L.H. Mc.HENRY & CO.

UNITED STATES TRUST BLDG.

Louisville 2, Ky.

February 27, 1946.

Mr. Marriner S. Eccles, Chairman,
Board of Governors,
Federal Reserve System,
Washington, D. C.

Dear Mr. Eccles:

I note your comments of February 25th, relative to the President's new Wage-Price policy, resulting in the possibility of a 10% increase in the cost of living, - You are right about it.

Relative to the Capital Gain and Loss provisions of the Income Tax law, the tax upon business trades, that is, where a security or other property is purchased with the idea of making a profit, is sound, and most all trades of this kind are generally completed within six months to a year. Such trades are voluntary; they are entered into with the idea of purchasing and selling at a profit, - it is a business transaction. They are entirely different from the transactions of an investor who, as you know, makes a purchase to obtain a return upon his capital. He gives little or no consideration to making a profit; he looks to the return. This is shown in that many securities sell above par, or above their call prices. Such profits which come from transactions of this kind should not be taxed at all; if they are taxed, as they are now, you are unfairly breaking down the investor's capital structure.

Another unjust feature of the present law is that if an investor acquires a security, and that security is paid by the issuing company before its due date, or is paid by act of law, the investor is taxed, although he has nothing whatever to do with the transaction, and never anticipated it when he made the purchase; he is punished through no act or intention of his own.

I trust you will give these matters serious consideration and do what you can to have the new tax law provide that no capital gains should be recognized where the property is held for, say, more than six months to a year, and where, in the case of securities, they are called for payment or paid before maturity by act of law.

Sincerely yours,

L. H. McHenry

LHM:mm

March 5, 1946.

Mr. L. H. McHenry,
L. H. McHenry & Co.,
United States Trust Building,
Louisville 2, Kentucky.

Dear Mr. Mc Henry:

This is to thank you for your letter of February 27. Unfortunately, the press misrepresented a reply I made to a question by Congressman Patman as to the increase in the cost of living. I did not predict that there would be a 10 per cent additional rise because, in the first place, it would be merely a guess to attempt to say how much further prices will rise. The OPA estimates that since the beginning of the war the increase has been 33 per cent. I said, in response to Mr. Patman's question, " I would expect that with increased wages and prices under the new wage-price policy that we will get some further increase. It is estimated that there is a possibility of it reaching as high as a mazimum of 40 per cent. I would think that if the cost of living can be held to 40 per cent above the prewar level that we will have done a fairly good job considering the size of this public financing that has been undertaken."

I was interested to have your comment on the capital gains tax. Several letters I have received mentioned the point you make as to cases in which a security is called with the result that the investor who had no desire to sell is required to pay the tax. This situation, of course, is in large part a result of the rising prices and hence declining yields brought about by speculative pressures. I have felt for a long time that the holding period should be extended, possibly to three years, and the rate of the capital gains tax increased because, in my judgment, this would effectively eliminate the speculative element, buying for the rise and relative quick turnover, instead of buying for the investment return and the longer range.

While I see no present prospect that such a tax will be enacted by Congress, I think that if it were put into effect it would go far to stop the higher prices and declining yields which, in turn, provide the inducement for refunding operations and the calling of outstanding issues.

In proposing a special capital gains tax, I have sought to emphasize that the tax should be applicable to future and not to past transactions. Accordingly, my proposal would not apply to existing situations and would, I am sure, greatly reduce or eliminate entirely the inducement for refundings to take advantage of declining rates.

Sincerely yours,

M. S. Eccles,
Chairman.

ET:b