

GEORGE WITSMA, JR.  
AMBASSADOR BUILDING  
SAINT LOUIS, MO.

November 27, 1941

Dear Mr. Eccles:

I notice in the St. Louis papers that you are quoted as desiring heavier taxes on corporations and more prosperous individuals before a levy is placed on wages of the lower income groups. With all respect for you, I differ from your conclusions. Corporations have reached a point where, to a large degree, all initiative and all incentive to make money is being killed.

I think I know what I am talking about, in view of the fact that I am a stockholder in several hundred companies, and am also the head of my own business. I have reached a point in my own life where my incentive to make money has been definitely killed, in view of the colossal amount of taxes I am compelled to pay. I am ambitious and hard-working and like to make money and have made plenty of it. I am not unwilling to pay taxes, but when I consider the amount of taxes that I am compelled to pay and the amount of effort that I have to put in to make them, I have come to the conclusion that it is cheaper for me, and I shall probably prolong my life, by making less money, and I have heard other men who are the heads of various businesses express the same sentiment.

Speaking in terms of the future, this policy of taxing corporations to death, in my opinion, will retard the progress of our great United States. Incidentally, it might be well to remind you that by taxing corpora-

GEORGE WITSMA, JR.

tions any heavier than they are now taxed, will probably be creating a hardship for many people who are depending on the dividends from many corporations for their sustenance. It is not my purpose to tread on the under-dog, because my own conclusions are that the country prospers when labor and other people in the lower brackets prosper. But not until such people are taxed, in my opinion, and definitely made to feel the burden of this situation, will they ever come to realize how serious it is. Hitherto taxes have been something that the other fellow always paid. I predict that when they reach the great masses, there will go up a cry to heaven, figuratively, which will make our government a little bit less prodigal than it has been in the past.

Surely a man of your experience and vision would be willing to agree with me that to say the least, in the last eight years our government has been extremely careless with money. It has been suggested by various economists whose remarks I have consistently followed that the government could cut off many billions of dollars per year in useless expenses. Before thinking of higher taxes, may I suggest this as the chief remedy.

Respectfully yours,



Mr. Marriner S. Eccles, Chairman,  
Federal Reserve Board,  
Federal Reserve Building,  
Washington, D.C.

December 2, 1941.

Mr. George Witsma, Jr.,  
Ambassador Building,  
St. Louis, Missouri.

Dear Mr. Witsma:

This is to acknowledge your letter of November 27 with regard to my recent talk before the National Industrial Conference Board. As the newspaper accounts gave a very much abbreviated version of it, I am enclosing a copy of the text.

However, I would not agree with you that at this juncture there is any necessity from the public interest standpoint for making the incentive for investment any greater than it is under present or, for that matter, prospective tax laws. As you know, more and more production must go for defense and we have reached, if we have not already passed, the maximum of production for civilian use. Because of the existing and probable shortages of strategic materials, to say nothing of skilled labor, it would not be wise public policy to attempt through incentive taxation to build new plants for civilian production. Moreover, there is no shortage of capital -- quite the contrary -- and, therefore, no need in the public interest to give capital further incentive to invest. Certainly our tax structure does not bear on capital any more heavily than is the case in all the leading countries that I know about today.

For a long time I have advocated spreading the income tax base. So far as the low income groups are concerned, however, they have been heavily

Mr. George Witsma, Jr.        -2-

assessed on consumption taxes, which have been greatly increased in the last decade.

Finally, I cannot go along with your on your assumption that "the government could cut off many billions of dollars per year in useless expenses." That is constantly being said, but it is wholly unrealistic and, in my opinion, far from being the chief remedy. I have no doubt that some expenditures could and should be cut drastically, but the aggregate would not be significant in the totals today.

While we do not see eye to eye, I nevertheless appreciate your courteous letter.

Sincerely yours,

M. S. Eccles,  
Chairman.

enclosures

ET:b

ROSS B. MATEER  
LICENSED PROFESSIONAL  
ELECTRICAL ENGINEER  
1869 WYNNEWOOD ROAD  
PHILADELPHIA, PA.

November 29-1941

Mr. J. Edgar Hoover  
Washington DC

Dear Sir:

The attached clipping is from a recent issue of the Wall Street Journal and I am amazed to hear of your passing a Confiscatory tax, camouflaged as a withholding tax: Such a drive on wages or Commissions is just like the Labour Racketeer, who plays his game under the flag of Unionism and frankly declares there are many who will defy their employer or the Administration to hold back on compensation earned. But withholding is cheating as you know, as well as the Government gets its returns on anything collected and refuses to be sized to collect. So the remedy must be in the individual who refuses to be regimented as to his earned rewards for energy, manual or brain. So, it is suggested you soft peddle a withholding tax and substitute a general sales tax. Then you hit at the root of things, purchases of necessities and you check rising prices.

Very truly  
R B Mateer

December 3, 1941.

Mr. Ross B. Mateer,  
1869 Wynnewood Road,  
Philadelphia, Pennsylvania.

Dear Mr. Mateer:

This is to acknowledge your letter of November 29 with regard to the so-called withholding tax. This is not my particular invention, but one which Treasury experts have considered and they, of course, have the responsibility for presenting tax programs to Congress.

The name is perhaps an unfortunate one, but in principle the tax is sound and equitable. It is based on ability to pay. It is collected at the source, which is a relatively convenient way to collect taxes, and it would bring funds into the Treasury currently out of incomes, dividends, etc. As I stated in a recent talk, I would like to see consideration given to coupling such a tax with some form of compulsory savings.

As for the general sales tax which you suggest, I have been and I continue to be wholly opposed to it because it is not based upon ability to pay and it bears with particular severity upon the lowest income groups who have the least at stake and the least to defend. Moreover, they are already subject to heavy indirect consumption taxes.

Sincerely yours,

M. S. Eccles,  
Chairman.

ET:b

# TAXES

*The* TAX MAGAZINE

214 N. MICHIGAN AVE., CHICAGO

EDITORIAL OFFICE

Chicago, December 2, 1941

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

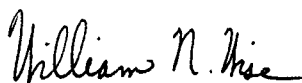
Dear Mr. Eccles:

May we have your permission to reproduce as an article in TAXES your recent address (Government Release Z-615) before the National Industrial Conference Board in New York City? Use of the material of course would be conditioned upon the Conference Board's agreement to release the material to us.

Please advise us at your early convenience.

Very truly yours,

TAXES - The Tax Magazine



William N. Wise, Editor

WNW:lw

December 4, 1941.

Mr. William N. Wise, Editor,  
Taxes, The Tax Magazine,  
214 N. Michigan Avenue,  
Chicago, Illinois.

Dear Mr. Wise:

Chairman Eccles requested me to acknowledge your letter of December 2 and to say that you have permission to reproduce as an article in "Taxes" his recent address before the National Industrial Conference Board, a copy of which I enclose.

This text was made public by being given to the press at the time of the address and therefore is released in full for publication, so you do not need to obtain permission from the Conference Board for republication.

Sincerely yours,

Elliott Thurston,  
Special Assistant  
to the Chairman.

enclosure

ET:b



*file*

# TAXES

The TAX MAGAZINE

214 N. MICHIGAN AVE., CHICAGO

EDITORIAL OFFICE

December 30, 1941

Marriner S. Eccles, Chairman  
Federal Reserve Board  
Washington, D. C.

Dear Mr. Eccles:

Separately we are sending you, with our compliments,  
5 copies of our January, 1942 issue, at page 9 of which  
appears your article entitled "Financing Full Production."

It was a privilege and a pleasure to present your  
interesting discussion to our readers, and we hope that in  
the very near future we shall again be honored to number  
you among our contributors.

Very truly yours,

TAXES - The Tax Magazine

*William N. Wise*

William N. Wise, Editor

WNW/da

*not sent Conf Bd  
NY - 11/26/41*

A COMMERCE CLEARING HOUSE PUBLICATION

CC: Marriner S. Eccles, Chairman ✓  
Board of Governors  
Federal Reserve Board  
Washington, D. C.

Chicago, December 2, 1941

National Industrial Conference Board  
247 Park Avenue  
New York, N. Y.

Gentlemen:

May we have permission to reproduce as an article in an early issue of TAXES the address of Chairman Marriner Eccles of the Federal Reserve Board delivered before a meeting of your Board in New York City on November 25, 1941 (Government Release No. Z-165) ?

A copy of our correspondence with Mr. Eccles, in similar vein, is attached.

Very truly yours,

TAXES - The Tax Magazine

William N. Wise, Editor

WNW:lw

BOARD OF GOVERNORS  
OF THE  
FEDERAL RESERVE SYSTEM

## Office Correspondence

Date December 3, 1941C Chairman Eccles

Subject: \_\_\_\_\_

From Professor Hansen

I have read your paper which you gave before  
the National Industrial Conference Board a week ago and  
I think it is a first-class job. It presents in bold and  
vigorous fashion precisely the point of view that needs  
to be stated and restated throughout the country.

A.H.H.

# THE SEABOARD REFINING CO., Ltd.

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907 BARONNE BLDG. - NEW ORLEANS, U. S. A.  
Dec. 4, 1941.

Hon. Marriner S. Eccles,  
Federal Reserve Board,  
Washington, D.C.

Dear Gov. Eccles:

I write to congratulate you on the excellent address delivered in New York at a recent meeting of the National Industrial Conference Board. It cannot but prove enlightening to many and inspiring to all who are really willing to do their full share toward National Defense.

There are, I regret to say, many successful business men putting forth dire prophecies as to the inability of this Country to stand the amount of taxation necessary to see World War No. 2 through to a satisfactory conclusion. Likewise, equally as many perhaps predicting a long and destructive depression, following a return to peace.

I am in hearty accord with your economic philosophy, as given in second paragraph, page 3, of the timely and admirable speech mentioned.

I am particularly glad to note frequent favorable references in the Press of the Country in recent days to your sound and specific recommendations made to Congress some months ago, concerning methods of taxation, price control, avoidance of inflation, etc. I earnestly trust a strong and helpful influence will yet develop therefrom.

I am anxious to aid the Federal Reserve System in every way possible and look forward with satisfaction to my third term of three years each, beginning Jan. 1, 1942, as a Class B Director in the Atlanta Bank, to which I was recently elected.

What are the prospects of a visit to New Orleans? Be sure to come whenever the opportunity offers.

Hoping you and yours are well, I remain, with regards and best wishes,

Cordially,

*Ernest T. George*

ETG/LM

December 10, 1941.

Dear Mr. George:

You were very thoughtful to write me your note of December 4 in regard to my recent talk before the National Industrial Conference Board. I appreciate having your favorable and encouraging comments.

While I do not see any immediate prospect of getting to New Orleans, particularly now that this war situation has come upon us, I have frequently recalled with pleasure my visit in 1935 and the luncheon that you gave for me.

I am glad to know that your interest in the System continues and that the Atlanta Bank is to have the advantage of your service as a Class B Director.

Sincerely yours,

Mr. Earnest T. George,  
The Seaboard Refining Co., Ltd.,  
907 Baronne Building,  
New Orleans, Louisiana.

ET:b

RUTGERS UNIVERSITY  
NEW BRUNSWICK NEW JERSEY

DEPARTMENT OF ECONOMICS

Dec. 4, 1941.

Dear Governor Eccles:

Last night I had the opportunity of reading your National Pub. Conference Board speech as printed in full in the American Banker. I enjoyed every word of it and, even though I am guilty of some presumption in offering an opinion, permit me to say that it was an extraordinary sound and convincing presentation. More strength to you!

Very sincerely yours

C. C. Egger

W. M. Munn  
Hon. Marriner S. Eccles.  
Washington, D.C.

December 11, 1941.

Dear Dr. Agger:

This is to thank you for your thoughtful note of December 4 with regard to my recent talk before the National Industrial Conference Board.

It is encouraging to have your favorable comments, the more so because of your knowledge of economic conditions.

Sincerely yours,

(Signed) M. S. Eccles

Dr. E. E. Agger,  
Department of Economics,  
Rutgers University,  
New Brunswick, New Jersey.

ET:b

Rec. 6<sup>th</sup> 41

My dear Mr. Eccles,

Your statement about raising  
Income Taxes even more dispro-  
portionately has left me winded.

Do for goodness sake realize  
what you are doing to modest  
women citizens like me; it is  
no part of Democracy for the  
government to play "Dick Turpin".  
(Rob the Rich to feed the poor.) We,  
too, have our responsibilities,



and if you kill the peace who lay  
the golden eggs, the government of  
The United States will be in a  
jam.

Labor is getting the highest wages  
ever paid in the history of the  
world, and shouting & striking  
for more, and the money is  
spent drunkenly — go to  
any department store and see  
what is being bought — so play  
fair and impose a federal  
Sales Tax, that will touch  
everyone alike.

Most of the economies imposed  
by the too high taxes, come out  
of the hides of women like  
myself, men don't change their  
habits readily, we cannot cut  
down on necessities and edu-  
cation for our children, and  
we as a class - except for the  
very poor - have the largest  
families, - therefore we over-  
work and we worry, and as a  
group we are on the verge  
of nervous or physical breakdown,  
and we are good citizens,  
the Eccles.

Very truly yours,  
Mary T. Case

December 15, 1941.

Miss Mary P. Case,  
Charlton Farm,  
Avon, New York.

My dear Miss Case:

This is to acknowledge your note of December 6 with regard to taxation. Let me say frankly that I do not like it any better than you do.

Compared to other countries, particularly the British and Canadians, we have not yet imposed taxes on individuals and corporations as high as are thought vitally necessary in those nations, not so much for the purpose of financing the war as to drain off the rising tide of buying power coming on a market that must steadily shrink so far as consumer goods, especially the durable goods, are concerned. In a word, our citizens have the choice between inflation or doing the things necessary to prevent it. One of those things is to pay taxes. Another, I agree, is to curb organized labor demand for constantly increasing wages. In any case, it comes down to whether you would prefer the curbs on inflation on the one hand or an inflation on the other that would take as much or more away from you in high living costs.

If you will reflect a moment upon the sales tax, you will realize that it is not based upon ability to pay but falls heaviest on those who not only have the smallest incomes but have the least at stake and the least to defend. It is wholly inequitable. Those who are fortunate enough to be in the higher income groups have the most at stake and the most to defend. Certainly they cannot wisely wish to shift the tax load to lower income groups which are already more heavily taxed on consumption than I have felt was just. I recognize that there are great inequities as there is, especially from the standpoint of the fixed income groups, and I wish I knew of some practical way to avoid this injustice.

I am venturing to enclose a copy of the talk I gave recently before the National Industrial Conference Board, as I assume it was a newspaper reference to this that prompted your note.

Sincerely yours,

(Signed) M. S. Eccles

M. S. Eccles,  
Chairman.

enclosure

Feb. 9<sup>th</sup> 42.

My dear Mr Eccles,

Thank you very much for your kind reply to my letter of Dec. 6<sup>th</sup>, which I am enclosing to make the following intelligible.

Due to Christmas, and the fact I am "Mrs Case" and have five children - who are in fact the reasons for my protestations - I have not yet read your speech, but shall do so at the earliest opportunity.

Being only a house wife & mere de famille, I cannot make you a clever answer, so must answer you in a homely parable.

My brother and his wife have two children, one - sound, average & normal, two - having diabetes, deafness, bad sight & a bad heart; they have so geared their lives to preserve & raise the sick child that (with the kindest intent) they restricted & deprived the whole child of her natural rights; suddenly this summer the well child ran amok, nearly ruining her life - and of course her parents too - they rushed her to a psychiatrist, a nice man, who talked to the girl & found she had taken the rap (which was not of her own making) just too long, she hated her young ailing brother, wanted her own way & set out to get them, caring nothing whatsoever for her family.

I, and other women like me, know that the "charity case" is a "hopeless case", we've dealt, usually in kindness, with too many of them.

We have reached the point where the other guy can stand on his own feet, take his own chances, relax! It takes all we've got - and sometimes a bit more - to keep our own noses above water.

This state of affairs among the normally independent and propertied classes created Hitler in Germany, and everybody got sold down river.

Certainly tax the lowest income group exactly the same percentage as the highest income group; it's everybody's fight.

Income tax, inheritance tax, & every other institution aimed at any one class is undemocratic and unjust. Property is ~~the~~ <sup>one</sup> measure of what a man, and maybe his ancestors, have done with their time, no one can quage or jeopardize

a man's time, nor his right to it.

It seems to me there is a Parable in the Bible about a little man burying his few talents & getting Hell from the Lord about it.

The trouble with this letter is, it represents the sentiments of an increasing number of people, who might create a Hitler - (not Mr Roosevelt) - and of course the outcome would probably be the same too, - we'd all go down River cheap.

Please read this, and give ear to my small voice; but please don't bother to answer again, as you must

Received in  
Chairman's Office  
be a busy man.

FEB 11 1942

OFFICE OF GOVERNOR  
of the

Federal Reserve System

Very sincerely yours,  
Mary T. Case,

February 16, 1942.

Mrs. Mary P. Case,  
P. O. Box 28,  
Avon, New York.

Dear Mrs. Case:

Chairman Eccles was interested to have your letter of February 9. I am sorry that we addressed it incorrectly, but your previous letter did not give us any correct indication.

In accordance with your request, I am returning Mr. Eccles' letter to you, and I am enclosing also a copy of his radio talk at the Town Hall Meeting last week.

Sincerely yours,

(Signed) Elliott Thurston

Elliott Thurston,  
Special Assistant  
to the Chairman.

Enclosures 2

ET:b



REPEAL MISSOURI SALES TAX COMMITTEE

Phone  
Main 1861

CAMPAIGN HEADQUARTERS

Elmer E. Walter, 722 Chesnut St., St. Louis, Mo.,  
Chairman  
Chas. P. Johnson,  
Campaign Director.

2/6/42

Mr. Marriner S. Eccles, Chairman,  
Board of Governors, Fed. Res. System,  
New York City, N.Y.

Dear Mr. Eccles:

As stated in your Chicago address, because a "general sales tax... tended to drag the standard of living of the lower income wage groups to a point where health and national morale would suffer".


The direct appeal in your New York address fully concurred in, that all states should eliminate state sales tax. In my direct appeal to the Hon. Pres., Franklin D. Roosevelt, last October and copy to your office, set out the dangers for both our economic and social structures as well as gnawing at the foundation of democracy with a sales tax.

You can list Missouri as the first State to take the initiative for repealing this vicious tax. Survey of the State shows, 75 per cent of all business and consumers contacted in favor of repeal and 91 per cent for taking the tax off of food.

The repeal conducted by privileges set forth in both national and state constitutions, the right of petition. This is to appear on our general election ballot Nov. 3, 1942. Our requirements, 5 per cent of signatures of legal voters of the last general election in two-thirds of our 13 congressional districts. All work carried on through volunteer contributions. We feel more than confident, Missouri will be the No. 1 State in answering your appeal.

Will keep your office advised from time to time of progress and permit us to thank you in advance for further cooperation on this subject.

Very truly yours,

  
Chas. P. Johnson, Director.  
Ex-Capt/ S.C. U S A

CPJ/m

February 13, 1942.

Mr. Chas. P. Johnson, Director,  
Repeal Missouri Sales Tax Committee,  
722 Chesnut Street,  
St. Louis, Missouri.

Dear Mr. Johnson:

This is to acknowledge your letter of February 6. The objections to a general sales tax would, of course, apply to local as well as Federal taxation. However, I am strongly in favor of selective excise taxes at this time to discourage civilian consumption of critical materials, and I am wholly opposed to the principle of reducing local taxation at the present time in order to make it easier to pay Federal taxes.

I am venturing to enclose a copy of what I said at the Town Hall broadcast on February 12, as this pretty well summarizes my general viewpoint. In other words, I would not want to have it thought that my appeal is in any sense for a reduction in local taxation, though of course this would not bar repeal of unfair or inequitable taxes provided, however, some effort was made to replace them by taxation that would be fair and equitable.

Sincerely yours,

(Signed) M. S. Eccles

M. S. Eccles,  
Chairman.

Enclosure

ET:b

MINNEAPOLIS  
STAR JOURNAL AND TRIBUNE

JOHN COWLES  
PRESIDENT

December 22  
1941

Mr. Marriner S. Eccles  
Federal Reserve Board  
Washington, D. C.

My dear Marriner:

I was sorry not to get to see you when I was in Washington last week, but I can well appreciate how swamped you were with the new war developments.

Your address before the National Industrial Conference Board in New York on November 25th interested me very much, and I find myself in pretty complete agreement with all of your views. You are certainly right in saying that finance must be the servant of economic activity and must be used to stimulate production and employment, so that we will attain both a larger total and a more equitably distributed national income.

You will undoubtedly have considerable to do, either directly or indirectly, with framing the new tax law, and there are two points in connection with it that I would like to bring to your attention.

First, under the terms of the existing excess profits tax law, borrowed money capital is treated substantially less favorably than equity capital in computing the excess profits tax credit, whereas, in my opinion, borrowed money capital should be at least on a parity with equity capital and should conceivably be given a slight edge.

If a corporation is forced to suspend dividend payments on its common stock (or equity) capital, the corporation's future existence is not thereby jeopardized. Borrowed money capital, on the other hand, is a much more onerous thing than equity capital. If a company defaults on either its interest or its debt retirement provisions, it faces receivership.

While obviously from now on taxes are going to have to be extremely heavy, unless corporations are allowed an opportunity to earn enough, above interest and taxes, on borrowed money capital (1) to justify their taking that risk, and (2) to enable them to repay the borrowings out of the net earnings on that additional capital over a reasonable period of years, there will be no new borrowing or lending and the economic system will stagnate.

And if companies now owing borrowed capital in amounts large in proportion to their total capital are not permitted to earn net after interest and taxes amounts sufficient to enable them to retire their indebtedness over a reasonable period of time, we will have a lot of technical receiverships.

This would probably mean that we would have to have a new super-R.F.C. to refinance companies that, because of taxes, cannot meet debt retirement provisions. I also know various individuals who have purchased a business and had the company give its notes for the purchase price in the apparently reasonable expectation that over a period of years net earnings would be sufficient to retire the indebtedness. If the present discrimination against borrowed money is not eliminated in the new law many such individuals will lose their equity due to their inability to net sufficient above taxes to enable them to meet their obligations.

Under the present law, a company owing \$5,000,000 of notes or bonds payable at 4% interest

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1941

is allowed a credit for excess profits taxes of eight percent on half of that borrowed capital, which credit amounts to \$200,000. In addition, half the interest paid (half of \$200,000 or \$100,000) is regarded as a deductible expense, so the total credit before interest amounts to \$300,000. From that \$300,000 credit, \$200,000 of interest must be paid, leaving \$100,000. \$100,000 is 2% of the \$5,000,000 borrowed. If, because of borrowing that \$5,000,000, the company's earnings before interest increased exactly \$300,000 the company, after paying interest of \$200,000, would have \$100,000 left. This \$100,000 would be subject to the normal income tax of 31%, leaving net after interest and taxes \$69,000, or only 1.38% on the \$5,000,000.

In other words, the company could only earn 2% before normal tax, or 1.38% after normal tax, on its borrowed capital before being liable to excess profits taxes.

I realize that the problem is complicated, but I do not believe that our economic system will properly function unless it is possible to retain more than 1.38% net on borrowed money capital before paying excess profits taxes.

If the borrower were paying 5% interest he could then retain only slightly over 1% before paying excess profits taxes on the earnings from that borrowed capital. If he were paying only 2% interest, he could retain more than 2%. This variation in itself is an inequity. It favors the strong companies, that can borrow at low rates of interest, and penalizes the smaller or weaker companies that must pay a higher rate of interest.

My specific suggestion for remedying this inequity in the present law is that all companies be allowed to earn, net, say 5% above interest on existing borrowed money capital before being subject to any excess profits tax. That is certainly not an excessive percentage because if the normal corporation income tax is increased to 40% it would leave only 3% net after normal tax as the maximum that a company could retain on borrowed money capital earnings without being subject to excess profits taxes. That would enable companies, however, if they prospered, to earn enough on their borrowings to repay them over a period of 33 years.

Unless some such provision is written into the new law in regard to borrowed capital, I fear we will be permanently crippling the functioning of the economic system.

Another opinion regarding the new tax law that I want to throw into the hopper is something that a dozen different business men mentioned to me when I was in England last winter with Wendell Willkie. They said the greatest fiscal mistake the British government had made was to establish a 100% excess profits tax. They said the unintentional effect of that levy was to encourage higher costs and reduced efficiency; that during a period when there was already a shortage of man power, it was a serious mistake to levy a tax so high that there was no financial incentive for corporate managers to try to get along with fewer people on the payroll. They said that the theoretical possibility that part of this excess profits tax might be repaid after the war was not psychologically important enough to influence business executives' actions, and that because all earnings over the previous base figure had to be paid to the government in taxes there were needless employees and unnecessary waste in the administration of almost all businesses in England.

I assume that some people will advocate extreme increases in our present excess profits tax rates. I think it important that these rates not be put so high that they will eliminate the incentive for efficient, economical operation. I do not know the percentage of tax

December 22  
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at which the psychological breaking point comes, but there obviously is some such breaking point. If we pass that point I think we shall unintentionally encourage inefficiency, reduce the government's tax collections from corporations, and increase the economic forces trending toward inflation.

If and when you have the time, I should appreciate your writing me whether you are in general agreement with the views that I have expressed. If you are in such agreement I think you will be performing a genuine public service in seeing that your views are impressed upon the people who will be writing the new tax measure.

With warm personal regards, and the hopes that our paths will cross again in the not too distant future,

Sincerely yours,

A handwritten signature in cursive script, reading "John Cowles". The signature is fluid and elegant, with a long, sweeping underline that extends to the right.

John Cowles

January 5, 1942.

Mr. John Cowles, President,  
Minneapolis Star Journal and Tribune,  
Minneapolis, Minnesota.

Dear John:

This is to acknowledge your letter of December 22. I am glad to know that you are in general accord with my talk before the National Industrial Conference Board. I am sorry I did not have an opportunity to talk with you when you were in Washington.

You raise two points in regard to taxation that I have discussed with our staff here. While I appreciate the importance of enabling corporations to meet fixed obligations to repay debt, I do not believe it would be wise to increase the allowance for borrowed capital as it stands in the present law. Meeting obligations to repay debt is a method of reinvesting profits and it is difficult to see why the stockholders of A corporation should be allowed to make a larger amount of profits free of excess profits tax (because they invest part of the profits in the repayment of debt) than the stockholders of B corporation who have an equal equity investment but no corporate debt to repay.

The example you cite paints the picture a little blacker than it actually is. A corporation that makes 6 per cent on money borrowed at 4 per cent would have only 2 per cent to devote to the repayment of debt, if it had no taxes at all to pay on these earnings. The sum that can be devoted to the repayment of debt is not the amount earned "before being liable to excess profits" but the amount left after excess profits are paid. Earnings on equity capital are also available for the repayment of debt.

I am very much interested in the criticisms of the 100 per cent excess profits tax rate you heard on your trip to England. In the course of my statement in September on the price-control bill before the House Banking and Currency Committee I expressed my opposition to excess profits tax rates so high as to impair efficiency.

I hope I will have better luck the next time you are in town and we can get together.

With kindest personal regards,

Sincerely yours,

(Signed) M. S. Eccles

ET;b

BOARD OF GOVERNORS  
OF THE  
FEDERAL RESERVE SYSTEM

## Office Correspondence

Date December 31, 1941Mr. ThurstonSubject: Comments on Cowles LetterFrom Martin Krost  
MK

1. Most people would say excess profits ought to be defined in terms of return on funds provided by stockholders, not by creditors. If the stockholders of A corporation have an equity investment of \$100,000, they should be entitled to make the same profits, free of excess profits tax, as the stockholders of B corporation, who also have an equity investment of \$100,000. If B has borrowed \$100,000, the law allows it to deduct interest on the amount borrowed. If it makes more than interest on the money borrowed, B's stockholders will make more profits than A's stockholders. If A's profits are just enough, B's are excessive and properly subject to tax. In meeting its obligations to repay the principal of the debt, B is adding to its stockholders' equity and increasing their wealth. Why should the Government allow B's stockholders to make a tax-free reinvestment of profits and not A's stockholders, because B happens to be in debt and A does not?

In fact, however, the law does make a concession to stockholders of debtor corporations and allows the same rate of return on half of borrowed capital as on equity capital. The difference between the interest actually paid on borrowed funds and the 8 per cent statutory rate of return allowed represents a considerable concession, which should not be further increased.

2. The trouble with the corporation cited in Mr. Cowles' example is not excessive taxes, but inadequate earnings before taxes. If it makes only 6 per cent on its borrowings and pays 4 per cent interest, it would have only 2 per cent to devote to debt repayment even with no taxes at all to pay. If it makes 10 per cent on its borrowings, it will have 4.5 per cent to devote to debt repayment after paying normal and excess profits taxes at existing rates. What is available to repay debt is not what it can earn before it pays its first dollar of excess profits tax but what it has left after paying its actual excess profits tax liability. Moreover, anything earned on equity capital is also available to repay corporate debt, if the stockholders wish to dispose of profits in that way.

3. The simplest way to eliminate the differential cited by Mr. Cowles between earnings allowed to companies paying low rates of interest and companies paying high rates of interest would be to make no allowance for borrowed capital at all.

4. The Chairman is on record in the price-control hearings as being opposed to excess-profits tax rates so high as to destroy the incentive for efficiency in management.

5. The following paragraphs attempt to express these ideas in a form suitable for a reply:

To: Mr. Thurston

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While I appreciate the importance of enabling corporations to meet fixed obligations to repay debt, I do not believe it would be wise to increase the allowance for borrowed capital as it stands in the present law. Meeting obligations to repay debt is a method of reinvesting profits and it is difficult to see why the stockholders of A corporation should be allowed to make a larger amount of profits free of excess profits tax (because they invest part of the profits in the repayment of debt) than the stockholders of B corporation who have an equal equity investment but no corporate debt to repay.

The example you cite paints the picture a little blacker than it actually is. A corporation that makes 6 per cent on money borrowed at 4 per cent would have only 2 per cent to devote to the repayment of debt, if it had no taxes at all to pay on these earnings. The sum that can be devoted to the repayment of debt is not the amount earned "before being liable to excess profits" but the amount left after excess profits are paid. Earnings on equity capital are also available for the repayment of debt.

I am very much interested in the criticisms of the 100 per cent excess profits tax rate you heard on your trip to England. In the course of my statement in September on the price-control bill before the House Banking and Currency Committee I expressed my opposition to excess profits tax rates so high as to impair efficiency.