

DIARY

Book 185

Social Security - Part II

Social Security

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RE SOCIAL SECURITY RECOMMENDATIONS

January 21, 1939.
2:30 p.m.

Present: Mr. Gaston
Mr. Seltzer
Mr. Haas
Mr. Blough
Mr. Reagh
Mr. Murphy
Mr. Riefler
Mr. Viner
Mrs. Burns
Mr. Hansen
Mr. Brown

H.M.Jr: All right, Mr. Viner.

Viner: Well, you asked Mr. Reagh yesterday for certain material, and he has it for you.

Reagh: The only difference in the figures that I have today and those that I gave yesterday are that these figures are based on the additional assumption that the reserve would be allowed to decrease to zero before the Federal Government came in with a subsidy.

H.M.Jr: On that assumption?

Reagh: Yes. The figures I gave yesterday were based, you remember, on the fact - or on the assumption that the reserve would be allowed to increase until the actual outgo was equal to or began to exceed taxes and then it would be frozen at that point and the Government would come in with a subsidy to keep it at that level.

And these figures have all been checked with the Social Security Board.

I think I'll - shall I pass a copy of these figures out to everyone? Then I can read them at the same time.

These were the three schedules that I gave yesterday, and I have comparable figures on the three different bases where the reserve is allowed to go down to zero.

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H.M.Jr: Which one do you want me to look at first?

Reagh: I expect you're interested in the longer schedule there, because the shorter schedule is the one we talked about yesterday.

H.M.Jr: This one? Well now, explain it. Will you explain it?

Reagh: Yes. Have to talk from your copy, Larry.

The first schedule is based on the assumption that the present scale of tax rates would be left unchanged and that the Federal Government would come in with a subsidy when the reserve was exhausted. And on that basis note that the reserve reaches a maximum of about six billion dollars in 1952, and thereafter - no, I'm sorry, in 1955 or 1956 it reaches a maximum of six billion 617 million. At that time the reserve begins to decrease, and in 1969 the Federal Government comes in with a first subsidy of 132 million dollars.

Those figures increase - I might read them off by fives. In 1975 that has gone up to a billion 500 million - going up very rapidly in those first years. In 1980 the total Federal subsidy would be a little over two billion dollars annually. That represents approximately - or, expressed as a percentage of payrolls at that time, about five percent.

The next schedule is on the same general basis, except that the tax rate is frozen at one and a half percent on employer, one and a half on employee, with a Federal subsidy based on this three-way split, that is, equal contributions of employer, employee, and Federal Government. Under that schedule the reserve is exhausted in 1951, when the subsidy is 550 million. In 1955 that's increased to 706 million, and in '60 882; in '65 a little over a billion; ultimately, a billion and a half.

With the tax rate frozen at the present level of one percent on employee and one percent on employer, the reserve would be exhausted in 1946, when the Federal Government's subsidy would start at 309 million dollars, going up to 700 million in 1955,

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over a billion in 1965, a billion 350 in 1975, and ultimately a billion and a half.

Hansen: Incidentally, might I remark there, that last column there would also indicate the rate at which the payroll taxes would rise.

Reagh: That's right.

Hansen: So you see exactly how that would be stepped up.

Reagh: That column is merely the Federal subsidy expressed as a percentage of payrolls at that time.

Burns: In other words, it makes no difference in the subsidy as a percentage of payroll after about 1951. The two - the Federal subsidy is then uniform.

Reagh: Except on the first plan, if you allow the present tax rates to remain unaltered.

Burns: I mean on the second two plans.

Reagh: That's right; put it at that time on a strictly cost-by-years or pay-as-you-go.

Hansen: Has your office also got the figures that you gave last night by years, every single year?

Reagh: We could furnish those. It's quite a little clerical work to bring that forward, but we can do that if you're interested; and would you like to have me prepare that and send it to you?

Hansen: I would like it. I don't like to - I don't like to burden you.

Reagh: It's not too much of a job; it does take a little time.

H.M.Jr: Well, I think this is very enlightening. Is this the first time these figures have been prepared?

Reagh: No, Mr. Secretary. These figures have been obtained on a little bit different basis, however, and the basic figures are Social Security Board calculations. They have not been reviewed as to assumptions on which

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they're based by the Treasury; we have had no opportunity to do that.

H.M.Jr: But you will do that, won't you?

Reagh: We'll do that, yes, as soon as they come out with a specific proposal. They're changing every day so far, so it's not worth while to try to keep up with them.

Hansen: Mr. Secretary, I think this is the first time this kind of a table has been made up. I've never seen a table like this, have you, Brown?

Brown: I've seen it in various calculations by five-year periods; but, as Mr. Reagh says, it's been on different bases.

Reagh: We merely transformed Social Security figures to this particular basis.

Hansen: To this particular form of presentation.

Viner: Percent of payroll column - was that in the other tables?

Reagh: I don't believe it was.

Hansen: It's a new form, and very enlightening.

Brown: Very valuable form.

H.M.Jr: That means, for instance, if it's 3.05 percent of the payroll - subsidy, percent of the payroll. - is that - that would be in addition to whatever employer and employee contributed. Is that right?

Reagh: Yes, that means just this, that at that time the employee would be contributing at 3.05 percent, the employer at 3.05 percent, and an additional 3.05 by the Government.

H.M.Jr: That means over nine percent?

Reagh: Multiply those figures by three for the total.

H.M.Jr: Well now, what are these additional ones?

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Reagh: Well now, that shorter schedule is merely the figures which I gave to you yesterday on a slightly different basis, and that schedule is based on the assumption that the reserve would be held at its maximum point rather than being used to postpone the government subsidy.

H.M.Jr: Well now, interpret these. I've got three sheets of those. Which one do you start with?

Reagh: Let's see, you have - now, if you hold the present tax rates on this one - present taxes - those go hand in hand for the first one on this sheet. The only difference between these schedules is that I have worked them out on a year-by-year basis for a longer period of time. In this case, when the reserve gets up to a maximum of six billion 600 million, it's allowed to stay there; the Federal subsidy is brought in so that won't be used, and you freeze it at six six. On this one it goes up to six six, but it's used until it's depleted; then the subsidy comes in.

(Reagh and H.M.Jr converse in low tones, words not understandable)

H.M.Jr: What?

Reagh: Yes, I think that would be an improvement: a footnote

H.M.Jr: that you freeze it at six six. And this one you freeze at two four.

Reagh: At two four, because that's the maximum point it would get.

H.M.Jr: And in this one you freeze it at one seven. I think there ought to be footnotes. Do you want to explain to the rest of the people here what we're talking about?

Reagh: Yes. The point that the Secretary just brought out is that there might be a note of explanation as to the difference between those two schedules: that in one case the reserve is frozen at the point where it

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reaches a maximum

Burns: So is it right to call this contingency reserve in this other long table? Isn't it vanishing reserve?

Reagh: I wouldn't want to call it a contingency reserve any more.

Burns: I mean it isn't a contingency reserve.

Brown: Just a technical method of presentation which involves the elimination of the reserve. No, certainly when you say the word "frozen," it chills me a little bit, because the word "frozen" - this very reserve here is an elastic item to meet business depression; so that while on a table it looks like a constant figure of, say, six billion 600 million, it would certainly in fact be ...

Hansen: Rise and fall.

Viner: It would be secretly fluctuating but secularly stable.

Reagh: That's right; we didn't want to predict those cycles.

Brown: Well, that's a sound approach.

Reagh: This other schedule might be interpreted as a contingency reserve in which the contingency has arisen.

Viner: I'd call it a vanishing reserve. It's a disappearing reserve. You're eliminating the reserve here.

Reagh: That's right; in other words, we've reached a depletion.

Brown: We have a long contingency.

Blough: It's a trend to eliminate the reserve.

Burns: It isn't a contingency, in the normal

Viner: No, I don't think contingency

Reagh: It's not the right word there.

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Viner: A reserve for the preliminary period; no reserve for the later period.

Reagh: Should be corrected in that respect.

Viner: You might call it a growth period reserve.

Hansen: Yes, that's good.

Reagh: I think that's a good name for it; I'll put that on there. Can you think of a better one?

Viner: All rights reserved, including Scandinavian.

H.M.Jr: That's that. At any rate he's done a good job.

Viner: Yes, he certainly has.

Now - next point - we were discussing the problems of administration arising out of the extended coverage of the Social Security program - domestic servants, farm labor, and also incidentally to employees of very small concerns; and we had Mr. Graves in to tell us about the administrative problems of using the tax system, as he saw them.

Blough: Stamp.

Viner: I beg your pardon - of the stamp system, as he saw them. And Mr. Graves gave a pessimistic picture of the administrative problem if we tried to get anything like full compliance, although he said it would be a relatively simple problem if we accepted it as essentially a voluntary scheme.

Mr. Douglas Brown, from his study of the British system, thought, I think, that Mr. Graves' fears were excessive. And then in the discussion that resulted we reached this conclusion, which we presented to you as a recommendation of the group: "It is recommended that the Treasury Department send a group of qualified persons from its staff to study the operation of the stamp-book method of collection of social insurance contributions in England and other representative European countries."

H.M.Jr: You mean you're going to send Riefler there instead of Baruch?

Viner: No, no, send your own administrative staff.

H.M.Jr: I thought you might mean Mr. Riefler.

Viner: To Paraguay.

H.M.Jr: Paraguay.

Viner: That came up.

H.M.Jr: I got a telegram from Paraguay.

Viner: But we really do think there is not an adequate supply of knowledge in Washington as to the possibilities of using the stamp-book method.

H.M.Jr: Does Graves

Viner: Oh, he welcomed the recommendation. And that was unanimous, wasn't it? We all think that would be well worth doing, be a contribution to the Social Security program.

Hansen: I don't know whether you - pardon me.

H.M.Jr: Doesn't Social Security have that? Has Altmeyer

Brown: For many reasons I feel that for the persons who are on the tax side to actually, you might say, live with for a brief time the persons doing it

Viner: To work with the actual technicians on administrative control, to actually see how the thing is done over there, so when it comes to installing the American system they shall at first hand have seen the operation of the British system.

Hansen: I don't remember - did you bring out the point that this tax collection system is applicable to those that we hope to bring into coverage that are not now under coverage, namely, the agricultural workers in particular and

Viner: Yes, I said domestic servants, agricultural workers, and the employees of very small firms, where there is a single employee or two employees.

H.M.Jr: Agricultural workers, very small firms, and what else?

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Murphy: Domestic servants.

Viner: The point was also made that our experience might conceivably be such with the stamp-book method that we might want to extend it; it might be so successful that we might want to extend it into areas which we now attempt to control through the payroll method.

Brown: That would be in the very small employers.

Viner: Yes, but it would be an arrangement that's already covered by Social Security.

Brown: For example, employers employing three or less - that the advantages found in the case of farm labor and domestics might carry over in the form of taxes on employers of one, two, or three persons.

H.M.Jr: I saw - what's the name of this woman who just got out from the Social Security - in the White House. She says, "You're going to come to the stamp-book method whether you like it or not; might just as well make the best of it." What's her name?

Murphy: Miss Dewson.

H.M.Jr: Miss Dewson.

That's good, I think. Now what else?

Viner: We discussed at some length Mr. Reagh's plan for a reconstruction of the Social Security plan. We found it very interesting, and I think we're all agreed there were points of merit; also, some of us saw difficulties or objections to it. We're not prepared to make any recommendation on it. We think it would be a mistake on our part, without more study of it, to make any recommendation; but we would ask you to authorize or instruct Mr. Reagh to send such members of this group as are willing to spend some time and thought on the matter the material necessary for an appraisal of the plan, and they'll send memoranda to him or to you, as you please.

H.M.Jr: Well, he is instructed now. Which members of the group?

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Viner: Mr. Douglas Brown and Mrs. Burns in particular; I think they're most competent to appraise it, and they have ideas already. They are critical, both of them, but I think they both expressed the opinion that - I think it's a sound opinion - that our discussion was not adequate to justify anybody in coming to very firm conclusions.

H.M.Jr: What about Mr. Riefler?

Viner: Well, Mr. Riefler, I think - if you can - I think he ought to be persuaded. He resisted my request that he also prepare a memorandum on it.

Riefler: I was very much attracted by the plan at first sight, but I really am too busy; I couldn't possibly do it.

Viner: Now the next question is one on which I think we failed to give you a definite answer yesterday, and that is what our recommendation is as to the stepping up of the rates in 1940; and I think with the possible exception of Mr. Hansen we agree on a variety of grounds, different grounds for different persons, that the rates ought to be stepped up in 1940; that we follow the Advisory Council's recommendation that they ought to be stepped up in 1940-41, and that then later there could be reconsideration as to the next step-up.

With respect to Mr. Hansen, I think he ought to state his own position. I suggest you ask him what he would do if he were President of the United States.

H.M.Jr: No, I'll ask him what he would do if he were Secretary of the Treasury.

Hansen: Well, Mr. Secretary, I've stated it so often, I really don't see much point in my stating my position

H.M.Jr: Well, evidently Dr. Viner wants to put you in the Secretary of the Treasury's situation, and you're welcome to it. I'll sell it to you cheap.

Hansen: Why, my position is the same as that of a minority group in the Advisory Council, and the position is

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stated in the report of the Advisory Council as a footnote. It is not very conspicuous, but it is there, at any rate.

The position is simply this: In the first place, the reserve will amount by January 1940 to 1.7 billion. About that there isn't any dispute; everyone agrees to that. We regard that as a thoroughly adequate contingency reserve during at least the early period of the plan, since the benefit payments will be several years, as you can see from this table - very much smaller - very much smaller than that. It will take - it will be 1945 before the benefit payments, even on the basis of the generous maximum estimates, will be as much as a billion dollars a year.

We said in our brief minority report that we thought that taxes of this character, that weigh heavily on consumption, ought not to be collected unless it was really necessary, and made the argument that it wasn't necessary to collect these taxes beginning with 1940-41. We thought that we don't yet know what the - nobody knows what the scale of benefit payments will be, and therefore we phrased it in this manner: We said that when it becomes known what the benefit payments are going to be and it is apparent that the benefit payments will exceed the current tax receipts on the one percent basis, then additional revenue would be necessary; but in our judgment it wouldn't be necessary until then, in view of the fact that there is this what we would regard as an ample contingency reserve of 1.7 billion dollars.

The estimates here of five - over 500 million dollars of benefits in 1940 Mr. Altmeyer says - admits are maximum, and I know that there are a great many other people who have some competence with respect to appraising what that magnitude would probably be - I don't know anything about it, but I think that it's not at all - not at all likely that it will be of that order of magnitude. We have a feeling that so long as we don't know what the benefits are like and the contingency reserve is as large as it is, that we ought not to keep collecting consumption taxes that are not necessary. It doesn't mean

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we are abandoning the general scheme of taxation - I myself would be very much opposed to doing that - but merely in the light of what we know now, to postpone the period when the increase in tax rates should go into effect.

Now, I am quite willing to admit that one has to take cognizance of other considerations than the purely economic, or perhaps I may say the deflationary aspect of these tax collections, and everyone can appraise these other features as they best can. I admit that the other things must be considered.

My own view is that the mere postponement doesn't mean that the contributory system is thereby abandoned or endangered; and others I know have a different view of that matter.

H.M.Jr: You think it's an important decision?

Hansen: Yes, I think it's an important decision both from an economic standpoint and from the standpoint of the future of the system.

H.M.Jr: Well, I'm not going to express my viewpoint because I haven't been in it long enough and I want to think a lot more about it. After I've digested some of this, I want to give Mr. Altmeyer a chance to talk at me. But I appreciate - I mean I know your position and I know, if I may say, the school of thought which you express, huh?

Hansen: Yes.

Viner: I have one more suggestion, and that is this. We've been discussing these things for two days, and your staff has been there and we've been there, and we haven't, of course, put into writing all of the considerations that we gave weight to.

H.M.Jr: No.

Viner: But your people there were participating actively in the discussion and I think it would be a service to the Treasury, if anything that we said was worth anything, if your staff would sort of make a summary of the discussion, giving the important considerations as they remember them - not an elaborate one -

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for the record. Our record is incomplete. We've tried to jot down a few things; our record is incomplete, though. But they should have for their own working record the drift of arguments and considerations on both sides that entered into our recommendations.

H.M.Jr: Well, supposing that Blough and Reagh and Murphy do that - the three of them get together - Monday morning.

Viner: I think if they would send us a copy of those, we might - if we comment on them as to whether we think they really represent the gist of the discussion, I think in that way much more can be saved out of the conferences than if you just left it to memory.

H.M.Jr: If Reagh, Murphy, and Blough will do - stay at that until it gets done.

Viner: One other thing. We don't think we should leave, if we possibly can stay, until we have given some consideration to the question which you referred to us yesterday, as to the possibility of basing public assistance to the various states on the fiscal capacities of states. We haven't touched that yet, but we're prepared to stay on for another meeting and perhaps leave an oral memory with your staff as to what we think about it. We haven't yet said a word about it.

H.M.Jr: Well, I think it's important, because they're laying the foundation for something which may apply to all Federal aid. I mean it's this whole question of Pat Harrison on his education bill, for instance, and if this goes through, why, Mississippi just would be the ideal state to receive this sort of thing, you know.

Blough: The best.

H.M.Jr: What?

Blough: The best.

H.M.Jr: The best, huh?

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Viner: No, I think, as Mrs. Burns has pointed out, we couldn't do very much in an hour, but I - we might be able to make some suggestions as to how the problem might be approached and studied. It's a big problem, of course; there's a big literature and it requires in part types of ability and knowledge which are not, I think, particularly represented by the group you have here. It requires a sort of public finance and local finance type of knowledge.

H.M.Jr: Well, maybe

Viner: I mean the group you have here, the group of visitors; I'm not referring to your own staff.

H.M.Jr: Then you might suggest

Viner: Persons who....

H.M.Jr: ... persons who

Viner: ... who have dealt with the problem. It's a problem, of course, of Federal relationships, Federal financial relationships.

H.M.Jr: And do you want to take just a minute and give Naster the names of people we might have in on South America?

Viner: Well, I gave them to Mr. White. I wonder if that will do.

H.M.Jr: That will do perfectly; that will do fine.

Well now, supposing we get this - we get this in writing, get it written up, and get you copies. Reagh will put his plan down and send you each a copy of it, and when you get home you can decide whether you do want or do not want to comment on that. Isn't that the best way?

Viner: Yes, that's right.

H.M.Jr: Riefler may be just so interested he won't be able to tear himself away from it; never can tell.

Viner: Tear himself away from Paraguay.

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H.M.Jr: Then we'll see how we get along. The thought I had was that just as soon as Social Security says, "Well, this is the plan we think we want," I think we ought to take a table like that and say, "Here, you give it out, or we'll give it out, and let the public know." I mean just say, "Whatever your plan is, you tell us what your plan is. All right. Either you'll do it or we'll do it; but one or the other will have to give it out so the public will know this is what it costs."

Murphy: There is a difference, Mr. Secretary, in us giving it out, because the estimates are all theirs, and if we're giving it out we'll take responsibility for it.

Viner: They would give it out.

H.M.Jr: All I want is to get it in the hands of the public, that's all. I think it ought to come from them, but if they won't, I think this

Hansen: I think that's very important, that that sort of thing be given out.

H.M.Jr: Because - well, I think - I mean I got the feeling that nobody - maybe you did - all of you visualize the way it is there, but I certainly didn't.

Hansen: No, I didn't.

H.M.Jr: Don't you think it ought to be given out?

Hansen: Yes.

H.M.Jr: Well, I certainly appreciate very much the help; most likely will call on you again for some more assistance.

When are you leaving, Viner?

Viner: 5 o'clock - 5:45.

H.M.Jr: Well, thank you.

TREASURY DEPARTMENT

16

INTER OFFICE COMMUNICATION

DATE Jan. 30, 1939.

TO Secretary Morgenthau
FROM Mr. Haas 

Attached is a summary of the discussion and recommendations of the group of economists called to advise you on proposed Social Security legislation, January 20 and 21, 1939. The summary has been prepared by Messrs. Murphy, Reagh, and Blough.

Summary of the Discussion and Recommendations
of the Group of Economists Called to Advise
the Secretary of the Treasury
on Proposed Social Security
Legislation, January 20
and 21, 1939.

The group of economists invited to advise the Secretary on proposed social security legislation consisted of Mrs. Eveline Burns of Columbia University and Messrs. J. Douglas Brown of Princeton University, Alvin H. Hansen of Harvard University, Winfield Riefler of the Institution for Advanced Studies, and Jacob Viner of the University of Chicago. The group met with the Secretary and members of the Treasury staff on Friday morning, Friday evening, and Saturday afternoon, and with members of the Treasury staff on Friday afternoon and all day Saturday. All members of the group were present at all meetings with the exception of Mr. Riefler, who did not attend the discussions on Friday morning and Friday afternoon.

The discussion and conclusions of the group may be summarized as follows:

1. Deficiency in Reserve under Present Law.

The group recommended, subject to the approval of counsel, that the Secretary submit no estimate at the present time for a supplemental appropriation on account of the deficiency in the Old-Age Reserve Account shown in the actuarial valuation of the Account incorporated in the Annual Report.

The actuarial valuation of the Old-Age Reserve Account, incorporated in the Annual Report of the Secretary of the Treasury as required by law^{1/}, shows a deficit in the Account of a little over \$9 billions. This \$9 billions is the amount by which the present value (all figures as of June 30, 1938) of expected Title II benefit payments, discounted at 3 percent, exceeds the assets of the Account plus the present value of all expected Title VIII tax collections less administrative expenses, discounted at the same rate.

The Social Security Act provides "... There is hereby authorized to be appropriated to the Account for each fiscal year ... an amount sufficient as an

1/ Social Security Act, Title II, Section 201(f).

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annual premium to provide for the payments required under this Title (II), such amount to be determined on a reserve basis in accordance with accepted actuarial principles ... The Secretary of the Treasury shall submit annually to the Bureau of the Budget an estimate of the appropriations to be made to the Account."^{1/} In order to comply with this provision of law, it would be necessary, upon the basis of the current actuarial valuation to appropriate annually to the Account an amount equal to 3 percent of the deficit, or about \$270 millions a year in addition to all Title VIII tax collections, less administrative expenses.^{2/} Such an appropriation would never amortize the deficit, but would have to be made annually in perpetuity in order to hold the amount of the deficit constant.

The actuarial valuation of the Account was not completed until December and was not finally approved for inclusion in the Annual Report until the first week in January. In the meantime, the Treasury Department had submitted to the Bureau of the Budget, as the required estimate of the appropriation to the Account for the fiscal year 1940, an amount equal only to estimated Title VIII tax collections, less administrative expenses. This requested appropriation, which is that appearing in the Budget, is short between \$200 and \$300 millions of that required under Title II upon the face of the actuarial valuation of the Account included in the Annual Report.

The question is: "Should the Secretary submit a supplemental estimate for an appropriation equal to the amount of the deficiency?" The answer of the group is "No," subject, of course, to the approval of counsel.

Two considerations weighed heavily in this decision: First, the Social Security Act is expected to be drastically revised this spring, and it is

^{1/} Social Security Act, Title II, Section 201(a).
^{2/} There are other ways in which the amount of the required appropriation might be computed, but they may be neglected here. In any event, the amount of the required additional appropriation would be well over \$200 millions a year.

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probable that provision for an annual appropriation analogous to that now called for under Title II will be omitted completely in the revision. To ask for an additional appropriation at this time, upon the basis of the deficiency in the Account shown by the actuarial valuation, would serve no useful purpose and would merely confuse the issue during the discussion of the proposed revisions.

Second, the estimate was submitted to the Bureau of the Budget long before the actuarial valuation of the Account was completed. The valuation, in fact, was finally approved only two days before the publication of the Budget. The estimate submitted and incorporated in the Budget is correct upon the basis of last year's valuation of the Account, which shows it to be self-supporting upon the basis of the assumptions then used. The new valuation is based upon additional data which did not become fully available until late in the fall. In view of the time required for the actuarial valuation of the Account, it would seem a reasonable position that last year's valuation should be made the basis for this year's appropriation. Upon this basis no supplemental appropriation would be required at the present time.

2. The Full Reserve Method of Financing.

The group was opposed to the continuance of the full reserve method of financing.

If a program of old-age benefits is supported exclusively by the proceeds of earmarked tax collections, the full reserve plan of financing requires that the excess of tax collections over benefit payments during the early years of the system should be enough to build up a reserve, the interest upon which will be sufficient in the later years of the system to meet the expected excess of benefit payments over tax receipts. This is the theory of the present law. If the reserve is invested in Government bonds, the interest earnings will, of course, be paid by the Government itself, but will represent no burden to the Government additional to that which would have been incurred anyway, provided that the proceeds derived from the sale of securities to the Account have been used to retire other Government debt, or to prevent increases in this debt which would otherwise have taken place.

If this principle is to be maintained in the face of a substantial increase in benefit payments, plus a sizable deficiency in the Account as valued upon the basis of the present scale of benefit payments, Title VIII tax rates would have to be increased very materially, or some other earmarked tax levied in substantial amount. The increase in revenues required would be -- upon the basis of Social Security Board estimates -- of the order of magnitude of the yield of a 2 percent payroll tax (combined employer and employee shares) commenced immediately, in addition to the rates of taxation already provided for by Title VIII. The group considered such an increase in payroll taxes, or the levy of other earmarked taxes sufficient to maintain the full reserve plan, as unwise.

The full reserve plan could also be maintained by a continuing annual appropriation from general funds without any especially earmarked revenues. The appropriation so required, assuming full coverage, would be -- again upon the basis of Social Security Board estimates -- of the order of magnitude of a billion dollars a year in addition to Title VIII tax collections.

The effect of such a plan would be to give full accounting recognition to the annually accruing liability under the old-age insurance system, even though no financial provision might be made for it. If no such provision were made, it would mean that the Federal budget, even when balanced in all other respects, would show a formal annual deficit equal to the amount of the required appropriation. To achieve a formal balance would require that about a billion dollars a year in additional revenues be provided without any corresponding cash expenditures except for debt reduction.

The group, partly in consideration of the likely economic effects of such an excess of cash receipts over cash expenditures, did not consider this method of maintaining the full reserve plan practical or desirable; and, therefore, recommended that such plan, based either upon earmarked taxes or upon appropriations from general revenues be abandoned. Mr. Riefler was not present when this decision was made and may not concur in it.

3. Effect of Social Security Financing on the General Economy.

The group was divided in its opinion concerning the effect of social security financing upon the general economy.

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Mr. Hansen was strongly impressed with the necessity of avoiding any further encouragement of saving when the amount of saving already being attempted exceeds the amount of profitable investment outlets in the economy, and is likely to do so for sometime to come. This excess of attempted savings over available investments he considers a major cause of the present depression. He, consequently, considered it unwise that collections on account of social security taxes should ever run far ahead of payments on account of social security benefits, i.e., that any reserve should be accumulated. He recognized that the logical conclusion of this argument is a pay-as-you-go system, and consequently assented only with grave reservation to the conclusion of the group with respect to the contingency reserve as stated under (5) below.

Mr. Riefler took the opposite position. While he granted that over the short-run attempted savings might exceed available investment opportunities and that this might be a contributory cause of the depression, he believed that over the long-run undersaving is likely to be a more serious problem than oversaving. He was particularly concerned with the reduction in the amount of saving by persons in the lower income brackets which would likely be caused by the provision of old-age security through social action. The logical conclusion of this line of thought, taken by itself, is the full reserve method of financing; although, of course, this conclusion might be avoided by the force of other considerations. As previously noted, Mr. Riefler was not present at the meeting when the remaining members of the group opposed the full reserve plan.

Mr. Viner occupied an intermediate position, concurring, however, more with Mr. Hansen's views than with those of Mr. Riefler concerning the present and prospective position of saving and investment in the economic system. Mr. Viner set forth his own views on this matter in the following statement:

"The net effect of the social security program on the volume of national saving is an important consideration. What that effect is likely to be under alternative financing methods is not clear without further analysis than has yet been made. It seems desirable, however, that

each particular phase of governmental activity be handled autonomously with reference to its own internal needs and conveniences, and that the question of fiscal management be treated as an over-all problem, handled by the fiscal authorities. These fiscal authorities should think of their problem as involving not only compensatory action for undesired trends in non-governmental economic activity, but also compensatory action for undesired net trends in the combined fiscal results of the separate governmental agencies. If as the result of the social security program and other governmental and non-governmental activities, it should be decided that the volume of national decisions to save is excessive or deficient, the fiscal authorities should endeavor to compensate for it by balancing operations of their own, such as, for instance, deficit financing or debt liquidation."

Mrs. Burns and Mr. Brown appeared to subscribe to the middle school of thought upon this question, but were more interested in the social insurance than in the general economic aspects of the discussion. In their opinion, an effective policy of social insurance requires reasonably regular and predictable schedules of benefit payments and tax rates, and would be seriously jeopardized if these were made pliable instruments of fiscal and monetary policy, as proposed by Mr. Hansen.

4. Annual Statement of the Actuarial Status of the Contributory Old-Age Security Program.

The group recommended that the Secretary should present annually a memorandum showing forecasts of the cost of benefit payments under the then existing law for decennial years, 50 years in advance, as a ratio of covered payrolls, on the assumption of existing wage rates. The group further recommended that capitalized figures of future benefit payments and of future tax collections should no longer be presented.

The memorandum so recommended by the group is intended to take the place of the present annual actuarial valuation of the Old-Age Reserve Account. This valuation is in the form of a balance sheet in which the securities and cash held in the Account, plus the discounted value of future Title VIII tax collections, less

administrative expenses, are set up as assets, and the discounted value of future Title II benefit payments is set up as a liability. While existing law does not prescribe the form of the annual actuarial valuation which it requires, the present form, or one like it, seems necessary to carry out the intent of the law, particularly in determining the amount of the annual appropriation necessary to maintain the full reserve system. If the full reserve system should be abandoned, however, the present form of valuation would no longer be necessary, and the group believed that a memorandum in the form suggested would be more useful as a means of setting forth the status of the program to Congress and to the public than would a statement of capitalized future benefit payments and tax collections.

5. Contingency Fund.

The group recommended that a contingency fund be provided in the new law in lieu of the present full actuarial reserve, and that the amount of this fund should be approximately 3 years' benefit payments during the critical years of the plan (1940-45) and approximately 2 years' benefit payments when the plan is mature. During the years when benefit payments are rapidly growing, the amount of the fund should be related, not to the amount of the then current year's benefit payments, but to the amount of benefit payments forecast for the next 3 years, assuming normal business conditions.

Strictly interpreted, this resolution, combined with accurate forecasts of tax collections and benefit payments, would fix a policy with respect to future tax rates. The margin of error of the estimates is so large as to leave considerable room for dispute concerning tax-rate policy, even if this interpretation of the resolution should be accepted. A number of members of the group, however, appeared to believe that, even if accurate estimates were available, tax rates should not be fixed with sole reference to their effect upon the amount of the contingency fund.

Mr. Hansen, while not specifically objecting to the resolution, considered the proposed amount of the contingency fund high.

6. Tax Rate Policy.

All members of the group except Mr. Hansen were in favor of going ahead with the scheduled increase in Title VIII taxes from 1 $\frac{1}{2}$ -1 $\frac{1}{2}$ to 1 $\frac{1}{2}$ -1 $\frac{1}{2}$ on January 1, 1940. One of the most important

of the reasons for this decision, a reason which was particularly stressed by Mr. Brown, was the unfortunate psychological effect of both increasing benefit payments and reducing tax rates in the first important change made in the old-age insurance system since its enactment. Mr. Brown emphasized that the effect of such a change would be to minimize the contributory character of the system in the minds of prospective recipients of benefits and so stimulate the demand for further changes in the same direction.

Mr. Hansen believed that the 1%-1% rate should be maintained until an increase is necessary to take care of current benefit payments.

With the possible exception of Mr. Riefler, the remainder of the group appeared to be sympathetic to the proposal of the Advisory Council that the entire question of future increases in tax rates be studied during the period of the 1%-1% rate (1940-42) in the light of the data which will then be available.

7. Extension of Coverage.

The group was unanimously of the opinion that coverage under the contributory plan ought to be extended, and was inclined to minimize the difficulties of doing this.

Mr. Graves presented the viewpoint of the Bureau of Internal Revenue with respect to the administrative difficulties of extending the coverage. He believed these difficulties to be extremely serious. He stated that about 35 percent by number of present Title VIII taxpayers are habitually delinquent. About five-sevenths of these, that is about 25 percent of the whole number, ultimately file late returns or are reached by correspondence. The remainder -- about 10 percent of the whole number of taxpayers -- have to be reached by field investigation, and the cost of such investigation is a very large proportion of the total cost of enforcing collection of the taxes, although the amounts of tax involved are small. Many of the small employers who fall into this class are illiterate or quasi-illiterate, and are accustomed to pay taxes only when a tax collector catches up with them and fills out the form for them.

An extension of coverage to include domestic servants and agricultural workers would bring in a large number of additional employers of the type who are now causing the major portion of difficulties in collection. The amounts due from each employer

would be trifling, and the administrative difficulties of collection appalling. Mr. Graves thought it not unlikely that the cost of collection might exceed the amount collected from these classes of employers if real enforcement were undertaken. He stated that costs could, of course, be kept down if the group would be content with, perhaps, a 65 per cent enforcement for these classes, which would in effect put the system upon a quasi-voluntary basis with respect to domestic servants and agricultural workers. He did not believe that the stampbook method of collection would solve the difficulties which he envisaged.

Mr. Brown, who had made a personal investigation of the stampbook method of collection in England, was inclined to discount Mr. Graves' skepticism. While he granted that there might be many difficulties in the early years, he believed that such a method of collection could ultimately be put upon a smoothly running basis in this country also as people became accustomed to it. He thought that the chance of successfully installing and enforcing such a system would be very substantially increased by the proposed changes in benefit payments, and particularly by the institution of benefits for survivors of persons dying before reaching retirement age.

In view of the conflict of expert opinion, the group recommended that the Treasury Department send a group of qualified persons from its staff to study the operation of the stampbook method of collection of social insurance contributions in England and other representative European countries.

8. Reagh Plan.

The group discussed at some length the plan for old-age security presented by Mr. Reagh, and designed as a substitute for the present system. A summary of this plan is appended hereto. The group asked that the Secretary instruct Mr. Reagh to provide them with copies of this plan and certain additional data, in order that they might continue their study of it, and Mrs. Burns and Mr. Brown undertook to prepare criticisms of it.

9. Variable Grants to the States for Public Assistance Purposes.

The group recommended that the Treasury take the initiative in securing the formation of an interdepartmental committee on fiscal relations between the Federal Government and

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the States; that this committee take as its first subject of consideration the question of variable grants to the States; and that as a preliminary to such consideration this committee arrange for a collation and analysis of the many studies and collections of data bearing on this problem which have already been made by Federal and other agencies.

The group believed that three factors should be taken into consideration in any program for variable grants to States for public assistance purposes. These factors are the variations between States with respect to (1) fiscal capacity, (2) living costs, and (3) living standards. The group saw both advantages and disadvantages in a program of variable grants and did not desire to take a position with respect to the over-all desirability of such a program without further study.

REAGH PLAN

(Copy)

27

November 4, 1938.

To: Mr. Haas

From: Mr. Reagh

Subject: Some general conclusions regarding old-age insurance and a proposed plan designed to remedy some of the defects in the existing law.

1. Any system of old-age insurance providing annuity benefits as a matter of right (no means test) which does not apply to substantially the entire population should be supported by special social security taxes levied only against those covered by the benefit provisions. Federal subsidies with limited coverage mean inequitable taxation of those excluded from the benefit provisions of the plan.

2. A self-supporting system of payroll taxes applied to a limited group cannot possibly be levied on the "current cost" or progressively increasing rate basis because the rate would ultimately be so high that all new entrants would be required to pay several times as much for their annuities as they would have to pay an insurance company for the same benefit. This same principle caused the breakdown of the old fraternal (step-rate) insurance organizations. The number of individuals who would be required to pay exorbitant tax contributions would ultimately be so large that they would probably vote the system out of existence at the expense of the then aged.

3. From (1) and (2) it follows that an equitable system of old-age insurance with limited coverage requires earmarked taxes at rates far in excess of immediate cash needs and therefore large reserves. The practical necessity of collecting tax revenues far in excess of immediate cash needs, and of therefore accumulating large reserves, would be eliminated, however, if the coverage of the system were made substantially universal.

4. Universal coverage would remove the inequity of a substantial Federal subsidy. However, if benefits are to be paid largely from Federal subsidies, as a matter of right, to those retired in the early years, there seems to be no possible justification for excluding those who are already

past the age of 65 and unemployed. Can there be any justification for providing individuals who will reach 65 within the next 5 or 10 years with deferred annuities, the major part of which will be paid out of general tax revenue, and at the same time denying all annuity rights (except on a means test) to the present aged?

5. Any system which offers powerful incentives for overpayment or underpayment of taxes will be extremely difficult if not impossible to police and this would be especially true as applied to the self-employed and to those who receive an important portion of their earnings in the form of board, lodging, tips, etc. Such incentives are embodied in the existing law and to an even greater degree under AC-13 now under consideration by the Social Security Advisory Council. Any system which provides free benefits in proportion to earnings or which requires taxes greatly in excess of the value of the corresponding benefits is open to sharp practice and fraud at the expense of the general taxpayer.

6. It would be exceedingly difficult, if not impossible, to enforce the collection of payroll taxes from the employers of domestic servants, farm laborers, and casual laborers.

7. The above considerations lead to the conclusion that a satisfactory solution to the old-age insurance problem requires a radical change from the existing law. The longer such changes are deferred, the more difficult it will become to effect them, because the public will acquire an increasing feeling of vested rights in the benefits of the present law.

Many of those who are studying the old-age insurance problem appear to believe that there is no practicable solution to the difficulties outlined above because of administrative and political considerations. Perhaps a perfect solution could never be found, but it appears likely that a relatively simple plan could be devised which would remedy many of the defects in the existing law and at least partially solve many of the administrative problems involved in universal coverage. Attached hereto is a tentative outline of a plan which seems to be capable of universal coverage and which would greatly reduce many of the administrative difficulties embodied in the existing law and the proposed AC-13.

The plan outlined in the following pages retains as many of the principles of the existing law as seem possible - that is, it is a contributory plan under which benefits bear a definite relationship to earnings. If this principle could be discarded the obvious solution to most of the problems would be a flat benefit scheme having no relation to earnings, and financed with general rather than specifically earmarked social security taxes. Many students of social security believe that a flat benefit would lack much of the appeal of a contributory plan under which the beneficiaries are made to feel that they are somehow paying for their annuity as they pay for life insurance. Another objection often made against the flat benefit scheme is that while the benefit may be adequate in certain areas where the cost of living is relatively low, the same benefit would be far from adequate in other areas. The various proposals which have been seriously considered by the Social Security Advisory Council have been of the contributory type with benefits geared to earnings.

Preliminary outline of an old-age insurance plan designed to eliminate incentives for either overpayment or underpayment of tax and which would be administratively feasible with universal coverage.

A. Old-age Retirement Benefits.

1. Old-age annuity. Every individual who has reached the age of 65 and is not regularly employed shall be eligible for an "old-age annuity," computed on an annual basis as follows:

- (a) \$108 plus 90 percent of average annual income 1/ in excess of \$120 and not in excess of \$200; plus

1/ Average annual income is equal to the aggregate amount of income limited to \$200 in any tax year - as shown by the individual's social security tax return - divided by the number of years that the individual was subject to the Act. For this purpose each individual will be considered as subject to the Act during the period beginning on January 1st of the year immediately following the tax year for which he filed his first social security tax return and ending with December 31st of the year immediately preceding the year in which he is retired; provided, however, that years prior to the year in which the individual attained the age of 25 will be excluded from the calculations. In order that periods of unemployment will not cause too severe a reduction in the annuity, it might be further provided that one year out of each ten-year period, or fraction thereof, could be excluded from the calculations.

(b) 1.00 percent of taxable income	2/ reported prior to age 25; plus	
.85 percent of taxable income	reported between ages 25-30; plus	
.70 " " " "	" " " "	30-35; "
.55 " " " "	" " " "	35-40; "
.45 " " " "	" " " "	40-45; "
.35 " " " "	" " " "	45-50; "
.30 " " " "	" " " "	50-55; "
.25 " " " "	" " " "	55-60; "
.20 " " " "	" " " "	at age 60 and over.

Part (a) of the benefit formula provides minimum annuities of \$9 per month to all individuals above the age of 65 who are not regularly employed, including the present aged.

2. Allowance for widows. Married women will be given credit for one half of the combined earnings of husband and wife. The system thus provides automatically for widows benefits without complicated survivorship annuities.

B. Disability Benefits.

Disability benefits may be incorporated into the plan if found desirable. However, it is suggested that such benefits should be postponed until other important changes have been made and the system is operating smoothly. When and if such benefits are provided, the tax rates should be adjusted to cover the additional cost.

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- 2/ Taxable income for any tax year shall not exceed \$3,000 for a single individual or \$6,000 for a married couple. The amount of such taxable income shall include first all wages and salaries from regular employment (up to the limit specified). Taxable income up to the limit specified as a total shall also include all other income (except investment income) in excess of \$120 (\$240 for a married couple), such as commissions, wages received from irregular employment, or net income derived from a business enterprise. In the case of married couples the income credit (for annuity purposes) is divided equally between the husband and wife. It is suggested that employees who receive wages in kind might, at their option, report a reasonable amount of income in respect to such allowances and that employees who receive compensation in the form of tips should report such income as wages. As a further suggestion the tax form might contain a printed schedule showing fairly broad brackets of net business income and the corresponding amount of the tax. The taxpayer would be permitted to estimate his net business income within these broad brackets. (This definition of taxable income is merely suggestive; the important point to be made is that regardless of how taxable income is defined or reported, the system would be sound from a cost standpoint.)

C. Death Benefits - Widows and Orphans Benefits.

The 2-percent tax rate provides, in addition to the annuity benefits under (b), a death benefit equal to $2\frac{1}{2}$ percent of aggregate taxable earnings. The scale may be adjusted so that a 2-percent tax rate will provide additional benefits for widows with minor children.

D. Taxes.

There will be no payroll taxes levied against employers. Employees will pay an individual income tax of 2 percent on taxable income as defined in the footnote on the preceding page.

The following tables compare the annuities payable under the existing law with the proposed plan AC-13 and the alternative proposal described above.

Annuities to Married Couples 1/

Average monthly taxable earnings: 2/	3 years' coverage 3/				5 years' coverage				10 years' coverage				15 years' coverage			
	Existing law	AC-13	Proposed 4/		Existing law	AC-13	Proposed 4/		Existing law	AC-13	Proposed 4/		Existing law	AC-13	Proposed 4/	
\$10	-	\$ -	\$18.06	\$ -	\$ -	\$ -	\$18.10	\$ -	\$ -	\$ -	\$18.22	\$ -	\$ -	\$ -	\$18.38	
15	-	-	18.09	-	-	-	18.15	-	-	-	18.34	13.50	20.25	18.56		
20	-	-	18.12	-	-	-	18.20	12.00	18.00	18.45	15.50	23.25	18.75			
30	-	-	27.18	-	-	-	27.30	15.50	23.25	27.68	17.00	25.50	28.12			
50	-	-	30.30	15.00	22.50	30.50	17.50	26.25	31.12	20.00	30.00	31.88				
75	-	20.25	30.45	16.25	24.38	30.75	20.00	30.00	31.69	23.75	35.62	32.81				
100	-	23.25	30.60	17.50	26.25	31.00	22.50	33.75	32.25	27.50	39.38	33.75				
150	-	25.50	30.90	20.00	30.00	31.50	27.50	39.38	33.38	35.00	45.00	35.62				
200	-	27.75	31.20	22.50	33.75	32.00	32.50	43.12	34.50	42.50	50.62	37.50				
250	-	30.00	31.50	25.00	37.50	32.50	37.50	46.88	35.62	50.00	56.25	39.38				
300	-	30.00	31.80	25.00	37.50	33.00	37.50	46.88	36.75	50.00	56.25	41.25				
400	-	30.00	32.40	25.00	37.50	34.00	37.50	46.88	39.00	50.00	56.25	45.00				
500	-	30.00	33.00	25.00	37.50	35.00	37.50	46.88	41.25	50.00	56.25	48.75				

Average monthly taxable earnings: 2/	25 years' coverage				35 years' coverage				45 years' coverage			
	Existing law	AC-13	Proposed 4/		Existing law	AC-13	Proposed 4/		Existing law	AC-13	Proposed 4/	
\$10	\$15.00	\$22.50	\$18.78	\$16.00	\$24.00	\$19.40	\$17.00	\$25.50	\$20.32			
15	16.25	24.38	19.16	17.75	26.62	20.10	19.25	28.88	21.49			
20	17.50	26.25	19.55	19.50	29.25	20.80	21.50	32.25	22.65			
30	20.00	30.00	29.32	23.00	34.50	31.20	26.00	38.25	33.98			
50	25.00	37.50	33.88	30.00	41.25	37.00	35.00	45.00	41.62			
75	31.25	42.18	35.81	38.75	47.82	40.50	46.25	53.43	47.44			
100	37.50	46.88	37.75	47.50	54.38	44.00	53.75	59.07	53.25			
150	50.00	56.25	41.62	57.50	61.88	51.00	55.00	67.50	64.88			
200	56.25	60.93	45.50	66.25	68.43	58.00	76.25	75.00	76.50			
250	62.50	65.62	49.38	75.00	75.00	65.00	85.00	75.00	88.12			
300	62.50	65.62	53.25	75.00	75.00	72.00	85.00	75.00	99.75			
400	62.50	65.62	61.00	75.00	75.00	86.00	85.00	75.00	123.00			
500	62.50	65.62	68.75	75.00	75.00	100.00	85.00	75.00	146.25			

* not qualified for annuity.

See page 8 for footnotes.

Annuities to Single Individuals

Average monthly taxable earnings: 2/	3 years' coverage 3/			5 years' coverage			10 years' coverage			15 years' coverage		
	Existing ¹	AC-13	Proposed ⁴	Existing ¹	AC-13	Proposed ⁴	Existing ¹	AC-13	Proposed ⁴	Existing ¹	AC-13	Proposed ⁴
	law		4/	law		4/	law		4/	law		4/
\$10	*	\$	\$ 9.06	\$	\$	\$ 9.10	\$	\$	\$ 9.22	\$	\$	\$ 9.38
15	*	*	13.99	*	*	13.65	*	*	13.84	13.50	13.50	14.06
20	*	*	15.12	*	*	15.20	12.00	12.00	15.45	15.50	15.50	15.75
30	*	*	15.18	*	*	15.30	15.50	15.50	15.68	17.00	17.00	16.12
50	*	*	15.30	15.00	15.00	15.50	17.50	17.50	16.12	20.00	20.00	16.88
75	*	13.50	15.45	16.25	16.25	15.75	20.00	20.00	16.69	23.75	23.75	17.81
100	*	15.50	15.60	17.50	17.50	16.00	22.50	22.50	17.25	27.50	26.25	18.75
150	*	17.00	15.90	20.00	20.00	16.50	27.50	26.25	18.38	35.00	30.00	20.62
200	*	18.50	16.20	22.50	22.50	17.00	32.50	28.75	19.50	42.50	33.75	22.50
250	*	20.00	16.50	25.00	25.00	17.50	37.50	31.25	20.62	50.00	37.50	24.98

Average monthly taxable earnings: 2/	25 years' coverage			35 years' coverage			45 years' coverage		
	Existing ¹	AC-13	Proposed ⁴	Existing ¹	AC-13	Proposed ⁴	Existing ¹	AC-13	Proposed ⁴
	law		4/	law		4/	law		4/
\$10	\$15.00	\$15.00	\$ 9.78	\$16.00	\$16.00	\$10.40	\$17.00	\$17.00	\$11.32
15	16.25	16.25	14.66	17.75	17.75	15.60	19.25	19.25	16.99
20	17.50	17.50	16.55	19.50	19.50	17.80	21.50	21.50	19.65
30	20.00	20.00	17.32	23.00	23.00	19.20	26.00	25.50	21.98
50	25.00	25.00	18.88	30.00	27.50	22.00	35.00	30.00	26.62
75	31.25	28.12	20.81	38.75	31.88	25.50	46.25	35.62	32.44
100	37.50	31.25	22.75	47.50	36.25	29.00	53.75	39.38	38.25
150	50.00	37.50	26.62	57.50	41.25	36.00	65.00	45.00	49.88
200	56.25	40.62	30.50	66.25	45.62	43.00	76.25	50.62	61.50
250	62.50	43.75	34.38	75.00	50.00	50.00	85.00	56.25	73.12

* Not qualified for annuity.
See page 8 for footnotes.

Footnotes:

- 1/ Annuities under the existing law are based on the assumption that the indicated earnings are credited entirely to one member of the married couple. Annuities under AC-13 are equal to 150 percent of the annuities determined by the indicated earnings, if credited entirely to one individual. Annuities under the proposed plan are based on the assumption that one half of total earnings is credited to each member of the couple. The illustrations in these tables do not take into account earnings in excess of \$3,000 per year, except in the case of married couples under the proposed plan.
- 2/ The schedules apply only to individuals having no income other than wages derived from regular employment, no part of which is exempt from tax.
- 3/ Applicable to benefits first payable in 1940.
- 4/ Annuities under this plan are computed on the assumption that the entry age is equal to 65 minus the period of coverage.

General Reasoning Behind Benefit Formula

In sharp contrast to the existing law, the proposed plan provides for universal coverage. It would include the self-employed, and even the unemployed, as well as wage earners, salaried workers, and housewives. It would also include the present aged.

The system would be virtually self-policing. No substantial incentive is provided for either underpayment or overpayment of taxes. Those who never paid a tax, including the present unemployed aged, would receive a minimum benefit of \$9 a month. Those with taxable incomes who fail to file returns would be automatically penalized through a reduction in the value of their benefit payments greater than the amount of tax avoidance. It is probably true that those who file returns at all are apt to use considerable care in reporting. Only those who have a taxable income of less than \$200 are offered any incentive for over-reporting their earnings.

An important characteristic of the proposed benefit formula, and one of its chief advantages over that of the existing law, is its automatic provision for wives, widows, and divorcees.

The proposed plan, if adopted, would in effect provide for a \$9 monthly old-age benefit payment as a matter of right (without a means test) to all unemployed persons now aged 65 or more. Title I of the Social Security Act now provides that the Federal Government match dollar for dollar all payments made by State and local governments for old-age assistance, subject to the means test, up to a total amount of \$30 per month per recipient. If the present proposal were adopted, the pension provided as a right under the proposed plan (a minimum of \$9 per month) could be substituted dollar for dollar for the Federal share of any grant-in-aid under Title I. This would mean that the maximum Federal grant per individual recipient under Title I would be reduced from \$15 to \$6 and would only be applied to matching State and local contributions in excess of an amount equal to the pension received as a right from the Federal Government. When this amounted to \$15 a month or more, no payment would be made with respect to such recipient under Title I. It will readily be seen that Federal grants-in-aid under Title I of the Act would rapidly be reduced to negligible proportions.

RE SOCIAL SECURITY RECOMMENDATIONS

January 30, 1939.
4:00 p.m.

Present: Mr. Gaston
Mr. Bell
Mr. Haas
Mr. Reagh
Mr. Blough
Mr. Altmeyer
Mr. J. Douglas Brown

Altmeyer: On this matter of costs, we figured that probably the safest thing to do if we are asked to give estimates, and we undoubtedly will be, is to give what we consider reasonable minimum and reasonable maximum estimates, so that there is a range, so they can't pin on a specious accuracy to long range estimates. And so our people are proceeding to calculate costs on that basis.

Gaston: Yes.

Altmeyer: So I'm sure if we do it on that basis, we'll all of us be in agreement as to range, because we'll make the range wide enough so there won't be disagreement. And that seems to be the only way to do it, because there are so many assumptions that have to be made that are in the nature of things incapable of definite determination.

H.M.Jr: Well, what's your thought as to - what would you like the Treasury to do now? I mean is it clear in your mind?

Altmeyer: Yes.

H.M.Jr: Will you tell me?

Altmeyer: There are a number of questions on the financing that we would very much like to have the Treasury decide as to what position it will take. And secondly, we'd like to know how far, if at all, the Treasury wants us to go in making any estimates of costs or making any statements relative to financing. Now, if - see, we don't want to get over into your

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H.M.Jr: No, I don't - I think we ought to decide which agency is going to do it, then have one agency do it. But if, for example, we were going to do it, we'd want to submit all of our costs to you people, have your people check them - I mean if you ask us to do it. But I simply feel our approach is any way to make it easiest for you.

Now, as to these various - we had a two-day session here last week and out of that they drew up three tables here showing, using A.C. 14 as a basis - then we submitted to your people - what this would mean over - from now until 1980. If you mean by financing plan - do you want us to take a position whether the tax should increase or not? Is that it: whether it should go up?

Altmeyer: (Nods yes)

H.M.Jr: Should we take a position on the reserve?

Altmeyer: Yes.

H.M.Jr: Huh?

Altmeyer: Yes.

H.M.Jr: And what else is there?

Altmeyer: Financing out of other than payroll taxes.

Bell: General fund.

H.M.Jr: General fund. Well, I'm not ready to take a position yet, because I don't think - as far as I know, I don't think that the Treasury has jelled on that. And we had these people down and we listened. The only thing that the President's ever discussed with me, and I don't know whether he has with you, is this question of increasing the tax in '40, and he said he wants it. I don't know - has he said anything to you on it?

Altmeyer: No.

H.M.Jr: Well, he's told me that he wants it.

Altmeyer: Fine.

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H.M.Jr: Because, he said, he felt that if we didn't get it now we might never get it. I've felt that as I got into this thing - I think we could simplify it sufficiently - because its repercussions are so terrific financially, that we might get these things down one, two, three, then say, "Won't you give us an afternoon or an evening?" because I would want him to be acquainted and I'd like to get his advice on the thing, because I don't know anything financially which is before the house, so to speak, which is as important.

And we might say, "Well, we don't think that we should increase the tax." I mean certain people around town think it's deflationary, so forth and so on - and building up this reserve, and all that. And I think we could put it down fairly simply. Then if he'd give us an afternoon or evening - maybe he has with you; he never has with us - and we'll simply present the thing and discuss it before him. That's what I'd like to do.

Now, after all, he's leaving on the - what is it, February 14?

Bell: I don't know the date; around the middle of the month, I understand.

H.M.Jr: I think we could get that ready, make up our own minds where we're at, find out what you have, find out what Professor Brown would advise us on that. What I've asked him to do is to see me personally through this thing for the next two or three months, and if he can get permission from Princeton he's going to see me through - I mean advise me personally on this whole thing. That's what I've asked him to do. And the University will let you know, as I understand it, if you can see me through this thing.

Brown: Work it out up there.

H.M.Jr: Try to work it out. I think it's a crime, after the three or four years' accumulation that he has, not to get the benefit of it. What I want is his judgment. I mean - so if I could have Professor Brown see me through with it, maybe life would be livable in this field.

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Now, what would you think of that, Mr. Altmeyer: if we could get the President to listen to us for an afternoon or evening?

Altmeyer: That would be swell.

H.M.Jr: What?

Altmeyer: That would be fine.

H.M.Jr: We could make an agenda which wasn't too big, and have him cross-examine us. But I don't want to go up and say, "I believe in this," and then find out that either he doesn't understand it or he has another opinion. What?

Altmeyer: (Nods agreement)

H.M.Jr: Now, as to the - what amounts to the actuarial work, which way would you rather have it? Would you rather have - it isn't only your plan, but it's the Townsend plan and all the other plans. Now, would you want to analyze these as they come along, or would you like the Treasury to do it?

Altmeyer: As I said to you over the phone, I think it would be stronger if the Treasury made statements relative to the costs of these various plans. That's my feeling. But we're making analyses of them and we'll have our figures available and we can make statements if that's what is decided.

H.M.Jr: Well, I understood - I think Mr. Doughton, from what I gather, would like the Treasury to do the cost analysis, but I don't - don't want to do it unless, as I say - if it's agreeable to you, I'm willing to do it, with the understanding that whoever does it for us will have the benefit of your people, see?

And if Mr. Brown gets the permission, I'm going to turn everybody over that we've got to him, and he's just going to kind of supervise it and watch it, you see, for us, which would naturally be agreeable to you.

Altmeyer: Yes.

H.M.Jr: What?

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Altmeyer: Yes.

H.M.Jr: But if we could sort of pool our people on that and then our people could do each one, and then have them pool, and then have somebody - I don't know who the best person in the Treasury is - who would go up and explain the cost. But as to the financial policies, if we get - if we decide what they are, why, I'd go up myself, because I think it's so big that I should, if I could make up my mind where I stand on it.

Altmeyer: Then there wouldn't be any - you wouldn't be prepared by Wednesday to go up.

H.M.Jr: Oh no. Oh no.

Altmeyer: And so I think probably the best thing - they want someone from the Government to make a general statement, and I think probably all that we could do on Wednesday would be to make a statement relative to the present operation of the law, show the benefits that are being paid out, and costs, and that sort of thing; and then, secondly, explain the report that we have already sent up to the President and to Congress, and to state that we would prefer to

(Reagh comes in)

H.M.Jr: Do you know Mr. Reagh?

Altmeyer: Yes. Hello.

Reagh: How are you, Mr. Altmeyer?

Altmeyer: ... we'd prefer to discuss details later, when the Committees have a chance to consider these various suggestions in relationship to each other, because they dovetail into each other and some of them may not appeal to the Congress and some may, and it would be helpful to us if we can have some reaction from the Committee to these general suggestions before we go into further detail.

Bell: You wouldn't expect the hearings to continue then every day?

Altmeyer: Then let them go ahead and hear these other people

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on their specific bills and then let us come in with the detailed discussion of any proposals that we may have worked out among ourselves and which the Committee wants to hear us on.

H.M.Jr: Your thought is that you'd make the general statement, then let the Townsends and everybody else go ahead first.

Altmeyer: Yes. Then the Government could come in in a two-fold manner. It could undertake to present cost estimates of all the bills that have been presented to the Committee, and cost estimates and description of any detailed application of the general suggestions we have made in our report.

H.M.Jr: What do you think of that, Dan?

Bell: Sounds all right to me.

H.M.Jr: What?

Bell: Sounds good, because that gives Treasury and the Social Security Board quite a bit of time to get together on that program. And that program you suggest probably will extend some time - just to take care of the Townsends.

Altmeyer: The Townsends alone want a week. I don't think the Committee will give them that much time. But it will probably take the Committee two weeks to hear all these various people.

H.M.Jr: What would you think of that, Brown?

Brown: That has been the - my impression was that these people that want the world with the gold fence around it - not only Townsend, but General Welfare - are raring to go and they will, of course, come out with all kinds of plans that will cost tremendous sums. And if, on the other hand, a constructive plan is presented first, they have a chance to criticize the picayunish benefits afforded and then offer their grand plans afterward. And I've talked to Altmeyer about it and I'd go along with the general notion that that might be a good way.

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H.M.Jr: Yes. Is Mr. Hanes coming?

Gaston: Hanes is before the Ways and Means Committee and he said he'd come directly from the Hill here as soon as he could get away.

H.M.Jr: Oh. Oh, he's before the Ways and Means Committee.

Gaston: Yes.

H.M.Jr: George, you got any ideas?

Haas: No, I think that arrangement is quite good.

Brown: About how long would it be that the Townsend and General Welfare people would probably take?

Altmeyer: I don't think anybody knows. I don't think the Committee knows.

Brown: Two weeks.

Altmeyer: It all depends on what the Committee wants to do; and the Democratic members, of course, don't know what the minority members will do, whether they'll undertake to prolong the hearings or what. So I don't think they could tell us today how long it's going to take.

Bell: Don't you think that they'll allow everybody to be heard that wants to be heard, in view of the promises that were made in the election?

Altmeyer: Yes, but how long will they let them be heard, do you think?

Bell: It seemed to me that the minority would be particularly anxious that the

Altmeyer: You're speaking of the minority now.

Bell: No, I'm speaking of the whole Committee; but it would seem to me that the Committee minority would particularly want the hearings prolonged so they could fill the records.

Altmeyer: I would think so too.

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H.M.Jr: Then our job would be for the Treasury to make up its mind what its position is, get the thing down as simply as possible. I mean what it really is - to list the things and try to put two alternatives, put them right down in parallel columns, and then ask the President - and the implications - whether he'd give us, say, an afternoon or an evening and come in and discuss this thing.

And then, after we have adopted a policy, if we could - out of that would be where I'd come in personally to state the views, on the financial side only. I'm not going to - I'm going to very, very carefully avoid saying whether Plan A.C. 14 is good or bad, or whether a child should have \$18 or \$180 or how much - I mean in any of the plans. I mean that's not my job and I'm going to keep out of it. But as to how we should continue, why, I think somebody ought to say something. I guess that's me.

Brown: Could I ask a question there? At what stage would a definite A.C. 14 appear? I mean is that at the - a bill to be presented on the Hill?

Altmeyer: Well, the way I'd like to have it go - I mean you can't manipulate those things the way you'd like to have them go, but rather than a specific bill being introduced, I'd rather that the Committee, after it's had all these hearings, would meet and discuss these general suggestions that are made, and then call us in and ask us for more detailed discussion of them, and then as a result of that discussion evolve a bill. And I'd like to see them appoint a smaller group that could meet oftener to report back to the full Ways and Means Committee, because that's such a large Committee, I doubt whether they'd ever move along on this. Their present plan, however, is to consider it in full committee - the whole thing; but I doubt when they get down to details whether they'll find it practicable to do so.

Brown: What I mean is, there are so many complications in a bill that there are bound to be many points that they wouldn't come to except through protracted discussions, and the question that's worried me is, at what stage do they get something that's fairly definite that embodies the major principles they have discussed but still also embodies a lot of detailed

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things that they have never had time to work through. I mean remembering the Social Security bill earlier, of course they did take what came up from this end of town and took it apart entirely and put it together again. But whether they'd want to go to that limit or rather start with something that was fairly definite, once they had accepted principles, and then have the rest of it done from this end ...

Altmeyer: My feeling is that after they have finished with these hearings they might call us in to discuss the general suggestions that have been made, and we could at that time give illustrations of what is meant by this, what is meant by that, and then after a few days of discussion, or when it seemed appropriate, give them something as an example. . Or you might not be able to wait several days, you might have to give it to them right away, I don't know. I don't think you could say in advance. But I think the Government ought to try to keep out of the position of backing a specific cut-and-dried bill, because opinions are - it's a matter of opinion, a large part of it. We can go around this room here and after having discussed the thing for two weeks we'd have differences of opinion.

H.M.Jr: Oh yes. Well, I don't - as far as I know, I don't think I have any request from Doughton to come up Wednesday. Will you be talking to him?

Altmeyer: Yes, I'll be talking to him. I called him Saturday. I think he'd like to have you come up, from what he said. But I don't think it's anything....

H.M.Jr: Well, why don't you call him and tell him we've had this meeting, and is this agreeable to him, and if it isn't, if he'll give me a ring, I'd like to explain and back you up. If you'll just call him up and say we all sat down and talked it over and this is the way we'd like to proceed; if he's not satisfied, if he'll give me a ring, why, I'll just talk to him.

Altmeyer: All right.

H.M.Jr: I want him to feel that the Treasury is there to

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back you up but not to get in your way.

Altmeyer: Well now, on these cost estimates, I don't see how he can ask us before these people have had a chance to be heard on their bills for cost estimates; so I think it's perfectly logical to wait with those until these various bills have been heard.

H.M.Jr: Now, who do those go to? Do they go to Blough or Reagh or who?

Haas: The cost part? They go to Reagh.

H.M.Jr: They go to Reagh.

Haas: The tax part goes to Blough and the cost to Reagh.

H.M.Jr: Is that the way it goes?

Haas: Uh-huh.

H.M.Jr: I mean that's the way it would divide up. But I mean it will be like the surplus tax; they'll be wanting an estimate every hour.

Altmeyer: On the hour.

H.M.Jr: And on the hour. And every member of the Committee wanted a different estimate. He'd have his pet plan; he'd call up - "Give me an analysis of this plan."

Haas: This is going to be even more of an amateur night.

H.M.Jr: How many estimates did you have to send up on surplus tax?

Haas: We have a record of it. I don't recall off-hand.

H.M.Jr: Fifty or a hundred - somewhere between fifty and a hundred, weren't there?

Gaston: We had twelve in one day, I know.

H.M.Jr: Just to digress a minute, did you ever take those figures that Byrd introduced on those big corporations and what they'd do to them - and he gave a lot of

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estimates - did you ever go back and analyze the figures in the light of what's happened?

Haas: No; it would be interesting to do that.

H.M.Jr: Why don't you do that? He had these big sheets, all these big companies, and said this would happen and that would happen.

Haas: I remember it.

H.M.Jr: I think it would be interesting to see, in view Huh?

Haas: I'll do that, Mr. Secretary.

H.M.Jr: We had all those sheets, didn't we?

Haas: I think they're in the Record too. No, that was a confidential

H.M.Jr: Well, he must have ...

Haas: I'll see if I can get them.

H.M.Jr: Well now, you're going to contact Doughton, tell him we met and this is the way it is, and that we're ready to do the estimating. Now, who would our boys contact in your place? I mean so when we do it

Altmeyer: They know.

H.M.Jr: They know. All right.

Altmeyer: They've been contacting them, I guess, for a long time.

H.M.Jr: Bell, you got anything else?

Bell: No, I haven't anything.

H.M.Jr: Herbert?

Gaston: No.

H.M.Jr: Brown?

Brown: (Nods nothing)

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Blough: (Nods nothing)

Altmeyer: Now, here are the kind of questions that I was going to ask. I've split it up into

H.M.Jr: You going to ask us some questions?

Altmeyer: Yes.

H.M.Jr: All right; you're going to make us work.

Altmeyer: I have them split up into several parts. Under benefits, I get it from your statements you think we should develop a pattern of benefits.

H.M.Jr: The pattern.

Altmeyer: The pattern of benefits.

H.M.Jr: Don't you?

Brown: Yes, sir.

Altmeyer: And I listed here:

Should monthly benefits begin in 1940?

Should benefits be increased in early years?

Now, this is a Treasury item, though under benefits: Should eventual total benefit costs in later years be increased or decreased or kept the same as at present? We take the position it should be kept the same as at present. I take it that the Treasury probably would concur in that. Well, I think so.

Bell: I think so. No higher than the present - put it that way.

H.M.Jr: Well, I'm not going to make any decisions this afternoon, if you don't mind.

Altmeyer: All right. Well, I take it that there won't be much time to be spent on the benefit thing.

But, now, coming to taxes, we have: Should the step-up in the tax rate in 1940 be maintained?

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I take it that we can all say yes, it should be maintained. There is no difference of opinion on that, is there?

H.M.Jr: There is in the Treasury. We'd have to do a little - we have a whole group that thinks no. And the President asked the Fiscal and Monetary Committee to take the thing. And I think Mr. Eccles and his whole group are opposed to it. So we'd have to - I think I'm right - you're (Bell) a member of that.

Bell: (Nods yes)

H.M.Jr: Didn't Eccles - isn't he opposed to increasing the tax?

Bell: Yes, I think you can say that. He was opposed to it if it's shown that it's going to have a detrimental effect on the economy.

H.M.Jr: You'd have to put a question mark after that. We had Professor Hansen down, and he's absolutely opposed to increasing the tax. Wasn't he?

Blough: He was. He didn't quite put it "absolutely."

Brown: Well, he took two positions.

Blough: He said if he were President he might not be against increasing it, but as an economist he was.

H.M.Jr: What else have you (Bell) got?

Bell: I think we'd be interested also in the total costs of these benefit payments. While the scale of benefit payments certainly should be developed by the Board, yet the Treasury ought to know the total amount involved.

Murphy: In terms of present values?

Bell: As I understand, these are outside of the old-age - I mean you're talking about the total benefits under the Act.

Altmeyer: No, I'm just talking about old-age, so

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Bell: Excuse me, I thought you were talking about the whole

Altmeyer: Then, under taxes, the second question: Should the step-ups in the tax rate after 1940 be changed? Should they stay as they are now and up to 1949, three percent each? Now, we take the position - we thought we were taking the Treasury's position - that they shouldn't be touched. They're in the wood, to use Douglas Brown's expression, and we think they should stay in the wood. I mean from a Social Security standpoint as well as a tax standpoint, we think certainly for from now until 1949 that is much better than any juggling around of tax rates to match receipts and disbursements, although there is a principle involved of how soon the Government should start contributing out of the General Fund. And so we have taken the position, in opposing any change in the present tax rates, that a Government contribution shouldn't come in at least until after the present tax rates prove to be insufficient to cover current expenditures.

H.M.Jr: Well, that would be one of the things that we should pass on, I'd say. Opinion hasn't jelled yet. I wasn't at this meeting, but they spent three afternoons with Eccles and Mr. Delano, didn't you?

Bell: Yes, sir.

H.M.Jr: Didn't you for two or three or four hours - there was no agreement?

Bell: Arthur was present at one of them.

Altmeyer: I don't think there ever will be.

Brown: In the Advisory Council we thrashed that thing out until the cows came home, and the best balance that I can see in all the points of view was for the schedule of taxes as in the law now, but that certainly by 1941 or 1942 - say by the end of '41 - we'll have definite - far more definite knowledge on certain long-run forces affecting the cost of benefits, if the benefits start in 1940, and five years of tax experience, tax coverage; the possibility of covering farm labor and domestics would

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be much more certain, and by that time you can make some pretty definite decisions.

- Altmeyer: Then the next question was: Does the Treasury oppose having the system partly financed by direct Government subsidy from other than payroll taxes? When should such a subsidy begin and in what proportion? Should any specific taxes be levied at this time or as of a definite date in the future - that is, to take effect at a definite date in the future - to provide the subsidy?
- And finally: Should Titles VIII and IX be combined?
- Blough: You mean for administrative purposes.
- Altmeyer: One tax, making the definitions the same in both titles.
- Reagh: That's assuming - yes, in both titles: benefits coverage - both sides.
- Altmeyer: Yes.
- Blough: Put only a small amount of it goes to unemployment compensation anyway because of the offsets.
- Altmeyer: That's right. There wouldn't be any change in the collections - I mean the amount collected. It would just be - well, except so far as the coverage was changed; but it would give us a chance probably to simplify reporting procedure somewhat by employers.
- Gaston: You'd have to restate the Federal tax, wouldn't you? You wouldn't have the same opportunity for the offset. Just have to state the Federal tax on the straight basis.
- Altmeyer: Instead of, this year, three percent over in one title and two percent over in the other title, it would be five percent, or rather, four percent for the employer and one percent for the employee, in one title. It would be 2.7 offset for unemployment compensation; that's the way you'd express it.
- Then, under reserve provisions, I had several questions. One is the over-all question: Should

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the present reserve provisions be retained?

Bell: That's tied in with your previous question as to when and what amounts you're going to take out of the General Fund.

H.M.Jr: Excuse me. (Steps out)

Altmeyer: Well, it's not necessarily tied in, because you could - the fact that you might raise funds or provide funds out of other than payroll taxes wouldn't mean that you went off the reserve system necessarily.

Bell: No, but if you're going off the reserve system, you certainly don't need additional taxes at this time.

Blough: If you're going all the way off.

Gaston: That's a question.

Haas: Or you could stay on just by making appropriations - just stay on as far as the books are concerned.

Reagh: Be on the same basis as the Civil Service Retirement fund; don't have any appropriation for - it depends on whether you make an appropriation on an accrual basis or cash basis. Be a reserve if you'd go through ...

Brown: Be pretty healthy cost in the way of taxes.

Reagh: It would be independent of actual financing.

Brown: Yes. I mean rather than deficit financing, if it were made up by taxes, then it would be pretty healthy taxes.

Haas: Give us a perpetual deficit, wouldn't it? Formal deficit.

Reagh: I think so. Just about that.

Blough: If we can get a reserve somewhere in between, not just a contingency reserve but a healthful reserve - wasn't that the original idea? I mean the idea of

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the Committee on Economic Security. Ten billion dollars as a healthful reserve, or about fifteen.

Altmeyer: About fifteen.

Brown: Wasn't in the reports. Might have been behind closed doors. It was self-financing

Altmeyer: In our report, at the very last minute we said, "Here's a plan." We didn't say it was a plan recommended by the Committee on Economic Security, which showed a building up of a reserve to a figure of fourteen or fifteen billion dollars, as I recall.

Blough: I gather from Ed Witte that such a plan was in considerable favor at one time in the Committee.

Brown: Well, the last reserve, as I remember, was eleven - the maximum was eleven billion 400 million, wasn't it? And then that included farm labor and domestics, so that if you cut them out it would come under ten billion. I'm not sure, but

Altmeyer: That was very interesting: that the actuaries started out swearing by all that was holy that they'd have to have a full reserve, and the financiers started out saying, "No, sir, we just can't handle more than 16 billion dollars"; and at the end of three months the actuaries were saying, "You shouldn't have a full reserve," and the financiers said, "We can handle all the money you can give us." Just exactly changed their positions.

Blough: That shows what education will do.

(H.M.Jr returns)

H.M.Jr: Have you got them all settled while I was out?

Altmeyer: No, no. Then, after that blanket question, should the present reserve provisions be retained, the question, should the payroll taxes go directly into a special trust fund or into the general treasury as now provided?

Blough: See, that was a recommendation of the Advisory Council, wasn't it?

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Bell: Only changed for constitutional reasons, wasn't it?

Altmeyer: Yes. Then, should such a fund be managed by a Board of Trustees? That was in the Advisory Council. If so, who should be the trustees? Should the present three percent interest rate be eliminated so that outstanding obligations can be purchased?

Now, it is a requirement that the fund must earn three percent. Should it be required that only outstanding obligations be purchased?

I think I know the answer to some of them.

Bell: Give Reagh a nice job, if you let them purchase all kinds of coupons, determining the valuation.

Reagh: Of course, from the standpoint of cost, it would seem pretty silly, if we're going to get off a reserve basis, to make a distinction between subsidy and a form of interest.

Haas: A form of arbitrary sinking fund which is not the least desirable type of sinking fund; but because of adverse effects on your economic system - if you knew - I mean the Secretary was obliged to retire, say, a billion or two billion dollars at a fixed time, maybe the top of the business boom

Altmeyer: Yes. Well, I thought I understood your position there, but

Haas: I don't know what the Secretary's position is.

Altmeyer: Vandenberg, for instance - his bill proposes that you can only purchase outstanding obligations.

Murphy: The last draft of it I saw still kept the same three percent rate.

Bell: A little bit inconsistent, too.

Altmeyer: I don't know how that's to be accomplished, but perhaps he knows.

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On coverage possibly this question: Will the Treasury oppose extension of Act to cover farm labor and domestic servants?

H.M.Jr: That's the sort of thing we won't take a position on.

Altmeyer: I see. I think the Treasury did take a position last time because of the administrative - the possibility of collecting the taxes.

H.M.Jr: Well, that's a pretty weak position.

Bell: Well, that's the one matter that you've got in mind, isn't it? Doing it by some means of - eliminate some of the administrative difficulties.

H.M.Jr: I know, but it's up to us to - if they want it, it's up to us to find a way to do it, huh?

Brown: I think it's coming, sir.

H.M.Jr: No, I - I mean if that's the policy, then it's up to us to find a way to do it. I mean that's what I would say.

Reagh: I think Mr. Graves the last time mentioned that, said we could do it but it would cost more than the taxes collected.

H.M.Jr: That's all right; we can tell them that.

Altmeyer: You mean by the present methods.

Reagh: Or with the stamp system - either way. Might cost more with the stamp system, I think he believed.

H.M.Jr: The suggestion was made last week that we send somebody - Harold Graves or somebody immediately to England and study their methods a couple weeks and come back. I think we'll do that. These economists in their resolutions said that we should. Didn't you say

Brown: Yes.

H.M.Jr: ... send somebody like Harold Graves to England for a month to study this thing and come back.

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Altmeyer: And finally - this is the question we started out discussing -: Should specific tables be presented showing the estimated contributions, disbursements, reserve, and Government subsidy, from now until 1980? Before you (Reagh) came in I think I made the suggestion we might, in presenting our estimates, present reasonable minimum and reasonable maximum figures rather than one series of figures.

Reagh: Limits.

Altmeyer: Yes, so they can't attach a specious accuracy to our figures.

Reagh: Just one thing that you said I'd like to see you get away from. Instead of saying 1980, why not say for 40 years? That 1980 has got to be a mythical figure, just as the 47 billion dollars, which is, of course

H.M.Jr: Could I have that?

Altmeyer: Oh yes.

H.M.Jr: Now, I think the thing for us to do is to take that and make up our own mind and, if we could, have the answers on those things which we think belong to the Treasury, and then fix them up. That would be the thing: first make our decision - "This is what we think the Treasury's position is, and why; these are the questions." And then that would be - based on this thing would be the thing we'd want to put up to the President, if he'd give us an evening, wouldn't it? But we'd first - the Treasury would have to first make up its mind, huh?

Altmeyer: That's right.

H.M.Jr: Well, we've just got to do it, that's all, and we'll do it as fast as we can. I guess that's the only thing I want Professor Brown to help me on: make up my mind for me. I'll get busy on this.

Who's going to do this? Now - I mean who's going to really work on this thing, because this is going to be a three-months job. Are you (Blough) - how busy are you?

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Blough: Well, we're all very busy. The tax aspects of this I should think we'd want to work on. I should think some of them shouldn't be worked on in our division.

H.M.Jr: Well, George, until Professor Brown gets a clearance, see, from ...

Brown: Well, of course, as we talked about it, I'll have to take it up - all up - whether I could do such a thing, and I'd want to work it out pretty carefully.

H.M.Jr: All right, but in the meantime get busy and in two or three days talk to me about it again; but have something for me, huh?

Haas: O.K.

H.M.Jr: Huh?

Haas: Yes, sir.

H.M.Jr: Then divide it up.

Policy Questions on Social Security Submitted to
the Secretary of the Treasury by
Chairman Altmeyer, January 30, 1939*

- Question 1. Should monthly benefits begin in 1940?
Question 2. Should benefits be increased in the early years?

It is recommended that the Treasury should not oppose commencing old-age benefit payments in 1940 or increasing their amount in the early years.

- Question 3. Should the ultimate annual benefit cost of the system be increased, decreased, or kept the same as at present?

It is recommended that the Treasury should take the position that the ultimate annual cost of the revised system, as a percent of covered payrolls and including all types of benefits should not be increased. It is recommended that the Treasury oppose the institution of disability benefits at the present time.

- Question 4. Should the step-up in the tax rate in 1940 be maintained?

It is recommended that the Treasury Department take the position that the 1940 step-up in payroll taxes should go into effect as provided in the existing law.

- Question 5. Does the Treasury Department favor the step-ups in the tax rate after 1940 as provided in the 1935 Act?

It is recommended that following the 1940 payroll tax rate increases and before 1943, the financial provisions of the old-age insurance system be re-examined. It is further recommended that pending such re-examination, the tax rate schedule now embodied in Title VIII of the Social Security Act be left unchanged.

* These questions all bear on the "old-age insurance system", broadly interpreted to include the other types of benefits administratively associated with this system. No questions on public assistance are included.

Question 6. Does the Treasury approve having the system partly financed by direct government subsidy from other than payroll taxes?

It is recommended that the Treasury Department recognize the need for, and approve the principle of, a Federal subsidy to the old-age insurance system.

Question 7. In case a Federal subsidy is approved, when should such a subsidy begin?

It is recommended that since no immediate need for a Federal subsidy exists, and since all relevant data are not now available, decision regarding the timing of the subsidy be postponed pending the re-examination of the financial provisions of the old-age insurance system following 1940, proposed in Question 5 above.

Question 7-a. In case a Federal subsidy is approved, what should be its relative magnitude?

It is recommended that pending a re-examination of the financial provisions of the Social Security Act after 1940 (proposed in Question 5 above), and pending the availability of more information regarding the financial requirements of the old-age insurance system, decision regarding the relative magnitude of the Federal subsidy be postponed.

Question 8. In case a Federal subsidy is approved, should legislation be immediately enacted providing specific taxes to be collected in the future at such time and in such amounts as will be required for the Federal contribution?

It is recommended that pending a re-examination of the financial provisions of the Social Security Act after 1940 (proposed in Question 5 above), and pending the availability of more information regarding the financial requirements of the old-age insurance system, decision regarding the manner of financing the Federal subsidy be postponed.

Question 9. Should Title VIII and Title IX taxes be combined?

It is recommended that the Treasury Department assist the Social Security Board in developing a practical plan for coordinating Title VIII and Title IX taxes.

Question 10. Should the present reserve provisions be retained?

It is recommended that the Treasury favor the abandonment of the full reserve method of financing, either with or without current financial provision for the accruing reserve liability. It is recommended that the Treasury favor the accumulation of a moderate contingency reserve.

Question 10-a. If the full reserve method of financing is abandoned, what provision should be made for setting forth to Congress and to the public the current status and future commitments of the old-age insurance system?*

It is recommended that, if the full reserve method of financing is abandoned, the Secretary of the Treasury should be required by law to present annually to Congress a memorandum showing forecasts of the cost of benefit payments under the then existing law for decennial years, fifty years in advance, as a ratio of covered payrolls, on the assumption of the wage rates existing at the time of the preparation of each memorandum. Capitalized figures of future benefit payments and of future tax collections should no longer be presented.

Question 11. Should the payroll taxes go directly into a special trust fund?

It is recommended that if, in the opinion of counsel, the proposed change would in any way jeopardize the constitutionality of the Act or of the taxes levied under it, it should not be made. Otherwise the Treasury should not oppose it.

* Question added by Treasury staff.

Question 12. Should such a (special trust) fund (for the segregation of Title VIII taxes) be managed by a Board of Trustees?

It is recommended that if a special trust fund is established, it should be managed by a board of trustees.

Question 13. Who should be the trustees (of a special trust fund for the segregation of Title VIII taxes)?

This is a matter upon which we do not feel qualified to make a recommendation. Among the persons who would seem logical candidates are the Secretary of the Treasury, the Director of the Budget, the Treasurer of the United States, the Chairman of the Social Security Board, and the Attorney General.

Question 14. Should the present 3 percent interest rate be eliminated so that outstanding obligations can be purchased?

Question 15. Should it be required that only outstanding obligations be purchased?

It is recommended that the present provisions of law be retained in this respect, -- that is investment in special issues or in outstanding securities should be at the option of the Secretary of the Treasury (or the Board of Trustees if one is set up), subject to the requirement that no securities may be purchased to yield less than 3 percent. This means, in effect, that all investments must be in special issues as long as no Government securities are obtainable to yield as much as 3 percent.

Question 16. Will the Treasury approve extension of the Social Security Act to cover farm labor and domestic service?

It is recommended that the Treasury Department approve the principle of the extension of coverage under the old-age insurance system to employment in agriculture and domestic service in private homes, but (except with respect to large-scale agriculture) request postponement of such extension until the next session of Congress, to permit further study of the ways and means of overcoming administrative difficulties inherent in the application of payroll taxes to these employments.

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Question 17. Should specific tables be presented showing the estimated contributions, disbursements, reserves, government subsidy, etc., from now until 1980?

It is recommended that the tables to be presented to Congressional committees in connection with the current hearings should cover the next 40 or 50 years rather than extend specifically to 1980. The use of this date fosters the erroneous impression that the system will reach a mature condition at that time.

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- Question 1. Should monthly benefits begin in 1940?
Question 2. Should benefits be increased in the early years?

Recommended Treasury decision.

It is recommended that the Treasury should not oppose commencing old-age benefit payments in 1940 or increasing their amount in the early years.

These two questions must be discussed together.

A. Affirmative Arguments.

(1) The social need for old-age security is immediate. No annuities may be paid under present law, however, until January 1, 1942 and the annuity which would be payable to a person retiring on that date, who had been in covered employment at an average salary of \$150 per month during the entire period of the Act, would be only \$20 per month, and this sum would not be increased if he had a dependent wife. To meet social needs, it is necessary that monthly benefits begin as soon as possible and be increased in the early years.

(2) The administration of the tax provisions of the Act would be made easier if benefit payments are begun in 1940 and are larger in the early years. Employees would be more interested in seeing that the proper taxes are paid upon their behalf by their employers and by themselves if the value of coverage under the Act is brought home to them by the actual payment of worthwhile benefits to someone they know.

(3) The old-age insurance benefits provided under the present law will, for many years, in the case of married couples in many States, be less than the non-contributory old-age assistance which they could receive under Title I. Increasing the amount of benefits in the early years will result in a better balance between the non-contributory old-age assistance and the contributory old-age insurance programs. Not all of the cost of the increased old-age insurance benefits will be additional, as there will be some decrease in the cost of old-age assistance.

(4) There is considerable political pressure for the enactment of an extravagant old-age pensions system of the Townsend type. Unless the existing old-age insurance system is liberalized, the whole matter of old-age security may be taken out of our hands and placed upon a basis certain to result in ultimate collapse, thereby discrediting the entire idea of providing for old-age security through social action.

B. Negative Arguments.

(1) According to Social Security Board estimates, the cost of Plan AC-14 without disability benefits, is about 40 percent higher (present value) than the cost of the benefits provided under existing law. This increase arises entirely from commencing benefit payments sooner and paying more in the early years, as the ultimate level of benefit payments as a percent of covered payroll is expected to be no higher under Plan AC-14 than under present Title II. This increased cost will involve either a substantial increase in payroll taxes effective immediately, a greater increase in these taxes effective in future years than at present contemplated (to a level higher, in many cases, than private insurance company rates), or a large Government subsidy in later years. Any one of these alternatives is bad. The present benefit schedule should, therefore, not be tampered with.

(2) The proposed changes will greatly weaken the (already weak) "contributory" character of the present old-age insurance system, that is, they will make the relationship between each individual's contribution and his benefit relatively slight, at least for many years to come. This will remove one of the important checks to unlimited demands for further increases in benefits which exists in some measure in the present law.

(3) Commencing benefit payments in 1940 and increasing their amount in the early years will mean that most of the annuities paid for many years to come will not have been earned in any substantial part by the contributions of the annuitants and their employers. It is intellectually dishonest to pay unearned benefits of this character on the basis of "ceremonial" contributions, while denying annuities-as-of-right to the unemployed present aged, whose need, on the average, is greater, and whose contributions, for practical purposes, are as great as those of the persons who will receive annuities.

C. Affirmative Opinions.

(1) The Social Security Board supports these proposals in its report to Congress and the President.

(2) The President specifically endorsed the Social Security Board's proposals in these respects in his message of transmittal, stating: ". . . The report suggests a two-fold approach which I believe to be sound. One way is to begin the payment of monthly old-age insurance benefits sooner, and to liberalize the benefits to be paid in the early years. . ."

(3) The Advisory Council on Social Security also endorses both proposals in its final report. There was no dissent in the Council with respect to either proposal.

D. Negative Opinions.

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Question 3. Should the ultimate annual benefit cost of the system be increased, decreased, or kept the same as at present?

Recommended Treasury decision.

It is recommended that the Treasury should take the position that the ultimate annual cost of the revised system, as a percent of covered payrolls and including all types of benefits should not be increased. It is recommended that the Treasury oppose the institution of disability benefits at the present time.

It is understood that increasing the coverage will increase the annual cost of the system both in dollars and as a proportion of the national income, but this is not considered an additional burden as long as the coverage is increased proportionately. In the following discussion, therefore, the ultimate annual cost is taken as a percent of covered payrolls.

The cost of the present system is subject to a wide error of estimate. Despite this, it provides a convenient basis for comparison with the costs of proposed changes as, by the use of common assumptions, the same error of estimate may be made to apply, in large part, to both the present law and the proposed variations.

A. Arguments in favor of an increase in total benefit cost in the later years.

(1) It is argued by some that the present scale of benefits, even in the later years, is not adequate and ought, therefore, to be increased. This is particularly urged with respect to permanent disability benefits, and it has been the position of both the Social Security Board and the Advisory Council that, if such benefits are to be included, their cost should be additional to that of the present system, even in the later years. These additional costs, it is generally supposed, can be taken care of by taxation "in accordance with ability to pay".

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B. Arguments in favor of a decrease in total benefit cost in the later years.

(1) The present system involves an ultimate cost estimated at between 10 and 15 percent of covered payrolls. This is too high, and may be a larger proportion of future national income than can be canalized through the national Government for a single purpose without endangering its solvency. The next generation will know more, both about its own resources and what it wants to do with them than we do; and we should not tie its hands. Benefits should not be lightly promised on the basis of anticipated national income alone, as there is a bad transfer problem involved in collecting a large proportion of this income as taxes, and the resultant friction may decrease the amount of the income itself.

C. Arguments in favor of keeping total benefit cost in the later years the same as that contemplated in the present law.

(1) It is always easy to increase commitments, but hard to reduce them; and while, in view of the temper of the times, it seems impracticable to reduce our future commitments with respect to old-age security at the present time, it would seem unwise to increase them.

D. Opinions in favor of an increase in total benefit cost in the later years.

(1) Mr. Pressman, representing the CIO viewpoint in the Advisory Council, opposed any reference to ultimate cost in the Council's report. His intention was clearly that this cost should be increased.

(2) The Advisory Council's report did not take a definite position on the immediate institution of disability benefits, the report stating that some members favor this while others oppose it. The entire Council agreed, however, that such benefits should be instituted ultimately, and that their cost should be additional to the ultimate cost of the present program.

(3) The Social Security Board did not take a definite position in its report with respect to the immediate institution of permanent disability benefits. The report states, however, that, if such benefits are included, they would raise the cost of the system in later years above that contemplated by present law.

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E. Opinions in favor of a decrease in total benefit cost in the later years.

F. Opinions in favor of keeping total benefit cost in the later years the same as that contemplated in the present law.

(1) The Advisory Council recommended that "The eventual annual cost of the insurance benefits now recommended, in relation to covered payroll and from whatever source financed, should not be increased beyond the eventual annual disbursements under the 1935 Act". As previously noted, however, disability benefits, if any, would be in addition to this amount.

(2) The Social Security Board states in its report: "When the System is fully matured, its eventual cost with the changes here recommended . . . would be somewhat less than the cost of the present system . . . If permanent total disability insurance should also be included, the eventual cost, when the system is fully matured, would be somewhat more than the present system." In view of the attitude of the Board, as determined by personal discussion, this opinion is listed with those in favor of keeping the ultimate cost the same as contemplated in the present law rather than as in favor of a decrease in ultimate cost.

Question 4. Should the step-up in the tax rate in 1940 be maintained?

Recommended Treasury decision.

It is recommended that the Treasury Department take the position that the 1940 step-up in payroll taxes should go into effect as provided in the existing law.

A. Affirmative Arguments.

(1) Public understanding of the fact that the old-age benefits program involves a heavy tax burden would be undermined by failing to increase taxes, as provided in the 1935 Act. The argument is especially pertinent if benefits are increased at the present session of Congress.

(2) If a contingency reserve is not built up in advance on the momentum of the 1935 Act tax rates, it will probably not be built up at all, because of the powerful incentives on Congress not to increase taxes.

(3) The pressures for high expenditures and against increased taxes are so great that the improvement in the fiscal position of the government through the automatic increase in the payroll taxes should not be abandoned.

(4) The necessity for financing from the general budget will be postponed.

(5) These taxes are part of a contributory system and their character should not be altered by requirements of the government's general financial policy which may be temporary.

B. Negative Arguments.

(1) The effect of collecting more in payroll taxes than is paid out in benefits is deflationary and increases the "deficit spending" in the general budget necessary to produce the desired net contribution to buying power. The argument is less significant if cash benefits paid in 1940 should be substantial.

C. Affirmative Opinions.

- (1) The Social Security Board favors the step-up in 1940.
- (2) The majority of the Advisory Council favors the step-up in 1940.
- (3) The group of economists called to advise the Secretary on Social Security matters, with the exception of Professor Hansen, favors the step-up in 1940.

D. Negative Opinions.

- (1) Professor Hansen, together with others making up a small minority of the Advisory Council, does not favor increases in payroll taxes in 1940.
- (2) The Chairman of the Federal Reserve Board does not favor increases in payroll taxes in 1940.

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Question 5. Does the Treasury Department favor the step-ups in the tax rate after 1940 as provided in the 1935 Act?

Recommended Treasury decision.

It is recommended that following the 1940 payroll tax rate increases and before 1943, the financial provisions of the old-age insurance system be re-examined. It is further recommended that pending such re-examination, the tax rate schedule now embodied in Title VIII of the Social Security Act be left unchanged.

A. Affirmative Arguments.

(1) If the full reserve system is to be continued as provided in the 1935 Act it is necessary for the step-ups in the tax rate after 1940 to take place as scheduled. (If additional benefit payments are provided even greater rate step-ups would be required.)

(2) If the full reserve system is to be abandoned but a substantial contingency reserve is to be built up, at least some of the scheduled rate step-ups will be necessary. The number of rate step-ups that may be postponed will depend on the volume and timing of additional benefits which may be provided.

(3) Certainty that payroll taxes will actually reach the scheduled maximum and that the general treasury will not have to bear a very large part of the total cost of benefits can best be achieved by not disturbing the existing rate schedule.

(4) Beneficiaries under the old-age insurance system will be more nearly assured of benefit payments in future years if their contributions are substantial in the early years since thereby they build up an equitable claim to benefit payments.

(5) It is too early at this time to decide whether or not the step-ups in tax rates should continue as provided in the present scale. The future financial requirements of the old-age insurance system cannot now be predicted with certainty.

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As experience accumulates and more information becomes available the financial provisions of the system will have to be re-appraised. Pending such re-study, nothing would be gained by premature alterations in the present provisions of the Social Security Act.

B. Negative Arguments.

(1) Stepping up the tax rates after 1940 according to the present schedule would have a continued deflationary effect for a considerable number of years until the benefit payments exceed tax yields.

(2) Since in the early years the reserve would be built up at a rapid rate, some of the objections raised to the full reserve system would apply. Even if benefits are increased as proposed, the reserve would be built up for 10 or 15 years.

C. Affirmative Opinions.

(1) The Social Security Board appears to favor the fulfillment of the scheduled rate step-ups until the rates reach the maximum provided in the present law.

D. Negative Opinions.

(1) The Advisory Council favors the study of tax rates in 1941 with a view to revision of policy if found desirable.

(2) The general sentiment of the five economists advising the Secretary of the Treasury on old-age insurance was to the effect that the size of the contingency reserve and other factors should determine the tax rates and that accordingly, there should be no automatic acceptance at this time of the increases provided in the present law.

Question 6. Does the Treasury approve having the system partly financed by direct government subsidy from other than payroll taxes?

Recommended Treasury decision

It is recommended that the Treasury Department recognize the need for, and approve the principle of, a Federal subsidy to the old-age insurance system.

A. Affirmative Arguments.

(1) Since the nation as a whole would benefit from a system of old-age security, parts of the cost of such a program ought properly be borne by the nation as a whole. Provision of old-age security is now recognized as a general governmental responsibility similar to other public services financed from general revenues.

(2) Payroll taxes which would be required to finance the projected scale of old-age benefits would be very high and would severely undermine the standard of living of workers whose wages are insufficient to provide savings for old-age security.

(3) The old-age security program will eventually replace in part other welfare activities, notably public assistance and general relief, which would otherwise have to be financed from general revenues.

(4) The provision of a government subsidy would forcefully call to the attention of the American people that Title VIII taxes plus interest on the reserve will not fully finance the liabilities which are likely to accrue in connection with an insurance system. It would therefore serve to restrain further increases in benefits. (However, see B-3 below.)

(5) Governmental participation in the financing of a social insurance program has long been accepted as sound public policy in other countries.

(6) If the full reserve principle is abandoned (as recommended in Question 10 below), and only a moderate contingency reserve is provided, a Government subsidy would be virtually indispensable, for in its absence the payroll taxes required to pay benefits would have to be so high that many individuals could purchase less expensive old-age security from private insurance companies.

B. Negative Arguments.

(1) Pending the extension of coverage to include substantially all gainfully employed, it is doubtful whether, on ground of justice, a governmental subsidy is defensible. Such subsidy would have to be paid from general revenues contributed by all taxpayers for the benefit of a restricted group of workers, which is already subsidized by the public at large, in part by the payment of artificially high yields on the reserve and in part through the shifting of the incidence of the tax on employers. (However, it is probable that even under present coverage 75 or 80 percent of gainfully employed will be eligible for benefits by the time they reach old age.)

(2) The provision of a direct government subsidy for old-age security would become a heavy drain upon the Treasury.

(3) The financing of benefits from payroll taxes serves as a restraint on expenditures. The removal of that restraint and the precedent for providing general revenues for old-age security may encourage raids upon the Treasury for increasingly larger contributions and benefits. (However, see A-4 above.)

(4) A program financed entirely by payroll taxes would be more acceptable to those who disapprove of public assistance and believe that security for old age should properly be provided by individual initiative.

C. Affirmative Opinions.

(1) The Advisory Council recommends that the system be supported one-third by employee, one-third by employer and one-third by the government.

(2) The Social Security Board believes it would be sound public policy to pay part of the eventual cost of the benefits out of taxes other than payroll taxes.

D. Negative Opinions.

(1) At the time of the consideration of the Social Security Act in 1935, the Treasury Department stressed its preference for a program financed entirely by payroll taxes.

(2) The President in his early statements stressed the self-supporting character of the old-age insurance system.

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Question 7. In case a Federal subsidy is approved, when should such a subsidy begin?

Recommended Treasury decision.

It is recommended that since no immediate need for a Federal subsidy exists, and since all relevant data are not now available, decision regarding the timing of the subsidy be postponed pending the re-examination of the financial provisions of the old-age insurance system following 1940, proposed in Question 5 above.

A. Various Possibilities.

(1) The timing of a subsidy would of necessity be determined by three other variables:

- (a) The volume of benefits.
- (b) The extent to which the increases in payroll taxes now scheduled in the Social Security Act are permitted to go into effect.
- (c) The amount it is desired to accumulate for reserve.

(2) The subsidy might be introduced:

- (a) Immediately (1940).
- (b) Shortly after 1940 when the yield from the combined 2 or 3 percent payroll tax is inadequate.
- (c) After 1950 when combined payroll taxes are increased to 6 percent.
- (d) At any time during the interim.

(3) A decision on this point will be affected by the decision respecting the step-up in tax rates (Question 4), and the decision respecting size of the reserve (Question 10), and these in turn will be affected by the decision respecting the timing of the subsidy.

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(4) If the payroll taxes, as scheduled, are allowed to go into effect uninterruptedly, no need for a subsidy would arise until some time after 1950, since until then current tax collections would exceed current benefit payments. Similarly, the smaller the reserve that is decided upon, the longer can the introduction of the subsidy be postponed since a subsidy would not be required to build up reserves in the early years, and also since part of the principal of the reserve would be available to pay benefits.

B. Arguments favoring the early introduction of a subsidy.

(1) The early provision of the subsidy would add to the acceptability of the old-age insurance program by the working population. This consideration is of particular importance in connection with the extension of coverage to groups not now covered.

(2) It would forcefully put the population on notice that the old-age insurance system requires a subsidy and that any increases in the scale of benefits would of necessity increase the size of that subsidy.

(3) It would either accelerate the accumulation of a reserve or permit a postponement of increases in payroll taxes.

C. Arguments opposing early introduction of subsidy.

(1) Early introduction of a government subsidy would reduce the probability of scheduled payroll tax increases being permitted to go into effect.

(2) If the case for a government subsidy rests upon the argument that the working classes are in themselves unable to provide adequately for their old-age, then the subsidy is justified only after these working classes have made their maximum contributions (presumed now to be 3 percent of payrolls.)

(3) In view of the present budgetary deficit, it would be desirable to postpone the introduction of the subsidy as long as possible.

(4) Collections from present taxes are adequate to meet benefit payments in the early years. If the plan for a sizable reserve is abandoned, there is no need for an immediate subsidy. Moreover, the question of timing of the subsidy

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cannot be answered until more information is available regarding the actual operation of the financial provisions of the old-age insurance system.

D. Opinions concerning the timing of the subsidy.

(1) The Advisory Council's plan calls for a study of the timing of the Federal subsidy during the period when the combined payroll tax rate is 3 percent (1940-1942).

(2) The Social Security Board has indicated its preference for the postponement of the introduction of the Federal subsidy to a time in the future when current outgo for benefit payments exceeds current income from already scheduled payroll taxes and interest on reserves.

Question 7-a. In case a Federal subsidy is approved, what should be its relative magnitude?

Recommended Treasury decision.

It is recommended that pending a re-examination of the financial provisions of the Social Security Act after 1940 (proposed in Question 5 above), and pending the availability of more information regarding the financial requirements of the old-age insurance system, decision regarding the relative magnitude of the Federal subsidy be postponed.

A. General Alternatives.

(1) The Federal Government may assume one-third of the cost of benefits. This answer is suggested by the view that security for old-age is the joint responsibility of the worker, the employer and the general public, and that all three benefit equally from a system of old-age security. Carried to its logical conclusion this alternative would imply the introduction of a government contribution as soon as benefit payments are begun.

(2) The Federal Government may assume the residual responsibility, that is, it may cover the deficit between benefit payments and payroll tax collections. This answer is suggested by the view that the wages of some workers are inadequate to provide savings for old-age security without severely undermining the standard of living of the working population. This alternative would imply the postponement of the introduction of a Federal contribution until some time after the initiation of the payment of benefits. It would further imply acceptance of some tax rate, say 3 percent, as the maximum which workers could contribute for the security of their old age.

(3) The Federal Government may assume residual responsibility but not in excess of a fixed proportion, say one-third, of the total cost of benefits. This combines some features of the two preceding alternatives and implies that eventually the payroll tax rates may be allowed to increase in excess of the 6 percent now scheduled by the Social Security Act.

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B. Relevant Considerations.

(1) It is readily apparent that the decision respecting the relative size of the Federal contribution will in part be determined by the decision respecting the scheduled increases in payroll taxes and in part by the decision respecting the size of the reserve. Both of these in turn are affected by decisions respecting the size of the Federal contribution.

(2) In general it may be stated that the greater the proportion of the general population covered by the insurance system the stronger the case for a larger subsidy.

C. Opinions concerning the magnitude of the subsidy.

(1) The Advisory Council's plan calls for distributing the eventual cost of the old-age insurance system by means of approximately equal contributions by employers, employees and the government.

(2) The Social Security Board expressed no official view on the subject beyond indicating that the portion of the total cost financed from the government subsidy should depend upon the proportion of the general population covered by the insurance system. In interdepartmental communications it suggested the limitation of the Federal contribution to one-half of payroll tax collections (approximately one-third of benefit payments), even if such a limitation implies eventual increases in payroll taxes above the scheduled 6 percent rate.

Question 8. In case a Federal subsidy is approved, should legislation be immediately enacted providing specific taxes to be collected in the future at such time and in such amounts as will be required for the Federal contribution?

Recommended Treasury decision.

It is recommended that pending a re-examination of the financial provisions of the Social Security Act after 1940 (proposed in Question 5 above), and pending the availability of more information regarding the financial requirements of the old-age insurance system, decision regarding the manner of financing the Federal subsidy be postponed.

A. Affirmative Arguments.

(1) The designation of specific taxes or increases in specific tax rates which will be required for old-age benefits would impress upon the public the cost aspects of old-age insurance.

(2) It would give the workers now paying payroll taxes some assurance that the government's share of the cost of the old-age insurance program will be forthcoming.

B. Negative Arguments.

(1) The earmarking of specified taxes for particular functions interferes with the judicious budgeting of public revenues. Each Congress should be left with discretionary power to determine the relative merits of the various claims for public revenues.

(2) The earmarking of special taxes handicaps the development of individual tax sources. If the income tax, for instance, were earmarked for old-age security, an effective argument would be provided against such future expansion of the income tax for general revenue purposes as may be desirable.

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(3) Designation of a specific tax to be used in the future for old-age insurance does not provide assurance that it would actually be so used. It would be clearly within the authority of any subsequent Congress to repeal or modify any provision a preceding Congress may have made.

(4) Foreign countries in general abstain from the practice of earmarking specific taxes for the government's share of old-age insurance costs and provide that the subsidy be financed out of the general revenues of the treasury.

C. Affirmative Opinions.

D. Negative Opinions.

(1) The Advisory Council's recommendations make no reference to the type of taxes which should be used for the financing of the government's share of old-age insurance cost.

(2) The Social Security Board does not recommend immediate enactment of the tax but indicates its preference for the use of income and inheritance taxes when and if a government subsidy is provided.

Question 9. Should Title VIII and Title IX taxes be combined?

Recommended Treasury decision.

It is recommended that the Treasury Department assist the Social Security Board in developing a practical plan for coordinating Title VIII and Title IX taxes.

A. Various possibilities.

(1) Coverage and specifications under the two taxes may be made more uniform so that information supplied for the computation of one tax would suffice for the computation of the other tax as well.

(2) The two taxes may be physically combined so that both are imposed at one and the same time.

B. Affirmative arguments.

(1) Both taxes are levied on the same base, payrolls. The combining of the two taxes would enable a computation of tax liability under both titles on a single tax return. This would simplify taxpayers' compliance and reduce cost of tax administration in the case of those individuals liable under both titles.

C. Negative arguments.

(1) Some employers are subject to both Title VIII and Title IX taxes on behalf of all their employees. In the case of other employers, however, some employees are covered under one title but not under the other. The making uniform of coverage so that no employer will have some employees covered under one title but not under the other would require more extensive revisions than are warranted by ease of administration and tax compliance.

(2) Standardization of the Federal taxes would not remove variations between them and State-imposed taxes and accordingly the taxpayer would not secure much relief from keeping records on two bases. This will grow in importance with the introduction of State merit rating provisions.

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(3) Title VIII taxes are collected quarterly and Title IX taxes annually with a State tax credit allowable as a deduction. There are also other differences between the laws that might prove difficult of standardization.

(4) Alterations in the scope or structure of Title IX will generally require corresponding alterations in State unemployment insurance taxes.

D. Opinions regarding the coordination of Title VIII and Title IX taxes.

(1) The Social Security Board recommends that the Federal unemployment compensation tax provisions be combined with those for old-age insurance which relate to employers.

Question 10. Should the present reserve provisions be retained?

Recommended Treasury decision.

It is recommended that the Treasury favor the abandonment of the full reserve method of financing, either with or without current financial provision for the accruing reserve liability. It is recommended that the Treasury favor the accumulation of a moderate contingency reserve.

I. The Full Reserve Method

The arguments for and against the full reserve system are somewhat different, depending upon whether current financial provision is or is not expected to be made for the annual appropriations in recognition of the accruing reserve liability. If such financial provision is expected to be made, it will be necessary to raise payroll taxes or other taxes (earmarked or not earmarked) drastically at present or in the very near future. If no financial provision is expected to be made for the accruing liability, the full reserve method of accounting would commit us to formally unbalanced budgets for a generation to come.

Some arguments on each side apply to both concepts of the reserve and some to only one. When an argument applies to only one concept of the reserve this will be indicated, otherwise it may be supposed that the argument applies to both concepts.

A. Affirmative Arguments.

(1) The full reserve method is the only one by which the annually accruing liability under the old-age insurance system is given full recognition within the regular system of appropriation accounting.

(2) The full reserve method of financing, by making the cost of future benefit payments felt in the present, acts as a check on increases in benefit rates.

(3) The full reserve method of financing is based upon the analogy of private insurance company practice and, as such, facilitates public understanding and acceptance of the old-age security program.

(4) The full reserve method of financing will result, for many years to come, in a substantial excess of cash receipts over cash disbursements when the formal budget is exactly in balance, and an equality of cash receipts and cash disbursements even when there is a considerable bookkeeping deficit. This will help the financing problem of the Treasury, and will have a restraining influence upon the economy which under some circumstances may be desired. (This argument is relevant only if financial provision is made for the accruing reserve liability.)

(5) It is argued by some that undersaving is likely to be a serious problem over the course of the next generation. It is argued, in particular, that if old-age security is provided by social action it will increase our need for income-producing capital in the future, while it will, at the same time, decrease the incentive for saving among the lower income classes. The full reserve system is the only one which will provide an adequate volume of annual saving to fill this gap and to provide for the capital needs of our still growing economy and so lighten the burden of paying old-age benefits in the future. (This argument is relevant only if financial provision is made for the accruing reserve liability.)

B. Negative Arguments.

(1) In order to finance Plan AC-14 according to the full reserve method, it would be necessary, upon the basis of the estimates of the Social Security Board, to put into effect immediately a payroll tax of about 2 percent (employer and employee shares combined) in addition to the rates of tax already provided by Title VIII, or to levy other taxes of equivalent present value. The levy of such additional taxes is not economically feasible, and, therefore, the full reserve method of financing must be abandoned. (This argument is relevant only if financial provision is made for the accruing reserve liability.)

(2) The accumulation of a large reserve will encourage the spending of larger amounts by the Government both for old-age insurance and other purposes. (This argument is relevant only if financial provision is made for the accruing reserve liability.)

(3) The restraint to increases in future benefit payments assumed to be provided by the full reserve method of accounting is illusory, since the mathematical requirements of this method may be met as well by the levy of future taxes as of present ones.

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(4) Considering the longer run, the full reserve method of financing, with financial provision for accruing liability, means a substantial excess of cash receipts over cash expenditures for many years to come. It means that many billions of dollars which would otherwise have been devoted to consumption will instead be saved. The real problem of the country in this respect is the excess of attempted savings over available investment opportunities, rather than the reverse as alleged under (5) of Affirmative Arguments. The full reserve method of financing will assure us of a substantial backlog of deflationary influence upon our economy from the old-age insurance system for a generation to come. (This argument is relevant only if financial provision is made for the accruing reserve liability.)

(5) If the full reserve method of accounting is continued without making current financial provision for the accruing reserve liability, it will result in a continuous budgetary deficit for the next generation. It is, of course, by no means certain that this could be carried out in practice, since during this period there would be a constant pressure to "balance the budget". Assuming, however, that a bookkeeping deficit could be deliberately maintained for such a prolonged period, it would be a depressing influence upon business during the entire period of its continuance.

The only reasonable explanation for failure to make financial provision for the accruing reserve liability, while incorporating it in our appropriation accounting, is that such provision is not economically feasible until actual benefit payments are being made. But, if so, why punish ourselves by our bookkeeping? Self-flagellation may have been good for the souls of medieval hermits, but is it good for a modern economy?

C. Affirmative Opinions.

(1) The Treasury Department favored the full reserve method of accounting (with current financial provision) in 1935.

(2) Mr. Riefler, one of the group of economists called to advise the Secretary on social security matters, appeared to lean toward the full reserve method of accounting (with full financial provision) at the present time, although he did not definitely commit himself upon this point.

D. Negative Opinions.

(All of these opinions are irrespective of whether or not current financial provision is expected to be made for the accruing reserve liability.)

(1) The Advisory Council recommended against the full reserve method of financing. While it is possible that Mr. Witte dissented on this point, he made no notation to that effect in the final report.

(2) The Social Security Board, in its report to Congress and the President, recommended the abandonment of the full reserve method of financing.

(3) All members (except Mr. Riefler) of the group of economists called to advise the Secretary on social security matters were in favor of the abandonment of the full reserve method of financing.

II. Contingency Reserve

Assuming that the full reserve method of financing and accounting is abandoned, the question remains whether a contingency reserve should be accumulated. The arguments for and against accumulating such a reserve may be summarized as follows:

A. Affirmative Arguments.

(1) It is desirable, for reasons already stated, to maintain, at least for the time being, the present scale of taxes. It is impracticable, on the other hand, to step up benefits in the early years sufficiently to absorb the difference between the revenues which will be so raised, and the cost of benefits in the early years. The resultant excess of tax collections over benefit payments can best be absorbed by accumulating a contingency reserve.

(2) "... it is desirable to make provision for a contingency fund to insure ready payment of benefits at all stages of the business cycle and under varying conditions resulting from fluctuations in such factors as the average age of retirement, the total coverage under the program, and average wage rates. It is desirable that the payment of benefits should not be dependent upon quick Congressional

action in levying emergency taxes to meet deficits or in sudden raising of contribution rates when disbursements exceed current tax collections or normal appropriations to the system." (Quoted from the Report of the Advisory Council on Social Security.)

(3) The interest on even a small contingency reserve would reduce somewhat the amount of the necessary Federal subsidy in the later years of the system.

B. Negative Arguments.

(1) The excess of tax collections over benefit payments during the years when the contingency reserve is being built up would, taken in itself, be deflationary.

(2) The benefit payments provided by law are "moral" obligations of the United States to the extent that one Congress can or should commit succeeding Congresses. If succeeding Congresses find it in the public interest to be bound by this obligation, they will appropriate moneys for the payment of such benefits in the same manner as for the payment of other Government expenses. If the contingency reserve is meant in some way to bind future Congresses against their will, it is both ineffectual and improper.

C. Affirmative Opinions.

(1) The Social Security Board states in its report to Congress and the President: "The tax provisions embodied in the present law would probably cover the increased annual cost for the first 15 years. They would also probably provide a small reserve, which would be invested and earn some interest."

(2) The Advisory Council on Social Security in its final report states: "The financial program of the system should embody provision for a reasonable contingency fund to insure the ready payment of benefits at all times and to avoid abrupt changes in tax and contribution rates."

(3) The group of economists called to advise the Secretary on social security matters recommended that "... a contingency fund be provided in the new law in lieu of the present full actuarial reserve, and that the amount of this fund should be approximately 3 years' benefit payments during the critical years of the plan (1940-45) and approximately 2 years' benefit payments when the plan is mature. During the years when benefit payments are rapidly growing, the amount of the fund should

be related, not to the amount of the then current year's benefit payments, but to the amount of benefit payments forecast for the next 3 years, assuming normal business conditions."

D. Negative Opinions.

(1) Mr. Hansen, one of the group of economists called to advise the Secretary on social security matters, expressed some reservation with respect to the resolution of the group on the matter of the contingency fund. He did not directly oppose it, however, and might have favored a reserve of smaller amount than that recommended.

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Question 10-A. If the full reserve method of financing is abandoned, what provision should be made for setting forth to Congress and to the public the current status and future commitments of the old-age insurance system?*

Recommended Treasury decision.

It is recommended that, if the full reserve method of financing is abandoned, the Secretary of the Treasury should be required by law to present annually to Congress a memorandum showing forecasts of the cost of benefit payments under the then existing law for decennial years, fifty years in advance, as a ratio of covered payrolls, on the assumption of the wage rates existing at the time of the preparation of each memorandum. Capitalized figures of future benefit payments and of future tax collections should no longer be presented.

A. Arguments in favor of the suggested method of presentation.

(1) A schedule of expected future benefit payments is more intelligible to laymen (i. e., non-mathematicians) than a capitalized statement of the "present value" of an expected series of future benefit payments, or of the excess or deficiency of such "present value" over or under that of an expected series of future tax collections.

(2) Data presented on the basis suggested are also more valuable even to persons accustomed to interpreting actuarial valuations since they are free from dependence upon an assumed rate of interest. It is not valid to push the doctrine of compound interest too vigorously in long-range social planning since compound interest cannot be secured in practice upon large sums and over long periods, due, among other things, to the lack of adequate investment opportunities. To take an extreme example, a fund of one dollar set up today and allowed to accumulate at interest for a thousand years ought to permit the entire population, at the completion of that period, to retire and live on the interest. But would it?

* Question added by Treasury staff.

B. Arguments opposed to the suggested method of presentation.

(1) The suggested memorandum would be just another actuarial report which few persons would read. If the burden of the old-age insurance system is to be really brought home, it must be incorporated in the system of appropriation accounting.

C. Opinions with respect to method of presentation.

(1) The Advisory Council states: "Sound presentation of the government's financial position requires full recognition of the obligations implied in the entire old-age security program and treasury reports should annually estimate the load of future benefits and the probable product of the associated tax program."

(2) The group of economists called to advise the Secretary on social security matters recommended a memorandum in the form here suggested.

Question 11. Should the payroll taxes go directly into a special trust fund?

Recommended Treasury decision.

It is recommended that if, in the opinion of counsel, the proposed change would in any way jeopardize the constitutionality of the Act or of the taxes levied under it, it should not be made. Otherwise the Treasury should not oppose it.

A. Affirmative Arguments.

(1) Such a change would lessen public criticism to the effect that Social Security taxes are being diverted and spent for other purposes.

B. Negative Arguments.

(1) Such a change might render the Act, or important portions of it, unconstitutional.

C. Affirmative Opinions.

(1) The Advisory Council unanimously recommended such a change.

D. Negative Opinions.

(1) Counsel, in 1935, feared that such a provision might endanger the constitutionality of the entire legislation. Subsequent court decisions may have altered this opinion.

Question 12. Should such a (special trust) fund (for the segregation of Title VIII taxes) be managed by a Board of Trustees?

Recommended Treasury decision.

It is recommended that if a special trust fund is established, it should be managed by a board of trustees.

A. Affirmative Arguments.

(1) Management by a board of trustees would further the purpose for which the fund is proposed to be established, i.e., to increase public confidence in the proper use of the proceeds of payroll tax collections.

B. Negative Arguments.

(1) The trustees would have nothing to do. (They could, however, all be regular Government officials serving ex officio.)

C. Affirmative Opinions.

(1) The Advisory Council recommended the management of the fund by a board of trustees.

D. Negative Opinions.

Question 13. Who should be the trustees (of a special trust fund for the segregation of Title VIII taxes)?

Recommended Treasury decision.

This is a matter upon which we do not feel qualified to make a recommendation. Among the persons who would seem logical candidates are the Secretary of the Treasury, the Director of the Budget, the Treasurer of the United States, the Chairman of the Social Security Board, and the Attorney General.

- Question 14. Should the present 3 percent interest rate be eliminated so that outstanding obligations can be purchased?
- Question 15. Should it be required that only outstanding obligations be purchased?

These two questions must be treated together, but divide themselves into the two further questions: (1) Should the fund be guaranteed a 3 percent return? and (2) Should the fund be invested in special issues or outstanding obligations? These two questions can logically be decided separately, as, if the decision should be in favor of guaranteeing the fund a 3 percent rate but of investing it in outstanding obligations, the difference in return might be made up to the fund from the Treasury.

I. Should the fund be guaranteed a 3 percent return?

Recommended Treasury decision.

It is recommended that the fund should be guaranteed a return of 3 percent.

It should be noted that the rate of interest guaranteed to the fund becomes of much less importance if the full reserve method of financing is abandoned and only a small contingency fund accumulated.

A. Affirmative Arguments.

(1) It is only by the use of a definite interest rate that a present value may be set upon future payments. Such a rate must be assumed, for example, to determine the extent to which any individual's annuity has been earned by his own and his employer's contributions, or to compare the present value of a Federal subsidy with that of the proceeds of present and future payroll taxes.

(2) Upon the basis of past experience, 3 percent seems the most reasonable round figure to take for this purpose. It is not too high upon the basis of present rates if the reserve is considered a perpetual loan to the Government.

(3) Even if the 3 percent rate should be considered too high, it merely results in a reduction in the amount of

Government subsidy which would otherwise be necessary. It is just as well that a portion of the Government subsidy be in the form of a guaranteed rate of interest.

B. Negative Arguments.

(1) The whole amount of Government subsidy to the system should be clearly stated as such. It is misleading accounting to conceal a portion of it in the form of a guaranteed rate of interest.

(2) If the full reserve method of financing and accounting should be abandoned, the necessity of a fixed interest rate for use in actuarial computations of the required annual premium is obviated.

C. Affirmative Opinions.

D. Negative Opinions.

II. Should the fund be invested in special issues or outstanding obligations?

Recommended Treasury decision.

It is recommended that the present provisions of law be retained in this respect, -- that is investment in special issues or in outstanding securities should be at the option of the Secretary of the Treasury (or the Board of Trustees if one is set up), subject to the requirement that no securities

may be purchased to yield less than 3 percent. This means, in effect, that all investments must be in special issues as long as no Government securities are obtainable to yield as much as 3 percent.

A. Arguments in favor of investing in special issues.

(1) The use of special issues permits the transactions of the fund to be handled with less disturbance to the securities markets. By means of special issues, the fund can secure interest, commencing immediately after its money becomes available for investment, while the money paid over to the Treasury for the special issues may be used to reduce the amount of refunding of currently maturing issues which would otherwise be necessary. It is a needless disturbance to the bond market for the fund to be compelled by law to purchase outstanding securities, while the Treasury is at the same time selling refunding issues. (Sometimes, of course, the purchase of outstanding issues under such circumstances might be good bond market policy, but it should not be made mandatory.)

(2) If the fund is to be guaranteed a fixed return, this can be handled most conveniently by means of special issues. As previously noted, however, it could also be handled by an over-all subsidy to bring the rate of return on the investments of the fund up to the guaranteed rate.

B. Arguments in favor of investing in outstanding securities.

(1) The investments of the fund would seem more "real" to the public if they were made in previously outstanding securities, rather than in new Treasury "I.O.U.'s".

C. Opinions in favor of investing in special issues.

D. Opinions in favor of investing in outstanding securities.

Question 16. Will the Treasury approve extension of the Social Security Act to cover farm labor and domestic service?

Recommended Treasury decision.

It is recommended that the Treasury Department approve the principle of the extension of coverage under the old-age insurance system to employment in agriculture and domestic service in private homes, but (except with respect to large-scale agriculture) request postponement of such extension until the next session of Congress, to permit further study of the ways and means of overcoming administrative difficulties inherent in the application of payroll taxes to these employments.

A. Affirmative Arguments.

(1) Farm laborers and domestic servants are in the income classes that need most the protection of old-age benefits.

(2) The present and proposed subsidies from the Treasury would be more justifiable if coverage were extended to these groups.

(3) If benefits are increased and speeded up it will be more feasible to bring such groups under the act than has been the case in the past.

B. Negative Arguments.

(1) The extension of coverage to farm labor and domestic service would involve tax collection procedures that would be very expensive in relation to the revenue collected, if anything approaching complete enforcement was attempted.

(2) Under the existing schedule of benefits many taxpayers would probably overpay because of the large subsidy which could be secured by such overpayment.

(3) The persons that underpaid or did not pay at all might, when they reached retirement age, politically force the payment of a free benefit not related to earnings.

C. Affirmative opinions.

(1) The Advisory Council favors bringing agricultural labor and domestic service under the Act by January 1, 1940, if administratively feasible.

(2) The Social Security Board favors bringing laborers in large-scale agriculture under the Act immediately, and domestic servants and the remaining farm laborers after a sufficient lapse of time to work out the administrative problems.

D. Negative opinions.

Question 17. Should specific tables be presented showing the estimated contributions, disbursements, reserves, government subsidy, etc., from now until 1980?

Recommended Treasury decision.

It is recommended that the tables to be presented to Congressional committees in connection with the current hearings should cover the next 40 or 50 years rather than extend specifically to 1980. The use of this date fosters the erroneous impression that the system will reach a mature condition at that time.

A. Affirmative Arguments.

(1) Estimates over a long period of time are necessary to show the magnitude and the problems of the social security program. Short-term estimates, while serving useful purposes, do not present a complete picture and are very misleading.

B. Negative Arguments.

(1) It is impossible to predict with any claim to great accuracy, amounts relating to the distant future, especially when these amounts are dependent upon so many complicated and unpredictable factors.

RE SOCIAL SECURITY RECOMMENDATIONS

February 3, 1939.
11:00 a.m.

Present: Mr. Haas
Mr. White
Mr. Murphy
Mr. Blough
Mr. Reagh
Mr. Duffield
Mr. J. Douglas Brown
Mr. Ecker-Rocz

H.M.Jr: Are these all predigested?

Haas: They were digested night before last, Mr. Secretary, but I don't know how the digestion would feel today.

H.M.Jr: Ever since that fellow put the budget in the meat scales - did you see that - that picture? The budget weighed five and a half pounds. Didn't you see that picture? It said: "The budget this year weighed half a pound more than last year."

Blough: That's weighing your ideas.

H.M.Jr: (On phone) Tell Gaston if he's not very busy to come in, we're doing Social Security.

Ye gods, this is terrible.

Haas: Seventeen questions. The first part of it is just the question and recommended Treasury decision.

H.M.Jr: I'm weak before I start. This is awful.

Blough: I don't think it's as bad as it looks, Mr. Secretary.

Brown: It's good, solid paper.

H.M.Jr: "Should monthly benefits begin in 1940?" I'm not - I'll just ...

(On phone) Hello. - Well, when he's back tell him to come in.

H.M.Jr: "It is recommended that the Treasury should not

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oppose commencing old-age benefit payments in 1940 or increasing their amount in the early years."

Do you want to - how should we work this thing? What would you suggest? I mean that - I mean I've got to be educated as we go along. I mean the answer is here, but why?

Brown: Well, I'd be glad to join in in explaining my

H.M.Jr: Would you?

Brown: ... conclusions on that.

H.M.Jr: Suppose you do that.

Brown: I feel, in the case of beginning in 1940, that there is, of course - it is very important, rather, that the contributory insurance idea be firmly established. Whereas when the Act was passed it was expected that five years should ensue before benefits begin, both to perhaps accumulate funds and to indicate that it was truly contributory, that five years of contributions were not too much to expect of a person getting benefits, since 1935 I feel the idea of contributory insurance has become more widely accepted; at the same time, it is being challenged by various other devices such as the Townsend plan, the General Welfare bill, and various other dangerous programs, and that if the public generally is to be educated and to be kept educated to the idea of contributory insurance, it is sound public policy to commence payments as soon as feasible. And from the Board point of view, they feel, I believe, that it is entirely feasible to begin payments in 1940.

Now, of course, that will be the thin edge - - I mean the numbers coming up actually for benefits in 1940 will be relatively small, but at the same time the educational effect, as well as the general welfare effect, will be considerable.

Now, as far as the benefits being increased in the early years, I feel the benefits called for under the present Act are neither here nor there; that is, they are insufficient to provide for the majority of the people an adequate old-age retirement allowance.

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At the same time, you have, under Title I of the Act and the state assistance programs, assistance grants being paid in many states which are in excess - that is, either to the individual or especially where the individual and the aged wife both receive benefits -

H.M.Jr: Excuse me one second. (Holds conversation aside with Lochhead)

I'm sorry, but I

Brown: Well, under the present schedules of benefits under Title II, it would mean that a very considerable number of people who were without income or considerable savings might both have to take the benefit under the old-age insurance program and also apply for assistance. And the idea of two plans being necessary to take care of the individual and his wife seems to be - well, contrary to sound public policy. So that if the amount of the benefits in the early years could be enhanced sufficiently that a majority of those going on benefits could at least have their basic needs taken care of by those benefits, that would be much preferable.

H.M.Jr: Now - well then, does anybody want to talk on ...

Haas: Mr. Secretary, on each one of these questions, what you're looking at is the summary there, which consists merely of the question and answer. If you look back through that you'll see that we've listed under each question what we thought the affirmative arguments were, the negative arguments, the affirmative opinions, the negative opinions.

Douglas Brown has to a large extent reviewed that for you orally.

H.M.Jr: Pardon me?

Haas: Dr. Brown has reviewed that orally.

H.M.Jr: Has he had a chance to see whether he concurs?

Brown: I haven't had a chance to read other than the summary, Mr. Secretary. So what I've just said is from my own

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- H.M.Jr: Well, what I - we'll do - I'll run as long as I've got, until 12 o'clock, and then if you could spend the balance of the day with these people and tell them where you either agree or differ in your conclusions, and where you differ perhaps it would be done over again.
- Brown: Be very glad to.
- H.M.Jr: I mean this is just the form I want it in. This is the form I should have it in, and they've got their recommendations and you're down here as a consultant, and you can tell them, "This is where we're together and this is where we're not," and then the thing could be rewritten, and keep at it. But they don't seem to be making an awful lot of progress on the Hill, do they?
- Haas: Still working on it.
- H.M.Jr: Do we have an observer up there?
- Blough: I doubt it.
- H.M.Jr: What?
- Blough: I doubt if we do. We should.
- H.M.Jr: Amongst you people, arrange that there should be an observer at all those hearings, see? I mean George, will you see that amongst you three gentlemen sitting there - Reagh, Blough, Haas - arrange it.
- Brown: Is it possible to get the daily record of the hearings?
- H.M.Jr: I don't know. We ought to have it. But you three men ought to get that, you ought to keep digesting it, going over it. And I think there should be an observer there for the three of you. Huh?
- Blough: I very much think so.
- H.M.Jr: Yes. All right, let's go on. Are you (Brown) planning to be here one or two days?
- Brown: Well, today this week and then two days from now on.

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H.M.Jr: And which are the days which are the best for you?

Brown: The middle of the week is best, but I'll do what I can to fit it to whatever is convenient.

H.M.Jr: Tuesday and Wednesday or Wednesday and Thursday?

Brown: Wednesday and Thursday is the ideal.

H.M.Jr: All right, just so they know. And then - and you (Haas) arrange some way of having - going on the Hill; I think it should be very much digested for me and then a copy could be given, mailed as it is digested, or saved until Professor Brown comes down, whichever way he wants, so we can get the feel of where they're going, you see.

George?

Haas: Yes, I'll do that.

H.M.Jr: But you three men - Blough and Reagh and Haas - I'm going to hold you responsible for this. All right.

Brown: Then question 3: "Should the ultimate annual benefit cost of the system be increased, decreased, or kept the same as at present?"

I feel that it should be kept within the ultimate costs under the present system - that is, not to exceed - but that the benefit structure be so designed as to possibly keep slightly under or at the same amount rather than any amount in excess; because that particular figure of 1980 or wherever you want to say - 1980 or 1990 - appeared to be the maximum amount that we as of this time should commit the American people to for this particular plan of protection. There are other types of protection coming along. The public may decide to go in on health insurance; it might decide to go in on disability protection or other types of protection. But as far as old-age insurance is concerned, the future costs involved in any present system should not be in excess of those under Title II of the present Act.

Reagh: I'd like to make one comment on that. Would you

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say that the word "materially" might be added after - "should not be increased materially," because these estimates of what the benefit payments are going to be in 1980, or such dates - can't be estimated except within a margin of error of that kind. There will be some range. And if there was five or ten percent over, I just wonder if you'd throw out a particular program for that reason.

Brown: I'd certainly agree we have to come to a definite conclusion that in planning these future costs there are bound to be variables and that there must be a spread, in other words, and that this particular pegging involved in question 3 can't be stated exactly, but that the - as you suggest, that the ultimate annual cost under any revised plan should be designed so far as is possible not to exceed, and that gives you a certain margin of error, keeping it within the general framework of those future costs.

Blough: Would you notice the last line of this particular recommendation - says "including disability benefits." Would you favor the recommendation with that inclusion?

Brown: Well, the way I'd make that point is that, first of all, I don't think the time is ripe for adding disability benefits now; that - of course, the Advisory Council split on that, and the feeling on the part of one group, of which I was a member, was that in all development of social insurance you have to evolve, and that it takes a certain length of time for the public to understand and to be willing to contribute, either as employers and employees or the Government, to that particular plan as well as take on any new plan. So that my feeling would be that the addition of disability protection should be delayed.

Now, as far as the pegging of costs, it was my reaction that the things we're considering should be pegged within the maximum of the present Act. The Act doesn't include disability protection. The old-age protection now involves a certain figure; old-age protection as revised should come within

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that figure.

Blough: Then you don't

Brown: include disability. No.

Blough: Don't include disability in your thinking.

Brown: I think that's a new issue for the American people to decide: whether they want disability; if so, how much they are willing to pay for it. They have decided they want old-age protection; the idea of the revision is to give them the type of old-age protection which is an improvement over the type they are getting under Title II.

(Gaston comes in)

Well then, shall I go on?

H.M.Jr: If you please.

Herbert, are you all right, can you stay here awhile, or have you got something else?

Gaston: I have a gentleman in my office.

H.M.Jr: Maybe you better take care of him. We're getting along all right. We've got a good memorandum.

(Gaston goes out)

All right.

Brown: Question 4: "Should the step-up in the tax rate in 1940 be maintained?"

It is my belief that it should be, for several reasons. One is that to expand benefits and to hold down taxes at the same time would be unfortunate as a matter of public education as to what contributory insurance involves; that it would be better to proceed with the one and a half percent step-up as of the time that benefits are being expanded.

Secondly, that there are many variables involved

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about which we do not have sufficiently accurate information, and that by some time such as 1941-42, any question of future policy on taxes could be more accurately determined.

Shall I proceed with question 5?

H.M.Jr: Yes, please.

Brown: Question 5: "Does the Treasury Department favor the step-ups in the tax rate after 1940 as provided in the 1935 Act?"

Well, it seems to me that since they are in the Act probably the best procedure is to consider that they remain unchanged as schedules; but at the same time it seems to me sound policy to indicate that, as will always be the case with old-age insurance, there will be revaluations and restudy to determine future tax schedules and future benefit schedules. In other words, if the impression were that the Treasury Department or the Social Security Board were adamant against any future changes, that that is not as sound policy as to say, the present schedules being in the Act, we feel they should remain there but are perfectly willing to see restudies made in future years as to whether they should be changed. Restudies then would be made - one suggestion has been every five years - as well as, of course, continuing studies; but every five years there would be a very definite revaluation of future costs, of future benefits; that is, as of that time it would be normal to make recommendations as to changes in tax schedules.

"Does the Treasury approve having the system partly financed by direct government subsidy from other than payroll taxes?"

My own view is that the whole revision definitely involves a commitment to governmental appropriations to the system. That is, if the benefit structure is to be revised to increase early benefits, holding down future benefits, and if thereby the reserve method of financing is altered, removing the large reserve which is to provide interest to supplement payroll taxes, that there is a commitment

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involved to the principle of Federal contributions to the system. Personally, I feel that that is a very sound principle and one which is justified for many other reasons than the precise method of financing the system.

H.M.Jr: Well, my own thinking isn't clear on that particular one; I mean this idea that there be a third - divide up into thirds. I mean I haven't been able yet to cross that bridge. I'll have to argue about it. But that's one big question I have in my mind.

Brown: That's one of the more important questions.

H.M.Jr: Doesn't that question get into the question of the whole reserve, too?

Brown: Yes.

H.M.Jr: I mean I'm all right - so far, I think for the good of the idea we oughtn't - we ought to go ahead with the tax program as it is. I mean I'm pretty well sold on that. I mean I'm not unsold on account of the deflationary aspects of it - I mean increasing the taxes.

On this question of government contribution and maintaining the size of the reserve, I've got a big question.

Brown: Well, it goes to the very core.

H.M.Jr: You say that goes to the core?

Brown: I think so.

Reagh: That's right, Mr. Secretary.

H.M.Jr: What? Well, those two things - I mean I've got to be educated.

Brown: All right?

H.M.Jr: Huh?

Brown: I - do you want me to give my reasons now on that?

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H.M.Jr: Sure, I'm getting along all right.

Brown: Well, it seems to me that - first I might make this proposition: There is a difference between a commitment in principle and implementation of that by definite appropriations. And in the Advisory Council, for example, the conclusion was unanimous that the principle of government contributions over time was sound, but that on account of the variable factors as to costs of the system of tax collections on the one hand, and the precise structure of benefits and the cost of those benefits, that any implementation of that principle should wait until, say, '41, '42; but if the benefits in the early years are to be enhanced, that those funds must eventually come from somewhere. Now, if they are to come from payroll taxes it will involve payroll taxes considerably more than six percent total. So when the early benefits are enhanced, the issue immediately arises, where are those additional costs coming from? Now if they come from payroll taxes alone - three and three - plus, say, an additional two and two, that would be five percent each, or a total of ten percent. You could get into definite questions of public policy whether such a level of payroll taxes is not dangerous from the point of view of encouraging the displacement of labor.

You are trying to protect labor, but, on the other hand, you are establishing taxes which tend to force employers to avoid employment of more labor. From the employee point of view, it adds a five percent load, we'll say, eventually, which in addition to other social charges, such as unemployment insurance, possibly health insurance, may become excessive. Meanwhile the Government, on its side, is relieving itself to a certain extent of old-age assistance costs and other charges for old people, which previously it paid from general revenue.

Blough: But you don't believe that it is possible to take the position that's taken here, that the Treasury postpone action, since no decision is necessary; you think the other decisions will constitute the decision here whether we want it to or not. Is that it?

Brown: That's right. Let me just try to see it in as

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practical a way as possible. The benefit structure, as a bill or as an offering, is announced. The question immediately arises: This will cost more money than the present structure, at least over a period of years, see, until the eventual costs arrive. In other words, there is a wedge added to the cost of the early years. The next question is, where does that come from? If the answer is it's - we do not say, then the alternatives are two:

They can say, "Do you mean to say that you're adding that to payroll taxes and going to involve yourself in payroll taxes up to five percent each?" Well, if that's the statement, it would certainly be challenged that such payroll taxes are excessive.

Now, the other alternative is future government contributions to the system.

So I would say the better position is to accept the notion of future government contributions to the system rather than to leave it in the air and be challenged that it involves high payroll taxes, because it would be very difficult to defend, I feel, those high payroll taxes. It might well be that you wouldn't enhance early benefits if you knew that it did involve high future payroll taxes.

White:

I think there is a further somewhat similar argument that might be advanced: that that type of tax is definitely bad economically, and since a portion of it at least is passed on in any case, it becomes a general tax. Therefore, the question is not whether the people as a whole shall be taxed or whether the particular beneficiary shall be taxed, but rather, what is the best method that the Government has of raising those funds? If the question is approached that way, I think very few would answer it with payroll taxes. That's a very important argument in favor of a government contribution, it seems to me.

Brown:

In other words, if the government contribution permits the financing of the system to be better matched to your economy, so that you have the taxation of the payroll, you might say, at the lowest

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level, you have the taxation of the employee, then the taxation of the employer, part of which is certainly passed to consumption, part possibly back to labor, but you need a certain third element in there to match that source of revenues to broad ability to pay.

Blough: Of course, I believe, too, that this is something - if you make a decision you want to go off the reserve basis, then the subsidy follows.

H.M.Jr: Off the reserve, then the government subsidy follows?

Reagh: I think it's necessary.

H.M.Jr: One follows the other?

White: It's inevitable.

Brown: It's the two ends of a see-saw.

White: One means the other.

Blough: I wouldn't mean that's inevitable, but it very likely follows as a matter of public policy.

Brown: You could make an assumption that would permit it to be otherwise, but I would say that assumption is so contrary to fact, to probable facts, that you'd probably have to say that it's all the same.

Blough: You mean you think it's simply out of the realm of reasonableness to permit the payroll taxes to go as high as ten percent.

Brown: I do, and I think it's not - the minute that proposition is made it will be carried back to a very realistic question of the present, and it would be a very difficult thing to answer: that you're recommending a form of benefits which involves, say, five and five percent on payroll taxes.

H.M.Jr: All right.

Brown: "In case a Federal subsidy is approved, when should such a subsidy begin?"

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First of all, on the near side, it seems to me that the earliest time such a subsidy might begin would be on - following a time of reconsideration such as in 1941-42, which would come before taxes are raised beyond one and a half percent each. The outside limit of time would be such as is suggested in the Security Board report, which is to await the need for such government contributions following the leveling off of payroll taxes at three percent each.

Personally, I would prefer to see government subsidies come in at an earlier stage than what the Board recommends, and I have argued that out with the Board people, and it was argued at considerable length in the Council. And it seems to me sounder public policy to involve the general taxpayer in costs as a matter of public education and proper sacrifice long before 1960-62, if he's to stand for such a program. It might well be that if you await these long distant times, the taxpayer may become accustomed to having a schedule of benefits to which he is not contributing directly and then as of that time begin to resist, and cause a change in your system adverse to a fair schedule of benefits.

So my own thinking so far is that, as far as the implementation of a government subsidy principle - that it will not become an immediate issue until 1941-42, as to timing, but that following that, looking forward, that it might be preferable as public policy to bring in that contribution earlier than what the Board recommends.

Reagh: Incidentally, the Board's recommendation results in a subsidy in 1969, according to these estimates.

H.M.Jr: You mean that's when it would start?

Reagh: Yes.

H.M.Jr: In '69.

Reagh: '69; that is, allowing the present scale of tax rates to remain in effect, probably.

Blough: No, I'm sorry, that

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- White: The benefits will be increased before that, so I think that much of that discussion is academic.
- Blough: I'm sorry, this contemplates using up all the reserve; the report wouldn't contemplate all that in its recommendation. This would bring the contribution in in 1955.
- Reagh: That's true. Mr. Blough points out the Board recommended that the reserve not be used after it reached a maximum point.
- Brown: But in any case be a matter of some twenty years or more.
- Reagh: Be about '56 - yes, 1956.
- Brown: I think there is a very considerable opinion on the part of various groups in the public - that is, employers and trade people and others - that these step-ups in taxes should be leveled off sooner, than three and that government contributions be brought in sooner, because meanwhile you have other costs, you have health insurance, if it should develop, disability if it should be added; your unemployment insurance scheme is still in the experimental stage. Therefore, this concept of a three-way division earlier would give a better balance of protection against old age as over against other lines of protection.
- White: Isn't there likewise a theoretical justification for a government contribution on the ground that that is exactly what social insurance implies: that there is a responsibility on the part of the government as a whole. That's what justifies the title "social insurance" being applied to a system designed to be more comprehensive than any system of private insurance; that there is a responsibility that the government has for it, and it would take this form of early contributions here.
- Brown: I would certainly go along with that a hundred percent, because both from the point of view of social policy in this country now and also going back with the precedents in foreign countries, you do have the concept that social insurance is made

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more universal, more flexible, in meeting the needs of your community than private insurance, and that one of the principal reasons is that the government comes in not merely on administration, but also on financing.

Haas: That would mean, though - I mean this argument holds provided you have a broad coverage.

Brown: I would say that the argument as to relationship between coverage and government contribution is fair up to a point, but you can always raise the answer if it is carried to too extreme a point, such as precise timing and so on, that persons not now covered are receiving a hundred percent protection - what they get on a different basis is a hundred percent protection from the government alone; so that, while in the contributory old-age insurance they are not being protected if they are, say, domestics and farm labor, for the time being, of course, they may be protected long before a government contribution amounts to much, and in any case during the intervening time they are being protected under another form of government contribution.

Haas: But it involves the means test.

Brown: It involves the means test. But I think that - it isn't a hundred percent logic, but it's a very practical question.

H.M.Jr: All right.

Brown: "In case a Federal subsidy is approved, what should be its relative magnitude?"

I feel that while in the long run certainly the three-way split is the logical basis, that that does not necessarily mean a precise balancing three ways, especially during the earlier stages of the development of your system; that one reason for bringing in the government subsidy much earlier, say, than what the Board calls for, is to get toward something approximating a three-way split before - well, time out of mind or Kingdom Come or whatever those years are.

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White: I think that's one point where the Treasury might well afford to be very conservative. It isn't going to make any practical difference and it will make quite a little psychological difference, with so much deficit in prospect anyhow, so much expenditure in prospect anyway, that if once the principle of contribution is established, I think at that point, if the Treasury is called upon to make any recommendations, it ought to be as small as possible, in view of the general situation.

Brown: I would certainly say it would be sound not to establish a principle of three-way division as any precise accurate logic; that in the case of any plan of government contribution, the implementation, which is the thing that involves the precise arrangements as to the split, would certainly not come before 1941-42 anyway, if such recommendations as these are involved.

Question 8: "In case a Federal subsidy is approved, should legislation be immediately enacted providing specific taxes to be collected in the future, at such time and in such amounts as will be required for the Federal contribution?"

It seems to me that that is something certainly to be postponed and that the question of implementation of this principle in general is to be postponed; therefore, all the more any consideration of precise financing of such a subsidy. And personally I feel that, whatever the Government contributes to social insurance, the source of those funds is definitely a matter of broad fiscal policy and that there should not be any rigidity placed upon the Treasury as to how it should develop those funds, so to speak, to be provided for social insurance.

Then: "Should Title VIII and Title IX be combined?"

I would certainly go along with the answer there; that anything which can be done to simplify the work done by the employer in reporting on taxes for Social Security is to the advantage of the Government generally and particularly to the advantage of social insurance programs.

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Then: "Should the present reserve provisions be retained?"

I would say no, and that of course fits in with this 6 and 7.

Then question 11: "Should the payroll taxes go directly into a special trust fund?"

I believe that they should. I feel that a very important part of that is psychological.....

H.M.Jr: Yes...

Brown: and that it is in order to educate the public as to what contributory social insurance involves and that certain techniques might be developed to establish on a basis of a permanent appropriation the placing of these funds in a special trust fund.

White: It would be a very valuable and important power if the Treasury had - and possibly they have already; I'm asking the question - the power to sell the obligations represented in that special fund, as well as buy them, should the need arise. Does the Treasury have that power?

Brown: I'm afraid I couldn't answer that.

Reagh: They have to be - they can't sell the special certificates that are in the fund; have to make a new certificate.

Brown: In other words, for the time being it's only a

Reagh: They're only specials.

Brown: They're only specials. Therefore it's a theoretical question. But should they purchase from the general market under the restrictions of the Act, I suppose it would involve the power to sell and repurchase other securities, so long as the restrictions of the Act were met.

Blough: It is definitely provided in the law that they may sell them.

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White: It becomes an open market power that exceeds - will soon exceed, might soon exceed - that possessed by the Federal Reserve Board.

H.M.Jr: They can sell those?

Murphy: Specially provides that "any obligations acquired by the account, except special obligations issued exclusively to the account, may be sold at the market price."

Reagh: Of course, nothing but specials are in there yet, so they can't sell those.

Haas: But even if they sold them and got cash back in the account, the Treasury would have to make up the three percent which they lose in interest.....

White: They could make up the interest; couldn't keep it in cash.

Haas: ... until they have a higher yield.

White: Some day that may be quite important.

Brown: I would say, sir, that might be all the more reason for not having that fund too large.

Blough: Then it goes on to say: "Special obligations may be redeemed at par plus accrued interest." So they could get their money at any time.

White: May be redeemed at the Secretary of the Treasury's desire.

Murphy: Yes, and the general market obligations sold - they could only be acquired in the first place if they yield three percent.

Brown: Well, certainly a question would arise as to the carrying on of such operations, as to whether a Board of Trustees was empowered to so act or that the Treasury be entire fiscal agent, so to speak, and that a Board of Trustees be merely a safeguarding or reporting agency, reporting, say, once a year, to someone - Congress, say - that funds were intact.

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- White: If this is going to come up for revision, you might wish to examine that with such alterations as may be called for to provide a monetary weapon that might be extremely important some time.
- H.M.Jr: Good point. Don't tell the Federal Reserve about it; they'll grab it away from me. If anybody wants to get dizzy, look at the chart of the Federal Reserve Board on bank controls. Off on the side there they give me a lot of stuff, just hand it all to me as Secretary of the Treasury - fiscal, monetary policy - I have the whole policy.
- Brown: "Should such a special trust fund for the segregation of Title VIII taxes be managed by a Board of Trustees?"
- I feel that there should be a Board of Trustees somewhat similar to British precedent which would serve ex-officio, or it might be added to by two or three others; but that certainly a small Board of Trustees standing before the public in a, you might say, broad fiduciary capacity, certifying that these funds were what they're supposed to be, is educational.
- White: I should like to register a definite objection to that. I think that it should be exclusively under the control of the Secretary of the Treasury because of its magnitude and importance.
- H.M.Jr: You might - this might be a place to put ex-Presidents of the United States as trustees.
- White: All right. There aren't many of them.
- Murphy: You may not on occasions have any.
- Haas: That would be all right.
- H.M.Jr: And so what?
- Murphy: There have been times
- White: That's why it's a good plan.
- H.M.Jr: Thanks, Henry, for helping me out.

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Blough: Dr. Brown,

Brown: Yes, sir.

Blough: You will notice in the recommendation under question 11 it is pretty strong that if there is any constitutional question we'd better not tamper with this problem of the Board of Trustees - if there is any constitutional question there that might throw out the whole system because the taxes were tied up with the expenditures. What's your thought on that, if I may ask?

Brown: Not being a lawyer, I went to the best - the man I thought knew quite a bit about it - Rozansky. I worked with Rozansky a bit, good bit, in defending - building up a case to defend the law. While I wouldn't want to commit him at all, I think he would say that the law was - the precedent was sufficiently clear that it would not be dangerous. Now, it's a question of the degree of danger. Perhaps you would only do it if it were 99 percent safe. You might not be willing to risk it. But I would say it's a question of the degree of risk you would be willing to take, and from my own personal point of view, not being a lawyer and having to listen to the advice of lawyers, I would say that the risk is relatively so slight and the advantages so great, relatively, that personally I feel it is a risk well worth taking.

Blough: And you - yet you're going to abolish the big reserve anyway, so what's the advantage?

Brown: You mean of trustees?

Blough: Uh-huh.

Brown: As I said before, I would say a large part of that advantage is psychological, in order to implement in the minds of the public what social insurance is; that is, that taxes are collected and benefits paid from those taxes, and that meanwhile there is a contingent reserve and that contingent reserve is definitely defined in some way, not as an account in the Treasury but as a fund. Well, how does the

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public know it's a fund? Well, by setting up some arrangement....

White: Aren't you exaggerating the significance and the importance of that type of educational work, or the necessity for its existence? Won't they soon forget it? Will they be interested in it? If this thing works out year after year, they take that for granted just as much as, I imagine, the Government employees, who haven't got the slightest idea who the trustees for their fund are - most of them.

Brown: I'm afraid I would say that I do feel that when employees throughout the country are going to depend as of age 65 for an important part of the financing of the remainder of their life from funds provided under social insurance, that they'll have increasing interest in the mechanism that provides those funds.

Now, in talking around a good deal with people, with workers and others, as I was saying a while ago, I find that they don't worry so much about sizes of funds but there has been a great deal of newspaper talk about diversion and that's the thing that seems to click in their mind.

Reagh: They wouldn't get much satisfaction, though, out of a three billion dollar fund when they know that that amount is relatively negligible compared to ...

Brown: As I say, I don't think they worry so much about the sizes as they worry about the mechanism itself. And the man in the street - most men in the street have been in lodges, they've had experiences of various sorts. Now, to them, the embodiment of security of funds is in the arrangement that makes those funds secure; that there is auditing, that there is so and so and so and so. Well, I would say this Board of Trustees is symbolic of the notion that these funds are

Blough: You don't think they'll worry whether the trustees loan the money to the Government and the Government spends it.

Brown: I'd like to ask you, how many men in the street understand when a fund is invested, anyway?

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Reagh: That's - they don't, that's quite obvious.

Brown: Then you have to give them a symbol, and this is a symbol.

H.M.Jr: Now where are we?

Brown: Well

H.M.Jr: Which number?

Brown: 9 or - no.

White: 13.

Haas: We're on 13.

Brown: I jumped over; I guess I was looking at the wrong page.

Haas: Recommendations for the job.

Brown: "Who should be trustees of a special fund for the segregation of Title VIII taxes?"

My mind certainly is not clear as to the precise set-up. I feel that certainly at least three ex officio officers of the Government - the two that come first in your mind are the Secretary of the Treasury and the Chairman of the Social Security Board, with the possible addition of the Chairman of the Federal Reserve Board, or someone else associated with the financing side of government.

Then the question of how much more, if any; if there should be two additional persons, they should in some way implement the notion possibly of the employer interest and the employee interest. Or you might - personally I'd rather avoid the notion of political interests. One suggestion has been that they represent, you might say, leaders on the Hill in some way. But personally I think that, say, three ex officio officers of the executive branch of government might be sufficient.

H.M.Jr: I think this - it's not important.

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Brown: Well, then: "Should the present 3 percent interest rate be eliminated so that outstanding obligations can be purchased? Should it be required that only outstanding obligations be purchased?"

I'd say no on both counts. It seems to me that the present 3 percent arrangement is justifiable and that the flexibility of being able to purchase either special 3 percents or purchasing outstanding securities to yield 3 percent or better seems a reasonable arrangement.

"Should the fund be guaranteed a 3 percent return?"

White: May I register opposition to that in passing?

H.M.Jr: Yes, let's pass it.

White: I want to register opposition to it in passing.

H.M.Jr: When it goes to the court, you want to be noticed.

Brown: I might say, Mr. Secretary, I feel extremely dogmatic, and I'll say that this is a rather - coming in cold, and I want to discuss all these things.

H.M.Jr: All these things. This is the most peaceful meeting of experts I have ever had. They've all got on their good manners. They don't know you very well. Wait until you get to know them; they're an awfully nasty bunch.

Brown: I was going to say, I haven't been in any academic surroundings where I've got away with as much as this.

H.M.Jr: They've just got on their company manners.

Brown: "Should the fund be guaranteed a 3 percent return?"

I would say yes. I feel that the long-run planning of the fund from the social insurance point of view, with the necessary estimating of costs, etc., and as a proper function of government in providing security to its people that the guaranty of a 3 percent return is reasonable."

Then II: "Should the fund be invested in special

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issues or outstanding obligations."

I have already answered that; I would say in both.

Question 16: "Will the Treasury approve extension of the Social Security Act to cover farm labor and domestic service?"

My feeling is that that's sound public policy - to have such extension - but on account of the administrative problems involved it should not be rushed, and that there be adequate planning to prevent unfortunate breakdowns or abuse or too small a proportionate tax enforcement. But on the other hand, delay cannot be so long as to wait for a perfect system; in other words, the way to begin, after a certain amount of planning is done, is to begin. But there is much to be learned, of course, from other countries.

Question 17: "Should specific tables be presented showing the estimated contributions, disbursements, reserves, government subsidy, etc., from now until 1980?"

It seems to me that as far as possible the sacred number of 1980 should be avoided, but that estimates be in terms of flows; that is, as suggested here, of future incomes, future disbursements, resulting reserves, and especially interpreted in terms of payroll tax costs, which I think are the most understandable figure to the public.

Reagh: I would say, rather than 40 or 50 years, that the logical point to which to extend such estimates would be that point to which they can be reasonably assumed to increase; what would happen thereafter one couldn't state. But that would be approximately 40 or 50 years; I assume they increase until that time, then be expected to remain level thereafter.

Brown: I would say it's a moving platform into the future, and unfortunately the public has got it very much imbedded in its mind that 1980 is some very important turning point in the whole system.

H.M.Jr: Well, I think what we're doing - I think, first

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place, the Treasury experts have certainly cleared their thinking a lot, haven't you? And I'm beginning to learn a little bit about it - not much. I've got to do a lot more work, and this whole question - I mean I haven't - it hasn't sunk in enough on me that I can express myself. I mean as to the reserve question, whether we should use the reserve or whether we shouldn't - I mean that it's a good or bad thing, looking ahead 40 or 50 years.

But I think we're making progress. I'm pleased. I think if you gentlemen could make the best use of Professor Brown's time today and continue this thing; I would certainly work with him while he's here and get the thing in shape. And arrange to have somebody on the Hill, arrange to get the testimony down.

Brown: I want to say, Mr. Secretary, I am very anxious to learn all I can through discussion with the various persons here. And of course, I have views that I have worked on for some time, but at the same time I am very anxious to discuss those with persons here ...

H.M.Jr: Well, these men

Brown: ... and learn all I can from the Treasury point of view.

H.M.Jr: Well, these men, with the exception of White, are available for the balance of the day.

Policy Questions on Social Security
Submitted to the Secretary
of the Treasury by
Chairman Altmeyer

- Question 1. Should monthly benefits begin in 1940?
Question 2. Should benefits be increased in the early years?

It is recommended that the Treasury should not oppose commencing old-age benefit payments in 1940 or increasing their amount in the early years.

- Question 3. Should the ultimate annual benefit cost of the system be increased, decreased, or kept the same as at present?

It is recommended that the Treasury should insist that the ultimate annual cost of the revised system, as a percent of covered payrolls and including all types of benefits (including disability benefits), should not be increased.

- Question 4. Should the step-up in the tax rate in 1940 be maintained?

It is recommended that the Treasury Department take the position that the 1940 step-up in payroll taxes should go into effect as provided in the existing law.

- Question 5. Does the Treasury Department favor the step-ups in the tax rate after 1940 as provided in the 1935 Act?

It is recommended that the Treasury Department take the position that the rate structure of Title VIII taxes after 1940 be not altered since there will be time enough after the 1940 rate step-up to restudy the problem and arrive at a more mature decision.

- Question 6. Does the Treasury approve having the system partly financed by direct government subsidy from other than payroll taxes?

It is recommended that the Treasury Department postpone taking action since no decision is necessary at this time.

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Question 7. In case a Federal subsidy is approved, when should such a subsidy begin?

It is recommended that the Treasury Department take the position that, since no immediate need for a subsidy exists, and in view of the recommendations made on other questions, no subsidy be introduced in the near future.

Question 7-a. In case a Federal subsidy is approved, what should be its relative magnitude?

No decision is necessary at the present time.

Question 8. In case a Federal subsidy is approved, should legislation be immediately enacted providing specific taxes to be collected in the future, at such time and in such amounts as will be required for the Federal contribution?

No decision is necessary at the present time.

Question 9. Should Title VIII and Title IX taxes be combined?

It is recommended that the Treasury Department assist the Social Security Board in developing a practical plan for coordinating Title VIII and Title IX taxes.

Question 10. Should the present reserve provisions be retained?

It is recommended that the full reserve method of financing should be abandoned.

Question 11. Should the payroll taxes go directly into a special trust fund?

It is recommended that if, in the opinion of counsel, the proposed change would in any way jeopardize the constitutionality of the Act or of the taxes levied under it, it should not be made. Otherwise the Treasury should not oppose it.

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Question 12. Should such a (special trust) fund (for the segregation of Title VIII taxes) be managed by a Board of Trustees?

It is recommended that if a special trust fund is established, it should be managed by a board of trustees.

Question 13. Who should be the trustees (of a special trust fund for the segregation of Title VIII taxes)?

This is a matter upon which we do not feel qualified to make a recommendation. Among the persons who would seem logical candidates are the Secretary of the Treasury, the Director of the Budget, the Treasurer of the United States, the Chairman of the Social Security Board, and the Attorney General.

Question 14. Should the present 3 percent interest rate be eliminated so that outstanding obligations can be purchased?

Question 15. Should it be required that only outstanding obligations be purchased?

These two questions must be treated together, but divide themselves into the two further questions: (1) Should the fund be guaranteed a 3 percent return? and (2) Should the fund be invested in special issues or outstanding obligations? These two questions can logically be decided separately, as, if the decision should be in favor of guaranteeing the fund a 3 percent rate but of investing it in outstanding obligations, the difference in return might be made up to the fund from the Treasury.

I. Should the fund be guaranteed a 3 percent return?

It is recommended that the fund should be guaranteed a return of 3 percent.

II. Should the fund be invested in special issues or outstanding obligations?

It is recommended that investment in special issues or in outstanding securities should be at the option of the Secretary of the Treasury (or the Board of Trustees if one is

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set up), subject to the requirement that no securities may be purchased to yield less than 3 percent. This means, in effect, that all investments must be in special issues as long as no government securities are obtainable to yield as much as 3 percent.

Question 16. Will the Treasury approve extension of the Social Security Act to cover farm labor and domestic service?

It is recommended that the Treasury Department ask for a postponement of the application of the Act to these groups of employees while it engages in active study of ways and means of overcoming difficulties inherent in the administration of taxes with respect to them, with a view to reporting at the next session of Congress.

Question 17. Should specific tables be presented showing the estimated contributions, disbursements, reserves, government subsidy, etc., from now until 1980?

It is recommended that such tables be presented covering the next 40 or 50 years rather than extending specifically to 1980. The use of this date fosters the erroneous impression that the system will reach a mature condition at that time.

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- Question 1. Should monthly benefits begin in 1940?
Question 2. Should benefits be increased in the early years?

Recommended Treasury decision.

It is recommended that the Treasury should not oppose commencing old-age benefit payments in 1940 or increasing their amount in the early years.

These two questions must be discussed together.

A. Affirmative Arguments.

(1) The social need for old-age security is immediate. No annuities may be paid under present law, however, until January 1, 1942 and the annuity which would be payable to a person retiring on that date, who had been in covered employment at an average salary of \$150 per month during the entire period of the Act, would be only \$20 per month, and this sum would not be increased if he had a dependent wife. To meet social needs, it is necessary that monthly benefits begin as soon as possible and be increased in the early years.

(2) The administration of the tax provisions of the Act would be made easier if benefit payments are begun in 1940 and are larger in the early years. Employees would be more interested in seeing that the proper taxes are paid upon their behalf by their employers and by themselves if the value of coverage under the Act is brought home to them by the actual payment of worthwhile benefits to someone they know.

(3) The old-age insurance benefits provided under the present law will, for many years, in the case of married couples in many States, be less than the non-contributory old-age assistance which they could receive under Title I. Increasing the amount of benefits in the early years will result in a better balance between the non-contributory old-age assistance and the contributory old-age insurance programs. Not all of the cost of the increased old-age insurance benefits will be additional, as there will be some decrease in the cost of old-age assistance.

(4) There is considerable political pressure for the enactment of an extravagant old-age pensions system of the

Townsend type. Unless the existing old-age insurance system is liberalized, the whole matter of old-age security may be taken out of our hands and placed upon a basis certain to result in ultimate collapse, thereby discrediting the entire idea of providing for old-age security through social action.

B. Negative Arguments.

(1) According to Social Security Board estimates, the cost of Plan AC-14 without disability benefits, is about 40 percent higher (present value) than the cost of the benefits provided under existing law. This increase arises entirely from commencing benefit payments sooner and paying more in the early years, as the ultimate level of benefit payments as a percent of covered payroll is expected to be no higher under Plan AC-14 than under present Title II. This increased cost will involve either a substantial increase in payroll taxes effective immediately, a greater increase in these taxes effective in future years than at present contemplated (to a level higher, in many cases, than private insurance company rates), or a large Government subsidy in later years. Any one of these alternatives is bad. The present benefit schedule should, therefore, not be tampered with.

(2) The proposed changes will greatly weaken the (already weak) "contributory" character of the present old-age insurance system, that is, they will make the relationship between each individual's contribution and his benefit relatively slight, at least for many years to come. This will remove one of the important checks to unlimited demands for further increases in benefits which exists in some measure in the present law.

(3) Commencing benefit payments in 1940 and increasing their amount in the early years will mean that most of the annuities paid for many years to come will not have been earned in any substantial part by the contributions of the annuitants and their employers. It is intellectually dishonest to pay unearned benefits of this character on the basis of "ceremonial" contributions, while denying annuities-as-of-right to the unemployed present aged, whose need, on the average, is greater, and whose contributions, for practical purposes, are as great as those of the persons who will receive annuities.

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C. Affirmative Opinions.

(1) The Social Security Board supports these proposals in its report to Congress and the President.

(2) The President specifically endorsed the Social Security Board's proposals in these respects in his message of transmittal, stating: ". . . The report suggests a two-fold approach which I believe to be sound. One way is to begin the payment of monthly old-age insurance benefits sooner, and to liberalize the benefits to be paid in the early years. . ."

(3) The Advisory Council on Social Security also endorses both proposals in its final report. There was no dissent in the Council with respect to either proposal.

D. Negative Opinions.

Question 3. Should the ultimate annual benefit cost of the system be increased, decreased, or kept the same as at present?

Recommended Treasury decision.

It is recommended that the Treasury should insist that the ultimate annual cost of the revised system, as a percent of covered payrolls and including all types of benefits (including disability benefits), should not be increased.

It is understood that increasing the coverage will increase the annual cost of the system both in dollars and as a proportion of the national income, but this is not considered an additional burden as long as the coverage is increased proportionately. In the following discussion, therefore, the ultimate annual cost is taken as a percent of covered payrolls.

A. Arguments in favor of an increase in total benefit cost in the later years.

(1) It is argued by some that the present scale of benefits, even in the later years, is not adequate and ought, therefore, to be increased. This is particularly urged with respect to permanent disability benefits, and it has been the position of both the Social Security Board and the Advisory Council that, if such benefits are to be included, their cost should be additional to that of the present system, even in the later years. These additional costs, it is generally supposed, can be taken care of by taxation "in accordance with ability to pay".

B. Arguments in favor of a decrease in total benefit cost in the later years.

(1) The present system involves an ultimate cost estimated at between 10 and 15 percent of covered payrolls. This is too high, and may be a larger proportion of future national income than can be canalized through the national Government for a single purpose without endangering its solvency. The next generation will know more, both about its own resources and what it wants to do with them than we do; and we should not tie its hands. Benefits should not be lightly promised on the basis of anticipated national income alone, as there

is a bad transfer problem involved in collecting a large proportion of this income as taxes, and the resultant friction may decrease the amount of the income itself.

C. Arguments in favor of keeping total benefit cost in the later years the same as that contemplated in the present law.

(1) The cost of the benefits provided by present law has no particular sanctity, and is subject to a wide error of estimate. Despite this error of estimate, it provides a convenient basis for comparison with the costs of other proposals; as, by the use of common assumptions, the same error of estimate may be made to apply, in large part, to both the present law and the proposed variations. It is always easy to increase commitments, but hard to reduce them; and while, in view of the temper of the times, it seems impracticable to reduce our future commitments with respect to old-age security at the present time, it would seem unwise to increase them.

D. Opinions in favor of an increase in total benefit cost in the later years.

(1) Mr. Presseman, representing the CIO viewpoint in the Advisory Council, opposed any reference to ultimate cost in the Council's report. His intention was clearly that this cost should be increased.

(2) The Advisory Council's report did not take a definite position on the immediate institution of disability benefits, the report stating that some members favor this while others oppose it. The entire Council agreed, however, that such benefits should be instituted ultimately, and that their cost should be additional to the ultimate cost of the present program.

(3) The Social Security Board did not take a definite position in its report with respect to the immediate institution of permanent disability benefits. The report states, however, that, if such benefits are included, they would raise the cost of the system in later years above that contemplated by present law.

E. Opinions in favor of a decrease in total benefit cost in the later years.

F. Opinions in favor of keeping total benefit cost in the later years the same as that contemplated in the present law.

(1) The Advisory Council recommended that "The eventual annual cost of the insurance benefits now recommended, in relation to covered payroll and from whatever source financed, should not be increased beyond the eventual annual disbursements under the 1935 Act". As previously noted, however, disability benefits, if any, would be in addition to this amount.

(2) The Social Security Board states in its report: "When the System is fully matured, its eventual cost with the changes here recommended . . . would be somewhat less than the cost of the present system . . . If permanent total disability insurance should also be included, the eventual cost, when the system is fully matured, would be somewhat more than the present system." In view of the attitude of the Board, as determined by personal discussion, this opinion is listed with those in favor of keeping the ultimate cost the same as contemplated in the present law rather than as in favor of a decrease in ultimate cost.

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Question 4. Should the step-up in the tax rate in 1940 be maintained?

Recommended Treasury decision.

It is recommended that the Treasury Department take the position that the 1940 step-up in payroll taxes should go into effect as provided in the existing law.

A. Affirmative arguments.

(1) Public understanding of the fact that the old-age benefits program involves a heavy tax burden would be undermined by failing to increase taxes, as provided in the 1935 Act. The argument is especially pertinent if benefits are increased at the present session of Congress.

(2) If a contingency reserve is not built up in advance on the momentum of the 1935 Act tax rates, it will probably not be built up at all, because of the powerful incentives on Congress not to increase taxes.

(3) The pressures for high expenditures and against increased taxes are so great that the improvement in the fiscal position of the government through the automatic increase in the payroll taxes should not be abandoned.

(4) The necessity for financing from the general budget will be postponed.

(5) These taxes are part of a contributory system and their character should not be altered by requirements of the government's general financial policy which may be temporary.

B. Negative arguments.

(1) The effect of collecting more in payroll taxes than is paid out in benefits is deflationary and increases the "deficit spending" in the general budget necessary to produce the desired net contribution to buying power. The argument is less significant if cash benefits paid in 1940 should be substantial.

C. Affirmative opinions.

- (1) The Social Security Board favors the step-up in 1940.
- (2) The majority of the Advisory Council favors the step-up in 1940.
- (3) The group of economists called to advise the Secretary on Social Security matters, with the exception of Professor Hansen, favors the step-up in 1940.

D. Negative opinions.

- (1) Professor Hansen, together with others making up a small minority of the Advisory Council, does not favor increases in payroll taxes in 1940.
- (2) The Chairman of the Federal Reserve Board does not favor increases in payroll taxes in 1940.

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Question 5. Does the Treasury Department favor the step-ups in the tax rate after 1940 as provided in the 1935 Act?

Recommended Treasury decision.

It is recommended that the Treasury Department take the position that the rate structure of Title VIII taxes after 1940 be not altered since there will be time enough after the 1940 rate step-up to restudy the problem and arrive at a more mature decision.

A. Affirmative arguments.

(1) If the full reserve system is to be continued as provided in the 1935 Act it is necessary for the step-ups in the tax rate after 1940 to take place as scheduled. (If additional benefit payments are provided even greater rate step-ups would be required.)

(2) If the full reserve system is to be abandoned but a substantial contingency reserve is to be built up, at least some of the scheduled rate step-ups will be necessary. The number of rate step-ups that may be postponed will depend on the volume and timing of additional benefits which may be provided.

(3) Certainty that payroll taxes will actually reach the scheduled maximum and that the general treasury will not have to bear a very large part of the total cost of benefits can best be achieved by not disturbing the existing rate schedule.

(4) Beneficiaries under the old-age insurance system will be more nearly assured of benefit payments in future years if their contributions are substantial in the early years since thereby they build up an equitable claim to benefit payments.

(5) It is too early at this time to decide whether or not the step-ups in tax rates should continue as provided in the present scale. Accordingly any change in the future schedule should be postponed until more experience is available for making a decision.

B. Negative arguments.

(1) Stepping up the tax rates after 1940 according to the present schedule would have a continued deflationary effect for a considerable number of years until the benefit payments exceed tax yields.

(2) Since in the early years the reserve would be built up at a rapid rate, some of the objections raised to the full reserve system would apply. Even if benefits are increased as proposed, the reserve would be built up for 10 or 15 years.

C. Affirmative opinions.

(1) The Social Security Board appears to favor the fulfillment of the scheduled rate step-ups until the rates reach the maximum provided in the present law.

D. Negative opinions.

(1) The Advisory Council favors the study of tax rates in 1941 with a view to revision of policy if found desirable.

(2) The general sentiment of the five economists advising the Secretary of the Treasury on old-age insurance was to the effect that the size of the contingency reserve and other factors should determine the tax rates and that accordingly, there should be no automatic acceptance at this time of the increases provided in the present law.

Question 6. Does the Treasury approve having the system partly financed by direct government subsidy from other than payroll taxes?

Recommended Treasury decision.

It is recommended that the Treasury Department postpone taking action since no decision is necessary at this time.

A. Affirmative arguments.

(1) Since the nation as a whole would benefit from a system of old-age security, parts of the cost of such a program ought properly be borne by the nation as a whole. Provision of old-age security is now recognized as a general governmental responsibility similar to other public services financed from general revenues.

(2) Payroll taxes which would be required to finance the projected scale of old-age benefits would be very high and would severely undermine the standard of living of workers whose wages are insufficient to provide savings for old-age security.

(3) The old-age security program will eventually replace in part other welfare activities, notably public assistance and general relief, which would otherwise have to be financed from general revenues.

(4) The provision of a government subsidy would forcefully call to the attention of the American people that Title VIII taxes plus interest on the reserve will not fully finance the liabilities which are likely to accrue in connection with an insurance system. It would therefore serve to restrain further increases in benefits. (However, see B-3 below.)

(5) Governmental participation in the financing of a social insurance program has long been accepted as sound public policy in other countries.

(6) If a pay-as-you-go system is adopted, a subsidy would be indispensable, for in its absence the required payroll taxes would have to be very high and individuals could purchase less expensive old-age security from insurance companies.

B. Negative arguments.

(1) Pending the extension of coverage to include substantially all gainfully employed, it is doubtful whether, on ground of justice, a governmental subsidy is defensible. Such subsidy would have to be paid from general revenues contributed by all taxpayers for the benefit of a restricted group of workers, which is already subsidized by the public at large, in part by the payment of artificially high yields on the reserve and in part through the shifting of the incidence of the tax on employers. (However, it is probable that even under present coverage 75 or 80 percent of gainfully employed will be eligible for benefits by the time they reach old age.)

(2) The provision of a direct government subsidy for old-age security would become a heavy drain upon the Treasury.

(3) The financing of benefits from payroll taxes serves as a restraint on expenditures. The removal of that restraint and the precedent for providing general revenues for old-age security may encourage raids upon the Treasury for increasingly larger contributions and benefits. (However, see A-4 above.)

(4) A program financed entirely by payroll taxes would be more acceptable to those who disapprove of public assistance and believe that security for old age should properly be provided by individual initiative.

C. Affirmative opinions.

(1) The Advisory Council recommends that the system be supported one-third by employee, one-third by employer and one-third by the government.

(2) The Social Security Board believes it would be sound public policy to pay part of the eventual cost of the benefits out of taxes other than payroll taxes.

D. Negative opinions.

(1) At the time of the consideration of the Social Security Act in 1935, the Treasury Department stressed its preference for a program financed entirely by payroll taxes.

(2) The President in his early statements stressed the self-supporting character of the old-age insurance system.

Question 7. In case a Federal subsidy is approved, when should such a subsidy begin?

Recommended Treasury decision.

It is recommended that the Treasury Department take the position that, since no immediate need for a subsidy exists, and in view of the recommendations made on other questions, no subsidy be introduced in the near future.

A. Various possibilities.

(1) The timing of a subsidy would of necessity be determined by three other variables:

- (a) The volume of benefits.
- (b) The extent to which the increases in payroll taxes now scheduled in the Social Security Act are permitted to go into effect.
- (c) The amount it is desired to accumulate for reserve.

(2) The subsidy might be introduced:

- (a) Immediately (1940).
- (b) Shortly after 1940 when the yield from the combined 2 or 3 percent payroll tax is inadequate.
- (c) After 1950 when combined payroll taxes are increased to 6 percent.
- (d) At any time during the interim.

(3) A decision on this point will be affected by the decision respecting the step-up in tax rates (Question 4), and the decision respecting size of the reserve (Question 10), and these in turn will be affected by the decision respecting the timing of the subsidy.

(4) If the payroll taxes, as scheduled, are allowed to go into effect uninterruptedly, no need for a subsidy would arise until some time after 1950, since until then current tax collections would exceed current benefit payments. Similarly,

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the smaller the reserve that is decided upon, the longer can the introduction of the subsidy be postponed since a subsidy would not be required to build up reserves in the early years, and also since part of the principal of the reserve would be available to pay benefits.

B. Arguments favoring the early introduction of a subsidy.

(1) The early provision of the subsidy would add to the acceptability of the old-age insurance program by the working population. This consideration is of particular importance in connection with the extension of coverage to groups not now covered.

(2) It would forcefully put the population on notice that the old-age insurance system requires a subsidy and that any increases in the scale of benefits would of necessity increase the size of that subsidy.

(3) It would either accelerate the accumulation of a reserve or permit a postponement of increases in payroll taxes.

C. Arguments opposing early introduction of subsidy.

(1) Early introduction of a government subsidy would reduce the probability of scheduled payroll tax increases being permitted to go into effect.

(2) If the case for a government subsidy rests upon the argument that the working classes are in themselves unable to provide adequately for their old-age, then the subsidy is justified only after these working classes have made their maximum contributions (presumed now to be 3 percent of payrolls.)

(3) In view of the present budgetary deficit, it would be desirable to postpone the introduction of the subsidy as long as possible.

(4) Collections from present taxes are adequate to meet benefit payments in the early years. If the plan for a sizable reserve is abandoned, there is no need for an immediate subsidy.

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D. Opinions concerning the timing of the subsidy.

(1) The Advisory Council's plan calls for a study of the timing of the Federal subsidy during the period when the combined payroll tax rate is 3 percent (1940-1942).

(2) The Social Security Board has indicated its preference for the postponement of the introduction of the Federal subsidy to a time in the future when current outgo for benefit payments exceeds current income from already scheduled payroll taxes and interest on reserves.

Question 7-a. In case a Federal subsidy is approved, what should be its relative magnitude?

Recommended Treasury decision.

No decision is necessary at the present time.

A. General alternatives.

(1) The Federal Government may assume one-third of the cost of benefits. This answer is suggested by the view that security for old-age is the joint responsibility of the worker, the employer and the general public, and that all three benefit equally from a system of old-age security. Carried to its logical conclusion this alternative would imply the introduction of a government contribution as soon as benefit payments are begun.

(2) The Federal Government may assume the residual responsibility, that is, it may cover the deficit between benefit payments and payroll tax collections. This answer is suggested by the view that the wages of some workers are inadequate to provide savings for old-age security without severely undermining the standard of living of the working population. This alternative would imply the postponement of the introduction of a Federal contribution until some time after the initiation of the payment of benefits. It would further imply acceptance of some tax rate, say 3 percent, as the maximum which workers could contribute for the security of their old age.

(3) The Federal Government may assume residual responsibility but not in excess of a fixed proportion, say one-third, of the total cost of benefits. This combines some features of the two preceding alternatives and implies that eventually the payroll tax rates may be allowed to increase in excess of the 6 percent now scheduled by the Social Security Act.

B. Relevant considerations.

(1) It is readily apparent that the decision respecting the relative size of the Federal contribution will in part be determined by the decision respecting the scheduled increases in payroll taxes and in part by the decision respecting the size of the reserve. Both of these in turn are affected by decisions respecting the size of the Federal contribution.

(2) In general it may be stated that the greater the proportion of the general population covered by the insurance system the stronger the case for a larger subsidy.

C. Opinions concerning the magnitude of the subsidy.

(1) The Advisory Council's plan calls for distributing the eventual cost of the old-age insurance system by means of approximately equal contributions by employers, employees and the government.

(2) The Social Security Board expressed no official view on the subject beyond indicating that the portion of the total cost financed from the government subsidy should depend upon the proportion of the general population covered by the insurance system. In interdepartmental communications it suggested the limitation of the Federal contribution to one-half of payroll tax collections (approximately one-third of benefit payments), even if such a limitation implies eventual increases in payroll taxes above the scheduled 6 percent rate.

Question 8. In case a Federal subsidy is approved, should legislation be immediately enacted providing specific taxes to be collected in the future at such time and in such amounts as will be required for the Federal contribution?

Recommended Treasury decision.

No decision is necessary at the present time.

A. Affirmative arguments.

(1) The designation of specific taxes or increases in specific tax rates which will be required for old-age benefits would impress upon the public the cost aspects of old-age insurance.

(2) It would give the workers now paying payroll taxes some assurance that the government's share of the cost of the old-age insurance program will be forthcoming.

B. Negative arguments.

(1) The earmarking of specified taxes for particular functions interferes with the judicious budgeting of public revenues. Each Congress should be left with discretionary power to determine the relative merits of the various claims for public revenues.

(2) The earmarking of special taxes handicaps the development of individual tax sources. If the income tax, for instance, were earmarked for old-age security, an effective argument would be provided against such future expansion of the income tax for general revenue purposes as may be desirable.

(3) Designation of a specific tax to be used in the future for old-age insurance does not provide assurance that it would actually be so used. It would be clearly within the authority of any subsequent Congress to repeal or modify any provision a preceding Congress may have made.

(4) Foreign countries in general abstain from the practice of earmarking specific taxes for the government's share of old-age insurance costs and provide that the subsidy be financed out of the general revenues of the treasury.

C. Affirmative opinions.

D. Negative opinions.

(1) The Advisory Council's recommendations make no reference to the type of taxes which should be used for the financing of the government's share of old-age insurance cost.

(2) The Social Security Board does not recommend immediate enactment of the tax but indicates its preference for the use of income and inheritance taxes when and if a government subsidy is provided.

Question 9. Should Title VIII and Title IX taxes be combined?

Recommended Treasury decision.

It is recommended that the Treasury Department assist the Social Security Board in developing a practical plan for coordinating Title VIII and Title IX taxes.

A. Various possibilities.

(1) Coverage and specifications under the two taxes may be made more uniform so that information supplied for the computation of one tax would suffice for the computation of the other tax as well.

(2) The two taxes may be physically combined so that both are imposed at one and the same time.

B. Affirmative arguments.

(1) Both taxes are levied on the same base, payrolls. The combining of the two taxes would enable a computation of tax liability under both titles on a single tax return. This would simplify taxpayers' compliance and reduce cost of tax administration in the case of those individuals liable under both titles.

C. Negative arguments.

(1) Some employers are subject to both Title VIII and Title IX taxes on behalf of all their employees. In the case of other employers, however, some employees are covered under one title but not under the other. The making uniform of coverage so that no employer will have some employees covered under one title but not under the other would require more extensive revisions than are warranted by ease of administration and tax compliance.

(2) Standardization of the Federal taxes would not remove variations between them and State-imposed taxes and accordingly the taxpayer would not secure much relief from keeping records on two bases. This will grow in importance with the introduction of State merit rating provisions.

(3) Title VIII taxes are collected quarterly and Title IX taxes annually with a State tax credit allowable as a deduction. There are also other differences between the laws that might prove difficult of standardization.

(4) Alterations in the scope or structure of Title IX will generally require corresponding alterations in State unemployment insurance taxes.

D. Opinions regarding the coordination of Title VIII and Title IX taxes.

(1) The Social Security Board recommends that the Federal unemployment compensation tax provisions be combined with those for old-age insurance which relate to employers.

Question 10. Should the present reserve provisions be retained?

Recommended Treasury decision.

It is recommended that the full reserve method of financing should be abandoned.

The arguments for and against the full reserve system are somewhat different, depending upon whether current financial provision is or is not expected to be made for the annual appropriations in recognition of the accruing reserve liability. If such financial provision is expected to be made, it will be necessary to raise payroll taxes or other taxes (earmarked or not earmarked) drastically at present or in the very near future. If no financial provision is expected to be made for the accruing liability, the full reserve method of accounting would commit us to formally unbalanced budgets for a generation to come.

Some arguments on each side apply to both concepts of the reserve and some to only one. When an argument applies to only one concept of the reserve this will be indicated, otherwise it may be supposed that the argument applies to both concepts.

A. Affirmative Arguments.

(1) The full reserve method is the only one by which the annually accruing liability under the old-age insurance system is given full recognition within the regular system of appropriation accounting.

(2) The full reserve method of financing, by making the cost of future benefit payments felt in the present, acts as a check on increases in benefit rates.

(3) The full reserve method of financing is based upon the analogy of private insurance company practice and, as such, facilitates public understanding and acceptance of the old-age security program.

(4) The full reserve method of financing will result, for many years to come, in a substantial excess of cash receipts over cash disbursements when the formal budget is

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exactly in balance, and an equality of cash receipts and cash disbursements even when there is a considerable bookkeeping deficit. This will help the financing problem of the Treasury, and will have a restraining influence upon the economy which under some circumstances may be desired. (This argument is relevant only if financial provision is made for the accruing reserve liability.)

(5) It is argued by some that undersaving is likely to be a serious problem over the course of the next generation. It is argued, in particular, that if old-age security is provided by social action it will increase our need for income-producing capital in the future, while it will, at the same time, decrease the incentive for saving among the lower income classes. The full reserve system is the only one which will provide an adequate volume of annual saving to fill this gap and to provide for the capital needs of our still growing economy and so lighten the burden of paying old-age benefits in the future. (This argument is relevant only if financial provision is made for the accruing reserve liability.)

B. Negative Arguments.

(1) In order to finance Plan AC-14 according to the full reserve method, it would be necessary, upon the basis of the estimates of the Social Security Board, to put into effect immediately a payroll tax of about 2 percent (employer and employee shares combined) in addition to the rates of tax already provided by Title VIII, or to levy other taxes of equivalent present value. The levy of such additional taxes is not economically feasible, and, therefore, the full reserve method of financing must be abandoned. (This argument is relevant only if financial provision is made for the accruing reserve liability.)

(2) The accumulation of a large reserve will encourage the spending of larger amounts by the Government both for old-age insurance and other purposes. (This argument is relevant only if financial provision is made for the accruing reserve liability.)

(3) The restraint to increases in future benefit payments assumed to be provided by the full reserve method of accounting is illusory, since the mathematical requirements of this method may be met as well by the levy of future taxes as of present ones.

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(4) Considering the longer run, the full reserve method of financing, with financial provision for accruing liability, means a substantial excess of cash receipts over cash expenditures for many years to come. It means that many billions of dollars which would otherwise have been devoted to consumption will instead be saved. The real problem of the country in this respect is the excess of attempted savings over available investment opportunities, rather than the reverse as alleged under (5) of Affirmative Arguments. The full reserve method of financing will assure us of a substantial backlog of deflationary influence upon our economy from the old-age insurance system for a generation to come. (This argument is relevant only if financial provision is made for the accruing reserve liability.)

(5) If the full reserve method of accounting is continued without making current financial provision for the accruing reserve liability, it will result in a continuous budgetary deficit for the next generation. It is, of course, by no means certain that this could be carried out in practice, since during this period there would be a constant pressure to "balance the budget". Assuming, however, that a bookkeeping deficit could be deliberately maintained for such a prolonged period, it would be a depressing influence upon business during the entire period of its continuance.

The only reasonable explanation for failure to make financial provision for the accruing reserve liability, while incorporating it in our appropriation accounting, is that such provision is not economically feasible until actual benefit payments are being made. But, if so, why punish ourselves by our bookkeeping? Self-flagellation may have been good for the souls of medieval hermits, but is it good for a modern economy?

C. Affirmative Opinions.

(1) The Treasury Department favored the full reserve method of accounting (with current financial provision) in 1935.

(2) Mr. Riefler, one of the group of economists called to advise the Secretary on social security matters, appeared to lean toward the full reserve method of accounting (with full financial provision) at the present time, although he did not definitely commit himself upon this point.

D. Negative Opinions.

(All of these opinions are irrespective of whether or not current financial provision is expected to be made for the accruing reserve liability.)

(1) The Advisory Council recommended against the full reserve method of financing. While it is possible that Mr. Witte dissented on this point, he made no notation to that effect in the final report.

(2) The Social Security Board, in its report to Congress and the President, recommended the abandonment of the full reserve method of financing.

(3) All members (except Mr. Riefler) of the group of economists called to advise the Secretary on social security matters were in favor of the abandonment of the full reserve method of financing.

Question 11. Should the payroll taxes go directly into a special trust fund?

Recommended Treasury decision.

It is recommended that if, in the opinion of counsel, the proposed change would in any way jeopardize the constitutionality of the Act or of the taxes levied under it, it should not be made. Otherwise the Treasury should not oppose it.

A. Affirmative Arguments.

(1) Such a change would lessen public criticism to the effect that Social Security taxes are being diverted and spent for other purposes.

B. Negative Arguments.

(1) Such a change might render the Act, or important portions of it, unconstitutional.

C. Affirmative Opinions.

(1) The Advisory Council unanimously recommended such a change.

D. Negative Opinions.

(1) Counsel, in 1935, feared that such a provision might endanger the constitutionality of the entire legislation. Subsequent court decisions may have altered this opinion.

Question 12. Should such a (special trust) fund (for the segregation of Title VIII taxes) be managed by a Board of Trustees?

Recommended Treasury decision.

It is recommended that if a special trust fund is established, it should be managed by a board of trustees.

A. Affirmative Arguments.

(1) Management by a board of trustees would further the purpose for which the fund is proposed to be established, i.e., to increase public confidence in the proper use of the proceeds of payroll tax collections.

B. Negative Arguments.

(1) The trustees would have nothing to do. (They could, however, all be regular Government officials serving ex officio.)

C. Affirmative Opinions.

(1) The Advisory Council recommended the management of the fund by a board of trustees.

D. Negative Opinions.

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Question 13. Who should be the trustees (of a special trust fund for the segregation of Title VIII taxes)?

Recommended Treasury decision.

This is a matter upon which we do not feel qualified to make a recommendation. Among the persons who would seem logical candidates are the Secretary of the Treasury, the Director of the Budget, the Treasurer of the United States, the Chairman of the Social Security Board, and the Attorney General.

Question 14. Should the present 3 percent interest rate be eliminated so that outstanding obligations can be purchased?

Question 15. Should it be required that only outstanding obligations be purchased?

These two questions must be treated together, but divide themselves into the two further questions: (1) Should the fund be guaranteed a 3 percent return? and (2) Should the fund be invested in special issues or outstanding obligations? These two questions can logically be decided separately, as, if the decision should be in favor of guaranteeing the fund a 3 percent rate but of investing it in outstanding obligations, the difference in return might be made up to the fund from the Treasury.

I. Should the fund be guaranteed a 3 percent return?

Recommended Treasury decision.

It is recommended that the fund should be guaranteed a return of 3 percent.

It should be noted that the rate of interest guaranteed to the fund becomes of much less importance if the full reserve method of financing is abandoned and only a small contingency fund accumulated.

A. Affirmative Arguments.

(1) It is only by the use of a definite interest rate that a present value may be set upon future payments. Such a rate must be assumed, for example, to determine the extent to which any individual's annuity has been earned by his own and his employer's contributions, or to compare the present value of a Federal subsidy with that of the proceeds of present and future payroll taxes. Upon the basis of past experience, 3 percent seems the most reasonable round figure to take for this purpose, probably erring somewhat on the high side.

(2) Even if the 3 percent rate is too high, it merely results in a reduction in the amount of Government subsidy which would otherwise be necessary. It is just as well that

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a portion of the Government subsidy be in the form of a guaranteed rate of interest.

B. Negative Arguments.

(1) The whole amount of Government subsidy to the system should be clearly stated as such. It is misleading accounting to conceal a portion of it in the form of a guaranteed rate of interest.

C. Affirmative Opinions.

D. Negative Opinions.

II. Should the fund be invested in special issues or outstanding obligations?

Recommended Treasury decision.

It is recommended that investment in special issues or in outstanding securities should be at the option of the Secretary of the Treasury (or the Board of Trustees if one is set up), subject to the requirement that no securities may be purchased to yield less than 3 percent. This means, in effect, that all investments must be in special issues as long as no Government securities are obtainable to yield as much as 3 percent.

A. Arguments in favor of investing in special issues.

(1) The use of special issues permits the transactions of the fund to be handled with less disturbance to the securities markets. By means of special issues, the fund can secure interest, commencing immediately after its money becomes available for investment, while the money paid over to the Treasury for the special issues may be used to reduce the amount of refunding of currently maturing issues which would otherwise be necessary. It is a needless disturbance to the bond market for the fund to be compelled by law to purchase outstanding securities, while the Treasury is at the same time selling refunding issues. (Sometimes, of course, the purchase of outstanding issues under such circumstances might be good bond market policy, but it should not be made mandatory.)

(2) If the fund is to be guaranteed a fixed return, this can be handled most conveniently by means of special issues. As previously noted, however, it could also be handled by an over-all subsidy to bring the rate of return on the investments of the fund up to the guaranteed rate.

B. Arguments in favor of investing in outstanding securities.

(1) The investments of the fund would seem more "real" to the public if they were made in previously outstanding securities, rather than in new Treasury "I.O.U.'s".

C. Opinions in favor of investing in special issues.

D. Opinions in favor of investing in outstanding securities.

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Question 16. Will the Treasury approve extension of the Social Security Act to cover farm labor and domestic service?

Recommended Treasury decision.

It is recommended that the Treasury Department ask for a postponement of the application of the Act to these groups of employees while it engages in active study of ways and means of overcoming difficulties inherent in the administration of taxes with respect to them, with a view to reporting at the next session of Congress.

A. Affirmative arguments.

(1) Farm laborers and domestic servants are in the income classes that need most the protection of old-age benefits.

(2) The present and proposed subsidies from the Treasury would be more justifiable if coverage were extended to these groups.

(3) If benefits are increased and speeded up it will be more feasible to bring such groups under the Act than has been the case in the past.

B. Negative arguments.

(1) The extension of coverage to farm labor and domestic service would involve tax collection procedures that would be very expensive in relation to the revenue collected, if anything approaching complete enforcement was attempted.

(2) Under the existing schedule of benefits many taxpayers would probably overpay because of the large subsidy which could be secured by such overpayment.

(3) The persons that underpaid or did not pay at all might, when they reached retirement age, politically force the payment of a free benefit not related to earnings.

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C. Affirmative opinions.

(1) The Advisory Council favors bringing agricultural labor and domestic service under the Act by January 1, 1940, if administratively feasible.

(2) The Social Security Board favors bringing laborers in large-scale agriculture under the Act immediately, and domestic servants and the remaining farm laborers after a sufficient lapse of time to work out the administrative problems.

D. Negative opinions.

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Question 17. Should specific tables be presented showing the estimated contributions, disbursements, reserves, government subsidy, etc., from now until 1980?

Recommended Treasury decision.

It is recommended that such tables be presented covering the next 40 or 50 years rather than extending specifically to 1980. The use of this date fosters the erroneous impression that the system will reach a mature condition at that time.

A. Affirmative Arguments.

(1) Estimates over a long period of time are necessary to show the magnitude and the problems of the social security program. Short-term estimates, while serving useful purposes, do not present a complete picture and are very misleading.

B. Negative Arguments.

(1) It is impossible to predict with any claim to great accuracy, amounts relating to the distant future, especially when these amounts are dependent upon so many complicated and unpredictable factors.

Proposed plan AC-14: Estimated^{1/} benefit payments, taxable payroll, reserve, and Federal contributions, with present tax schedule and Government contributions as needed when reserve is depleted

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(In millions of dollars)

Year :	Benefits :	Payroll :	Reserve :	Federal :	Subsidy as
:	:	:	:	subsidy :	percent of
:	:	:	:	:	payroll
1940	556	30,390	2,001		
1941	688	30,440	2,225		
1942	782	30,440	2,362		
1943	872	30,440	2,718		
1944	968	30,770	3,001		
1945	1,042	31,080	3,230		
1946	1,169	31,440	3,651		
1947	1,263	31,780	4,007		
1948	1,368	32,140	4,286		
1949	1,453	32,470	4,813		
1950	1,542	32,810	5,286		
1951	1,661	33,180	5,675		
1952	1,747	33,530	6,009		
1953	1,837	33,870	6,282		
1954	1,946	34,230	6,475		
1955	2,014	34,580	6,626		
1956	2,147	34,970	6,671		
1957	2,240	35,320	6,644		
1958	2,355	35,700	6,523		
1959	2,444	36,060	6,331		
1960	2,537	36,420	6,060		
1961	2,649	36,790	5,690		
1962	2,731	37,150	5,248		
1963	2,808	37,500	4,735		
1964	2,899	37,860	4,136		
1965	2,947	38,190	3,489		
1966	3,067	38,550	2,724		
1967	3,156	38,920	1,868		
1968	3,249	39,260	913		
1969	3,330	39,620	-	132	.33%
1970	3,425	39,970		1,147	2.87
1971	3,524	40,290		1,228	3.05
1972	3,622	40,620		1,307	3.22
1973	3,730	40,940		1,397	3.41
1974	3,832	41,270		1,480	3.59
1975	3,931	41,590		1,561	3.75
1976	4,034	41,620		1,662	3.99
1977	4,135	41,660		1,760	4.22
1978	4,252	41,700		1,875	4.50
1979	4,352	41,750		1,972	4.72
1980	4,456	41,780		2,074	4.96

^{1/} Figures based on estimates prepared by the Social Security Board.

Proposed plan AC-14: Estimated^{1/} benefit payments, taxable payroll, reserve, and Federal contributions, assuming a step-up in payroll taxes to 1 $\frac{1}{2}$ % in 1940 and three-way division of cost between employer, employee, and Government starting when reserve is depleted
(In millions of dollars)

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Year	Benefits	Payroll	Reserve	Federal subsidy	Subsidy as percent of payroll
1940	556	30,390	2,001		
1941	688	30,440	2,225		
1942	782	30,440	2,362		
1943	872	30,440	2,413		
1944	968	30,770	2,378		
1945	1,042	31,080	2,277		
1946	1,169	31,440	2,040		
1947	1,263	31,780	1,712		
1948	1,368	32,140	1,279		
1949	1,453	32,470	741		
1950	1,542	32,810	107		
1951	1,661	33,180		550	1.66%
1952	1,747	33,530		616	1.84
1953	1,837	33,870		646	1.91
1954	1,946	34,230		683	2.00
1955	2,014	34,580		706	2.04
1956	2,147	34,970		751	2.15
1957	2,240	35,320		782	2.21
1958	2,355	35,700		821	2.30
1959	2,444	36,060		851	2.36
1960	2,537	36,420		882	2.42
1961	2,649	36,790		920	2.50
1962	2,731	37,150		947	2.55
1963	2,808	37,500		973	2.59
1964	2,899	37,860		1,004	2.65
1965	2,947	38,190		1,021	2.67
1966	3,067	38,550		1,061	2.75
1967	3,156	38,920		1,091	2.80
1968	3,249	39,260		1,122	2.86
1969	3,330	39,620		1,150	2.90
1970	3,425	39,970		1,182	2.96
1971	3,524	40,290		1,215	3.02
1972	3,622	40,620		1,248	3.07
1973	3,730	40,940		1,284	3.14
1974	3,832	41,270		1,319	3.20
1975	3,931	41,590		1,352	3.25
1976	4,034	41,620		1,386	3.33
1977	4,135	41,660		1,420	3.41
1978	4,252	41,700		1,459	3.50
1979	4,352	41,750		1,492	3.57
1980	4,456	41,780		1,527	3.65

Beginning in 1951, the required tax rate on employer and on employee would rise from the previous level of 1 $\frac{1}{2}$ %, as indicated in the final column.

^{1/} Figures based on estimates prepared by the Social Security Board.

Proposed plan AC-14: Estimated benefit payments, taxable payroll, reserve, and Federal contributions, with continuance of present 1½-1% after January 1, 1940, until reserve is depleted, and with three-way division of cost between employer, employee, and Government when Government contribution exceeds 1%
(In millions of dollars)

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Year	Benefits	Payroll	Reserve	Federal subsidy	Subsidy as percent of payroll
1940	556	30,390	1,697		
1941	588	30,440	1,608		
1942	782	30,440	1,422		
1943	872	30,440	1,141		
1944	968	30,770	760		
1945	1,042	31,080	301		
1946	1,169	31,440		309	.98%
1947	1,263	31,780		447	1.41
1948	1,368	32,140		483	1.50
1949	1,453	32,470		517	1.59
1950	1,542	32,810		547	1.67
1951	1,661	33,180		587	1.77
1952	1,747	33,530		616	1.84
1953	1,837	33,870		646	1.91
1954	1,946	34,230		683	2.00
1955	2,014	34,580		706	2.04
1956	2,147	34,970		751	2.15
1957	2,240	35,320		782	2.21
1958	2,355	35,700		821	2.30
1959	2,444	36,060		851	2.36
1960	2,537	36,420		882	2.42
1961	2,649	36,790		920	2.50
1962	2,731	37,150		947	2.55
1963	2,808	37,500		973	2.59
1964	2,899	37,860		1,004	2.65
1965	2,947	38,190		1,021	2.67
1966	3,067	38,550		1,061	2.75
1967	3,156	38,920		1,091	2.80
1968	3,249	39,260		1,122	2.86
1969	3,330	39,620		1,150	2.90
1970	3,425	39,970		1,182	2.96
1971	3,524	40,290		1,215	3.02
1972	3,622	40,620		1,248	3.07
1973	3,730	40,940		1,284	3.14
1974	3,832	41,270		1,319	3.20
1975	3,931	41,590		1,352	3.25
1976	4,034	41,620		1,386	3.33
1977	4,135	41,660		1,420	3.41
1978	4,252	41,700		1,459	3.50
1979	4,352	41,750		1,492	3.57
1980	4,456	41,780		1,527	3.65

Beginning in 1947, the required tax rate on employer and on employee would rise from the previous level of 1½, as indicated in the final column.

1/ Figures based on estimates prepared by the Social Security Board.

Proposed plan AC-14: Estimated^{1/} benefit payments, taxable payroll, contingency reserve,^{2/} and Federal contributions, with present tax schedule and with Government contributions when needed

(In millions of dollars)

Year	Benefits	Payroll	Reserve	Federal subsidy	Subsidy as percent of payroll
1940	556	30,390	2,001		
1941	688	30,440	2,225		
1942	782	30,440	2,362		
1943	872	30,440	2,718		
1944	968	30,770	3,001		
1945	1,042	31,080	3,230		
1950	1,542	32,810	5,286		
1955	2,014	34,580	6,600		
1960	2,537	36,420	6,600	263	.72%
1965	2,947	38,190	6,600	572	1.50
1970	3,425	39,970	6,600	949	2.37
1975	3,931	41,590	6,600	1,362	3.27
1980	4,456	41,780	6,600	1,877	4.49

^{1/} Figures based on estimates prepared by the Social Security Board.

^{2/} The contingency reserve is the amount of excess taxes over benefit payments accumulated at 3 percent interest. When benefit payments exceed taxes the contingency reserve is held constant, i.e., a Federal subsidy is then introduced in the amounts necessary to supplement current taxes plus interest income on the amount of the reserve.

Proposed plan AC-14: Estimated^{1/} benefit payments, taxable payroll, contingency reserve,^{2/} and Federal contributions, with step-up in payroll taxes to $1\frac{1}{2}\%$ - $1\frac{1}{2}\%$ in 1940 and three-way division of cost between employer, employee, and Government beginning when the Government contribution reaches $1\frac{1}{2}\%$ of the taxable payroll.

(In millions of dollars)

Year :	Benefits :	Payroll :	Reserve :	Federal :	Subsidy as
:	:	:	:	subsidy	percent of
:	:	:	:	:	payroll
1940	556	30,390	2,001		
1941	688	30,440	2,225		
1942	782	30,440	2,362		
1943	872	30,440	2,413		
1944	968	30,770	2,400	22	.07%
1945	1,042	31,080	2,400	100	.32
1950	1,542	32,810	2,400	523	1.59
1955	2,014	34,580	2,400	682	1.97
1960	2,537	36,420	2,400	858	2.36
1965	2,947	38,190	2,400	997	2.61
1970	3,425	39,970	2,400	1,158	2.90
1975	3,931	41,590	2,400	1,328	3.19
1980	4,456	41,780	2,400	1,503	3.60

Beginning with 1950, the required tax rate on employer and on employee would rise from the previous level of $1\frac{1}{2}\%$, as indicated in the final column.

^{1/} Figures based on estimates prepared by the Social Security Board.

^{2/} The contingency reserve is the amount of excess taxes over benefit payments accumulated at 3 percent interest. When benefit payments exceed taxes the contingency reserve is held constant, i.e., a Federal subsidy is then introduced in the amounts necessary to supplement current taxes plus interest income on the amount of the reserve.

Proposed plan AC-14: Estimated^{1/} benefit payments, taxable payroll, contingency reserve,^{2/} and Federal contributions, with continuance of present 1%-1% after January 1, 1940, and Government contributions up to 1% when needed. Three-way division of cost between employer, employee, and Government thereafter.

(In millions of dollars)

Year	Benefits	Payroll	Reserve	Federal subsidy	Subsidy as percent of payroll
1940	556	30,390	1,697		
1941	688	30,440	1,700	92	.30%
1942	782	30,440	1,700	183	.60
1943	872	30,440	1,700	273	.90
1944	968	30,770	1,700	326	1.06
1945	1,042	31,080	1,700	351	1.13
1950	1,542	32,810	1,700	530	1.62
1955	2,014	34,580	1,700	689	1.99
1960	2,537	36,420	1,700	865	2.38
1965	2,947	38,190	1,700	1,004	2.63
1970	3,425	39,970	1,700	1,165	2.91
1975	3,931	41,590	1,700	1,335	3.21
1980	4,456	41,780	1,700	1,510	3.61

Beginning with 1944, the required tax rate on employer and on employee would rise from the previous level of 1%, as indicated in the final column.

^{1/} Figures based on estimates prepared by the Social Security Board.

^{2/} The contingency reserve is the amount of excess taxes over benefit payments accumulated at 3 percent interest. When benefit payments exceed taxes the contingency reserve is held constant, i.e., a Federal subsidy is then introduced in the amounts necessary to supplement current taxes plus interest income on the amount of the reserve.

RE SOCIAL SECURITY RECOMMENDATIONS

February 23, 1939.
3:15 p.m.

Present: Mr. Haas
Mr. J. Douglas Brown

H.M.Jr: Now, as I remember it, since I last saw you, there's a couple little things I want to look at - a comparison of

Brown: Yes. That's the old-age assistance, the effect on old-age assistance provided old-age insurance is in effect. Of course, these figures are very rough figures. But if old-age insurance is in effect - only Title I - that's the 50-50 grants to the states.

H.M.Jr: That's the way it is now?

Brown: Now, without any old-age insurance - that's the presumption contrary to fact.

H.M.Jr: Oh, without any?

Brown: Without any old-age insurance, old-age assistance would mount up to two billion for the Federal Government and two billion for the state governments by 1980.

H.M.Jr: I don't understand that.

Brown: It's in order to show the effect of an old-age insurance plan being in effect....

H.M.Jr: What have you got now?

Brown: Under present conditions Title II is in effect, so that the 1940 - since old-age insurance doesn't begin paying, it will be the same for old-age assistance as now; but as you gradually get into these later years with Title II, the old-age insurance taking over more and more people, it tends to hold down the cost of old-age assistance, so that the Federal Government is saving there 400 million dollars from what it would otherwise appropriate for old-age assistance to the states, because of the fact there is old-age insurance.

H.M.Jr: I don't get it.

Brown: It is complicated as the dickens.

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If old-age insurance were not in effect, that is, if the Congress had only passed Title I in 1935

H.M.Jr: What's Title I?

Brown: The old-age assistance title, whereby the Federal Government puts up half up to \$15 of what the state puts up - the other \$15.

H.M.Jr: That's what you call old-age assistance?

Brown: Yes. That's in effect now. But if there were no old-age insurance it would get out of hand. See, it would gradually go up to two billion dollars.

H.M.Jr: That's the Federal?

Brown: Just the Federal load would go up to two billion.

H.M.Jr: That's 50 percent.

Brown: That's right. The state would put up the other 50, at least two billion. But the idea in '35 was that the insurance as time went on would hold down the assistance, since more and more people would get an old-age benefit rather than the old-age assistance.

H.M.Jr: Don't you have to add these two?

Brown: Well, in that sense it wouldn't work to add the two, because this is the effect after another condition develops - that is, the old-age insurance is in effect. Perhaps it would be better to take this figure, either one of these; because of the fact that old-age insurance is in existence, the Federal Government saves these sums of money year by year.

H.M.Jr: Well, that's better for me. Savings resulting from the present Title II, which is old-age insurance.

Brown: That's right.

H.M.Jr: And we save

Brown: ... that much money ...

H.M.Jr: ... each year.

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Brown: That's right.

H.M.Jr: That I can understand.

Brown: Because if it were not for the insurance scheme, there would be many more people who would need to go on relief, and that relief money would have to come 50 percent from Federal, roughly, and 50 percent from the states. Since there is old-age insurance in effect and these people help to contribute and their employers contribute, it means that the Federal Government saves something roughly approximating these figures.

And I believe the way that point came up in our discussions was that we were discussing the use of other than payroll taxes, and I said that because the old-age insurance was in effect the Government would save money and that would be a justification for the Federal Government using other than payroll taxes to help in the old-age insurance scheme.

H.M.Jr: Now, see if I get it. Savings through the old-age insurance plan to the Federal Government is this much.

Brown: Yes, that's it - of course, as much as you can approximate it.

H.M.Jr: Now what I want - I get this on this column - now then, I ask, if we changed and went on a basis that the Federal Government assumed one-third of the cost of the old-age insurance plan

Brown: Yes.

H.M.Jr: ... now much would that cost us in addition over the present system, where we're going 50-50? Is that the way you're working the thing out?

Brown: Well, you could put it that way. You could say that under the old-age assistance plan the Federal Government is putting up under the present Act these sums of money.

H.M.Jr: I see.

Brown: Now, if it were not - it's a sort of an opportunity relationship - if the Federal Government were not being

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relieved by these payroll taxes coming in for old-age insurance, it would otherwise have been spending this much. And the argument is that, since it is saving all this sum, over a billion dollars by 1980, that there is a justification for the Federal Government using that sum more or less to assist in the insurance scheme.

H.M.Jr: Now, at the same time, by 1980, if we go on the basis where the Federal Government is going to assume one-third of the cost, how much will that one-third cost?

Brown: It will be somewhat more than that. It is difficult to estimate, because a great deal depends on what timing you use. In other words, if you hold down the payroll taxes earlier, it would mean that the Federal Government does come in

H.M.Jr: No, I mean supposing we go to one and a half, one and a half.

Brown: A third would be one billion 574 million.

H.M.Jr: That's the total cost to the Federal Government in 1980.

Brown: That's right, the appropriation by the Federal Government, allowing payroll taxes going - continuing at one and one, and then going above that as necessary. And by that time each of the three would be paying 3.77 percent.

H.M.Jr: I see. And that would cost the Federal Government one billion 574.

Brown: Whereas the amount of saving from the fact that there is an insurance over against what it would have to pay for assistance is one billion 145.

H.M.Jr: I see.

Brown: Save a considerable part of what the Government otherwise would be paying. And the Government would be saving all these years in addition to these years. Would be an offset proposition.

H.M.Jr: Would it be more impressive if we totaled them?

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Brown: It might, yes.

H.M.Jr: You see?

Brown: Of course, one difficulty is these figures are approximations, and you can't have anything better than approximations from now until 1980; but the principle is entirely sound and it's a question, in my mind, of the precise premises of your estimates. And that was, by the way, a basic assumption from the first, that the old-age insurance will lift more and more people out of the need for assistance. Assistance is paid for 50-50 by the Federal Government and the state government, with no employee or employer contribution. Therefore, since the old-age insurance does lift these people out and does save the Federal and state governments considerable sums, these sums here, there is a justification for the use of other than payroll taxes.

H.M.Jr: Has that been stated that way before? Is that the usual way to state it?

Brown: Well, it's - I don't know if just that way. Of course, in various conversations I've had, I've stated it that way, but it hasn't been stated publicly that way very often. Most people don't - haven't gone into it very much.

H.M.Jr: How am I going to "gee" my position over on taxes and still be consistent if I'm for one and a half, one and a half?

Haas: Way in the future.

Brown: It's way in the future.

H.M.Jr: How far in the future?

Brown: I'd say it's variable.

H.M.Jr: That goes in effect in '40.

Brown: In '40, one and a half, one and a half - that's already in the law. That's no change of what's on the books now. Now, for that matter, two and two

is in the law. And personally, I think a sound principle is that if you go to one and a half, one and a half, then on the basis of five years' tax experience there will be restudy as to the matter of future tax rates or future use of other than payroll taxes, because by 1941-42 the basis of computations will be much more accurate.

H.W.Jr:

Well, I want to just talk a minute on this thing. I mean this is the thing that I've been thinking about. This is the thing that's going through my mind - I've talked about this to Bell - that we all have these pressures on the Treasury from particular interests, and the only way that I see that we can get ourselves on a fairly sound basis - and I'm just toying with this thing, and I called up Bell here a couple days ago, asked him to think about it - is that we apply what I call the principle of the Comptroller of the Currency's office: that if the banks want to be examined and if the people of the United States think the banks should be examined, that's a service we render to the banks and therefore we tax the banks to pay for that Federal service. If the shipping interests of this country want the harbors deepened and docks built, so forth and so on, we should put a tonnage tax on shipping and let them pay for that service. If we want good roads, then all gasoline taxes and automobile taxes and tire taxes should be earmarked and spent only for good roads and eliminating grade crossings, so forth and so on. We spend, I don't know, five hundred million, a billion dollars, a billion and a half dollars, that we can get back selling bonds to the public against particular public works; that should go in a revolving fund, and that money, whatever it is, should be spent over and over again; as the revenue pays it back, voted out by Congress for new public works; have a revolving fund, five hundred million or a billion dollars, self-liquidating public fund, for public improvements, reclamation, power, so forth and so on.

Now, if that theory is right - I mean that the normal taxes we place on business - I mean I'm just - I mean this is very confidential, because it's still in very much of a nebulous state - the normal taxes to be raised will pay for the normal

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expenses of government. Then the Post Office and all these other special things that we do should be self-supporting. And then, in times of emergency, you have only two extraordinary expenditures, and one is for armaments and the other is to take care of the unemployed.

Then it leads me to this thing, which is that if that theory is right, then these various insurance schemes should be self-supporting. See what I mean?

Brown:

Yes, but in here you're asking payroll taxes that the employer and employee pay not merely to do the self-supporting thing, which is to take care of persons now in productive employment, but to meet an unearned benefit which Congress has decided should be provided in giving a man much more than he contributes because he happens to be now old. And I think to carry that proposition through you would say that for all young persons, see, all persons, say, under 35 or under 30, this scheme should be self-supporting. But since we started in the middle of the stream and we have plenty now that are 45 and 50 and 55, and yet Congress sees fit to give them a larger benefit than they have earned, that should not necessarily be attributed to payroll taxes.

Now, a second argument there would be that Congress has already committed itself to this old-age assistance; by doing a better job on the insurance, in large measure it is not adding a new cost but is transferring the cost from assistance cost to insurance cost by paying a better unearned benefit.

See what I mean? I feel that if you allocate the cost of these unearned benefits entirely to payroll taxes, it will tend to displace labor by charging as a labor cost the full charge of displacing these old workers that are already 60, 65; and I think it would be better fiscal policy to attribute that charge to general revenues.

H.M.Jr:

Well, are you saying to me that we meet this thing half-way and say that when the people who are now 30, 35, become 65, they should be self-supporting, but we just take care of the people who are over 35?

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Brown: Well, it approximates that, but you never meet it quite that way. In other words, the biggest argument for government contributions to this scheme is the fact that you're paying an unearned benefit to persons who are too late in life now to have contributed enough to earn their own benefit alone that they and their employers share. If we had started this scheme forty years ago

H.M.Jr: How many years ago?

Brown: ... - forty - it would have meant that the persons that we are now retiring, see, would have contributed over a lifetime, in their employers' share and their share, what would probably be entirely sufficient as an average, top and bottom, to take care of their own benefits. But like all private employers, when they first put in a pension plan, they have to take for granted that they will put in additional costs, since a good many of their people are too old to contribute enough to pay for their own benefits.

You see, in a way the Government is committed in either way. If it pays it by assistance, it pays it by a hundred percent Federal and state. If it pays it by insurance, it - now it's getting all of it from payroll; it would still be, in a sense, ahead of the game in part if it put part of the money in and still got a certain fraction from employers and a certain fraction from employees.

H.M.Jr: Well, as I understand it, if we go a third, a third, a third, and the Government puts up a third, we won't - the cost to the Federal Government

Brown: A full third would cost the Federal Government more than this.

H.M.Jr: More than the present system, when we put in 50 percent, by about 400 million?

Brown: If it were a full third, that third would be one billion 500 million by 1980; the saving over against old-age assistance, which alone would be one billion, 145

H.M.Jr: Now, what the states would do - if we're relieving them of their entire burden, what do they do in

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return?

Brown: That would be a question, as to whether there would be any way. Of course, you could argue that if the states by so much were relieved of taxation, that there would be in general a source of further revenue to the Federal Government.

H.M.Jr: Well, I got an idea I'd like to put up to the states, and say we wouldn't do this in a state unless they concur; that is that a state give up all right to inheritance taxes to the Federal Government, for this.

Brown: Of course, they'd say, "Well, we'll wait; we'd like to wait until these benefits really begin to be paid."

H.M.Jr: I mean I'm very anxious to get the Federal Government the exclusive right to tax estates, see? Make a note of that, George, see? I mean

Haas: That's the best tax to start with, too.

H.M.Jr: And how much the states collect, see? Now on a quid pro quo basis, if we're going to do this, then I'd like to have it fixed that the state - that we'd keep on in the state on a 50-50 basis, but if we take it over and contribute a third, then the state has to give up all rights to inheritance taxes. Now, would we collect 400 million on that basis, on the present inheritance tax? See, it's very conflicting, this thing of inheritance and estate taxes. That's one of the things Magill while he was here was trying to tell me.

Excuse me a minute. (On phone) Mrs. Klotz, please. Well, Miss Chauncey. - Hello. - Tell Chauncey or McHugh to come in here: one or the other.

Now, figure out, you see, what do the states collect? When the states collect it, it's called what?

Haas: Some of them have inheritance tax, some estate tax, others a combination.

H.M.Jr: I'd like to get the states out of this entirely and say all inheritances taxes - all death taxes;

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that's the word I want to use - should belong to the Federal Government. Now, how much would we gain if it's just on the present basis?

Haas: We'll give you a figure.

H.M.Jr: What do you think of that idea for a trading basis?

Brown: I'd certainly say all to the good. You're relieving them, as time goes on, as the old-age insurance benefits are more adequate - you're relieving not only the states, but, say, in Oregon, the counties that are putting up their share against the state's share, against which the Federal Government puts up 50 percent.

H.M.Jr: "Now, we say we're going to do this for you; we'll write it in the law that we'll only do this provided you will say that for the term of the act..." - or something; the lawyers would have to do that - "you'll give up to the Federal Government all right to all death taxes."

(McHugh comes in)

Bob, some place or other there is a little black book that Dr. Magill left on taxes, written by Magill and Carl Shoup. It was all very confidential, and it's a black book that he wrote - somewhere, some place.

McHugh: It's on taxes.

H.M.Jr: Specially bound book written by Magill and Shoup, just for me.

(McHugh goes out)

Brown: Of course, I'm trying to look at it from the state point of view, the relief to the state because of the payment of old-age benefits as an entering wedge, you know; it moves up gradually. The first year they're relieved in part, of those 65; the following year it will be the ones now 66 and those 65; next year, 67, 66, and 65.

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- H.M.Jr: For a long time we've been talking about overlapping taxes; there's nothing more overlapping than death taxes.
- Haas: And it's a type of taxes - better type to be collected by the Federal Government. People make their fortunes on a national basis.
- H.M.Jr: And I want to greatly increase that - I mean the one tax which is not deflationary, and I'm anxious to increase that greatly. But I could do it much more rapidly if it was exclusively a Federal tax. And we would then be making an entering wedge on the question of overlapping taxes, which is a thing I haven't done in five years; and I don't know any place that it's better to start than on death duties.
- Brown: Yes.
- H.M.Jr: And this thing might taste a hell of a lot sweeter, George, if we could say, "Here we're giving up ..." I don't know what we're assuming for the states. I'd like to get this, to look at it from the states' picture: how much are we relieving the states of?
- Haas: That's the same figure.
- Brown: It's exactly the same as Federal.
- H.M.Jr: How much do we relieve them of? A billion one. That's a hell of a lot of money.
- Brown: But it comes in gradually.
- H.M.Jr: That's all right.
- Brown: It gets into big money ten or fifteen years from now.
- H.M.Jr: But you'll find the death duties the states collect don't approach a billion dollars, and the way to do it is to average it over thirty or forty years. And after all, if we're going to write into the law that we're going to contribute to the states that are poor, it ought to also be possible to say "but provided that the state does not collect any taxes on deaths."

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- Brown: Of course, this would be a contribution to a Federal Act, but that the Federal Act, because of its more adequate benefits, relieves the state of having to pay old-age assistance - to that extent - you can't say to that precise extent; you can say, since the Federal Act is going to pay the old person, say, before he dies, if the revisions go through, say, plus twenty dollars for the wife - that's sixty dollars - Joe Fish now does not have to go around to the state assistance office and ask for sixty dollars; he goes to the Federal old-age insurance, puts his claim in, and gets sixty; therefore, the state saves thirty and the Federal saves thirty. And the argument would be that the Federal, in saving its thirty on the assistance, has made this sixty dollars more possible by being willing to contribute a part of that old-age insurance cost over time. And the state certainly is saving, say, thirty dollars in the case of that couple.
- H.M.Jr: Yes, but I - you could throw into what's-his-name's lap
- Haas: Blough's lap. On estates, I don't/Florida has any; some estates go down there and escape it completely. think
- H.M.Jr: On the other hand, New York, for instance - they have high estate taxes, and that applies definitely.
- Brown: Jersey got a lot of its relief costs from the Dorrance estate, after a long fight.
- H.M.Jr: And this would be an entering wedge into solving this thing we've talked about - nobody's done it - this question of overlapping taxes. We've always said we didn't want to start the conversations because whatever thing we started, we felt the Federal Government would be getting the worst end of it. But here we are, definitely doing something for the cost of carrying old-age benefits.
- Brown: Part of - there still would be those not covered under old-age insurance. There would still be an affinity between those concepts: those who die rich help those who get old poor.
- H.M.Jr: You mean that's why the states

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Brown: You might make that argument - very logical - that if the Federal Government is to assist old people more adequately ...

H.M.Jr: That carries out my idea: if the old people want the service, we make those who die rich

Brown: Those who die rich help those that get old poor.

H.M.Jr: Write that down. Those who die rich help those that get old poor. That's a good slogan.

Brown: Some have more than they need, others not enough.

H.M.Jr: Do you think - this suggestion of mine isn't out of the realms of possibility?

Brown: I don't know how it could be implemented in statutory form, but there certainly is a very definite logic in the argument that the states are being assisted in meeting their costs of old age by having a Federal old-age insurance scheme, and the Federal old-age insurance scheme, to the extent it costs the Federal Government money, saves in the long run the state money.

H.M.Jr: Now, where are we on this damn law anyway? When they going to get around to me?

Brown: Well, the last word I had from Altmeyer - the thing that got me up in the air just now is, he wants me to go up there Monday as representing the Advisory Council; then there's Folsom and several business people - Swope and maybe Stettinius. Then I think from the strict Government end he'll go back up as representing the Board, and then they'll probably ask you.

Haas: Why should you go up there, Mr. Secretary, until they have the law written?

Brown: From Altmeyer's position, I would say toward the end of next week, beginning the following ...

H.M.Jr: Why should I go up if I can avoid it?

Haas: Yes.

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H.M.Jr: Because I'd much rather not.

Haas: I think you can work out a pretty good case why you shouldn't. As you said, the social insurance part of it is Altmeyer's, and until they can have something concrete from the financial aspect, you can't comment.

H.M.Jr: Haven't they got that?

Haas: No.

Brown: I think the important thing, sir, is whenever you care to give clearance, whatever you think you want to give, to Altmeyer, because he's the one who has to begin a constructive case. Naturally, he doesn't want to begin his constructive case until he clears.....

H.M.Jr: I don't know where the hell the President stands on this one and a half, one and a half, see? That's my great trouble.

Brown: As I've seen it around here,

(Mrs Klotz comes in)

H.M.Jr: Do you know Mrs. Klotz, Professor Brown?

Brown: How do you do?

Klotz: How do you do, Professor Brown?

I think the thing you're (H.M.Jr) asking for is the thing we had bound.

H.M.Jr: Yes.

Klotz: I think you've got that home.

Haas: Doesn't Blough have a copy?

H.M.Jr: There's nothing at home.

Klotz: I think you took it up to the country one week-end. We'll continue looking, but

H.M.Jr: I don't need it tonight. I mean tomorrow will do.

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Klotz: All right.

H.M.Jr: Somebody could look through there - go up to my bedroom and look through there. You might ask Janet to take a look. I've got a lot of books up there.

Klotz: Probably. I don't - know we haven't got it here.

H.M.Jr: I have nothing in the country.

Klotz: You haven't? Well, we'll find it.

(Mrs Klotz goes out)

Brown: Well, the main issue, of course, in that list of questions that Altmeyer sent over, as we have discussed it at various times, comes to that question of the use of other than payroll taxes. Now, in the Board report it supports the principle that there be the use of other than payroll taxes, in addition to going to three and three percent on payroll taxes. And the whole program as recommended by the Council and recommended by the Board hangs on that point.

H.M.Jr: Well, let's see where we're at tomorrow. You going to be here tomorrow?

Brown: I can stay over, sir.

H.M.Jr: Or are you going to be

Brown: You see, since they asked me to come Monday - if you'd like to have me stay, I'd like very much to stay, sir. Whichever way

H.M.Jr: No, it's not necessary. Tomorrow's a difficult day. What time you going on the Hill?

Brown: Altmeyer said he'd put me on as early as he could.

H.M.Jr: You mean Monday.

Brown: But I can come down here ten o'clock.

H.M.Jr: When you get through, why don't you come down?

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Brown: I'll do that, yes, sir.

H.M.Jr: Huh?

Brown: Yes, sir, I'll be here Monday.

H.M.Jr: I better give you an appointment for Monday, because first thing you know I get all stacked up. I'm putting it down for 2:30 on Monday.

Brown: 2:30 on Monday.

RE SOCIAL SECURITY RECOMMENDATIONS March 17, 1939.
10:05 a.m.

Present: Mr. Hanes-
Mr. Bell-
Mr. Haas-
Mr. White-
Mr. Duffield-
Mr. Altmeyer
Mr. Eccles
Mr. Ruml
Mr. Frederic A. Delano
Mr. Currie
Mr. Brown
Mr. Blough-

H.M.Jr: All right, gentlemen.

Mr. Altmeyer, this constitutes a so-called fiscal and monetary group for the President. We're an informal organization at work for him and report to him. Confidentially, the President is having you and myself and Mr. Hanes and a representative from the bill and Professor Douglas Brown at 12 o'clock Monday to discuss his position and the position that I will take before the Committee.

Now, naturally, any position that I take will be, as we agreed before, only as it affects fiscal problems.

And if you would state to this group what you think you want from the Treasury - a fiscal position - or what are the things that the President has to say yes or no to, what do I have to say yes or no to, and what would you like us to say? The floor is yours. Do I make myself plain?

Altmeyer: Yes.

H.M.Jr: I mean Jere Cooper is coming down, you see; he said he wanted me to come up there this week. I said, "No, I don't know where the President stands on some of these things." So I arranged for the meeting for 12 o'clock Monday. Now, what is there for the President to say yes or no to and what is there for me to say yes or no to, and what would you like us to say?

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Altmeyer: I think it breaks down into two categories of questions, Mr. Secretary, one dealing with costs and how they will be financed, and secondly, dealing with how the fund shall be handled, what sort of bookkeeping arrangements, what sort of trustee arrangement, if any - that sort of thing.

Now first on the matter of the benefits and how they shall be financed. The Social Security Board is recommending that benefits be commenced next year instead of in 1942 under this old-age insurance system, and that the benefits in the early years be liberalized.

H.M.Jr: George, give me a pad, will you?

(Bell hands H.M.Jr a pad)

You've got to watch this Director of the Budget. That's why I'm having him changed.

Bell: I've got all your pads?

H.M.Jr: He won't let me keep a piece of paper.

Bell: Do you think you'll get them back by changing?

H.M.Jr: I don't know, but I'll be a little safer.

All right. I'm sorry, but we have our troubles here in the Treasury.

Altmeyer: I can appreciate that.

So the first question we'd like to know about is whether the Treasury is in accord with the recommendation of the Board that benefits start next year and that the benefits in the early years be liberalized.

H.M.Jr: What does that mean: benefits start next year?

Altmeyer: Under the present law, monthly benefit payments start January 1942.

H.M.Jr: January 1942.

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Altmeyer: Benefits start.

H.M.Jr: Yes.

Altmeyer: Now we recommend that they start in 1940. If Congress acts by July 1 of this year, we think that administratively we would be in a position to process the claims by January 1, 1940 - I mean by July 1, 1940. We think we probably ought to have a year to expand our field force from the time that Congress acts, although conceivably we could start earlier.

On the liberalization

H.M.Jr: Now the benefits under the present law start January 1, 1942, and you're recommending that they should start January 1, 1940.

Altmeyer: We don't say specifically what date in 1940. We say in 1940.

H.M.Jr: O.K., I get you.

Altmeyer: Now, on the matter of liberalization, we recommend that the benefits payable to those retiring in the early years be larger than they are under the present law, but that in readjusting the benefit structure we readjust it in such a way that as the system matures we reach a level of annual benefit cost no greater than our present estimated annual benefit cost. And that's been the problem that's confronted us for three years. We tried to work on the benefit schedule so that we wouldn't have a permanently higher annual benefit cost.

H.M.Jr: How does that work? You mean you begin to pay the younger people - I mean just how does that work out in practice?

Altmeyer: We pay the older people who are retiring in the early years more in proportion to the contributions that have been made on their behalf.

H.M.Jr: That's a change in schedule?

Altmeyer: That's a change in schedule, but the schedule we propose to change in such a way that as the system

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goes on year by year, the benefits in proportion to past contributions are not as great. Therefore you come out in 1980, when we figure the system will be matured, at an annual benefit cost no greater than the present law.

H.M.Jr: It will be no greater.

Altmeier: No greater.

H.M.Jr: Over how long a period?

Altmeier: Never any greater.

H.M.Jr: Oh.

Altmeier: The second big question, it seems to me, confronting the Treasury is, how shall these benefits be financed? Under the present law, as you know, it is contemplated that all of these benefits shall be financed out of payroll taxes. So the question is whether we shall continue the present policy laid down in the law of financing these benefits entirely out of payroll taxes for all time to come, or whether we shall recognize that eventually there would be some contribution out of revenues derived from other than payroll taxes.

The Board's recommendation is that the present schedule of payroll taxes not be disturbed. There is a one-half percent increase every three years until 1949, and we recommend that that schedule not be disturbed, and that after that date, when the cost of benefits, annual cost of benefits, exceeds the annual payroll taxes, then the Federal Government undertake to finance that deficiency out of other than payroll taxes, in some proportion, we don't say what proportion, depending upon how much of the population is covered under the old-age insurance system. At present we estimate that there are about 70 percent of the - 75 percent of the workers covered - not of the gainfully occupied, but of the workers covered, and that percentage increases as time goes on, automatically, because people are in for a portion of their working life and build up certain benefit rights. So that in the course of years, even without any amendment to extend coverage, you will get a considerable proportion of the gainfully occupied

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population having developed some rights under the old-age insurance system.

Well, summing it up in a nutshell, I think the most important question before the Treasury is whether it will recognize the principle of making contributions out of other than payroll taxes at some time in the future.

H.M.Jr: Is that what is known as the three-way plan?

Altmeyer: The three-way plan. I think the timing of when those contributions shall be made, and the amount, are subsidiary questions.

Bell: Do you think the maximum amount that the general taxes might contribute would exceed a third?

Altmeyer: Should not.

Bell: Even if you adopted the maximum program in your report, it would not exceed a third of the cost out of general taxes.

Altmeyer: You mean retaining the present tax schedule?

Bell: Yes.

Altmeyer: I think you'd have to step up your present payroll taxes eventually, maybe 30-odd years from now, from three percent to perhaps three and a half percent each, or even four percent each, if you kept the Government contribution down to one-third. If our original estimates are correct, then they would not have to be increased. I mean you could have a three-way split with the present payroll taxes. But the evidence that we have collected since the Act's been in operation indicates that our estimates were probably too low. But as years go by we may find out they were all right, or even too high. It's too soon to make any definite estimates.

H.M.Jr: May I ask a question? Starting these benefits in '40, would that - how much does that mean in dollars that would go out of the Treasury?

Altmeyer: Well, it depends upon how far Congress goes in

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liberalization. I don't think that in the year 1940 under any conceivable plan you can get a great amount of money out in benefits without destroying the principle of contributory social insurance.

H.M.Jr: But that - but I mean starting it - there must be some dollar figure.

Altmeyer: Yes, yes.

Bell: You estimated, didn't you, \$50,000,000 in the last six months of 1940 if you started January 1.

Altmeyer: Oh, more than that.

Bell: Well, I've seen some figure of \$50,000,000 as a minimum.

Altmeyer: As a minimum, that's right.

Hanes: Nearer 500 million.

Altmeyer: It conceivably could go up to 500 million.

H.M.Jr: Johnny, should Blough be here?

Hanes: I'll

H.M.Jr: I'll get him.

(On phone) Tell Blough to come in, please.

Altmeyer: If we started benefit payments January 1, 1940, as an extreme outside figure you might be able to pay out benefits of half a billion dollars. I think it is more likely that you could not do that without destroying the principle of contributory social insurance, and that it would be closer to 100 million dollars. That is my off-hand guess.

H.M.Jr: Well, what's the answer? I mean what I'm trying to get at is - there is this one school of thought which says we shouldn't increase the taxes by one percent, shouldn't increase it from two to three. Now, one percent amounts to about 300 million, doesn't it? What?

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Altmeyer: 250 million dollars, about.

Bell: 250 million.

H.M.Jr: Well, does starting the benefits in '40 offset - I mean on the basis of net contribution, does starting the benefits in '40 - would that about equal the one percent that ...

Altmeyer: It might, but I - of course, our judgment is that this is a social insurance system and that we shouldn't be looking at 1940 and deciding what we're going to do either as regards benefits or taxes just thinking of 1940. I'd rather see the system scrapped, I think the country would be better off if we abandon the whole idea of contributory social insurance, than to think we could run a system of contributory old-age insurance on a year-to-year basis and make it the tail to the Government's fiscal policy. I think it should be just the other way around. I think that's where we split entirely with the other school.

H.M.Jr: Well, I'm going to expose you, if you don't mind, in a minute or two, to that school - if you don't mind.

Eccles: He's been exposed before.

(Blough comes in)

H.M.Jr: Now, Professor Brown, did - I mean I've got to keep refreshing my mind all the time. On this question of starting the benefits in 1940, are the Advisory Committee and Social Security one on that?

Brown: Yes indeed.

H.M.Jr: Yes. Now, on continuing the tax program the way the law is written?

Brown: The preponderant majority of the Council favored the continuance of the step-up, that is, going to one and a half in 1940. There was a minority group that favored holding the tax down on certain provisos which were related to the cost of benefits.

H.M.Jr: Mr. Altmeyer, are there other things that you want

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to bring up that are up to the Treasury besides this?

Altmeier: Well, that's the category of the benefit cost. But as I say, there's the other category of questions: whether the handling of the funds shall be altered. That doesn't involve ...

H.M.Jr: Well, I think I'm right, am I not, Bell, in saying that whether you're a trustee or whether you put it in another fund, it all amounts to the same thing when you're all through, doesn't it? I mean the money is there; until the budget is balanced we've got to use that money, unless we expect to sterilize it. Isn't that what it amounts to?

Bell: That's right.

H.M.Jr: I mean all these arguments on that, I think, are perfectly silly. You can have a board of trustees and the Chief Justice of the United States and a few other people, and put it there, and if the money is there, is he going to sterilize a billion dollars or - if it's the Chief Justice - or is he going to give it to the Treasury and we're going to use it and borrow a billion dollars less. I mean I think that personally on that I see perfectly clearly. I mean it's just - as far as I'm concerned, it's a perfectly silly argument.

Altmeier: There's only one thing

Brown: Well, there, Mr. Secretary, ...

H.M.Jr: I mean these other things I'm not so sure of.

Brown: The Council saw that you might say technically the position is the same, but they felt very definitely that as a matter of public understanding - that the great majority of people do not understand these fiscal arrangements and that they do understand the rather age-old arrangements of trusteeship, and that while the actual arrangement of funds would be similar, that there would be an entity they could look to as being trustees of the old-age insurance fund.

H.M.Jr: Well, of course, Professor Brown, I'm willing to say

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publicly - we're trustees for somewhere over - exclusive of the stabilization fund, we're trustees for over five billion dollars - the Treasury. I say that the Treasury Department is a trustee and if the Congress hasn't got confidence, then let's take all the money away. See what I mean? But if they have sufficient confidence to let us handle five billion dollars worth of funds, plus the stabilization fund - seven billion dollars - if they haven't got confidence, then take it all away, I don't want any of it.

But I mean the Government Life and all these other 69 trust funds that we have - up to now I don't think anybody in Congress has ever said we don't administer these things honestly, and it's a question of, when the thing is placed with the United States Treasury, either they have confidence or they don't. I'd rather, if they don't have confidence, let them take it all away. I mean I'm willing to say that publicly.

I think this whole thing of this thing being there - I don't think the people would say that they really want to understand it - I mean the politicians that argue about it.

Did your group feel strongly on that?

Brown:

Well, you see, the Advisory Council group throughout its existence had this problem coming up repeatedly, and it felt that the simplest thing to do to avoid these misunderstandings in the case of a very large fund which affected practically every wage-earner was to make this simple arrangement of trusteeship; that probably the actual officials involved, or the arrangements, would be very similar.

There is a certain British precedent there: that it would be largely nominal, but yet would be one of those symbols that make for public understanding.

W.H.J.F:

Well, as far as I'm concerned, as I say, I don't - I mean as long as they don't try to sterilize the money, I don't care. But if they want to tie it up and lock it up so we can't use it, then I do care. But if they want trustees, why, they can make the Chief Justice of the United States a trustee if they want to. You know what I mean?

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Brown: Yes.

H.M.Jr: Let me just - Mr. Altmeyer, supposing we say - I would say, unless some other person - I'll give them a chance in a minute - I would say that the decision to start the benefits in '40 as against '42 - I would say that that was your decision.

I don't know whether anybody wants to talk about that - do you, Mr. Eccles? - the decision as to when to start the benefits?

Eccles: Well, the sooner the better. I certainly wouldn't object to starting them in '40. I think that if the Social Security doesn't do something about starting them in '40 - I think Congress will anyway. It's just a question of whether the Administration is going to provide a leadership in this scheme, or whether it's going to be taken away from them by Congress or by the Republican Party next year. I mean that's what you're up against.

H.M.Jr: Well then, as far as you're concerned, you're in sympathy.

Eccles: I'm certainly for starting them in '40.

H.M.Jr: Mr. Delano?

Delano: That's our idea.

H.M.Jr: Mr. Ruml?

Ruml: Well, I can't answer that question without saying something first. May I?

H.M.Jr: You can say anything you want.

Ruml: It seems to me the fundamental questions here are whether the Social Security program as a whole is to be deflationary, inflationary, or neutral. I've been looking at it from the standpoint of fiscal and monetary policy. If for political reasons it must be deflationary, then some offset to that must be found elsewhere for the time being. And accordingly, it seems to me that anything that could be done prudently that will make the burden of carrying the deflationary

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load of the program less on the budget as a whole would be all to the good, because as long as it has to be carried at the present time it will appear as a deficit in the budgetary operation and will tend to disturb the general public confidence with respect to the handling of the rest of the operation.

- H.M.Jr: well, but getting back to this particular question of starting the benefits in '40?
- Ruml: I think it tends to make a smaller burden on other aspects of the fiscal and monetary operation.
- H.M.Jr: Dan?
- Bell: I think they ought to be started in '40.
- H.M.Jr: John, have you got anything to say?
- Hanes: I believe they should be started in '40.
- H.M.Jr: You're (Brown) on record, aren't you?
- Brown: (Nods yes)
- H.M.Jr: Currie?
- Currie: (Nods approval)
- H.M.Jr: Well, who doesn't think they should be started in '40? All right. At least we've got agreement on one thing for you. Now, on the next thing we're going to have a little argument.
- Altmeyer: May I ask, does this also include the liberalization of the benefits in the early years?
- H.M.Jr: Well, I didn't think - I mean I don't know whether anybody wants to take a position. I mean I didn't want to take a position because, if I may say it, this group - my position has been that Mr. Altmeyer is the architect and draws the plans, and he submits them to me and it's up to me to finance them, and I don't want to - I'm the contractor and not the architect. Now, if somebody else wants to be consultant to Mr. Altmeyer, it's all right. I mean does anybody? That doesn't - I mean I'm just stating my

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own position. Does anybody want to get in on that question?

McCles: Well, it seems to me that I see no purpose of this committee, as a Fiscal and Monetary Committee, considering it at all unless we're going to consider it from the standpoint of effect upon the national economy. We discussed this whole budgetary matter and submitted to the President in December a program with reference to an 80 billion dollar income as an objective, and it seems to me that this program here should be considered in the light of a recovery program. And if the program as is proposed by the Social Security now is put into effect, we ought to recognize its deflationary effect and be prepared to offset that deflationary effect by other appropriations.

and so it seems to me that we have - as a Fiscal and Monetary Committee we have to approach this from a standpoint of its general effect upon the economy and what is the objective of fiscal and monetary policy.

H.M.Jr: Well, I'm not arguing, but I've got a time factor here which Congressman Cooper raised - it was a day or two ago - he wanted me to come up this week, and I didn't want to go up this week without having a chance to talk with you people and get your advice on this thing, and I don't think that the President's ever committed himself definitely yet. At least, he hasn't in any conversation with me. Has he with you, Altmeyer?

Altmeyer: Yes, he apparently favors the 1940 beginning date and liberalization of benefits in early years.

H.M.Jr: Has he committed himself on the increase in the taxes?

Altmeyer: I don't think he has.

H.M.Jr: I don't either, and that's

Bell: He almost endorsed the report that went up, in which they didn't exactly recommend, but almost recommended that this present schedule of taxes remain. Is that right?

Altmeyer: My discussion with him was upon the assumption that

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the present schedule of taxes would remain, and there was no question raised on that.

H.M.Jr: Well, from what he said the other day, I think he's changed, and that again is ...

Eccles: I think so too.

H.M.Jr: I think he's changed. I haven't. And that's another reason why I asked for a meeting, and to have you there, because I thought you were under the impression he hadn't. But I think he has. And as I say, while this - Marriner, I realize personally it's only one piece of it, but I've got this - I've got a time factor, and I wanted to know where you fellows stood, and I thought it was only fair to Altmeyer that he sit in while at least this group was making up its mind.

Eccles: We had a two-day session or two while you were away, and so Mr. Altmeyer knows

H.M.Jr: But he didn't take your advice.

Eccles: Who didn't?

H.M.Jr: The President.

Eccles: We never discussed it with him.

H.M.Jr: You sent him a memorandum.

Eccles: No, the memorandum never went to him.

H.M.Jr: Oh, I didn't know that.

Eccles: No, there was no memorandum ever went to him. Dan got sick. In the meantime - this was on a Friday we were to go over; we were to go over Friday afternoon. Dan got sick, and in the meantime the report of the Board went over Saturday; it was signed and went up. So we never - we just dropped it.

Bell: I thought the report went over.

Eccles: The report never went over.

- H.M.Jr: I never knew that. I may have known it, but
- Eccles: The thing never was discussed with the President.
- H.M.Jr: Well, I was under the impression that it had been. Well, anyway, that still brings us back to the important - I think the important thing is to get down to the question of the increase in the taxes.
- Witneyer: May I say a word on that from the social insurance standpoint? I don't want to presume to talk about the fiscal and monetary end of it. But from the social insurance standpoint, I think we're at the cross-roads on this business, and if we can't make the contributory insurance principle stick in this next year or two, it won't stick at all and we go to a system of free pensions financed out of general revenues; and I think it's right in the balance now.
- Now, the thing that disturbs me is how to maintain a reasonable balance between contributions and benefit payments in these early years and impress the public with the fact that you cannot pay increased benefits unless you make increased contributions. If we can't get that idea across now, we'll never get it across in the future.
- Even under the present law the amount of benefits that are paid to an old person who retires in 1942 is 72 times as much as he contributes. Now, that's going a long ways from the principles of private insurance. and I feel strongly that if at the same time we liberalize benefits, increase benefits, we say we can cut taxes, that the public will be entirely confused as to what is meant by a contributory insurance system, and that the next time we come along to Congress and say we have to increase taxes, there will be much question about whether it's all worth the candle - "Isn't this just a huge book-keeping arrangement where you go through a lot of motions, but after all it doesn't amount to much, and why isn't it much simpler to pay people thirty, sixty dollars a month out of general revenues and have done with it?"
- That's the problem as I see it. Now, there's no country in the world that speaks of these as taxes.

That's the first unfortunate thing that we have to contend with: that we speak of these payroll taxes as taxes. They're spoken of as contributions in every other country that has a contributory old-age insurance system, and that brings home the close relationship between the two.

And secondly, there is no country in the world that I know of that has started with such a low rate of contributions in comparison with the benefits promised, as we've started with. Under our proposals, the ultimate benefit cost may be six billion dollars a year in 1980. It will surely be between 800 million and a billion dollars probably in the next five years. We're headed for tremendous annual costs. And it seems to me just folly from the standpoint of maintaining an insurance system not to recognize the years to come - and I don't mean 1980, I mean the next five to ten years - in our financing arrangements, rather than to just look at 1940.

It seems to me that it is most encouraging that the leaders in both factions of labor and the leaders among the employer groups have endorsed the step-up in 1940. Now, I don't know of another tax, if you want to call it a tax, where the people who pay the tax say, "We're ready to pay the increase." Now, it is certainly strange if the people who pay the tax are willing to pay the tax and the increase in tax, that the Government should say, "Well, you don't have to pay it."

And I think the reason they're willing to pay it, these people who sat in on Mr. Brown's committee, is that they recognize that unless we establish this reasonable relationship between contributions and benefits, we're sunk on this whole approach to social security.

Brown:

Mr. Secretary, I'd like to corroborate that. I feel very strongly on this point: that should the tax rates not be increased to one and a half percent in 1940, that you're definitely endangering the whole contributory program. I think you're involving sums of money far, far in excess of these sums in 1940-41-42. In other words, it has only been in the last three years that the American wage-earner, the American employer, became aware of the principles of contributory social insurance. We're still at a very

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delicate stage in public education. We haven't helped that public education by calling these taxes. One of the reasons the Advisory Council was interested in the placing of funds with trustees and so forth, was to give the notion to the people that this wasn't the ordinary type of tax, but it was a contributory social insurance program.

Now, should the one percent continue and the adjustment of rates of contribution be altered from time to time, not because of the social insurance program but because of other fiscal or credit problems of government, you very soon begin to lose the sense of relationship in the mind of the wage-earner and the employer that the contributions in turn bring about the benefits. And I feel that is particularly true in the case of a change made in 1940, when there is the probability that benefits will be enhanced; that if taxes can be held down at the very same time that benefits are enhanced, you have a double reason for assuming that this is not contributory social insurance, but it's a sort of a tax program on one hand and a more or less free pension arrangement on the other.

Now, we have tremendous pressure toward free pensions, and it doesn't take much of a spark to encourage Congress to switch to the free pension idea, away from contributory social insurance.

And I'd like to say too that I've talked with labor leaders - I talked with George Harrison last night - it happened that he was in Princeton - about this very thing, and he is well aware of the problems because of his association in the railroad field, and he felt very definitely that both A.F. of L. and, to the extent he knew, C.I.O., were agreeable to come along definitely on this one and a half, on the assumption that it did identify the system as contributory social insurance.

On the other hand, from the testimony of Folsom and Swope and others among the employers, those on the Council and many others who followed the thinking of the Council, felt very definitely that if we were to have a contributory social insurance scheme, that this first step-up should go in to identify it

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definitely as a social insurance scheme.

Altmeyer: I just want to add one point, that regardless of whether the step-up is made in 1940, the costs are going to be such in the next five years that there will have to be step-ups unless there is going to be considerable Government contribution out of other than payroll taxes; so that the net result will be that instead of this established known step-up each year - each three years of half a percent, you will have irregular, unpredictable step-ups, and it seems to me from a fiscal and monetary standpoint that the deflationary effect of uncertain step-ups in payroll costs is much greater than that of the known cost that you can calculate and know from now until 1949 where you stand.

And my understanding is that this 250 - that what we're talking about really is 250 million dollars, and that's about three percent of the Federal budget. And I don't presume to talk on the fiscal and monetary side of it, but it does seem to me that we ought to pause when we're considering this three percent of the Federal budget and decide what the effects upon the social insurance system may be when we undertake to work on the three percent.

H.M.Jr: Now, who, so we don't - what one person would like to take the opposite side from Mr. Altmeyer? Who wants to argue on the other side from the increase in the contributions - see, I've learned - from one to one and a half? Who wants to take the other side?

Accles: Well, I'm willing to do it. I don't want it to appear that this is all a one-sided affair, and nobody else seems to speak up here for the honor.

H.M.Jr: Mr. Altmeyer is my guest, and I thought if we'd let one person argue with him ...

Accles: I think Mr. Delano or Mr. Ruml or Dr. Currie here could take it on just as well as I could. Would you like to take this on, Beardsley?

Ruml: Provided if my statements are not in conformity with what the rest of you think, you'll supplement, amend, destroy, or whatever else is necessary.

Well, I think it's a terribly difficult problem, because it's perfectly clear that, as has been pointed out, the principle of the contributory plan is to a certain extent at stake. Of course, it is also at stake in the question of whether or not you can maintain an increasing level of business and national income in 1940, because if you run into another 1937 in 1940, your contributory plan is out anyway.

Now, therefore, it seems to me that the problem is this: To what extent can the program of the Social Security Board, within the frame of its policy, be compromised, if you please, with the exigencies of the present economic situation, and at the same time maintain what is of value in terms of the principles that they have?

Now, accordingly, you'd look in two directions for help from the Social Security program. One is in terms of the liberalization of the benefits that seem reasonable and prudent and would be accepted by the public as within the frame of policy of the Social Security Board.

The other thing you'd examine is whether or not the income side of the Social Security program can be modified so as to, again, be less of a burden on the general business situation than would be the case if the present plan goes through.

Now, it would seem to me that, although I haven't been in any of the conferences - that it would be entirely possible for the program to be justified in terms of a three-way contribution of the Federal Government, the employers and the employees, maintaining the contribution principle, but for the time being at a somewhat lower rate. If that is not done, you will have serious alternatives, it seems to me. You will have the necessity of maintaining over a longer period of time a Federal deficit in the ordinary budget operations, unless someone is ingenious enough to devise extra-budgetary corporations that can operate outside the budget, and progress on that line has been, I think, rather slow and very difficult because you run into the great difficulty of competition with private business and the other criticisms that are raised toward that sort of

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operation, that it's a subterfuge, and so forth.

The other danger you run into is the danger of precipitating a deflationary movement in 1940 and the Social Security plan having to take the brunt of it. Now, \$250,000,000 doesn't sound large in a budget of \$8,000,000,000; \$250,000,000 is large in terms of a deficit and must amount to somewhere between - coming from this source of revenue, must amount to, oh, between half a billion and a billion dollars national income. Well, that's a significant amount. The significance of the national income is not in terms of its absolute amount, but its marginal effect on profits. In other words, at \$62,000,000,000 a corporation is most likely losing money, and at 63 or 70 most of them are making money. I don't say there aren't other effects that cause national income to go up and down; but, just isolating this particular effect, I think it's a substantially serious burden to throw into the business picture in 1940.

Eccles: Is that all you've got to say?

Brown: Can I, Mr. Secretary - can I take up that

Ruml: Well, I'd rather - if I didn't make a complete statement, wouldn't it be better if we got more, because I haven't been in conference with these people at all, and I'm simply talking without any benefit of consultation.

Eccles: Do you want me to say something on this?

H.M.Jr: Sure. I'm only - I mean I'm here both as Chairman and I'm here with my own responsibilities, and I haven't made up my mind. I mean I'm listening and I'm going to have to go up some time next week and take a position, and my mind is still open. Otherwise, I wouldn't ask you fellows over here. I mean I'm both a member of the Committee and I've got responsibilities as Secretary of the Treasury, and my mind is still open. And I'm not

Eccles: I

H.M.Jr: And as Professor Brown knows, we have had meeting

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after meeting, and on this question you've never heard me take a position; I've listened up to now.

Brown: Right.

H.M.Jr: I haven't taken any position. I don't know what the answer is.

I'm supposed to be at the White House at 11:30; if we don't get through, I'd be glad to meet again at 10 tomorrow. I'd be glad to meet again at 10 o'clock tomorrow.

Eccles: Yes. Got about 15 minutes to get through. It would be pretty difficult to do that, wouldn't it?

H.M.Jr: Why not just stop here? And could you (Brown) stay over or not?

Brown: Yes.

H.M.Jr: Because we're going to make up our minds. I mean you'd like to be in at the killing. What?

Brown: Yes indeed.

H.M.Jr: I think maybe it would be better. I'd like to see one thing - maybe it's all ready - and that is this difference of how much money will go out in '40 by advancing these payments as offset by the increase in the tax. That ought to be fairly easy, oughtn't it?

Haas: Depends on what plan

Bell: We want a minimum.

H.M.Jr: We're talking in general amounts. What does it mean if we're going to increase the tax? Then also, what does it do to this other thing, the reserve fund?

Eccles: How much will they take in in total if they increase the tax? What are you taking in now? What will you take in if you increase the tax? What will you put out? Which means the difference is impounded in the

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reserve fund, which means the Treasury has got to borrow it, and so the deficit

H.M.Jr: What effect will this have on the reserve?

Altmeyer: It will cut the reserve, we estimate, from 47 billion to about six billion dollars at the maximum.

H.M.Jr: Cut it how much?

Altmeyer: To six billion dollar maximum reserve.

Bell: In 1980.

Altmeyer: In 1955 or so you'd reach your maximum, and then you'd have to maintain your reserve through Government subsidy.

Eccles: What does it do next year? That is, by way of - you pull in in taxes, if you increase this, about a total, as I understand it, assuming a 1937 payroll - if conditions are the same as in '37, you'll pull in in taxes close to 900 million next year, won't you?

Altmeyer: I didn't think it was that much. I thought it was about 750.

Brown: Could I make two or three comments there before we close?

Mr. Ruml spoke of the possibility of a neutral position of the Social Security program.

H.M.Jr: It would be wonderful if you could fix one up for me; it would be marvelous.

Brown: Mr. Viner and others at our conference felt very strongly that we should do what we can to preserve that neutral position. Knowing, however, that the program has already been compromised to fiscal necessities, first of all in the gradual step-up and then taking one of the two alternatives that Mr. Ruml spoke of, the increase in the early benefits, we feel very definitely that if you compromise still further and

both increase benefits and decrease taxes, that you've compromised to the point of virtually wiping out the close connection in the minds of the people as to what is a contributory program.

Now, as far as 1937 is concerned, the Social Security taxes did take a very definite step-up, because you had a one percent for unemployment insurance that was not collected until the early part of 1937; then you had an increase of two percent on your state unemployment insurance taxes, plus the Federal one percent. So that we'll never have a time with as rapid a step-up in Social Security taxes as we had in that year; at the same time there were practically no benefit payments.

H.M.Jr: In thirty- ...

Brown: In '37.

H.M.Jr: seven.

Brown: So that was, you might say, the peak of the impact of the Social Security program on business. Now, from now on, there's a half percent already expected; as Folsom said, he assumed it was already integrated in business planning. There's a very definite difference from that '37 situation.

Altmeyer: Well, answering your question, Mr. Secretary, taking 1940, there is no question in my mind that you cannot step up benefits sufficiently perhaps even to absorb the 250 million dollars additional tax. I don't think you can do it without just letting down the bars too far and destroying the contributory principle. So if you're looking to 1940, you have to recognize that there is going to be more money collected than paid out.

Eccles: By how much?

Altmeyer: Well, I said that the conceivable maximum to my mind is \$500,000,000 that could be paid out in benefits; but my guess is it would be closer to \$100,000,000 in benefits.

Eccles: You'd collect seven or eight hundred million dollars.

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- Bell: Is that fiscal or calendar year?
- Altmeyer: I'm talking about the calendar year.
- Eccles: You'd collect 800 million.
- Altmeyer: 750 to 800 million, yes.
- Eccles: So that would mean then you'd be taking out in these taxes - call them contribution if you want, but it's a tax, I think, on consumption - so you pull that out and you put back a hundred million; so you've got 600, 700 million more that you've taken out, so that it means you've got to have that much more of a deficit, that much more W.P.A. or other expenditures, to put back into consumption what you pull out in taxes.
- H.M.Jr: Well, if it's only a difference of 150, I think Mr. Wallace can fix that up for you by Monday three or four times over.
- Bell: Parity payments will take care of that.
- Brown: You've got old-age assistance payments gradually rising.
- Eccles: You've got those anyway.
- H.M.Jr: You take the parity payments - 220 million parity payments; we're not going to get any taxes to offset that. I think in fairness to Mr. Altmeyer and to the budget, we ought to take some of the other things that are going to happen in 1940 and not just Social Security and see what they all add up to. Now, we've got 220 on parity payments; the agricultural program is going to be from one to five hundred million dollars extra.
- Altmeyer: I ought to add that my guess is Congress will liberalize other features of the Social Security Act which will cost us about 75 million dollars more. I think that's rather certain.
- Bell: Talking about children
- Altmeyer: Children and old-age assistance. In fact, I think

we'll be lucky if we get by with 75 million dollars.

H.M.Jr: Currie, why don't you in the next 24 hours have a - Mr. Bell can give you five minutes now, he can tell you some of the things which may happen, which are in the wind, such as cotton and so forth and so on, which easily may total up to a billion dollars. I think if you could have that as an offset, so that we just don't concentrate on Altmeyer and say, "Well now, here's one thing that mustn't be done, but it's all right for Wallace to do it, it's all right for somebody else to do it; but Altmeyer, who is looking after how many million people - we can't let him run his thing, see? See, he can't do it but everybody else can." And after all, if Bell can tick off to you several hundred million dollars in about five seconds

Bell: I don't know ...

H.M.Jr: ... it's interesting. What?

Currie: Yes.

H.M.Jr: Don't you think so? And would you gentlemen come back at 10 o'clock tomorrow - those of you that could.

Coles: I can.

H.M.Jr: Well, I'm available, anyway. Could you (Altmeyer) come back?

Altmeyer: Yes, be glad to.

H.M.Jr: It's helpful to me. And what I'd like to do is, when I go over Monday I'd like to if possible be in agreement with you, so that you and I at least when we see the President will agree.

Altmeyer: Well, is the President going to reach a conclusion before we meet with the legislators or at the time we meet?

H.M.Jr: Twelve to one on Monday.

Altmeyer: But the legislators are going to be there.

H.M.Jr: One - Jere Cooper. Maybe you want to see him before.

Altmeyer: Well, I'll see Jere right now, but not to sew him up on this.

H.M.Jr: Well, Jere Cooper will be there.

RE SOCIAL SECURITY RECOMMENDATIONS

March 18, 1939.
9:45 a.m.

Present: Mr. Bell
Mr. Haas
Mr. Blough
Mr. Altmeyer
Mr. Brown
Mr. Duffield

H.M.Jr:

The reason I asked you gentlemen to come in is, first, I think I've got a solution and I wanted to get the benefit of your advice without the monetary experts around. Dan and I are just a couple of practical fellows, see?

Now let me read something which was given me in confidence, a paper of a page and a half that McCles wrote for the President, stating his position. And out of that I got an idea. Has anybody seen this?

"Controversial issues raised by the report of the Social Security Board...." - you (reporter) needn't take this. (Reads further in memorandum)

Now get this next paragraph:

"In view of the foregoing considerations, it would appear advisable to defer approval of scheduled increases in the tax rate."

Then the next paragraph to the last one:

"If the tax rate increase is postponed at this time little difficulty in securing increases in payroll taxes in the future may be anticipated if such tax increases are actually necessary to finance current benefits and if, at the same time, a portion of the costs of such benefits is borne out of general taxation, as is the case in England and other countries."

Now he says, going back -: "In view of the foregoing considerations, it would appear advisable to defer

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approval of scheduled increases in the tax rate."

Well, of course, he has it wrong. But if you people are for a neutral position, I think I've got something which is so easy and so natural, I just wanted you to hear it before. That is this: that my position will be that I am not going to recommend any changes in the existing law until I see whether Congress advances the benefits of the aged from '42 to '40; if Congress should do that, then I'm in favor of letting the tax increase go into effect. O.K.?

Altmeyer: All right. Fine.

H.M.Jr: And I'm furthermore going to say, "This is one of the really fundamental pieces of New Deal legislation, and I'm opposed to anything that may undermine it."

Now, I was groping for something. Now, Eccles just puts it the other way around. But he says he's saying the thing - "In view of the foregoing, it would appear advisable to defer approval..." You can't defer approval of an existing law.

Altmeyer: No.

H.M.Jr: But if ...

Bell: When was that written?

H.M.Jr: The 13th. Handed to me yesterday.

Bell: He gave it to you yesterday?

H.M.Jr: Gave it to me yesterday. Going to send it to the President.

I think I've got my position. I think I can stand on that.

Altmeyer: I think so.

H.M.Jr: What?

Haas: I think so.

H.M.Jr: Huh?

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Altmeyer: I think so.

H.M.Jr: What do you think, Dan?

Bell: Well, supposing they don't advance the benefits to '40 and increase the schedules of the benefit payments. Are you willing for the tax to drop out?

H.M.Jr: Say that again.

Bell: If they allow the law to stand just as it is, with no increase in benefits and no advance in the date.

H.M.Jr: No, then I don't want the tax to go into effect.

Bell: That doesn't quite follow your ...

H.M.Jr: Oh yes, it does.

Bell: No. You say you're not going to recommend any changes in the tax law until Congress acts on the benefits.

H.M.Jr: That's right.

Bell: And if Congress acts on the benefits, increases them, advances the schedule, then you're going to approve the increase in tax going into effect. Then the question arises that you on the other side insist that the present schedule be changed - that is, not increasing the rate in 1940 if they don't do that.

H.M.Jr: I'm not going to insist on anything. I mean I'm on the basis - as I say, I don't think we ought to pass a tax bill until the last appropriation bill is passed. I've said that right along. My position is the same as that. I want to see what they do in the way of increasing the cost, and if they increase the cost then I think the tax rate should go into effect. But if they do nothing

Bell: Yes.

H.M.Jr: ... if they don't change the law at all and pass measures which will to a large degree

Bell: On the payment side, if they don't change the payment side

H.M.Jr: ... then the tax schedule should be lowered.

Bell: Is that your position? That isn't what you stated yesterday.

Altmeyer: That second thing, I think, is a condition contrary to fact.

Bell: Well, they postponed something yesterday, the consideration of it, and

H.M.Jr: Well, I think my position would be, if they leave - if they don't do anything on the benefit payments or anything, or leave it just at this time as it is, then certainly you couldn't criticize me very severely if I said, "Well then, let's postpone increasing taxes." You wouldn't have any row with me over that, would you?

Altmeyer: Well, I would.

H.M.Jr: I mean we're talking amongst ourselves here.

Altmeyer: The way I feel about this thing is, you've got your tax schedule in the law, people know what it is, and they know

H.M.Jr: You've got to be consistent. But from my standpoint, I'd be on safe ground.

Altmeyer: Of course.

H.M.Jr: Now, you've got to be consistent. Do you mind - this fellow is here advising me - would I be on consistent grounds?

Brown: I'd like to put it this way.

H.M.Jr: I mean you've (Altmeyer) got to stay consistent; it's all right.

Bell: I'd like to see you together.

H.M.Jr: He (Altmeyer) and I aren't apart on this thing. I don't expect him to say so, but

Brown: You're in a stronger position to stand for continuance

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of the one percent if benefits are not expanded. The point that I'm afraid of is that benefits are not expanded at all and taxes are kept at one percent, which means you're going to have a much lower over-all schedule of old-age protection.

H.M.Jr: Now listen, I up to now have been very careful; I'm not getting into anything on the benefits, whether they should or shouldn't, or how they should do.

But towards these people - I mean towards the Eccles theorists, I think my position is perfectly sound. Christ, I'm quoting right from his own letter; I'm quoting right from his own letter.

Altmeyer: Yes.

H.M.Jr: Now, whether he'll come my way as much as to say this - but if on the other hand I can get him to say that.... "If on the other hand these benefits are advanced, will you then be willing to say that the tax should go into effect?" - I don't know. See?

Brown: Well, one thing, Mr. Secretary

Altmeyer: I think that's good.

H.M.Jr: Now, whether you follow that ...

Bell: If nothing is done, what you going to do about that?

H.M.Jr: Well, we'll cross that bridge when we come to it.

Strictly in the room, if you would do the arguing, because I get a little restless in arguing with Mr. Eccles; I mean I'm known for that. And therefore I try to curb myself. But this is your shop and your responsibility. But I finally feel here that I've arrived at a position which is consistent, that it's friendly to your work, it doesn't interfere with your work and when you people go up on the Hill. And I can take the same position that I do on taxes: that no tax bill should be passed until the last appropriation bill is passed. In the meantime they may vote two, three, four, five hundred million, a billion dollars, for agriculture. Then look how silly this thing looks. They just pick on you - which is one

of the few really underlying fundamental things that we have done.

Brown: Mr. Secretary, I think it's better as you suggest there, to go on the basis of principle rather than to get into these precise figures; that is, just exactly what will one and a half percent bring, and all that; because the Eccles group have been citing all kinds of figures there.

H.M.Jr: Yes, I'm just going to stick to principle. If I've got to go up on the Hill - "Now gentlemen, just as I've said, now I don't want to take any position about changing the existing law as it affects Social Security as to revenue until you people decide what you're going to do about changing the benefits, and after I've seen that, why, then the Treasury will advise you. But if you increase these benefits and advance the law as is recommended in ..." - what do you call it, the President's report? Is that what you call it?

Brown: The Board's report. The President merely sent it up.

H.M.Jr: "... the Board's report, then I think the tax should be permitted to rise to one and a half percent, without getting into whether it's one hundred million or five hundred million." That's what you mean.

Blough, are you satisfied on that?

Blough: I'm satisfied. You will recognize, of course, that any failure to go up to the one and a half percent is in effect some reversal of the 1935 law. But aside from that I would say

H.M.Jr: But I'm looking for a position which is cooperative with the Board, that is good fiscal policy, and that I can personally believe in. Now, I can do this and believe in this, and I don't have to get into all of this fight.

George?

Maas: I think you're absolutely O.K.

H.M.Jr: Takes a month to bring out a mouse, but ... - what?

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Hass: Well, I think you're all right.

H.M.Jr: Don't you think so, Dan? I mean you could go up and you'd back me up on this, wouldn't you?

Bell: Yes, I'll back you up to the extent that they don't do anything, and when they don't do anything I'm still in favor of the schedule going into effect.

Brown: That's one chance in a hundred.

Bell: Well, I think that's probably right, but ...

H.M.Jr: But to go over there on Monday - I feel very happy.

Now, I walked down with McNeynolds. "e talked about it. I was surprised to hear Mac say that he was in favor of not increasing the tax. But I said, "Mac, do you know that they're going to start the benefits in '40?"

"No." He said, "Oh, that changes the whole picture." He said, "I didn't know that. Well, that changes the whole picture."

And incidentally, I was surprised that Hanes is one hundred percent for letting the tax go up to one and a half. Unequivocal. I didn't know where he was at. I mean I asked Hanes.

Bell: I think that's right.

H.M.Jr: I asked Hanes before he left. But a hundred percent for letting the tax go up.

(To Kieley) Are those other gentlemen here?

Kieley: No.

H.M.Jr: When Mr. Eccles and the others come, let me know.

Well now, are you (Brown) satisfied with your pupil?

Brown: (Laughs)

Kieley: Mr. Eccles and Mr. Delano.

(Following discussion transcribed as
separate meeting.)

RE SOCIAL SECURITY RECOMMENDATIONS

March 18, 1939.
10:00 a.m.

Present: Mr. Bell
Mr. Haas
Mr. White
Mr. Plough
Mr. Altmeyer
Mr. Brown
Mr. Eccles
Mr. Delano
Mr. Duffield
Mr. Currie

H.M.Jr: Well, gentlemen, to continue where we left off, Mr. Eccles gave me a memorandum which I took home and read last night and I read this morning, and there is one - next to the last paragraph - if you don't mind, I'd like to read it.

Eccles: All right.

H.M.Jr: Do you mind if I read it?

Eccles: Go ahead, read it all if you want.

H.M.Jr: No, I'll read the next to the last. Maybe you'd rather read it.

Eccles: No, go ahead and read it.

H.M.Jr: He said: "In view of the foregoing considerations, it would appear advisable to defer approval of the scheduled increases until it is known what the benefit payments adopted by Congress will amount to for the calendar year 1940."

Well, what I feel is this, and then you people can see what you think of it. What we do here in the Treasury - we like to take the position that they should defer any action on the tax bill as long as possible, until we can see what the various appropriation bills are; and, applying that same rule to this, and taking that - just paraphrasing what Mr. Eccles said, I feel this way: that I can take the position with the President, with the Congress, that until we see what Congress does about changing the present law, and also - I mean with regard to

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benefits, particularly old-age pensions, why, I won't take any position about making any recommendations to change the existing law as it affects taxes; but if the Congress should decide to advance the benefits from '42 to '40 and make other changes which are in the Board's recommendations, why, then my position would be that I would want to ask Congress to change the law as it affects the Social Security taxes.

Well now, Mr. Delano, that's the way I feel. Now, what's wrong with my position?

Delano: Well, I don't say that there's anything wrong with your position. I recognize that Mr. Altmeyer has made a strong position.

I have a statement that Ruml and I agreed on, and it's based on the best advice we're able to get from our Industrial Committee, who have talked about this a good deal - other than Alvin Hansen, whom we have consulted for some time.

H.M.Jr: Do you want to give it? Read it.

Delano: I'll just read the first.

H.M.Jr: Could I say one word before? I don't want you to feel - what I'd like to say before you read it, if you don't mind - I just want to say this: that I think this Social Security legislation is one of the underlying fundamental pieces of legislation that this Administration has put through.

Delano: I agree with you absolutely.

H.M.Jr: I want to do everything that I can to hold up Mr. Altmeyer's hand, and I think it is so important that I don't want to in any way do anything which he feels is going to undermine this Social Security legislation. And I think that

Delano: Well, I'd go so far even as to say that I have a high regard for Mr. Altmeyer's judgment and that I'm willing to give way finally to his decision if he will only weigh these points that we raise.

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"A Social Security program can act as a drag on full employment in two ways."

By the way, I wish it wasn't called a Social Security program. I wish it was Social Insurance. I think the public would understand it much better.

"(a) The taxes out of which it is financed may be levied in such a way as primarily to limit expenditures for consumption goods;

"(b) The program may pay out currently a much lower amount in benefits than is currently deducted in taxes."

And of course, in a time like this, we want to avoid that. If we were starting this thing out in boom times, we wouldn't worry about that; but at a time like this to be absorbing funds faster than you're paying them out - it's a serious matter.

H.M.Jr: Look, may I interrupt you? We're paying out four billion dollars more than we're collecting. I mean you can't ...

Delano: Well, of course, how you justify that is not my business at all.

H.M.Jr: Well, I don't try to justify it at all.

Eccles: Well, the budget shows you're not actually paying out more cash than you collect by four billion dollars.

H.M.Jr: Yes.

Bell: He's deducting the old-age investments; brings it down to about two eight.

Eccles: But it makes it appear four because of this, makes your picture look a lot worse than it is.

H.M.Jr: It's about what?

Bell: About three billion.

H.M.Jr: Three billion.

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- Bell: On the other hand, you're looking at these taxes as part of your budget structure, where as a matter of fact Mr. Altmeyer looks upon them as part of a separate system.
- Eccles: I know that.
- Delano: Well, I think Mr. Altmeyer is right in that sense; if you could regard this thing as insurance and not as
- Eccles: As long as you build up a reserve, the Government's got to run a deficit to use the darn reserve or use it to pay off the debt.
- Brown: Hasn't had any trouble so far.
- Eccles: I mean that's what you've really got, in principle.
- Bell: Haven't had any difficulty in the past ten years.
- H.M.Jr: I'm sorry to have interrupted you.
- Delano: "The present Social Security program has definitely acted as a drag on our recovery in both these respects. The character of the taxes, however, is probably less important than the lack of balance between tax withdrawals and benefit payments. This lack of balance exists even if allowance is made for payments on account of old-age assistance. To a lesser extent it is also true that taxes for unemployment insurance have not been matched by benefit payments.
- "Taxes resting on the lower income levels come almost entirely from consumption, whereas taxes on the middle income brackets would come partly from idle savings. There are, however, political difficulties involved in shifting the tax burden, and political advantages in retaining a sense of public responsibility by wide participation in the costs of the Social Security program.
- "In my opinion it is essential that payroll taxes should not be stepped up, as now provided by law, on January 1, 1940, unless these receipts can be

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offset elsewhere. We are running along on a low economic level with a condition of such stagnation that we have no adequate outlet for current savings. Under these conditions a Social Security program is an untimely compulsory savings program which seriously curtails the volume of consumption expenditures.

"I favor provision for a three-way contribution to the old-age insurance program - from employers, from employees, and from the Federal Government. This would involve no change in the incidence of present taxes, but would change permanently the incidence of taxes that must eventually be levied.

"So far as unemployment insurance is concerned, a strong effort must be made to raise the standard of administration in all the various states so that payments can be made promptly. The waiting period should be made as short as the requirements of a sound unemployment system will permit. Apparently also in many states the provision for benefit payments are such that the receipts from payroll taxes continue far into a depression period to exceed benefit payments."

I don't think it's necessary to read the supporting data.

H.H.Jr: Well, Mr. Hansen was down. I'll read it, but I - he was down and spent two days with us.

Delano: Yes.

H.W.Jr: Well, what you say here, Mr. Delano, wouldn't change what I said earlier.

Delano: No, I don't know as it would. I think about the only thing that I see in opposition is that, rather than increase this percentage to be levied on employers and employees, we think that the Federal Government should contribute one-third.

H.W.Jr: Well, they will.

Eccles: As I understand your ... You see, the tax goes into effect now if nothing is done.

H.H.Jr: Uh-huh.

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Eccles: It isn't a question of legislating to get the tax; it's legislating to prevent it. Otherwise it goes into effect next year. You said something about not taking a position on it until it was determined what the benefits would be.

H.M.Jr: That's right.

Eccles: I was just wondering from a practical approach how that could be done. Congress - this Committee, for instance, is going to have to report out a bill, and they will report out a bill, likely, if they follow Mr. Altmeyer's recommendations, that will call for - that will not change the present tax provisions, so that it would mean that the Committee of the House then would report out a bill requiring a tax.

Now, the question is if, according to Mr. Altmeyer, the benefit payments are not likely to be more than a hundred or two hundred million dollars - at the wildest guess, under the present program, they couldn't exceed five hundred million - whereas even if the tax isn't put into effect you'll collect next year close to six hundred million. So, in other words, even if there is no tax put in effect next year, you would not disburse as much as is paid in.

H.M.Jr: Is that right? I thought we made it up by 300 million dollars.

Bell: I don't understand. We would not disburse

Eccles: For instance, under your present two percent tax - it's two percent in effect now - you'll collect close to six hundred million next year, if the payroll next year is equal to the '37 payroll. Mr. Altmeyer stated, when we discussed this thing with him in January, that there wasn't possible an amount under their proposal - if everything was accepted, if they covered, if they broadened their program - greatly in excess of five hundred million that they would pay out in benefits; whereas yesterday he said he didn't think it would be more than a hundred or two hundred million. So in that case you would accumulate next year, even if you don't increase the tax, anywhere from a hundred million to five hundred million.

Brown: Well, Mr. Eccles, I think that that's one of the mistakes of that position, that you begin to figure in precise figures.

Now, fundamentally I feel that the most important things here are matters of principle, and that if you expand benefits and enhance their scope and begin them in 1940, you have very important matters of future planning there, much beyond 1940, matters of public understanding which justify going to one and a half, especially since you can't deal in precise figures anyway.

The reason for the Council's position was the number of variables involved in just exactly what those benefits would involve: extent of life, the number of persons that would retire at 65, and so on.

H.M.Jr: If you people are interested in how much cash would go out, are worrying that there isn't enough going out of the general fund, we draw on how much for state aid?

Bell: I think it's about 300 million dollars under the Social Security Act, not covered by taxes.

H.M.Jr: I mean you've got to take that into consideration.

Bell: What Mr. Eccles is saying is that we're not going to accumulate as much next year in the fund as we did this year if benefit payments start; so you're really going to pay out

Eccles: You won't accumulate as much; but the point is, you're still likely to accumulate, therefore why put the tax on to accumulate more?

Bell: I understood the first statement was we'd accumulate more. As a matter of fact, we'll pay out more and accumulate less.

Eccles: If you put no tax on next year, then certainly your pay-out would be closer to your accumulation; I mean you'd accumulate less. On the other hand, if you increased the tax, you put yourself about where you've been.

Bell: That's right.

Eccles:

So what I'm arguing is, why let the tax go into effect next year? It only adds to the reserve. Now, true, you're going to - you may run a heavy deficit and borrow the money in the reserve, which is - you certainly will do that in any case; you borrow that and a lot more. The point is, however, that you show a deficit here that is far more than the cash deficit really is, because of the fact that when borrowing from this fund you treat it just the same as when you borrow from the market.

Blough:

Would it be sound to say that what you are really balancing here so far as 1940 is concerned, is the looks of the budget against the effects that the action will have on the contributory system of insurance?

Eccles:

Well, I think this, that you've got a whole - if I can just say a word with reference to the whole trend of insurance, not only in this country but it seems to me in the world, with reference to getting away from a compensatory system to the extent that this thing is set up; and you take the British system, you take the Swedish system, you take what the German was up to 1930 - what it is now I don't know, but I mean up to that time - and you find that it's a contributory system but the governments are very heavy participants in those systems.

And here's just one paragraph on it, a short one: "The important fact remains that in Europe a definite trend away from reserve fund principles is apparent and that full reserve systems are practically non-existent. Almost universally it has been found that a self-supporting contributory system with full reserves has been impossible to maintain, and it has not solved the problem of providing pensions, and the principle has been more or less diluted by the introduction of current cost devices."

Now, of course, you know the drive for a pay-as-you-go insurance basis, which it seems to me has tremendous sponsorship. You take - I left practically won his election in Ohio on that basis. And the popular trend - if you'll take this Gallup poll analysis here, it's somewhat indicative, it seems to me, of the

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general demand for old-age pensions that are - from the figures here, the average, as I get it, is \$40 for a single person and \$60 for a couple. What they want - they want to get it now, in a depression period, and I think that you've got to - you've got to face this issue if you're going to preserve this system in any degree of soundness. It's important to preserve it and I'm for a contributory system. I think as a practical matter you can't operate the thing except on a contributory basis - that as a basis of accounting.

But I do think that we've gone - on this reserve principle, we've put it in at an unfortunate time, a depression period, and we've gone to a very unfortunate extent, and what I'm afraid that's going to happen is that the very people who were responsible for this social reform may be licked in part because it hasn't been effective in its benefits to the people that thought they were going to get benefits from it.

and looking at it from purely a fiscal and a monetary standpoint for next year, to collect more money into this fund, to increase the tax on consumption next year, which means a further addition to this reserve when the reserve at the end of the year will already be a billion 700 million, just seems to me fantastic and entirely unjustified.

Brown:

Mr. Eccles, I think you'll find that most of us that have been working on social insurance would agree with you as to this question of full financing, large reserve, and so on, but I think in your logic there you have pushed the pendulum much too far. That is, you want to balance your benefits to - your contributions and benefits, but you don't want to do so to the precise mathematical extent you would if you were thinking in terms of fiscal policy alone, because when you push that to that extent, you involve certain other important elements in social insurance, and that is that it's long-range planning and that graduated step-ups are necessary to educate the public mind that it is essentially contributory.

Eccles:

I'm not arguing that you can balance them out every year. I realize that's impossible. There may be

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some year when you will accumulate something in the reserve. I think next year you will accumulate something in the reserve even if you don't increase the tax. There may be other years when you pay out more than the reserve. Certainly in a period of high business activity your collection in the reserve is going to be greater than in a period of low activity. In such a period you may pay out more. I realize that the income in the fund is not always going to just be made to balance with the outgo.

But it does seem to me as a practical thing next year that to push for an increase in this tax is the height of fiscal fallacy - to do so; and also, recognizing the trend up there, I don't think you're going to get it anyway.

Brown: Well, on the side there of what happens in 1940, I think that those of us who are interested in preserving this plan feel it is highly critical, and that to change your policy of contributions within three years at the very time you're expanding benefits certainly tends to confuse the public mind as to the fact that this is essentially a contributory program for which they must bear a very considerable part of the cost.

Eccles: All you do is postpone the tax. It isn't that you won't put it on later when your benefits get closer to your income. You could easily postpone that tax a year or two years.

Brown: We think you're gambling.

Eccles: I think you're gambling to try to put this present program in. I think from a fiscal standpoint and also from a standpoint of the general public reaction to the present set-up, you're gambling with the Townsendites and all the rest of them when you stick to a program that collects eight, nine hundred million in taxes and pays out a hundred million. Now, I certainly think you're gambling.

H.M.Jr: That isn't correct, is it?

Eccles: Yes, it is.

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nease: No, it isn't correct. You're speaking on an accrual basis.

Eccles: I'm speaking of the tax you collect next year. If the tax goes into

Belano: Calendar or fiscal?

Eccles: Calendar year. If this tax goes into effect and if you have the same payroll next year as you had in '37, see, you'll collect close to 900 million in taxes; according to Altmeyer's statement yesterday, he doubted very much if you'd get out more benefits than a hundred to two hundred million. So that you'll be collecting more in this fund and these old people will see that and the propaganda is naturally going to be, "Why, you've collected this fund; you are now adding to it another 800 million, 700 million, and we're getting 150 million, 200 million." It just looks to me like that doesn't - from a practical standpoint, that kind of a thing jeopardizes your fund, jeopardizes the soundness of the fund.

Luffield: Looking at this from beyond 1940, have you considered the feasibility of using this program as a monetary or fiscal control device? I mean is it really flexible enough to work both ways? In other words, if you get into a boom period, would you then want to raise this tax?

Eccles: Well, I question if you'd want to do that. It seems to me, however, you can't devise any program that looks to what is going to happen ten years from now. We never have in anything; I don't think you can do it in this. There are too many uncertain factors. But this is the way this thing, it seems to me, would work: that in a depression year - looking to the future, when you get the benefits once in operation - you're very likely to pay out in some years more than you take in, that in itself would tend to cushion your deflation. It has worked that way in foreign countries, I understand. It's been very helpful in England, in that they had their old-age benefits going out, they had their unemployment insurance, and it tended to act as a cushion in a depression period. Whereas we, on the other hand, have been

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collecting in a depression period; we have been collecting the taxes in from consumption in excess of what we have been paying out, and it's had the opposite effect, that we will have collected into the two funds by the end of the year at least three billion dollars of taxes and

Duffield: What is their experience in another sort of business period, when you've got ...

Brown: Well, the British did that in the beginning of their unemployment insurance. Of course, fortunately, there weren't - business was relatively prosperous and the coverage of the fund was smaller. But I think - you take our case - that we did step up taxes pretty fast in '37, but that's water over the dam.

Eccles: That tax still is a burden. That tax is still there. Now you want to step them up still further, add to it.

Brown: But the issue now is a half percent on each at a time when both unemployment benefits and old-age benefits will be advanced.

Eccles: But you still are arguing for a further increase in the reserve, at a time when you want further business activity and prosperity; you want to put a further burden of taxation on consumption.

Brown: We're arguing for something deeper than that, and that is to uphold the contributory principle so that at a time of expanding benefits there be public understanding that costs must be planned for for more than a single year at a time, and that such expanded costs must involve taxes.

Currie: Mr. Brown, do you recall the original Committee report of Social Security in '34 - did it refer to the contributory principle?

Brown: Certainly. But there's been a change in the situation

Currie: Seems to me there's some confusion in tying up the contributory social insurance with a particular schedule of taxes and of benefits. As long as those

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covered are contributing to the fund from which benefits are paid, it seems to me that's the essence of the contributory principle. That doesn't depend upon any particular schedule of tax rates and tax increases. In fact, the original Committee didn't provide for reaching this three percent rate until 1947, I believe.

Brown: But understanding of the contributory principle does involve that at a time when benefits are being expanded, and when widows and dependents are being brought in - dependent children being brought in - that it be understood that all those things are paid for in part by the employee.

Currie: That's right, and as long as you have them paid in part by the employee, you have your contributory principle.

Eccles: Whether they pay 90 percent or 50 percent.

Brown: The impact of the change is what I'm talking about.

Altmeyer: The point is that on the reserve - I don't think we ought to mix up our discussion with the reserve at all. I have never been a full reservist in my heart. I have defended it because that was Administration policy, and this is the first time I've said I wasn't for it in my heart. I think it can be defended. I think an alternative plan can be worked out that is sounder.

But under this Committee proposal that you mention that was brought out in 1935, the reserve would have built up to 10 or 15 billion dollars, as I recall, instead of 47 billion dollars, and you're perfectly right in saying that there was a different step-up in benefit rates. But that doesn't affect our situation now, for this reason: that we've got a certain step-up now in the law and we've got a certain benefit scale provided in the law. Now the Board is recommending a liberalization of the benefits and a broadening, as Mr. Brown says, and so you've got the psychological situation that you already have a scale of taxes laid down in the law and a recommendation that the benefits shall be liberalized and broadened. Now if at the same time that you

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propose to increase benefits and that sort of thing you propose to change the tax

Eccles: You don't change it, you leave it where it is.

Brown: We change it from the schedule.

Altmeyer: We change it from the schedule.

Eccles: What I understand is that you keep your two percent rate instead of increasing from two to three percent.

Altmeyer: The present law provides for that automatic step-up for three years.

Eccles: The public aren't conscious of the fact that there's a change. They pay the same tax if it's left unchanged, and if you put this increase on in '40 they pay the increase.

Altmeyer: They're perfectly conscious now that there's going to be a step-up in 1940. That's the whole point of this discussion, as I see it: that if at the same time we propose a great increase in benefits we propose to change and reduce the present scale of taxes and the step-ups, why, then the whole question arises: "Well, what is this?" And our reason for doing it, we say, is because of business conditions and the business cycle. Well then, the public will say, "What is this, is this insurance or is this..."

Brown: "... magic?"

Altmeyer: "... magic? Or has it something to do with the business cycle? What have we got here? We thought we were paying in something in return for which we get future benefits related to what we pay in; but now it seems as though what we pay in is determined not by what we're going to get in the future by way of benefits, but by business conditions generally."

Now, there is no contributory insurance system, Mr. Eccles, abroad that has ever contemplated operating on a basis where the tax rates - and they don't call them tax rates; they're contributions - should be fixed in accordance with business conditions.

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Eccles: "ho's arguing that?

Altmeyer: "ell, I thought you were arguing that now.

Eccles: I'm not arguing that you raise your tax up and down. I'm arguing a postponement of the increase in the rate until you get some benefits out.

Altmeyer: You're arguing for the postponement because of business conditions.

Eccles: I'm arguing as a matter of fiscal and monetary policy. If you had a very high full employment now and a runaway situation, this would act as somewhat of a restraint, and there couldn't be the objection necessarily to putting it in that there is at the present time.

Brown: Suppose this one should continue, and then with the continued lack of recovery persons retire soon after 65 and benefits are considerably expanded, because that would in turn politically encourage more liberal benefits; suppose that these tax rates had to be shoved up suddenly to a full two and two, total of four.

Eccles: If you're paying out the full amount, all right; I wouldn't object to it.

Brown: Might be more deflationary.

Eccles: Not if you're accumulating reserves - I'd object.

I want to say this. Hanson invited Taft - he happened to be on the Banking and Currency Committee - he knew him, and he was down to lunch about a month ago, and I sat in. And we got to the question of this thing he raised, this - he got talking about his campaign in Ohio, and he said that the thing that he was sure elected him was Social Security. He said he used this argument. He went on to show how much money had been taken out of the State of Ohio from consumers on these payroll taxes and the unemployment insurance, and had left the State of Ohio and come into Washington, and then how little had been put back into Ohio, at least from that source. True, he said,

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it came in on W.P.A. and other things.

Bell: You should have added P.W.A. and W.P.A. That's Guffey's argument.

H.M.Jr: That's the most specious argument I ever heard. It's intellectually dishonest.

Eccles: It may be dishonest, but that's what happens; it goes over with the public.

H.M.Jr: Let me get Mr. what's-his-name, Director of N.E.C., to tell us the total of money that we get into Ohio; he has it by states. What's his name?

Bell: Lowell Mellett.

H.M.Jr: I'd like to campaign on that, and take just the way Roosevelt did in New York State; with each county we did it. I'd like to take the State of Ohio and show the net amount of this money that this government poured in there over and above that amount.

Eccles: Bulkley had all that.

Haas: He didn't do it effectively.

H.M.Jr: He must have been dumb. I'd like to go to mat on that. I mean you can't take one piece of a thing; you've got to take the whole Federal Treasury, and what is the net amount that we pour into Ohio. I don't know the figures, but have you seen these figures that N.E.C. has?

Eccles: Of course, there's been more money put back in every state than paid out; otherwise you wouldn't have this deficit.

H.M.Jr: I think so with the exception of New York. I don't think ...

Altmeyer: I'm glad to hear what Mr. Eccles says about Ohio, because Bulkley thinks I licked him because I didn't restore grants for old-age assistance. So that relieves my conscience.

Haas: In all the discussions the fiscal and monetary effects have been determined on the basis of government

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spending. I'd like to raise the question of what effect the change in the Social Security Act might have on the question of private spending, which is after all the important and the large one. And here's the serious question I think should be considered: if at a time when the benefits are substantially increased you also decrease the taxes, what effect is that going to have psychologically and in turn affect the private spending? Might not the people who now have apprehension with regard to fiscal affairs of the Government have considerably more, and so you have a deterrent there to private spending? It looks as if you're going toward a Townsendite proposition.

Eccles: What we ought to do, George, is balance the budget to get public confidence to restore recovery.

Haas: If you want to use that argument, I'll say to you we ought to issue currency.

Eccles: The point is we're not talking about a decrease in the taxes. I'm not arguing for a decrease in the tax. You've got a two percent tax on now. It will be three percent, and you say everybody knows it. The average worker doesn't know anything about it. It's true that a lot of - some of the business men know, but so far as the great - the bulk of the people, they don't know anything about the fact that there is going to be an increase in tax next year.

H.M.Jr: Well, the labor unions know it.

Eccles: The average person - if you ask the average person now what the tax is, they couldn't tell you.

Haas: Well, the average are not so very well informed, but they're not so important. It's the business man's decision to spend the money.

Brown: The trade union groups have done a lot of education among the memberships on the whole business.

Altmeier: I think the main thing about this contributory system - and I don't like to seem so obdurate and doctrinaire -

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about the thing - but I think the wonderful thing about this contributory insurance thing is that in spite of the fact we haven't paid any benefits we've gotten so much support. Now, in fact, as you know, in 1936 we thought we were going to be licked by this payroll campaign; as a matter of fact, we won the election because the Republicans were stupid enough to attack the old-age insurance system. It was popular enough that the labor people reacted violently against that sort of an attack on the thing. But now that we've got what I think is wonderful acceptance of it, in spite of the Townsend movement and that sort of thing, I hate to see action taken at this time that would jeopardize the gains that we have made in public acceptance.

H.M.Jr: May I interrupt a minute? Just let me ask this. As I understand it, the figures using the one percent increase - if it goes into effect it means another 250 million dollars?

Altmeyer: That's right.

Eccles: On which payroll? It depends on what payroll. Is that the '38 payroll or '37 payroll basis?

Bell: Well, you're using 300 million. Doesn't make much difference. Use the 300 million.

H.M.Jr: I want to use the extreme. Let's use 300 million dollars. I want to use the highest we take out. And the minimum that you say you pay back is a hundred. So the worst this could be would be 200 million. That right? I mean taking the minimum that you put back and the maximum you take out, we're talking about 200 million dollars. Do you check on that?

Eccles: You mean by reason of the increase, not by reason of what is being collected now.

H.M.Jr: That's right. Now, what I say is this: we're discussing whether or not we should withdraw, in addition to what we are already doing, another 200 million dollars. Now, on the other hand, the way I'm listening, we've got this whole theory which is

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underlying this Social Security, this question of building up these reserves and everything else, and I think that that's so important that the President should make up his mind whether he wants to scrap that whole idea not on account of 200 million dollars

Eccles: I wouldn't scrap it. I don't

H.M.Jr: No, but I think that that's what we're talking about, because in my lifetime here I've seen the bonus drive and the rest of the thing, and what I'm fearful of is that - I mean I'd much rather have the President say, "Well, as far as I'm concerned, let's have a three-year reserve and that's enough, and from now on we go on a pay-as-you-go basis," and not get down to a question whether 200 million should decide what I think is a far greater question: what is the future of Social Security. Now, you can go along with me on that, can't you, Currie?

Currie: Yes. I'd say this is a step toward flattening out the increase in your reserve, get it gradually working to a pay-as-you-go basis, and I don't think, Mr. Secretary, that does endanger the contributory principle.

H.M.Jr: Well, what I'm trying to get at is, rather than let 200 million dollars influence me, I'd much rather decide the more important thing which we have discussed here: that three years' reserve is enough, that we shouldn't try to build up more than that, but we should collect each year enough to maintain that three-year reserve.

Eccles: That isn't your proposal, though.

Altmeyer: Yes, it is.

Eccles: You mean you stopped

Altmeyer: No.

H.M.Jr: May I have one second more? And I think that we're letting 1940 and 200 million dollars influence us too much, and I'd much rather put the discussion on the basis, "Well, as this thing was founded in '35 - we think this is unwise and the thing should be changed and we should look forward toward a three-year reserve

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that's enough, and we don't want to build up more than three years' reserve, and the taxes should be planned and then in '42 let's take another look at the thing." I'd much rather approach it from that angle than - because if you ask me, do I want to take another 200 million dollars away from consumption, and just stick to that, the answer is no, that I don't want to take another nickel out of consumption, and I want to put it back, we've still got too many skips in our engine. But in doing that for one year, I don't want to do something which may rock his system so that it may rock it off its base.

Currie: I think that's an awful important point, Mr. Secretary, which we haven't stressed enough here - the implications of this.

H.M.Jr: Do you see?

Currie: Yes.

H.M.Jr: I've been going to school with these people for over a month now. Now, I'd much rather be, as far as - as I say, be aboveboard and not inch up on this thing and not get at this thing with a smoke screen of 200 million dollars.

Currie: Suppose we put aside this matter of 200 million in '40 and put it on the basis of, do we want to regard a contingent reserve of one billion seven as sufficient? If so - and there are arguments against reducing the tax in 1940, I can see that, from the two percent rate; but if you hold it there and increase your benefits beginning in '40 through '41, '42, '43, you will have gotten to a pay-as-you-go reserve of two billion dollars.

Plough: No, boy, you're a billion dollars too high, on a pay-as-you-go basis.

H.M.Jr: Gentlemen, Mr. Bell would like to say something.

Bell: My mind's been running along the same channels as the Secretary's, but I'd like to ask Mr. Altmeyer this. Of course, if you increase this tax rate,

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allow the tax rate increase to go into effect on January 1, you would get approximately 300 million additional in 1941, talking on a calendar year basis. How much will your hundred million dollars that you anticipate putting out in '40 increase in 1941?

Altmeyer: It steps up rapidly. Of course - now, the low estimate is 286 million dollars.

Bell: You see, when you get to '41 you're stepping it up to the amount of increase in your tax, and as you go along your reserve that you are now building up is going to gradually decrease, isn't that right?

Eccles: When you get on a pay-as-you-go basis.

Currie: Not until you get up to out-payments of around 900 million.

Bell: No, it equals it in '41. What I mean is that you're not making the present situation worse after 1941. Are you?

Eccles: But the present situation is too bad now. You've got to make it better. What I'm arguing now is that at the end of this year you've got a reserve of a billion 700 million. Now, you certainly ought to in '40 get closer to - the outgo ought to get closer to the income. What I'd like to see in 1940 is the benefits get up to four or five hundred million dollars and the tax not increased. In other words, I don't - in 1940, I don't think we ought to be accumulating a lot of money in the reserve. So I think it's more than the 200 million difference that you point out, which is, of course, as compared with the present, which I think has been bad - both the present - both this year and last year, because you've been

Bell: All you want to do is go to a pay-as-you-go.

Eccles: Well, I think so - as close as you can in 1940; don't build up reserves after 1940, but get a pay-as-you-go basis by raising the tax; then, looking to the future, by raising it as the out-payment - in accordance with your schedule of out-payments, but having the Government start

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its contribution as a participant in it, instead of ten years, which you now figure, at some time - that you start the Government's contribution at an earlier date.

Brown: Well, our fear is that in trimming it down to such a - you might say, a neat balance for fiscal arguments

Eccles: No, I'm thinking of Social Security arguments.

Brown: ... you kill the tree.

Eccles: Failing to do it I think would kill it.

H.M.Jr: May I ask a question? Supposing you change the existing law so the tax would not go from two to three; now, as I understand it, if we do this in 1939, and the end of three years is '42 - we take another look at it in '42, is that right?

Brown: That's right.

H.M.Jr: And the thing is left - I mean is changed so that the one percent does not go into effect, but we do start paying now.

Eccles: In '40.

H.M.Jr: In '40. Where would the reserve be in the year - at the end of '42 where would the reserve be? How much reserve would be left?

Blough: It depends on how fast those out-payments go up.

H.M.Jr: Give us an upper and lower.

Blough: On the basis of earlier figures which assumed out-payments beginning at around 500 million dollars, which you say now is too large, it would have been one billion four at the end of 1942.

H.M.Jr: Yes, but taking it out - starting at a hundred million out, I mean.

Blough: Oh.

H.M.Jr: What would it be?

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Blough: Well, what would it be the second year if it's a hundred million the first?

Altmeyer: 287.

Blough: And what would it be the third year?

Currie: One billion seven at the end of this year, two billion two at the end of '40. The second year payment is 287, you said.

Blough: 1941 is 287. What's 1942?

Altmeyer: 441.

Currie: At the end of '41 it would be two and a half billion.

Eccles: You actually build your reserve up, based on your outgo.

H.M.Jr: Excuse me. The easiest way would be to take the two and a half and our original figures of one billion four, which is three nine, and divide it by two, and you get roughly two billion dollars. I mean if you took your five hundred million the way we had it - I mean the average would be about two, between a minimum and a low maximum; would be about two billion, wouldn't it?

Eccles: Altmeyer has a schedule of the out-payments that you'd make in '40, '41, '42, '43.

Altmeyer: On a great many different assumptions.

Eccles: But on the assumption you gave yesterday of a hundred million now, what would you pay out in '41?

Altmeyer: 287.

Eccles: All right, and what in '42?

Altmeyer: 441.

Eccles: In '43?

Altmeyer: 569.

Eccles: Even if you don't increase the tax, on this assumption you're building a reserve in '43.

Altmeier: Not '43.

Eccles: What do you pay out in '43?

Altmeier: 569.

Eccles: You just about balance it; at that time you could increase your tax. But why raise the tax now when you're going to build up the reserve now for three years?

Brown: You'd have to begin to build up taxes much more steeply, much more suddenly; you've got questions of incidence and acceptance here.

Eccles: When you get down to the psychology of acceptance, you're not talking about economics.

Brown: I disagree with you there, Mr. Eccles, because certainly we have to deal with social insurance in terms of the people that are going to help pay for social insurance. And the industrial group, like Swope and Folsom and Teagle - one of the things they've worried about from the first was that this program of taxes should be gradual.

Eccles: Well, we've discussed this for a good long while. All I'd like to do is give to you to file with the President my views of the thing.

H.M.Jr: O.K., if you'll give me yours; and I've got Mr. Delano's. And I'll give them to him when I go over.

Delano: May I say a word, Mr. Secretary. I don't want to prolong this argument. My conception may be entirely wrong, but as I look at it I believe that we should have a fund which is a cushion; my conception is that in a cycle that goes like this (in up and down curves) that in the lean years you ought to draw on that cushion, you ought not to be raising in contributions more than you are paying out, in fact you ought to be taking less; and then in the fat years you're building up that cushion again.

Now, that's my notion. The thing that made this problem so difficult was that we tried to build up a fund in the years when it was most mischievous in

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its effect on our fiscal situation. I think it was a courageous and splendid thing to do; I'm proud of the Administration for doing it. But I think you can overwork that thing. We had a serious recession in '37 which was in part due, I think, to this situation. And I side with those who have spoken in favor of not pulling quite as much as you are trying to do now. But I'm perfectly willing to leave it to the judgment of those who are responsible.

H.M.Jr: All right, sir.

Anybody else want to say anything?

O.K.

At the Eccles letter that
was received, which was dated
April 13, but similar.

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March 17, 1939.

The President,
The White House.

Dear Mr. President:

In our capacity as members of the Fiscal and Monetary Advisory Board we have carefully considered the three main proposals made by the Social Security Board in connection with amendments to the old age insurance program, viz., commencing benefit payments in 1940, liberalizing benefit provisions, and permitting the scheduled tax increase in 1940 to go into effect. We support the proposals to commence benefit payments in 1940 and to liberalize, to the fullest extent feasible, benefit provisions. We are opposed to the scheduled increase in payroll taxes.

The collection of payroll taxes in excess of benefit payments imposes a serious drag on recovery. We are faced with a long term problem of deficient consumer buying power, -with an excess of savings over outlets for private capital expenditures. To continue a system which aggravates this deficiency intensifies our problem and postpones the day when it will be possible to balance the budget without interfering with business recovery.

The Social Security Board's recommendation envisages the further accumulation of a reserve fund, and the further net withdrawal of purchasing power. Approval of this recommendation would imply acceptance of a principle of financing old age insurance for which there is a rapidly decreasing expert and popular support. The accumulation of reserve funds is appropriate to private but not social insurance. This has long been recognized in other countries.

The contributory principle, in our judgment, would not be endangered by a failure to increase the tax in 1940, as this principle does not rest on any particular schedule of tax rates or tax increases, nor on the absence of a federal contribution. The greatest danger to the contributory system will arise from a failure to achieve a higher national income.

In 1937 the excess of payroll tax collections over benefits was a major contributory factor in the decline in consumption that preceded the downturn in business.

The President

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In 1938, about \$1,000,000,000 had to be spent by the Government merely to offset the deflationary effects arising from the unemployment and old age insurance programs and in 1939 another \$1,000,000,000 will have to be spent for the same purpose. This has the effect of increasing the deficit without securing a corresponding increase in buying power.

In 1940 and thereafter, the increase in payroll tax collections arising from (a) increasing payrolls, (b) an extension of coverage, and (c) a fifty percent higher tax rate, may entail a repetition of the 1937 experience or the necessity of incurring a much larger deficit than would otherwise be necessary, unless the benefits are increased sufficiently to offset tax collections.

Since it is likely that tax accruals on old age account will approach \$900 million in 1940 if tax rates are advanced since it is highly improbable in our judgment that liberalized benefit provisions will result in a sum in the next year exceeding \$100 million and since the reserve fund will amount to \$1,700,000,000 at the beginning of 1940, we feel strongly that it would be dangerous from a fiscal and monetary point of view if the scheduled increase in the payroll tax rate should go into effect on January 1, 1940.

Although we are not at this time making any recommendations relating to unemployment insurance, we think it pertinent, in connection with the proposed increase in the payroll tax rate for old age insurance, to point out that the excess of payroll taxes over benefits on unemployment insurance account will, in our judgment, amount to around half a billion dollars, assuming a national income in 1940 no higher than in 1937.

If the tax rate increase is postponed at this time little difficulty in securing increases in payroll taxes in the future may be anticipated if such tax increases are actually necessary to finance current benefits and if, at the same time, a portion of the costs of such benefits is borne out of general taxation, as is the case in England and other countries.

In view of the foregoing considerations, it would not appear advisable to approve the scheduled increase in the tax rate.

Respectfully,

statement by Frederic A. Delano
Prepared for the Fiscal and Monetary Advisory
Committee
with the assistance of the
Industrial Committee,
National Resources Committee
March 17, 1939.

A Social Security Program can act as a drag on full employment in two ways:

- (a) The taxes out of which it is financed may be levied in such a way as primarily to limit expenditures for consumption goods;
- (b) The program may pay out currently a much lower amount in benefits than is currently deducted in taxes.

The present Social Security Program has definitely acted as a drag on our recovery in both these respects. The character of the taxes, however, is probably less important than the lack of balance between tax withdrawals and benefit payments. This lack of balance exists even if allowance is made for payments on account of Old Age Assistance. To a lesser extent it is also true that taxes for unemployment insurance have not been matched by benefit payments.

Taxes resting on the lower income levels come almost entirely from consumption, whereas taxes on the middle income brackets would come partly from idle savings. There are, however, political difficulties involved in shifting the tax burden, and political advantages in retaining a sense of public responsibility by wide participation in the costs of the Social Security Program.

In my opinion it is essential that payroll taxes should not be stepped up, as now provided by law, on January 1, 1940, unless these receipts can be offset elsewhere. We are running along on a low economic level with a condition of such stagnation that we have no adequate outlet for current savings. Under these conditions a Social Security Program is an untimely compulsory savings program which seriously curtails the volume of consumption expenditures.

I favor provision for a three-way contribution to the Old Age Insurance Program, - from employers, from employees, and from the Federal Government. This would involve no change in the incidence of present taxes, but would change permanently the incidence of taxes that must eventually be levied.

So far as Unemployment Insurance is concerned, a strong effort must be made to raise the standard of administration in all the various States so that payments can be made promptly. The waiting period should be made as short as the requirements of a sound unemployment system will permit. Apparently also in many States the provision for benefit payments are such that the receipts from payroll taxes continue far into a depression period to exceed benefit payments.

Frederic A. Delano

RE SOCIAL SECURITY RECOMMENDATIONS

March 20, 1939.
2:15 p.m.

Present: Mr. Gaston
Mr. Haas
Mr. Blough
Mr. Duffield
Mr. Hanes
Mr. White

H.M.Jr: Well now, the point is we went over to see the President, and he asked me first where I stood on this Social Security plan, and I told him no increase in taxes and permit the benefits to start in '40 instead of '42. And he asked about the others and I gave him all these plans; he's got everyone of them. And when he got all through he said I'm simply an opportunist and he was for what he called the Douglas Brown plan, which was the Social Security plan, of course. He gave me a lecture on taxes, that if we didn't get them now never would get them, if he knew Congress - if we postponed raising taxes. As we used to say in Albany, he went very noble on me.

Gaston: I agree with both of you.

(Laughter)

Haas: Perfect all around.

Gaston: I think we need more and not less taxes now, but that's the wrong way to get them.

(White comes in)

H.M.Jr: You missed a good one, Harry.

(On phone) Hello, Frederic Delano. - Henry Morgenthau. (Conversation with Delano follows:)

March 20, 1939.
2:35 p.m.

HMJr: Hello.

Operator: Frederic Delano.

HMJr: Who?

O: Go ahead.

HMJr: Hello.

Frederic Delano: Hello, Mr. Secretary.

HMJr: Frederic Delano?

D: Yes.

HMJr: Henry Morgenthau.

D: Yes.

HMJr: I went over to see the President this morning.....

D: Yes.

HMJr: And took your plan amongst others.

D: Yes.

HMJr: I also on behalf of the Treasury recommended no increase in taxes and to start the benefits in '40.

D: Good for you.

HMJr: Well now, wait a minute. And he turned me down cold.

D: He did?

HMJr: And he is for the Social Security Board plan.

D: All right.

HMJr: He called me an opportunist.

D: All right. (Laughter)

HMJr: And gave me quite a lecture, and he had -- he had what I call Eccles plan one and two -- he had the National Resources plan -- the Douglas Brown plan -- and what we called a better name the Curry-Cohen plan

- 2 -

D: Yes.

HMJr: What the President called the curry-comb plan.

D: Yeah.

HMJr: But he didn't like any of them, and he upheld Altmeyer's hand.

D: All right.

HMJr: Now, there you are.

D: Well, that's all right.

HMJr: But I've got to go up on the Hill the end of the week and I thought I'd let it simmer a little bit and see what happens. I'm still against increasing the taxes.

D: Well I am too, but still, I was thinking -- I -- after I left your office I began thinking a little bit about a -- a ground half-way between; that is, not to -- not to increase the payments until July 1, 1940, and not to increase the taxes until then.

HMJr: Well -- but he -- he wants to increase the taxes.

D: I see. Well, it's all right.

HMJr: I thought I'd tell you.

D: Well, thank you very much for letting me know.

HMJr: You're welcome.

D: Thank you.

HMJr: Good bye.

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H.M.Jr: You (White) weren't here when I said I gave him these plans, and Herbert Gaston says he agrees with both the President and me.

White: I didn't get that, but ...

H.M.Jr: Yes, the President - what we used to call in Albany - he went noble on me in a big way this morning, gave me quite a lecture on taxes, so forth and so on. But I didn't press it today, because this is - for instance, Douglas Brown, Chairman of this Advisory Committee, had never seen the President in his life - this was all pretty new.

Gaston: Was he with you - Douglas Brown?

H.M.Jr: Yes. He did a lot of talking too.

(On phone) Hello. - Hello. (Conversation with Eccles follows:)

March 20, 1939.
2:37 p.m.

HMJr: Hello.

Operator: Chairman Eccles. Go ahead.

HMJr: Hello.

Marriner
Eccles: Hello.

HMJr: Marriner?

E: Yes, Henry.

HMJr: I marched over to the White House this morning and presented all the plans -- both of yours.....

E: Listen, Bob, I haven't got two plans.

HMJr: Well, you've got two letters anyway.

E: No, I only gave you one letter.

HMJr: Well, I had two.

E: Not from me.

HMJr: Yeah, you left me one the other day.

E: Oh well, that -- that one the other day was a -- was a rather a technical long -- what I did was more or less digest it onto a -- it wasn't quite as heavy. The sub -- the substance.....

HMJr: I thought that I -- I understood, maybe I understood wrong, was that you wanted the other day -- the President to see that.

E: Well, I.....

HMJr: Well.....

E: It doesn't make any difference, I guess, but I meant to substitute the one that I gave you this morning for it, because it was -- I felt it would be much -- it was shorter and much more readable for the President.

HMJr: Well, if I heard, I heard on the side.

E: Well that's -- that's O. K.

HMJr: And -- well, then he had what we call the -- well, we gave him what I call the curry-comb plan.

E: Well, I -- Curry talked to me about that last -- I think Wednesday or Thursday -- and I didn't go over it. I just got the general substance of it, and I told him that although I was in sympathy with a much broader picture that I felt that it was too late -- I didn't want to go over there and -- and open this whole thing up again. So I -- I didn't -- don't.....

HMJr: Well, I didn't -- I gave it to him under their own name.

E: Oh, I see. O. K.

HMJr: Because they asked -- at least Cohen asked to see me and I saw him yesterday. So that, and then I gave him the Treasury plan, which was not to increase the taxes and start the benefits in '40.....

E: Well, hell, that's my plan. We're together.

HMJr: Right.

E: We're -- we're together on it then.

HMJr: Right. And we gave them all -- all of them, and he turned us all down and took the Social Security Board recommendation.

E: Uh-huh. Well, that's -- that's all we can do is to make the.....

HMJr: Well, I -- I've got to go up on the Hill towards the end of the week and I thought I'd let the thing kind of simmer, and see what happens.

E: In other words, he wants the tax to go into effect.

HMJr: That's what he told us today.

E: Boy, I'm sorry he did that, because I don't think you're going to get it through up there anyway.

HMJr: And I was surprised -- there was a fellow there from the Labor Department, representing Miss Perkins, and he said he didn't know what Miss Perkins' position

was. He most likely will get murdered for it, so I -- so I asked the President to call on him and he's applauded the plan for no increased taxes.

E: Yeah.

HMJr: So.....

E: I think the Social Security is going to be alone on that thing, and I -- I think that your position and my position is -- is a compromise between the extreme position that -- of going and starting all over again, and the position of the Social Security. And I think that -- that it -- that our position is a very much more defensible position and one that would be very much easier defended and one likely that they will finally end up with anyway.

HMJr: I think so.

E: So, well.....

HMJr: Well, I -- I went over there, and he called on me first, and I told him where we stood.

E: Um-hm.

HMJr: And then gave him this other stuff, and he read it all.

E: Well, I'm glad to know that you took that position, because you see, I didn't know the other day whether you were going to be for or against -- against that tax.

HMJr: I didn't know either until eleven-thirty.

E: Well, I'm -- personally, I'm -- I'm delighted to know that -- that we came out at the same place on it.

HMJr: Yeah, as a matter of fact, you and Delano and myself agree entirely.

E: Well now, that's fine, but it appears that the President is -- doesn't pay an awful lot of attention to his Fiscal and Monetary Committee, does he?

HMJr: I would say not.

E: Not on this one.

HMJr: No.

E: Well, we've made a record, and had our say, and...

HMJr: Well, I.....

E: As far as I'm concerned, I'm satisfied.

HMJr: Well, I got -- excuse me, I had to sneeze -- I've got to testify on this.

E: Well, you.....

HMJr: Well, I'm.....

E: I don't know whether I'll have to or not...

HMJr: Well.....

E: I -- I....

HMJr: I can't.....

E: You -- you will, that's a certainty.

HMJr: Well, I'm -- I've got to.

E: Well, you've got to take -- what are you going to do?

HMJr: Well, I'm going to write out a statement of -- on the position that we don't think the tax ought to go up.

E: The President wouldn't object to that.

HMJr: I don't know.

E: Well, after all.....

HMJr: I -- I've either got to say that, or say nothing. I can't -- I can't say what I don't believe in.

E: No, no, that's right. That's right.

HMJr: So I'm either going to say that or -- or I won't....

E: Or just not testify.

HMJr: Yeah.

- E: Well, I think if you say that it will be -- it would be a great help, and I think, even if nothing is said, that that's likely the way it will end anyway, but I think if you said it that -- that would be the -- that would be the deciding factor on it.
- HMJr: It would be a novelty anyway, wouldn't it?
- E: Well.....
- HMJr: As a matter of fact,.....
- E: I don't think so, because after all, you -- you've been pretty consistent on this question of consumer taxes.
- HMJr: Well, entirely. That's what I said over there. What the hell is the difference of this and the processing tax.
- E: Well there isn't any. I mean, it -- the whole damn thing is put on the cost of the things that the people all have to buy and it increases -- it decreases their buying power, and -- and there isn't a bit of difference, it seems to me, in the final effect on the economy as a whole, between taking out a billion dollars, or six or seven hundred million dollars a year in that way, and taking it out in the processing tax. Not a bit.
- HMJr: Well, the -- I don't know where the President got it from, but he's -- I'm going to give him a couple days to think it over, because he said it was new to him.
- E: What was new, the -- this.....
- HMJr: This whole question.
- E: New to him?
- HMJr: That's what he said. He said, "I'm entirely green on it."
- E: Well, he just -- of course, he has so damn many things to think about and worry, you can't -- you can't wonder that he forgets a lot of them, but he -- he isn't green on it at all; I mean, he shouldn't be because I -- I know -- oh, I haven't seen him since --

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for three months, I guess, -- well, I haven't seen him since -- since December. I haven't seen him since before Christmas. At that time -- it was after -- it was before his budget message, and I know at that time I -- I talked a little to him about the -- in line with the statement that our Committee made to him. Do you remember?

HMJr: I remember very well.

E: And I -- I discussed this whole Social Security question primarily as being one of the most important matters for consideration in looking to further recovery. I mean, it was -- it was almost the principle thing I discussed.....

HMJr: Well, Marriner, he -- he -- frankly, the questions he asked, he really didn't understand it. I -- I'm just telling.....

E: Yes. Well, I guess he didn't -- of course, the damn -- as a matter of fact, the damn thing is -- is certainly complex, now. It -- it -- you've got to live with it to understand the -- the way that that Fund operates.

HMJr: Well.....

E: I'm not surprised that it.....

HMJr: I'm -- I'm going to prepare a statement now. I had the boys prepare one for me, and.....

E: I've got to go up -- I've got to go up on the Hill in the morning on -- before Pittman's committee.

HMJr: Yeah.

E: I got a call Saturday.

HMJr: Oh, I thought you went.

E: No, the -- the -- I was going to go and then they called up and -- and said they had to put it off because the members of the committee were all on other committees.....

HMJr: I see.

E: And they had asked that it be postponed, and so I thought that they'd forget it. You see, I thought that, well, hell it will be all a thing of the past.

HMJr: Well.....

E: But I found out they called up Saturday and I called Pittman again, and he said, "No, no," he said, "We just postponed that. We didn't expect at all to let you off." So I've got to go up there on it.

HMJr: Well.....

E: By the way, I want to -- I'm going to call you later tomorrow, if I can.

HMJr: O. K.

E: The Open Market Committee -- we called them as a result of the meeting with you last week, and I want to I want to make a report to you.

HMJr: Good.

E: So I'll call you on the phone tomorrow.

HMJr: Do that, please.

E: O. K.

HMJr: Good night.

E: Good bye.

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H.M.Jr: Gee, that was funny. Old Marriner found he was going to tell me what he last told the President. It was the funniest thing I ever saw.

Gaston: He started to tell you he hadn't seen the President in six months.

Haas: Three months. Then he hedged a little.

Gaston: He was about to tell you that

H.M.Jr: (Laughs)

Gaston: He was about to tell you that he had been telling the President about this no longer ago than two or three days ago.

H.M.Jr: Oh, thank God we all have a sense of humor.

Well, besides entertaining you gentlemen I thought you might prepare me a statement.

(On phone) Hello. (Conversation with Currie follows:)

March 20, 1939.
2:47 p.m.

*Laughlin
Curry*
Laughton
Curry:

Mr. Secretary.

HMJr: Good afternoon.

C: Good afternoon.

HMJr: I took over your plan -- what I called the curry-comb plan.....

C: (Laughter)

HMJr: And along with the others we presented it to the President between twelve and one.

C: Yes.

HMJr: And you'll be interested to know the Treasury's position before him was for no increase in the taxes and let the benefits go in in '40.

C: Yes.

HMJr: That's the position that I took.

C: Yes.

HMJr: Well, he read all of our plans and he turned them all down and took the Social Security one.

C: Oh, really.

HMJr: Yeah.

C: (Laughter) Well, we -- we all failed badly then.

HMJr: We all failed, but I hope to have another try at him before I go -- have to testify.

C: Yes.

HMJr: But I wanted you to know that he has -- he has your plan along with the other.....

C: Well, I'm awfully grateful to you, Mr. Secretary, for putting that in. It was kind of insufficient. I didn't really realize it was going to be put up that way.

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HMJr: Well, that's the way you wanted it, wasn't it?

C: Yes. Yes, I mean, I'm awfully.....

HMJr: I mean, it was put up in all sincerity and seriousness.

C: Yes.

HMJr: It was given to him, and -- along with four or five others.

C: Yeah. Gene checked with me this morning on the summary and I thought it was a very clear summary.

HMJr: Well, I asked him to check.

C: Yeah. Yeah.

HMJr: So he -- he had it, and got it along with the others. He wants the tax to go in -- the increase.

C: I see, yeah. Well.....

HMJr: And there we are.

C: Yeah. You don't -- you don't mind if I pass this right along to the Chairman?

HMJr: I just got through talking to him.

C: Oh you did?

HMJr: Yeah.

C: Yeah. Fine. Thank you so much for calling.

HMJr: That is all.

C: All right. Good bye.

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H.M.Jr:

I thought you'd (Blough) better start it, if you will, and I'd like to have it not later than Wednesday: a statement for me to go up on the Hill with, saying why I don't want the tax to increase. You see? And as I feel today, I want to base it on two things. I feel that we can go along until '43 putting in the benefits as we see them because (1) I feel that the increase in the tax is a business deterrent and (2) I am opposed to a reserve larger than from two to three years. See?

Now, there were all kinds of statements made there today which didn't check as to whether the reserve - where the reserve would be by '43 before we'd come in again with the tax.

(On phone) Hello. - (Conversation with Ben Cohen follows:)

March 30, 1939.
2:50 p.m.

HMJr: Hello.

Operator: Ben Cohen.

HMJr: Thank you.

O: Go ahead.

HMJr: Hello.

Ben
Cohen: Hello, Mr. Secretary.

HMJr: This is Henry Morgenthau.

C: Yeah.

HMJr: I wanted you to know that we -- I presented your plan today, along with four or five others, to the President on social security.

C: Yes.

HMJr: Along with my -- with the Treasury recommendation, which was we recommended flatly no increase in the tax and the benefits to start in '40.

C: Yeah.

HMJr: And the President listened to me and he read all the other plans, and turned us all down.

C: All of you?

HMJr: All of us. And took the Social Security Board recommendation.

C: Well, what -- what is that?

HMJr: Theirs is to increase the tax and start the benefits.

C: And start the benefits?

HMJr: Yeah. I just wanted you to know, but he -- he had your recommendation on his desk.

C: All right.

HMJr: I wanted you to know that.

C: Sure. Thank you so much, Mr. Secretary. I'm -- I -- I don't know whether either of us are happy, but.....

HMJr: Well, I'm.....

C: At least.....

HMJr: I'm -- I'm distinctly not, because I've got to testify and I'll have to take the position -- and if I testify I'm going to say what I just told you or I won't testify at all. See what I mean?

C: Yes.

HMJr: I mean, I'm not going to go up on the Hill and testify recommending that the tax should be increased.

C: Well, I can understand that, because increasing the tax and paying the benefit is not really the contributory system.

HMJr: No. Well.....

C: And -- that is, I think, on fiscal grounds some change has to be made, but I don't think that's the happiest.

HMJr: Yeah. Well, I just wanted you to know this -- the document was on his desk along with the others.

C: All right. Well, thank you so much.

HMJr: And he had ample time to read it.

C: And I -- I want you to understand the reason I came over, I just thought it best to try to iron the things out together rather than.....

HMJr: That's all right. It's -- it's hard on me physically, but mentally I want it.

C: All right. If I can be of any help, don't hesitate to call on me.

HMJr: Well, I'd much rather, any time, have you come over and let me know, and let me have -- know what you have on your mind, and -- I'm always available.

C: All right. I'll take advantage of it.

HMJr: Please do. Please do it again.

C: All right.

HMJr: Thank you.

C: Thank you.

HMJr: Good bye.

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H.M.Jr: No, I want - you see, the thought which they had was, let's put this thing into effect, let's say, and then - in '42 would we take up the tax again, or '41?

Blough: '43 - the new

H.M.Jr: No, what calendar year would we be studying it? Would it be March '41? Be three years from now, wouldn't it - '40-41-42.

Blough: Three years from now would be March '42, and we would study it in connection with the next increase, which is scheduled to go into effect in '43.

H.M.Jr: Now, the thing on which some said yes and some said no - that at the end of '42 the benefit payments would be such that they'd begin to draw down the reserve, and that therefore at that time, it would be obvious that we should increase the tax. Now, I don't know whether that's correct or not. If it is, it would be a pretty picture.

Do you follow me?

Blough: Yes.

(On phone) Hello. - I'll take it in the washroom.

Do you see what I mean? Anyway, whatever the facts are - naturally, I don't want to fudge them. But I mean where would we be three years from now, and would it seem logical to increase the taxes?

White: With the new benefits.

H.M.Jr: With the new benefits. The argument of the President is they'll never do it. But anyway, what would the size of the reserve be and what would we be facing three years from now, what would the picture be?

Wait for me please.

(Leaves office)

White: If you knew what those new benefits would call for - isn't that the trouble?

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Blough: That's the hitch.

White: The error in that diminishes as the years go on.

(Discussion continues very informally
until H.M.Jr returns)

H.M.Jr: Mrs. Morgenthau says, "Well, the President's going conservative on you."

I really think, you know - here's the left, these three gentlemen, you see; here's poor old Eccles and me right in the middle; and here's the President way over to the right.

Gaston: There isn't a conservative in the lot of you. I'm the only conservative extant here - me and Danny Bell.

H.M.Jr: Now, where are you? I'd like to make a record of it. Where are you?

Gaston: Just as I told you this morning, I'm stupefied.

White: That's the only way I can explain your amazing position - a sport in your character. Liberal in everything else, but in this matter he's certainly gone hide-bound conservative.

Gaston: It means complete repudiation of everything we said in 1935.

H.M.Jr: Anyway, please let me have by tomorrow morning - this isn't so difficult - I want a statement. Let's take a look, because it's more of ...

(Hanes comes in)

H.M.Jr: Hello. How should I say - I'm having what's-his-name prepare me a statement. I'm telling my wife, and when I got through she said, "You've got the two C's over to the left, you and Eccles in the middle, and the President way over to the right."

Duffield: I think John Hanes is over there too, isn't he?

H.M.Jr: No, John's with me; at least, he was when I went

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into the White House.

Hanes: I said, "When we go out the front door, we're like that."

H.M.Jr: What's that?

Hanes: I said, "When we go out the front door, we're just like that." That's just where I was.

Haas: You know, Hansen said he would go that way, for different reasons. His reasons were these. He said in the first place that the original bill was the President's bill; second place, when there was some question about his bill, a Committee was set up. "Well," Hansen said, "I was on the Committee, but the majority said leave the President's bill as is if an increase in taxes was contemplated; then the labor groups came out for the increase. How could he go anywhere else? But as an economist I want to recommend he don't do it." But he thought the President would go just that way.

H.M.Jr: Fix me up: where would we be three years from now, with no increase in taxes, putting the benefits into effect as we know them; what will the picture look like - reserve, etc., etc.; and in the three years how much money do we collect and how much money goes out?

White: The first part of that question ought to be pretty easy to answer.

H.M.Jr: Well, and then you might take this; then you might say, "All right, in '43 we increase the tax by one percent." See? And then how long would that run us before we begin to eat into the reserve, see? Does that

Blough: Very clear.

H.M.Jr: What?

Blough: That's very clear.

H.M.Jr: We run the way we are now for three years; then in three years let's say we increase the tax by one percent.

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Blough: How long will that last before we need more - without government subsidy in the meantime?

H.M.Jr: That's right.

Blough: Do you wish, before you go on the Hill, any preparation on other questions that the Committee is likely to ask you?

H.M.Jr: Oh hell, if we get on anything else I'll turn to you.

Hanes: Are you going to go up on the Hill on this thing?

H.M.Jr: What I'm doing - I'm going to prepare this. I thought I'd let this thing simmer, see, and I'll hear from Jere Cooper. Then I want this prepared and I want to go over and say, "Mr. President, this is what I'm going to say. If you don't want me to say this, then I won't go up on the Hill. But if I'm going up on the Hill"

Hanes: You're going to recommend no increase in tax.

H.M.Jr: If I go. See?

Hanes: Well, Cooper and I came - I walked over with Cooper and the rest of them, and I think they're under the impression that the President had decided the thing. Is that the impression you've got?

H.M.Jr: No. Well, the President said this - I mean the way he put it was, he said - he said, "I'm pretty green on this thing, but if I had to decide it now"

Hanes: Curbstone opinion.

H.M.Jr: I wouldn't take that.

Hanes: You don't think that's final?

H.M.Jr: No. No, I definitely don't. Definitely.

Hanes: Altmeyer and Cooper and that other fellow from the Labor Department - I never did get his name -

H.M.Jr: Who would that be - from Labor?

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Duffield: Hinrichs.

H.M.Jr: Who?

Duffield: Hinrichs.

H.M.Jr: No, that wasn't Hinrichs. Very thick gray hair - shock of hair.

Hanes: Well, at any rate, all of them were under the impression that the President had taken the so-called Brown plan; that's the one he referred to.

H.M.Jr: Which is the Social Security Board's.

Hanes: Which is leaving the tax go up, to increase a half of one percent, and increasing the benefits, moving them up in 1940.

H.M.Jr: No, I don't take that as final by any means. I mean as far as I'm concerned, I don't, because I'm not going to go up and

Hanes: No. Well, I

H.M.Jr: Well, you're asking me. I just didn't - I thought I'd let the thing rest and I'd talk some more to the President.

When he went into a long discussion on this: the only way to do this thing was to make it obligatory that everybody set aside so much money out of their wage for old age, so forth and so on, and just make it obligatory. And I said - well, the whole discussion about the South and everything else - this thing didn't solve anything; so forth and so on.

No, I feel as far as I'm concerned that I certainly expect to have a rebuttal, because he wasn't - he certainly wasn't well posted on this, was he?

Hanes: No, he said he wasn't. He said, "This is"

H.M.Jr: And you notice they let him get away with statements that just weren't so. Nobody corrected him. The President didn't know about the reserves and how much went in, how much went out, and all the rest. But I thought if Blough would fix me up a very rough

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draft for tomorrow morning, we'll take a look at it and then kind of fix it up. I mean just where would we be? And I want to show that to the President.

Hanes: The only reason I'm telling you that these other fellows got the other impression - you might want to tell them before you go up there.

H.M.Jr: That's a good idea, so there won't be a misunderstanding. A lot of people go over and the President sits back like that, and they take it as final. Where would you and I be today if we took something he said as final last week?

Hanes: Not very far.

H.M.Jr: See? Hell, I only made up my mind at a quarter of twelve. I've got to see my own opinion through for at least one day.

Would you (Duffield) look up that testimony of the fellow from Standard Oil of New York, where he stood on increasing the taxes? Anybody could have bet me one dollar or a hundred dollars that he was in favor of increasing the taxes.

Duffield: When they were first here?

H.M.Jr: Yes.

Duffield: No, this is right.

White: With the group meeting he very definitely was not in favor of increasing the taxes. You remember how surprised we were.

Duffield: You said after that meeting, "He's in the same corner with Hansen."

H.M.Jr: Yes. I guess I'm slipping, John.

White: The right way.

Hanes: You have a whole lot on your mind. I'll forgive you for that slip you made this morning.

H.M.Jr: All right.

March 20, 1939

The Secretary gave all of this material to the President at the meeting at the White House today at 12 o'clock. Also present were Mr. Hanes, Mr. Altmeyer, Prof. Brown, and Secretary Perkins.



BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

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OFFICE OF THE CHAIRMAN

March 20, 1939.

Personal and Confidential

Honorable Henry Morgenthau, Jr.,
Secretary of the Treasury,
Washington, D. C.

Dear Henry:

In accordance with the conversation I had with you on Saturday, I am enclosing herewith a letter to be delivered to the President setting forth my views on the contemplated amendments to the old age insurance program.

Although the letter is shorter than the memorandum I left with you on Saturday, the substance is the same with the exception of the last paragraph.

Yours sincerely,

Marriner

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BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

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OFFICE OF THE CHAIRMAN

March 20, 1939.

The President,
The White House.

Dear Mr. President:

In my capacity as a member of the Fiscal and Monetary Advisory Board I have carefully considered the three main proposals made by the Social Security Board in connection with amendments to the old age insurance program, viz., commencing benefit payments in 1940, liberalizing benefit provisions, and permitting the scheduled tax increase in 1940 to go into effect. I am in favor of commencing benefit payments at the earliest possible moment, and of liberalizing, to the fullest extent feasible, benefit provisions. I am opposed to the scheduled increase in payroll taxes.

For three years the collection of payroll taxes in excess of benefits, with the resulting accumulation of a reserve fund, has imposed a serious drag on recovery and has necessitated increased Government expenditures elsewhere. On both unemployment and old age insurance account the deduction from consumer buying power amounts to one billion dollars a year for the years 1937-39. This deduction will be even greater in 1940 unless increased benefits exceed increased tax collections. Actually, it appears that the tax increase will yield from \$250 million to \$300 million additional, while the contemplated increase in benefits will amount only to between \$100 million and \$200 million.

It appears an opportune time to raise the whole question of the financing of old age insurance. The trend in all other countries, and in expert and popular opinion in this country, has been away from the reserve fund principle. Even if the tax increase is postponed, the reserve fund will continue to accumulate through 1942. If the tax is increased, this will tend to extend still further the period over which the fund will grow.

The President.

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In view of the gravity of our major economic problem of deficient consumer buying power relative to our productive capacity, I urge that no further increase in the payroll tax rate take place next year. The economic repercussions resulting from a continued excess of tax collections over benefits will do more, in my judgment, to jeopardize the contributory system than would postponing the scheduled tax increase.

I am confining my recommendations to the specific proposals placed before the Advisory Board. I cannot refrain from adding, however, that in my judgment the proposals of the Social Security Board do not meet the demand in this country at this time for an adequate national old age security program.

Respectfully,



M. S. Eccles

Received Mark Eccles
18, 1939

January 13, 1939.

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CONTROVERSIAL ISSUES RAISED BY THE REPORT OF THE SOCIAL SECURITY BOARD

I - The Financing of Social Insurance

The collection of payroll taxes in excess of benefit payments imposes a serious drag on recovery. We are faced with a long term problem of deficient consumer buying power, - with an excess of savings over outlets for private capital expenditures. To continue a system which aggravates this deficiency intensifies our problem and postpones the day when it will be possible to balance the budget without interfering with business recovery.

The Report of the Social Security Board approves the imposition of a higher payroll tax rate in 1940 and hence envisages the further accumulation of a reserve fund, and the further net withdrawal of purchasing power.

Endorsement of the Report in its present form, either implicitly or explicitly, would imply acceptance of a principle of financing old age insurance for which there is a rapidly decreasing expert and popular support. The accumulation of reserve funds is appropriate to private but not social insurance. This has long been recognized in other countries.

II - Deflationary Effects of Present System

In 1937 the excess of payroll tax collections over benefits was a major contributory factor in the decline in consumption that preceded the downturn in business.

In 1938, about \$1,000,000,000 had to be spent by the Government merely to offset the deflationary effects arising from the unemployment and old age insurance programs and in 1939 another \$1,000,000,000 will have to be spent for the same purpose. This has the effect of increasing the deficit without securing a corresponding increase in buying power.

In 1940 and thereafter, the increase in payroll tax collections arising from (a) increasing payrolls, (b) an extension of coverage, and (c) a fifty percent higher tax rate, may entail a repetition of the 1937 experience or the necessity of incurring a much larger deficit than would otherwise be necessary, unless the benefits are increased sufficiently to offset tax collections.

III - Recommendations

Since it is likely that tax accruals on old age account will exceed \$900 million in 1940 if tax rates are advanced as recommended in the report; since it is highly improbable in my judgment that liberalised

benefit provisions will result in a sum in the next year or two approaching this figure or even the figure of about \$600 million in taxes that would be collected if tax rates were not advanced; and since the reserve fund will amount to \$1,700,000,000 at the beginning of 1940, I feel strongly that it would be dangerous from a fiscal and monetary point of view if the scheduled increase in the payroll tax rate should go into effect on January 1, 1940.

Although I am not at this time making any recommendations relating to unemployment insurance, I think it pertinent, in connection with the proposed increase in the payroll tax rate for old age insurance, to point out that the excess of payroll taxes over benefits on unemployment insurance account will, in my judgment, amount to around half a billion dollars, assuming a national income in 1940 no higher than in 1937.

In view of the foregoing considerations, it would appear advisable to defer approval of the scheduled increase in the tax rate until it is known what the benefit payments adopted by Congress will amount to for the calendar year 1940.

If the tax rate increase is postponed at this time little difficulty in securing increases in payroll taxes in the future may be anticipated if such tax increases are actually necessary to finance current benefits and if, at the same time, a portion of the costs of such benefits is borne out of general taxation, as is the case in England and other countries.

NATIONAL RESOURCES COMMITTEE
PLAN

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Payroll tax should not increase in 1940 unless the increased receipts are offset by expenditures elsewhere.

The Government should eventually contribute a portion of the cost of an old age benefit plan.

Statement by Frederic A. Delano
Prepared for the Fiscal and Monetary Advisory
Committee
with the assistance of the
Industrial Committee,
National Resources Committee
March 17, 1939.

A Social Security Program can act as a drag on full employment in two ways:

- (a) The taxes out of which it is financed may be levied in such a way as primarily to limit expenditures for consumption goods;
- (b) The program may pay out currently a much lower amount in benefits than is currently deducted in taxes.

The present Social Security Program has definitely acted as a drag on our recovery in both these respects. The character of the taxes, however, is probably less important than the lack of balance between tax withdrawals and benefit payments. This lack of balance exists even if allowance is made for payments on account of Old Age Assistance. To a lesser extent it is also true that taxes for unemployment insurance have not been matched by benefit payments.

Taxes resting on the lower income levels come almost entirely from consumption, whereas taxes on the middle income brackets would come partly from idle savings. There are, however, political difficulties involved in shifting the tax burden, and political advantages in retaining a sense of public responsibility by wide participation in the costs of the Social Security Program.

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In my opinion it is essential that payroll taxes should not be stepped up, as now provided by law, on January 1, 1940, unless these receipts can be offset elsewhere. We are running along on a low economic level with a condition of such stagnation that we have no adequate outlet for current savings. Under these conditions a Social Security Program is an untimely compulsory savings program which seriously curtails the volume of consumption expenditures.

I favor provision for a three-way contribution to the Old Age Insurance Program, - from employers, from employees, and from the Federal Government. This would involve no change in the incidence of present taxes, but would change permanently the incidence of taxes that must eventually be levied.

So far as Unemployment Insurance is concerned, a strong effort must be made to raise the standard of administration in all the various States so that payments can be made promptly. The waiting period should be made as short as the requirements of a sound unemployment system will permit. Apparently also in many States the provision for benefit payments are such that the receipts from payroll taxes continue far into a depression period to exceed benefit payments.


Frederic A. Delano

MEMORANDUM ON THE PRESENT SOCIAL SECURITY PROGRAM AND THE PROBLEM

WHETHER IT CONSTITUTES A DRAG ON RECOVERY

By

Alvin H. Hansen

1. A Social Security Program can act as a drag on full employment in two ways: (a) The program may be financed by a type of tax which weighs heavily on consumption, or it may be financed by a type of tax which weighs heavily on incomes a relatively large proportion of which would not be spent on consumption goods. In the former case the program would act to reduce the volume of consumption expenditures, in contrast with the situation which would obtain under the latter type of tax. Here it is not a question of whether or not the sums collected in taxes are paid out in benefits, but purely a question of the incidence of the taxes imposed upon consumption. (b) A Social Security Program may constitute a drag on full employment by paying out a much lower amount in benefits than is deducted in taxes. Here it is not a question of how taxes themselves affect expenditures, but rather the failure to offset any effect of taxes on consumption by distributing these sums to the community.

On both counts the Social Security Program has, I think, definitely acted as a drag on our recovery. In my view the really serious matter, however, is not the character of the taxes themselves, but rather the fact that in the case of the Old Age Program the taxes have been matched scarcely at all with benefit payments. This is true to a lesser extent in the case of the Unemployment Insurance, but still true to a degree which is extremely unfortunate.

2. There are those who would dispense altogether with the payroll taxes and who would raise the necessary funds exclusively from the general revenues, especially by imposing higher surtaxes on personal incomes. From the standpoint of pure tax principles and the incidence of the tax structure upon consumption and investment expenditures, a strong case can certainly be made for an extension of the personal income tax system and a repeal or reduction of a variety of other taxes which peculiarly weigh upon consumption. There is, however, the practical difficulty politically of getting a sufficiently low exemption and sufficiently high rates in the middle-income brackets to make the income tax carry the necessary load. Payroll taxes are a practical solution in a measure for the political difficulty of securing a low exemption in the income tax. Moreover, there is the historical precedent of practically all countries having extensive Social Insurance Programs of placing a major part of the burden directly upon the beneficiaries or upon employers.

This procedure has certain definite advantages from the standpoint of securing a sense of public responsibility with respect to the cost of such programs. In my own view I think from this standpoint it is particularly important that wage earners should contribute to the program as provided by present legislation. The present Social Security tax structure does, however, I think, go too far in this direction. There is justification for a direct government contribution from general revenue to the Old Age Security Program. In this manner a balance can be achieved between the aim of securing a sense of public responsibility by wide participation in the costs of the program and at the same time through the government contribution insuring that the tax collections shall not reduce consumption expenditures unduly. So far as the tax structure is concerned, I think the program can be changed to help the attainment of a higher national income and full employment by providing for a three-way contribution to the Old Age Insurance Program, one-third from employers, one-third from employees, and one-third from the federal government.

3. More important at the moment is the current and prospective failure to distribute benefits approximately equal to the tax receipts. So far as the Unemployment Insurance is concerned, a strong effort must be made to raise the standard of administration in all the various states so that payments can be made promptly. This is certainly a most serious matter which calls for determined effort. In the next place, the waiting period should, at any rate from the cyclical compensatory standpoint, be made as short as the requirements of a sound unemployment system will permit. In most cases the waiting period is now too long. Apparently also in many states the provision for benefit payments is too conservative, so that the receipts from payroll taxes continue far into a depression period to exceed benefit payments. From the purely cyclical compensatory standpoint, it would be desirable to make the waiting period very short and to make large benefit payments, (even though this requires a shorter period of benefit payments) in order that out-payments shall quickly equal and then exceed the tax collections once the depression is on. It is admitted, however, that other considerations besides the purely cyclical compensatory one must be taken account of. Each one of the current State acts certainly ought to be thoroughly scrutinized from the standpoint of the speed of the adjustments of income and benefit payments to changes in employment. It is apparent that currently the lag is altogether too great.

With respect to the Old Age Insurance, the immediate question relates to whether or not the payroll taxes shall be stepped up, as now provided by law, on January 1, 1940. On this date the Old Age Reserve Account will have accumulated approximately \$1,700,000,000. It was the view of a minority of the Social Security Advisory Council, including myself, that this reserve was adequate for the time being and that the step-up in payroll taxes ought not to be made until it was clear that current benefit

payments called for such a step-up in taxes in order to prevent an encroachment on the contingency reserve. The main argument, as I see it, against this recommendation is the feeling which several have expressed that, if the payroll taxes are not stepped up, as now provided, the whole contributory system will go by the board. I do not know how to appraise this peculiarly political factor, but I am personally not able to see that the mere postponement of the step-up, if in itself a rational procedure, inevitably endangers the continuation of the contributory system.

Had we been living in a period of vigorous private investment activity with full employment in periods of prosperity, we could perhaps wisely have afforded the extremely conservative Social Security financing program which the present law provides for. There is of course a merit in starting such a program on a strong financial basis with an accumulation of reserves. It is unfortunate for a Social Security Program to head at once straight into bankruptcy. These considerations have doubtless weighed heavily with those persons who lean on the side of conservative financing for the Social Security Program. We are, however, faced with the situation that we are not enjoying currently vigorous private investment activity. Running along, as we are, on a low level with a condition of chronic stagnation, we cannot afford, it seems to me, the luxury of a Social Security Program which turns out in effect to be essentially a compulsory savings program, and which thereby seriously curtails the volume of consumption expenditures.

It therefore seems wise to me, so far as the Unemployment Insurance Program is concerned, to secure, if possible, an amendment of the State acts so as to make them more quickly responsive to changes in employment, thereby insuring the rapid paying out of benefits as soon as a downswing develops, and making the benefit payments sufficiently generous so that the Unemployment Insurance system shall not build up over the cycle positive reserves. So far as the Old Age system is concerned, it should be amended in two ways, to liberalize the benefits, as recommended by both the Social Security Board and the Social Security Advisory Council, and to postpone the step-up in payroll taxes until current benefits exceed the tax collections.

GURRY-COHEN PLAN

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The present contributory old age benefit plan of the Social Security Board would be supplemented beginning in 1940 by a system of non-contributory pensions for all persons over 65. Persons becoming 65 after January 1, 1940 could elect to take either the pensions or the benefits.

A basic minimum pension of \$15 per month for single persons, \$25 per month for couples is suggested. An additional \$5 for single persons and \$7.50 for couples could be added by the Federal Government if the states matched these additions, making maximum pensions of \$25 and \$40 per month.

The cost to the Federal Government of pensions in 1940 for 6 million old persons is estimated at approximately 1 billion dollars, which is approximately the same as appropriations for the old age reserve and old age systems under the present plan.

REVISION OF THE OLD AGE SECURITY PROGRAM

Now that the Social Security Act is up for revision an effort should be made to devise a plan that would:

- (1) meet the widespread demand for national old age pensions.
- (2) permit differentials in monthly payments in different parts of the country.
- (3) preserve the contributory principle.
- (4) entail no additional appropriations nor taxes over those contemplated for 1940.
- (5) add to consumer buying power in 1940 and thereafter.

Such a plan would meet the major criticisms of the present system, would prevent the threatened deficiency in consumer buying power in 1940, and yet would cost no more than the present plan. The five points listed above could be met in the following ways:

1. A Minimum National Pension

Provide a basic minimum for all persons over sixty-five provided their own income from work or property, added to their pension, does not exceed a certain amount. The basic minimum might be \$15 per month for single persons and \$25 for couples. In some states, old-age pensions for the indigent do not average more than \$4 per person. Under the proposed federal pension plan, in 1940 some six million old persons would be benefitted by federal aid to the extent of approximately one billion dollars as contrasted with some 1,800,000 persons who would benefit by federal aid to the extent of \$250 million if the present old-age assistance system is continued.

2. Regional Differentials.

Over and above the basic national minimum, provide for matching State contributions dollar for dollar up to \$5 additional for single persons and \$7.50 for couples. In the wealthier States this would permit pensions of at least \$25 and \$40 per month, the maximum Federal contribution being \$20 and \$32.50.

3. The Contributory Principle.

Persons becoming sixty-five after January 1, 1940 who have paid payroll taxes for requisite periods and in requisite amounts, will remain eligible for old age benefits under the present contributory system, unless being also eligible for pensions, they elect to take the latter. Permit self-employed (including farmers) to qualify for old age benefits under the contributory system by paying old age insurance premiums on a voluntary basis.

4. No Additional Appropriations or Taxes over Those Scheduled for 1940.

This can be accomplished by making all old age payments out of the Old Age Reserve Fund and making all appropriations for old age security to that Fund. There will be available in 1940 over \$900 million in payroll taxes, plus a \$250 million appropriation for old age assistance. It is estimated that the combined cost to the federal government of the pensions and the old age benefits during 1940 will not exceed \$1,150,000,000, and that in addition the operation of the proposed plan should result in some savings on work relief.

5. Add to Consumer Buying Power.

The combined old age insurance and assistance programs, under amendments proposed by the Social Security Board, will result in a probable net deduction from buying power of \$500 million in 1940. The present plan will add some \$200 million net, or a difference of some \$700 million.

The plan, of which the above is a skeleton outline, appears to be both administratively and politically feasible.

L. Curry
B. Cohen

BROWN'S SUGGESTIONS

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Payroll tax increase should be allowed to go into effect in 1940 in accordance with existing law. Benefits should be advanced to 1940.

Experience under this arrangement should be restudied in 1941-42.

MEMORANDUM ON THE TAX SCHEDULE UNDER THE
OLD AGE INSURANCE PROGRAM

1. The old age insurance system is a long range program of government affecting the security of many millions of employees. The financing of the system should not be subjected to sudden change for the purpose of stimulating or retarding business activity. Rather, changes in the financing of the system should be based primarily on thorough study of the problems arising within the government's program for social security and the taxes necessary, over time, to finance that program.

2. Contributory social insurance is still a new and little understood mechanism in this country. To raise benefits and, at the same time, lower the schedule of taxes in the third year of operation of the scheme will seriously endanger public understanding of the nature of contributory insurance as distinguished from free pension (Townsend) plans.

3. A reduction in the schedule of tax rates at this time would certainly require a more rapid increase in tax rates, payroll or other, in the future. It may well be that such more

rapid increases will then be opposed as deflationary. Indefinite postponement of tax increases may destroy the Government's opportunity to develop a constructive program of contributory social insurances, and necessitate a return to needs-test programs alone.

4. Labor and progressive employer groups have come to accept the present schedule of taxes, at least up to 1942. Labor would regard a downward revision with suspicion since it might well involve a future limitation on benefits. Employers who have had experience in their own companies with contributory insurances understand the great advantage, both economic and social, of preserving the contributory principle if adequate protection is afforded to the public. The tax is a "contribution" and will become all the more so as benefits begin.

5. The end sought by reducing the tax schedule is at best a chance that business will thereby be stimulated. Outstanding economists question the advisability of such a move quite apart from the dangers incurred in the Social Security program. It is a gamble as to the effect of a relatively small change in the total budget with serious risk to one of the most constructive programs developed by the present Administration.

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6. The Social Security taxes cannot be disassociated in their fiscal aspects from the over-all fiscal position of the Government. To set them apart in vacuo is unrealistic. Expenditures for relief, assistance and other welfare programs certainly counterbalance in large measure the deflationary effects of the Social Security taxes during the period before such taxes are offset in large measure by benefit payments.

7. The previous position of the Treasury in regard to the financing of the old age insurance program has been a conservative one. To approve a reduction of taxes at this time while many factors are uncertain and unknown and while increased benefits are under consideration might well be regarded as an extreme change in position. Business groups which realize the large future costs of the old age insurance program might regard the change as an added factor of uncertainty as to future taxes on business.

8. A change in $1/2\%$ on payrolls in industry must be compared to other changes in payroll costs to which industry is accustomed. Wage increases frequently run

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to 5% of payroll. The increased charge of 3 to 4% for Social Security taxes in 1937-38 was sudden and not offset by the payment of any considerable volume of benefits in most states. An increase of but 1/2% in 1940 would be offset in part by benefits in that year and by a larger volume of benefits in 1941 and 1942.

In summary, the undersigned is convinced after sustained study of the problem that the soundest position that the Treasury can take in regard to the tax schedule under the old age insurance program is that taken by the Advisory Council on Social Security:-

1. No departure from the existing schedule at this time.
2. Restudy in the light of experience in 1941-42.

W. Douglas Brown
Mar 18, 1939.

ECCLES PLAN (#1)

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The tax increase scheduled for 1940 should not be allowed to go into effect. Subsequent increases in payroll taxes should be asked only when necessary to finance current benefit payments after the Government has contributed a portion of those benefits out of general taxation.

Benefits should be started in 1940.

January 13, 1939.

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Received March 18, 1939 Eccles

CONTROVERSIAL ISSUES RAISED BY THE REPORT OF THE SOCIAL SECURITY BOARD

I - The Financing of Social Insurance

The collection of payroll taxes in excess of benefit payments imposes a serious drag on recovery. We are faced with a long term problem of deficient consumer buying power, - with an excess of savings over outlets for private capital expenditures. To continue a system which aggravates this deficiency intensifies our problem and postpones the day when it will be possible to balance the budget without interfering with business recovery.

The Report of the Social Security Board approves the imposition of a higher payroll tax rate in 1940 and hence envisages the further accumulation of a reserve fund, and the further net withdrawal of purchasing power.

Endorsement of the Report in its present form, either implicitly or explicitly, would imply acceptance of a principle of financing old age insurance for which there is a rapidly decreasing expert and popular support. The accumulation of reserve funds is appropriate to private but not social insurance. This has long been recognized in other countries.

II - Deflationary Effects of Present System

In 1937 the excess of payroll tax collections over benefits was a major contributory factor in the decline in consumption that preceded the downturn in business.

In 1938, about \$1,000,000,000 had to be spent by the Government merely to offset the deflationary effects arising from the unemployment and old age insurance programs and in 1939 another \$1,000,000,000 will have to be spent for the same purpose. This has the effect of increasing the deficit without securing a corresponding increase in buying power.

In 1940 and thereafter, the increase in payroll tax collections arising from (a) increasing payrolls, (b) an extension of coverage, and (c) a fifty percent higher tax rate, may entail a repetition of the 1937 experience or the necessity of incurring a much larger deficit than would otherwise be necessary, unless the benefits are increased sufficiently to offset tax collections.

III - Recommendations

Since it is likely that tax accruals on old age account will exceed \$900 million in 1940 if tax rates are advanced as recommended in the report; since it is highly improbable in my judgment that liberalized

benefit provisions will result in a sum in the next year or two approaching this figure or even the figure of about \$600 million in taxes that would be collected if tax rates were not advanced; and since the reserve fund will amount to \$1,700,000,000 at the beginning of 1940, I feel strongly that it would be dangerous from a fiscal and monetary point of view if the scheduled increase in the payroll tax rate should go into effect on January 1, 1940.

Although I am not at this time making any recommendations relating to unemployment insurance, I think it pertinent, in connection with the proposed increase in the payroll tax rate for old age insurance, to point out that the excess of payroll taxes over benefits on unemployment insurance account will, in my judgment, amount to around half a billion dollars, assuming a national income in 1940 no higher than in 1937.

In view of the foregoing considerations, it would appear advisable to defer approval of the scheduled increase in the tax rate until it is known what the benefit payments adopted by Congress will amount to for the calendar year 1940.

If the tax rate increase is postponed at this time little difficulty in securing increases in payroll taxes in the future may be anticipated if such tax increases are actually necessary to finance current benefits and if, at the same time, a portion of the costs of such benefits is borne out of general taxation, as is the case in England and other countries.

ECCLES PLAN (#2)

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The payroll tax should not be allowed to increase in 1940. The old age reserve, which has been accumulating for three years, would continue to accumulate for some years even though the tax is not increased and the proposed benefits are approved.

The benefits as suggested by the Social Security Board should be allowed to go into effect.

Even in the liberalized form the program does not meet the public demand for an adequate national old age security program at this time.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON

OFFICE OF THE CHAIRMAN

March 20, 1939.

The President,
The White House.

Dear Mr. President:

In my capacity as a member of the Fiscal and Monetary Advisory Board I have carefully considered the three main proposals made by the Social Security Board in connection with amendments to the old age insurance program, viz., commencing benefit payments in 1940, liberalizing benefit provisions, and permitting the scheduled tax increase in 1940 to go into effect. I am in favor of commencing benefit payments at the earliest possible moment, and of liberalizing, to the fullest extent feasible, benefit provisions. I am opposed to the scheduled increase in payroll taxes.

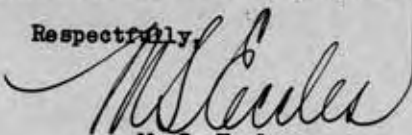
For three years the collection of payroll taxes in excess of benefits, with the resulting accumulation of a reserve fund, has imposed a serious drag on recovery and has necessitated increased Government expenditures elsewhere. On both unemployment and old age insurance account the deduction from consumer buying power amounts to one billion dollars a year for the years 1937-39. This deduction will be even greater in 1940 unless increased benefits exceed increased tax collections. Actually, it appears that the tax increase will yield from \$250 million to \$300 million additional, while the contemplated increase in benefits will amount only to between \$100 million and \$200 million.

It appears an opportune time to raise the whole question of the financing of old age insurance. The trend in all other countries, and in expert and popular opinion in this country, has been away from the reserve fund principle. Even if the tax increase is postponed, the reserve fund will continue to accumulate through 1942. If the tax is increased, this will tend to extend still further the period over which the fund will grow.

In view of the gravity of our major economic problem of deficient consumer buying power relative to our productive capacity, I urge that no further increase in the payroll tax rate take place next year. The economic repercussions resulting from a continued excess of tax collections over benefits will do more, in my judgment, to jeopardize the contributory system than would postponing the scheduled tax increase.

I am confining my recommendations to the specific proposals placed before the Advisory Board. I cannot refrain from adding, however, that in my judgment the proposals of the Social Security Board do not meet the demand in this country at this time for an adequate national old age security program.

Respectfully,

A large, stylized handwritten signature in dark ink, appearing to read 'M. S. Eccles', is written over the typed name.

M. S. Eccles

Mr. Guth
Mr. Sargeant
Mr. Chamblin

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STATEMENT SUBMITTED TO THE TREASURY DEPARTMENT
MARCH 20, 1939 ON BEHALF OF THE NATIONAL AS-
SOCIATION OF MANUFACTURERS BY GEORGE GUTH,
MANAGER OF ANNUITY AND INSURANCE DIVISION,
SOCONY-VACUUM and VICE CHAIRMAN OF N.A.M.
COMMITTEE ON ECONOMIC SECURITY

1. This entire memorandum relates only to those aspects of the social security act which are directly related to the tax burdens upon employers.
2. It is assumed that social security in the larger sense is not promoted unless economic recovery is promoted.
3. In the field of social security taxes the best contribution which could be made to recovery would be to keep payroll taxes at their present level and eliminate the automatic 50% increase in the old age annuity tax scheduled to begin in 1940. The following arguments are submitted on behalf of this position -

- (a) The scheduled increase would amount to an increased federal tax burden upon corporate employers of approximately 15% which would be a most appreciable, business-disturbing and employment-reducing burden.
- (b) As further evidence of the advisability of reducing - or at least preventing an increase in - the industrial tax burdens we find a study just completed by Standard Statistics Company, which surveyed total taxes paid by 80 corporations in 1938 shows that the amount of taxes paid was nearly 54% greater than the actual net income of the same companies.
- (c) The President of the United States has declared that from the standpoint of government the federal tax burden upon business can not be reduced below its present level. American industry similarly is of the belief and firm conviction that any increase in the federal tax burden upon business would be a serious factor in preventing or delaying recovery, and that the prospective anticipation of such increase in 1940 will continue to be a serious deterrent during the balance of 1939. Likewise if it were to be announced during

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1939 that this 50% increase in the old age annuity tax were not to take effect in 1940 a substantial incentive for business hopes and plans would be provided.

- (4) It may be objected that the proposed tax increase must go into effect if the benefits contemplated in the law are to be provided, but actuarial studies made by the National Association of Manufacturers indicate that the present rate of joint contribution under Title 8 of the Social Security Act would be sufficient to provide the annuities contemplated in the act at the present time until 1971. They further indicate that if the benefits begin in 1940 instead of 1942 the present contribution rate will be sufficient until approximately 1958.
- (5) The National Association of Manufacturers directly represents employers and cannot specifically speak for employees. Nevertheless as employers its members frequently receive voluntary expressions from employees upon current matters. It may be observed that according to this experience there is a growing belief among employees that the old age annuity tax is, in effect, an income tax, and that they will especially resent a 50% increase when it goes into effect, particularly when they realize, as they do, that it is being used either exclusively or primarily for social security purposes. Both employees and employers are aware of the fact that as the law now stands huge funds for old age annuity are being utilized for government expenditures in no way related to social security.

March 26, 1939

To: Secretary Morgenthau

From: Herbert Gaston *HG*

Re. SOCIAL SECURITY

The Old Age Benefit system embodying the so-called full reserve as enacted in the Social Security Act of 1935, largely at your instatence, is a fiscally sound system. None of the alternative proposals now advanced is fiscally sound. They carry the seeds of hopeless confusion, unbearable tax burdens and probable repudiation.

The present system accepts the principle that the liabilities which the government is assuming to beneficiaries are measurable. They are calculated and set up formally as a part of the public debt as they accrue. Approximately equivalent taxes are levied on the beneficiaries, which go into the general fund. This means a large accumulation of government liability in the first 40 or more years, on which interest at a fixed rate is to be paid. This does not add to Government budget costs in the future, since, if the funds had not been received in payroll taxes, they would have had to be borrowed in the market. Current taxes plus interest on the so-called reserve would meet all future costs.

It is proposed now under any of the plans under contemplation to destroy the contributory nature of the system, since other beneficiaries are added and ultimately the general budget will have to bear a large share of the cost.

If other and earlier benefits are to be added, in my opinion sound fiscal policy requires that we raise the money to meet them by current taxation, but not by additional payroll taxes. This is what I was talking about when I said at one of the "peaks and valleys" meetings that we ought to reach into the middle brackets for more tax revenue, because we would need it for Social Security.

If we are going to adopt AC14 or any of the other reform plans, I agree with you
(payroll)
that we ought not to make the scheduled tax increase, since it won't be fair ^{to Contributors}