

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date October 15, 1943.

To Chairman Eccles

Subject: Compulsory Savings.

From Mr. Stark

With only the exception of the Secretary of the Treasury, the principals in the administration's consideration of taxes believe that compulsory savings in some form should have an important place in the tax program. Yet, as far as public statements are concerned, on the Hill or otherwise, no one in authority has directly and actively sponsored the idea -- or explained it at all adequately. The impression has been allowed to develop that somehow there is something positively sinister about it.

Refundable taxes were made part of the Treasury program in a rather halfhearted way. Much more positively, they are a part of the recommendations that you have already submitted to the Committees. Presumably, you will be asked to testify before the Ways and Means Committee. May you not be less hampered by the restraints which thus far have precluded a forthright discussion of the subject by others, and so be in a position to deal with it more positively and adequately than they?

Following are the main points on which the case for your refundable taxes (compulsory savings) rests:

1. The most common objection is that voluntary investment by individuals in government securities -- particularly in savings bonds -- would tend to be reduced.

The answer begins with the fact that tax increases operate in the same manner.

Voluntary lending to the government is not the primary goal of a fiscal program. The first aim is to provide the Treasury with assured sources of revenue by compulsory means -- heretofore, taxes. If it were practicable to do the whole job this way, no one, least of all the Secretary of the Treasury, would wish to rely on voluntary contributions. Since that is not practicable, we go as far as the will of Congress and the technique of writing legislation will permit, and then do as large a residual job as we can of absorbing additional private funds through the voluntary purchases of securities (in order to cut down as far as possible the need to rely on bank credit). The refundable tax (compulsory saving) is proposed as a supplement to ordinary taxes and as part of the business of providing the Treasury with assured funds by compulsory means. By definition, it should take precedence over voluntary lending to the government.

The objection that compulsory savings would curtail voluntary subscriptions to savings bonds reflects garbled thinking that needs to be

straightened out by someone in authority answering with a simple and direct "Yes -- so would higher taxes", and then explaining what purposes would be served by compulsory saving.

2. This leads to the most important point, the fact that compulsory savings provide the Treasury with an opportunity to correct at least partially the trend toward a dangerous accumulation in private hands of virtual demand obligations in the form of savings bonds (over \$24 billion at the end of September).

Refundable taxes can and should be restricted as to redemption so as to afford the Treasury some measure of discretion in timing repayments. So long as we are committed to the present form of savings bonds for voluntary purchasers, there would be a positive advantage in shifting substantial amounts of private savings into refundable taxes -- or some other form of compulsory savings -- thus restricted as to redemption.

This point is of tremendous importance in connection with postwar problems, and up to the present time, there has not been the slightest mention of it in public statements on the tax program. I have discussed it with Randolph Paul and he is in full agreement, but despite his intention to bring it up if he is called upon to testify again, it is obvious that he will find it difficult to handle at all positively.

3. Prevailing conditions require that a disproportionate part of the proposed additional taxes be drawn from the lower income brackets. In the face of this necessity, the requirements of equity will be better served if increase in the tax burden on these groups is coupled with arrangements for refunds after the peak of wartime payrolls have been passed.

A corollary point is that refundable taxes made subject to some measure of Treasury control would offer a better prospect that the related funds (the "cushion of savings") would be made available at times when individuals and the economy of the country would be most benefitted.

4. The attitude of some people toward even the mention of compulsory savings suggests a feeling that there is something almost immoral about the idea. Doubtless, it stems from an instinctive revulsion against any association between compulsion and the act of saving which has traditionally been regarded as a voluntary procedure. If so, there is nothing to the point but tradition. For what it is worth, the answer is that while compulsory savings are no less compulsory than taxes, they do have the advantage from the taxpayer's viewpoint that he gets them back.

