

Date October 11, 1943.

To Chairman Eccles

From R. A. Musgrave *R. A. M.*

MESSAGE:

For your information, I am attaching two brief memoranda presenting

1. A summary of the Treasury tax program, and
2. A discussion of the program and comparison with your proposals to Mr. Stam.

Attachments

Message delivered by _____

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date October 11, 1943.

To Chairman Eccles

Subject: Treasury Tax Proposal.

From R. A. Musgrave

The Treasury tax program -- for summary, see attached memorandum -- is conservative in its general approach and avoids details. Primary reliance is based on the individual income tax which provides for nearly two-thirds of the total increase in yield. The second most important item consists of increases in excises. Corporation rates are raised to 50 per cent.

The general structure of the Treasury program is quite similar to that of the program which you submitted to Mr. Stam. But there are important differences in total yield and in the impact of the increased taxes by income groups.

(a) Under both programs, the victory tax is repealed, but under the Treasury program, the reduction in exemptions is much smaller (exemptions for married taxpayer are to be lowered by \$100) than you had proposed. Also, the Treasury program does not provide for an increase in the normal tax to offset the repeal of the victory tax. As a result, the effective rates under the Treasury program are much lower for incomes under \$3,000, and remain substantially lower up to about \$6,000. From \$10,000 to \$20,000, the rates under the two proposals are about the same, but above \$20,000, the rates under the Treasury program are substantially higher. (See attached chart for a comparison of effective rates under both programs.) Of course, the higher rates in the upper income groups under the Treasury proposal do not offset the loss of revenue resulting from the lower rates at the other end of the scale, so that on the whole, the gain in gross yield from the Treasury schedule is only one-half that provided by the rates under your proposal.

(b) The Treasury program contains a tentative suggestion for tax refunds quite similar to that provided for in your plan. However, the Treasury program takes no position regarding the desirability of refunds. Refund schedules are merely submitted to Congress for consideration as a measure of relief if the Treasury rates are felt to place too great a burden on the lower-income groups. The one "innovation" of the Treasury program is the proposal to give the taxpayer the option to claim his refunds after the war in the form of paid-up life insurance policies rather than cash.

(c) Should refunds be given, the Treasury program recommends that taxpayers with "fixed" incomes be relieved of the refundable part.

(d) The Treasury program contains recommendations for sharp increases in estate and gift tax rates, not contained in your program. From the revenue

point of view, this part of the Treasury program is not significant.

(e) In connection with its program, the Treasury urges an expansion of Social Security which, if adopted, would become a substitute for part of the rate increases otherwise proposed for the income tax.

The Ways and Means Committee gave the Treasury program a very cool reception, notwithstanding Judge Vinson's strong plea in its support. (It should be noted, however, that Judge Vinson's testimony was more in favor of a 10 billion dollar program than in favor of the specific schedules proposed by the Treasury.) The basic criticism on the Committee's part reflects the fact that the members are not convinced of the need for a stiff program of any kind and the feeling that the taxpayer (particularly in the middle income groups) "can't bear any higher burden". With respect to the Treasury program in particular, the main criticism appears to be directed at the relatively light increase in rates for the lower income groups. Much emphasis was placed on the estimate that net income classes under \$3,000 would contribute only 30 per cent of the additional taxes while receiving 61 per cent of income payments, and that net income classes under \$5,000 would contribute only 54 per cent of the additional taxes while receiving 80 per cent of income payments. At the same time, there does not seem to be strong support for a general sales tax or a substantial reduction in exemptions. On the whole, it appears more likely that the Committee will refuse to pass a substantial bill of any kind than that it will vote a substantial sales tax.

Attachments

R. A. M.

EFFECTIVE INCOME TAX RATES
 PRESENT AND PROPOSED
 MARRIED TAXPAYER-NO DEPENDENTS

