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AFFILIATED WITH NORTHWEST BANCORPORATION

DULUTH 1, MINNESOTA

February 21, 1945

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

Dear Mr. Eccles:

It is reported that on February 20th in a general discussion before the Senate Banking Committee you outlined certain measures which might be adopted to combat the threat of inflation. The first two methods appear to me to be desirable, namely, (1) a balanced Federal Budget, and (2) continuation of price controls and material allocations.

Regarding your item No. 3, in which you propose a Capital Gains Tax "to eliminate the speculator", the following considerations deserve attention.

1. Capital appreciation does not produce income, and thus a tax on Capital Gains is actually a tax on capital, taking the country as a whole.

2. An exorbitant Capital Gains Tax would tend to diminish the free flow of trade and, therefore, accentuate the very thing which you are trying to avoid, namely, price appreciation, because you would be eliminating many sellers through disinclination on their part to establish a capital gain subject to tax. Even under present rates many a sale is postponed or avoided because the holder realizes that after the Capital Gains Tax has been paid he has less money to purchase some other capital asset. The result is that prices are allowed to mount to ridiculous levels before holders can be induced to sell. An increase in Capital Gains Tax would accentuate this tendency.

3. Increases in the value of stocks which results from the accumulation of corporate earnings should not be taxed at a high rate, since, as you have pointed out, those corporate earnings have already been taxed at rates going up to 95%. For that matter, dividends resulting from corporate earnings should not again be taxed to the individual. This combination of double taxation on corporate enterprise is stifling to the growth and development of free enterprise as opposed to Government ownership and operation.

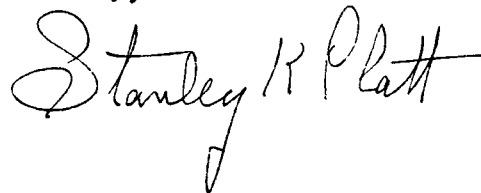
This leads up to another point. In order to place private corporations on equal footing with municipally operated enterprises and co-operatives it may become highly desirable to eliminate taxes on corporate income entirely and rely chiefly upon individual income taxes. In that event the Capital Gains Tax would be justified to the extent that the capital gain results from accumulated earnings of a corporation which are

not paid out to a stockholder in the form of dividends. In other words, it would be desirable to eliminate corporation taxes, but tax dividends and the individual's share of retained earnings of the corporation not distributed by the corporation. This would be more desirable and equitable than the present system. But if present corporate taxes are to be retained taxes on dividends and capital gains should be reduced or eliminated.

My reason for writing this letter is that the level of taxation has become so high due to influences of the War and the necessity of ultimately reversing the deficit financing of the past many years that the allocation of taxes has become a determining influence which will work for or against the health of American business.

It seems to me important that if Government ownership and operation of business is to come in this country that it should do so only because of demonstrated efficiency and superiority and not because of an inequitable system of taxation which discourages private enterprise and encourages municipal or Federal enterprise.

Yours sincerely,



SKP:EC

P.S. The above is a personal expression of opinion and does not concern the bank with which I am associated.

February 26, 1945.

Mr. Stanley K. Platt,
First and American National Bank,
Duluth 1, Minnesota.

Dear Mr. Platt:

This is to acknowledge your letter of February 21 in regard to my testimony before the Senate Banking and Currency Committee. I had not expected to be questioned on the inflationary dangers in the uncontrolled fields of capital values and did not have a prepared statement. Thus the press accounts, which were at best rather sketchy, were also misleading.

I am, of course, familiar with your various observations about the capital gains tax under normal conditions. You recognize that virtually all taxation has some effect on risk capital, though I sometimes grow impatient with the exaggeration characteristically inherent in arguments against a capital gains tax. Most of the special pleaders are all against any tax on the gains, but they are fanatically in favor of allowance for losses.

However, what I was proposing as an emergency anti-inflationary instrument was a special penalty rate on speculative capital gains. To the extent that such a rate would drive the speculator, that is, the buyer thinking only in terms of a quick turnover, out of the market, and to the extent that it would narrow the indefensible differential under wartime conditions between the income tax and the normal capital gains tax, the proposal I have in mind would protect capital.

I have previously discussed the deterrent effects of double taxation affecting equity capital and agree with you on this point. With regard to the total elimination of corporate taxation as proposed in the Ruml-Sonne plan, among others, while I agree in principle, I doubt very much that the Congress could be persuaded to go that far.

I wanted you to know that I was interested to have your letter and appreciated your thoughtfulness in writing.

Sincerely yours,

M. S. Eccles,
Chairman.

ET:b