kelsey-Hayes Wheel Company		
2. Tennessee Powder Company	6	
The terms of this transfer called for cash refunds of \$6 million and relief from commitments of \$29 million. However, the Treasury understands that the British contract for the product of this plant was not a firm commitment, and we have not, therefore, included the \$29 million.		
3. New Jersey Powder Company	49	
4. Vultee Airplanes	12	
5. Remington Arms Company	33	
6. Savage Arms Company	25	
7. Mack Trucks, Incorporated	4	
8. Pressed Steel Car Company	6	
The preliminary contract for this transfer calls for payments not to exceed \$9 million. It is expected that the total payment will be about \$6 million.		
8. Ordnance contracts	84	
Under the terms of this transfer the War Department has agreed to the take-over of some 44 British contracts for ammunition, explosives, and tanks, aggregating \$84 million.		
	—	\$247

Payment for materials diverted from British contracts for the uses of the United States.

1. Aircraft items	\$ 70	
An additional payment on these items is expected when the values of the materials diverted are finally determined.		
	—	70
Grand Total		<u>\$419</u>

- 3 -

The cooperation of the War Department, the Maritime Commission, the Lend-Lease Administration, and the Defense Plant Corporation has made possible the completion of this program.

Very sincerely yours,

Secretary of the Treasury

Sir Kingsley Wood,
The Chancellor of the Exchequer,
London, England.

SEP 2 1942

My dear Dr. Herrera-Arango:

This is in reply to your letter of August 13, 1942, enclosing an informal letter to the Secretary of the Treasury from the Ambassador of Cuba entering an order for approximately \$5 million of gold.

The Treasury has taken all of the necessary steps for the sale of this amount of gold to the Cuban Government as requested in these letters.

Sincerely yours,

(Signed) H. D. White

H. D. White
Assistant to the Secretary

Dr. Roca Herrera-Arango,
Second Secretary, Cuban Embassy,
2630 Sixteenth Street,
Washington, D. C.

EMB:jmr:1 9/2/42

C
O
P
YEMBAJADA DE CUBA
Washington, D. C.

August 13, 1942.

Mr. Harry D. White,
Assistant to the Secretary,
Treasury Department,
Washington, D. C.

My dear Mr. White:

With reference to my telephone conversation of yesterday, and pursuant to the suggestion made by Mr. E. M. Bernstein of your Department, I beg to enclose an informal letter addressed to the Secretary by the Ambassador, entering an order for the purchase of approximately \$5,000,000.00 in gold, pursuant to the agreement of July 6, 1942.

Sincerely yours,

/s/ Raoul Herrera-Arango
Raoul Herrera-Arango
Secretary of Embassy

EMBAJADA DE CUBA
WASHINGTON, D. C.

August 13, 1942.

INFORMAL

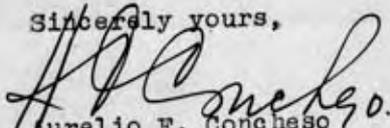
Honorable Henry Morgenthau, Jr.,
Secretary of the Treasury,
Washington, D. C.

Sir:

Pursuant to the agreement of July 6, 1942, under which the Government of the United States undertakes to sell gold to the Government of the Republic of Cuba from time to time under stated conditions, and to the instructions received from my Government, I hereby beg to enter an order for the purchase of approximately \$5,000,000.00 in gold, said gold to be earmarked for the account of the Treasury of the Republic of Cuba at the Federal Reserve Bank of New York.

My Government would wish, if this be agreeable to the Government of the United States, to make payment for this gold at the Havana branch of any American Bank which the Treasury may designate, upon receipt of notice of earmarking and total cost thereof to the Cuban Government.

Sincerely yours,


Aurelio F. Conchoso
Ambassador.

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Sept. 2, 1942

Mr. Liversy

Mr. White

Will you please send the attached telegram to the American Embassy, Chungking,
China.

RH:lc:9/2/42

September 2, 1942

TO: Adlai, Chungking, China.
FROM: Secretary of the Treasury.

Reference your cable of August 24, TF-55, regarding Central Bank of China application.

(a) Treasury is not sure that it understands purpose of suggestion made by British member of the Board that \$1 million of the sterling assets of the Board should be kept to meet current liabilities. It is not clear as to the significance in this connection of the difference between liabilities incurred during the past few months and liabilities to be incurred during the coming months, particularly since the demands of the Board for sterling already exceed its assets. Please inform us by cable as to your reaction to this proposal of the British member. It will be recalled that in our cables of May 2 to you and of June 16 to Mr. Fox it was pointed out that the Treasury assumed that the Board would not use its dollar funds for the purchase of sterling until the sterling assets had been exhausted.

(b) Treasury would like to have more detailed account of Central Bank's application, including application for sterling, since meeting of Bank's application will necessitate calling on the U. S. contribution of \$75 million and since the dollar assets of the Board will be used to purchase sterling. The Secretary must obtain this information to fulfill his obligations to Congress.

107/cfs
W/AS

Distributed to: ~~Secretary~~ (H.M.B.)
Mr. Bell
Mr. Paul
Mr. White (Friedman)
Mr. Friedman
Mr. B. Bernstein
Mr. H.M. Bernstein
Mr. Dietrich

(From E. Ayers - Em. 317)

BRITISH MOST SECRET
U.S. SECRET

OPTEL No. 305

EGYPT. During the 2nd September the main enemy forces were concentrated in the area southwest of ALEM EL BUEIB with their flanks protected by an armoured screen. Our main forces remained in their battle positions all day without being engaged. Enemy mechanical transport columns were engaged continuously by our artillery and by our mobile forces in the south. Our ground troops confirm the excellent results of the R.A.F. bombing which together with the artillery fire caused many casualties and fires and kept the enemy mechanical transport on the move.

During the night 2nd/3rd enemy laagers were attacked and the R.A.F. had most successful bombing on the best target yet seen in a locality about ten miles southwest of ALEM EL BUEIB. At first light on 3rd our armoured patrols pushed forward into close contact with the enemy protective screen and at 1330 air reconnaissance reported a general enemy movement westward in three main columns in the back area. In the forward area the enemy withdrew slightly. Our forces continue to harass him from all sides.

OPTEL No. 306

Information received up to 7 A.M., 4th September, 1942.

1. AIR OPERATIONS

WESTERN FRONT. Night 2nd/3rd. KARLSRUHE 170 aircraft dropped 190 tons of H.E. and 180 tons of incendiaries including 54 4,000 lbs. and 56 2,000 lb. bombs. There was only slight haze and crews were able to pin-point the objective. Fires were well concentrated and towards the end of the attack very large fires were reported blazing in the centre of the town and in the docks with smoke rising to a great height. Defences were slight to moderate and there were few night fighters.

3rd. Five enemy aircraft crossed our coasts. Spitfires destroyed one and damaged another.

3rd/4th. Eleven bombers were sent to attack EMDEN. Two are missing.

EGYPT. 1st/2nd. Enemy tanks and transport were continuously bombed and considerable damage was inflicted on mechanical transport. TOBRUK was also bombed. A 2,500 ton ship southbound off DERNA was hit by torpedo and another ship in the same convoy by bombs.

2nd. 167 bomber and 507 fighter sorties were flown. Enemy concentrations were subjected to ten attacks. Fourteen enemy aircraft were shot down, seven probably destroyed and seven damaged by fighters and four more were destroyed by anti-aircraft. Ten of our fighters are missing but four pilots are safe.

3rd/4th. Our aircraft attacked an enemy convoy off DERNA hitting a destroyer and a tanker.

- 2 -

MEDITERRANEAN. 1st. U.S. bombers hit a ship at HERAKLION, CRETE.

2nd/3rd. Naval aircraft scored two torpedo hits on an escorted 5,000 ton vessel off CAPE SPARTIVENTO (ITALY). The ship was later reported aground. Wellingtons hit a 4,000 ton tanker off the West Coast of GREECE.

BURMA. 31st. U.S. medium bombers with fighter escort attacked barracks warehouses and the railway terminus at MYITKYINA.

2. HOME SECURITY

Yesterday morning two 500 KG bombs dropped from a low level at SELSEY bounced and exploded in the air damaging 100 houses and causing 27 service casualties. Four H.E. bombs were dropped on a railway station in SOMERSET blocking the main Great Western Line for a short time.

SEP 8 1942

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OFFICE OF STRATEGIC SERVICES
WASHINGTON, D. C.

September 2, 1942

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

Dear Henry:

The attached is a summary of the
Weekly Intelligence Report issued by the
British Ministry of Information for the week
of August 28.

Sincerely,

Bill
William J. Donovan
Director

SECRET**Developments on Industrial Resources**

1. The delivery of an unstated number of new type 50 locomotives from Germany to Roumania and thought to be in the order of several hundred, is said to be assured. Also, Roumania is to receive 60,000 tons of rails from Germany.
2. Reports, in which the details are vague say that rail freight traffic between Turkey and Bulgaria via the Maritza Bridge without transshipment at the border has been reestablished.
3. Germany is now sending two to three locomotives a day, and 42 freight cars every other day. As yet it is not known whether this is under the Clodius agreement or under earlier arrangements.
4. 1100 locomotives which the Germans requisitioned from the French have been taken over from the Nord region.
5. The Montecatini aluminum plant has been having difficulty with the petroleum coke which it has been receiving from Germany for electrode purposes. Italian petroleum coke has been sent to Germany for processing. The ash content has been found so high as to impair seriously the usefulness of the material upon its return.
6. An intercept shows that Krupp is redesigning locomotive bearing lubrication ducts to avoid clogging which was experienced last winter on the Russian front.
7. In synthetic oil manufacture the substitute for a cobalt catalyst is sintered iron ore of a special type. In May Germany imported about 4000 tons of this, and in June 6,851 tons. The plant for the special treatment required by this ore is of the type which is required for nickel refining. It is thought that the Oppau Nickel refinery has a capacity just sufficient for handling Petsamo ore.

8. There are reports of French machine tool installations being dismantled and shipped to Germany, and they are particularly prevalent in regard to the Renault works. These are regarded with reserve by M.E.W.

9. Under the new decree, passenger travel on German railroads is to be confined to that essential for war purposes. On the other hand, the freight position seems slightly easier and although goods will not be needed for some months, shippers have been urged to move them before the harvest season.

Developments Regarding Shipping

1. It has been announced by the Germans that they will move idle cargo handling machinery from Holland to Baltic State ports where installations were destroyed by the retreating Russians.

2. In July a cargo of rails was shipped to Nemours from Marseilles, perhaps for construction purposes on the trans-Saharan line. Reports on the rate of present construction, if any, of such a line are unsatisfactory and conflicting.

3. Intercept source indicates that the French ship Nevo arrived in Marseilles via North Africa in August having left Hanoi in July. Cargo particulars are not available.

4. All German coal for Finland and Sweden must pass through Rotterdam. This may be designed to increase the carriage of Swedish iron ore to Rotterdam in addition to easing German coal transport problems.

SECRET

September 3, 1942
10:04 a.m.

Robert
Rouse: Good morning, sir.

HMJr: How are you?

R: Pretty good, and you?

HMJr: I'm all right. Look, Rouse, do you think I ought to have some of these bond people down tomorrow or wait till Tuesday? From New York.

R: I think it might be a good idea to have them down tomorrow, sir.

HMJr: You do think so?

R: Yeah, because it - you want time to make up your mind afterwards rather than be hurried on Tuesday, you see, Monday being a Labor Day holiday.

HMJr: Well, now I can give you - can you come?

R: Yes, I can come.

HMJr: All right, well, let's say I give you from ten to eleven, and from eleven-fifteen to twelve.

R: Right.

HMJr: How's that?

R: Good.

HMJr: Well, could we - now I would like to see the discount fellows....

R: Yes.

HMJr:and I would like to see, what's-his-name....

R: Devine?

HMJr: Devine.

R: Yeah.

- 2 -

HMJr: And I'll leave the rest to you.

R: All right, sir. How about outside New York? Your committee pretty well covers that, doesn't it?

HMJr: Oh, I think so.

R: Yeah.

HMJr: I don't think bringing in Detroit helps much.

R: No.

HMJr: What?

R: No, and you've got Boston and Chicago and St. Louis in your other group.

HMJr: Yeah, yeah. And I'd allow these fellows....

R: Twenty minutes?

HMJr: Twenty minutes, yes.

R: Right.

HMJr: That means I can see three in an hour.

R: Well, I'll - I'll confirm who is coming and the appointments later.

HMJr: Yeah, would you - would you mind - no, you've got the Fed. Let Lieutenant Commander Stephens know.

R: All right. Good.

HMJr: Give it to him.

R: Yeah.

HMJr: Thank you.

R: Right, sir.

September 3, 1942
10:58 a.m.

HMJr: Hello.

Operator: Judge Rosenman.

HMJr: Hello.

Judge
Rosenman: Hello.

HMJr: Sam?

R: Yeah.

HMJr: What you all doing?

R: Where are you?

HMJr: Here in the Treasury.

R: Well, (laughs) did Mrs. Klotz tell you I phoned?

HMJr: Yeah.

R: Oh, well....

HMJr: Then I got this, and I wondered if I could just walk across with it, because I'm all by myself. Everybody's on the Hill. I need a little advice. I don't understand it.

R: Well, yes, except that I - I got to go in with him. He's seeing the four farm leaders today, and then the....

HMJr: What time?

R: At - at eleven, and then at eleven-thirty he's going to see the labor leaders, and I got to be in with him on both.

HMJr: Yeah, well, when - what - what are you doing at lunch time?

R: Well, at lunch I have a date. I'll - why don't I give you - do you want to make it sometime this afternoon, because we're not leaving now till tonight. It's been changed.

- 2 -

HMJr: Oh. Yes, I mean the only appointment I can't change is from three to three-thirty.

R: Well, Henry, why - why don't we make it at - well, let's see what's convenient. Two o'clock?

HMJr: Two o'clock?

R: All right.

HMJr: Where will it be?

R: By that time you'll have seen Randolph, won't you?

HMJr: Well, I don't know. He's on the Hill.

R: Well, do you want to make it later, because it - there really isn't any sweat on it. Why don't you talk with him first?

HMJr: Well, if I could make it - could I....

R: Because we're not leaving now until after dinner.

HMJr: What are you doing around four?

R: Four o'clock? It's clear so far, yeah. Want to make it at four?

HMJr: Four - four o'clock would be perfect.

R: All right.

HMJr: Well, as near as I can make out - have you got a second?

R: Yeah. I see - you see, what - I tell you what happened.

HMJr: Yeah.

R: He got a very tough letter from Budget, you know....

HMJr: Yes.

R:and last night at about eleven o'clock when we finished on the thing today, he said, "Let's see the Order in its present form." He started to go - he really went through it for the first time....

- 3 -

HMJr: Yeah.

R:and when he came to this thing, F told him just what the facts were, that Smith was kicking and had sent them a letter, and he said he remembered the letter and he'd read it....

HMJr: What was Smith kicking....

R:and he wanted to take out that part about fiscal policy, and so then he - he really worded it the way it is now....

HMJr: But....

R:and he put in - I said, "The same thing would apply to Eccles as applies to Henry," so he wrote in that member of the Reserve Board - Governor of the Reserve Board.

HMJr: Yeah, but what I don't understand, Sam, is this, and maybe - should I worry or shouldn't I? Do you think....

R: No, I think it's all right, Henry.

HMJr: Well, let me just take one second.

R: I mean if you want my opinion, I think it's okay.

HMJr: Well, I - I'm asking you now....

R: What this does is to exempt you from directives, and merely says that with respect to you and Eccles on - how's he got it - public revenues....

HMJr: Well, let me just read, because it looks - the way I read it, it looks as though it singled us out. May I just take one....

R: Yes.

HMJr:there's one word there - "but the administration activities relating to the national economics shall remain with the departments and agencies now responsible for such activities, but such administration is to conform to the direct policies issued by the administrator, except with respect to the public revenues...." and so forth. Now

cont.

- 4 -

HMJr:
(cont.)

this - "the administrator shall only make such recommendations as he deems desirable to the Secretary of the Treasury." It's the word "desirable" - I don't understand it.

R:

Well, he can - shall only make such recommendations as he thinks should - well, desirable - what he thinks ought to be done.

HMJr:

Well, he could - that means he could tell me anything.

R:

Well, only recommendations. But the idea of the except business is that you - you see, it says that you should follow policy - that all should follow policy except you and Eccles.

HMJr:

Oh, and that is he....

R:

That was the intention of it.

HMJr:

Well....

R:

You see, where it says everybody else - the administration - the administrative details are left with the different departments....

HMJr:

Yeah.

R:

....but as to policy everybody has to follow Mr. X, and then it says except that as to revenues, etcetera - the theory is you don't have to follow that policy, and all that he can do is make recommendations to you.

HMJr:

You think it's all right.

R:

I think it's all right, but we could put in some words that - well, that - I was thinking of a way of putting in that you don't have to follow the recommendations if you don't want to - I mean, that - that would be a strange language in an Order.

HMJr:

Well, what I was thinking - of such recommendations.

R:

Yeah.

- 5 -

HMJr: I - I mean, I'm not a lawyer....

R: Yeah.

HMJr:"to the Secretary of the Treasury and to the...."
- "as I, the Secretary of the Treasury, deem desirable." Do you see what I mean?

R: Well, no, that isn't - that wouldn't be - that wouldn't be right if it was - the purpose of this is to say that if he says to Leon, "You got to raise the price"....

HMJr: Yeah.

R:that Leon's got to do it, you see....

HMJr: Yeah.

R:that the prices have to be raised. Now if he says to you, "You got to issue a three per cent bond instead of two per cent bonds," that's merely a recommendation which you don't have to follow.

HMJr: Well....

R: That - that's the - that's the purpose of it.

HMJr: Well, this is language, and if you could let me come over at four, will that be a firm appointment?

R: Four o'clock, yeah.

HMJr: Is that firm?

R: Right. And if - have Randolph try to get up some language which is - which - which he thinks is better.

HMJr: Uh huh.

R: You understand the purpose of it?

HMJr: I now do. I didn't before.

R: Yes. Well, now if that language - that's midnight language and it may not be the best. What the President wanted to cut out was the statement that

cont.

- 6 -

R: (cont.) you alone were responsible for fiscal policy because that's what Budget complained about. And that's a major scrap that shouldn't be settled in an Order that has nothing to do with it.

HMJr: No.

R: That's what he wanted to take out.

HMJr: Well, they claim - they claim they're responsible to....

R: Well, it's - it's a long memo. They claim they have a joint responsibility.

HMJr: I see.

R: And that ought to be settled some time, but certainly not in a parenthesis in an Executive Order.

HMJr: I agree with you.

R: So - but - but you understand the purpose of this now is to say that so far as you and Eccles are concerned on fiscal policy, he doesn't issue directives to you but only recommendations.

HMJr: Yeah.

R: You got that?

HMJr: I got it.

R: Now if you want to change the language in a way that will do that, I'm sure the President won't mind.

HMJr: I got that. And you will - we'll be over at four and if the boys aren't satisfied, I'll....

R: Let them - let them suggest some changes in language and I - I can pass on that in a minute.

HMJr: Right.

R: Okay.

HMJr: We'll be there at four.

- 7 -

R: All right.
HMJr: Thank you.
R: Okay.

September 3, 1942.
11:37 a.m.

HMJr:to be left alone with Mr. Paul on the Hill. I've got to have somebody that functions in the General Counsel's office.

Huntington Cairns: Well, I'll come right up and....

HMJr: Well, I mean here something has broken. I've been trying for one - since eleven o'clock to locate somebody. Bernstein's away, you're out of the office, the Executive Order has come over from the White House vitally affecting the Treasury, and nobody's here.

C: I left a man at my desk, and Mr. Tietjens is in charge.

HMJr: Well, Tietjens - what the hell does Tietjens know about this?

C: Well, I'll be there.

HMJr: What are you doing over at the Art Gallery?

C: The meeting has just adjourned. I represent....

HMJr: Well, I mean what - what - I mean I'm left here absolutely flat with nobody.

C: Well, I'll be there in two minutes.

HMJr: All right.

C: I'll come right up.

September 3, 1942
4:56 p.m.

Operator: Go ahead.

HMJr: Hello.

Myron Taylor: Mr. Secretary.

HMJr: Yes.

T: How are you?

HMJr: Fine.

T: This is Myron Taylor.

HMJr: How do you do?

T: I wanted to get a little information. Mrs. Taylor has been asked in New York by the Woman's Voluntary Service Organization to accept the National Chairmanship of the Bond and Stamp Sales Committee of the National - of the Woman's Voluntary. Before she undertakes to do much about it, in talking it over....

HMJr: Yes.

T:she decided that she would like to know whether this activity by the Woman's Voluntary is acceptable to the Treasury Department, and if she went into it, she would first try to discover a chairman of each State....

HMJr: Yes.

T:among the Woman's Voluntary Organization to act in each State to promote the sale of bonds and stamps. Now is that consistent with what you are already doing, and....

HMJr: Well....

T:do you favor it?

HMJr:I - I can't tell you off-hand, but if you could - where could you be reached tomorrow forenoon?

- 2 -

T: I'll be in the Mayflower until I go to Mr. Berle's office at half-past ten.

HMJr: Mayflower?

T: Yes.

HMJr: Well, I'll have Miss Elliott, who is in charge of our women, you see....

T: Yeah.

HMJr:phone you before ten-thirty tomorrow morning.

T: All right.

HMJr: I - I can't answer you myself, but Miss Elliott of the University of North Carolina, who's with us....

T: I wonder if it would help if I sent to you today a copy of the letter that Mrs. Taylor addressed to Mrs. King and Mrs. MacLean in which she raises this question....

HMJr: Good.

T:and then you'll have everything before you before she telephones.

HMJr: We'll put it all into a package, and Miss Elliott will - will phone you tomorrow morning at the Mayflower....

T: It would suit me better if she phoned around two-thirty.

HMJr: Well, why don't you - why don't you - at the Mayflower?

T: Yeah.

HMJr: At two-thirty?

T: Yeah.

HMJr: I'll tell - I'll ask her to phone you at two-thirty at the Mayflower.

- 3 -

T: Or three o'clock, either one that suits her.

HMJr: Well, let's say two-thirty.

T: What's her name?

HMJr: Miss Elliott.

T: Elliott.

HMJr: Yes.

T: And how are you?

HMJr: I'm fine.

T: Good.

HMJr: I'm fine. I don't know - I can't tell you, but she can. I think if everything is all right, I think it would be a fine thing for your wife to do.

T: Well, I don't want her to get into it too deep in something, you know, that....

HMJr: No.

T:that's going to make a lot of hard work and trouble, but....

HMJr: Yeah, I think it would be a fine thing, but I - I don't want to - we have Miss Elliott in charge of all women activities on War Bonds and I'd like to have her clear it.

T: All right. Thank you very much.

HMJr: Thank you.

T: Goodbye.

Original to Miss Elliott

September 3, 1942

Myron Taylor phoned the Secretary this afternoon, and said that Mrs. Taylor had been asked in New York by the Woman's Voluntary Service Organization to accept the National Chairmanship of the Bond and Stamp Sales Committee of the Woman's Voluntary. Before Mrs. Taylor undertakes to do much about it, she decided that she would like to know whether this activity by the Woman's Voluntary is acceptable to the Treasury Department, and if she went into it, she would first try to discover a chairman of each State among the Woman's Voluntary Organization to act in each State to promote the sale of bonds and stamps.

Mr. Taylor asked whether this was consistent with what the Treasury is already doing and whether Mr. Morgenthau favored it. The Secretary said he couldn't tell him off-hand, but he would be glad to have Miss Elliott call him tomorrow. It was agreed that Miss Elliott should phone Mr. Taylor tomorrow at 2:30 at the Mayflower.

Mrs. Taylor has written a letter to Mrs. King and Mrs. MacLean in which she raises this question, and Mr. Taylor will send the Secretary a copy of this letter.

copy to Miss Smith 189
9/4/42.

Dear Mr. Secretary:

Herewith the letter I referred to in our conversation this afternoon.

Myron C. Taylor
Myron C. Taylor

Washington, D.C.
September 3, 1942.

COPY

MEMORANDUM OF THANKS TO MRS. TAYLORfromTHE AMERICAN WOMEN'S VOLUNTARY SERVICES

The Board of Directors met yesterday at their monthly meeting and they were overjoyed that you are interested and have accepted the National Chairmanship for our bond and stamp sales.

They want to help you in every possible way and asked that I, as Chairman, personally convey to you the fact that the entire Board is overjoyed and stand firmly behind you to help in any way they can.

July 8 1942
(By telephone
to Mrs. Taylor's
Secretary)

Isabella Greenway King,
Chairman.

COPY

Murray Hill 3-0835

AMERICAN WOMEN'S VOLUNTARY SERVICES, Inc.
New York City
181 Madison Ave.

Office of the President
Mrs. Alice T. McLean

Defense Division

July 9 1942

Air Raid Protection
Uniforms & Insignia
Other Defense Activities

Mrs. Myron C. Taylor
16 East 70th Street
New York City

My dear Mrs. Taylor:

At the request of our Board of Directors I am hereby appointing you National Chairman of A.W.V.S. War Savings Staff of the U. S. Treasury Department. We are delighted that you are willing to undertake this important phase of our work for us, and feel confident of its national expansion and success under your guidance.

I can't tell you how happy I am personally to think of working so closely with you. It will be a joy to have you taking an active part in our organization.

Yours sincerely,

(Sd) ALICE T. McLEAN,

President.

COPY

598 Madison Avenue
Room 1203
New York
September 2 1942

Mrs. Isabella Greenway King,
Chairman of the Board,
American Women's Voluntary Services, Inc.,
181 Madison Avenue, New York.

My dear Mrs. King,

I am writing this letter to make more clear my position as National Chairman of the War Bond and Stamp Sales project of the American Women's Voluntary Services, Inc., my appointment having been covered by your message of July 8 1942 reciting the action of its Board of Directors, and by the letter of Mrs. Alice T. McLean, President, dated July 9 1942, appointing me National Chairman of A.W.V.S. War Savings Staff -- copies of which are attached hereto.

My understanding of the appointment was that my authority was to select candidates for State Chairmen of the Bond and Stamp Sales in each State, wherever a Chairman had not been appointed. I would submit and recommend the names of these candidates to you and through you to the Directors of the A.W.V.S. for approval, and with this approval the women in question would be appointed Chairmen by your office and would proceed to organize the sale of War Bonds and Stamps in their respective States.

After the approval and appointment by you of these State Chairmen it would be the duty of our office to maintain contact with them, to encourage them in organizing their local units, etc., and then to report to you at proper intervals the results of these state-wide efforts.

It was not my thought or intention that this office should make contact with particular groups within the States when once a Chairman was selected and appointed. That would be the duty of the State Chairman.

Also it is my understanding that the Bond and Stamp sales activity within the American Women's Voluntary Services has been encouraged and approved by the United States Treasury Department.

Before proceeding further with my activities, I feel that my understanding of the matter as covered by the above paragraphs must be clarified and given further written approval by you and the Directors of the American Women's Voluntary Services and by the Treasury Department.

Most sincerely yours,

(Mrs. Myron Taylor)

Diary

September 3, 1942

MEMORANDUM FOR THE SECRETARY'S DIARY:

Secretary Morgenthau, Mr. Gaston, and Mr. Cairns saw Judge Rosenman at the White House at 4 o'clock today with respect to the proposed Executive Order creating an officer to be known as the Economic Stabilization Administrator. Judge Rosenman was handed the attached Redraft No. 1, which Judge Rosenman, after reading, stated was satisfactory. However, Secretary Morgenthau remarked that Judge Rosenman was a friend of the Treasury and requested Mr. Cairns to show him the attached Redraft No. 2. Judge Rosenman said he thought Redraft No. 2, for his purposes, was better than Redraft No. 1 since it was less of a red flag. He said he would prefer to use No. 2 if it was entirely satisfactory to Secretary Morgenthau. Secretary Morgenthau reread No. 2 and said that it was entirely satisfactory to him. Judge Rosenman then stated that it would be used without change in the Executive Order. Mr. Cairns told Judge Rosenman that the reason for redrafting the President's language, as it appears in the original draft of the Executive Order,

- 2 -

was that the language was ambiguous. As the language now appears, it might mean that the Administrator was not under a duty to make recommendations to the Secretary, but that he could make such recommendations as seemed to him desirable. These recommendations might be binding since the Executive Order did not state that he could not issue directives to the Secretary. Judge Rosenman said he thought the point was well taken and he would adopt the redraft. Judge Rosenman added that as the Secretary knew he was, of course, opposed to the exception as a policy matter. He said that Leon Henderson was raising the devil because the Secretary was excepted and he knew that others, such as Jesse Jones, would raise the devil when they heard of it.

Huntington Cairns

Attachments.

3. The guiding policy of the Administrator and of all departments and agencies of the Government shall be to stabilize the cost of living and to insure the fair and equitable distribution and allocation of materials and commodities, including agricultural commodities, and it shall be the duty and responsibility of the Administrator and of all departments and agencies of the Government to cooperate in the execution of such legislative programs as may be necessary to that end. The administration of activities related to the national economic policy shall remain with the departments and agencies now responsible for such activities, but such administration shall conform to the directives on policy issued by the Administrator, except that with respect to public revenues, borrowings, credits, taxation and public finance, the Administrator shall not issue directives pursuant to this Order, but shall only make recommendations to the Secretary of the Treasury, and to the Board of Governors of the Federal Reserve System.

3. The guiding policy of the Administrator and of all departments and agencies of the Government shall be to stabilize the cost of living and to insure the fair and equitable distribution and allocation of materials and commodities, including agricultural commodities, and it shall be the duty and responsibility of the Administrator and of all departments and agencies of the Government to cooperate in the execution of such administrative programs and in the development of such legislative programs as may be necessary to that end. The administration of activities related to the national economic policy shall remain with the departments and agencies now responsible for such activities, but such administration shall conform to the directives on policy issued by the Administrator, except that with respect to public revenues, borrowings, credits, taxation and public finance, the Administrator shall only make recommendations to the Secretary of the Treasury, and to the Board of Governors of the Federal Reserve System, pursuant to this Order.

September 3, 1942.
5:06 p.m.

HMJr:in all this excitement. Rosenman wants me to tell Paul that in the light of what we said today and everything else, should the President say anything about taxes in this message Monday night, you see....

Huntington
Cairns:

Yes.

HMJr:and if he should -- he's already sent something over, you see --

C: Yes.

HMJr:he could give it to me tomorrow afternoon when I go up to the country, and I could take it with me, you see?

C: Yes.

HMJr: And I could deliver it to Rosenman. You - are you following me?

C: Well, I'm a little mixed up.

HMJr: For the President's Labor Day speech....

C: Yes.

HMJr:Paul has already supplied him with material on taxes.

C: Yes.

HMJr: Now in the light of what I said today on the Hill, does Paul want to change it any?

C: I see.

HMJr: And if he does, would he rewrite it....

C: I see.

HMJr:and give it to me tomorrow afternoon to take up to Hyde Park.

- 2 -

C: Fine.

HMJr: Okay?

C: Fine. What time are you leaving?

HMJr: Well, you better tell him three o'clock.

C: All right, fine.

HMJr: See?

C: Fine. I'll tell him.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

Sub
149

DATE

September 3, 1942

TO Secretary Morgenthau
FROM Mr. Cairns

The Executive Order creates an officer to be known as the Economic Stabilization Administrator. That officer will be a Special Assistant to the President and will be in the Office for Emergency Management. There is also created an Economic Stabilization Board to advise the Administrator. You will be a member of that Board.

The Administrator will have complete control of policy in connection with the general economy of the country, including purchasing power, profits, prices, wages, rationing, cost of living, saving, movement of labor, private credit, subsidies, and related matter.

The Order provides that until otherwise determined by the Administrator all wage rates shall be frozen, except that adjustments may be made to meet rising costs of living, to eliminate sub-standards of living, to correct serious inequalities, and to make adjustments

- 2 -

for increased productivity of workers. Increases in salaries above \$7500 are frozen even tighter.

The Administrator is given control over the fixing of prices and allocation of agricultural commodities, the prices not to be fixed below parity.

The Administrator may order any department or agency of the Government to exercise any powers which it has in order to carry out the orders of the Administrator with respect to wages and agricultural commodity prices and allocations.

10c

September 3, 1942

Reading copy of the Secretary's statement before
the Senate Finance Committee, meeting in Executive Session,
when he proposed the Spendings Tax.

I have come before you today with a program to raise substantial additional sums to finance the war effort. I intend to leave the details of the presentation to Mr. Paul and his associates and to limit myself to emphasizing the gravity of the situation as I see it and the imperative need for legislation along the lines we are suggesting.

Up to this point our huge war expenditures have been financed in an orderly way and with a minimum of inflationary effects. But the more successful the war production program becomes, the greater are the dimensions of the fiscal problem we have to face.

- 2 -

We have to plan for expenditures of eighty billion dollars in the present fiscal year, while the revenue in sight on the basis of the tax bill now before you is only approximately twenty-four billions.

The Treasury has sought diligently and will continue to seek funds from those sources where borrowing will have the least inflationary effect, and we have done so with what I believe to be most gratifying results. We can foresee with confidence provision for the Government's fiscal needs for the remainder of this calendar year.

- 3 -

But I am here today to tell you frankly that I need your help in the form of legislation which will enable me to meet, with the same degree of confidence, the much greater problem of raising the necessary funds for next year.

The legislation which we are proposing has a double purpose. The first purpose is to draw into the Treasury substantial additional funds out of the earnings and savings of the people. The second purpose is even more important. It is to reduce consumer spending directly by withdrawing funds otherwise available for expenditure, and to reduce it also indirectly by creating a strong tax incentive to saving.

- 4 -

The measures we propose are two: first, a tax on consumer spending which will reach into the lowest income groups above the level of bare subsistence income and will provide high penalty rates for luxury spending; second, a further lowering of the exemptions from the income tax applying to family income.

The two proposals will reach into incomes aggregating some sixty-five billions of dollars and will draw into the Treasury an estimated six and one-half billion dollars otherwise available for consumer spending.

- 5 -

But of this total some four and a half billions, although raised as a tax, will be treated not as revenue but as a debt to the individuals from whom it was collected, to be repaid after the war.

Revenue is not the sole purpose, nor even the primary purpose, of either of these proposals. Their main purpose is to restrict consumer spending so that, as far as possible through fiscal means, we may avoid the perils of inflation in the huge financing program that we have ahead of us.

- 6 -

It can be expected that the new spending tax will reduce in many individual cases the amounts which workers can afford to set aside for War Bonds under voluntary payroll deduction plans. In the face of present conditions we can no longer afford to rely entirely upon voluntary lending. The new proposals are intended, therefore, to supplement the voluntary bond purchase program.

It is my belief that the voluntary War Bond program has produced and will continue to produce a great contribution to the nation's war effort. This is due to the unselfish service that hundreds of thousands of men and women throughout the country have given to it.

- 7 -

They deserve the thanks of the nation for the magnificent work they have done, are doing, and will, I hope, go on doing, in encouraging the American people to put their dollars to work for their country. The voluntary War Bond program will, of course, be continued.

Our present and urgent problem is to borrow the great amounts that will be needed to finance the war effort in ways that will not contribute to inflation. Inflationary pressure is created by consumer demand exceeding the supply of goods available. The Treasury is seeking in these proposals to attack the problem at its roots and to attack it drastically.

- 8 -

The control of prices is of course not exclusively a fiscal problem. But with full allowance for all that can be done through price regulation, rationing and other devices to control supply, I think that we, who are jointly responsible for tax policy and legislation, shall be doing very much less than our full duty if we do not deal with the problem as effectively as possible in the fiscal field. What I have presented is a method -- and the best method the Treasury has been able to devise -- for accomplishing this result.

- 9 -

If the proposals we make seem drastic, I should like to say with all possible emphasis that I believe nothing less drastic will accomplish the results we must have. This is no time for half-way measures.

With the fullest respect for the Committee on Finance, but with a strong sense of our joint responsibility in these critical times, I do not merely recommend bold action along these lines; I request it and I urge it most seriously, and with the profound conviction that it must be done.

September 3, 1942

Harold Graves
Secretary Morgenthau

I think you should send a telegram of my statement in full to the forty-eight State Administrators. I would send it in the form of a day letter and would file it at ten-thirty this morning.

Sent 9/3/42

C O P Y

TELEGRAM

OFFICIAL BUSINESS—GOVERNMENT RATES

FROM Mr. Graves Office - Off. of Sec.
162
BUREAU _____
CHG. APPROPRIATION Expenses of Loans -
War Savings Staff.

U. S. GOVERNMENT PRINTING OFFICE 10-1728

(Following DAY LETTER to go
to all State Administrators of
War Savings Staff.)

September 3, 1942

Following is full text of Secretary's statement this morning before Senate Finance Committee: Quote. (See attached copy of Secretary's statements.) Unquote. Please note specially that there is no intention of superseding or abandoning any aspect of voluntary plan for purchase of War Bonds. Stop. While proposal for new taxes if adopted will undoubtedly tend to reduce bond sales, the effect will be to increase rather than reduce the need for promotion efforts by War Savings Staff. Stop. Furthermore, adoption of these taxes is by no means certain, and if adopted they will in no case be effective before January 1 and possibly not until later. Stop. At an early date we intend to have conference of War Savings Staff representatives from all States to discuss problems growing out of pending tax proposals, and in meantime we hope that there will be no abandonment of your efforts in any direction. Stop. Please acknowledge by letter. Stop. Regards.

HAROLD N. GRAVES
Assistant to the Secretary.

Statement of Secretary Morgenthau
before the Senate Finance Committee,
Thursday, September 3, 1942.

I have come before you today with a program to raise substantial additional sums to finance the war effort. I intend to leave the details of the presentation to Mr. Paul and his associates and to limit myself to emphasizing the gravity of the situation as I see it and the imperative need for legislation along the lines we are suggesting.

Up to this point our huge war expenditures have been financed in an orderly way and with a minimum of inflationary effects. But the more successful the war production program becomes, the greater are the dimensions of the fiscal problem we have to face. We have to plan for expenditures of \$80 billion in the present fiscal year, while the revenue in sight on the basis of the tax bill now before you is only approximately 24 billions.

The Treasury has diligently sought and will continue to seek funds from those sources where borrowing will have the least inflationary effect,

- 2 -

and we have done so with what I believe to be most gratifying results. We can foresee with confidence provision for the Government's fiscal needs for the remainder of this calendar year.

But I am here today to tell you frankly that I need your help in the form of legislation which will enable me to meet, with the same degree of confidence, the much greater problem of raising the necessary funds for next year.

The legislation which we are proposing has a double purpose. The first purpose is to draw into the Treasury substantial additional funds out of the earnings and savings of the people. The second purpose is even more important. It is to reduce consumer spending directly by withdrawing funds otherwise available for expenditure, and to reduce it also indirectly by creating a strong tax incentive to saving.

The measures we propose are two: first, a tax on consumer spending which will reach into the lowest income groups above the level of bare subsistence

- 3 -

income and will provide high penalty rates for luxury spending; second, a further lowering of the exemptions from the income tax applying to family income.

The two proposals will reach into incomes aggregating some 65 billions of dollars and will draw into the Treasury an estimated six and a half billion dollars otherwise available for consumer spending. But of this total some four and a half billions, although raised as a tax, will be treated not as revenue but as a debt to the individuals from whom it was collected, to be repaid after the war.

Revenue is not the sole purpose, nor even the primary purpose, of either of these proposals. Their main purpose is to restrict consumer spending so that, as far as possible through fiscal means, we may avoid the perils of inflation in the huge financing program that we have ahead of us.

It can be expected that the new spending tax will reduce in many individual cases the amounts which workers can afford to set aside for War Bonds under voluntary payroll deduction plans. In the face of

- 4 -

present conditions we can no longer afford to rely entirely upon voluntary lending. The new proposals are intended, therefore, to supplement the voluntary bond purchase program.

It is my belief that the voluntary War Bond program has produced and will continue to produce a great contribution to the nation's war effort. This is due to the unselfish service that hundreds of thousands of men and women throughout the country have given to it. They deserve the thanks of the nation for the magnificent work they have done, are doing, and will, I hope, go on doing, in encouraging the American people to put their dollars to work for their country. The voluntary War Bond program will, of course, be continued.

Our present and urgent problem is to borrow the great amounts that will be needed to finance the war effort in ways that will not contribute to inflation. Inflationary pressure is created by consumer demand exceeding the supply of goods available. The Treasury is seeking in these proposals to attack the problem at its roots and to attack it drastically.

- 5 -

The control of prices is of course not exclusively a fiscal problem. But with full allowance for all that can be done through price regulation, rationing and other devices to control supply, I think that we, who are jointly responsible for tax policy and legislation, shall be doing very much less than our full duty if we do not deal with the problem as effectively as possible in the fiscal field. What I have presented is a method -- and the best method the Treasury has been able to devise -- for accomplishing this result.

If the proposals we make seem drastic, I should like to say with all possible emphasis that I believe nothing less drastic will accomplish the results we must have. This is no time for half-way measures.

With the fullest respect for the Committee on Finance, but with a strong sense of our joint responsibility in these critical times, I do not merely recommend bold action along these lines; I request it and I urge it most seriously, and with the profound conviction that it must be done.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE

September 3, 1942

TO Mrs. Klotz

FROM Secretary Morgenthau

I would like to send a copy of my statement and of Paul's statement to the big group around town - the President, the Vice President, the Cabinet, and the heads of all independent agencies. A letter should go to the President, the Vice President, and the members of the Cabinet. To the rest, just attach my card. This is to be done before I go on the Hill. I'll sign them. Certainly the one to the President I want to be done before I go on the Hill.

This is being done -

September 3, 1942

My dear Mr. President:

I am sending you herewith a copy of the statement I am making today before the Senate Finance Committee proposing a spending tax. I am also enclosing a copy of Mr. Randolph Paul's statement.

Yours sincerely,

(Signed) H. Morgenthau, Jr.

The President,
The White House.

Del. by SS Agent 9/3/42 at 10:25

File in Diary

September 3, 1942

My dear Henry:

I am sending you herewith a copy of the statement I am making today before the Senate Finance Committee proposing a spendings tax. I am also enclosing a copy of Mr. Randolph Paul's statement.

Yours sincerely,

(Signed) Henry

Hon. Henry A. Wallace,
The Vice President.

By Hand (Short) 9/3/42 10:30 a.m.

September 3, 1942

My dear Cordell:

I am sending you herewith a copy of the statement I am making today before the Senate Finance Committee proposing a spending tax. I am also enclosing a copy of Mr. Randolph Paul's statement.

Yours sincerely,

(Signed) Henry

Hon. Cordell Hull,
~~Secretary~~ Secretary of State.

By Hand (Veach) 9/3/42 10:30 a.m.

September 3, 1942

My dear Henry:

I am sending you herewith a copy of the statement I am making today before the Senate Finance Committee proposing a spending tax. I am also enclosing a copy of Mr. Randolph Paul's statement.

Yours sincerely,

(Signed) Henry

Hon. Henry L. Stimson,
Secretary of War.

By Hand (Veach) 9/3/42 10:30 a.m.

September 3, 1942

My dear Frank:

I am sending you herewith a copy of the statement I am making today before the Senate Finance Committee proposing a spendings tax. I am also enclosing a copy of Mr. Randolph Paul's statement.

Yours sincerely,

(Signed) Henry

Hon. Frank Knox,
Secretary of the Navy.

By Hand (Veach) 9/3/42 10:30 a.m.

September 3, 1942

My dear Harold:

I am sending you herewith a copy of the statement I am making today before the Senate Finance Committee proposing a spending tax. I also am enclosing a copy of Mr. Randolph Paul's statement.

Sincerely yours,

(Signed) Henry

Honorable Harold L. Ickes,
Secretary of the Interior,
Washington, D.C.

By Hand (Veach) 9/3/42 10:30 a.m.

September 8, 1942

My dear Frank:

I am sending you herewith a copy of the statement I am making today before the Senate Finance Committee proposing a spendings tax. I also am enclosing a copy of Mr. Randolph Paul's statement.

Sincerely yours,

(Signed) Henry

Honorable Frank C. Walker,
The Postmaster General,
Washington, D.C.

By Hand (Short) 9/3/42 10:30 a.m.

September 3, 1942

My dear Claude:

I am sending you herewith a copy of the statement I am making today before the Senate Finance Committee proposing a spending tax. I also am enclosing a copy of Mr. Randolph Paul's statement.

Sincerely yours,

(Signed) Henry

Honorable Claude R. Wickard,
Secretary of Agriculture,
Washington, D.C.

By Hand (Short) 9/3/42 10:30 a.m.

September 3, 1942

My dear Francis:

I am sending you herewith a copy of the statement I am making today before the Senate Finance Committee proposing a spending tax. I also am enclosing a copy of Mr. Randolph Paul's statement.

Sincerely yours,

(Signed) Henry

Honorable Francis Biddle,
Attorney General of the United States,
Washington, D.C.

By Hand (Short) 9/3/42 10:30 a.m.

September 3, 1942

My dear Frances:

I am sending you herewith a copy of the statement I am making today before the Senate Finance Committee proposing a spending tax. I also am enclosing a copy of Mr. Randolph Paul's statement.

Sincerely yours,

(Signed) Henry

Honorable Frances Perkins,
Secretary of Labor,
Washington, D.C.

By Hand (Short) 9/3/42 10:30 a.m.

September 3, 1942

My dear Jesse:

I am sending you herewith a copy of the statement I am making today before the Senate Finance Committee proposing a spending tax. I also am enclosing a copy of Mr. Randolph Paul's statement.

Sincerely yours,

(Signed) Henry

Honorable Jesse Jones,
Secretary of Commerce,
Washington, D.C.

By Hand (Short) 9/3/42 10:30 a.m.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE

September 3, 1942

TO Secretary Morgenthau
FROM Mr. Paul

You will be interested in the attached comment
by Senator Walsh on the Treasury's proposal on
spendings tax.

RSP.

September 3, 1942

C
O
P
Y

STATEMENT OF SENATOR WALSH

The Treasury's proposal is entitled to careful study and should not be rejected because it is a new and untried Tax Plan.

Aside from the rates which may necessitate some revision downward the Plan has the merit of effectively combating inflation, checking spending, and would provide a large increase in the Federal Revenue, which is absolutely necessary if the Government finances are to be kept in a sound basis during the war emergency.

THE SECRETARY OF STATE
WASHINGTON

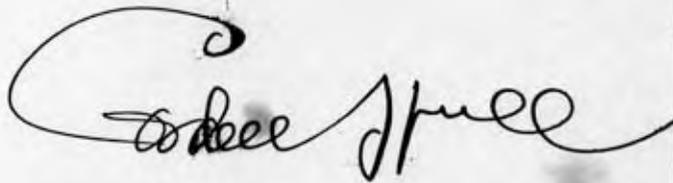
September 3, 1942

Dear Henry:

I wish to thank you for your letter of September third enclosing a statement which you are making today before the Senate Finance Committee proposing a spending tax and also a copy of Mr. Randolph Paul's statement, both of which I look forward to examining with interest.

With best wishes,

Sincerely yours,

A handwritten signature in cursive script, appearing to read "Cordell Hull". The signature is written in dark ink and is positioned below the typed name.

The Honorable

Henry Morgenthau, Jr.,

Secretary of the Treasury.



THE SECRETARY OF THE INTERIOR
WASHINGTON

September 3, 1942.

Dear Henry:

Thank you for sending me a copy of your statement prepared to be made before the Senate Finance Committee today. So far as I have been able to judge this proposal has been sound and I hope for you better luck than you have had to date.

Sincerely yours,

Harold G. Ickes

Secretary of the Interior

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

SPEAKING OF GOVERNMENTS

By SEYMOUR PERKINS, JR.

If the rest of the branches of the Government could effect a stabilization of prices such as the Treasury Department has made in the Government market, our fears of inflation would be quickly dissipated.

However, the regulation which has clamped down the Treasury market no doubt has been a lot easier to accomplish than in other fields. Everyone now appears satisfied with the 2½% long-term rate with lower coupons for the shorter dated maturities. While some may have wanted higher yields, they have seen the wisdom of the Treasury's ideas. Institutions have realized that interest rates had to be fixed, or the war financing would stall.

Accordingly, where many institutions were nervous about entering subscriptions for new cash issues when the Treasury used to give away from one to three points with allotments never amounting to more than 10%. Now you have the same institutions putting in for larger commitments with premiums amounting to only about 100-4/32nds, and allotments running up to 5%. In one case it was only a premium of eight cents per \$1,000 certificate.

The Treasury and the Federal Reserve Board have built up so much confidence in the Government market that even the layman not only is beginning to understand the necessity for stabilization of interest rates, but also the power our Government has to control them.

Tax-Exempt Bonds

For the past few weeks tax-exempt bonds have been in supply versus a small demand for the taxable issues. One reason is that many institutions which have tax problems are waiting for the new Treasury financing. But there has also been another theory circulating among Government bond circles which is extremely interesting. The idea has been advanced that banks have all the tax-exempt bonds which they want and have no extra cash with which to buy more. This condition will continue to exist for the duration, because the Federal Reserve will only free enough required reserves to take up the new cash issues; viz, the recent cut in requirements of 2% in New York and Chicago which was just about enough to tide these two districts over the last certificate issue and subsequent war loan calls.

The above argument is true in so far as it goes. There are banks who had sought as many tax-exempt bonds as they were able under previous reserve requirements, but as excess funds are released from time to time, we have reason to believe that these institutions will continue to add to their tax-exempt holdings.

We favor tax-exempt securities for the obvious reason that they are being retired at the rate of about \$3½ billion per annum. That means by 1947 approximately \$16½ billion of the present tax-exempt securities will be refunded or paid off out of a total of \$33½ billion now outstanding. Another reason in favor of tax-exempts: if a bank in the 45% tax class can improve its yield after taxes by 21 basis points over a seven-year longer bond, the purchase of the tax-exempt bond would appear reasonable. This is a comparison between 2½%, 72/87, at 161-5/32, to yield 1.33%, after the proposed 45% tax, and 2½%, 68/60, at 110-3/32, to yield 1.64%, after the proposed 21% surtax.

Another example: Treasury 2s, 1951-49, yield 1.06%, after the proposed 45%

tax, versus Treasury 2½s, 59/49, on a 1.26% basis after the 21% surtax. If the taxable bonds are stopped at par the tax-exempt bonds cannot go down too far without making the present yield spread even more in favor of the 2½s, 1953/49.

It is also argued that banks will have to buy so many Governments that their earnings will be increased to a point where they will have to pay taxes anyway.

For reasons of stabilization it is true the large institutions may somewhat curtail their move from taxable securities to tax-exempts. Therefore, at times, the market supply—those bonds coming from tax-exempt institutions—may more than be sufficient to take care of the demand for tax-free bonds. This is apparently taking place now. However, we feel that if the current yield spread becomes any more favorable to the tax-exempts, the visible supply which is now overhanging the market will quickly vanish.

Furthermore, we believe that as soon as the new tax bill is settled with the resulting higher taxes, there will be a scramble to buy tax-exempt securities.

Capital Ratios

As the banks take on more Governments for war financing, the old capital ratio of 1 to 10 is becoming more and more outmoded. However, it has been pointed out previously in these columns that the ratio might well be 1 to 20 if all the additions to a bank's portfolio over the 1 to 10 ratio were confined to Treasury bills, certificates, and notes maturing within two years.

Preston DeJano, Comptroller of the Currency, will give his point of view on the question in an article appearing in the "United States Investor" of September 5. He points out that the nature and quality of the assets rather than any fixed ratio determines the protection afforded by the capital structure. By that he does not mean that he would be one to cast a benign eye upon undercapitalized institutions. He feels, however, that banks should continue to buy Government obligations to help the war effort even though their capital ratio is greater than 1 to 10. That means the future increases should be in short-term obligations. Here we see the Federal Reserve Board, the A. B. A. and the Comptroller getting together on the future war financing. In brief, under 10-year maturities for banks.

It's Said:

Insurance companies bought six million Governments the week of August 23—That weekly Treasury bills are continuing to attract sizable subscriptions, \$872 million—That the market is doing nothing and will not until the next offering—That a certificate offering would probably be most popular now, but a reduction in the coupon would not help in getting country distribution as the recent ½% did—That New York City has lost about \$97 million notes, mostly 1948 and 1944 maturities, since the week of July 29. But during that same time they have added \$136 million bills and \$276 certificates.

SEP 8 1942

Dear Mr. Purcell:

Thank you for your letter of August 31, 1942, regarding the proposed rule governing certain security transactions.

It was unfortunate that your communication, dated July 29, 1942, addressed to the securities industry, was received by them on or about the date they were notified of an impending Treasury offering. The request for comments from the industry by August 12, 1942, contained in your communication, had the effect of retarding the sales effort of the Victory Fund Committee in connection with the recent offering of registered 2½% bonds.

To avoid an occurrence of similar incidents in the future, I think it advisable that the Commission determine the Treasury financing schedule before sending out any communication which might interfere with the program.

Sincerely yours,

(Signed) H. Morgenthau, Jr.

Mr. Ganson Purcell, Chairman,
Securities and Exchange Commission,
Philadelphia, Pennsylvania.

File returned to Buffington's
office direct
Photostat file in Diary

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9/3/42

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON

OFFICE OF THE CHAIRMAN

August 31, 1942.

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

My dear Mr. Secretary:

Recently officials of the Treasury Department brought to our attention the fact that certain dealers in securities had communicated with the Department relative to a rule recently suggested by the Commission's staff for adoption and circulated for comment, a copy of which is enclosed. We were advised that these dealers stated at the time that their efforts to sell United States Government bonds in conjunction with the "Victory Fund" program were being seriously hampered because of the necessity for considering this proposed rule. I discussed these reports at the time with my colleagues on the Commission when we considered the suggestion that we communicate to certain dealer organizations our desire not to interfere in any way with the current financing program of the Treasury. We, of course, have every desire to avoid interference with any of the Government's financing programs, particularly during time of war, but because of the circumstances, we did not feel that it was necessary to make such an assertion to the groups indicated and so advised your representatives. I stated at the time, however, that I would address a full communication of our views and the background of the proposed rule to you so that you might have it upon your return to Washington. I regret to say that other pressing problems have prevented me from writing this letter sooner.

This suggested rule was originally mailed to members of the securities industry and to other interested persons on July 29, 1942. To date we have received a substantial number of comments, many of which were in opposition to the proposed rule, but in only a very few cases has there been any mention whatsoever of possible interference with the sale of Government bonds.

The Commission's staff proposed this rule as the result of its many years of experience in policing the so-called over-the-counter markets. The Commission itself has taken no position either for or against the rule and will dispose of the proposal solely on its merits. In line with its usual practice it solicited suggestions and comments. When the Securities Exchange Act of 1934 was enacted its principal emphasis was on regulation of national securities exchanges, their members, and their trading practices. Since at that time little was known concerning the over-the-counter market, Congress entrusted to the Commission the task of informing itself concerning the practices of that market and imposed upon it the duty of adopting rules which would give the public similar protection to that surrounding exchange trading.

The Commission, since its formation, has studied the over-the-counter market continuously. From time to time it has proposed amendments to the Securities Exchange Act to facilitate the regulation of that market; those amendments have been adopted by Congress. The Commission has also promulgated certain rules and regulations under its general rule-making powers which were designed to protect investors from loss due to the employment of fraudulent, manipulative or deceptive devices by over-the-counter dealers in the purchase and sale of securities.

The Commission has become increasingly aware of a practice which is growing in the over-the-counter market for dealers to buy from or sell to their customers at prices bearing no reasonable relationship to prevailing market prices. This practice is indulged in by many over-the-counter dealers, not only in connection with the purchase and sale of securities which are traded exclusively in the over-the-counter market, but also in connection with transactions in securities which are listed on national securities exchanges. As a result of the discovery of this practice, the Commission in the past two years has instituted many proceedings against dealers for the purpose of revoking their registrations and thus denying them the right to engage in the securities business by the use of the facilities of interstate commerce and the mails. It is strongly urged on the Commission that adequate protection of the public in matters of this kind requires the adoption of appropriate regulations by this Commission which will make available to customers current information about market prices to enable them to make an informed and intelligent judgment in each transaction of purchase and sale.

- 3 -

The practice of buying and selling at prices bearing no reasonable relationship to the prevailing market, is believed to thrive during periods when persons who are uninformed concerning security markets have in their possession extra sums of cash. Securities frauds flourished in the lush period of the last war. That reason alone, it is argued justifies the Commission in taking some action at this time to eradicate a practice which is growing to alarming proportions. There is substantial basis for the belief that the unscrupulous securities dealers who are able to take advantage of their customers' ignorance of the prevailing market for the security dealt in, threaten the proper fulfillment of the Treasury's program for the sale of Government bonds, including those bonds which are sold in small denominations. Not only do they interfere with the sale of new securities being offered by the Government, but they also switch persons who are already holders of older Government issues out of those issues and into second-grade securities. For example, the Commission has recently instituted a proceeding against a dealer in which the charges are as follows:

Two elderly, uninformed investors were persuaded by a dealer to sell a United States Government bond on the representation that the dealer would invest the proceeds in a security which would provide a better yield and increase more rapidly in value. As a result of the dealer's effort, these two investors sold their bond and immediately purchased from the dealer certain second-grade bonds. Although these bonds were then offered in the market at 17 1/4, the two trusting investors were charged 33 1/4 per bond, or more than 80% above the quoted market price.

In another recent case the Commission has proceeded against a dealer wherein it is charged that he followed the practice of switching his customers from Government bonds to second-grade securities at prices materially higher than the prevailing market. In this latter case some of the Government bonds which customers were persuaded to sell were savings bonds in denominations as small as \$75, while others were regular Government issues.

These cases are by no means unique. As I have stated before, there is increasing evidence that unless the Commission takes some affirmative step to protect uninformed members of the public more and more of the excess cash held by individuals today will be taken from them by unscrupulous security dealers.

In view of the foregoing, which gives but a thumbnail sketch of the situation, I am sure that you will agree that mere assertions that consideration or adoption of the proposed

rule will have an adverse effect upon the sale of Government bonds should not cause us to abandon all efforts to arrive at a solution of the problem which confronts us. Many of the objections being urged against the adoption of this rule are reminiscent of those made at the time of the passage of the Securities Act and the Securities Exchange Act. You will recall that in those days the cry went up that the enactment of these statutes would freeze the capital markets and thus prevent the fulfillment of the President's recovery program. Certainly those who can find time to devote themselves to perpetrating the kinds of practices described above are in no position to complain that a consideration of this proposed rule is an unwarranted intrusion upon their time.

I also wish to point out that the National Association of Securities Dealers, with a membership of over 2000 dealers, has now pending before this Commission a proposed amendment to its by-laws imposing a minimum capital requirement as a qualification for membership. Since the Association urges that the protection of the public and of the industry itself demands the approval of this rule by this Commission, it is obvious that that Association finds nothing in the present scene which prevents taking the necessary time to afford adequate protection for investors.

Moreover, the Commission has not yet adopted this rule; it is merely engaged in soliciting constructive criticism which will facilitate the drafting of a rule designed to eradicate evil practices with the least possible disruption to legitimate over-the-counter transactions. The rule is still in the discussion stage and in an effort to obtain the views of all interested persons, the Commission has extended the time for filing such comments to September 15, 1942. I trust that you will agree that the time expended in such discussions should not interfere in the slightest with the marketing of Government bonds.

Very sincerely yours,
Ganym Purcell
 Ganym Purcell
 Chairman

Enclosure.

July 29, 1942

SECURITIES AND EXCHANGE COMMISSION

Trading and Exchange Division

Proposed RULE X-15C1-10

DISCLOSURE OF MARKET PRICE

(a) *General Provisions.* - The term "manipulative, deceptive, or other fraudulent device or contrivance" and the term "fraudulent, deceptive, or manipulative act or practice" as used in Sections 15 (c) (1) and 15 (c) (2), respectively, of the Act are hereby defined to include any act of a dealer designed to effect a sale to or a purchase from a customer, by such dealer, of any security, unless such dealer, at or before the completion of each such transaction, discloses to such customer in writing -

(1) (A) the best independent bid and asked prices for the security at the time of the sale or purchase which the dealer is able to ascertain upon the exercise of reasonable diligence; or

(B) the best independent bid or asked price at such time, if the dealer, after the exercise of reasonable diligence, is unable to ascertain both a bid and an asked price; or

(C) if neither such a bid nor such an asked price can be obtained after the exercise of reasonable diligence, the price at which the dealer was able to acquire the security in that *bona fide* transaction which is closest in point of time to the proposed sale to or purchase from the customer, but which is not more remote than sixty days prior to such proposed sale or purchase, provided, however, that if the dealer has had no such transaction he shall make the disclosure required by paragraph (2) hereof; and

(2) if the disclosure is made pursuant to (B) or (C) of paragraph (1) hereof, the fact that after the exercise of reasonable diligence he was unable to ascertain a current independent bid or asked price, or both, as the case may be.

(b) Nothing in this rule shall be understood as preventing any dealer from stating in the written notice required by paragraph (a) hereof (1) that the bid and asked prices so disclosed apply to an amount of the security less than that sold to or purchased from the customer, if such be the fact; (2) that the information pertaining to the bid and asked prices disclosed to the customer has been obtained from sources believed to be reliable, if such be the fact, but that he is not able to state that a transaction could be effected at the disclosed price or could not be effected at a better price; and (3) any other fact, not inconsistent with the purposes of this rule, which the dealer may wish to disclose.

(c) *Records To Be Kept.* - Every dealer who makes a disclosure pursuant to paragraph (a) (1) of this rule shall make and preserve a record of (1) the

information so disclosed; (2) the date and time as of which such bid and asked prices were current; (3) the sources of the information disclosed; and (4) the date and time such information was obtained.

(d) *Exemptions.* - This rule shall not apply to the following:

(1) any transaction in a security during the thirty-day period following the date on which the security is first publicly offered, provided that a registration statement is in effect as to such security under the Securities Act of 1933, as amended, and provided further that the dealer, in connection with such transaction, gives to the customer the prospectus required by that Act;

(2) any transaction effected on a national securities exchange;

(3) any transaction which is a part of a secondary distribution approved by a national securities exchange and which is effected during the course of such distribution; and

(4) any transaction in an exempted security, provided, however, that no transaction in an exempted security which is a direct obligation of or an obligation guaranteed as to principal or interest by a State or any political subdivision thereof or any agency or instrumentality of a State or any political subdivision thereof or any municipal corporate instrumentality of one or more States shall be exempt from the provisions of this rule unless such transaction occurs in the course of a public offering of such security by the issuer thereof.

QUESTION

How do you propose to finance the deficit without inflation?

ANSWER

1. If we are to avoid inflation, the deficit must be financed out of savings.

2. Savings of individuals during the second quarter of 1942 were at the annual rate of over \$24 billions, according to the Department of Commerce. This is the largest in the history of the country by a wide margin, more than twice what they were a year ago. Savings of corporations, plus the amount of their depreciation and depletion reserves, will add substantially to this figure.

3. The increase in savings has been created largely by the restrictions required by the war effort. As our war effort increases, savings and taxes, or both, must continue to rise in order to permit the deficit to be financed in a noninflationary way. This requires new restrictions on consumer spending. It is precisely the necessity for such additional restrictions which brings me here today.

4. It is impossible to say in advance what will be the exact securities by which these funds will be channeled into the Treasury and who will be the immediate purchasers of the securities. To the extent that individuals choose to save by buying War bonds, War bond sales will be increased. To the extent that they choose to repay debts held by banks, or to accumulate savings in the form of bank accounts, insurance, etc., Government securities will be sold to banks, insurance companies, and other institutions. In any case, however, the sales will be noninflationary as long as they are backed by an equivalent amount of bona fide savings.

UNITED STATES SAVINGS BONDS - TOTAL

Comparison of September sales to date with sales during the
same number of business days in August and July 1942

(At issue price in thousands of dollars)

Date	: September : daily : sales	Cumulative sales by business days				: September as : percent of August
		: September	: August	: July		
September 1942						
1	\$ 19,162	\$ 19,162	\$ 26,267	\$ 28,418		73.0%
2	24,558	43,720	65,032	52,687		67.2

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

September 3, 1942.

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

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

UNITED STATES SAVINGS BONDS - SERIES E

Comparison of September sales to date with sales during the same number of business days in August and July 1942

(At issue price in thousands of dollars)

Date	September daily sales	Cumulative sales by business days				September as percent of August
		September	August	July	September as percent of August	
September 1942						
1	\$ 11,634	\$ 11,634	\$ 14,044	\$ 15,821		82.8%
2	14,748	26,381	36,222	30,701		72.8

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

September 3, 1942.

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

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

UNITED STATES SAVINGS BONDS - SERIES F AND G COMBINED

Comparison of September sales to date with sales during the same number of business days in August and July 1942

(At issue price in thousands of dollars)

Date	September daily sales	Cumulative sales by business days				September as percent of August
		September	August	July	September as percent of August	
September 1942						
1	\$ 7,528	\$ 7,528	\$ 12,222	\$ 12,597	61.6%	
2	9,811	17,339	28,810	21,986	60.2	

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

September 3, 1942.

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

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

Sales of United States savings bonds
September 1-2, 1942
Compared with sales quota for same period
(At issue price in millions of dollars)

Date	Series E				Series F and G				Total			
	Actual sales		Quota	Sales	Actual sales		Quota	Sales	Actual sales		Quota	Sales
	Daily	Sept. 1 to date	Sept. 1 to date	to date as % of quota	Daily	Sept. 1 to date	Sept. 1 to date	to date as % of quota	Daily	Sept. 1 to date	Sept. 1 to date	to date as % of quota
1	\$ 11.6	\$ 11.6	\$ 14.9	77.9%	\$ 7.5	\$ 7.5	\$ 6.9	108.7%	\$ 19.2	\$ 19.2	\$ 21.8	88.1%
2	14.7	26.4	34.5	76.5	9.8	17.3	16.6	104.2	24.6	43.7	51.1	85.5
3			55.5				26.4				81.9	
4			81.0				35.6				116.6	
5			98.3				42.2				140.5	
8			143.3				58.1				201.4	
9			168.8				67.8				236.6	
10			193.4				76.7				270.1	
11			220.6				84.4				305.0	
12			239.2				90.1				329.3	
14			272.7				99.7				372.4	
15			288.2				105.0				393.2	
16			307.6				112.1				419.7	
17			327.2				119.2				446.4	
18			350.1				125.7				475.8	
19			365.4				130.5				495.9	
21			399.6				141.0				540.6	
22			415.7				147.0				562.7	
23			436.2				155.2				591.4	
24			457.1				163.4				620.5	
25			481.4				171.0				652.4	
26			497.4				176.6				674.0	
28			532.7				188.7				721.4	
29			549.2				195.5				744.7	
30			570.0				205.0				775.0	

September 3, 1942.

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

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.

Note: Quota takes into account both the daily trend during the week and the monthly trend during the month.

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Secretary Mergenthan.

My dear Mr. Mergenthan:

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I must thank you for the understanding you include you agreed to Mr. Jackson's request. This makes it possible for him to explain my situation to the Board of Trustees of the University.

It has been a rare experience to work with Mrs. Mergenthan and also to have an opportunity to know you. I assure you that I will do my best to make a success of responsibilities which you have given to me.

Most cordially
September 3 '42. David White



TREASURY DEPARTMENT
PROCUREMENT DIVISION
WASHINGTON

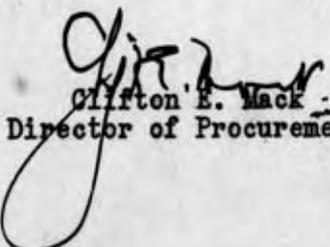
OFFICE OF THE DIRECTOR

September 3, 1942

MEMORANDUM TO THE SECRETARY:

There is attached Treasury Department Requisition No. 11, for your signature. The requisition will be used to seize 100 Ford Truck Chassis to be utilized in filling Lend Lease requirements.

The Chairman of the War Production Board approved the allocation of these truck chassis August 29, 1942.


Clifton E. Mack
Director of Procurement

Enclosure



REQUISITION
BY
THE UNITED STATES OF AMERICA
UNDER ACT OF OCTOBER 10, 1940, AS AMENDED

DA-TFS-No. _____

Treasury Department Req. No. 11

TO: Mr. John W. Knox, Procurement Officer,
San Francisco, California

In the interest of National Defense it has been determined necessary that the articles or materials listed below be requisitioned and taken over for the use or operation by the United States or in its interest:

100 Ford Truck Chassis, described as follows:

Cases -	Total
Nos. 7077/7103	27 cases
Nos. 1/8 - 26/31 - 34/57 - 76/99 - 100/124 - 151/169 - 175/176 - 226/232	115 cases
Nos. 201/225	25 crates
Nos. 251/254 Oil	4 drums
Nos. 255/256 Enamel	2 pails
Nos. 170/174 Closed cabs on skids	5 unboxed
Nos. 1117 - 1121 - 21769/21773 - 1139 - 1140	9 cases
Nos. 14851/14920 - 21751/ 21768 Wheels & Auto Parts	88 bundles
No. 1126	1 crate
No. 1138	1 carton
No. 177	1 case
Nos. 276 - 277	2 bundles
Nos. 278 - 279	2 cases
No. 7161	1 case

All the above are marked
Ford Manila or M.T.S. Manila.

284 Total

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You are authorized and directed to take possession of above described articles or materials and to furnish receipt for the same in the name of the United States, and to inform the Director of Procurement, Procurement Division, Treasury Department, 7th and D Streets, S. W., Washington, D. C. of your action in execution of this requisition.

All persons having any claim to or interest in any of the above-described articles or materials are directed to give notice of their claims at once to THE SECRETARY OF THE TREASURY, Washington, D. C. who will prescribe the form and manner of filing such claims.

Washington, D. C. Sept 10, 1942.

(sgd) H. Morganthau Jr.

Secretary of the Treasury.

September 3, 1942.

MEMORANDUM

TO: Secretary Morgenthau
FROM: Mr. Gaston

With reference to the attached letter from General Strong:

(1) We are ordering an immediate investigation of the incident at Tampa on August 15.

(2) We have no power under the law to grant complete freedom from Customs examination to anyone except those persons for whom a request for free entry is made by the State Department and their designation as diplomats or distinguished visitors. We can, however, instruct Collectors of Customs to treat members of the British armed forces with all possible courtesy and to facilitate and expedite their examination, reducing it as closely as possible to a formality. This is, I believe, the general practice at all our ports, but we will renew and emphasize these instructions.

(3) We cannot speak positively about the Tampa incident until we get a report, but I cannot conceive that Customs officers there would carry on so rigorous an examination as is indicated except upon some request or indication from the other investigative services that a rigorous examination for their purposes was desired. This sometimes happens, but I don't know of any instance in which it has happened in the case of soldiers of a friendly country in uniform.

(4) We will get out special instructions for the most considerate treatment possible of rescued seamen and others in distress, but we have not heretofore received any reports indicating any lack of consideration for persons in this category.

CONFIDENTIAL

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WAR DEPARTMENT
WAR DEPARTMENT GENERAL STAFF
MILITARY INTELLIGENCE DIVISION G-2
WASHINGTON

September 3, 1942.

The Honorable,

The Secretary of the Treasury.

My dear Mr. Secretary:

Reference our telephone conversation of yesterday, I am in receipt of a report which indicates a most regrettable procedure in handling a British ship which docked at Tampa, Florida, on August 15. On board was personnel of the British Navy, Army, Air Force, and some 40 odd recruits for the Canadian Army, which personnel arrived for transshipment or transiting the United States for destinations in the British Empire. In addition there were approximately 60 survivors of the British Mercantile Marine whose ships had been torpedoed in the Caribbean. An R.F.A. Corporal, Patrick Kane, No. 536744, Fleet Air Arm from Trinidad, was promptly transferred to a Tampa hospital.

The remaining military personnel was individually subjected to a thorough investigation lasting from half an hour to an hour by the Immigration Service, by the F.B.I. and, I am ashamed to say, by one or more members of the M.I.S., and largely on matters which, in my opinion, were immaterial if not stupid. Thereafter they were taken in hand by the Customs and, in some cases, completely stripped and searched in a most humiliating manner. The British Staff Captain, B.D.O. Jones, pointed out to the Customs officers concerned that he would accept responsibility for them as they were part of a draft officially advised from Washington and whose names he had on a list compiled by the D.E.M.S. Staff Officer in Trinidad. Captain Jones' appeals appeared to be of no avail, and unfortunately he did not have the background or the force on which to register an official protest.

The Merchant Seamen, both officers and men, were subjected to the same examination and many were kept standing as much as 18 hours in the ship's alleyways, although many were still suffering from the effects of the torpedoing of their ships. One of these officers, the Captain of the S. S. WEIRBANK, was in a particularly nervous condition but he was treated in exactly the same way as the Seamen.

I am informed that the British Vice Consul is sending in an official report on the matter to the British Embassy here.

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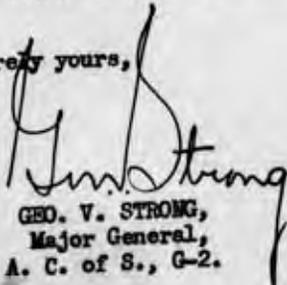
CONFIDENTIAL

In my opinion, the procedure followed at Tampa is not only a scandal and a disgrace but which, if repeated, is apt to cause resentment and ill feeling not only to the prejudice of our good relations with Great Britain, but also may seriously jeopardize our war effort. It certainly does not take a great effort of imagination to realize the howl that would go up in our press were American troops landing in England, or in Egypt, subjected to the same treatment on the part of the British authorities.

I am very strongly of the opinion that any inspection or examination by Immigration, Customs, F.B.I., Military or Naval Authorities of members of the British Armed Services arriving at ports in the United States, either for transshipment or transiting the United States for destinations in the British Empire, is not only unnecessary but, under the circumstances, is highly undesirable. It does appear necessary, however, that such personnel be properly identified and vouched for by the British authorities. In consequence, I have arranged with the British Military Attache that, in the future, this office be notified of the prospective arrival of members of the British Armed Services in this country, and that the British authorities have a staff officer present at the Port of Debarkation to identify such personnel and to furnish such certificates covering their status as may be required by the departments of this Government concerned. Upon the receipt of such information in this office I shall be very glad to notify such officer in your department, as you may see fit to designate, in order that such personnel may be exempted from Customs examination. May I express the hope that you can find a way to issue such instructions to the personnel of your department that will accomplish the end desired.

In regard to British Merchant Seamen who are survivors from torpedoings at sea and who arrive at a port in this country for transshipment to destinations in the British Empire, I hope that similar arrangements can be made as result of identification and certification by a British Consul Officer.

Very sincerely yours,



GEO. V. STRONG,
Major General,
A. C. of S., G-2.

CONFIDENTIAL

STRICTLY CONFIDENTIAL

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MEMORANDUM FOR THE FILE

September 3, 1942

Mrs. Klots called me today and asked me to advise the State Department and the JDC of the decision of Mr. Paul relative to the request by the JDC for permission to authorize its Shanghai representative to borrow funds locally for relief purposes in Shanghai.

I telephoned the JDC offices in New York. Mr. Hyman and Mr. Levitt were both out of the city on vacation and I spoke to Miss Morrissey, Assistant Treasurer, the only officer of the organization available. I advised her of the decision not to authorize the transaction and told her that I would be glad to confirm the decision to Mr. Hyman or Mr. Levitt when they returned.

I also telephoned Mr. James E. Henderson of Mr. Green's office in the State Department and advised him of the decision not to authorize this transaction. I asked him to notify Mr. Welles and Mr. Joseph Green accordingly, which he said he would do.

(Signed) J.W. Pehle

JWPehle:mgt 9/3/42

SEP 8 1942

My dear Mr. Ambassador:

I wish to refer to the agreement dated January 3, 1942, relative to the purchase of 602,000 fine troy ounces of gold by the Secretary of the Treasury from the Government of the Union of Soviet Socialist Republics, against which an advance of \$80,000,000 was made on January 3, 1942.

I take pleasure in enclosing for your information two copies of the assay report of the United States Mint at Denver, Colorado, giving an analysis of the gold which was deposited at Denver on August 18, 1942 for the account of the Secretary of the Treasury.

You will observe from the enclosed report that the shipment, after melting and upon assay, was determined to contain 160,691.179 fine troy ounces of gold and to have a value of \$5,684,189.87. After the deduction of the amount of \$14,221.87, representing the melting charge of \$160.00 plus the 1/4% handling charge of \$14,060.47, the net value of the gold was \$5,609,968.60. This amount of gold has been applied by the Treasury against the amount of gold agreed to be purchased by the Secretary of the Treasury under the agreement of January 3, 1942.

Sincerely yours,

(Signed) H. Morgenthau, Jr.

Secretary of the Treasury.

His Excellency
Maxim Litvinoff,
Ambassador of the Union of Soviet
Socialist Republics.

Enclosures.

Initialed: RH FD RMB EDW
AFL

RH:lc:8/29/42

NOT TO BE RE-TRANSMITTEDCOPY NO. 13BRITISH MOST SECRET
U.S. SECRETOPTEL No. 303

EGYPT. 2nd. There was no material change in the general situation but the main enemy columns are reported to have withdrawn slightly to the South. In this area a large concentration of enemy M.T. was seen and harassed all day from the air and by our troops from the South.

OPTEL No. 304

Information received up to 7 A.M., 3rd September, 1942.

1. NAVAL

Last night one of our motor torpedo boats raided a light house in the CHANNEL ISLANDS and took 7 prisoners.

ATTACKS ON SHIPPING. From 29th August to 1st September inclusive 19 ships were reported torpedoed between 24th and 31st August. A Norwegian and Panamanian ship in homebound convoy in North Western approaches. 3 U.S. ships in convoy off the Canadian coast. One British, 1 Norwegian and 2 Dutch ships in the WEST INDIES. A British and a Dutch tanker in convoy in the CARIBBEAN. A large U.S. tanker north of the AZORES. A British and a Dutch ship in homebound convoy south-west of CAPE FINISTERRE. 2 British ships in FREESTOWN area. A British ship in the INDIAN OCEAN and another off coast of NEW GUINEA. A British ship was also torpedoed in the MEDITERRANEAN but reached port in tow. A British ship was mined off LOWESTOFT and a Norwegian bombed off PALMOUTH, but both were beached.

2. MILITARY

RUSSIA. The Germans continue to make slow progress in their advance on STALINGRAD from the South West. In the CAUCASUS fierce fighting is in progress in the region of the KLUKHOR PASS in which considering the difficult terrain fairly large enemy forces are engaged. The German forces advancing through the other passes consist of small groups. The approaches to TUAPSE and NOVOROSSISK are being firmly held.

3. AIR OPERATIONS

WESTERN FRONT. 1st/2nd. SAARBRUCKEN. Nearly 90% of the bombers sent out attacked the objective. About 430 tons of H.E. and incendiaries were dropped in about equal proportion. H.E. included 54 bombs of 4,000 lbs. and 80 of 2,000 lbs. There was no haze. Flare dropping was accurate and helpful. Little opposition from enemy fighters, A.A. or searchlights. Evidently a most successful attack. A Whitley obtained a direct hit on tanker at ST. NAZAIRE.

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2nd. Single Mosquito bombed COLOGNE, ESSEN and OSNABRUCK and oil installations near GHENT. Two F.W. 190's were shot down into the channel by 2 Spitfires.

2nd/3rd. 202 aircraft were sent out - KARLSRUHE 199, seaming 3. 8 aircraft are missing. Visibility over KARLSRUHE was good. 4 enemy aircraft flew over YORKSHIRE, one of them was destroyed by fighters off SCARBOROUGH and another crashed in ESSEX.

EGYPT. 31st/1st. Our bombers attacked TOBRUK Harbour, landing ground near EL DABA and enemy M.T. in the Southern sector.

1st. Although dust storms hampered operations our escorted light bombers flew a number of sorties against tanks and M.T. in the Southern sector. Beaufighters attacked eastbound M.T. between GAMBUT and SIDI BARRANI, many vehicles were destroyed or damaged. 10 enemy aircraft were destroyed by fighters and A.A. 5 were probably destroyed and 16 damaged. We lost 16 aircraft.

BURMA. 29th. Allied bombers attacked LASHIO Town and aerodrome.

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U.S. SECRETOPTEL NO. 311

Following is supplementary resume of operational events covering period 27th August to 3rd September, 1942.

1. NAVAL

NORTHERN WATERS. The Pocket Battleship ADMIRAL SCHEER is reported again in Northern Norwegian waters. It is possible that this ship has returned from a cruise in Arctic and North Russian waters and that it was this ship which carried out the bombardment on DICKSON ISLAND, KARA SEA on the 25th. The Battle Cruiser SCHARNHORST still in Baltic is considered now ready again for service. There was a heavy raid on ARCHANGEL on 31st.

MEDITERRANEAN. There was considerable activity by both submarine and aircraft against enemy shipping during period 28th August to 3rd September inclusive. 10 ships are claimed sunk or seriously hit and 4 others also damaged. An enemy destroyer is also claimed hit. A recent air reconnaissance showed the third LITTORIO Class Battleship at TARANTO.

SUBMARINE WARFARE. U-boat attack was still directed against Atlantic convoys and shipping in the West Indies area. Two Atlantic convoys were attacked during week and 5 ships sunk. Provisional figures for the week ending 30th August - 20 ships sunk by submarine. Aircraft assistance despatched to two convoys attacked in the Atlantic proved notably effective. During the week ending 2nd September, there were 23 attacks on U-boats by aircraft and 19 by surface craft of which 3 by aircraft and 5 by surface craft are considered promising.

FRANCE. 2 French merchant ships totalling about 12,000 tons reached CASABLANCA from NEW YORK on 27th.

RUSSIA. In the Black Sea Russian Naval Aircraft have carried out a series of attacks on landing craft in enemy occupied ports and a force of Russian Cruisers is reported to have bombarded THEODOSIA on 27th.

TRADE. Imports in convoy into the United Kingdom for the week ending 30th August were 670,000 tons including 166,000 tons of oil.

2. MILITARY

EGYPT. After a period of comparative quiet fighting broke out on the morning of 31st August when German forces including Armoured Formations pushed forward against the Southern flank of the Eighth Army. On the following day the enemy columns swung Northwards towards the central sector. The object of this attack appeared to be the capture of the high ground running Northeast from ALAM EL BUEIB. This attack was not pushed home and on the next day the enemy remained concentrated Southwest of ALAM EL BUEIB and since then has withdrawn. The enemy was continually harassed during his withdrawal by our light mobile forces. Our Artillery and Air Force pounded enemy M.T. with good results.

FAR EAST.

CHINA. The Japanese have withdrawn along the CHEKIANG-KIANGSI Railway and the Chinese have reoccupied a distance of some 200 miles between NANCHANG in the West and KINWHA in the East, both of which places remain in Japanese hands. The Chinese reoccupation of this stretch of line was occasioned by the Japanese withdrawal and not by any Chinese major offensive.

BURMA. Some re-grouping of Japanese forces is taking place at AKYAB and on the ASSAM-BURMA Frontier. Reliefs have been brought from RANGOON since according to reports the discipline and morale of the Japanese Garrison at AKYAB was low. There are no indications of troop movement in the FORT HERTZ area in UPPER BURMA. The principal Japanese Garrisons are in the MANDALAY Area to which they withdrew during the Monsoon.

JAPAN. 10 Divisions are believed to have been formed in JAPAN in December, 1941, and to be now ready for service overseas. Forces in JAPAN are therefore estimated at 16 Field Divisions, and the Japanese Army at 85 Divisions.

3. AIR OPERATIONS

WESTERN FRONT. Bomber Command kept up our night offensive against German industry by flying 1,028 sorties during which more than 1900 tons of bombs were released, including 4 bombs of 8,000 pounds, and 198 of 4,000 pounds. The main objectives were KASSEL, NUREMBERG, KARLSRUHE and the SAAR. Attacks were favoured with good weather and fires started by "Pathfinders" sent on ahead and the flares dropped by them added greatly to the success of the operations. KARLSRUHE had not previously experienced a heavy attack. Coastal Command sent out 228 sorties on anti-submarine operations in addition to some Biscay patrols by Bomber Command. Our Air/Sea Rescue Service during August carried out 35 rescues and saved 114 Allied personnel. Every aircraft sighted by the Rescue Service was saved, in some cases at a considerable distance from our coasts.

MEDITERRANEAN. Our activity over the battle area compared in intensity with the peak effort of last May and June. Our light bombers met heavy opposition from anti-aircraft fire and enemy fighters but were well protected by our fighter escorts. The enemy also displayed considerable activity over the battle area and many heavily escorted Stuka formations were intercepted by our fighter patrols and often forced to jettison their bombs. 13 JU 87's and 15 fighters were shot down by our aircraft as well as 15 more enemy aircraft by our A.A. fire. Axis bombers from CRETE made 2 night attacks with 80 and 50 aircraft respectively on our aerodromes south of ALEXANDRIA. 4 aircraft on the ground were destroyed and 10 damaged. 3 enemy bombers were shot down. It is estimated that Allied aircraft sank 2 and damaged 11 ships on the ITALY-AFRICA supply route or in Axis occupied harbours. These figures include a Destroyer damaged and 2 large tankers and one smaller one set on fire. Fighters carried out offensive operations over SICILY.

4. EXTRACTS FROM PHOTOGRAPHIC AND INTELLIGENCE REPORTS ON RESULTS OF AIR ATTACKS ON ENEMY TERRITORY IN EUROPE.

SAARBRUCKEN. A newspaper report on 19th August states that in order to repair the worst of the damage workers from many other districts have had to be brought into the town.

DIEPPE. A reliable source reports that German Staff Officers have stated that the R.A.F. plan was bold and well executed and that R.A.F. aggressiveness gave them the most difficult defence problem in this type of raid. They fear that in the future heavier bombs may be used on a larger scale. They admit about 170 aircraft lost during the attack.

MAINZ. It is reported that 400 people were killed and many more injured. 40,000 have been evacuated, 30,000 of whom, nearly one third of the population, were homeless.

GENERAL: In DUISBURG, the July raids are said to have dislocated the GERMANY-ITALY coal traffic for a week. The effect of the attacks on BREMEN has created a problem for the housing authorities, especially in the case of Focke Wulf workers since, owing to the extent of destruction to the workers' dwellings, a large proportion have had to be housed in emergency hutments totally unsuitable for winter conditions.

5. OPERATIONAL AIRCRAFT BATTLE CASUALTIESMETROPOLITAN AREA

<u>BRITISH</u>		<u>ENEMY</u>			
<u>In the Air</u>		<u>Dest.</u>	<u>Prob. Dest.</u>	<u>Damaged</u>	
Bombers	82	Bombers	8	2	10
Fighters	17	Fighters	10	9	16
Coastal	10	Miscellaneous	2	11	1
Total	109		20	11	27

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MIDDLE EASTIncluding MALTA

	<u>BRITISH</u>			<u>ENEMY</u>		
	<u>In the Air</u>	<u>On the Ground</u>		<u>Dest.</u>	<u>Prob. Dest.</u>	<u>Damaged</u>
Bombers (incl. 1 U.S.)	12	3	Bombers	20	7	12
Fighters	38	1	Fighters	23	11	29
Others	<u>1</u>	<u>Nil</u>	Miscellaneous	5	1	3
Total	51	4	Total	<u>48</u>	<u>19</u>	<u>44</u>

1 crew and 9 pilots are safe.

Of the above totals, 10 were destroyed, 2 probably destroyed and 1 damaged by A.A.

NOTE: No account is taken of enemy aircraft destroyed on the ground in any theatre, or of British naval aircraft casualties.

6. HOME SECURITY

Estimated casualties for week ending 6 A.M. 2nd - Killed 92, seriously wounded 91.

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NUMBER 47

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OFFICE OF STRATEGIC SERVICES

THE WAR THIS WEEK

August 27-September 3, 1942

Printed for the Board of Analysts

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The Secretary of the Treasury

Office of Strategic Services

THE WAR THIS WEEK

Although the Nazis are closing their pincers about the inner defenses of Stalingrad, the reduction of that city may still involve a costly siege. In both the Groznyi and Black Sea sectors the German drives have slowed, and a final decision in the Caucasus (if that is the Nazis' intent) still lies some weeks in the future.

Rommel's long awaited blow has fallen in the southern sector of the Egyptian front, but it is not yet clear whether this is a serious thrust for the Delta or a drive for limited objectives.

The Germans continue to press Laval for concessions in Africa and Metropolitan France. Laval is pliant, but the Minister of Marine, Admiral Auphan, is reported to have resisted Nazi demands both for a Franco-German defense agreement on Africa and for the surrender of French merchant tonnage. Internal tensions in Spain appear to be mounting.

In the Far East the Japanese are executing extensive withdrawals in China and have suffered further reverses in the Solomons and at Milne Bay in New Guinea. Indeed recent Allied successes in the southwest Pacific have notably strengthened our position there. Some observers meanwhile interpret these Japanese withdrawals and the sudden resignation of Foreign Minister Togo as pointing to an early attack on Siberia, but these forecasts are still definitely in the realm of speculation.

The important urban centers in India are beginning to return to a more normal life, but a settlement is not yet in

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sight and a general civil disobedience campaign remains a distinct probability.

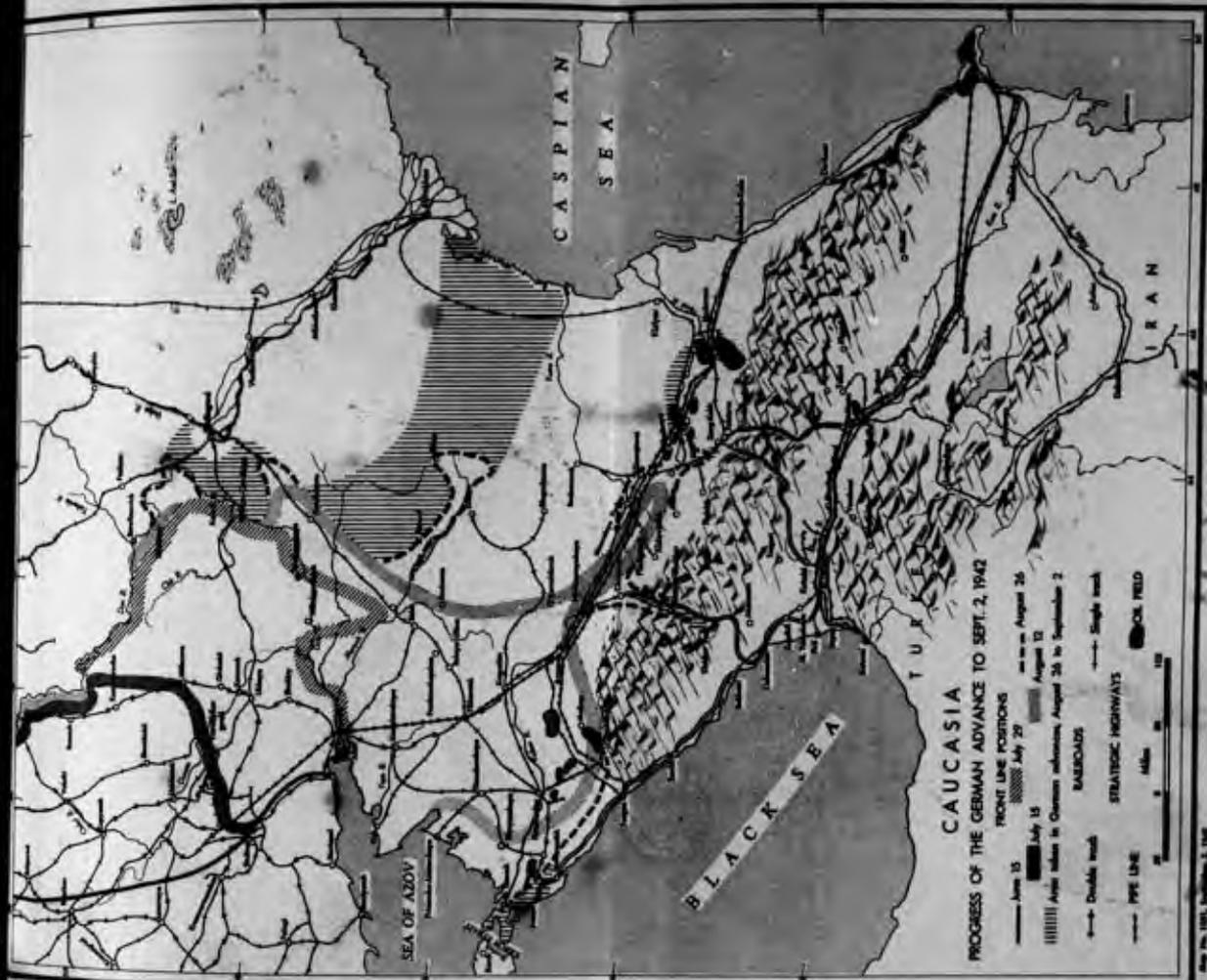
The Siege of Stalingrad

The Germans have now reached the inner defenses of Stalingrad. On the north, south, and west they are approximately 15 miles distant from the city. Except for the river to the east, the defenders are in a state of siege, harassed by continual day and night air attacks. North of Kletskaya, however, they have succeeded in recrossing the Don behind the German lines.

As yet there is no sign that Stalingrad is about to fall. The accompanying map indicates that in the past three weeks the Germans' progress has been notably slower than in the earlier phases of their offensive. Five weeks ago the invaders had already occupied most of the Don bend. Three weeks ago their mechanized columns had come up against stubborn Soviet resistance in the Kletskaya area and had penetrated south of the river beyond Kotelnikovo. A week ago they had reached the Don along its whole course and had established a new bridgehead north of Stalingrad. Now, with their pincers closed on the city, the Nazis may be facing a costly siege.

Anapa and Novorossiisk; the Trans-Caucasus

With the fall of the small port of Anapa, the slow German advance on the Black Sea littoral may be within three miles of Novorossiisk. The siege of this latter city has probably already begun. A greater menace to the Soviet position on the Black Sea coast, however, appears in the report that crack German mountain units have taken the Klukhor pass on the Sukhumi military highway. Such a move might represent an effort to outflank the Soviet defenders of the Black Sea ports by striking at Sukhumi south of the moun-



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tains. On the other hand, the seizure of the pass might be a purely defensive effort to protect the southern flank of the German divisions driving east toward Groznyi from a possible Russian surprise incursion.

Around Groznyi the Soviet defenses have again slowed the German advance, which is apparently nearing Gudermes. And even beyond Groznyi the Russians will be favored by the low foothills between Gudermes and the Caspian. The fall of Gudermes, however, would cut off the rail and pipe line connections of the Groznyi area.

Despite the threat to the passes over the western Caucasus mountains, it is still likely that the main battle for the Trans-Caucasus will occur in the east around Makhach-Kala or Derbent, perhaps not until several weeks from now. And by that time the passes of the Caucasus will be filling with snow. According to a source ostensibly with German staff connections, the Nazis are already dissatisfied with their progress in Russia, and feel that the Trans-Caucasus cannot be taken this year. Their goal is now to capture Stalingrad and to reach the Caspian, and thereafter to cut off so far as possible the resources of the Trans-Caucasus from the rest of Russia. Already German columns from Elista have probably reached the Caspian from the Kuma River to the mouth of the Volga. This advance across lightly defended territory may represent simply an effort to protect the north flank of the Nazi drive in the Groznyi area.

The Black Sea Fleet

With the present menace to the whole west Caucasus shore, attention has once again centered on the Russian Black Sea Fleet. If the Caucasus is entirely lost, this fleet would face two alternatives: internment in a Turkish port or scuttling. In 1918 the Russian sailors of the Black Sea Fleet preferred to

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blow up their ships rather than to hand them over to the Germans. In the opinion of a Soviet observer, the Fleet's tradition is now so strongly rooted that it would never surrender, even in the most hopeless situation, but would again act exactly as it did in 1918.

According to the same observer, the fleet includes the old battleship *Parizhskaia Kommuna* (launched, 1911), the cruisers *Krasnyi Kavkaz* (1916), *Krasnyi Krym* (1915), and *Chervonaia Ukraina* (1915), the aircraft carrier *Stalin* (1937-22 planes), and numerous destroyers, submarines, torpedo boats, and smaller craft, most of them built in the last five years. Its Commander-in-chief is Admiral Philip S. Oktiabrski, who rose from a stoker through the ranks to the command of the Black Sea Fleet in 1938. Well known as one of the builders of the Soviet Pacific Fleet, he supervised personally the defense of Sevastopol (according to the Russian press) and was the last commanding officer to leave the fortress. An active member of the Communist Party, he is in high official favor, and is considered one of the "strong men" of the regime.

The Russian Center and the North

In the Rzhev sector, General Zhukov's month-old counter-offensive, while forced back around Medyn, has taken Zubtsov and reached the defenses of Rzhev. But it has failed to crack the main German defensive system and may already have spent its force. In the opinion of some American military observers, Zhukov's losses in men and matériel have been out of all proportion to the ground he has gained. American journalists—permitted for the first time this year to visit the fighting lines on the central front—have, however, seen little evidence of these heavy casualties.

Last week-end's air attack on Helsinki, which scored direct hits on a branch telegraph office, a large military warehouse,

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and a locomotive repair shop, was, in the opinion of a well-placed American observer in Finland, the most successful bombing in this war or in the Winter War which preceded it. Other reports from Helsinki suggest that the Germans have sent several of their mountain divisions from North Finland to the Caucasus, and have replaced them with three newly-formed mountain divisions of older men. A possible further sign of a manpower shortage on the Eastern Front is the report that the Nazis are now training Finnish volunteers for service with the *Wehrmacht*—or perhaps as replacements for the *Jaeger* battalions of Finns now apparently fighting with the Germans on the southern Russian front.

In the much-bombed seaport of Murmansk, Soviet morale is evidently still comparatively high. According to a Russian sailor just arrived in this country, the people of Murmansk have become so used to air raids that the work in the port does not stop during bombardments. All young men being in the army, it is the old men and women who unload the ships. Special brigades remove ruins and clean up the streets after air raids. With meat and fish practically nonexistent, the average meal consists of a plate of soup and a piece of bread. Although greatly depressed by the Russian reverses in the Caucasus, the people of Murmansk hail every Allied convoy with joy and still feel that they may eventually win the war, our observer concludes.

Rommel's Offensive in Egypt

On the night of August 30 Marshal Rommel attacked on the southern sector of the Egyptian front. While British press releases suggest that his immediate objective may be certain strategic desert ridges, military observers here do not exclude the possibility that this may be a major offensive.

In this attack, which is led by his two German armored divisions, Rommel is using the bulk of his veteran German

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desert fighters, and has in immediate reserve an Italian corps. Supporting motor transport is concentrated in the southern sector. The German armored columns apparently advanced through the British minefields, but there is as yet no indication that they have penetrated main British positions or overcome any major British forces.

It is as yet too early to judge the character of the action. If Rommel were to break through, he might either strike directly at Alexandria and establish there a new base for supplies; or he might swing south of the rocky trough that runs eastward from the Qattara depression and strike directly at Cairo across smooth and open desert.

Decline in Enemy Air Activity

In the air the enemy has been relatively inactive prior to this attack, apparently reflecting a desire to conserve either planes or gasoline or both. Meanwhile Allied air forces have continued their heavy attacks on enemy ports, shipping, and supply lines. These raids, together with submarine action, have taken an increasing toll of enemy shipping and may have been the cause of Rommel's twice delaying his offensive. It is assumed that despite certain shortages, Rommel must have sufficient supplies to sustain active operations; and there are indications that a strategic reserve is being built up in the Mediterranean area for possible use in either Egypt or Northwest Africa.

Bombing attacks on Malta and air activity in the whole Mediterranean theater have lately been sharply reduced. The ships of the convoy that arrived at Malta in mid-August were unloaded without interference from Axis planes. The failure of the enemy to attack suggests that Axis strategists may have felt that the expenditure of planes was not justified even for so important a target. Meanwhile Malta's reinforced fighters took the offensive and raided the airdromes of

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Sicily, destroying at least 10 aircraft, in addition to those damaged.

Near Eastern Quiet

Egypt proper remains quiet. Prime Minister Nahas, on the sixth anniversary of Egyptian Independence Day, made an outspoken address in which he professed Egypt's loyalty to the British and looked forward to the triumph of the democracies. Serious differences are reported, however, between the Egyptian Chief of Staff, who is supported by King Farouk, and the Minister of War, who has the backing of the Prime Minister. The Chief of Staff's loyalty to the Government is questioned by the War Minister, and one observer believes that the situation might reach a point where the British would be forced to intervene with the King in support of the Government.

Little new information is available concerning the Anglo-French dispute in the Levant. De Gaulle and Casey have failed to arrange a meeting, and De Gaulle has declined Churchill's request that he hurry back to London to discuss the situation, stating that conditions did not yet allow him to depart from Syria. Rommel's attack in Egypt puts De Gaulle in an unfortunate position: to precipitate a conflict in the Levant now would undoubtedly provoke a serious reaction in the Anglo-American attitude toward the De Gaullist cause.

In Turkey an improvement in relations with Russia has been reported. The new Turkish Ambassador was apparently most cordially received in the Soviet. On the other hand at least one Turkish paper has treated with concern an article by Professor Renner of Columbia stating that the Allies must not again repeat the error of denying Russia an outlet through the Dardanelles. Repercussions of this entirely unofficial article even appeared in Turkish Government circles, one observer believes.

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The Germans and Dakar

The defenses of French West Africa and the transfer to the Nazis of merchant tonnage controlled by Vichy were discussed by Laval and high German representatives at Nevers on August 27, according to a well-placed informant. Admiral Auphan, Minister of Marine, and other officials accompanied Laval.

The Germans sought Vichy's agreement to a military observer or control commission at Dakar, in return for permitting the French further to strengthen the defenses there. Our informant also believes that the Germans offered to arrange a general Franco-German agreement for the defense of French North and West Africa. Although Laval is reported to have approved this proposal, Admiral Auphan, objecting that such a pact would invite Anglo-American attack, apparently threatened to resign. Laval was obliged to put aside for the time being the proposed defensive pact, but is believed by our informant to have consented to the sending to Dakar of some kind of German observer or commission.

The Germans are reported to have sought to send a Stuka squadron to Dakar at an earlier date, but Boisson, the Governor General, while willing to have the planes, threatened to resign if German pilots came with them. Boisson is understood now once again to have proffered his resignation, presumably in connection with Laval's new negotiations. Pétain, however, has ordered him to continue at Dakar. Meanwhile General Barreau, the Commanding Officer in Dakar, and a man considered very friendly toward America, is expected to go on indefinite leave, to be replaced by a naval officer of unknown sympathies.

The German controlled press has been giving increasing attention to the Allied "menace" to Northwest Africa. Lately it has accused the United States of planning to seize

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the Atlantic islands and then Dakar as convenient bases for the transfer of troops from Brazil across Africa to Egypt.

At Nevers the Germans apparently also demanded a total of 200,000 tons of merchant shipping. Our source suggests that Laval will consent to turn over the 70,000 tons of shipping now interned in French ports which belongs to countries at war with Germany; but Laval may try to avoid turning over the balance in French shipping, for a time at least. Admiral Auphan, our informant states, strongly opposed the surrender of French tonnage.

Collaboration Measures at Home

In support of collaboration at home, Laval is said to have sent the Germans a telegram of congratulations following the Dieppe affair, and to have signed the Marshal's name as well as his own (it is not definitely known whether this was with or without Pétain's consent). While Laval might well consider this an easy way of gratifying the Axis at no cost, evidence of further material collaboration appears in the report that French powder factories at Bergerac, Toulouse, and Angoulême (the first two in Unoccupied France) will produce nitrate cellulose for the Germans after October 1. One informant believes that German orders now amount to 80 to 90 percent of industrial production in France.

Laval is apparently planning partially to meet German demands for labor by the deportation, first of Jews, and then of other foreign groups. Despite strong pleas from the Vatican and the United States, Laval has apparently not relented in his reported plan to expel 10,000 or more foreign Jews who have fled to France illegally since 1936. More than 3,000 have already been sent to Germany, according to one source. From Occupied France come reports of concentration camps in which several thousand Jewish children have been isolated and their identification papers destroyed.

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In what may be an effort to show that he is nevertheless attached to republican institutions, Laval has authorized the creation of "advisory" departmental councils. At the same time, however, he has swept away the last vestiges of Parliamentary control in a decree abolishing the Senate and the Chamber of Deputies. These bodies had long been prohibited from assembling except by special convocation, but they had apparently been meeting informally, to the annoyance of Vichy. Advices suggest that Laval may now reorganize the purely consultative National Council as a sop to Republican sentiment.

Internal Tension in Spain

Current tension between the Monarchists and the Falange is greater than at any previous time, according to a reliable and well placed observer, and the possibility of an explosion can not be ignored. The immediate issue is the bomb episode reported last week, in which prominent members of the Falange were allegedly implicated. Several resignations of high government officials are expected, among them that of the War Minister, Varela, a man of Royalist sympathies. The Franco press has been agitating about the need of loyalty to the Party at this time, and political unrest is general, according to diplomatic sources. A number of prominent Royalist leaders have come to Madrid. Franco's prestige and moral standing are reported to have suffered severely from his failure to condemn the Bilbao outrage, and his relations with the Army may become further strained if the death penalty is not imposed on the offenders.

Some straws indicating resistance to German demands have come from Madrid. Spanish authorities are reported to have refused entrance visas to some 50 Germans who would have been appointed to auxiliary services of the German Embassy. A Nazi request for the removal of the Captain General of

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Barcelona has also been declined, according to diplomatic sources. Nor was the German economic mission successful in attempting to go over the heads of the Spanish negotiating committee. There is no indication, however, that the latter made much headway in its trading with the Nazis.

Japanese Withdrawals

Japanese campaigns in the Far East were generally characterized by withdrawals during the past week. As the Chinese advance in Chekiang continued, it was evident that the Japanese were undertaking a wholesale evacuation of the areas which they had only recently conquered. In the south-eastern Solomons, after a hard skirmish with Allied air power, Japanese naval forces—apparently either unwilling or unable to press the fight decisively—withdraw. At Milne Bay in New Guinea, where a Japanese landing party ran into an Allied trap, they again withdrew.

Only in the Gilberts, where they already are in possession of Makin Island, did the Japanese move forward. Here, apparently against no opposition, they extended their control southwestward to include Nauru and Ocean Islands. In the Aleutians too the Japanese recently have been increasingly active, possibly indicating plans for further offensive moves, but as yet these have not been made. Japanese planes have been sighted around Atka Island, which lies 60 miles or more eastward from Adak Island. Adak itself was previously the easternmost area in which the Japanese displayed any marked interest. Signs of increased activity at Kiska are not wanting, and may even indicate the arrival of reinforcements.

Fighting on the Middle Melanesian Front

Aside from the continuing air duel, fighting on the Middle Melanesian front is now restricted to the rugged area around

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Kokoda in New Guinea, 60 miles across the Owen Stanley Range from Port Moresby. Ground units clashed sharply here this week, and Japanese pressure has increased. Reinforcements continue to arrive in the Salamaua area.

While an overland drive to Port Moresby is still not an impossibility, the security of this base has been greatly strengthened by our new position at Milne Bay. This strategic inlet at the southeastern tip of New Guinea dominates the China Strait, virtually the only channel through the barrier reefs and islands which extend eastward from the New Guinea mainland to Rossel Island, easternmost of the Louisiade Group. With Milne Bay and the southeastern Solomons in our possession, a successful Japanese advance on Port Moresby by sea is unlikely. On the contrary, the Japanese position in Middle Melanesia takes on an increasingly defensive aspect.

Allied air successes in this area have been particularly notable. Japanese attacks on our newly-gained air base at Guadalcanal have been repulsed with heavy losses to the Japanese and inconsequential casualties for the defenders. At the Japanese air base near Buna on New Guinea, 10 Zeros were caught taking off: six were destroyed, two damaged. By August 29 Allied airmen at Rabaul were encountering Zeros of an old type, slow and unable to obtain altitude, and our airmen in this theater appeared definitely to have the upper hand.

Withdrawals in Southeastern China

Hard on the heels of the withdrawing Japanese, Chinese troops reoccupied Chekiang's two most important airport towns—Ch'u-hsien, on the Chekiang-Kiangsi railroad, and Li-shui, northwest of Wenchow. Chungking announces that its forces are now approaching the railroad city of Chin-hua (Kinhwa), where another airfield is situated. At the western

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end of the railroad, in Kiangsi, the Japanese have fallen back on their base at Nan-ch'ang, where the Chinese claim to have carried the fight into the suburbs. In Kwantung province, other Japanese withdrawals have opened the way for a Chinese advance southward along the Hankow-Canton railroad.

Japanese Plans: Siberia?

The evidences of Japanese withdrawals in China and reverses on the Middle Melanesian front, the appearance of second-rate planes in the latter theater, and finally the sudden resignation of Foreign Minister Shigenori Togo may all point to the long expected attack on Siberia. Chinese officials, who have been somewhat puzzled as to the meaning of the Japanese withdrawals, now apparently are convinced that the troops are being sent north. Some 60,000 Japanese formerly in Chekiang, they believe, have been sent to North China. General Joseph Stilwell, now in India, has himself subscribed to the Siberian thesis, according to newspaper despatches.

The Resignation of Togo

Togo's resignation especially has been widely interpreted as presaging the Siberian attack. Justification for this view is derived from the part which Togo is reputed to have played in easing Russo-Japanese relations during his term as Ambassador at Moscow (1938-1940), and from the fact that Japan has avoided difficulties with the Soviets while he has been Foreign Minister.

Other observers point out, however, that Togo's resignation might just as well point to the opposite conclusion. His career has been marked by German influence. His wife is German, his college studies at Tokyo Imperial Uni-

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versity were primarily devoted to German literature, he has been Ambassador to Germany, and he was regarded as one of the prime engineers of the anti-Comintern pact. His resignation might, therefore, be construed with equal logic as indicating developments in Japan displeasing to friends of Germany—such as a Japanese decision *not* to attack Siberia.

These observers also point out that Togo's relinquishment of the Ministry of Foreign Affairs may amount merely to a further step toward the elimination of civilian influence in the cabinet. Until further events shed light on the reasons for the shift, these observers feel that speculation as to the significance of Togo's resignation must remain pure guesses.

In the past week, meanwhile, no changes have been reported in military dispositions along the Siberian border.

Japanese Treatment of Americans

There seems to have been neither rhyme nor reason in the variations of treatment of Americans in Japan and Japanese occupied territory, according to a competent observer who has had opportunities to talk at length with many of the passengers on the exchange ship *Gripsholm*. In Tokyo for instance, some American citizens were imprisoned, some were interned in a camp, others were interned at home, and still others were left free to move about the city. Some Americans in Shanghai were allowed the freedom of the city, while others were kept in solitary confinement. Some citizens had all property seized outright, while others had their holdings carefully listed and filed by Japanese authorities. There was an obvious animus against newspaper correspondents and a grudge against certain missionaries in Korea, but in very few of the other cases was there any evident reason for the particular type of treatment meted out.

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Economic Conditions in Japan

Passengers on the *Gripsholm* reported a variety of shortages in Japan. There was a severe shortage of fish in the first three months of 1942, attributed by some observers to scarcity of gasoline. Rice and sugar have been put under a rationing system, as well as salt and meat. Leather is extremely hard to get, and there is a shortage of paper. The clothing rationing allowance of one hundred points allows few purchases, a winter kimono alone using up 48 points. Drugs and medicines are scarce. The observers felt, however, that the drastic efforts which have been made to bring financial machinery under control, to increase taxes and prevent inflation have been to a degree successful, and that there is a general Japanese willingness to live up to regulations. The Japanese are fully organized for their war effort. Moreover, these observers believe that Japan is succeeding in consolidating her economic position in the conquered territories, and that she is growing stronger month by month.

Japanese Concept of the War

Informed observers on the *Gripsholm* believe that the racial aspect of the war, the task of "throwing the white barbarians out of Eastern Asia," is not to be disregarded as an element in the Japanese concept of the war. Although few of these observers would attempt a purely economic explanation of the war, many of them stressed the importance of the Japanese feeling that Japan must win a wide area which is as nearly as possible self-sufficient, and which provides all materials necessary for the waging of war. With but few exceptions however, these observers felt that in addition to racial and autarchic concepts, the Japanese were influenced by a mystical conviction of the mission of Japan, and the assurance that Japan was divinely called to bring order into Eastern Asia.

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The observers pointed out that those who hold such a faith can only be disabused of it by complete defeat.

Pause in India

Although outbreaks and sabotage are continuing in the countryside, urban and manufacturing centers in India are apparently beginning to return to normal. The East Indian Railway has resumed restricted service between New Delhi and Calcutta under military guard. Passengers report, however, that along one stretch of road between Gaya and Mogul Serai every station has been burned. At Calcutta, mica production, a few weeks ago curtailed by a half, now appears to be returning to normal, while about 10 percent of the factory hands who have been on strike have returned to work. Nevertheless, in the textile industry there have been further walkouts. At Madras, the two largest textile mills, both of which had important army orders, have shut down, while at Calcutta 6,000 of the 7,000 employees of a large cotton mill have gone on strike for what are described as "purely political reasons."

With the suppression of Gandhi's *Harijan*, the Government has now banned virtually every important nationalist journal in India. Against these press restrictions, the All-India Conference of Newspaper Editors, meeting at New Delhi, has vigorously protested. Although the Government has refused to relax the censorship, reports from New Delhi suggest that a new arrangement will provide for the precensorship of news by local Government advisers in consultation with local press representatives. Under this arrangement, some newspapers may resume publication.

In Calcutta, however, official pressure has evidently forced the resignation of the editor of the *Statesman*, India's leading paper. Although British-owned and edited, the *Statesman* has always shown an understanding of Indian nationalism

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and in the present emergency has appealed for conciliation. Now with a former information chief of the Government of India as its new editor, the *Statesman* will become little more than an official mouthpiece.

Actually the political situation in India has improved very little, and a general civil disobedience campaign is still threatening. Compromise proposals advanced thus far have not gone to the root of India's difficulties. A plan suggested by Sir Firoz Khan Noon, Defense Member of the Viceroy's Executive Council, for dividing India into five autonomous dominions, is simply the Moslem League's idea of *Pakistan* reduced to its logical absurdity, according to an observer in New Delhi. Such a proposal—providing for a federation of India as unworkable as that of the United States under the Articles of Confederation—would please neither Congress nor Moslem League. Nor have these two parties as yet come any nearer to a mutual understanding—despite a report to the effect that the Vice-President of the Moslem League has asked Jinnah to begin negotiations with Gandhi. Meantime, a resolution adopted by the Working Committee of the Hindu Mahasabha—the organization of Orthodox Hindus—has called for the immediate independence of India and the formation of a national government consisting of representatives of all parties, threatening drastic action if the British reject these proposals.

Hispano-American Neutrality Pact?

The retiring Argentine Ambassador to Spain is returning to his country with the draft of a neutrality pact to which the adherence of Spain, Portugal, Argentina, and Chile will be sought, according to unconfirmed information received from Buenos Aires. The pact presumably is a last-minute Axis-inspired move to counteract the effects of Brazil's

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declaration of war, especially in Portugal, and to fix Chilean policy before President Rios' visit to the United States.

Rios' visit meanwhile has been debated in the Chilean Senate—a debate which produced the first discussion of Chilean foreign policy during the current Chilean Congress. One Senator asked whether, if Chile were going to break with the Axis, it would not be better to do so before the President's trip, thus avoiding any appearance of yielding to pressure from Washington. No conclusion was reached, and the Senate has voted to hold a secret session for further discussion.

Cardenas Reenters Mexican Politics

The appointment of ex-President Cárdenas as Minister of National Defense marks a significant turning point in both the domestic and international activities of the present Mexican Government. Cárdenas, who is expected to have complete control of the Army, Navy, and Air Force, becomes the most powerful figure in Mexico, next to President Avila Camacho. The uneasy balance of power which has characterized the present regime from its inception now moves decidedly to the left, for Cárdenas represents more truly and effectively than any other person in Mexico the combined forces of organized labor, the agrarian reform movement, and the liberal and radical elements from every walk of life.

The return of Cárdenas to national prominence can be expected to instill confidence in the Avila Camacho Government on the part of Mexico's rural population, which is suffering considerably because of economic dislocations brought on by the war and consequently has become prey to the defeatist, anti-government and anti-Yankee propaganda of the fifth column. The weekly *El Sinarquista*, for example, which has been rather successfully exploiting the poverty and hunger of Mexican peasants, expressed the

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greatest alarm at the prospects of the Cárdenas appointment, indulging in one of its rare attacks on the ex-President, whose popularity with the rural masses it has generally respected.

Despite earlier controversy concerning the possible attitude of the new Defense Minister toward the United States, it can be stated conclusively that General Cárdenas is fully committed to the most vigorous prosecution of the war. It can thus be anticipated that Mexico's positive contributions to the war effort will be notably stepped up, in terms of both military preparation and political vigilance.

APPENDIX I

THE GERMAN TRANSPORTATION SITUATION

Since the outbreak of war in 1939, many observers have predicted the collapse of the German transportation system, which has been operating under great strain. Even when the increasing demands on the distant Eastern Front are considered, however, there is no evidence at present that would indicate an imminent breakdown, according to an analysis by the Central European Section of the Office of Strategic Services. On the contrary, it is conceivable that the volume of traffic can be still further augmented without serious impairment of the Axis war effort.

The factors which favor the German position are: first, Germany's absolute domination of the continental rail network, which has made possible the pooling of freight cars and locomotives for common use where and when they are most needed; second, new construction of equipment, the production of which may now considerably exceed previous estimates; third, the reorganization of railway management within Germany itself; and finally, the solution—partial at least—of the admittedly difficult problem of personnel.

On the debit side of the ledger is the current British air offensive, the results of which cannot yet be evaluated in detail. Present bombings are probably seriously interfering with transportation in certain areas, and further efforts systematically to disrupt German traffic and transportation may in time produce substantial results.

Unification Under German Control

At the beginning of 1938 the German National Railroads operated 33,790 miles of line. Territorial annexations to the Reich have increased this mileage to 47,700, and in addition 6,373 miles in the Government General of Poland and the Protectorate of Bohemia and Moravia are either under German management or subject to close German supervision. In occupied Russia about 18,000 miles of railroad have been converted from five-foot to standard gauge. Divisional commands, composed principally of German railroad officials but acting under military command, control operations in this area. German methods of management, operation, and maintenance have been introduced on all these lines, thereby integrating them in a unified network and increasing the efficiency of the system as a whole.

In other subjugated countries—as well as in Hungary, Rumania, and Bulgaria—management and operation are closely supervised by German authorities. The methods are very flexible. In some countries supervision is concentrated at the headquarters of the railroads, in others German officials are stationed at strategic points throughout the organization. In the whole of Axis Europe Germany thus controls a railroad system of 164,000 miles, almost all of it standard gauge and operated on a unified plan.

Pooling of Equipment

Uniformity of planning on a large scale notably influences the distribution of equipment. A pooling system of freight cars already is in operation throughout the territory of the German National Railroads and in the Protectorate. This pool now includes 1,100,000 cars. About 6,000 locomotives and more than 100,000 freight cars have been commandeered from the dominated countries or leased from Italy and from neutral countries.

Production Step-Up

To increase this pool, Germany has made remarkable efforts to step up locomotive and freight car production. At the outbreak of the war 31,000 locomotives were available in the areas now operated by the National Railroads and in the Protectorate, many of them over-age. In the three years from 1939 to 1941, 2,900 locomotives were built. A British report on equipment production estimates the present annual locomotive capacity in Germany and the occupied countries at 1,000-2,500. It is possible, however, that these figures may still need to be revised upward. Polish intelligence sources report that Julius Dorpmüller, Minister of Transport, has announced to the industry a new annual construction program of 7,500 "simple type" locomotives. While such a figure may seem startling at first glance, it is probably not impossible that after careful preparation the industry in Axis Europe could treble production, on the assumption of an expanded plant capacity, mass production methods, and a three-shift work day. Sufficient material and labor probably are being made available; reports from various sources indicate that equipment production has been given priority equal to that for aircraft, tanks, and submarines, and that skilled workmen are even being recalled from the armed forces.

At the beginning of the war 820,000 freight cars were available in the area now operated by the German National Railroads and in the Protectorate. It is estimated by the British that by 1941 production in Germany and the occupied territories had increased from 12,000 to 195,000 per year, and that a further increase may be expected in 1942. In spite of locomotive and car shortages, which up to date have been undeniable, the war-time demand has been met, and the supply probably will increase in the near future.

Traffic Regulation

On the lines operated at present by the German National Railroads, freight traffic was 36 percent higher in 1941 than in 1939. To cope with this traffic, passenger train service for civilians has been curtailed in Germany by about 50 percent, with even greater restrictions reported from other areas. Restrictions of this magnitude have had a decisive effect on the railroad operations throughout continental Europe, where in normal times passenger train mileage considerably exceeds the freight train mileage. (In the United States, peacetime passenger train mileage was about 45 percent of the total, in Germany it was nearly 65 percent.)

Freight traffic is regulated as to volume, distribution, and flow through a system of priorities and traffic regimentation. This system includes strict regulations for increasing the average carload and for speeding up loading and unloading. In 1941 the average freight train load was 12 percent higher than in 1938.

Reorganization of Railway Management in Germany

Germany has long been divided into three areas, in each of which a special agency under the supervision of the Ministry of Transport (known as *Oberbetriebsleitung*) had the right to make suggestions to the 31 Division Managements, the actual operating units in the railroad organization. Following the general pattern of concentration of power in the present German administration, the authority of these agencies was recently strengthened. They were elevated to *Generalbetriebsleitungen*, their managers were promoted from Directors to Presidents, and the Presidents were empowered to issue binding orders to the Division Managements. The effect has been a more efficient and more uniform handling of operating and traffic matters in large areas.

In addition, new agencies have been created to allocate and coordinate the tasks assigned to the various modes of transportation. Diversion of shipments to waterways is encouraged, and even enforced in particular cases, with the result that waterways traffic in 1941 was 21 percent greater than in 1940. The completion of the Midland Canal in 1938 established a direct connection between the Ruhr and central and eastern Germany, and the opening of the Adolph Hitler Canal in 1940 improved the situation in Upper Silesia. These developments have substantially reduced the pressure on the railroads.

Truck transportation never played a great role in Germany (only 300,000 trucks were registered before the war), and it has now been almost wholly discontinued because of the fuel situation. This has contributed to a slight extent in increasing the burden both on rail and water transport.

The Problem of Personnel

Before the war the German railroads had a staff of competent employees, but many of these have since been lost to the armed forces (especially to railroad and other technical units of the armed forces), and an increasing number of railroad men have been needed for work in the occupied areas. At home these employees have been replaced by less reliable persons. The 1,200,000 persons at present in the service of the German National Railroads include 80,000 women and 20,000 prisoners of war, as well as 90,000 other foreigners. This personnel policy may have affected the safety and reliability of operation in the Reich to some extent, but at the same time it has been an important factor in maintaining German control of the whole network of conquered Europe.

APPENDIX II

CHINA AND THE WAR—A COMMUNIST VIEW

(The following statements of General Chou En-lai, representative in Chungking of the Chinese Communist Party, were made to an American who was recently in Chungking. General Chou is recognized by authoritative American observers as one of present-day China's most important political thinkers. He lives in virtual isolation in Chungking, separated from social contact with other Chinese by reason of his party connections and the threat of official disapproval, and cut off by distance from his fellow Communists in northwest China. His views are presented here primarily for their interest as a reflection of Chinese Communist opinion.)

The Chinese War Effort

Asked whether Chinese Communists are satisfied with the Chinese war effort, General Chou distinguished two phases in the struggle with Japan. During the first two years, there was fierce fighting on many fronts, and the Central Government devoted its primary attention to military affairs—training troops, mobilizing the masses, and improving military organization. Although the Chinese lost many men, their armies became steadily stronger.

During the past three years, on the other hand, the Japanese attack has weakened, and most of the fronts have been relatively calm. Accordingly, the Central Government has paid little attention to the training of men in the modern technique of war and has been mainly concerned in disciplining the Communists. Only at such points as the Japanese actually attack, will Chinese troops fight.

Attitudes Toward Britain and America

General Chou said that historically Chinese authorities have developed their own way of dealing with British and Americans. When Britain had a strong position in the Far East, the Chinese were careful to preserve friendly relations. Now that the British have been defeated by the Japanese, Chinese authorities take a contrary attitude, and even fail to treat the British as allies in a united war effort. In reaction to the traditional arrogance of the British, anti-British sentiment in China is welling up.

Towards the United States, Chinese leaders have a different attitude. They consider that Americans in general know very little about China, and that the United States is easy prey for help, materials, and money. American generosity even excites some contempt. For example, when the United States Government gives loans and raises the question of terms, the Chinese now demand that there be no conditions—a loan must be a gift for their five years of fighting. If the United States refused to give help, the Chinese Government would threaten to make peace, but General Chou went on to say that there is no danger at all of China's making peace. Incidentally, he said, resistance has become a good business, since help is so easy to get. [Editor's note: Since the loss of Burma, the problem of supplying China has become notably difficult.]

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Probable Consequences in China of a Russo-Japanese War

Soviet influence on the Chinese Government is negligible, said General Chou. If the Japanese become involved in Siberia, Japanese armies in China will be deprived of offensive power. General Chou did not think that regular Chinese troops would attack Manchuria, but rather that the Chinese Government would utilize the new situation precipitated by Soviet-Japanese hostilities to make trouble at home. The Chinese Communists expect the Central Government to order them to attack the Japanese in Manchuria. When this order comes, General Chou said, the Chinese Communists will ask for supplies to strengthen their military position. It is unlikely that these supplies will be forthcoming. The Communists can not attack without them. The Central Government will accuse the Communists of disobeying orders and will then send troops against them.

Chinese "Imperialism"

Because the western imperialist powers have been expelled recently from some of their territories, one now hears, General Chou said, of Chinese "imperialism". It is impossible, however, to conceive of an imperialistic China in the present stage of Chinese economic development and while the pathetic disorganization now existing continues. China possesses large armies, but her military power is immobile. How then can China engage in military expansion southward? On the contrary, China after the war must discover a method of securing equal rights for herself in the South Seas.

Peace Aims of the Chinese Communists

China's first object must be to drive out the Japanese, said General Chou. All plans for the post-war future are illusory. Victory will be achieved only through democratization of China. Chinese economic democracy means state ownership and control of railways, arsenals, banks, and mines. But China is large. Her productive capacity can be increased by giving play to private capital. Without this it will be impossible for China to become a modern progressive economy. Only through private enterprise can advances be effectively accomplished outside the sphere reserved for nationalized enterprise.