July 31, 1937.

MEMORANDUM:

TO - The President

FROM - Chairman Eccles

The problem of foreign capital inflow, or hot money, as you have aptly called it, has been under consideration for more than nine months. That the problem was serious and that something should be done about it was publicly recognized last fall when you appointed a committee to study the matter and make recommendations.

The members of the Board and I have felt for several months that the situation could and should be dealt with promptly both by increasing substantially the withholding tax as well as by imposing a capital gains tax on equity securities, and that if these steps were taken to discourage capital from coming here, and foreign deposits already here from being invested, then it would be in order to supplement the tax legislation by a bill giving the Reserve Board authority to raise reserve requirements on foreign deposits. However, the Board feels, and I concur, that legislation increasing reserve requirements on foreign deposits would be entirely illogical unless coupled with an effective tax program.

During the past year more than four billions of gold have been sterilized by the actions of the Treasury and of the Reserve

Board. The Treasury has been criticized for increasing the public debt to buy gold and the Reserve Board has now exhausted its authority under the law to absorb gold by increasing reserve requirements.

While these actions dealt with the effects, nothing has been done to discourage the inflow up to now, largely because of the opposition of the State Department, which has been ready and willing at all times to discuss the problem, but has felt all along that the suggested methods of dealing with it by taxation would interfere with the trade agreements program, including the pending negotiations with the British and the ratification of the Canadian treaty.

In view of this, and considering the present situation in Congress, which would make it difficult to obtain adequate legislation now, and the fact that the gold movement has abated, at least temporarily, I believe that it would be preferable to defer action altogether until Congress meets again in January, and then if the situation requires it, to adopt a comprehensive tax program as well as the proposed banking legislation.

If the Treasury considers it desirable to enact the tax measures now proposed, of course, I would not object. However, I do not believe that this program is adequate to have an important effect on foreign capital inflow and investment in this country, particularly as it affects the stock market, and that it will not be considered as much more than a gesture after all that has been said upon this subject.