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TREASURY DEPARTMENT
WASHINGTON

January 11, 1943.

MEMORANDUM FOR THE SECRETARY:

I told you this morning that Mr. Odegard had gone to the Coast for a conference with Messrs. Skouras and Nesbitt about the Treasury Department motion picture.

Mr. Odegard just now (11:15 a.m.) phoned me from Amherst, saying that he had managed to see Nesbitt in New York, and that his proposed trip to the Coast is therefore not necessary. He will be in Washington to-morrow morning.

I have called the meeting which you suggested, for Thursday afternoon at 2:30.

GRAVES.





OFFICE OF THE DIRECTOR

TREASURY DEPARTMENT

PROCUREMENT DIVISION

WASHINGTON

January 11, 1948

MEMORANDUM TO THE SECRETARY:

(Personal)

Your association with the Byrd Committee prompts this memorandum to outline a proposal for a regional organization for all Government agencies in the field service and a centralization at such regional headquarters of service facilities specifically accounting, disbursing, GAO audit, procurement and personnel. This proposal represents a consolidation of many viewpoints which I have been developing because of my interest in the conservation of office equipment and facilities.

All agencies of the Government, irrespective of their operations, have a common need for accounting, disbursing, personnel, and procurement. Approximately four-fifths of the Federal employees are located in the field; to a large extent, each agency has established its field organization independently of other Government agencies and frequently obtains office space and facilities without regard to the location of other Federal agencies. Similarly there is little standardization with regard to service functions which represent a substantial proportion of administrative activities. In New Orleans, for example, there are Federal agencies located at some forty different addresses, exclusive of Post Offices and military branches, and there, as elsewhere, the regional areas of the different agencies overlap.

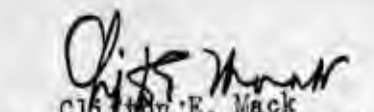
My thought is simply this, that the Byrd Committee, working in conjunction with a committee of the executive departments and agencies, make studies concerning the establishment of Federal districts which will be applicable to all agencies; that the headquarters of Federal agencies for each district be located in the same city and as far as possible in a single building. It would then be possible to centralize and consolidate in each district headquarters city the necessary accounting, disbursing, GAO audit, procurement, and personnel service functions for each district.



There would be substantial savings in personnel and greatly increased efficiencies in operation because of possible streamlining. In fact I consider that this plan has greater possibilities for more savings and better administration than any other approach.

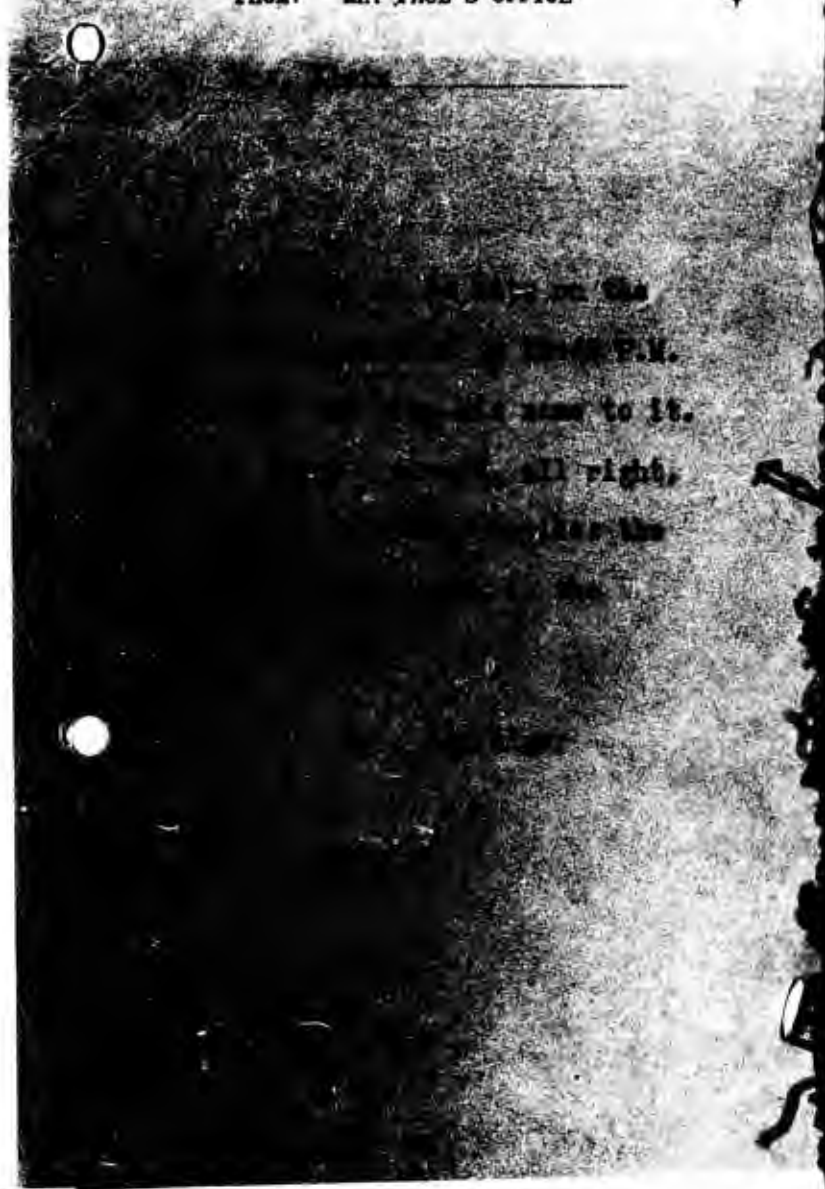
My preliminary thinking is to conserve office equipment which is becoming more critical each day but the most direct approach is through consolidation of service functions. Apart from the management advantages in utilizing personnel to the utmost, there would be a basis for the better use and upkeep of the vast quantities of equipment now owned by the field agencies and there would be a conservation of space through having a consolidation of inactive files in a common location (files now require from 1/4 to 1/3 of desirable and expensive personnel space); likewise there would be a savings in utility services. As an illustration, a combination of all Federal agencies for a given district in a single building within a headquarters city such as the Merchandise Mart in Chicago or the Empire State Building in New York City would permit the use of the least desirable space for the pooling of equipment for duplicating, photostating, etc., also for a common file space and a single common supply room to eliminate numerous separate inventories and coordination of personnel functions so as to avoid competition between the agencies. The advantages of having the accounting, disbursing, and GAO functions for each district would be the speeding up of Government business and elimination of Washington approval on routine matters which is now required to a very large extent. Title to Government property could be held by a single agency, for example the Public Buildings Administration, which would avoid the necessity of each agency moving its equipment and furniture each time there is a transfer with resulting delay and expense. At the present time each agency has title to its property in the District of Columbia and in the field service where private space is used but in Federal buildings the custodians have control. This could be standardized to advantage.

I feel very strongly that this is a real opportunity to effect substantial economies, to streamline the administrative procedure, avoid duplication, and develop effective coordination among all Government agencies.


Clifton E. Mack
Director of Procurement

FROM: MR. PAUL'S OFFICE

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TREASURY DEPARTMENT

INTER-OFFICE COMMUNICATION

DATE January 11, 1943

TO Secretary Morgenthau
FROM Randolph Paul

Pursuant to your telephone suggestion when I was in New York last week, I arranged appointments for today with Chairman Doughton of the Ways and Means Committee and Chairman George of the Senate Finance Committee with the thought in mind that I should communicate to them your attitude on the Budget message with particular reference to how you had supported your agreement with them that the Budget message should be general and should make no specific suggestions as to a tax program. I saw Chairman Doughton at 9:30 A. M., and spent about three-quarters of an hour with him. Later, at about 10:20, I saw Chairman George and spent about the same period of time with him. This memorandum is intended as a report of these conferences.

1. The first item of conversation with Chairman Doughton was the Groves report "Intergovernmental Fiscal Relations". I took with me a letter to the Chairman signed by Dan Bell as Acting Secretary, copy of which is attached hereto as Exhibit "A". The Chairman and I briefly discussed the scope and recommendations of this report. I made it clear to the Chairman that the recommendations were not Treasury recommendations. I gave him a few examples of recommendations and asked for his cooperation in getting the document (about 700 pages) published as an official publication. The Chairman promised cooperation.

2. I then said that I had one or two other things to discuss with the Chairman and he interrupted me to say that he would like to discuss with me the Ruml plan. There then followed a considerable discussion of that plan. The Chairman said that he was against the principle of the plan, but it had acquired such momentum

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that he thought we would have a hard time to resist it. I said the alternatives were complete resistance, complete acquiescence or some middle ground. I suggested the middle ground and specifically suggested a plan whereby the normal tax and the first bracket of surtax, or 19%, would be forgiven for 1942 and that some reasonable deferment would be arranged for the balance of the tax liability in the case of high-bracket taxpayers. This scheme would be coupled with very high collection at source. The Chairman did not commit himself on the idea but seemed reasonably favorably inclined. He asked that I discuss the plan with Stam and asked that after I discussed the plan with Stam that he and Chairman George and I should get together some evening for a further discussion.

3. I then went further with the Chairman with the suggestion that 1943 revenue legislation be separated into two parts - one part to consist of a modified Ruml plan and high collection at source, and (if you should agree with the idea) substantial compulsory saving, which items should be dealt with immediately so that collection at the source could be started at a high rate beginning with April 1, 1943. The Chairman seemed to think well of this suggestion and suggested that we should make it the subject of our evening conference.

4. I then discussed with Chairman Doughton the Budget message. I told him how the Budget had presented a draft message to us the week before last, following which it had been indicated to us on Saturday that no further policy suggestions would be permissible. I then told him how we had assembled in the Treasury on Sunday to prepare a stiff letter from you to the President. I did not show the Chairman the letter, but I did tell him some of the points made in the letter, and I did tell him particularly the point that you felt morally obliged to stand by your agreement with him that the Budget message should be general and not specific.

At this point the Chairman said "Now let me tell you something". He then told how the President had

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called him into conference last Tuesday with Senator George on the Budget message. They had been routed, since the President was not ready when the Chairmen arrived, through Justice Byrnes' office, and the three of them later saw the President. According to Chairman Doughton, they discussed the Budget message and several suggestions were made by Chairman Doughton. One of these suggestions, which the President accepted, was the language in the last paragraph:

"I shall be happy to meet with the appropriate committees of the Congress at any and all times in regard to the methods by which they propose to attain the objectives outlined in this Message. We are at one in our desire quickly to win this war and to avoid passing on to future generations more than their just share of its sacrifices and burdens."

Chairman Doughton thought that this was very tactful language and would do a great deal to help relations with Congress.

The Chairman and I then discussed your illness and he expressed considerable concern and friendly attitude toward you. Altogether his attitude was one of very considerable friendliness, both toward you and the Treasury. I asked him the attitude of the Committee toward the next tax bill and he said that it was quite good; obviously there were one or two members who might cause trouble. (I think he had in mind particularly Disney.) Incidentally, he said that the new Ways and Means Committee had been entirely chosen; the same ratio of fifteen Democrats and ten Republicans had been maintained, and he mentioned the names of the additional Democrats.

5. From Chairman Doughton's office I went to see Senator George. He very kindly routed me in ahead of my regular appointment time and ahead of a number of other callers. I told him that I had just seen Chairman

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Doughton. I repeated what I had said to Chairman Doughton, particularly with reference to the Ruml plan and collection at the source and Chairman George said that he approved of the idea of a preliminary meeting between Stam and me, which would be an evening meeting between Stam and me and Doughton and George. I think I began this meeting as I had begun the one with Chairman Doughton by discussing the Groves report. He thought the report should be published and said he would take the "laboring oar" to have passed in the Senate a Joint Resolution for the publication of the report.

6. Chairman George then discussed at some length your personal situation and indicated that he had a discussion of your personal situation with the President on the previous Tuesday. I told you today over the telephone what he said the President had told him. I think his discussion on this point was quite frank.

7. Chairman George did not commit himself on any of the tax points under discussion, but he did ask one significant question. When I spoke about 19% forgiveness for 1942, he asked whether we meant to take it all the way up the line to the big incomes. I said we did, and he seemed pleased that we were not limiting the forgiveness at some points where forgiveness got high.

8. I then brought into the conversation one of the real points of my visit to George - your attitude toward the Budget message. I told him pretty much what I had told Chairman Doughton. He then replied in what I thought was a much more candid way by saying that he and Chairman Doughton and Justice Byrnes had seen the President the previous Tuesday and that the President had told him all about your letter protesting against the draft. The Senator seemed quite generally familiar with your letter, the contents of which I had not revealed in detail. He spoke about having stopped with the President after Chairman Doughton and Justice Byrnes had left (on another matter) so that I am not entirely

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sure that this discussion did not occur after the others had left. This may explain Doughton's professed ignorance of the letter. At any rate, the President had apparently fully discussed your letter with Chairman George and had told him that the letter had opened his eyes to the fact that there was not agreement in the Executive Departments on the tax bill.

9. The next item in my conversation with Senator George was the \$25,000 limitation. At this point he appeared more friendly than I had felt him to be in any previous conversation when he asked me for my views on this limitation. He stated his own view that the limitation was most inadvisable for a liberal government since it penalized earned income and did not touch unearned income. I told the Senator quite frankly that I saw no excuse for this discrimination but that even without the discrimination the idea of a \$25,000 absolute limitation introduced very serious administrative problems. I frankly indicated that some of the best Bureau men were being detailed to work on the limitation program and that in my own personal view (this not being necessarily the Treasury view) the only practical way to handle the situation was an increase of the surtax rates which would accomplish a practical limitation and which would be administered as part of the regular income tax. I gathered the impression that the Senator would be willing as a compromise to take some increase of surtax rates in order to get rid of the existing situation.

Senator George expressed himself as being puzzled as to why Justice Byrnes had fallen in so readily with the \$25,000 limitation. I explained to the Senator that Justice Byrnes had come into this picture somewhat later and that the early stages of the development of the \$25,000 limitation had been handled by Judge Rosenman and others.

I gathered the impression that Senator George was very pleased with your attitude and the attitude of

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the Treasury at the moment and that he felt extremely hopeful that some program for early 1943 might be worked out in cooperation between the Treasury and the Congress.

10. I had lunch with Congressman Frank Carlson of Kansas who has introduced a Ruml plan which will be up in debate today for a limited period of twenty minutes in the House of Representatives. I pointed out to Carlson that his plan did not contain any collection at source mechanism and he said that he realized this deficiency and merely meant to get the subject started in discussion.

In the course of my luncheon with Carlson at the House restaurant, I ran into Disney of Oklahoma, McGrannery of Pennsylvania, and other members of the House. Carlson was very friendly in introducing me to practically all of the new members of the Ways and Means Committee. I had a pleasant brief discussion with each one of them.

11. I had a conference immediately after lunch with Carlson at the Wardman Park Hotel with John Hanes, Cheeva Cowden, some representatives of the National Association of Manufacturers and Ellsworth Alvord. I discussed with them further a general compromise plan, particularly involving a modified Ruml plan and heavy collection at the source. No conclusions were reached at this conference.

12. Late this afternoon I attended a cocktail party given by Mr. Justice Murphy at his apartment at the Washington Hotel. In the course of this meeting, Harold Smith grabbed me and discussed at some length with me his reaction to the Budget message. Generally the reaction was the same as I had previously heard from him to the effect that the relations between the Treasury and the Budget had worked out very unfortunately on this Budget message. I mostly listened with the general statement to the effect that the whole situation was very unfortunate. Smith suggested that we get together at an early date so as to avoid this sort of thing in the future.

13. In the middle of this afternoon, Mr. Gerhardt Colm called on me with respect to the last paragraph of my recent memo to Mr. Bell, which you will remember was forwarded to the President. Colm did not appear to know that the memo had gone to the President

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but he professed to be very perturbed at the statement in this last paragraph about his misrepresentations about the attitude of other agencies. I told him that I had not accused him of deliberate misrepresentations, but that I had merely said that other agencies did not agree with him. We left the matter with the thought that nothing more should be done on this point since Smith was not going to fire him because of my statements.

R.C.P.

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January 11, 1943

My dear Senator:

You will recall that in June, 1941, the Secretary of the Treasury designated a special committee to reexamine the problem of Federal-State-local fiscal relations. Study given the subject by the Department over a period of several years indicated that the increasing pressure on the same sources of revenue by Federal and State Governments made this problem one of major importance. It was clear that a vigorous and comprehensive inquiry was called for by a staff freed from all other responsibilities within the Department.

Accordingly, a small temporary research staff was assembled under the direction of Dr. Luther M. Gulick, Director of the Institute of Public Administration, Dr. Harold M. Groves, Professor of Economics at the University of Wisconsin and a former member of the Wisconsin Tax Commission, and Dr. Mabel Newcomer, Professor of Economics at Vassar College. The project was financed in part by special funds provided for this purpose by the Congress. The Institute of Public Administration provided funds to carry through such parts of the work as could not appropriately be financed by Federal funds.

The report of this Committee has recently been submitted to the Secretary of the Treasury. While this study was made within the Treasury and with the cooperation of responsible officers of the Treasury, its findings and recommendations are those of the committee and do not necessarily reflect the views of the Treasury Department.

This report is an important contribution to the problem of intergovernmental fiscal relations and brings together a body of current information which will be helpful to members of Congress and to others concerned with problems of Federal-State-local fiscal relations. For this reason, you may

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wish to consider the desirability of arranging for the publication of this report as a Congressional document. It would comprise an approximately 700-page printed document.

I am addressing a similar communication to the Chairman of the Ways and Means Committee of the House of Representatives.

Sincerely yours,

(Signed) D. W. Bell

Acting Secretary of the Treasury

Honorable Walter F. George
United States Senate
Washington, D. C.

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January 11, 1948

My dear Mr. Doughton:

You will recall that in June, 1941, the Secretary of the Treasury designated a special committee to reexamine the problem of Federal-State-local fiscal relations. Study given the subject by the Department over a period of several years indicated that the increasing pressure on the same sources of revenue by Federal and State Governments made this problem one of major importance. It was clear that a vigorous and comprehensive inquiry was called for by a staff freed from all other responsibilities within the Department.

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This report is an important contribution to the problem of intergovernmental fiscal relations and brings together a body of current information which will be helpful to members of Congress and to others concerned with problems of Federal-State-local fiscal relations. For this reason, you may

- 2 -

wish to consider the desirability of arranging for the publication of this report as a Congressional document. It would comprise an approximately 700-page printed document.

I am addressing a similar communication to the Chairman of the Committee on Finance of the United States Senate.

Sincerely yours,

(Signed) D. W. Bell

Acting Secretary of the Treasury

Honorable Robert L. Doughton
Chairman of the Ways and Means Committee
House of Representatives
Washington, D. C.



ASSISTANT SECRETARY

TREASURY DEPARTMENT

Washington.

January 11, 1943.

My dear Mr. Secretary:

In accordance with your request of January 8th I am enclosing herewith two memoranda. The first contains a proposed draft of legislation to relieve the estates of members of the armed forces who died as a result of active service. The second is a review of the tax status of members of the armed forces.

The proposed legislation is not approved by myself or by anyone with whom I have discussed the matter. Saturday, January 9th, I had occasion to talk with Admiral Carter of the Navy and General Carter of the Army. In the course of our conference they both spoke about the Vandenberg article and indicated their disapproval of the proposed type of relief. I did not disclose to either of them our interest in the matter.

If you care for a memorandum stating the case against this legislation, I will be glad to furnish it.

I am also enclosing a galley proof of the Federal income tax information to be sent to the men in the Navy by the Navy Department. A similar pamphlet is being prepared for use by the War Department.

As a result of our conference Saturday with the Army and the Navy, we are to issue a press release clarifying the tax incidents of allotments and family allowances. In addition to this we are to prepare a brief statement setting forth the taxability or non-taxability of the particular check involved and these statements will be enclosed with all checks sent out by the Army and the Navy for the next two months. This should clarify the situation for the families of all servicemen.

Sincerely yours,

Honorable Henry Morgenthau, Jr.,
Secretary of the Treasury.

DEFENSE

BUY
UNITED
STATES
SAVINGS
BONDS
AND STAMPS

MEMORANDUM

January 9, 1943.

TO: Secretary Morgenthau
FROM: Mr. Sullivan JLS
RE: Proposed Legislation Relieving the Estates
of Members of the Armed Forces from Federal
Income Tax Liability.

The following is a proposed draft of legislation which would relieve the estates of members of the armed forces of the United States who die as a result of active service performed during the present war and who leave surviving them widows, minor children, or dependent relatives:

"Be it enacted by the Senate
and the House of Representatives of
the United States of America in
Congress assembled,

That Chapter 1 of the Internal Revenue
Code is amended by inserting after
section 128 the following new section:

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Sec. 129. Tax Liability in respect of Deceased Members of the Armed Forces.-- In the case of a member of the military or naval forces of the United States who dies as a result of active service performed in such forces during the present war and who leaves surviving him a spouse, minor child, or any dependent relative, the liability for all Federal income taxes attributable to any income received or accrued by him during the taxable year in which his death occurs and during any preceding taxable year is wholly cancelled."

NAVY DEPARTMENT
BUREAU OF SUPPLIES AND ACCOUNTS
WASHINGTON, D. C.

DECEMBER 18, 1942.

FEDERAL INCOME TAX INFORMATION

1. The following information, for all persons in the naval service, relative to Federal income tax, calendar year 1942, and Federal Victory Tax, calendar year 1943, is published with the approval of the Bureau of Internal Revenue.

PENALTIES

2. Heavy penalties are imposed:

- (a) For failure to file return.
- (b) For failure to file return on time.
- (c) For submitting false return.
- (d) For wilful failure to pay the tax.

DEFINITIONS

3. "Earned income" means wages, salaries, professional fees, and other amounts received as compensation for professional services actually rendered, but does not include any amount not included in gross income, nor that part of the compensation derived by the taxpayer for personal services rendered by him to a corporation which represents a distribution of earnings or profits rather than a reasonable allowance as compensation for the personal services actually rendered. In the case of a taxpayer engaged in a trade or business in which both personal services and capital are material income producing factors, a reasonable allowance as compensation for the personal services actually rendered by the taxpayer, not in excess of 20 per centum of his share of the net profits of such trade or business, shall be considered as earned income.

4. "Earned net income" means the excess of the amount of the earned income over the sum of the earned income deductions. If the taxpayer's net income is not more than \$3,000, his entire net income shall be considered to be earned net income; and if his net income is more than \$3,000, his earned net income shall not be considered to be less than \$3,000. In no case shall the earned net income be considered to be more than \$14,000.

5. "Taxable year" means the calendar year, or the fiscal year ending during such calendar year, upon the basis of which the net income is computed. "Taxable year" means, in the case of a return made for a fractional part of a year under the provisions of this act or under regulations prescribed by the Commissioner with the approval of the Secretary, the period for which such return is made.

6. "Fiscal year" means an accounting period of 12 months ending on the last day of any month other than December.

7. The term "paid or incurred" and "paid or accrued" shall be construed according to the method of accounting upon the basis of which the net income is computed.

8. The term "trade or business" includes the performance of the functions of a public office.

NOTE.—Naval personnel are engaged in a "trade or business."

9. "Net income" means gross income less allowable deductions.

10. "Dividends" means any distribution made by a corporation to its shareholders, whether in money or in other property, out of its earnings or profits, accumulated after February 28, 1913, or out of the earnings or profits of the taxable year (computed as of the close of the taxable year without diminution by reason of any distribution made during the taxable year) without regard to the amount of the earnings and profits at the time the distribution was made.

RECORDS AND SPECIAL RETURNS

11. Every person liable for a Federal Income Tax shall keep such records, render such statements, make such returns, and comply with such rules and regulations, as the Commissioner deems sufficient to show whether or not such person is liable for an income tax.

ACCOUNTING PERIODS

12. The net income shall be computed on the basis of the taxpayer's annual accounting period, either calendar or fiscal year.

13. If the taxpayer has no accounting period, or does not keep books, the net income shall be computed on the basis of the calendar year, and the computation shall be made in accordance with such method as, in the opinion of the Commissioner, clearly reflects the income.

14. If a taxpayer, with the approval of the Commissioner, changes his accounting period from fiscal year to calendar year, from calendar year to fiscal year, or from one fiscal year to another, the net income shall be computed on the basis of such new accounting period. In such a case, the net income computed for the fractional part of a year shall be placed on an annual basis.

15. If the taxpayer, with the approval of the Commissioner, changes the basis of computing net income from fiscal year to calendar year, a separate return shall be made for the period between the close of the last fiscal year for which return was made and the following December 31.

If the change is from calendar year to fiscal year, a separate return shall be made for the period between the close of the last calendar year for which return was made and the date designated as the close of the fiscal year. If the change is from one fiscal year to another fiscal year, a separate return shall be made for the period between the close of the former fiscal year and the date designated as the close of the new fiscal year.

BLANK FORMS USED

16. Returns must be made on Form 1040, except in the case of an election of the optional tax under paragraph 65, when return is made on Form 1040A, with a statement in either case that it is made under penalties for perjury.

WHO MUST FILE RETURNS

17. Every individual who is single, or who is married but not living with husband or wife, if having a gross income for the taxable year of \$500 or over.

18. Every individual who is married and living with husband or wife, if no joint return is made under paragraph 19 and if—

(a) Such individual has for the taxable year a gross income of \$1,200 or over, and the other spouse has no gross income; or

(b) Such individual and his spouse each has for the taxable year a gross income and the aggregate gross income is \$1,200 or over.

19. In the case of a husband and wife living together the income of each (even though one has no gross income but has allowable deductions and/or credits) may be included in a single return made by them jointly, in which case the tax shall be computed on aggregate net income, and the liability with respect to the tax shall be joint and several.

20. If the taxpayer is unable to make his own return, the return shall be made by a duly authorized agent or by the guardian or other person charged with the care of the person or property of such taxpayer.

21. All persons making payment to another person of interest, wages, rent, etc., of \$500 or more in any taxable year, shall render a true and accurate return to the Commissioner of Internal Revenue, Returns Distribution Section, Washington, D. C. (not to the collector), on or before February 15 of each year in such form as he may prescribe, setting forth the amount paid, and the name and address of the recipient. The return shall be made on Form 1099, accompanied by Form 1096. Form 1099, however, will not be required with respect to payments during 1942 to persons in the armed forces of the United States, or with respect to wage payments in 1943 from which the Victory Tax has been withheld.

EXAMPLE: If a person pays \$500 or more rent to the owner he must send in the report. Report not necessary if rent is paid to a real-estate agent, as such agent is required to file the information return.

TIME FOR FILING RETURNS

Returns made on the basis of the calendar year shall be filed in the office of the collector on or before the 15th day of March following the close of the calendar year, and returns made on the basis of a fiscal year shall be filed in the office of the collector on or before the 15th day of the third month following the close of the fiscal year, unless the due date is otherwise extended or postponed.

23. The Commissioner of Internal Revenue is authorized to grant a reasonable extension of time for filing returns under such rules and regulations as he shall prescribe with the approval of the Secretary of the Treasury. Except in the case of taxpayers who are abroad, applications for extension of time for filing income-tax returns should be addressed to the collector of internal revenue for the district in which the taxpayer files his returns and must contain a full recital of the causes for delay and no extension for filing income-tax returns may be granted as prescribed in this paragraph, for more than 6 months.

24. In the case of American citizens residing or traveling abroad, including persons in the military or naval service on duty outside of the United States, the regulations issued by the Bureau of Internal Revenue permit an extension of time for filing returns of income tax to and including the 15th day of the sixth month following the close of the taxable year. Specific approval for this extension is not required but in all such cases an affidavit must be attached to the returns stating the cause of the delay in filing. Taxpayers who take advantage of this extension of time will be charged with interest at the rate of 6 percent per annum on the first installment of tax from the original due date until paid. (But see par. 68.)

25. The time for filing returns is further extended by the provisions of the act of March 7, 1942, and the Revenue Act of 1942 in the case of certain individuals. (See par. 68.)

PLACE FOR FILING RETURNS

26. Returns and payments shall be made to the collector for the district in which is located the legal residence or principal place of business of the person making the return; or if he has no legal residence or principal place of business in the United States, then to the collector of internal revenue at Baltimore, Md.

27. Officers, enlisted men and other employees of the naval service who have no legal residence:

- (a) When on duty in Alaska *may* file their returns with the collector of internal revenue, at Tacoma, Wash.
- (b) When on duty in the Hawaiian Islands, *may* file their returns with the collector of internal revenue at Honolulu, Hawaii.

GROSS INCOME TO BE REPORTED

28. "Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever.

29. In the case of a citizen of the United States satisfying the following conditions of section 251 (a) of the Internal Revenue Code, gross income means only gross income from sources within the United States:

- (1) If 80 per centum or more of the gross income of such citizen (computed without the benefit of this section), for the 3-year period immediately preceding the close of the taxable year (or for such part of such period immediately preceding the close of such taxable year as may be applicable) was derived from sources within a possession of the United States; and
- (2) If 50 per centum or more of the gross income of such citizen (computed without the benefit of this section), for such

period or such part thereof was derived from the active conduct of a trade or business within a possession of the United States either on his own account or as an employee or agent of another.

A citizen satisfying the above conditions is only required to include in gross income his income from sources within the United States or income derived from sources within or without the United States which is received by him or any agent of his within the United States. When compensation is received for services rendered, the "source" of the income is the place where the services are rendered rather than the place from which payment is made for such services. The salary or other compensation paid by the United States to the members of its civil, military, or naval personnel for services rendered within a possession of the United States represents income derived from the active conduct of a trade or business within a possession of the United States. The benefits of this section apply to personnel attached to United States naval vessels only for such periods as the vessels are within the territorial waters of a possession of the United States.

In the case of a citizen of the United States who cannot satisfy the above conditions of section 251, *supra*, all compensation received for services rendered to the United States, or any of its agencies, is required to be included in gross income, whether the recipient has lived all or any part of the year outside the continental limits of the United States.

30. From Navy sources:

- (a) Pay, base and longevity (active list), including pay as midshipmen, and including all allotments from pay.
- (b) Pay (retired list).
- (c) Extra compensation for special duty (aviation, submarine, etc.).
- (d) Mileage (report entire amount received as gross income and deduct necessary traveling expenses, *actually paid*, such as meals, railroad fares, lodging, etc.). Where optional Form 1040A is used, include as a part of gross income only the amount of mileage in excess of actual expenses.
- (e) Travel pay to discharged enlisted men (report in the same manner as mileage).
- (f) Transportation of families of officers and enlisted men (the actual cost of such transportation to the Government is considered taxable income. No deduction allowed.)
- (g) Interest on deposits of enlisted men.
- (h) All permanent and transient additions to pay (enlisted men).
- (i) One year's pay received by officers wholly retired.
- (j) Allowances received by retired enlisted men under act of March 2, 1907 (\$9.50 per month in lieu of rations and clothing and \$6.25 per month in lieu of quarters, fuel, and light).
- (k) Enlistment allowance (enlisted men).

31. From sources outside the Navy:

- (a) Compensation for personal or professional services.

- (b) Business income, either as an individual proprietor or as a partner in a business operated for profit.
- (c) Profits from sales and dealings in properties (real or personal, tangible or intangible).
- (d) Income from investments in properties or securities, such as rent or interest.
- (e) Dividends from a domestic corporation.
- (f) Pensions paid by a State for services are subject to the Federal income tax.

EXCLUSIONS FROM GROSS INCOME

32. *Life insurance.*—Amounts received under a life-insurance contract paid by reason of the death of the insured, whether in a single sum or otherwise (but if such amounts are held by the insurer under an agreement to pay interest thereon, the interest payments shall be included in gross income).

33. *Annuities.*—Amounts received (except as stated in par. 32 above) under a life insurance or endowment contract, but if such amounts (when added to amounts received before the taxable year under such contract) exceed the aggregate premiums or consideration paid (whether or not paid during the taxable year) then the excess shall be included in gross income. Amounts received as an annuity under an annuity or endowment contract shall be included in gross income to the extent of 3 per centum of the cost of the annuity (the aggregate premiums for consideration paid for such annuity, whether or not paid during such year), until he has received tax-free under this or prior income tax laws an amount equal to such cost; thereafter the annuity is taxable in full. In the case of a transfer for a valuable consideration, by assignment or otherwise, of a life insurance, endowment, or annuity contract, or any interest therein, only the actual value of such consideration and the amount of the premiums and other sums subsequently paid by the transferee shall be exempt from taxation under paragraph 32 or this paragraph. Where, however, the contract has a basis for gain or loss in the hands of the transferee, determined in whole or in part with reference to the transferor's basis, the provisions of the preceding sentence shall be inapplicable to taxable years beginning after December 31, 1940.

34. *Gifts, etc.*—The value of property acquired by gift, bequest, devise, or inheritance. Income from such property, or, if the gift, bequest, devise, or inheritance is of income from property, the amount thereof shall not be excluded from gross income under this paragraph.

35. *Tax-free interest.*—Interest upon:

- (a) Obligations of a State, Territory, or political subdivision, thereof, or the District of Columbia, or United States possessions; or
- (b) Obligations issued prior to March 1, 1941, under Federal Farm Loan Act, or under such Act as amended; or
- (c) Obligations of United States issued on or before September 1, 1917; or
- (d) Treasury Notes, Treasury Bills, and Treasury Certificates of Indebtedness issued prior to March 1, 1941; or

- (a) Principal amount of United States Savings Bonds and Treasury Bonds, not in excess of \$5,000, issued prior to March 1, 1941.

Any person owning any of the obligations enumerated above shall, in the income-tax return, submit a statement showing the number and amount of such obligations owned by him and the income received therefrom, in such form and with such information as the Commissioner may require. In the case of obligations of the United States issued after September 1, 1917, and in the case of obligations of a corporation organized under act of Congress, the interest shall be exempt only if and to the extent provided in the respective acts authorizing the issue thereof as amended and supplemented, and shall be excluded from gross income only if and to the extent it is wholly exempt from the taxes imposed by this income-tax law. Interest credited to Postal Savings accounts upon moneys deposited prior to March 1, 1941, in Postal Savings Banks is wholly exempt from income tax.

36. *Compensation for injuries or sickness.*—Except in the case of amounts attributable to (and not in excess of) deductions allowed under paragraph 41 in any prior taxable year, amounts received through accident or health insurance or under workmen's compensation acts, as compensation for personal injuries or sickness, plus the amount of any damages received whether by suit or agreement on account of such injuries or sickness. Also amounts received as a pension, annuity, or similar allowance for personal injuries, or sickness resulting from active service in the armed forces of any country.

37. *Stock dividends.*—No definite rule can be laid down regarding the taxability of stock dividends. Each case must be decided on its own merits.

38. *From naval sources.*—

- (a) Pay of military or naval personnel, below the rank of commissioned officer, for active military or naval service, during the present war, not to exceed \$250 in case of a single person, and \$300 in the case of a married person or head of a family. Status determined as of the end of taxable year. For example: An enlisted man in the Navy, who is single, received \$648 Navy pay during the calendar year 1942, and \$500 from dividends. He is required to include in his gross income only \$398 (\$648 less \$250) from Navy pay, plus \$500 from ~~stock~~ dividends.
- (b) Retired pay of persons retired from the naval service for physical disabilities incurred in line of duty.
- (c) Uniforms furnished in kind to enlisted men.
- (d) Rations furnished in kind to enlisted men.
- (e) Commutation of rations (enlisted men).
- (f) Gratuity pay (6 months' pay to beneficiary of a deceased officer or enlisted man).
- (g) Rental allowance (act of June 16, 1942); nor need any amount be reported on account of quarters, heat, and light furnished in kind.
- (h) Subsistence allowance (act of June 16, 1942).
- (i) Per diem allowance in lieu of subsistence.

- (j) Amounts received in reimbursement for losses, sustained by officers, nurses, enlisted men, and civil employees serving under the Navy Department in foreign countries, due to appreciation of foreign currencies in the relation to the American dollar, as authorized by the act of March 26, 1934 (48 Stat. 466), and by Executive order dated September 15, 1938, as amended.
 - (k) Personal cash allowance received by admirals and vice admirals.
 - (l) Uniform gratuity or allowance paid to officers, nurses, or enlisted personnel.
 - (m) Money allowance for quarters paid enlisted men under the act of October 17, 1942.
39. *From other sources.*—
- (a) Pensions received from the United States by the family of a veteran for services rendered to the United States in time of war are exempt as gifts.
 - (b) Pensions received from the United States by veterans under the World War Veterans' Act of 1924, as amended, and Emergency Officers' Retirement Act or for services in the Spanish-American War (act of August 12, 1935 (49 Stat. 607)).
 - (c) A pension paid by a State to a beneficiary for services rendered by another person is exempt from Federal income tax as a gift (I. T. 2689, Cumulative Bulletin XII-1, p. 68).
 - (d) Dividends from war-risk insurance policies.
 - (e) Periodic payments to a divorced or legally separated wife subsequent to a divorce or separate maintenance decree and attributable to property transferred in trust or otherwise, in discharge of a legal obligation incurred by husband under such decree or under a written instrument incident to such divorce or separation with respect to marital or family relationship shall not be includible in husband's gross income, except to the extent that such periodic payments represent amounts for the support of minor children of such husband as fixed by the terms of the decree or written instrument. Such payments excluded from the husband's gross income are income to the divorced or legally separated wife. Periodic payments within the meaning of this paragraph mean payment, whether or not made at regular intervals, and not lump sum payments of alimony. If there is a lump sum settlement payable in installments and the final payment under it is not to be made within 10 years, nor more than 10 per centum of the lump sum is paid in any taxable year, the amount paid in each taxable year will be considered a periodic payment.

DEDUCTIONS ALLOWED

40. *Business expenses.*—
- (a) Dues to professional societies.
 - (b) Subscriptions to professional journals.

- (c) The cost of items of equipment, such as sword, corps devices, full-dress belt, undress belt, epaulets, campaign bars, and aiguillets, are deductible as business expenses.
- (d) *Mess bills afloat.*—A naval officer while on permanent duty afloat who actually maintains a home elsewhere is entitled to deduct only the difference between amount expended for mess bill and the amount of his subsistence allowance. For example: An officer with dependents receiving subsistence allowance of \$18 per month and who pays a mess bill of \$30 per month is entitled only to a deduction of \$12 for each month. The existence of a "home" is a question of fact to be determined in each individual case (to the satisfaction of the Commissioner of Internal Revenue). If an officer does not have a "home," the difference between amount paid for mess bill and subsistence allowance received is not deductible.

41. *Extraordinary medical, dental, etc., expenses.*—Expenses paid by the taxpayer during taxable year for medical care of the taxpayer, his spouse, or a dependent of the taxpayer, which is not compensated for by insurance or otherwise, to the extent that such expenses exceed 5 per centum of the taxpayer's net income computed without this deduction, but limited however to \$2,500 in the case of husband and wife filing joint returns, and in the case of head of a family; and to \$1,250 in the case of all other individuals who file separate returns.

The term "medical care" includes amounts paid for the diagnosis, cure, mitigation, treatment, or prevention of disease or for the purpose of affecting any structure or function of the body, including amounts paid for accident, health or hospitalization insurance, or group hospitalization.

42. *Alimony payments, etc.*—Periodic payments (see par. 39 (e)) to a divorced or legally separated wife subsequent to a divorce or separate maintenance decree in discharge of a legal obligation incurred by the taxpayer because of the marital or family relationship. However, a deduction is not allowable for any such periodic payments, attributable to property transferred in discharge of such legal obligations, which are stated in paragraph 39 (e) not to be includible in the taxpayer's gross income.

43. *Losses.*—

- (a) Sustained during the taxable year and not compensated for by insurance or otherwise when incurred in trade or business.
- (b) Sustained in transactions entered into for profit, though not connected with trade or business and not compensated for by insurance or otherwise.
- (c) Sustained in transactions not connected with trade or business if arising from fire, storm, shipwreck, or other casualty, or from theft, and not compensated by insurance or otherwise. (Loss of personal property through accident, such as a ring from a finger, is not deductible).

- (d) A loss on the sale of residential property is not deductible, if used as taxpayer's residence up to time of sale. If before sale it was rented or otherwise converted to income-producing purposes and used as such up to time of sale, loss deductible, as provided in section 111, of the Internal Revenue Code, subject to limitation provided in section 117, in an amount not to exceed the value when changed to rental use over amount from sale.
 - (e) Losses on the sale of shares of stocks or securities are deductible, provided no deductions shall be allowed in cases where it appears that within 30 days before or after the sale the taxpayer has acquired (by purchase or by an exchange upon which the entire amount of gain or loss was recognized by law), or has contracted to acquire substantially identical stock or securities. The loss must be complete and net, and the transaction actually closed in the year in which deducted. Depreciation in value of stocks and bonds held by a taxpayer is not deductible; as loss to be deductible must result from a closed transaction.
 - (f) If securities such as shares of stock, stock rights, and bonds with interest coupons or in registered form, become worthless within the year and are capital assets, the resulting loss is to be treated for income tax purposes as a loss from the sale or exchange, on the last day of the year, of capital assets. It will therefore become subject to the limitations prescribed by section 117 of the Internal Revenue Code as explained in detail in the income tax return Form 1040.
 - (g) A loss occasioned by damage to an automobile maintained for pleasure, where such damage results from the faulty driving of the taxpayer or other person operating the automobile, but is not due to the wilful act or wilful negligence of the taxpayer, is a deductible loss in the computation of net income. If damage to a taxpayer's automobile results from the faulty driving of the operator of an automobile with which the automobile of taxpayer collides, the loss occasioned to the taxpayer by such damage is likewise deductible.
 - (h) *War losses.*—Losses of property destroyed or seized in the course of military or naval operations during the war, and of property located in enemy countries or in areas under enemy control (Sec. 156, R. A. 1942).
 - (i) Loss of naval disbursing officers due to replacement of shortage in accounts not due to negligence.
44. *Taxes.*—
- (a) Poll tax.
 - (b) State income tax.
 - (c) Admittance tax on theaters, amusements, etc. (records must be kept of such taxes paid).
 - (d) Tax on lodge or club dues, if substantiated by records kept.
 - (e) Real and personal property taxes (except when paid for local benefits, enhancing the value of the property, such as assessments for street improvements, sidewalks, sewers, etc.).

- (f) Taxes assessed by foreign country or a possession of the United States, except estate, inheritance, legacy, succession, and gift taxes, provided credit for such taxes is not taken under paragraph 67.
- (g) Taxes assessed by the United States (except Federal income tax, estate, inheritance, legacy, succession, and gift taxes). Postage is not a tax.
- (h) Taxes assessed by a State or Territory or political subdivisions thereof (except taxes for local benefits, estate, inheritance, legacy, succession, and gift taxes).
- (i) Miscellaneous taxes.
 - (1) The manufacturers' excise taxes under the Internal Revenue Code, as amended, are imposed by the law on the manufacturer and paid by him to the collector of internal revenue and are not regarded as taxes paid by the consumer of the article, even though they may be passed on to him in whole or in part in the price of the article. Accordingly, taxes paid on electricity, cigarettes, gasoline, lubricating oil, tires, and automobile accessories, firearms, matches, chewing gum, jewelry, wort, malt syrup, grape concentrate, radio, phonograph records, and cosmetics are not items which the consumer may deduct from his income as taxes paid by him.
 - (2) The Retailers' excise taxes under the Internal Revenue Code, as amended, are imposed by law on the retailer and paid by him to the Collector of Internal Revenue and are not regarded as taxes paid by the purchaser of the article, even though they may be passed on to him in whole or in part in the price of the article. Accordingly, taxes paid on pearls, precious and semiprecious stones, and imitations thereof; articles made of, or ornamented, mounted, or fitted with, precious metals or imitations thereof; watches and clocks and cases and movement therefor; gold, gold-plated, silver, silver-plated, or sterling flatware or hollow ware; opera glasses; lorgnettes; marine glasses, field glasses; binoculars; furs; and toilet preparations; perfumes, essences, extracts, toilet waters, cosmetics, petroleum jellies; hair oils, pomades, hair dressings, hair restoratives, hair dyes; aromatic cachous, toilet powders, and any similar substance, article, or preparation, by whatsoever name known or distinguished are not items which the purchaser may deduct from his income as taxes paid by him.
 - (3) The situation is different with regard to the tax on telephone, telegraph, safety deposit boxes, club dues, admissions, the various stamp taxes on securities and deeds. In the case of these taxes the law places the liability for tax on the person paying for the service, selling the securities, etc.,

although in some instances the person receiving the payment is required to collect the tax and pay it over to the Collector of Internal Revenue. Payments on account of these several taxes represent taxes paid by the individual which under the law he may deduct from his income.

- (4) In the case of gasoline the distinction between the application of State and Federal taxes should be noted. The Federal tax is imposed on the manufacturer and is *not* deductible by the purchaser, while the State taxes are held to be taxes imposed on the purchaser and are deductible by him from his income, *except* in the following States where the tax is imposed on the oil company, dealer, distributor, or wholesaler:

Alabama.
California.
Georgia.
Hawaii.
Kansas City, Mo.
Kentucky.
Louisiana.
Mississippi.
Nebraska.
Ohio (dealer, 1 cent; consumer, 3 cents).
South Carolina.
Tennessee.
Utah (deductible by consumer when purchased in original package for his own use).
Wyoming.

However, by Section 122 of the Revenue Act of 1942, the purchaser may also deduct such taxes of the foregoing named States when passed on to him if the taxes are separately stated by the seller, and are based on the gross selling price.

- (5) Automobile license fees are ordinary taxes.
(6) Stamp taxes imposed on the purchase or sale of securities are deductible as taxes. However, commissions on the purchase or sale of securities should be added to the purchase price or deducted from the selling price of such securities.
(7) State sales taxes imposed by the following States are deductible by the purchaser when substantiated by records:

Arkansas.
Colorado.
Iowa.
Kansas.
Missouri.
New York City.
North Dakota.
Ohio.
Oklahoma.
Utah.
Washington.
West Virginia.
Wyoming (except on sales of 24 cents or less).

The sales taxes imposed by other States are also deductible by the purchaser where they are passed on to him if the taxes are separately stated by the seller, and are based on the gross selling price of the article.

45. Interest paid on personal indebtedness is deductible. This does not include interest paid on indebtedness incurred or continued to purchase or carry obligations, except obligations of the United States issued after September 24, 1917, and originally subscribed for by the taxpayer, the interest upon which is wholly exempt from the income tax. Interest paid by the taxpayer on a mortgage upon real estate of which he is the legal or equitable owner, even though the taxpayer is not directly liable upon the bond or note secured by such mortgage, may be deducted as interest on his indebtedness. Interest charged by a broker on the balance due on the purchase of securities is deductible when actually or constructively paid by the deposit of cash, by the collection by the broker of dividends or interest for the account of the customer, or by the sale of securities of the customer held by the broker or to be received by him.

46. Repairs, alterations, and depreciation on property owned by the taxpayer for business purposes or for production of income are deductible under certain conditions set forth in detail in the Treasury Department's circulars and regulations.

47. *Gifts.*—

(a) Charitable gifts are deductible if payment is made within the taxable period to or for the use of (a) the United States, any State, Territory, or any political subdivision thereof, or the District of Columbia, or any possession of the United States, for exclusively public purposes; (b) a corporation, trust, or community chest fund or foundation created or organized in the United States or in any possession thereof, or under the law of the United States or of any State or Territory or possession of the United States, organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, or for the prevention of cruelty to children or animals. For example: Churches, Young Men's Christian Association, Red Cross, American Legion, the Soldiers' and Sailors' Club of New York, and Society for the Prevention of Cruelty to Animals.

(b) An itemized list, giving the names of the organizations; their locations, and the amount of the gift made to each, must be entered as a part of the return, or be appended thereto. The authorized deduction cannot exceed 15 percent of the taxpayer's net income as computed without the benefit of the deduction for gifts, or of the deduction for extraordinary medical expenses described in paragraph 41.

(c) Private gifts (as charity or for other reasons) to a person or persons are not deductible.

48. Bad debts may be deducted in the taxable year in which they become worthless. A statement must be made on the reverse of the tax return showing:

(a) Nature of the debts.

(b) When created.

(c) When due.

(d) The basis for declaring the debt as worthless.

If the debts are collected in whole or in part at a subsequent time, the amount collected must be reported as income in the year received, provided that the previous deduction did not reduce the income tax liability of the taxpayer for the year of the deduction. Bad debts sustained in connection with notes, bonds, and other securities with interest coupons or in registered form will, however, be treated the same as the securities referred to in paragraph 43 (f).

49. *Wagering losses*.—Losses from wagering transactions shall be allowed only to the extent of the gains from such transactions.

DEDUCTIONS NOT ALLOWED

50. War-risk insurance premiums or other premiums paid for life insurance.

51. *Uniforms*.—(Cost of uniforms held to be in the nature of personal or living expenses. No deduction is allowed on account of depreciation or obsolescence of uniforms.)

(a) Items of equipment, such as gold lace, chin strap, gilt buttons, gilt and silver devices on caps, and gold lace and gilt buttons on the uniforms are considered a part of the uniform and cap which take the place of regular clothing, and the cost thereof may not be deducted. The cocked hat takes the place of the hat ordinarily worn on full-dress occasions in civil life and the cost is not deductible.

(b) The cost of altering the equipment on a uniform subsequent to promotion or demotion is a personal expense and not deductible.

52. Loss of pay by sentence of court martial; or civil court fines and penalties.

53. Hospital-fund deductions from Navy pay. (But see par. 41.)

54. Personal, living, or family expenses, except extraordinary medical expenses deductible under paragraph 41.

55. Any amount paid out for new buildings or for permanent improvements or betterments made to increase the value of any property or estate.

56. Any amount expended in restoring property, or in making good the exhaustion thereof, for which an allowance is or has been made.

57. Loss from sales or exchanges of property, directly or indirectly,

(a) Between members of a family;

(b) Except in case of distributions in liquidation, between an individual and a corporation in which such individual owns, directly or indirectly, more than 50 percent in value of the outstanding stock.

(c) For the purpose of this paragraph, an individual shall be considered as owning the stock owned, directly or indirectly, by his family; and

(d) The family of an individual shall include only his brothers and sisters (whether by the whole or half blood), spouse, ancestors, and lineal descendants.

PERSONAL EXEMPTIONS

[Are credits against net income for both normal tax and surtax]

58. In the case of a single person, or a married person not living with husband or wife, a personal exemption of \$500.

59. In the case of the head of a family, or a married person living with husband or wife during entire taxable year, a personal exemption of \$1,200.

60. A husband and wife living together shall receive but one personal exemption. The amount of such personal exemptions shall be \$1,200. If such husband and wife make separate returns, other than returns under paragraph 65, the personal exemption may be taken by either or divided between them.

61. CREDIT FOR DEPENDENTS.—

(a) *Allowance in general.*—\$350 for each person (other than husband or wife) dependent upon and receiving his chief support from the taxpayer if such dependent person is under 18 years of age or is incapable of self-support because mentally or physically defective.

(b) *Exception for certain heads of families.*—If the taxpayer would not occupy the status of head of a family except by reason of their being one or more dependents for whom he would be entitled to credit under subparagraph (a), the credit under such subparagraph shall be disallowed with respect to one of such dependents.

(c) If the status of the taxpayer, insofar as it affects the personal exemption or credit for dependents, changes during the taxable year, the personal exemption and credit shall be apportioned, under rules and regulations prescribed by the Commissioner with the approval of the Secretary, in accordance with the number of months before and after such change. For the purpose of such apportionment a fractional part of a month shall be disregarded unless it amounts to more than half a month, in which case it shall be considered as a month.

CREDIT AGAINST NET INCOME FOR THE NORMAL TAX, BUT NOT FOR THE SURTAX

62. The amount received as interest, upon certain obligations of the United States, and included in the gross income. (See par. 35.) (Read instructions on income-tax blank form.)

63. *Earned income credit.*—Ten percent of the amount of the earned net income, but not in excess of 10 percent of the amount of the net income. (See Definitions, par. 4.)

NORMAL TAX ON INDIVIDUALS

64. There shall be paid for each taxable year upon the net income of every individual a normal tax of 6 percent of the amount of the net income in excess of personal exemptions and credits allowed.

**OPTIONAL TAX ON INDIVIDUALS WITH CERTAIN GROSS INCOME
OF \$3,000 OR LESS**

65. In lieu of the tax imposed under paragraphs 64 and 66, an individual who makes his return on the cash basis, may elect, for each taxable year, to pay the tax shown in the following table if his gross income for such taxable year is \$3,000 or less and consists wholly of one or more of the following: Salary, wages, compensation for personal services, dividends, interest, or annuities.

If the gross income is over—	But not over—	The tax shall be—		
		Single persons (not head of a family)	Married persons making separate returns	(1) Married person whose spouse has no gross income or (2) Married per- son making joint return or (3) Head of family
\$0.....	\$525	\$0	\$0	\$0
\$525.....	550	1	0	0
\$550.....	575	4	0	0
\$575.....	600	7	0	0
\$600.....	625	11	0	0
\$625.....	650	15	0	0
\$650.....	675	20	3	0
\$675.....	700	24	6	0
\$700.....	725	28	9	0
\$725.....	750	33	14	0
\$750.....	775	37	18	0
\$775.....	800	41	22	0
\$800.....	825	46	27	0
\$825.....	850	50	31	0
\$850.....	875	54	35	0
\$875.....	900	59	40	0
\$900.....	925	63	44	0
\$925.....	950	67	48	0
\$950.....	975	71	52	0
\$975.....	1,000	76	57	0
\$1,000.....	1,025	80	61	0
\$1,025.....	1,050	84	65	0
\$1,050.....	1,075	89	70	0
\$1,075.....	1,100	93	74	0
\$1,100.....	1,125	97	78	0
\$1,125.....	1,150	102	83	0
\$1,150.....	1,175	106	87	0
\$1,175.....	1,200	110	91	0
\$1,200.....	1,225	115	96	0
\$1,225.....	1,250	119	100	0
\$1,250.....	1,275	123	104	0
\$1,275.....	1,300	128	109	1
\$1,300.....	1,325	132	113	4
\$1,325.....	1,350	136	117	7
\$1,350.....	1,375	141	122	10
\$1,375.....	1,400	145	126	14
\$1,400.....	1,425	149	130	17
\$1,425.....	1,450	154	135	21
\$1,450.....	1,475	158	139	25
\$1,475.....	1,500	162	143	29
\$1,500.....	1,525	167	148	34
\$1,525.....	1,550	171	152	38
\$1,550.....	1,575	175	156	42
\$1,575.....	1,600	180	161	47
\$1,600.....	1,625	184	165	51

If the gross income is over—	But not over—	The tax shall be—		
		Single person (not head of a family)	Married person making separate return	(1) Married person whose spouse has no gross income or (2) Married per- son making joint return or (3) Head of family
\$1,625.....	\$1,650	\$188	\$169	\$55
\$1,650.....	1,675	193	174	60
\$1,675.....	1,700	197	178	64
\$1,700.....	1,725	201	182	68
\$1,725.....	1,750	206	187	73
\$1,750.....	1,775	210	191	77
\$1,775.....	1,800	214	195	81
\$1,800.....	1,825	218	199	85
\$1,825.....	1,850	223	204	90
\$1,850.....	1,875	227	208	94
\$1,875.....	1,900	231	212	98
\$1,900.....	1,925	236	217	103
\$1,925.....	1,950	240	221	107
\$1,950.....	1,975	244	225	111
\$1,975.....	2,000	249	230	116
\$2,000.....	2,025	253	234	120
\$2,025.....	2,050	257	238	124
\$2,050.....	2,075	262	243	129
\$2,075.....	2,100	266	247	133
\$2,100.....	2,125	270	251	137
\$2,125.....	2,150	275	256	142
\$2,150.....	2,175	279	260	146
\$2,175.....	2,200	283	264	150
\$2,200.....	2,225	288	269	155
\$2,225.....	2,250	292	273	159
\$2,250.....	2,275	296	277	163
\$2,275.....	2,300	301	282	168
\$2,300.....	2,325	305	286	172
\$2,325.....	2,350	309	290	176
\$2,350.....	2,375	314	295	181
\$2,375.....	2,400	318	299	185
\$2,400.....	2,425	322	303	189
\$2,425.....	2,450	327	308	194
\$2,450.....	2,475	331	312	198
\$2,475.....	2,500	335	316	202
\$2,500.....	2,525	340	321	207
\$2,525.....	2,550	344	325	211
\$2,550.....	2,575	348	329	215
\$2,575.....	2,600	353	334	220
\$2,600.....	2,625	357	338	224
\$2,625.....	2,650	361	342	228
\$2,650.....	2,675	366	347	233
\$2,675.....	2,700	371	351	237
\$2,700.....	2,725	376	355	241
\$2,725.....	2,750	381	359	245
\$2,750.....	2,775	386	364	250
\$2,775.....	2,800	391	369	254
\$2,800.....	2,825	396	374	258
\$2,825.....	2,850	401	379	263
\$2,850.....	2,875	406	384	267
\$2,875.....	2,900	411	389	271
\$2,900.....	2,925	416	394	276
\$2,925.....	2,950	421	399	280
\$2,950.....	2,975	426	404	284
\$2,975.....	3,000	431	409	289

In applying the above schedule to determine the tax of a taxpayer with one or more dependents there shall be subtracted from his gross income \$355 for each such dependent.

RULES FOR APPLICATION OF PARAGRAPH 65

(a) DEFINITIONS—

(1) Married person means a married person living with husband or wife on July 1, of the taxable year.

(2) Dependent means a person (other than husband or wife) dependent upon and receiving his chief support from the taxpayer on July 1, of the taxable year if on such date such dependent person is under 18 years of age or is incapable of self-support because mentally or physically defective, excluding as a dependent, in the case of a head of a family, one who would be excluded under paragraph 61 (b). A payment to a divorced or legally separated wife which is excluded from the taxpayer's gross income under paragraph 39 (e), or deducted from his gross income under paragraph 42, shall not be considered a payment to her for the support of any dependent.

(b) DETERMINATION OF STATUS.—The determination of whether a person is living with husband or wife, is a head of a family, or is a dependent, shall be made as of July 1 of the taxpayer's taxable year.

(c) SEPARATE RETURN OF HUSBAND AND WIFE.—If a husband and wife living together file separate returns, each shall be treated as a single person.

(d) MARRIED PERSONS NOT LIVING WITH HUSBAND OR WIFE.—An individual not a head of a family and not living with husband or wife on July 1, of the taxable year, shall be treated as a single person.

MANNER OF ELECTION

The election referred to in paragraph 65 shall be considered to have been made if the taxpayer files the return prescribed therein and such election shall be irrevocable. If the taxpayer for any taxable year has filed a return computing his tax without regard to paragraph 65, he may not thereafter elect for such year to compute his tax as provided therein.

CREDITS AGAINST TAX NOT ALLOWED

Foreign tax credit and credit for taxes withheld at source shall not apply with respect to the tax imposed by this paragraph.

CERTAIN TAXPAYERS NOT ELIGIBLE

The provisions of this paragraph shall not apply to a nonresident alien individual, to an estate or trust, to an individual filing a return for a period of less than 12 months or for any taxable year other than a calendar year, or to a married individual married and living with husband or wife at any time during the taxable year whose spouse files return and computes tax without regard to this paragraph.

SURTAX ON INDIVIDUALS

66. RATES OF SURTAX.—There shall be levied, collected, and paid for each taxable year upon the surtax net income of every individual the surtax shown in the following table:

If the surtax net income is:	The surtax shall be:
Not over \$2,000.....	13% of the surtax net income.
Over \$2,000 but not over \$4,000.....	\$260, plus 16% of excess over \$2,000.
Over \$4,000 but not over \$6,000.....	\$580, plus 20% of excess over \$4,000.
Over \$6,000 but not over \$8,000.....	\$980, plus 24% of excess over \$6,000.
Over \$8,000 but not over \$10,000.....	\$1,460, plus 28% of excess over \$8,000.
Over \$10,000 but not over \$12,000.....	\$2,020, plus 32% of excess over \$10,000.
Over \$12,000 but not over \$14,000.....	\$2,660, plus 36% of excess over \$12,000.
Over \$14,000 but not over \$16,000.....	\$3,380, plus 40% of excess over \$14,000.
Over \$16,000 but not over \$18,000.....	\$4,180, plus 43% of excess over \$16,000.
Over \$18,000 but not over \$20,000.....	\$5,040, plus 46% of excess over \$18,000.
Over \$20,000 but not over \$22,000.....	\$5,960, plus 49% of excess over \$20,000.
Over \$22,000 but not over \$24,000.....	\$6,940, plus 52% of excess over \$22,000.
Over \$24,000 but not over \$26,000.....	\$8,020, plus 55% of excess over \$24,000.
Over \$26,000 but not over \$28,000.....	\$9,200, plus 58% of excess over \$26,000.
Over \$28,000 but not over \$30,000.....	\$10,480, plus 61% of excess over \$28,000.
Over \$30,000 but not over \$32,000.....	\$11,860, plus 64% of excess over \$30,000.
Over \$32,000 but not over \$34,000.....	\$13,340, plus 67% of excess over \$32,000.
Over \$34,000 but not over \$36,000.....	\$14,920, plus 70% of excess over \$34,000.
Over \$36,000 but not over \$38,000.....	\$16,600, plus 73% of excess over \$36,000.
Over \$38,000 but not over \$40,000.....	\$18,380, plus 76% of excess over \$38,000.
Over \$40,000 but not over \$42,000.....	\$20,260, plus 79% of excess over \$40,000.
Over \$42,000 but not over \$44,000.....	\$22,240, plus 82% of excess over \$42,000.
Over \$44,000 but not over \$46,000.....	\$24,320, plus 85% of excess over \$44,000.
Over \$46,000 but not over \$48,000.....	\$26,500, plus 88% of excess over \$46,000.
Over \$48,000 but not over \$50,000.....	\$28,780, plus 91% of excess over \$48,000.
Over \$50,000 but not over \$52,000.....	\$31,160, plus 94% of excess over \$50,000.
Over \$52,000 but not over \$54,000.....	\$33,640, plus 97% of excess over \$52,000.
Over \$54,000 but not over \$56,000.....	\$36,220, plus 100% of excess over \$54,000.
Over \$56,000 but not over \$58,000.....	\$38,900, plus 103% of excess over \$56,000.
Over \$58,000 but not over \$60,000.....	\$41,680, plus 106% of excess over \$58,000.
Over \$60,000 but not over \$62,000.....	\$44,560, plus 109% of excess over \$60,000.
Over \$62,000 but not over \$64,000.....	\$47,540, plus 112% of excess over \$62,000.
Over \$64,000 but not over \$66,000.....	\$50,620, plus 115% of excess over \$64,000.
Over \$66,000 but not over \$68,000.....	\$53,800, plus 118% of excess over \$66,000.
Over \$68,000 but not over \$70,000.....	\$57,080, plus 121% of excess over \$68,000.
Over \$70,000 but not over \$72,000.....	\$60,460, plus 124% of excess over \$70,000.
Over \$72,000 but not over \$74,000.....	\$63,940, plus 127% of excess over \$72,000.
Over \$74,000 but not over \$76,000.....	\$67,520, plus 130% of excess over \$74,000.
Over \$76,000 but not over \$78,000.....	\$71,200, plus 133% of excess over \$76,000.
Over \$78,000 but not over \$80,000.....	\$74,980, plus 136% of excess over \$78,000.
Over \$80,000 but not over \$82,000.....	\$78,860, plus 139% of excess over \$80,000.
Over \$82,000 but not over \$84,000.....	\$82,840, plus 142% of excess over \$82,000.
Over \$84,000 but not over \$86,000.....	\$86,920, plus 145% of excess over \$84,000.
Over \$86,000 but not over \$88,000.....	\$91,100, plus 148% of excess over \$86,000.
Over \$88,000 but not over \$90,000.....	\$95,380, plus 151% of excess over \$88,000.
Over \$90,000 but not over \$92,000.....	\$99,760, plus 154% of excess over \$90,000.
Over \$92,000 but not over \$94,000.....	\$104,240, plus 157% of excess over \$92,000.
Over \$94,000 but not over \$96,000.....	\$108,820, plus 160% of excess over \$94,000.
Over \$96,000 but not over \$98,000.....	\$113,500, plus 163% of excess over \$96,000.
Over \$98,000 but not over \$100,000.....	\$118,280, plus 166% of excess over \$98,000.
Over \$100,000 but not over \$102,000.....	\$123,160, plus 169% of excess over \$100,000.
Over \$102,000 but not over \$104,000.....	\$128,140, plus 172% of excess over \$102,000.
Over \$104,000 but not over \$106,000.....	\$133,220, plus 175% of excess over \$104,000.
Over \$106,000 but not over \$108,000.....	\$138,400, plus 178% of excess over \$106,000.
Over \$108,000 but not over \$110,000.....	\$143,680, plus 181% of excess over \$108,000.
Over \$110,000 but not over \$112,000.....	\$149,060, plus 184% of excess over \$110,000.
Over \$112,000 but not over \$114,000.....	\$154,540, plus 187% of excess over \$112,000.
Over \$114,000 but not over \$116,000.....	\$160,120, plus 190% of excess over \$114,000.
Over \$116,000 but not over \$118,000.....	\$165,800, plus 193% of excess over \$116,000.
Over \$118,000 but not over \$120,000.....	\$171,580, plus 196% of excess over \$118,000.
Over \$120,000 but not over \$122,000.....	\$177,460, plus 199% of excess over \$120,000.
Over \$122,000 but not over \$124,000.....	\$183,440, plus 202% of excess over \$122,000.
Over \$124,000 but not over \$126,000.....	\$189,520, plus 205% of excess over \$124,000.
Over \$126,000 but not over \$128,000.....	\$195,700, plus 208% of excess over \$126,000.
Over \$128,000 but not over \$130,000.....	\$201,980, plus 211% of excess over \$128,000.
Over \$130,000 but not over \$132,000.....	\$208,360, plus 214% of excess over \$130,000.
Over \$132,000 but not over \$134,000.....	\$214,840, plus 217% of excess over \$132,000.
Over \$134,000 but not over \$136,000.....	\$221,420, plus 220% of excess over \$134,000.
Over \$136,000 but not over \$138,000.....	\$228,100, plus 223% of excess over \$136,000.
Over \$138,000 but not over \$140,000.....	\$234,880, plus 226% of excess over \$138,000.
Over \$140,000 but not over \$142,000.....	\$241,760, plus 229% of excess over \$140,000.
Over \$142,000 but not over \$144,000.....	\$248,740, plus 232% of excess over \$142,000.
Over \$144,000 but not over \$146,000.....	\$255,820, plus 235% of excess over \$144,000.
Over \$146,000 but not over \$148,000.....	\$262,900, plus 238% of excess over \$146,000.
Over \$148,000 but not over \$150,000.....	\$270,080, plus 241% of excess over \$148,000.
Over \$150,000 but not over \$152,000.....	\$277,360, plus 244% of excess over \$150,000.
Over \$152,000 but not over \$154,000.....	\$284,740, plus 247% of excess over \$152,000.
Over \$154,000 but not over \$156,000.....	\$292,220, plus 250% of excess over \$154,000.
Over \$156,000 but not over \$158,000.....	\$299,800, plus 253% of excess over \$156,000.
Over \$158,000 but not over \$160,000.....	\$307,480, plus 256% of excess over \$158,000.
Over \$160,000 but not over \$162,000.....	\$315,260, plus 259% of excess over \$160,000.
Over \$162,000 but not over \$164,000.....	\$323,140, plus 262% of excess over \$162,000.
Over \$164,000 but not over \$166,000.....	\$331,120, plus 265% of excess over \$164,000.
Over \$166,000 but not over \$168,000.....	\$339,200, plus 268% of excess over \$166,000.
Over \$168,000 but not over \$170,000.....	\$347,380, plus 271% of excess over \$168,000.
Over \$170,000 but not over \$172,000.....	\$355,660, plus 274% of excess over \$170,000.
Over \$172,000 but not over \$174,000.....	\$364,040, plus 277% of excess over \$172,000.
Over \$174,000 but not over \$176,000.....	\$372,520, plus 280% of excess over \$174,000.
Over \$176,000 but not over \$178,000.....	\$381,100, plus 283% of excess over \$176,000.
Over \$178,000 but not over \$180,000.....	\$389,780, plus 286% of excess over \$178,000.
Over \$180,000 but not over \$182,000.....	\$398,560, plus 289% of excess over \$180,000.
Over \$182,000 but not over \$184,000.....	\$407,440, plus 292% of excess over \$182,000.
Over \$184,000 but not over \$186,000.....	\$416,420, plus 295% of excess over \$184,000.
Over \$186,000 but not over \$188,000.....	\$425,500, plus 298% of excess over \$186,000.
Over \$188,000 but not over \$190,000.....	\$434,680, plus 301% of excess over \$188,000.
Over \$190,000 but not over \$192,000.....	\$443,960, plus 304% of excess over \$190,000.
Over \$192,000 but not over \$194,000.....	\$453,340, plus 307% of excess over \$192,000.
Over \$194,000 but not over \$196,000.....	\$462,820, plus 310% of excess over \$194,000.
Over \$196,000 but not over \$198,000.....	\$472,400, plus 313% of excess over \$196,000.
Over \$198,000 but not over \$200,000.....	\$482,080, plus 316% of excess over \$198,000.
Over \$200,000.....	\$491,860, plus 319% of excess over \$200,000.

CREDITS AGAINST TAX

67. The amount of income, war profits, and excess-profits taxes imposed by foreign countries or possessions of the United States shall be allowed as a credit against the regular income tax, in the case of an individual, to the following extent:

- (a) If the taxpayer chooses to have the benefits of such credits, the income tax shall be credited with, in the case of a citizen of the United States, the amount of any income, war profits, and excess-profits taxes paid or accrued during the taxable year to any foreign country or to any possession of the United States; and, in the case of a

resident of the United States the amount of any such taxes paid or accrued during the taxable year to any possession of the United States. The taxpayer's choice to take credit under this paragraph instead of claiming a deduction for such taxes under paragraph 44 (f) may be made or changed at any time prior to the expiration of the period prescribed for making a claim for credit or refund of his regular income tax.

- (6) The amount of the credit taken, hereunder, shall be subject, in the case of an individual, to each of the following limitations:
- (1) The amount of the credit in respect of the tax paid or accrued to any country shall not exceed the same proportion of the tax against which such credit is taken, which the taxpayer's net income from sources within such country bears to his entire net income for the same taxable year; and
 - (2) The total amount of the credit shall not exceed the same proportion of the tax against which such credit is taken, which the taxpayer's net income from sources without the United States bears to his entire net income for the same taxable year.

PAYMENT OF TAX

68. *Time.*—In general, the regular income tax is to be paid on or before the 15th day of March following the close of the calendar year, or, if the return is made on the basis of the fiscal year, then on or before the 15th day of the third month following the close of the fiscal year. The due date for any income-tax return and for any payment (including any installment payment) of income tax is postponed in the case of any individual in the military or naval forces of the United States who, at the time the return or payment would otherwise become due, is serving on sea duty or outside the continental United States. The new due date, in the case of any such postponement, is the 15th day of the third month following the month in which the individual ceases (except by reason of death or incompetency) to be a member of the military or naval forces of the United States serving on sea duty or outside the continental United States, unless prior to the expiration of such 15th day he is a prisoner of war of, or is detained by, any foreign government with which the United States is at war, or is beleaguered or besieged by enemy forces, or is again a member of the military or naval forces serving on sea duty or outside the continental United States.

The due date is likewise postponed in the case of any individual in the military or naval forces of the United States or any civilian officer or employee of any executive department, independent establishment, or agency (including corporations) in the executive branch of the Federal Government who, at the time the return or payment would otherwise become due, is a prisoner of war of, or is otherwise detained by, any foreign government with which the United States is at war, or is beleaguered or besieged by enemy forces.

The new due date, if it has not previously occurred pursuant to the provisions above, is the earlier of the two following dates:

(1) The 15th day of the third month following the month in which an executor, administrator, or conservator of the estate of the taxpayer is appointed; or

(2) The 15th day of the third month following the month in which the present war with Germany, Italy, and Japan is terminated, as proclaimed by the President.

69. *Installments.*—The taxpayer may pay the tax in four equal installments, in which case the first installment shall be paid on the date prescribed for the payment of the tax by the taxpayer, the second installment shall be paid on the 15th day of the third month, the third installment on the 15th day of the sixth month, and the fourth installment on the 15th day of the ninth month, after such date. If any installment is not paid on or before the date fixed for its payment, the whole amount of the tax unpaid shall be paid upon notice and demand from the collector.

70. *Extension of time for payment.*—

(a) At the request of the taxpayer, the Commissioner may extend the time for payment of the tax, or any installment thereof, for a period not exceeding 6 months from the date prescribed for the payment of the tax or any installment thereof. In such case the amount in respect of which the extension is granted shall be paid on or before the date of the expiration of the period of the extension.

(b) If the time for payment of the tax, or any installment thereof, is extended, there shall be collected as a part of such amount interest thereon at the rate of 6 per centum per annum from the date when such payment should have been made if no extension had been granted, until paid.

71. *Voluntary advance payment.*—The tax, or any installment thereof, may be paid, at the election of the taxpayer, prior to the date prescribed for its payment.

72. *Fractional parts of cent.*—In the payment of the tax, a fractional part of a cent shall be disregarded unless it amounts to one-half cent or more, in which case it shall be increased to 1 cent.

IMPORTANT

73. Within the limits of this information circular, it is impossible to anticipate questions that may arise in the minds of taxpayers.

74. It is suggested that income-tax returns be prepared as soon as possible after January 1, 1943, to permit of ample time for the submission of requests for additional information by the individual taxpayer direct to officials of the Bureau of Internal Revenue.

SUGGESTED

75. It is suggested that the taxpayer read the following "check-off" list before mailing his income-tax return:

(a) Use proper blank form (par. 16) and mail to "Collector of Internal Revenue." Be sure return is signed, and that remittance is enclosed with the return.

- (b) Payments of \$500 or more to other persons. Report to be made to the "Commissioner of Internal Revenue, Bureau of Internal Revenue, Washington, D. C." (par. 21).
- (c) Unless the due date for filing a return is deferred in accordance with paragraph 68, or the time for filing is extended in accordance with paragraph 70, the income-tax return must be received in the office of the "Collector of Internal Revenue" on or before March 15th following the close of the taxable year or the 15th day of the third month following the close of a fiscal year.

THE VICTORY TAX

76. The Victory Tax is an additional tax apart from the income tax. It is imposed at the rate of 5 percentum upon all Victory Tax net income in excess of \$624 received during the taxable year by every individual, other than nonresident aliens who are not engaged in a trade or business in the United States, from salaries and other compensation for personal services, dividends, interest, rents and royalties, annuities, net profits from business or professions or income from partnerships, fiduciary income and other income includible in gross income, except capital gains and certain interest on United States obligations, and compensation for injuries or sickness included in regular gross income because of medical expenses allowed as deductions in prior years.

77. The Victory Tax is not applicable with respect to income received during the calendar year 1942. It is applicable only with respect to taxable years beginning after December 31, 1942, and will expire after the date of cessation of hostilities in the present war.

WITHHOLDING TAX

78. To aid in the collection of the tax, every employer is required to withhold from each payment of salaries and wages made after December 31, 1942, 5 per centum thereof in excess of \$12 per week, except that the deduction shall not be withheld from, among others:

- (a) Remuneration paid to members of the military and naval forces of the United States, *including pensions and retired pay.*
- (b) Payments for agricultural labor, casual labor, and domestic services.
- (c) Payments for services performed as an employee while outside the United States, which includes only the States, the territories of Alaska and Hawaii, and the District of Columbia.

79. The withholding employer is required to file a return and pay to the Government each quarter, the taxes withheld.

VICTORY TAX RETURNS

80. It is provided that every individual having a gross income in excess of \$624 for the taxable year shall make, under regulations prescribed by the Commissioner of Internal Revenue, a return stating specifically the items of his gross income and the deductions and credits allowed by the Victory Tax law.

81. The Victory Tax will be computed on the regular income tax return. Against the "Victory Tax" shown to be due, the taxpayer will be allowed credit for the amount withheld at the source. The taxpayer will also be allowed a post-war credit against the tax. Such credit in the case of single persons would be equal to 25 per centum of the tax or \$500, whichever is smaller. In the case of the head of a family or a married person living with husband or wife, the credit will be 40 per centum of the tax or \$1,000, whichever is smaller. A similar credit for each dependent will be allowed at 2 per centum of the tax or \$100, whichever is smaller.

82. This post-war credit may be absorbed in the current return by

- (a) Life-insurance premiums paid during the year on life insurance outstanding on September 1, 1942.
- (b) Payments on debts contracted prior to September 1, 1942.
- (c) Amounts paid for the purchase of United States obligations specified by the Secretary of the Treasury.

83. Accordingly, the amount withheld at the source, plus, at the election of the taxpayer, amounts absorbed against the post-war credit during the calendar year under subparagraphs (a), (b), and (c) above, will be credited first against the "Victory Tax," and any excess of such credits will be credited against the regular income tax.

IMPORTANT TO NOTE

84.

- (a) The "Victory Tax" is an additional tax, apart from the income tax.
- (b) It is not applicable to income for calendar year 1942.
- (c) First "Victory Tax" return is due to be filed not later than March 15, 1944, subject of course, to the same extensions applicable to regular income tax returns.
- (d) Pay to members of military and naval forces of United States is not subject to the withholding tax although it is subject to the Victory tax.

W. B. YOUNG,
Rear Admiral, S. C., U. S. Navy,
Paymaster General of the Navy.

MEMORANDUM

TO: Secretary Morgenthau
FROM: Mr. Sullivan JES
RE: Tax Status of Members of the Armed Forces

Noncommissioned military and naval personnel receive an additional allowance of \$250, if single, and \$300, if married or the head of a family, thereby increasing the personal exemption to \$750 and \$1,500, respectively. The allowance is also granted for purposes of the Victory tax, which is not subject to withholding at the source.

Allowances for quarters, subsistence, and uniforms, as well as that part of the allowance for dependents contributed by the Government, are excluded from gross income.

If ability to pay income taxes is materially impaired by reason of military service, collection may be deferred for six months after the termination of service. No interest or penalties accrue during the period of deferment. Assignment to sea duty or duty outside continental United States extends the time for filing return and making payment of income taxes until approximately three months after return.

If a person in military service dies, all current and deferred income taxes become liabilities of the estate.

Attached is a more detailed analysis.

Attachment

I. Allowances for Persons in the Military Service.

Section 22 (b)(13) of the Internal Revenue Code, added by the Revenue Act of 1942, excludes from gross income so much of the compensation for active service during the present war received by noncommissioned military or naval personnel as does not exceed \$250, in the case of a single person, and \$300, in the case of a married person or head of a family. The effect is to allow to members of the armed forces the former exemptions of \$750, if single, and \$1,500, if married or the head of a family. The family status and status in the armed forces is determined at the end of the taxable year. The special allowance is applicable to the Victory tax, which is not withheld at the source as in the case of wages and salaries of civilians.

Amounts received by officers and enlisted personnel as commutation of quarters, for subsistence, or for uniforms are excluded from gross income, but no deduction is allowed for amounts paid for uniforms.

In the case of allowances provided for dependents of members of the armed forces, part of the allowance is deducted from the pay of the noncommissioned personnel and the balance is contributed by the Government. The latter is considered a gift by the Government rather than compensation for services and is not taxable to either the serviceman or his dependents.

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The part that is deducted from the pay, however, is taxable income of the person in the service. Amounts received as compensation for disability incurred in the military service are exempt from taxation, as also are pensions paid to widows, but retirement pay is regarded as compensation for services previously rendered and is subject to tax.

II. Deferment of Tax Liabilities of Persons in the Military Service.

The Soldiers' and Sailors' Civil Relief Act of 1940, as amended, defers the collection of income taxes from a person in the military service for a period of not more than six months after the termination of service, if his ability to pay the taxes is materially impaired by reason of such service. No interest or penalties accrue during the period of deferment. Relief may be had with respect to taxes which fall due prior to the period of military service, as well as taxes which become due during such service. Although the Act provides for deferment for not longer than six months, at any time during his period of military service or within six months thereafter a person may apply to any court for an additional stay of enforcement for a period not in excess of the period of military service.

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If a person is assigned to sea duty or to service outside the continental United States -- the States of the Union and the District of Columbia -- the time for filing his income tax return, or for paying taxes, for any taxable year beginning after December 31, 1940, does not become due until the fifteenth day of the third month following the month of his return, or until an equal time after termination of the war, whichever is the earlier. (Public Law 490, 77th Cong., 2d Sess., Approved March 7, 1942)

The time for performing certain other acts under the internal revenue laws, such as filing a claim for credit or refund of any tax, bringing a suit upon any such claim for credit or refund, or filing a petition with the Tax Court, may be extended by the Commissioner of Internal Revenue under regulations prescribed by him with the approval of the Secretary. (I.R.C., section 3804) If the person in the military service is assigned to duty outside the Americas -- North, Central, and South America (including the West Indies but not Greenland), and the Hawaiian Islands -- and if such person is outside the Americas continuously for a period in excess of ninety days, then the statutes of limitations with respect to these additional acts are suspended as a matter of right.

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In the case of death or incompetency of a person in military service outside the Americas or the continental United States, such taxes become due on the fifteenth day of the third month following the month in which the executor, administrator, or conservator of the estate of such person is appointed. Likewise, if payment of taxes has been deferred because of impairment of ability to pay resulting from the military service (regardless of where the service is rendered), the time for payment is a date no later than six months after death. The deferred taxes, as well as the tax for the year in which death occurs, become liabilities of the estate.

III. Definition of the Term "Military or Naval Forces of the United States."

As used in the Internal Revenue Code, the term "military or naval forces of the United States" includes "the Marine Corps, the Coast Guard, the Army Nurse Corps, Female, the Women's Auxiliary Corps, the Navy Nurse Corps, Female, and the Women's Reserve branch of the Naval Reserve." This definition is being construed to include the women's auxiliaries of all branches of the service. The Coast and Geodetic Survey and the Public Health Service are added for

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purposes of Public Law 490, but the women's auxiliaries are not included. Relief under the Soldiers' and Sailors' Civil Relief Act is expressly limited to members of the Army, Navy, Marine Corps, Coast Guard, Women's Army Auxiliary Corps, and certain officers of the Public Health Service.

TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE January 11, 1943

TO Mr. Gaston
FROM Mr. Schwarz

Leon Henderson's sponsorship of Rolf Nugent's proposal for current installment buying for post-war delivery was announced at a press conference at OPA at noon last Saturday, when the attached "release" was handed out. Prior to the conference the Secretary's views on the plan were called to the attention of the Office of War Information and the Information Division of OPA. As a result, Leon made it clear that the proposal was just that and had not been given any endorsements, that he would submit it to the President if the President wished to see it. The majority of the stories growing out of the press conference called attention to the Treasury's opposition to the proposal.

OWI controls information by OPA and other war agencies. That office approved and scheduled the press conference and gave its approval to the issuance of the release.

A Plan
for
INSTALMENT SELLING FOR POST-WAR DELIVERY

by

Rolf Nugent, Special Advisor
Office of Price Administration

Revised
December, 1942

Note: In the development of the plan presented in this memorandum the writer has had the helpful advice and assistance of Dr. Bonnar Brown, of the Board of Governors of the Federal Reserve System, of Mr. Abraham Friedman of the New York Bar, and of Messrs. Wroe Alderson and F. B. Hubachek of the Office of Price Administration.

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FOREWORD

Whatever its advantages or disadvantages in time of peace, the American practice of credit buying has real usefulness in time of war. Consumer credit lends itself readily to service in the progressive battle that must be fought against war-time inflation.

The development of our full military power was bound to produce distortions in our civilian economy. Government expenditures for armaments substantially increase the national income and total consumer purchasing power. On the other hand, the diversion of materials and labor to war production and the recruitment of manpower for the military forces limit the production of goods which consumers want to buy. Three stages in the transition to a war economy can be recognized. At each of these stages, there has been the possibility of using consumer credit as the means of easing the impact on the civilian economy.

The first stage is one in which there are shortages of specific materials, skills and productive equipment, while supplies in other fields remain abundant. At this stage, appropriate action in the consumer credit field would be to tighten credit terms for automobiles, refrigerators, oil burners, washing machines, and similar goods that absorb metals, skills and tools needed for armaments production. The purpose would be to reduce demand for these specific goods without preventing a continuous expansion of the national income that would draw idle productive factors into use. Consequently, an increase in down-payments for selected goods should be the primary restriction.

The second stage occurs when the area of shortages has expanded, when incomes and demand are increasing more rapidly than production, and when the general price level has begun to rise. At this stage more general restraints

upon consumer credit are called for. Stringent down-payment requirements should be applied over the broadest practicable field; the maturity of instalment contracts should be shortened generally; and restraints should be imposed upon charge-account credits, and so far as possible upon accommodation loans. In other words, the general deflationary influence of a rapid liquidation of consumer credit should be brought to bear upon the rising national income.

A third stage can be recognized when important consumers' durable goods industries have been completely converted to armaments production and when the goods formerly produced by these industries are no longer available in the market. Under these circumstances it would be appropriate to throw the instalment credit system into reverse--to sell goods on the instalment plan for post-war delivery. In this way, the deflationary effects of instalment payments could be continued after previous credit commitments have been liquidated.

We entered the first of these three stages in the late fall of 1940. By summer of the following year, the second stage had arrived.

Action on the consumer credit front came belatedly at the beginning of September 1941 with the promulgation of Regulation W by the Federal Reserve Board. Very properly, the initial regulation was directed primarily toward the tightening of down-payments, which would reduce demand for specific goods, and secondarily at the limitation of maturities, which would result in a general liquidation of consumer credit. Subsequent amendments have, with equal propriety, been directed toward broadening the scope of the down-payment restrictions and reducing maturities for instalment and charge account credits on a broad front.

The effects have been substantial; and of tremendous importance to the

Office of Price Administration. Demand for goods which competed with armaments for scarce materials and skills was reduced precipitately. The liquidation of consumer credit, induced in part by restrictions of the regulation and in part by limitations on the supply of goods commonly sold on credit, has provided a new and powerful deflationary force.

We are now well into the third stage. Production of passenger automobiles--next to residential housing the most important of all consumers' durable goods--was discontinued in February 1942 and the overwhelming majority of our citizenry has been excluded from the automobile market by selective rationing. Subsequently, civilian production of a large number of other consumers' durables has been stopped. For some of these goods, inventories have been reserved for specific purposes. For others, inventories have already been exhausted or are rapidly approaching exhaustion.

Both from a psychological and from an economic standpoint, the time is ripe for appropriate action on the consumer credit front.

It is the purpose of this memorandum to show how goods could be sold on instalment contracts calling for delivery in the post-war period and how such sales would aid in the fight against inflation.

THE PLAN IN BRIEF

The plan presented here is designed primarily to divert consumers' purchasing power from the market for current goods and thereby to relieve the inflationary pressure on the price level. It would, however, have a number of important by-products: it would provide additional funds for financing the war; it would build up a back-log of purchasing power that would facilitate the transition to a peace-time economy; it would provide the means of bringing post-war demand into line with supply in markets that are certain to be badly out of balance; it would provide some measure of current relief for enterprises that have been or will be hurt by the discontinuance of production of the goods which they sell; and it would preserve at least a rudimentary selling and financing structure as the basis for rapid post-war expansion.

Three cardinal principles have been followed in the development of the plan. First, the customary machinery of instalment selling has been relied upon so far as possible in its operation. This serves the dual purpose of enlisting the drive and ingenuity of private salesmanship in the selling and collection effort and of avoiding expansion of the federal bureaucracy. Second, payments on goods for post-war delivery have been related so far as possible to expenditures for merchandise, and characteristics that would link them to savings have been avoided. This is of prime importance because nothing would be gained on the anti-inflation front if consumers merely shifted their savings from purchases of war bonds or from other savings media

into post-war-delivery purchases. Finally, it has been the policy to avoid distortion of the normal machinery of distribution. The plan contemplates a shift to free market conditions as quickly as possible after the war and it attempts to preserve the position of various competitive elements in the distributive process.

It seems doubtful that many persons would be willing to buy, for deferred delivery, goods that can be bought for current delivery. Hence an essential requirement in the selection of goods to be sold under the plan is their unavailability at present. Many types of consumers' durable goods and even some services meet this requirement and would lend themselves to post-war-delivery sale. However, the plan is most readily adaptable to the sale of relatively high-priced goods that are presently in common use and are produced by comparatively small numbers of substantial manufacturers. For this reason it is proposed that the plan be applied at the outset only to automobiles, refrigerators, pianos, oil burners and automatic stokers. Later, the list should be expanded to cover other goods and services, where careful study and consultation with the trades concerned indicate the adaptability of the plan to their sale.

Because it is impossible to predict accurately the level of production costs after the war, no attempt would be made to establish at the time of the instalment sale the prices at which goods would be delivered. The purchaser would acquire a certificate which would be accepted in payment of the post-war purchase price of a specified article. Certificates would be issued in various denominations, identified with price-classes of goods, and they could be applied toward the purchase of any make or model in the

specified price-class. Manufacturers would probably build their products so far as possible to meet the market established by certificate values. But if post-war prices differed from the value of certificates, differences could be readily adjusted in cash or in finance company credits.

Certificates would be sold only on instalment terms in order to encourage payment out of current income. Payment schedules should be related to certificate values, ranging from 12 monthly payments for \$100 certificates to 25 monthly payments for \$2,000 certificates. In order to equalize the situation of civilians and persons in the armed forces, the latter would be permitted to buy on longer payment schedules.

To prevent speculators from acquiring claims to large quantities of goods for purposes of resale, the number of certificates that may be purchased by any one person would be limited. Prior to the date of their validation for the delivery of goods, certificates would be non-transferable except under a limited number of circumstances such as inheritance or bequest, executions in satisfaction of judgment, and distribution of assets in bankruptcy. Following their validation, certificates would be fully transferable.

Consumers would be offered two incentives for purchasing post-war-delivery certificates: a prior claim to the goods subject to sale, and a discount from the established post-war price.

Priority numbers would be determined by the month in which the purchaser entered his instalment contract, with adjustments for delinquency in making payments. Thus, if the purchaser entered his contract during the first month of operation of the plan and made his payments promptly, he would be assigned priority number 1; if the purchase was initiated during the second month, he would be assigned priority number 2; etc. If he were

delinquent beyond a reasonable grace period, his priority number would be increased in relation to the degree of delinquency.

The price discount would be accomplished by giving the post-war-delivery certificate a "merchandise" value greater than its purchase price. It is proposed that this differential be fixed at 10%. Thus, a certificate for which the purchaser pays \$200 would be worth \$220 in exchange for post-war goods and a certificate costing \$1000 would be worth \$1100 in exchange for goods. The differential would be made up at the time of delivery by the sacrifice of part of the normal gross profit by the dealer who completes the sale and by a rebate to that dealer by the manufacturer whose goods are delivered.

Certificate sales would be made by established dealer organizations -- by automobile sales agencies, by refrigerator and piano dealers and by heating equipment contractors. The purchaser would sign a post-war-delivery contract and make a modest down-payment, varying with the denomination of the certificate, which the dealer would keep as his initial sales commission. The dealer would then send the contract to a sales finance agency that had been authorized by a Federal Reserve Bank to supervise collections and do the bookkeeping.

Upon receipt of the post-war-delivery contract, the sales finance agency would issue a payment book to the purchaser and open a ledger account for him. These agencies would be responsible for recording payments, for transmitting funds to the Federal Reserve Banks, for sending delinquent notices, for referring defaulted contracts back to the dealer, for computing delinquency charges, and for assigning priority numbers.

Instalment payments would be made, however, to a different set of agencies. The agencies that accept payments from purchasers should be

readily available to all purchasers, equipped to accept money payments, financially responsible, and without an interest either in selling the purchaser goods or in lending him money. These local collection agencies might include the telephone, gas and electric companies -- in which case instalments could be paid with bills for services -- the telegraph companies and the Post Office. They would accept and receipt for payments, tear from payment books coupons that identify the purchaser, the sales finance agency, and the amount of the payment, and forward the coupons with remittances to the appropriate sales finance agencies, which would use the coupons to post its ledger accounts.

The sales finance agency would send the funds on to the Federal Reserve Bank or branch of the district in which its office is situated. The Bank would credit its receipts to a special post-war-delivery account in the name of the United States Treasury.

Both the sales finance agency and the local collection agency would receive modest commissions on payments handled by them to compensate them for their work. These commissions would be subtracted from collections in passing on the proceeds. The dealer would also receive a further sales commission upon completion of the purchaser's payments. Sales and collection commissions would be subtracted directly from the payments made by the purchaser; but they would be covered, when the certificate becomes valid for the delivery of goods, by the payment which the Treasury would make for the use of the purchaser's money. In this way each certificate would have three different values: (1) a withdrawal value equal to the amount paid in by the purchaser, less sales and collection commissions and delinquency charges;

(2) a cash value at maturity equal to the amount paid in by the purchaser, exclusive of delinquency charges; and (3) a merchandise value at maturity equal to 110 per cent of the cash value.

In addition to its regular commission on funds collected, the sales finance agency would also receive a more substantial fraction of delinquency charges to compensate for the work of sending delinquent notices and computing charges. The remainder should be divided between the Treasury, to compensate for the loss of the use of funds during the period of delinquency, and the Federal Reserve Bank.

When the purchaser has completed his payments and charges for delinquency have been collected, the sales finance agency would pay the dealer his final commission, assign a priority number to the purchaser's account and send it to the Federal Reserve Bank for audit. The Bank would examine the computation of charges and the assignment of priority and inspect its records to prevent the purchaser from acquiring more certificates than he is entitled to. If the record was satisfactory, it would then issue a registered, paid-up certificate bearing the appropriate priority number and send it to the purchaser.

The calling of priority numbers when production is resumed would be the responsibility of the Federal Reserve Board. As soon as dealers have received satisfactory inventories, priority numbers would be called as rapidly as additional goods are produced, unless there should be a tendency to expand productive capacity beyond the reasonable limits of normal demand. The Board should also have the power to grant special priorities where this was in the public interest.

Paid-up certificates, when countersigned by purchasers and exchanged for goods, would be deposited to dealers' bank accounts at their cash values and they would be honored by the Federal Reserve Banks from funds made available by the Treasury. Control of the distribution of goods would be exercised by the upstream flow of coupons attached to paid-up certificates, which would entitle the dealer both to a rebate from the manufacturer and to the shipment of another article to replace the one delivered to the certificate holder.

II.

OBJECTIVES OF THE PLAN

During the past several years between 10 and 12% of all consumer expenditures have been devoted to the purchase of consumers' durable goods, other than houses.

In 1941 expenditures for such goods approached 10 billion dollars, in spite of shortages of materials and limitations on production, and in spite of credit restrictions and excise taxes imposed during the latter part of the year to dampen demand. Almost three-fifths of this sum was spent for automobiles and for automobile parts and accessories, almost one-fifth was spent for household appliances and fixtures. The remainder went for home furnishings, pleasure boats, watches and jewelry, cameras, etc. Automobiles, refrigerators, pianos and automatic furnaces--the goods which would be most readily adaptable to post-war-delivery sale--accounted for more than 60% of the total volume of expenditures for consumers' durable goods, and perhaps as much as 90% of the total volume of expenditures for goods which have since disappeared, or are currently disappearing, from the open market.

Inflationary Significance of Conversion of Consumers' Goods Industries

War requirements have cut heavily into the industries that supplied these goods. Some of these industries, such as those manufacturing automobiles, refrigerators, washing machines, suction cleaners, and radios have been completely converted to war production. Others are in the process of conversion; and still others have been stopped or substantially curtailed

by the scarcity of essential materials. Of the whole list of consumers' durable goods only wooden furniture and certain types of housefurnishings have been relatively unaffected by the impact of military requirements. The volume of consumers' durable goods currently reaching the market is probably less than one-third the volume that came into the market a year ago. And it can be expected to decline still further in subsequent months.

Under normal circumstances, a decline in production of consumers' durable goods would be accompanied by a decline in the incomes of the factory workers, raw material suppliers, managers, landlords, and stockholders who depend upon such production for their livelihood. Thus, a decline in the supply of consumers' goods would be roughly compensated by a decline in the incomes available for expenditure on such goods. But at present most consumers' goods industries that have discontinued production are engaged in the manufacture of military equipment. Consequently, there has been no decline in incomes to compensate for the decline in the quantity of goods that are available to consumers. In fact, as the national income figures clearly show, money incomes have risen progressively throughout the period when production of many types of consumers' durable goods was being discontinued.

This situation provides one of the essential elements of inflation. Inevitably inflation has its origins either in a restriction of production of consumers' goods relative to the flow of money incomes or in an increase in

the flow of money incomes relative to production of consumers' goods.

But there is another essential ingredient: there must be a capacity and a will to spend the excess income. It is therefore of crucial importance to ask what consumers will do with the part of their incomes which they formerly spent for goods that are now no longer available.

This question brings us at the outset to an observation concerning the nature of expenditures for consumers' durable goods that is of prime importance to an understanding of the current problem.

Consumers' durable goods are family capital goods; and within the limits of the crude bookkeeping systems used by most families, purchases of such goods are treated in much the same way as the capital goods of business and industrial enterprises. And for much the same reasons, because neither the capital outlays of business enterprises nor the capital expenditures of consumers are properly chargeable to the immediate income period in which they are made.

Business enterprises charge their capital expenditures to capital accounts which are gradually reduced by depreciation charges against current income. The great majority of consumers buy their capital goods on the installment plan, which is merely another way of amortizing an initial capital expenditure by periodic payments out of income. From the standpoint of the market, such purchases take place when the goods are delivered. But from the standpoint of the individual purchaser, the purchase takes place over an extended period of time in the form of a series of payments from income, each of which is looked upon as an expenditure for the use and eventual

ownership of the article.

For this reason part of the current income of the American people is still being diverted to the purchase of consumers' durable goods, the production and sale of which have been stopped. Instalment payments will continue for some time to absorb at least part of the income that would otherwise be available for current purchases. But this drain will gradually dwindle in volume. As individual instalment contracts are completed, additional purchasing power will be freed for other purposes.

The deflationary effects of the liquidation of instalment sales contracts have been supplemented and reinforced by restrictions designed to compel partial liquidation of personal loans and charge accounts. However, because of the greater magnitude of instalment sales credits as compared with instalment loan and charge-account credits, the drain upon incomes resulting from the liquidation of consumer credit as a whole will certainly dwindle even if credit restrictions are broadened and intensified to their fullest practicable limit.

Ways of diverting surplus purchasing power

The purchasing power that will be freed by the gradual completion of the liquidation of previous instalment purchases could conceivably be captured and diverted from the market for goods in a variety of ways.

First, it might be taxed out of existence. The Revenue Act which has just been passed by the Congress provides for an impressive increase in taxes, and personal and corporate taxes applicable to 1942 incomes will be

the highest in our history with respect both to rates and to total yield. Yet the increase in tax revenues during the coming year will fall far short of the increase in military expenditures. The Director of the Budget estimated on October 7 that in spite of the increase in taxes, the Federal government deficit will increase from 21.7 billion dollars in the fiscal year ending June 30, 1942, to 63.1 billion dollars for the fiscal year ending June 30, 1943. These rising deficit expenditures will be a force for expanding the national income and increasing the volume of funds available for expenditure by consumers. Consequently the present tax program, however burdensome, cannot be expected to ease the inflationary pressure created by the disappearance of important consumers' durable goods.

Second, this excess purchasing power might be saved. There can be little doubt that the stoppage of production of most consumers' durable goods will give a considerable impetus to saving. Through tradition or trial and error experience, families generally accustom themselves to a crude allocation of their incomes between savings, food, housing, clothing, medical care, recreation, and consumers' durable goods. When funds cannot be spent for the latter goods, there will be resistance to increasing expenditures for other categories of goods. Consequently, savings can be expected to increase.

This resistance to an increase in expenditures for other goods has its limits, however, and it is only in the short run that a considerable part of the funds formerly spent for consumers' durables is likely to be saved. We know that a given savings margin between income and expenditures--a margin

which varies from income class to income class and from family to family--stands very high in the hierarchy of family values. When incomes are reduced, this margin will be preserved at the expense of most other budget items. But at a given income level the subjective value of additions to these established savings margins drops off very fast. Hence, with the passage of time, larger and larger proportions of the funds which can no longer be spent for consumers' durable goods are likely to be spent to satisfy other wants.

Third, we could continue to sell consumers' durable goods for delivery in the post-war period. Because it preserves the existing expenditure pattern, this would be the easiest way of preventing funds customarily spent for consumers' durable goods from being shifted to other markets. Funds that have customarily been spent for purchases of consumers' durable goods would continue to be spent for such goods, but delivery would be postponed. Since these funds would command no goods until the end of the war, they would in reality constitute savings. Yet there is every reason to believe that claims on post-war production could be offered in such a way that payments on them would be treated almost universally as current expenditures.

Expenditure vs. saving for post-war delivery

It is of substantial importance to the usefulness of installment selling for post-war delivery as an anti-inflationary weapon that consumers be encouraged to treat their installment payments as expenditures for goods

rather than as savings. To the extent that this is accomplished, the resistance to an increase in savings will be avoided and the diversion of purchasing power from the market for current goods will be substantially increased.

Installment selling for post-war delivery will produce deflationary effects only if it decreases the propensity to consume, or, in other words, if it reduces the proportion of the national income that would otherwise be spent for current consumers' goods and services. The flow of incomes is sustained by expenditures that lead to the production of additional goods. When consumers spend their incomes for current goods, their expenditures in turn create incomes for those who sell and deliver the goods and for those who participate in the production and shipment of additional goods to replace the goods that were sold. When consumers withhold part of their incomes from the market for current goods, the transmission of incomes is interrupted and the flow declines.

Even if installment payments for post-war delivery were treated as savings by all purchasers, some reduction in the total volume of expenditures that would come into the market could be confidently expected. The offer of a new kind of savings with an unusual appeal would, of itself, lead to some expansion of overall savings. In addition, there would be a particularly strong pressure on certain classes of consumers to increase their savings. Many persons whose entire savings take the form of fixed payments to pension

funds, for annuity premiums, for building and loan shares, or for debt retirement, would undoubtedly make instalment payments without reducing the flow of funds into these fixed savings programs. Many others, who are constitutionally incapable of foregoing the expenditure of every cent which comes into their hands, or who lack an incentive for, or an interest in, further saving, would divert part of their incomes to the purchase of post-war-delivery certificates rather than go without new goods when production is resumed. Still others save so little that even though their entire savings were shifted into post-war-delivery certificates they would have to increase their savings to meet the required payments.

The net increase in savings that would result even under these unfavorable circumstances would probably be sufficient to warrant the introduction of a plan for instalment selling for post-war delivery. But the deflationary effect of such sales can be substantially enhanced if consumers treat their post-war-delivery payments as current expenditures. In view of the importance of diverting as much purchasing power as possible from the current market, it is exceedingly worthwhile to do everything possible to produce this result.

Most gainfully-occupied persons who are prospective purchasers of post-war-delivery certificates have, particularly at a time of full employment at high wages, a considerable margin of "free" savings beyond their fixed or scheduled savings commitments. These free savings normally go into savings banks, into the securities markets, and into war bonds and stamps. If post-war-delivery certificates should satisfy all the requirements

of savings and provide an attractive medium for savings, there would be a substantial shift of savings from their normal channels into post-war-delivery certificates. To the extent that this occurred there would be no net gain in the diversion of purchasing power from the current market. But to the extent that post-war-delivery certificates fail to satisfy the requirements of ~~savings~~ and payments on such certificates are therefore treated as current expenditures, the invasion of other forms of savings will be minimized and payments for post-war-delivery certificates will be reflected largely in a decrease in expenditures for current goods and services.

Instalment payments as expenditures

Several circumstances will contribute to the treatment of instalment payments on purchases for post-war delivery as "spendings" rather than savings.

First, there is the established pattern of family expenditures and the resistance to change in that pattern. In part, the pattern is established by existing commitments: by insurance and annuity contracts, by agreements for purchase of building and loan shares, war bonds, etc.; by fixed rentals on houses and apartments; by real estate taxes and mortgage payments; by instalment purchase obligations. In part, it is established by intra-family budget allocations; by the husband's personal allowance; by allowances to the housewife for food, for clothing for herself and her children, and for household supplies and equipment; and by reserves for medical expenses and other emergency needs.

Purchases of goods for post-war delivery can be expected to fit

naturally and easily into this expenditure pattern. Such purchases need not disrupt established obligations nor distort customary budget allocations. On the contrary, they will fill the gap left by the disappearance of important consumers' durable goods from the market. For those who already have instalment commitments, payments on contracts for post-war delivery will merely replace payments on contracts for goods already delivered. For others, the family budget item for household equipment can be diverted, in the absence of current goods, to the purchase of "futures." Because instalment payments for goods for post-war delivery will replace expenditure items in family budgets, there will be a strong tendency to treat them as expenditure items.

Second, instalment payments have been traditionally treated as expenditures and it seems probable that this traditional treatment would carry over naturally into payments on goods for post-war delivery. In the normal instalment sales transaction periodic payments are almost completely disassociated from the delivery of the article subject to purchase and they bear no necessary relationship to its use. Yet each instalment payment represents a charge against current income--a periodic expenditure for the eventual ownership of the article.

The persistence of the treatment of instalment payments as current expenditures is illustrated by the reaction to changes in instalment credit terms. If the credit balance resulting from an instalment sale is paid off more rapidly than the goods depreciate in value, it is obvious that some part of each instalment payment represents a saving. The larger the payments on a given credit balance, the greater is the rate of saving. Yet this fact

appears to be virtually neglected in the budget calculations of consumers. One of the primary assumptions underlying the restriction of instalment credit terms by the Federal Reserve Board is that, when instalment payments are increased through the reduction of maturities, the consumer will continue to treat the increased payment as an expenditure and balance his budget by reducing his spendings rather than his savings. There is every reason to believe that this assumption is realistic.

Third, even if it were not for the traditional treatment of instalment payments as expenditures, it seems unlikely that consumers generally could be brought to look upon them as savings. Families generally save for three primary purposes: (1) to establish a reserve that can be used in emergencies, (2) to provide a competence for the period of retirement, and (3) to create an estate for the protection of wives and children. So long as post-war delivery sales are related to specific goods, instalment payments will fail to serve any of these purposes satisfactorily.

While these circumstances will contribute heavily to the general acceptance of instalment payments for post-war goods as current expenditures, it is nevertheless important to eliminate so far as possible any characteristics which might link these transactions to savings and thereby encourage competition with existing forms of savings.

The proposal to offer a special issue of war bonds that could be redeemed in goods after the war seems objectionable for this reason. Total sales of war bonds would undoubtedly be increased by the offer of a merchandise

bond. But for the most part such bonds would merely compete with other types of war bonds and with other forms of saving for the limited funds which consumers are willing to set aside from their current incomes. Total savings--in the sense of income funds withheld from the current market for goods and services--would probably increase very little.

In order to avoid so far as possible any savings aspect, purchases for post-war delivery should be linked to specific merchandise; liquidations in cash should be penalized prior to the time when priority numbers have been called; transferability of purchase certificates should be limited; and interest accruals should be avoided. The requirement of instalment payments is equally important. To be most effective purchases must be made periodically out of income. To permit purchases by full cash payment would be to encourage a shift of funds from savings banks, securities markets, etc., and to minimize the diversion of incomes from other types of expenditures.

Magnitude of deflationary effects

The potentialities of instalment selling for post-war delivery as an anti-inflationary weapon are tremendous. Yet only the crudest of estimates can be made to indicate the order of magnitude of the deflationary effects of the plan.

At present income levels, we could expect about 12 billion dollars worth of expenditures for consumers' durable goods, exclusive of houses, if materials, labor and productive capacity were available to make the goods. Expenditures for automobiles, refrigerators, and furnaces alone would probably be close to 8 billion dollars. The potential market for post-war-delivery

certificates, however, would be far greater than the potential market for delivered goods if peace and civilian production were suddenly and completely restored tomorrow. Prospective purchasers of actual goods under these circumstances would be confined to those who know they want immediately the goods subject to sale. Prospective purchasers of certificates, on the other hand, would include the far larger number of persons who believe they will want these goods in the indefinite future.

In the light of the strong incentives for post-war delivery purchases, it would not seem overly optimistic to assume that certificate sales could be maintained at an average rate of 6 billion dollars a year for several years, provided that the list of goods and services covered by the plan was progressively expanded. This means that the average annual volume of certificate sales would approximate the dollar volume of sales of automobiles, refrigerators, pianos and automatic furnaces in 1941, when incomes after taxes were substantially below present levels and when moderate restraints on demand for these goods had already been applied.

If certificate sales were distributed evenly at the rate of 500 million dollars a month and instalment payments were extended over the period of 24 months, collections would approximate $1\frac{1}{2}$ billion dollars during the first year, $4\frac{1}{2}$ billion dollars during the second year, and 6 billion dollars during the third year. It seems likely, however, that the rush to get low priority numbers, particularly for automobiles, would concentrate purchases heavily in the initial months of the program. Moreover, the period of payment for many certificates would be much shorter than 24 months. Hence the volume of

instalment payments during the first year would probably be substantially larger and the volume during the third year would probably be lower. The volume of payments might readily be 3 billion dollars during the first year, $4\frac{1}{2}$ billion during the second year, and $4\frac{1}{2}$ billion during the third year.

Not all of these payments would be diverted from the market for current goods and services. Commissions averaging about five percent of the volume of payments would be paid for sales and collections, and a large part of these disbursements would become spendable incomes again. This factor, however, is sufficiently small to be neglected for purposes of our crude calculations. Of substantially greater importance is the fact that in spite of every effort to encourage the treatment of instalment payments as expenditures, there would still be some encroachment upon savings. Many persons whose incomes are little above the subsistence level would be compelled to choose between post-war-delivery purchases and their customary methods of saving, and many others would cut into their savings in order to meet part of their instalment payments. These reductions in savings might, even under the plan presented here, reduce the deflationary effects of instalment payments for post-war-delivery by as much as 30 or 40 percent.

Leakages of this sort are bound to occur, however, no matter what means are used to attack the problem of excess purchasing power. The increased taxes provided for in the recent Revenue Act will bite heavily into the savings of many tax-payers, thereby limiting the impact of tax collections upon the volume of consumer expenditures. Similarly, the deflationary effects of purchases of war savings bonds are reduced substantially by the diversion of

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funds from previously accumulated savings and from other forms of current saving. Some students of the question believe that no more than 50 percent of the sales of war savings bonds represent increases in savings. Provided that care is taken to encourage the treatment of payments on post-war-delivery purchases as current expenditures, there is every reason to believe that the leakages in the deflationary effects of these payments would be no greater than the leakages in the deflationary effects of tax payments or of savings bond purchases.

The deflationary effects of a given volume of post-war-delivery payments appear, therefore, to be roughly comparable with the deflationary effects of at least an equivalent volume of tax collections and purchases of war savings bonds. However, since post-war-delivery payments would represent a new and additional deflationary force, it is appropriate to compare the prospective volume of payments with the prospective increment in tax collections and with the prospective increment in sales of war savings bonds. The increase in taxes that is expected to result from the new Revenue Act has been estimated at 7 or 8 billion dollars a year. Consequently, if our assumptions and calculations concerning the volume of post-war-delivery payments are correct, their deflationary effects during the first year would be less than half as great as those of the new Revenue Act, and during the second and third years they would be more than half as great as the effects of that Act. Since the outbreak of war, sales of war savings bonds show only a moderately rising trend, after adjustments are made for the shift of previously accumulated savings. Unless compulsion is used, the increase in such purchases can be expected to provide a much smaller deflationary force than that which would be contributed by payments on post-war-delivery certificates.

III

BY-PRODUCTS

While the creation of an additional deflationary force is the major objective of the plan presented here--and most characteristics have been designed to maximize its anti-inflationary effects--there would be a number of significant and highly desirable by-products. The most important of these appear to be: (1) the stimulation of business activity and employment in the post-war period; (2) the control of demand for consumers' durable goods when production is resumed; and (3) the preservation of selling machinery needed for rapid post-war expansion of civilian goods production.

Stimulation of post-war business activity

Much stress has been laid in the preceding section on the importance of inducing consumers to treat post-war-delivery payments as "spendings" rather than savings. This question of how instalment payments for post-war goods will be treated in consumers' budgets has an equally important bearing upon the stimulating effects of the plan in the post-war period.

There is strong resistance to the expenditure of savings. If payments on post-war-delivery certificates were looked upon exclusively as savings during the period of accumulation, the exchange of certificates for goods when production is resumed would be treated as an expenditure. Consequently, in order to preserve the balance between income and outgo, which is still just as essential to family well-being as it was in Poor Richard's day,

the purchaser would tend to cut other expenditures substantially. Under these circumstances, the call of priority numbers in the post-war period would be likely to result in a relatively minor and short-lived expansion of consumer demand and the resulting stimulus to employment and business activity would be minimized.

The situation changes, however, when instalment payments for post-war goods are treated as current expenditures. If each such payment is looked upon as money spent, the final exchange of the certificate for goods will represent merely the postponed delivery of something already fully paid for out of previous income and there will be no budgetary readjustments to compensate for the "spending" of the certificate. Under these circumstances the calling of priority numbers in the post-war period will pour out additional purchasing power into the markets for consumers' goods and services.

The effort to divorce certificate purchases so far as possible from savings is therefore directed at the maximization not only of the deflationary effects of instalment payments but also of the stimulating effects of post-war deliveries. The stimulating effects of the plan during the post-war period are controlled, and in large degree measured, by its deflationary effects during the war period. To the extent that instalment payments are met by reducing other forms of saving both the deflationary effects during the war period and the stimulating effects during the post-war period will be partially neutralized. To the extent that instalment payments are added to normal savings, purchasing power will be effectively skimmed

off the current market and added to the post-war market.

The release in the post-war period of purchasing power stored up in the form of post-war-delivery certificates would have economic effects similar to those of an equivalent deficit expenditure by the Federal government. Suppose the total amount of prepaid instalment sales should amount to 18 billion dollars at the close of the war and that priority numbers were called over a period of two years. Even if the net addition to total purchasing power were only two-thirds of the face value of certificates called, this would represent an injection of 6 billion dollars a year into the income stream. In view of the accumulating requirements for new industrial equipment, an additional stimulant of this magnitude might prove to be sufficient to keep the national income at a high level without recourse to government deficit spending.

The ability to avoid entirely, or to minimize, or even to delay the necessity for, government deficit spending in the post-war period without risking severe contraction of the national income would be exceedingly valuable. The public debt at the end of the war will be tremendous, and strong pressure for balancing the Federal government budget can be expected. From a social standpoint, also, production in response to consumer demand is likely to be preferable to production in response to expenditures by public agencies. If individuals make the choice, the nation will be assured of getting goods which its citizens want. If government agencies must make the choice, the very magnitude of the task of organizing quickly an adequate spending program is likely to produce goods that are less socially useful.

Control of demand for consumers' durables

It will be noted that the writer has avoided any claim that post-war-delivery instalment sales will increase the immediate post-war demand for consumers' durable goods. They will, it is true, create an assured and measurable market that will certainly be much larger over the long run than it would otherwise have been. But the primary consequence of a large backlog of prepaid order for consumers' durables will not be an enlargement of the post-war market for those goods but the preservation of the market for goods and services that would otherwise be sacrificed to meet payments for durables.

Regardless of the operation of any plan for selling goods for post-war delivery, demand for consumers' durables is likely to exceed productive capacity for considerable periods of time after production is restored. Demand for heavy consumers' durables is more volatile than that for any other category of consumers' goods and services. If the market were left to its own devices, we would no doubt have a tremendous and short-lived upsurge of demand, which would be accompanied by high prices, excessive profits, and over-expansion of facilities for production and distribution, followed by a severe drop in demand which would be accompanied by cut-throat price competition, dealer bankruptcy, unemployment, and idle equipment.

The machinery for controlling prices will undoubtedly be continued into the post-war period. But in the face of hunger for goods that have not been available during the war, a tremendously excessive demand in relation to the immediate supply of such goods, and the natural relaxation of public support of price regulations that would follow the end of the war, it seems

exceedingly unlikely that price control alone could be effective. Continuation of a full-fledged wartime rationing program would provide the necessary complement to price control. But political resistance to such a program after the restoration of production of civilian goods would undoubtedly be strong.

The system of priorities proposed here would provide a feasible solution to the problem of preventing chaotic conditions in the markets for consumers' durable goods. It would permit demand to be closely related to production, thereby preventing erratic price movements. Production itself could be limited by withholding the call of priority numbers if this seemed desirable either to prevent excessive plant expansion or to accomplish a systematic plan of gradual transition to peacetime production and employment, or to conserve materials more urgently needed for other purposes.

The system of priorities would amount in essence to a post-war rationing plan. But eligibility, under this form of rationing, would have to be earned by foresight and self-denial during the period of the war. This is certainly much more equitable and would have much more ready support from the public than a system which would give those in certain occupations greater rights than other citizens.

Preservation of sales machinery

The stoppage of production of automobiles, refrigerators, washing machines and many other consumers' durable goods threatens the existence of a large number of business enterprises that have been engaged in the retail distribution of those goods. Instalment selling for post-war delivery would

provide some measure of current relief to these agencies and would, by providing useful work, preserve at least a skeleton sales and financing structure upon which to build the post-war expansion of distribution.

The full impact of production stoppages upon sales and financing agencies has not yet been felt. Instalment payments on previous sales of consumers' durable goods are still being made to sales finance agencies. There is still a trickle of new car sales under the automobile rationing program and a substantial, though declining, volume of used car and service sales to sustain automobile dealers. Increased profit margins both on new car and used car sales have tended partially to offset the decline in the total volume of sales. For many other types of consumers' durable goods whose production has been stopped, retail inventories have not yet been exhausted.

Nevertheless, the machinery for selling and financing consumers' durable goods is rapidly disintegrating. Already, many dealers have gone out of business, some voluntarily, others as the result of bankruptcy and compulsory liquidation. Many sales finance companies have completely liquidated, and others have severely cut the number of their branch offices. The process of disintegration will continue and accelerate unless other use can be made of these facilities.

The misfortunes of these enterprises represent, in a sense, the hazards of war, which are never equitably distributed. Nevertheless, the public at large has interests of two kinds in their difficulties. In the first place, it has been the policy of all nations to prevent any one class

of citizens from bearing an unreasonably large share of the burden of war. In the second place, it is desirable to preserve at least a rudimentary sales and financing structure as a nucleus for post-war expansion.

Congress has already given evidence of its desire to ease the burdens imposed upon automobile dealers by the war. The Murray-Patman Act, a product of the deliberations of the Senate and House Small Business Committees, contains several features which come close to an outright subsidy to dealers in rationed goods. But while subsidies and other types of benefits may help individual business men, they will not prevent the disintegration of the machinery for selling and financing consumers' durable goods. The only way to preserve this machinery is to give it work to do.

Instalment selling for post-war delivery provides the opportunity for work that is both useful to the nation and reasonably profitable to selling and financing agencies whose business has been disrupted by the stoppage of consumers' durable goods production. Fortunately, the plan involves kinds of work that do not require able-bodied manpower needed elsewhere. The sales job can readily be handled by men who are beyond the age for military service and who have no aptitude for production or by men who are physically handicapped. The work of receiving, recording, and auditing can well be done by women.

IV

INCENTIVES FOR PURCHASERS

It scarcely needs to be said that the usefulness of instalment selling for post-war delivery in reducing the inflationary pressure does not guarantee its practicability. However dangerous the prospect of inflation for the nation as a whole, one cannot expect many individuals to act against their own self-interest to further so intangible an objective as the maintenance of stable prices. For example, everyone would concede that higher taxes are necessary to combat inflation, yet most individuals will struggle to minimize their own taxes and it is necessary to support tax legislation with an elaborate system of audit and compulsion.

Because voluntary action is contemplated, any plan for selling futures must rely upon strong individual incentives if it is to work on a satisfactory scale. The conditions must be such that consumers will want to buy goods for post-war delivery.

Resistance to the sale of futures

It has been argued by some that any plan of instalment selling for post-war delivery is bound to fail through the unwillingness of consumers to buy goods that are not yet in existence and therefore cannot be displayed or demonstrated. Let us examine the merits of this argument.

The history of merchandising is full of illustrations of sales of goods which the purchaser has not seen. The mail order houses have distributed tremendous quantities of goods and have progressively increased their

share of the market on the basis of catalogues which give photographs, sketches, or mere verbal descriptions of the articles offered for sale. Department stores and specialty shops make a considerable proportion of their sales in response to telephone or mail orders based on newspaper or handbill descriptions or sketches. Houses, cooperative apartments, and boats have long been sold from architects' plans; and one scarcely expects to see an oil burner, automatic stoker or home air-conditioning system demonstrated or displayed on the premises of the heating contractor who sells them.

It can properly be argued that the characteristics and performance of these goods are well-known to buyers even if they do not see them before making their purchases. Yet the consumer will certainly not be buying a pig-in-a-poke when he commits himself to the purchase of an automobile, a refrigerator, a piano, or an oil-burner. The usefulness and technical performance of these goods have long been demonstrated. The consumer knows that he will need such articles in the post-war period. He also knows that Chevrolet, Ford, Plymouth, and other automobile manufacturers will make good low-priced cars, and that Frigidaire, General Electric, Kelvinator, Servel, Westinghouse, and other manufacturers will make good refrigerators. Under the plan proposed here he would be free to choose among various makes and models at the time of delivery.

Technological advances induced by the war can be expected to change substantially the construction and design of most consumers' durable goods. But the consumer knows that these developments should make post-war goods more desirable than pre-war goods. Under these circumstances the inability of

manufacturers to describe precisely their post-war product may be an asset rather than a handicap to promotional efforts. It presents both a challenge and an opportunity to the advertising profession. Colorful sketches indicating progress in the improvement of design and performance could be used to attract the consumer's interest and to whet his appetite for the new goods. Color plastics, light metals, and functional design offer enormous potentialities for appeal to the eye.

There is nothing essentially novel in the idea of accumulating funds for the purchase of goods by instalment payments in advance of delivery. Examples of instalment buying for deferred delivery can be found both here and abroad. While these examples are far from conclusive, they provide no evidence to indicate that there would be any considerable resistance by consumers to post-war-delivery purchases.

The most comparable example is the sale of the Volkswagen or people's car in Germany. The motives underlying the original plan, which resulted from an order of Hitler in the spring of 1937, are obscure; but it seems probable that its purposes were: (1) to create a sufficiently large market to permit the manufacture of a small pleasure car at a price the German working classes could afford to pay, (2) to create a government-owned factory that would be useful for the production of military equipment, (3) to create a stock of civilian automobiles which could be used for military purposes, and (4) to gain popular support for large expenditures for highways intended for military use.

The details of the plan did not begin to emerge until August 1938, when it was announced that the price of the car would be 990 marks--the

equivalent of about \$350.00--payable in weekly instalments of 5 marks or multiples thereof. Collections, which started in September, were made through the Labor Front. Later the price was increased to 1230 marks to cover liability, fire, and theft insurance for the first two years, and shipping charges. A large plant, called the Volkswagen Works, with a town to house its workers, was built near Brunswick. Production was scheduled at 100,000 cars in 1940, 200,000 in 1941, and 250,000 in 1942.

While the original program appears to have contemplated delivery of automobiles before instalment payments were completed, the detailed plan made it clear that no car would be delivered until the purchase price had been fully paid. This suggests that an additional motive--to divert purchasing power from the market--had in the meantime been added to the earlier ones. It is even conceivable that the primary purposes from the start may have been to finance the production of armaments and to hide from the outside world the creation of an additional armament plant. Although models were shown at the International Automobile Show in Berlin in 1939 and later in various provinces, in order to stimulate instalment purchases, no cars were ever delivered even though thousands of buyers had paid the full purchase price.

By July 1939, 10 months after the plan became effective, 253,000 purchasers had paid in 110 million marks against the future delivery of cars. No later figures have been published. Following the outbreak of war in September, purchasers were urged to continue their payments and it was announced that the Volkswagen plant had been converted to war production.

Although the number of instalment purchasers was relatively small, it should be remembered that automobiles are owned only by the wealthy classes in Germany. Few among the working classes knew how to drive a car, and workers' homes lacked facilities for storing one. Moreover, the incomes of German workers were so low that even the relatively small instalment payments represented a substantial sacrifice.^{1/}

There have also been examples of instalment purchases for deferred delivery in this country. Lay-away plans, by which instalment payments are made in advance of the delivery of merchandise, have been common in many fields of merchandising, notably clothing. Christmas savings plans, the success of which was limited only by the low yields on short-term investments, were in reality means of accumulating the price of Christmas expenditures by advance instalment payments. In the automobile field, the General Motors Corporation experimented with a pre-payment plan in 1925 and 1926. In order to encourage a continuing relationship with the Chevrolet dealer who sold him a car, the purchaser was encouraged to accumulate payments for a new car and a discount on service bills was credited to his new-car fund.

Lay-away plans have never been used on a large scale and the Chevrolet experiment produced a relatively small number of prepaid sales. But the significant fact is that they should have succeeded at all under the

^{1/} The writer is indebted to the Research Project on Social and Economic Controls in Germany and Russia, undertaken by the Graduate Faculty of Political and Social Science, New York, and especially to Dr. Ernest Hamburger, for the information on which these comments on the Volkswagen were based.

circumstances of their use. Those schemes had to compete with offers of identical goods on the usual instalment terms, and it is little wonder that most consumers preferred to enjoy the merchandise while they were paying for it.

If the goods offered for sale under the post-war-delivery plan could be purchased for immediate delivery on the usual instalment credit terms, a very limited volume of sales could be confidently predicted. But the present situation is completely different from that under which deferred-delivery instalment sales have been offered previously. The goods subject to sale for post-war delivery would be those which are no longer available for current delivery on any terms. Under these circumstances deferred-delivery instalment sales need not compete with current-delivery instalment sales of the same goods. The only competition would be with increased quantities of other types of goods which remain in the market. This is a competition in which instalment sales for post-war delivery can readily come out on top if adequate incentives are offered.

Appeal of priorities

By far the most important of the two advantages that would be offered to purchasers of post-war-delivery certificates is the prior claim to the post-war product. By virtue of the stoppage of civilian production of major types of consumers' durable goods, a backlog of potential demand is rapidly being built up. The longer the war lasts the larger will be this pent-up demand. Besides, after the conclusion of the war it will take time to get

into production again. Millions of people will want a new automobile or refrigerator or oil-burner as quickly as possible after the conclusion of the war. But many will have to wait.

In the automobile field, for instance, at least 2.5 million cars would normally be junked each year and this rate is likely to be increased by gasoline and tire rationing. By the close of 1943, the replacement demand alone could be expected to equal the number of cars produced during the best previous automobile year. But even if the war ended then, it would take months to reestablish production lines for passenger automobiles. The period of transition to peace-time production has been estimated at roughly four months if 1942 models are repeated and at least eight months if the post-war automobile is to be redesigned. It is apparent therefore that, even if the war is of relatively short duration, the immediate replacement demand for automobiles is likely to exceed a full year's production. To the replacement demand must be added the inventory requirements of dealers for display and demonstration purposes and the demand from those who will want a car or an additional car for the first time. This means that some people who would like to buy a car promptly after the conclusion of the war will have to wait for months--and perhaps for years--if the war is long.

In varying degrees, the same thing is likely to be true of many other types of consumers' durable goods.

If a prior claim to post-war production is given to instalment buyers of "futures," each such sale would still further postpone the date of delivery for those who failed to make such purchases. As the number of instalment

purchasers increases, the hopes of well-established customers for preferential treatment from their dealers will disappear, and their only hope of prompt delivery will be to enter instalment purchase contracts themselves. As the war goes on, the wearing out of automobiles and household appliances will also impel participation in the plan. When these goods are no longer serviceable, it will be brought home to the consumer how important they are in his life and how desirable it would be to replace them as soon as possible.

The price discount as an incentive

The offer of a price discount would probably be a less powerful incentive than a priority to post-war production. Nevertheless, it should add substantially to the appeal of the plan. Every individual naturally tries to get the most for his money, and the strong sales appeal of a bargain price is well-known to the merchandising profession. The offer of a discount from the standard price for post-war-delivery purchases would permit "futures" to compete more effectively with present goods for the consumer's dollar.

Moreover, a price discount is fully justified by the circumstances. On one hand, since money commands a rental, the person who pays for his goods in advance of delivery should, in the interest of equity, obtain a price advantage over the person who pays at the time of delivery. On the other hand, the creation of a large backlog of prepaid orders for consumers' durable goods in specific price classes will permit economies in production and distribution which should be shared with the purchaser who helps to create them.

The allowance of a discount from the post-war price rather than an

interest rate is desirable for a number of reasons. First, it would eliminate expensive interest calculations. Second, it would encourage prompt use of certificates to obtain delivery of goods after their priority numbers have been called. Third, it would more clearly identify the instalment transaction with the purchase of merchandise. The delivery of an interest-bearing certificate would certainly induce a much higher degree of competition with other forms of saving.

Discounts from standard retail prices have been commonly offered by dealers in automobiles and other consumers' durable goods, either in the form of a reduced price or an excessive trade-in allowance. Consequently, only a relatively substantial price-discount would be considered significant by post-war-delivery purchasers. It is recommended that the discount from the established purchase price should approximate 10 percent. This can best be accomplished by giving the post-war-delivery certificate a merchandise value 10% greater than the amount paid in by the purchaser.

The amount of the discount for post-war-delivery purchases should be reconsidered from time to time in relation to the prospective period of deferment of delivery. For instance, the discount might be reduced progressively at six-month intervals, unless so many certificates had been sold that the delay in delivery after the war promised to offset the approach to the end of hostilities.

The price discount for post-war-delivery purchases would be made up when the goods were delivered by the sacrifice of part of the usual gross profit

margin on the part of the dealer who delivers the goods and by a rebate to that dealer on the part of the manufacturer whose goods are delivered. In the light of the relative benefits that would accrue to dealers and to manufacturers under the plan, a 10 percent price differential might be divided in the proportion of 7 to the dealer who delivers the goods and 3 to the manufacturer whose goods are delivered.

Since commissions paid out for the sale of certificates and for the collection and recording of payments would be covered by the Treasury payment for the use of the purchaser's money during the period prior to the delivery of the goods, the purchaser who meets his payments promptly could be guaranteed the return of the full amount paid after his priority number has been called if he should prefer to take cash instead of goods. The cash withdrawal right would probably never be exercised because at that point it would be possible to sell the certificate--undoubtedly at a profit. But the guarantee of the return of the amount paid in after priority numbers had been called would undoubtedly be a valuable selling point.

Cash withdrawals should also be permitted before the completion of payments and before the purchaser's priority number has been called. But such withdrawals would be penalized by the loss of the commissions paid out for sales and collections.

Incentives for prompt payment

Prompt payment of instalment accounts should be encouraged by penalizing delinquencies. Two types of penalties are readily available: the

deferment of the priority to which the purchaser would otherwise be entitled and a decrease in the price-discount allowed for advance payment.

The deferment of priorities in cases of delinquency is important not only as a means of encouraging prompt payment in order to minimize collection costs, but also as the means of assuring equitable treatment of purchasers. If there were no such penalty and if priorities were assigned solely on the basis of the date of the instalment purchase contract, it would be possible for the purchaser to get a low priority number by making an immediate down-payment and defaulting on all subsequent payments. This would give him an unfair advantage over those who meet their commitments. It is obviously desirable that the deferment of priorities be progressive--the greater the degree of delinquency, the greater the deferment of priority--and that the schedule of deferment be so arranged that the purchaser would benefit by waiting until he could meet his instalment payments rather than by entering a contract on which he would be unable to perform.

Similarly, the reduction of the price-discount in cases of delinquency is important not only to stimulate prompt payment but also to compensate for the additional expense of following up delinquencies and for the shorter period of time for which the United States Treasury would have the use of the purchaser's money. It would obviously be unfair to permit the purchaser who made an initial down-payment and defaulted on later payments to buy goods at the same price-discount as the purchaser who made his payments according to schedule. Like the deferment of priorities, the decrease in the price discount should be related to the degree of delinquency, and the schedule of

delinquent charges should be so adjusted that it would pay to postpone entering an instalment contract until payments could be met promptly.

Delinquency could be calculated most efficiently if all instalments were payable on the first of each month. However, in order to prevent peak loads for collection agencies, due-dates for individual contracts should be scheduled for the tenth, twentieth or thirtieth of each month, to suit the convenience of the purchaser. Each month should be treated as having thirty days for purposes of calculating delinquency. The use of rounded payment dates would still leave a very simple calculation, which clerks could soon compute and check with great speed.

Purchasers might be allowed a delinquency of 99 payment days without penalty. On a twenty-payment contract, this would represent an average grace period of 5 days for each payment. Such an allowance would compensate for payment dates that would fall on Sundays and holidays and allow a reasonable leeway for the receipt of mailed payments, for delays due to illness, etc. It is further recommended that the priority number to which the purchaser would be entitled by virtue of the date of entering an instalment purchase contract be increased by one for each additional two hundred delinquent payment days, or fraction thereof, and that delinquency charges be computed at 0.2% of the cash value of the certificate for each additional one hundred delinquent payment days, or fraction thereof.

Delinquency charges should be computed and collected after all scheduled payments have been met. Since it is an objective of the plan to insure regular periodic payments out of income, no compensating credit should be allowed for prepayment of any instalments.

Payment schedules

Payment schedules should be designed to produce as large payments as possible without creating excessive sales resistance and without penalizing too severely those with low incomes.

Two considerations point to the desirability of high payment requirements. The first is the cost of collection. Most cost elements vary with the number of items handled rather than with the number of dollars collected. This means that the larger and fewer the payments, the lower the total collection cost. The second is the deflationary effect: the larger the payments, the larger the diversion of purchasing power from a given income.

It is obvious, however, that excessive payment requirements could defeat the economic objectives of the plan. Large groups of potential purchasers would be eliminated from participation by firing down-payments and instalments at figures that are beyond their reach. Consequently, even though the flow of funds from those who could meet the required payments might be speeded up, the total deflationary effects of the plan would be substantially reduced by the reduction in the volume of certificate sales.

Beyond this there are social objections to excessive payments, because the priority system would operate to deny prompt delivery of goods in the post-war period to those who were financially unable to meet the payments. The exclusion of some prospective purchasers is unavoidable. Even though the payments were exceedingly low, some persons who would like to purchase post-war-delivery certificates would be unable to do so by virtue of their poverty. But these persons would be equally unable to buy such goods in an absolutely

free market. It should be a prime objective in fixing post-war-delivery payments not to increase the difficulties of low-income classes in acquiring consumers' durable goods. This means, in effect, that the terms offered for post-war-delivery sale should not be much more stringent than those which would normally be offered in a free market.

In the normal instalment sales transaction, particularly for automobiles, down-payments are fixed relatively high in order to cover the initial depreciation which occurs when the goods become "used." In actual practice, however, automobile down-payments are generally covered by trade-in allowances. A large down-payment for post-war-delivery sales is not only unnecessary, but undesirable because it would create additional sales resistance. The down-payment should be such that prospective purchasers would be likely to have the sum in their pockets at the time they are approached by salesmen. Other reasons for keeping the down-payment modest will be discussed in the succeeding section.

Instalment payments should be more substantial than down-payments. Once the purchaser has made a down-payment he can be expected to adjust his budget to meet a more substantial sum out of his next pay-check. These readjustments of expenditures are, in fact, the key to the deflationary effects of post-war-delivery purchases.

The following payment schedule is proposed as one which would maintain a satisfactory balance between these various conflicting objectives:

<u>Merchandise Value of Certificate</u>	<u>Cash Value of Certificate</u>	<u>Down Payment</u>	<u>Instalment Payment</u>
\$ 110	\$100	\$3	1 @ \$9 ; 11 @ \$8
165	150	4	10 @ \$11 3 @ \$12
220	200	5	13 @ \$14; 1 @ \$13
330	300	6	6 @ \$19; 10 @ \$18
440	400	7	15 @ \$22; 3 @ \$21
550	500	8	12 @ \$25; 8 @ \$24
770	700	9	19 @ \$33; 2 @ \$32
1,100	1,000	11.0	22 @ \$45
1,540	1,400	11	9 @ \$61; 14 @ \$60
2,200	2,000	12	20 @ \$83; 4 @ \$82

WORK AND MOTIVATION OF OTHER PARTICIPANTS

The willingness of consumers to buy is obviously of crucial importance to the successful operation of any plan of instalment selling for post-war delivery. However, the purchaser is but one of several parties to the instalment sales transaction. Adequate incentives must be offered to motivate the voluntary action of other participants. Dealers must want to sell post-war-delivery certificates; the collection agencies must be willing to handle funds and to maintain bookkeeping records; and manufacturers and public utilities companies must have reason to play the parts assigned to them.

Characteristics of certificate sales

There may be some broad categories of goods--such as food--which consumers will buy in stable quantities at given income and price levels, regardless of the amount of sales effort that is exerted. But this is not true of the category of consumers' durable goods. Even less is it true of individual articles in that category or of certificates for the future delivery of such articles. Sales effort will be needed to overcome the natural inertia that has always characterized markets involving commitments for the payment of relatively large sums.

Sales efforts cost money and the dealer should be compensated for them. Costs of selling post-war-delivery certificates, however, would be substantially lower than cost of selling the goods themselves and the commissions offered dealers can properly be much lower than the usual sales commission.

The techniques of selling for post-war delivery would differ substantially from those of normal sales. There would be no dickering for trade-in allowances, no competition with other makes at the point of the instalment sale, and no demonstrations. There would be no inventories to store and finance and no additional overhead to maintain. The primary objective of the sales effort would be to bring the advantages of instalment purchases for future delivery forcefully to the attention of every household. The potential list of customers would include all gainfully-occupied persons. House-to-house canvasses would probably be profitable as soon as solicitation of dealers' regular customer lists had been exhausted.

The sales efforts of dealers would be reinforced by pressures upon the purchaser which do not usually exist. Priorities would provide a powerful force for reducing sales resistance. In fact, many purchasers could be expected to seek out their dealers in order to buy post-war-delivery goods as promptly as possible. The sales campaign would be supported by government pronouncements that purchases for post-war delivery help the war effort. The complete freedom of choice of makes and models should also facilitate certificate sales. The purchaser would buy only a right to an automobile, or a refrigerator, or an automatic stoker, and he would have none of the hesitations and uncertainties that naturally arise when he puts his hard-earned money on the line for specific goods.

Not only is it practicable to offer relatively modest commissions but there are positive reasons for keeping commissions as low as possible.

In the first place, as has already been indicated, commissions paid for sales and collections should be limited to the amount which the Treasury would pay for the use of the purchaser's money prior to the date of delivery of the goods. In this way the purchaser can be assured of the return of the amount which he had paid if he should choose to take cash instead of goods when the priority number of his certificate has been called.

In the second place, the deflationary effects of instalment payments would be offset to the extent that these payments are diverted to the payment of sales and collection commissions.

Finally, it is in the interest of making the best use of our manpower resources to keep sales commissions low. The stoppage of production of major consumers' durable goods was necessary not only to release materials for production of military equipment but also to release manpower. Many of those who sold these goods are as readily adaptable to war work as those who operated machines or worked on assembly lines. The compensation offered to salesmen should be sufficient only to attract those who are for one reason or another not readily adaptable to other work. Sales could readily be made by physically handicapped men or by previously unemployed women. This work would lend itself readily to part-time employment. The number of salesmen engaged in selling post-war-delivery certificates should be only a small fraction of the number normally employed in selling goods for current delivery, but each salesman should be able to produce many times as many sales as the peacetime average.

Dealers' sales commissions

The down-payment made by the purchaser would be kept by the dealer as his initial sales commission. By treating the entire down-payment as part of the sales commission, the necessity of holding thousands of individual dealers accountable for funds collected by them can be avoided. The down-payment should vary with the value of the certificate, but it should be modest even on certificates of substantial value. This is desirable in the interests of reducing sales resistance and of minimizing competitive reductions in down-payments. If a large down-payment were required, there would undoubtedly be a tendency for buyers, knowing that the down-payment goes to the dealer, to "shop" for a dealer who would reduce the down-payment or eliminate it entirely.

An additional sales commission would be paid to the dealer upon completion of the purchaser's payments, or, if it seems desirable, at specific stages in the fulfillment of the instalment contract--for instance, upon the payment of the sixth, the twelfth, and, if there are more than twelve, the final instalment. These secondary commissions should be paid only to dealers who follow up delinquent accounts referred back to them by the sales finance agencies. Otherwise, dealers might prefer to take the secondary commissions that would come to them automatically and to avoid the exertion of additional sales pressure on accounts in default.

The amount to be paid dealers through down-payments and secondary commissions should be determined in relation to the amount which must be paid to cover costs of collection and the amount which the U. S. Treasury would pay for the use of the purchaser's money. The following schedule of dealers' commissions, however, would appear to be feasible:

<u>Purchase Price of Certificate</u>	<u>Initial Commission (Down Payment)</u>	<u>Secondary Commission (2% of Purchase Price) Monthly Payment:</u>	<u>Total Commission Amount</u>	<u>Commission Percent of Purchase Price</u>
\$ 100	\$ 3.00	\$ 1.94	\$ 4.94	4.9
150	4.00	2.92	6.92	4.6
200	5.00	3.90	8.90	4.4
300	6.00	5.88	11.88	4.0
400	7.00	7.86	14.86	3.7
500	8.00	9.84	17.84	3.6
700	9.00	13.82	22.82	3.3
1,000	10.00	19.80	29.80	3.0
1,400	11.00	27.78	38.78	2.8
2,000	12.00	39.76	51.76	2.6

Participation of dealers in the plan would be encouraged not only by the commissions that would be paid for selling post-war-delivery certificates but also by their stake in the final delivery of the goods. Even though the certificate would be valid for purchase with any dealer, it could be anticipated that most certificate holders would buy from the dealer who sold them their certificates. Certainly the dealer who made the initial sale would have a strong competitive advantage when the certificate becomes valid for delivery.

Beyond these incentives of self-interest, however, one can rely heavily upon the patriotic desire of consumers' durable goods dealers to participate in a program that will contribute to the war effort. Automobile dealers, refrigerator and piano dealers and heating equipment contractors are frequently among the leading citizens of their communities and most of them are itching for an opportunity to be more directly useful toward the winning of the war. Post-war-delivery sales would provide this opportunity, and even if the commissions were smaller than those suggested above, full

cooperation of dealers could be anticipated.

The dealer who finally delivers the goods in the post-war period would, as has been indicated, forego part of his normal gross profit. If the suggestion made here is followed, the final dealer would discount the established retail price by about 7 percent. But this concession would represent only a little more than $1/4$ of the customary dealer's gross profit margin on automobile sales and about $1/5$ of the customary dealer's margin on refrigerators, pianos and heating equipment. Besides, more than a commensurate part of the selling job would have been done. The development of customers, ready, willing, and able to buy, constitutes a very large part of the procedure of selling consumers' durable goods and the dealer who completes the sale in the post-war period will be presented with such customers.

Trade-in bargaining, particularly in the automobile field, would take place as usual when the sale is completed. But the dealer who completes the sale would be in a much stronger position to resist pressure for excessive trade-in allowances. In fact, since certificates would presumably cover the full purchase price of the new car, the sale of the used car might readily become an entirely separate transaction, the sale being made to the highest bidder whether he be the dealer who delivers the new car, another new car dealer, or a used car dealer.

Incentives for manufacturers and public utility companies

Manufacturers would be expected to contribute to the plan by providing part of the post-war-delivery price-discount in the form of a rebate to dealers who deliver their goods in exchange for a certificate. It has been suggested that this rebate should approximate 3% of the established retail price. They would also be expected to reinforce the sales efforts of dealers

and their salesmen through national promotional advertising.

In return for their contributions to the plan, manufacturers would benefit in four different ways.

First, the plan would help to preserve the present pattern of consumer expenditures. In the absence of some scheme for absorbing the purchasing power that can no longer be devoted to the purchase of consumer durables, other categories of goods are bound to get a larger share of the consumer's dollar. The further this shift of spending habits progresses, the more difficult it will be for durable goods manufacturers to regain their previous position in the expenditure pattern when production is restored.

Second, it would provide an enormous assured market for specific price-classes of consumers' durables in the post-war period. A large and measurable market has been the dream of every production man. It would permit the planning of production and distribution by the industries concerned in response to accurate advance knowledge of the character and distribution of demand. This would lower production and distribution costs all along the line, which might be the means of preserving the favorable competitive position of the American manufacturers of automobiles and other consumers' durable goods in relation to foreign manufacturers in the post-war period. Even more important it would facilitate rapid--but controlled--expansion of production and employment. The consumer durable goods industries are fully aware of their large responsibility for absorbing at the conclusion of the war a substantial part of the manpower now devoted to the military effort.

Third, it would help to preserve the facilities for retail sales upon which the manufacturer must depend for the distribution of his products in the post-war period. The mortality among their dealers has already led several automobile manufacturers to consider plans for dealer subsidies as a means of preserving a skeleton sales organization.

Fourth, it would help to conserve substantial investments in the trade-names of their products. Values built up through years of promotional advertising and product performance will gradually disintegrate if these trade-names are not kept before the public. From the standpoint of the manufacturers concerned, it is just as important to preserve these trade-names as it is to preserve the plant and specialized tools that are capable of manufacturing the product. There is general agreement that present institutional advertising campaigns, based on the contribution of the manufacturer to the war effort, have reached the point of rapidly diminishing returns and that a new advertising appeal is essential. Advertisements directed toward the promotion of instalment sales for post-war delivery would fill this need. They would serve the double purpose of contributing to the battle against inflation and preserving product trade-names.

Public utility companies would be expected also to support the sales campaign with promotional advertising and to serve as agencies through which payments would be made. These companies have long recognized their special interest in the sale of household appliances. Such sales not only increase the total market for gas or electricity, but produce operating economies through an increase in the average billing for domestic service and through the creation of a demand which tends to balance the industrial load.

These advantages, plus the prospect of excess productive capacity in the post-war period, can be expected to guarantee enthusiastic participation of the gas and electric power companies in the promotion of the sale of household appliances for post-war delivery. In fact, several such companies have indicated their willingness to bear the full cost of making such sales.

Selection of collection and bookkeeping agencies

Provision must also be made for the collection and recording of instalment payments if the plan for post-war-delivery sales is to work. It is not enough merely to collect the purchase price of the certificate by the time the instalment contract matures. If the deflationary potentialities of the plan are to be fully exploited and the Treasury is to get its money's worth, it is necessary to require regular payments at stated intervals, to send delinquent notices and to refer cases of substantial delinquency back to dealers, and to assess delinquency charges. This means that the amount and date of each instalment payment on each certificate must be recorded currently.

Two considerations make it seem inadvisable to permit dealers to collect instalment payments. First, instalment sales have been used by some merchants as the means of exposing customers to pressure for the purchase of additional merchandise at the time of each instalment payment. Since refrigerators and other household appliances are frequently sold by merchants who deal in household furnishings, clothing, or jewelry, post-war-delivery sales might be used to stimulate sales of these latter goods. Whatever the merits

of this merchandising device during normal times, it seems highly undesirable to allow a plan which is designed to take purchasing power off the market to be used to stimulate additional sales of current goods. Second, the mortality among dealers in consumers' durable goods is likely to be high, in spite of the additional income which instalment sales for post-war delivery would provide, and it is desirable to avoid the necessity of establishing an auditing system to protect purchasers against default by dealers.

The agencies best equipped to undertake the job of recording payments, sending delinquent notices and computing delinquency charges are the enterprises which have been previously engaged in financing instalment sales of consumers' durable goods. Moreover, because their businesses have been badly hurt by the discontinuance of production of such goods they have the best claim to the right to do it.

Sales finance agencies already have the personnel and the office equipment necessary for the work. The recording of payments for post-war-delivery certificates would replace naturally and easily the recording of payments on conventional instalment purchase contracts. The remaining branch-office structure and the clerical office force of these enterprises would be given employment and thereby kept intact. But there would be no need for the able-bodied men normally employed to chase "skips" and to repossess cars, who properly belong in the military forces or in war industries.

Sales finance agencies should be required to meet two standards before they are authorized to participate in the plan. First, they should

be required to show that at the time Regulation W was promulgated they were engaged, as a major activity, in financing the purchase of goods subject to post-war-delivery sale. This is desirable both for the purpose of assuring the availability of trained personnel, of adequate office equipment, and of established relationships with dealers--all of which would be important to smooth and efficient operation--and for the purpose of limiting the advantages of the plan to enterprises that have been most seriously affected by the discontinuance of production of consumers' durables. Second, they should be required to furnish a bond, to hypothecate securities, or otherwise to provide a guarantee of their responsibility for funds passing through their hands.

The sales finance agencies have, however, two important handicaps so far as the collection of instalment payments from purchasers is concerned. First, their remaining offices are situated primarily in the large cities, so that residents of smaller places would be able to make payment only by checks sent through the mail or by money order. Second, many of them are also engaged in the business of lending money. To permit these enterprises to use the personal contacts with individual purchasers which the acceptance of payments would give them for the solicitation of personal loans not only would handicap the attainment of the economic objectives of the plan but would be inequitable to competing lending agencies which would be excluded from participation.

For these reasons, it seems desirable to arrange for the acceptance of cash payments by agencies which have no interest in selling the purchaser goods or in lending him money and whose offices are numerous, readily accessible to purchasers, and equipped to accept cash payments. A number of agencies

would meet these standards. The telephone companies would be ideal. The post offices and the telegraph companies would be almost equally satisfactory. Mutual and other savings banks that have no personal loan service would also meet the requirements. The gas and electric companies could also be used, but care should be taken to protect the interests of independent household appliance dealers where the utility company is engaged directly or through a subsidiary in the sale of household appliances. Use of the telephone and public utility companies would permit the payment of instalments with bills for telephone, gas, or electric service.

Payments by check sent through the mail could go directly to the sales finance agency. But that agency should be prohibited from accepting cash payments, from addressing solicitations of any sort to purchasers for post-war delivery or from revealing the names of purchasers.

Work of the sales finance and local collection agencies

This division of labor between the sales finance agency, which would do the bookkeeping, and the local collection agency, which would accept and receipt for payments, need not involve any duplication of effort. On the contrary, this functional division is a natural one and it would assign to each agency the work which it is best equipped to do. The lack of offices generally accessible for cash payments has long been recognized as a handicap of sales finance companies. Only recently two large sales finance companies undertook to remedy this shortcoming by arranging for payment through the Western Union Telegraph Company, a device virtually identical with that proposed here.

The most satisfactory collection procedure would appear to be as follows:

Upon receiving a post-war-delivery sales contract from the dealer, the sales finance agency would issue a payment book to the purchaser and open a ledger account for him. The payment book should contain a coupon and a stub for each payment, imprinted with the purchaser's serial number, the payment number, the amount of the payment, and the name and address of the sales finance agency which issued it. The payment book should also show the names and addresses of the local collection agencies to which cash payments could be made in each community.

The local collection agency would accept payments made by the purchaser, stamp the coupon and the stub to show the collection agency and the date of payment, tear out the coupon and initial the stub in the payment book. Coupons would be sorted periodically and sent with remittances to the appropriate sales finance agency, which would use the coupons to post its ledger accounts. If the purchaser wished to do so, however, he could send checks or money orders directly to the sales finance agency.

The sales finance agency would keep a current record of payments for each purchaser to which it had issued a payment book, send a series of notices to delinquents, and refer cases of substantial delinquency to the dealer for additional sales effort. The notification of delinquents would serve not only to minimize delinquency but also to prevent theft by cashiers of local collection agencies, since the failure to forward payments would be quickly discovered. The sales finance agency would send remittances periodically to the Federal Reserve Bank or branch of the district in which its office

is situated. When the last payment has been made, it would compute delinquency charges, notify the purchaser of the amount and instruct him to make payment to his local collection agency. When delinquency charges have been collected, it would send the dealer his final sales commission, assign a priority number to the account, and send it to the Federal Reserve Bank for audit and the issuance of a paid-up certificate.

Collection and bookkeeping commissions

The work of local collection agencies could be handled at very little cost. There would be no necessity for maintaining files, for looking up records, for recording names and amounts, for making computations, or for referring to schedules of charges. Making change would be simplified by keeping the payments in even dollars. The cashier need only take the payment, stamp the payment book at two points, initial the stub, and tear out a coupon. This operation could be done with ease at the rate of two a minute, although allowances would have to be made for questions and for irregularities, such as the failure to present a payment book.^{1/} Many local collection agencies could handle this additional work by fuller utilization of present personnel.

The sorting of coupons could be done with great speed and would add

^{1/} Although receipts could readily be given by the local collection agency for payments made without the tender of the payment book, the difficulties of the sales finance agency in identifying the purchaser other than through the serial number and the possibilities of error in attempting to do so are such that it would appear to be the best policy not to accept any payment unless the book or the coupon was presented. A purchaser who has lost his payment book should be sent back to the dealer who would obtain a new payment book from the sales finance agency upon the payment by the purchaser of a small fee to cover the cost.

little to the cost. It would probably be necessary to list the serial numbers of the coupons by sales finance agencies as a protection against loss of the coupons in the course of delivery to sales finance agencies, but this also could be done very rapidly and would involve the transcription of only one figure.

The money-order service of the Post Office is somewhat similar to that which would be rendered by local collection agencies. Charges for money orders range from 6¢ an item for amounts of \$2.50 or less to 22¢ for amounts from \$80.01 to \$100. The procedure for handling them is elaborate. The money-order clerk must first get the customer to fill out a blank; then he must transcribe the names and addresses of the payor and payee and the amount to be sent at two places on the money-order form; he must stamp the form, look up the fee and add it to the amount to be sent, and collect the total from the customer. For each money order issued, funds must also be paid out to the payee and these transactions must be accounted for through inter-office bookkeeping.

Thus, while postal money orders serve a somewhat similar purpose, the procedure for handling them is of necessity far more costly than the collection system proposed here. Observations of actual transactions of both types indicate that the acceptance of payments on a coupon basis requires less than one-fifth as much time as the issuance of money orders. The difference in clerical time required for completing the transaction--from payment by the payor to repayment to the payee--is probably even greater.

Commercial services virtually identical with those that local

collection agencies would be expected to perform have been recently contracted for at 7¢ an item. Costs may have increased somewhat since these contracts were entered into, but any rise in costs would probably be offset by the tremendous volume of payments that could be expected. A fee of 7¢ an item would appear therefore to provide adequate compensation for local collection agencies. These fees should be subtracted from receipts in computing remittances to sales finance agencies.

Sales finance agencies would need larger commissions than local collection agencies to cover their costs. The posting of payments would be exceedingly simple since the amount of the payment would be determined by the value of the certificate subject to purchase and it would be necessary only to enter the date of payment on the purchaser's ledger account. In addition to posting payments, however, the sales finance agency would send delinquent notices, compute delinquency charges, pay dealers for secondary commissions, and assign priority numbers. They would also be expected to supply the contract forms used by dealers and the payment book issued to purchasers.

As compensation for sending notices to delinquents and for computing delinquency charges, sales finance agencies should be permitted to keep part of the delinquency charges. The income from such charges should be large enough to encourage a continuous effort to collect delinquent accounts. In the absence of such an incentive, some sales finance agencies could be expected to take the income from payments that came in automatically and to neglect their delinquent accounts.

It is suggested that the sales finance agency retain one-quarter of all delinquency charges collected, less the 7¢ per item retained by the local collection agency for its services. Since delinquency charges would be collected in a lump sum at the end of the payment period, and the grace period would avoid the collection of negligible amounts, the collection fee would usually be small in relation to the sales finance agency's share of delinquency charges.

As compensation for furnishing contract forms, payment books and bookkeeping services, for supervising collections, and for assigning priorities, the sales finance agencies should be given a commission on all collections handled by them. This commission should be expressed as a percentage of purchaser's instalment payments, and it should cover the fees paid to local collection agency. It is proposed that this commission be fixed at $1\frac{1}{2}$ percent of all payments less than \$30.00 and 1 percent of all payments of \$30.00 or more.

This method of computing bookkeeping commissions of the sales finance agencies has substantial advantages from an accounting standpoint. It is useful for purposes of internal controls and of reports to the Federal Reserve Banks to treat the total value of coupons collected as receipts. The fixed percentages of coupon values for bookkeeping and collection services would then be subtracted from receipts and credited to current earnings; another fixed percentage would be subtracted from receipts and transferred to a liability account for dealers' secondary commission; and the remainder would be

forwarded to the Federal Reserve Bank. The fees withheld by local collection agencies would be treated as an operating expense of the sales finance agency chargeable against its income account.

The use of two percentage rates in computing bookkeeping commissions adds a complication to the plan, but this appears to be unavoidable. If all dealers sold certificates covering the whole range of denominations, a single percentage rate could be established because sales finance companies would take the unprofitable accounts in order to get the profitable ones. Refrigerator dealers, however, would produce only certificates of the smaller denominations. Consequently, if a single percentage rate should be used, sales finance agencies could be expected to neglect refrigerator dealers in favor of automobile dealers, whose business would be considerably more profitable.

The lowest payment contemplated for refrigerator certificates is \$8. The collection and bookkeeping revenue from such a payment would be 12 cents, out of which the local collection agency would take 7 cents. The remaining 5 cents per item would not cover the sales finance agency's cost. However, refrigerator dealers will also produce contracts calling for payments of \$19, from which the revenue would be 29 cents per item. The sales finance agency would retain 22 cents, which would undoubtedly exceed its cost by a substantial margin. For payments of \$33 on \$700 automobile certificates revenue would be 33 cents per item, of which 26 cents would go to the sales finance agency. The highest payments would be \$85, for which the sales finance agency's revenue would be 76 cents per item.

The right of the sales finance agency to the fixed percentages of all collections should be absolute. Its right to one-fourth of the delinquency charges should, however, depend upon satisfactory performance. It should be within the power of the Federal Reserve Bank to limit any sales finance agency's share of the delinquency charges to the generally applicable collection commission if it persistently fails to follow up delinquencies or is chronically careless in the computation of delinquency charges.

Even if the compensation offered to sales finance agencies were unattractive, many would undoubtedly find it to their own interest to participate. When the war ends and production of consumers' durable goods is resumed, post-war delivery accounts subject to collection would be a principal source of sales finance business in the commodity fields covered by the plan. As the priority numbers of those whose payments had not been completed were reached, the agencies handling collections would naturally be the ones to finance the unpaid balance.

Commissions paid for bookkeeping and collections like those paid for sales would be taken directly from payment made by the purchaser and they would be subtracted from the amount paid in by him should he wish to withdraw funds prior to the time his priority number is called. Thereafter, these commissions would be covered by the payment which the Treasury would make for the use of the purchaser's money.

Work and compensation of the Federal Reserve Banks

The Federal Reserve Banks and their branches would have a number of functions under the plan.

At the outset they would select and assure the financial responsibility of sales finance agencies which would apply for authorization to participate in the plan. They would approve or disapprove local collection agencies which might be proposed by sales finance agencies. They would approve the contract form to be used by sales finance agencies, and they would print and sell payment books to them. The issuance of payment books by the Federal Reserve Banks would permit standardization of the form and content of the book, save printing costs, and facilitate control of the total liability of each sales finance agency. Payment books could be printed in blank and delivered to the sales finance agency for imprinting its name and its serial numbers, or arrangements could be made with the Federal Reserve Banks to include the name of the sales finance agency and its serial numbers when books are printed. The use of a separate set of serial numbers by each sales finance agency would facilitate the posting of payments.

The Federal Reserve Banks would receive periodically the funds collected by the sales finance agencies, less collection and bookkeeping commissions. They would credit these funds to a special post-war-delivery account in the name of the U. S. Treasury. They would audit the reports of the sales finance agencies and would forward summaries to the Federal Reserve Board.

When a Federal Reserve Bank receives the payment record of a purchaser who has completed his payments, it would examine the payment record, audit the calculation of delinquency charges and the priority assignment, check its files to prevent the purchaser from acquiring claims to more goods than he is entitled to, and issue a post-war-delivery certificate to the purchaser.

It will be noted that the dealer's secondary commission and the collection and bookkeeping commission proposed here have been expressed, for the sake of accounting simplicity, as percentages of instalment payments made by purchasers rather than as percentages of the total purchase price of certificates. These commissions do not apply to down-payments. Since the subtraction of down-payments from the rounded purchase price leaves odd amounts, the commissions resulting from the application of fixed percentages to these amounts are also odd. If, on the other hand, the same percentage rates were applied to the purchase price of certificates, the resulting commissions would be rounded figures.

It is convenient, therefore, to permit the Federal Reserve Banks to retain the difference between the amount withheld for dealers' and sales finance agencies' commissions and the amount that would result if the same commission rates were applied to the total purchase price. This is the same thing as saying that the Federal Reserve Banks should receive a percentage of down-payments equal to the percentage of instalment payments which dealers and sales finance agencies receive. This sum would range from 10 cents on \$100 certificates to 42 cents on \$2,000 certificates. Assuming that the average price of post-war-delivery certificates would be \$400, the revenue of the Federal Reserve Banks from this source would average 25 cents per certificate.

Since the time required to check the delinquency charges and the priority assignment before issuing a post-war-delivery certificate would depend in part upon the degree of delinquency, the Federal Reserve Bank

should also receive one-quarter of the delinquency charges. It is believed that these two types of revenues would provide adequate compensation for the "out of pocket" costs of the Federal Reserve Banks in fulfilling their obligations under the plan.

The Post-War-Delivery Corporation

It would probably prove desirable to create a ~~separate~~ corporate entity to enter into contracts with purchasers, sales finance agencies, local collection agencies, and other participants in the plan. Such a corporation, which should be controlled by the Federal Reserve Board, might well be called the Post-War-Delivery Corporation.

This corporation should receive an income which could be used to defray unforeseen expenses and to supplement the income of specific local collection agencies or other participants, if for one reason or another their commissions should prove inadequate to cover the costs of services essential to the operation of the plan. It is proposed that one-half of 1% of all payments of \$30 or more be transferred by the Federal Reserve Banks to the account of this corporation. This further payment out of the proceeds of collections would bring deductions for sales, collection and management expenses, exclusive of down-payments, to $3\frac{1}{2}\%$ of the cash value of all classes of certificates.

VI.

TREASURY PAYMENTS AND FEDERAL RESERVE BOARD
MANAGEMENT

Two government agencies would play important parts in the plan of instalment selling for post-war delivery. The United States Treasury would be expected to pay a part of the purchase price of each certificate for the use of the purchaser's money. The Federal Reserve Board would be expected to manage the operation of the plan.

Treasury payments

The Treasury would be asked to contribute to the cash value of each certificate a sum which would cover the commissions paid out to dealers, collection and bookkeeping agencies, Federal Reserve Banks, and the Post-war Delivery Corporation, provided that the certificate is held until its priority number has been called. In this way, the cash value of each certificate would equal its purchase price when it becomes valid for the delivery of goods. The Treasury's payment would be in lieu of interest for the use of the purchaser's money between the time the proceeds of each payment were credited to the Treasury's account with the Federal Reserve Bank and the time the paid-up certificate was presented for payment, following its exchange for goods.

If the schedule of commissions suggested here should be followed, the Treasury would be called upon to pay these amounts:

<u>Purchase Price of Certificate</u>	<u>Treasury Payments</u>	
	<u>Amount</u>	<u>Percent of Cash Value</u>
\$ 100	\$ 6.50	6.5
150	9.25	6.2
200	12.00	6.0
300	16.50	5.5
400	21.00	5.3
500	25.50	5.1
700	33.50	5.0
1,000	45.00	4.5
1,400	60.00	4.3
2,000	82.00	4.1

The payment by the Treasury of a fixed sum for the use of the purchaser's money means that the interest costs of funds raised through the sale of post-war-delivery certificates would vary with the length of the war and of the period that would be required to reestablish production of consumers' durable goods and to distribute an initial inventory to dealers. If the period between the initial instalment payment and the delivery of goods is short, the cost expressed as a rate of interest will be relatively high; but if the period is long, the interest cost will be low.

These variations, however, would appear to offer an advantageous hedge for the Treasury. If the war is short, the nation will be better able to absorb a relatively high interest cost. The longer the war, the more difficult will be the problem of financing government deficits and the more welcome a low interest rate.

Comparison with costs of war savings bonds

In order to compare the interest costs of funds raised through the sale of post-war-delivery certificates with the interest costs of funds

raised through the sale of war savings bonds, it is necessary to make assumptions concerning the length of the war and of the period that will be required to reestablish production and to distribute an initial inventory to dealers. It is impossible, of course, to make any accurate predictions concerning the duration of the war. There appears to be some degree of agreement as to the earliest possible date of its termination--that is, in the summer of 1944. But the probabilities seem to lie in the direction of a war of considerably longer duration.

Our calculations have been based on three assumptions concerning the date of termination of the war: (1) in July, 1944; (2) in February 1945; and (3) in January, 1947. In each case it has been assumed that sales of certificates will begin in January, 1945 and that retail deliveries will begin six months after the end of the war. It has also been assumed that certificate sales during the first month of operation of the plan would absorb the first month's production, that sales during the second month would absorb the second month's, and so on during the initial period to which these calculations pertain. Under these circumstances the Treasury would have the use of the funds for equal periods whether purchases were made in the first or fourth month. It should be remembered that the plan calls for a reduction of the Treasury's payment if this assumption should prove to be unrealistic.

The following figures compare the interest rates paid on Series E and G bonds with the interest cost of funds raised by post-war-delivery sales, subject to the schedule of commissions proposed here, under these three sets of assumptions:

<u>Purchase Price of Certificate</u>	<u>Interest Cost of War Bonds</u>		<u>Interest Cost of Funds Raised by Post-War-Delivery Sales</u>		
	<u>Series E</u>	<u>Series G</u>	<u>War Ends</u>	<u>War Ends</u>	<u>War Ends</u>
	<u>(Percent)</u>	<u>(Percent)</u>	<u>July 1944</u>	<u>Feb. 1945</u>	<u>Jan. 1947</u>
			<u>(Percent)</u>	<u>(Percent)</u>	<u>(Percent)</u>
\$100	2.9	2.5	4.41	3.20	1.67
150	2.9	2.5	4.34	3.12	1.61
200	2.9	2.5	4.34	3.10	1.58
300	2.9	2.5	4.14	2.91	1.46
400	2.9	2.5	4.20	2.90	1.42
500	2.9	2.5	4.34	2.94	1.41
700	2.9	2.5	4.23	2.82	1.33
1,000	2.9	2.5	4.12	2.71	1.26
1,400	2.9	2.5	4.05	2.63	1.22
2,000	2.9	2.5	4.02	2.59	1.03

This comparison suggests that if the war should end in February 1945 the interest cost of funds raised by the sale of post-war-delivery certificates would approximate the interest cost of funds raised through the sale of Series E bonds. If the war is shorter, the interest cost would be higher, and if the war is longer, the interest cost would be lower, than for Series E bonds. These figures, however, do not provide a fully accurate comparison. In actual practice, the true interest costs of post-war-delivery funds would be somewhat lower and the true interest costs of war-savings-bond funds would be substantially higher than the figures given above.

The calculated interest costs of post-war-delivery funds would be reduced by cancellations before maturity and by delinquency. The Treasury payment would accrue only when certificates were held until there priority numbers have been called. While this feature of the plan is designed to discourage withdrawals and to differentiate post-war purchases

from savings, it would also give the Treasury the use of some funds for which no compensation would be paid. True, a sacrifice of interest also accompanies the cancellation of war savings bonds. But the interest rate is not reduced to zero as is the case with post-war-delivery certificates. Delinquency would also reduce the average interest cost. Since the delinquency charges proposed here approximate 1 percent a month on delinquent payments, the payment of half of such charges to the Treasury would more than compensate for its loss of the use of delinquent funds.

Of considerably greater importance to the comparison is the fact that the interest calculations for post-war-delivery funds represent total costs after all operating expenses have been paid, while operating expenses must be added to the interest rates quoted for war savings bonds. Under the plan proposed here, the Treasury payment would be used solely to cover selling, collection, and administrative expenses. The commissions paid to dealers would provide the stimulus for sales. The commissions and fees paid to sales finance agencies, local collection agencies, and Federal Reserve Banks would provide compensation for the maintenance of detailed records, for the issuance of certificates, and for the channeling of funds in bulk to the Treasury's account.

In the sale of war savings bonds, on the other hand, the costs of selling and of collecting funds and accounting for them are in addition to the interest cost. These additional expenditures fall in part upon the

Treasury and in part upon the Post Office and private enterprises. The payroll, traveling expenses, advertising expenditures, and other operating expenses of the Treasury's War Savings Division are directly attributable to the cost of raising funds through the sale of war savings bonds. The expenses which the Post Office incurs in selling bonds or in handling franked promotional literature are equally attributable to such costs. Even the free services that private enterprises have devoted to the bond sales campaign are paid for in part by the Treasury through the loss of tax revenues. Free services rendered by individuals in the promotion of bond sales are expensive in terms of the diversion of manpower and they are likely to be less readily available as the labor shortage becomes more stringent.

Two other considerations need to be applied in comparing the interest costs of war savings bonds and post-war-delivery certificates.

First, in issuing Series E bonds, the Treasury contracts to pay \$33.33 per hundred for the use of funds for 10 years. In participating in the post-war-delivery plan under the commission schedules proposed here, the Treasury would pay from \$4.27 to \$6.95 per hundred for the use of accumulating monthly payments and, when payments have been completed, the full balance for the duration of the war and the subsequent period of preparation for retail distribution of the goods subject to sale. Disregarding the factors which distort these figures in favor of war savings bonds, the contracted payment for Series E bonds is five to eight times as great as the contracted payments for post-war-delivery certificates. If the war is long, the advantage to the Treasury of raising funds through the sale of post-war-delivery certificates is obvious. But if the war is short, the Treasury is in a position to refinance its obligation in a more favorable market.

When the war has ended and production of civilian goods has been fully restored, the inflationary danger of refinancing federal government obligations through financial institutions will have disappeared. There is little doubt that the Treasury could at that time refinance its obligations for post-war-delivery certificates for the remainder of the ten-year period at considerably less cost than the difference in the contracted payments.

Second, the plan of instalment selling for post-war-delivery would divert an additional volume of funds from the market for consumers' goods and services to the U. S. Treasury. If an accurate comparison is to be made, it is necessary to measure the costs of post-war-delivery funds not against the present average cost of war-savings-bond funds but against the still higher costs that would have to be incurred to raise an equivalent additional volume of funds through the sale of war savings bonds.

Taking all of these factors into consideration, it seems probable that, even if the war ends as quickly as the most optimistic forecasts would permit us to hope, the true costs to the Treasury of post-war-delivery funds under the schedule of commissions proposed here would probably be less than the costs of raising an equivalent additional volume of funds through the sale of war savings bonds. If the war is longer than this most optimistic minimum, sales of post-war-delivery certificates would become a progressively cheaper means of raising funds. The commissions proposed here, however, should not be taken as fixed. They are suggested only to illustrate the principles of the plan. It is possible that a more satisfactory schedule of commissions can be worked out.

Other advantages for the Treasury

The Treasury's interest in instalment sales for post-war delivery should, however, go far beyond their usefulness in raising funds at reasonable cost. Rising prices would add tremendously to the cost of the war. As fiscal agent for the federal government, the Treasury Department is vitally concerned with the maintenance of a stable price level. To the extent that additional purchasing power can be drained from the current market for goods through instalment sales for post-war delivery, the inflationary pressure will be relieved and the possibilities of maintaining the current price level will be substantially enhanced.

But there is still another aspect of the plan in which the Treasury has an enormous stake. As has already been pointed out, instalment selling for post-war delivery would create a reserve fund of purchasing power that can be poured into the post-war market. The economic effects of such an injection of purchasing power are similar to those of a deficit expenditure of equal magnitude by the federal government. The need for federal deficit spending as a stimulant during the period of transition to a peace-time economy may therefore be minimized by the release of post-war-delivery funds.

Measured by these standards, the ultimate saving to the Treasury through instalment selling for post-war delivery may indeed represent a substantial fraction of the principal amount raised by this device.

Administration of the Federal Reserve Board

The Board of Governors of The Federal Reserve System would appear to be the logical agency to undertake the job of administration. The

primary responsibility of the Board for credit and monetary management has been recognized by statute. A recent Executive Order also identifies the Board specifically with the field of consumer credit control, to which instalment selling for post-war delivery is intimately related. The semi-private character of the Federal Reserve System, its relative immunity from political pressures, and its decentralized system of administration through regional banks and their branches make the Board the ideal administrative agency for this purpose. Moreover, administration of the plan of instalment sales for post-war delivery can be done most efficiently and effectively when combined with the function of regulating consumer credit.

The Federal Reserve Board would be responsible for: (1) developing the forms and contracts to be used, and otherwise perfecting the details of the plan; (2) establishing standards for the selection of sales finance and local collection agencies; (3) issuing reports concerning post-war-delivery sales; (4) accounting to the Treasury for payments transmitted and certificates issued; (5) releasing goods covered by the plan by calling priority numbers.

When the rationing and price-control functions presently exercised by the Office of Price Administration and the War Production Board are discontinued, the Federal Reserve Board should have responsibility for issuing such special priority certificates as may appear to be in the public interest and fixing the maximum wholesale and retail price of goods covered by the plan where such price-fixing becomes necessary in order to prevent exploitation of post-war-delivery purchasers.

Administration planning and policy-making in connection with installment selling for post-war delivery would appear to be so closely related to the objectives of the Federal Reserve Board that these functions could be properly financed through its customary sources of revenue.

VII.

THE PROBLEM OF POST-WAR PRICES

One of the most difficult questions of operating detail is how to deal with the prices at which specific consumers' durable goods should be sold for post-war delivery. On one hand, there is the uncertainty concerning the level of production costs in the post-war period, and on the other hand there is the problem of how to assure competition with respect to price and quality in the face of a large prepaid demand that will tax productive facilities for a substantial period.

Advantages and disadvantages of selling at fixed prices

A number of important considerations suggest the desirability of providing for the sale of goods for post-war delivery at specific prices--for instance, the prices established for various types and models in 1940 or 1941, less the discount for prepayment. For one thing, this treatment would help to identify post-war-delivery transactions as sales of merchandise and to minimize their relationship to savings in the eyes of purchasers. For another thing, it would eliminate one of the variable elements in a plan which necessarily involves a number of such elements. Still further, it would appeal to those who might fear a substantial rise in prices. Purchases for post-war delivery at fixed prices would provide a hedge against inflation. But, unlike the hedge of putting money into current goods, which would accelerate the forces of inflation, purchases for post-war delivery would reduce the inflationary pressure by diverting purchasing power from the current market.

These advantages, however, are offset by a number of serious.

handicaps, which appear to be controlling. After extensive discussion and careful consideration of the pros and cons, it has seemed essential to avoid any attempt to sell goods at predetermined prices.

The most serious difficulty is that someone would have to take the risk of a substantial increase in the price-level. If manufacturers could reduce quality to compensate for increased costs, the purchaser would bear the risk and this would eliminate the principal advantages of selling at established prices. Manufacturers might be asked to guarantee delivery of goods of specified quality and thereby accept the risks of rising costs. It seems doubtful, however, that many would be willing to do so voluntarily and any attempt at compulsion would not only be difficult but would change completely the essential nature of the plan. The United States Treasury might also be asked to accept the risk of an increase in manufacturing costs. But the responsibility for action necessary to hold prices steady lies primarily with Congress and with the Office of Price Administration. The Treasury's authority in this field is limited. Lacking the power to assure a constant price level, the Treasury would undoubtedly object to underwriting the cost of production of tremendous quantities of goods.

Prospective changes in post-war products would also make it difficult to sell at established prices. Recent technological developments seem likely to revolutionize the post-war automobile and to have a substantial effect upon the construction and design of other consumers' durable goods. Consequently, the price for which pre-war models were sold might be utterly

inappropriate for post-war models. The possibility of great technological improvements and of substantially reduced costs might make consumers unwilling to buy specified models at established prices.

Use of post-war-delivery certificates

For these reasons the writer proposes that prices be kept flexible and that the instalment purchaser be offered certificates of various denominations, which can be exchanged for specific goods at prices to be established in the post-war period. The certificate denominations should correspond roughly with present price-classes for various goods. For instance, automobile certificates might be issued in \$700, \$1,000, \$1,400, and \$2,000 denominations; piano and automatic heating equipment certificates in \$200, \$300, \$400, and \$500 denominations; refrigerators in \$100, \$150, and \$200 denominations.

Certificates should be identified so far as possible with specific kinds of goods or with groups of specific kinds of goods. Thus, an automobile certificate should be valid only for the purchase of an automobile, and a refrigerator certificate should be valid only for a refrigerator. Certificates should also be identified with price-classes of goods. For instance, a \$700 automobile certificate should be valid only for the lowest price-class of cars, typified today by Plymouths, Chevrolets, and Fords; \$1,000 and \$1,400 certificates should be valid respectively for the next highest price-classes, typified today by Mercurys, Dodges, Pontiacs, and low-priced Buicks and

Chryslers, and \$2,000 certificates would be valid for the most expensive cars. Such an arrangement seems to be necessary in order to prevent those who want high-priced cars from acquiring a priority to them by purchasing a certificate of the lowest denomination.

Some degree of flexibility, however, seems to be important because the circumstances of many purchasers are bound to change. Some who now foresee the need for an inexpensive car will later want an expensive one, and some who believe they will want an expensive car will not be able to afford it when the time comes to take delivery. Also some who purchased an automobile certificate will want an oil-burner instead, and some who bought a piano certificate will later want an automobile.

There would seem to be no reason to prevent exchanges of certificates, provided that adequate measurements of the accumulated demand for various products and of the number of purchasers in each priority and price class can be maintained; and provided further that casual changes of mind were restrained by priority penalties and that costs of exchanges were met by fees. The Federal Reserve Banks might therefore be authorized to exchange certificates generally for a fee of \$1 and for a deferment of the priority number by 2. Each certificate might be made exchangeable for a certificate of equal value calling for delivery of another commodity. Certificates of larger denominations might be exchangeable for two or more certificates for different commodities or for a certificate of lower denomination and cash. A certificate of low denomination might be also traded in on a certificate of larger denomination upon the payment:

in cash of the difference between their cash values. The latter transaction, however, should require a larger penalty in the form of priority deferment.

The existence of large numbers of prepaid purchase certificates of various denominations will undoubtedly lead manufacturers generally to fit their products to the price classes established by certificate denominations. This will follow traditional practice since the design, material content, and construction of various consumers' durables have always been strongly influenced by the views of sales departments as to the price at which various products can be sold with the least resistance. Nevertheless, it is impossible to expect that all goods will be priced exactly at certificate values. For many types of commodities, model variations requiring price differentials will undoubtedly be more numerous than the certificate denominations. Also, freight charges will compel differences in price in various areas. It seems necessary therefore to include in the plan some method of dealing with differences between prices and certificate values.

Where post-war prices for individual commodities are higher than the values of certificates for their purchase, the situation can be handled very simply by the payment of the balance by the purchaser at the time of delivery either in cash or through a sales finance agency. Where certificate values are higher than post-war prices of the goods which they command, the purchaser should be entitled to a cash rebate. Since commissions for selling and collection will have been paid out of the proceeds of the instalment sale, rebate should bear the same relationship to the excess value of the certificate

as the cash value of the certificate bears to its merchandise value.

Some dealers would undoubtedly prefer to encourage the purchaser to spend the remainder of the face value of his certificate for merchandise. There would seem to be no reason for preventing this, provided that the purchaser has the option of taking the cash rebate.

Post-war price competition

Since the plan of instalment selling for post-war delivery contemplates the sale of "futures" by dealers who have heretofore sold the same products and the reenforcement of these selling efforts through national advertising by manufacturers, it is tempting to propose that Ford dealers should sell Fords, Studebaker dealers should sell Studebakers, General Electric dealers should sell General Electric refrigerators, etc. This would obviously increase the interest of dealers and manufacturers in maximizing the number of deferred delivery sales. However, the effects of such an arrangement on the post-war market seem to outweigh substantially any advantages which might be gained.

In the first place, it would undoubtedly tend to cut down substantially the number of enterprises which could enter the post-war market. Manufacturers who might, by virtue of their war production experience, want to turn to the field of consumers' durable goods would lack a market for their production. Also the competitive position of small independent enterprises would probably be injured. Many purchasers, who would prefer the goods of small independent manufacturers if they could wait until the goods were delivered before making a choice, would probably feel impelled to buy

the products of large and well-established manufacturers if a choice had to be made at the time of entering an instalment contract for post-war delivery.

In the second place, it would seriously restrict post-war price competition if individual manufacturers were presented in the post-war period with prepaid orders which would absorb their productive capacity for a long time and which could be cancelled only with substantial sacrifice to purchasers. There would be no competitive pressure toward minimizing prices and maximizing quality. And in the absence of effective price competition, the Federal government would undoubtedly be compelled to fix prices--a recourse which the writer would like to avoid if possible.

For these reasons it seems desirable to sell certificates for automobiles and refrigerators and other consumers' durable goods of certain price classes and to permit the purchaser to choose the make and specific model at time of delivery. Since there would be a strong tendency for the purchaser to take delivery from the dealer who originally sold the certificate, individual dealers would still have an important stake in the sale, apart from their immediate compensation. But the preference for the original dealer and the make which he handles would hold only where the product competed favorably with other products with respect both to price and to quality. Business would certainly flow to the dealer and manufacturer who offered superior values.

Each industry as a whole would of course be in somewhat the same position as an individual manufacturer with guaranteed orders. But the effects upon price competition are far different when it is the industry rather than the individual enterprise that has the orders. The priority scheme would

provide the means of limiting demand at any one time to the available supply. This would prevent run-away prices and assure a considerable degree of price competition among individual dealers and manufacturers. In fact, the intensity of price competition can be determined by the Federal Reserve Board through its policy in timing its calls of priority numbers. It is true that shifts to the more popular makes would be restrained by the fact that certificate holders whose priority numbers had been called would have to wait longer to get delivery of products that were in greatest demand. But a situation in which certificate holders were willing to wait a month or two after their priority numbers had been called to obtain the best "buy" would exert strong competitive pressure for price readjustments by other manufacturers. Sales of products which failed to compete would be slowed down with respect to production schedules, with consequent increases in costs of production, storage, and inventory financing. Also, the manufacturer would lose prestige, which is always a substantial factor in competition in the consumer durable goods field.

The offer of a prior claim to post-war production to those who buy post-war-delivery certificates also raises a number of difficult questions. What kinds of goods lend themselves most readily to priority control? How far can we afford to go in giving those who hold post-war-delivery certificates the right to acquire goods ahead of those who need such goods for the performance of essential services? What can be done to prevent the priority scheme from penalizing those in the military services? What can be done to prevent speculators from acquiring priorities to large quantities of goods for resale at excessive prices? How can uncompleted contracts be assigned priorities?

Selection of goods for post-war-delivery sale

As has already been indicated, only goods which are no longer available should be selected for post-war-delivery sale. Most consumers would probably be unwilling to purchase post-war-delivery certificates for goods that can be bought freely in the current market. This is partly because the appeal of present goods is stronger than the appeal of future goods of the same type, and partly because the offer of priorities would be an empty gesture when there is no prospect of a large unsatisfied demand for the goods subject to sale.

Two other criteria for selecting goods for the post-war-delivery sale have been suggested or implied in the preceding sections. One of these is a relatively high price. Because the ratio of selling costs to

certificate values increases as the denomination of the certificate declines, it is desirable to limit post-war-delivery sales to goods of substantial value. The other is general consumer acceptance. The more important the place a particular article has in the consumption pattern and the more general the knowledge of its usefulness and performance, the easier it will be to sell post-war-delivery certificates for that article.

But there is an equally important criterion that has yet to be discussed; i.e., the applicability of priorities to the distribution of the commodity. Several characteristics play an important role in determining whether specific goods lend themselves readily to priorities control.

First, the goods subjected to priority control, however important in the pattern of consumption, should not be necessities of life. For instance, even if food met all the other standards for post-war-delivery sale, it would scarcely be feasible to exclude those who failed to buy certificates from post-war food markets. This requirement is met automatically, however, if the plan is applied only to goods whose production has been discontinued for the duration of the war.

Second, there should be reason to anticipate an excessive post-war demand in relation to immediate productive capacity. Unless there is such a prospect, there is little point to the priority device. The fact that civilian goods will not be available for the period of the war does not necessarily assure a post-war shortage of those goods. For instance, even though airplanes cannot now be purchased for ordinary civilian use and the post-war

demand will undoubtedly be large, the ready convertability of our enormously expanded facilities for producing military transport and training planes can be expected to assure an adequate supply to meet civilian demand.

Third, the goods should be produced by a relatively few manufacturers. This would not only facilitate the enforcement of priorities in the post-war period but would increase the benefits that would accrue to each manufacturer from a large volume of prepaid orders for specific types of goods.

Fourth, the goods should be such that large-scale production and a considerable capital investment are necessary. It would be exceedingly difficult to enforce the control of priorities for goods which could be produced readily by a small-scale assembly operation, or in an ordinary foundry, sheet-metal shop, or electrical repair shop. Moreover, it would appear to be undesirable from an economic and social standpoint to prevent the expansion of small-scale production of such goods.

It is with these considerations in mind that the recommendation has been made to limit the application of the plan at the outset to automobiles, refrigerators, pianos, oil burners, and automatic stokers. These goods meet all of the standards for post-war-delivery sale. They are no longer generally available to the public and post-war demand for them is likely to exceed productive capacity for considerable periods of time. Their prices are relatively high; even the lowest price-classes of refrigerators and pianos can properly be covered by \$100 certificates. They require large-scale, capital-intensive production and they have been produced in the recent past by a relatively

small number of manufacturers. Although these goods are well-established in the consumption pattern, they are not necessities. There will be used cars, used refrigerators and used pianos on the market for those who cannot get along without these articles, and hand-fired furnaces can serve the purpose of those who fail to acquire post-war-delivery certificates for automatic equipment.

These goods should represent only the beginning. It would be unfortunate if the plan were not progressively extended to other goods and services which fall short of the ideal standards. Careful examination of the problems that would be created in each field by the application of instalment selling for post-war-delivery would undoubtedly indicate solutions if the full cooperation of the trades concerned can be obtained.

There are a number of types of consumers' durable goods that meet the standards in all respects but price. Among these are washing machines and dryers, suction cleaners, household sewing machines, radios and phonographs, cameras, and household motion-picture projectors. Although many models of these goods have been priced too low to be readily adaptable to post-war-delivery sale, the prices of other models have approached or exceeded \$100. It might be possible therefore to subject only the deluxe models to post-war-delivery sale. These would probably be the models which would appeal most strongly to post-war-delivery purchasers. If necessary, certificates could be sold in denominations of \$70.

If such a segregation by price-classes should be found to be practicable, a number of additional fields would be opened. The principal

shortcomings of stoves, ranges, and water-heaters for post-war-delivery sale are (1) the low prices of the cheaper models, (2) the fact that they may be necessities under some circumstances, and (3) the ease with which certain types could be produced by handicraft production. However, all of these handicaps would be removed if priorities were applicable only to deluxe models and the cheaper and less desirable models could be bought in the open market. Studies of the post-war market have indicated that many housewives have their eyes firmly fixed upon durable water-heaters, made of copper or nickel alloys, and upon streamlined cooking ranges, done in colors or light metals with all the up-to-date gadgets.

Still another group of consumers' durable goods meets all the standards except that of widespread consumer acceptance. In this group are electric dishwashers, home air-conditioning systems, and television sets. While electric dishwashers have been on the market for a long time, and many are in use, the general public has never been fully convinced of their practicability. Few consumers have had an opportunity to try out a modern television set or to appraise its worth in terms of the price asked. Home air-conditioning systems, while no longer a novelty, have not been installed on a considerable scale.

It would be an important contribution to post-war employment if a large market for these goods could be developed through sales of post-war-delivery certificates. The potentialities of television are enormous but the development of this field has been prevented by the lack of receiving sets in

the hands of the public, on one hand, and the rapid obsolescence of expensive sending equipment on the other. These obsolescence charges can be borne only if there is a large receiving audience. For electric dishwashers and home air-conditioning systems, an enlargement of the market would permit price reductions, which in turn would further enlarge the market. Thus post-war-delivery sales, by creating a large volume of prepaid orders, may be the key to unlock the mass market for these goods.

The job of selling such goods on a large scale would be difficult but not in the least impossible. Sales of television sets in particular would challenge the ingenuity of the marketing profession. But if manufacturers of unquestioned integrity and technical competence offered to produce a television set that would meet certain standards of performance, and if the broadcasting companies announced their intention to televise programs as soon as sending equipment could be had, a well-organized campaign should offer real hope of success. In order to minimize the natural "show-me-first-your-wares" reaction, it might be desirable to sell certificates that would be valid either for a television receiving set or for a fine radio-phonograph combination. In appraising the adaptability of such goods to post-war-delivery sales, it should be remembered that millions of wage-earners are now receiving far larger incomes than ever before and the goods upon which these incomes would normally be spent are no longer available. Under these circumstances, intensive sales efforts are likely to produce substantial results in fields that would normally be barren.

Some services would also be susceptible to post-war-delivery sales if modifications are made in the priority scheme. For instance, pleasure cruises and foreign travel, which had widespread consumer acceptance before the war, have been virtually eliminated by the war. The American people, restricted in their movements by automobile, gasoline, and tire rationing and weary of wartime shortages, can be expected when the war ends to be hungry for the freedom and luxury of cruise ships, and cabin space is likely to be in great demand. It should be possible for travel agencies, among the first business casualties of the war, to sell post-war-delivery certificates for cruises and trans-Atlantic and trans-Pacific passages. Foreign travel by air might also be sold for post-war-delivery. If railroad travel should be restricted, all-expense trans-continental tours might well be covered also.

Priorities would create the major problem in applying the plan to transportation services. It would obviously be impractical to prevent those who failed to purchase post-war-delivery certificates from undertaking necessary business travel. This difficulty might be avoided, however, by reserving sections of ships or specific ships on certain runs for certificate holders, or by reserving only the most desirable accommodations in luxury trains and in transport planes.

Army jeeps could also be sold very readily for post-war delivery. Soldiers who have driven them have frequently expressed the wish to own one after the war, and many civilians have had their fancy caught by their small size, efficiency, and rough and tumble quality. When the war ends there will

undoubtedly be many thousands of jeeps in good condition for which the Army will have no further use and it can be expected that these will be offered for sale. The liquidation of military vehicles at that time, however, would have had economic effects since expenditures for them would not create additional income. This unfortunate consequence would be avoided to the extent that they could be sold now and their purchase price collected out of current incomes.

Residential houses are by far the most important type of consumers' durable goods and the potentialities of their sale for post-war delivery, both from the standpoint of current deflationary effects and from the standpoint of peace-time reconstruction are enormous. The difficulties of applying the plan, however, are also great.

The problems that would arise out of the application of priorities would constitute the primary handicap. Production of houses is localized, and it would be highly unlikely that certificate sales would be distributed in accordance with construction facilities in each community. Consequently, if priority controls were exercised on a nation-wide basis, there would be a shortage of supply in relation to certificate demand in some places and an excess of supply, with resulting unemployment in the building trades, in other communities. Moreover, even if priority numbers were called in relation to the demand-supply situation in each locality--a policy which would be exceedingly difficult to administer--control would be virtually impossible because of the large number of small builders and the difficulty of establishing standard prices for non-standard goods.

If prefabricated houses should be offered by a few manufacturers, these problems would be avoided. Post-war-delivery sales of such houses would fit nicely into the plan proposed here. For homes that are to be built locally, however, it would appear to be necessary to eliminate the priority feature. While priorities to post-war production appear to be essential at the outset to stimulate widespread public participation in the plan, it may be possible, once consumers have been educated to such purchases, to eliminate the offer of priorities in order to cover goods which do not lend themselves readily to priority control.

Goods needed for essential services

Instalment selling for post-war delivery should be limited, of course, to goods that are designed primarily for household or personal use. The field of producers' goods should be avoided. This means that passenger cars should be included, while trucks and busses should be excluded from the plan; that refrigerators of the sizes commonly used by households should be included, and the sizes commonly used in hotels, restaurants and butcher shops should be excluded; that oil burners and automatic stokers designed for private homes should be included and those designed for theatres, apartment houses, business buildings and factories should be excluded. The need to distinguish consumer goods from goods of the same class that are used predominantly for business purposes has arisen in connection with the regulation of consumer credit and the precedents established by the Federal Reserve Board for this purpose will be helpful in defining the field of post-war-delivery sales.

Even after the exclusion of goods specifically designed for business use, however, there is still the problem of an overlap. For instance, passenger automobiles of the types generally used for personal and family transportation are also used by police and fire departments, by physicians, by public utility companies for inspection, repair and collection services, by manufacturers and wholesalers for the transportation of salesmen, etc. Hotel rooms may be equipped with radios that are commonly used for household purposes, and refrigerators of household sizes may be purchased in quantity for use in apartment houses.

No matter how essential the services which they render, there would appear to be no reason to exclude any group from the operation of the priority system, provided that purchases of certificates were feasible for that group and the objectives of the plan would be served by compelling them to acquire priorities in this way. For instance, physicians could purchase automobiles for post-war-delivery just as readily as those who wanted cars for purely personal use; and the economic effects of advance purchases by physicians could be expected to be generally similar to those of purchases by ultimate consumers. The same thing would hold true for other professional people, for farmers and for small business men. Most of them use passenger automobiles both for business and personal purposes. To exclude them not only would be unfair to those who were compelled to pay in advance in order to assure prompt delivery, but also would minimize the deflationary effects of the plan, since professional people, farmers and small business men, as well as ultimate consumers, are likely to threat their instalment payments as

current expenditures.

When we come to large business enterprises, the situation is somewhat different. These enterprises, with their advanced accounting systems, would undoubtedly treat post-war-delivery payments as capital investments. Consequently, unless shortages of cash compel restriction of other expenditures in order to provide funds for instalment payments, certificate purchases by this group would not be deflationary. Nevertheless, because of the difficulty of distinguishing between productive and consumptive uses of goods in the professional, agricultural and small business fields, it seems desirable to require participation in the plan by all business enterprises which may wish to obtain prompt delivery of goods subject to post-war-delivery sale.

There is even greater reason for subjecting purchases by public agencies to the requirements of the plan. The accounts of states, counties, and municipalities are generally kept on a cash, rather than on an accrual, basis. There is usually an effort to keep current expenditures within tax revenues. Large capital outlays are generally financed by specific bond issues, but purchases of automobiles and other consumers' durable goods are likely to be treated as current expenditures. For this reason, instalment purchases for post-war delivery by government agencies would undoubtedly have a deflationary effect.

Some exceptions, however, must be made. New businesses will be needed to stimulate private employment in the post-war period, and their development should not be retarded by their inability to buy necessary equipment. For some types of enterprises, automobile priorities might prove to be

a serious handicap. Also the construction of apartment houses, the need for which cannot be accurately foreseen, should not be prevented by the inability of builders to equip them with refrigerators.

The right to exempt purchasers from the priorities system should rest with the Federal Reserve Board. So long as the Office of Price Administration and its local War Price and Rationing Boards remain in existence, the Federal Reserve Board might well establish general rules for exceptions and delegate administration to OPA and the Boards. Thereafter, the Federal Reserve Banks might well become the administrative agency.

Two tests for exemption suggest themselves: (1) the importance to the community of the use to which the goods would be put; and (2) the inability of the applicant to foresee the need for the goods and to provide for them by buying post-war-delivery certificates. Naturally those permitted to acquire goods without certificates would not be entitled to a discount.

Protecting the military forces

It would be unfortunate indeed if post-war-delivery sales operated to give civilians an advantage over the military forces in post-war markets for consumers' goods. But there is no reason why this should be so.

Soldiers, sailors, and marines could, of course, enter instalment purchase contracts like anyone else. The principal handicap to their participation lies in the fact that their incomes are generally lower than those of comparable civilians. This disadvantage, however, can be overcome by offering the military forces long-term contracts, by making sales through personnel

officers, chaplains, the Red Cross, and the U.S.O., and by making collections through payroll deductions.

By reducing monthly payments for the uniformed services to half the payments required of civilians, goods subject to post-war-delivery sale could be brought within ready reach of those in the lowest salary grades. The avoidance of commissions for sales and collections would eliminate down payments and give certificates a cash value equal at all times to the full amount paid in. This would permit military personnel to buy certificates at lower prices than civilians. Treasury payments should be reduced to $1/3$ of the amount payable on civilian certificates to compensate for the smaller amounts available to the Treasury. But these payments would be added to the amount paid in by the purchaser in determining the cash value of military certificates upon maturity. After adding the Treasury payment, the merchandise value of these certificates would be increased by ten per cent. The military forces would therefore get a better deal than civilians.

So far as the battle against inflation is concerned, it is just as useful to divert purchasing power of military personnel from the current market for goods as to do the same thing for civilians. The matter has become more important since the recent increase in the base-pay of the various fighting services. This increase has not only added substantially to their purchasing power, but has provided a surplus beyond the traditional standard of expenditures of men in the ranks, from which savings can be drawn without hardship. Since the great majority of enlisted men have no dependents, the additional funds are likely to be reflected to a considerable extent in larger

expenditures of doubtful social value. It would probably be a boon to those interested in morale and discipline, as well as to the men themselves, to have a plan which would encourage the withholding of part of their pay for goods that they can enjoy in the post-war period.

Because of the difficulty of reaching quickly military men in foreign service, such men should be entitled to the lowest priority number if they enter instalment contracts any time within six months of the initiation of the plan. It would seem proper also to give all men in the fighting services an edge over civilians by distinguishing their priority number as 1A, 2A, etc., as compared with B, 2B, etc., for civilians. This would also permit a more refined adjustment between demand and supply by the administrative agency.

Preventing speculation

It seems desirable to discourage the purchase of post-war-delivery certificates for the purpose of resale of the goods when production is resumed. Without such restraint there might readily be a large initial rush of instalment purchases by business enterprises or individual investors in anticipation of the resale of goods to non-certificate holders at a substantial profit in the post-war period. This would risk giving a limited number of individuals a monopolistic position in the post-war free market for goods subject to priorities. It would also minimize the economic objectives of the plan, since such large-scale purchases, even though paid by instalments, would undoubtedly be treated as investments to be financed out of capital accumulations

rather than as an expenditure to be paid out of current income.

The best means of preventing purchases for resale would appear to be to limit the number of post-war-delivery certificates which could be issued to any one person or corporation. Each person or corporation should be able to buy only one priority certificate for each type of goods covered by the plan or one priority certificate for each such article owned by him at the time of entering the purchase contract. Since the assignment of priority numbers would be controlled by the Federal Reserve Banks after the installment payment contract had been completed, the risks of discovery and of loss of priority would probably prevent attempts to acquire priorities to large numbers of cars.

The limitation of purchases to the number of articles now owned seems to be the most effective way of dealing with business enterprises which might want to buy certificates to replace their passenger car fleets or with landlords who might want to buy certificates to replace refrigerators, stoves, and other household appliances in dwellings owned by them. While the policy of permitting those who own a number of pleasure cars to acquire an equal number of priorities might be questioned, the number of such buyers is not likely to be large and the administrative difficulties inherent in any effort to distinguish between business and personal uses would seem to outweigh the desirability of a further limitation on purchases by those who own several cars for purely personal use.

It has been previously suggested that priority certificates should

be non-assignable. This seems important not only to prevent borrowing against the collateral value of the certificate, which would minimize the economic effects of the purchase but also to prevent the acquisition of certificates by speculators. Once instalment payments had been completed and priority numbers had been assigned, it would be difficult to prevent speculators from buying up certificates if they were then freely assignable.

On the other hand, there would appear to be no reason to prevent the resale of goods subject to purchase, even if it were feasible to do so. People's circumstances change. In the post-war period, some certificate holders will no longer want the goods to which they have claims while other persons who failed to purchase certificates will want the goods that others command. It would be both foolhardy and unnecessary to try to keep buyers and sellers apart at this point. When goods are ready for delivery, the person who has acquired a claim to them through foresight and thrift should be able to sell at a profit to any person who then wants the goods more than the original buyer. It would appear therefore to be only a matter of practical convenience to permit free negotiability of certificates after their priority numbers have been called.

By deferring the negotiability of certificates until their validation for purchase, it seems likely that the development of large speculative holdings can be avoided and unconscionable resale prices can be prevented. Instead of a concentration of free-market goods in the hands of a relatively few enterprises, there are likely to be large numbers of persons ready to

give up their claims for a modest profit. Moreover, the full economic advantages of the plan would by that time have been assured.

Treatment of incomplete payments

The plan of instalment selling for post-war delivery contemplates the assignment of priority numbers after the last payment has been made. When the war ends, new post-war-delivery sales would be stopped; but payments on existing contracts would be continued. By the time production has been resumed and stocks of goods have become available for retail distribution, millions of paid-up certificates bearing appropriate priority numbers would presumably have been issued. As early priority numbers are called and certificates are exchanged for goods, it could be expected that payments would be completed on other contracts and additional paid-up certificates would be issued. Consequently, instalment contracts subject to payment when the war ends would generally have been completed before goods have become available for delivery to these purchasers.

But these expectations would not be realized under all circumstances. Since payment schedules on some civilian certificates would extend for as long as 24 months, it is fully conceivable that civilian production might be resumed before the final payment was due on any contract for the purchase of such certificates. A similar situation could arise if certificate sales were small in relation to production capacity. In the latter case paid-up certificates might be exhausted before payments had been completed on all contracts.

More important is the situation of military purchasers, where payments would be spread over a longer period than those of civilians. Even though an ample number of civilian certificates should be available to absorb production, members of the military forces whose payments had not yet been completed would be entitled to the same priority as civilian certificate-holders who entered instalment purchase contracts during the same month.

For these reasons, it is necessary to provide for the issuance of certificates and the assignment of priority numbers to purchasers whose payments have not been completed.

It is proposed that whenever the number of paid-up certificates is expected to be inadequate to absorb production, the Federal Reserve Board should direct the Federal Reserve Banks to instruct sales finance agencies to forward accounts subject to payment for the issuance of certificates and priority numbers and to notify purchasers to discontinue payments after a certain date. Accounts would be called in order of the month in which instalment contracts were entered into. The purchaser would receive a partial-payment certificate having a cash value equal to the amount of his payments, less accrued delinquency charges, and a merchandise value ten percent greater than its cash value. Priority numbers would be assigned in the same way as paid-up certificates. The partial-payment certificate would, therefore provide the same priority to goods as paid-up certificate, but its cash and merchandise value would be less than those of paid-up certificates. Differences between the merchandise value of partial-payment certificates and the

purchase price of goods for which they are exchanged would be settled by cash payments or by credit arrangements.

It is proposed also that military accounts be closed upon the discharge of the purchaser from the military forces. Payment records would be forwarded to the Federal Reserve Banks for the issuance of partial-payment certificates. Those who remain in the military forces and continue their payments should be notified whenever the Federal Reserve Board anticipates calling priority numbers to which they would be entitled by virtue of the date of entering their contracts. They should be given the choice of completing their payments or of obtaining partial-payment certificates.

MECHANICS OF THE PLAN IN OPERATION

All the essential elements in the plan of instalment selling for post-war delivery have now been described. Only minor operating details have yet to be added. Consequently, it seems desirable at this point to complete the picture of the mechanics of the plan by showing how it would work in practice.

Let us undertake first to describe chronologically in generalized terms the various steps involved in purchasing goods for post-war delivery and then to follow a typical transaction through from application to delivery, for each of the various participants.

Instalment contracts

The first step in the plan is the signing of an instalment contract for a post-war-delivery certificate. The initiative may come either from the purchaser or from a dealer. Since the plan should be put into effect with as much publicity as possible, many prospective purchasers can be expected to apply to dealers from whom they have previously made purchases. After the first rush of such applicants is over, however, contracts are more likely to arise as the result of solicitation by dealers and their salesmen.

Instalment contracts should be made in duplicate on forms supplied to dealers by authorized sales finance agencies. The forms should conform to a standard prescribed by the Federal Reserve Board. The dealer should have

the right to choose the sales finance agency with which he prefers to deal. Thus, an automobile dealer selling General Motors cars might choose to do business with the General Motors Acceptance Corporation, another sales finance company, or with a local bank, provided that each of these institutions had qualified with the district Federal Reserve Bank.

The contract form should give the name of the agency which issued it. It should provide space for recording the date, the name and address of the dealer, the name and business and home address of the purchaser, the name and address of a beneficiary and of a contingent beneficiary, to whom the certificate would revert in case of death. It should indicate the kind and denomination of certificate subject to purchase and the date when the purchaser wished his payments to come due, i.e., the 10th, 20th, or 30th of each month. Each purchaser should be required to state that he wishes to buy the goods for use and not for resale, and he should be asked whether he has entered a previous contract for the same kind of certificate.

A separate contract should be made for each type of goods. But if the purchaser wishes to buy several automobiles or refrigerators or pianos, these should be covered by a single contract. In such cases, the applicant should be required to state the number of such goods which he presently owns and the use to which they are put.

At the time of executing the contract, the purchaser would make a down-payment, varying with the denomination of the certificate, and get a receipt from the dealer. The dealer would keep the down-payment as his initial sales commission, acknowledge its receipt on the contract form, and

send the original copy of the contract to the sales finance agency.

Contracts would be forwarded by the sales finance agencies to the Federal Reserve Banks, where they would serve four purposes. First, they would provide statistical information concerning the number of various types of post-war-delivery contracts that had been executed. Periodic publication of totals by types of goods and by areas would be likely to stimulate further purchases, since it would remind those who had not entered such contracts of the growing number of prior claims to post-war goods. Second, they would reveal purchases from several dealers, thereby preventing multiple buying for speculative purposes. Third, they would provide protection against defalcations by sales finance agencies. Knowledge of the number and value of accounts subject to collection would permit the Federal Reserve Bank to assure that the amount of the bond or of escrow securities is sufficient to cover the liability of each sales finance agency. Transmission of contracts could be enforced by limiting the initial quantity of payment books furnished to sales finance agencies and by sending additional books only as contracts are received. Fourth, they could be used to test collections. If receipts from any sales finance agency should fall substantially below anticipations based on its contracts, the issuing agency may either be withholding funds or failing to follow up delinquencies. In either case, action by the Federal Reserve Bank would be called for.

Collections and transfers of funds

The sales finance agency that receives the contract from the dealer

would issue a payment book to the purchaser and open a ledger account for him. Payment books should be printed for each kind and denomination of certificate. They should indicate the dates when payments are due and contain coupons showing the amount of each payment. They should give the names of local collection agencies to which cash payment can be made and the name of the sales finance agency to which ^{mail} payments can be made only through the mail. The sales finance agency would send the payment book to the dealer for delivery to the purchaser.

If payments are made in cash, the purchaser would take his payment book and cash or a check for the payment to one of the local collection agencies named in the payment book. The cashier would accept the payment, stamp the date on the coupon and stub, initial the stub, and tear out the coupon. The local collection agency would record the serial numbers and forward the coupons to the sales finance agency with its check for the total value of coupons received, less collection fees. The coupons would then be used by the issuing agency to post to customers' accounts. If payments are made by mail or money order, the coupon should be mailed to the sales finance agency with a check or money order for the payment. Acknowledgment of such payments could be made on a penny postcard.

Sales finance agencies would maintain a ledger account for each purchaser. They would send delinquent notices to purchasers whose payments were two weeks past due. A second notice calling attention to the provision of the contract for delinquency charges and for the deferment of priorities

should be sent two weeks later. If payment has not been received by the end of a further two-weeks period, the account should be referred to the dealer for further sales effort. It might be desirable to provide a means of adjusting contracts to lower certificate values wherever purchasers find themselves unable to keep up their payments.

Local collection agencies would transfer funds and coupons to issuing agencies weekly. Presumably each local collection agency would deal with a number of sales finance agencies. Consequently, in preparing their weekly reports, coupons should be sorted and serial numbers listed by the name of the sales finance agency stamped or printed on the back.

Each sales finance agency should report monthly to its Federal Reserve Bank or branch, showing the total amount payable that month on various types of certificates, the amount of payments collected, and the amount of commissions withheld by it for its own account and for the account of local collection agencies and dealers. When instalment contracts have been completed, the sales finance agency would also report the amount of delinquency charges collected and the amount withheld for commissions. A check for the amount collected less commissions withheld should accompany the report.

The Federal Reserve Banks would credit receipts from sales finance agencies, less their own commissions, to a special post-war-delivery account in the name of the United States Treasury. The Banks would send notices of credits to that account to the appropriate officials of the Treasury Department. They should report monthly to the Federal Reserve Board, giving

summaries of the monthly reports of sales finance agencies and showing the amount credited to the account of the Treasury during the month.

When payments have been completed on any instalment contract, the sales finance agency would calculate the number of delinquent payment days. If total delinquency does not exceed the grace period allowed, the card should be marked with the priority number appropriate to the date of entry into the instalment purchase contract and sent to the Federal Reserve Bank or branch. If delinquency exceeds the grace period, the sales finance agency would compute the delinquency charges and notify the purchaser that they must be paid before a certificate can be issued. When the delinquency charges have been paid, the sales finance agency would send the card with a deferred priority assignment to the Federal Reserve Bank. The dealer's secondary commissions would be paid periodically or upon completion of each instalment contract.

Upon receiving the ledger card the Federal Reserve Bank should check the calculations of delinquency charges and the priority number. If the delinquency charges were inaccurately calculated by more than 10 cents, the sales finance agency should be required to make appropriate adjustments with the purchaser. If the delinquency charges and priority assignments are accurate, the Federal Reserve Bank would issue a post-war-delivery certificate showing the kind of goods subject to purchase, the denomination of the certificate, and the name and address of the purchaser and his contingent beneficiaries. The certificate should indicate its cash value before and after its priority number had been called. A manufacturer's credit coupon

should be attached to the certificate.

The certificate would then be sent to the dealer for delivery to the purchaser. The dealer should require the purchaser to sign the certificate so that his counter-signature can be compared before goods are delivered when the certificate is presented in exchange for goods.

Delivery of goods

When production is resumed in the post-war period the Federal Reserve Board would authorize the shipment to dealers of initial inventories of goods subject to priorities in accordance with any scheme proposed by manufacturers which appears equitable. The method of distributing inventories should, however, take into consideration the geographical distribution of post-war-delivery certificates and the time required for transportation from the point of production. After the initial inventory has been distributed, further shipments from factories to dealers should be permitted only to replace goods delivered on post-war-delivery certificates.

As soon as an initial inventory, somewhat larger than the number of holders of priority number 1, has reached dealers in all parts of the country, the Federal Reserve Board would declare certificates bearing priority number 1 to be valid for obtaining delivery. If the number of such priority certificates should be exceptionally large, the class could be divided by calling only number 1A certificates, i.e., those sold to men in the military forces. The next priority number should not be called until additional factory production had equaled the total number of certificates bearing that priority

number. Thereafter, the calling of successive priority numbers for various types of goods should be determined by the volume of production and by the number of certificates bearing those priority numbers in each field. Allowance should be made for those who will postpone taking delivery of goods even though their priority numbers have been called. Inventory and price movements should be watched carefully and stabilized by speeding up or slowing down the call of priority numbers in relation to production.

The post-war-delivery purchase will have been completed when the certificate holder has selected, and a dealer has delivered, goods of a specific make and model in the price-class covered by the certificate. The purchaser would countersign the certificate in the dealer's presence and hand it to him in payment in the same way as he would tender a traveller's check in exchange for a purchase. The certificate would be accepted at its face value by the dealer in full or in partial payment of the purchase price of the goods and the purchaser would pay any balance due in cash or through a sales finance company. If the face value of the certificate should exceed the retail price of the goods, the customer would be entitled to change, calculated on the basis of the cash value of the amount by which the merchandise value of the certificate exceeds the purchase price of the goods. The dealer would clip the manufacturer's credit coupon and forward it to the wholesaler, jobber, or manufacturer from whom he purchased goods of the type sold. This coupon would provide dealers not only with the means of obtaining additional goods to replace those delivered in exchange for certificates but also with a credit amounting to 3 percent of the retail purchase price against

his supplier's billing for additional goods.

The remainder of the certificate would serve as a Treasury note maturing with the calling of its priority number. The dealer would merely deposit the certificate, properly countersigned by the purchaser and endorsed by the dealer, to the credit of his bank account. The Federal Reserve Banks would honor properly endorsed matured certificates at their cash value from funds supplied by the Treasury to meet each call of priority numbers.

A typical transaction

The essential simplicity of the plan from the standpoint of individual participants can readily be illustrated by following through parts of the buyer, seller, sales finance agency, local collection agency and Federal Reserve Bank would play in a typical transaction.

Let us take, for example, the purchase of a \$1,000 automobile certificate from a Dodge dealer in York, Pennsylvania, during the first month of operation of the plan. The dealer, who has customarily sold his installment sales contracts to the Commercial Credit Company, wishes to continue this relationship. So ^{he} uses the application forms of that company, which has previously qualified its nearest branch office at Harrisburg with the Federal Reserve Bank of Philadelphia. The local collection agencies in York are the post office, and the local offices of the Bell Telephone Company of Pennsylvania, the Western Union and Postal Telegraph Companies, the Penn Central Light and Power Company, and the Peoples Gas Company.

The purchaser's part in this transaction is confined to a few very

simple steps:

1. He pays \$10 down, signs the instalment purchase contract for a \$1,000 automobile certificate calling for 22 payments of \$45 each; names his wife and son as beneficiaries; and elects to make payments on the 10th of each month.

2. On the 10th of the following month he makes his first payment to the Bell Telephone office, bringing with him the payment book which has in the meantime been delivered him by the dealer.

3. He makes 21 additional payments--ten on the due date; three five days late; two fifteen days late; and six a month late, by virtue of skipping a payment which fell due while he was on vacation

4. Soon after the last instalment has been paid, he gets a notice from the Commercial Credit Corporation that there was a total delinquency in his account of 225 payment days for which there is a charge of \$4.00 and a priority deferment of 1. He pays the delinquency charge to the Bell Telephone office on his next pay day.

5. Two weeks later the Dodge dealer delivers to him a paid-up certificate for an automobile, having a merchandise value of \$1,100, a cash value at maturity of \$1,000, and an interim withdrawal value of \$955. The certificate bears priority number 2. The dealer has him sign the certificate and warns him not to countersign it until he is ready to take delivery of the car.

6. When the Federal Reserve Board matures the certificate by

validating priority number 2 for purchase, the purchaser examines a number of makes and models which the Board lists as being in the price-classes covered by a \$1,000 certificate. While the purchaser had in mind one of the more expensive Dodges when he purchased the certificate, he now prefers a Chevrolet which sells for \$850 delivered. He countersigns his certificate in the presence of the dealer and receives \$227.27 in change (the cash value of the \$250 difference between the merchandise value of the certificate and the purchase price of the automobile). He drives the car away and the transaction is completed.

The Dodge dealer's part in this transaction is primarily one of explaining the plan to the prospective purchaser and inducing him to enter a post-war-delivery instalment contract. He collects and keeps the \$10 down-payment as a sales commission. If the purchaser had defaulted, the dealer would have been expected to attempt to resell him on the desirability of completing his contract. When the instalment contract has been completed or at specified intervals, the dealer would receive an additional sales commission totaling \$19.80.

The dealer also performs a number of relatively minor ministerial acts. He assists the purchaser in filling in his contract and forwards a copy to Commercial Credit Company. When the payment book is received, he delivers it to the purchaser and explains its use. And when the paid-up certificate is received, he delivers it to the purchaser and explains the purchaser's rights and privileges under it.

The part of the Bell Telephone Company office in this transaction is purely mechanical. It has no interest in the identity or performance of the purchaser. Its function is solely to accept the monthly payments of \$45 with their identifying coupons and to transmit money and coupons to the Commercial Credit Company. It receives 7 cents a payment, or a total of \$1.54, as compensation for this service.

The Commercial Credit Company must do a number of things before it is ready to do business. First, it must qualify its offices with the appropriate Federal Reserve Banks by showing that they were engaged in financing instalment sales before September 1, 1941, and by meeting the requirements with respect to a bond or escrow securities. Second, it must prepare contract forms based on the Federal Reserve Board's model for distribution to dealers whose collection business it wishes to solicit. Third, it must make arrangements for cash payments with local collection agencies in the communities in which it chooses to solicit dealers' business.

When the contract is received by the Commercial Credit Company's Harrisburg office, it issues a payment book and sends it to the Dodge dealer in York for delivery to the purchaser, opens a ledger account for the purchaser, and sends the application to the Federal Reserve Bank of Philadelphia. When coupons and payments are received from the telephone company office, it enters the payments in the purchaser's ledger account, and transmits the face value of coupons, less $\frac{3}{4}\%$, to the Federal Reserve Bank of Philadelphia. On each coupon of \$45, the Commercial Credit Company would transmit \$43.65 or \$1.35 less than the value of the coupon. Of the latter sum 90 cents would be

credited to the dealer, 7 cents would already have been withheld by the telephone office, and the remaining 38 cents would be retained by the Commercial Credit Company as compensation for its services.

The Commercial Credit Company sends notices of delinquency, and when the final instalment has been paid, it computes the number of delinquent payment days. Since the delinquency exceeds the grace period, it computes the delinquency charge and the priority penalty and notifies the purchaser of both. When the \$4.00 delinquency charge has been collected, the ledger card with a priority number assigned is sent to the Federal Reserve Bank of Philadelphia, together with three-fourths of the delinquency charge. The Commercial Credit Company would retain the remaining fourth of the delinquency charge, less the 7 cent collection fee of the telephone company office. The responsibility of the Commercial Credit Company toward the transaction would be fulfilled when it has transmitted the final commission to the dealer. Its total compensation for handling the account would be \$9.29.

The dealer who delivers the Chevrolet automobile in the post-war period also plays a part in the transaction. He displays the car and delivers it in exchange for the countersigned certificate and a cash rebate. He clips the manufacturer's credit coupon and sends it to the factory branch office of the Chevrolet Motor Company. The coupon entitles him to delivery of an additional ~~car~~ car and to a credit of a specified percentage of the retail purchase price of the car delivered. He deposits the remainder of the certificate in his bank account, where it is credited at its cash value.

The part which the Federal Reserve Bank of Philadelphia plays in this transaction also begins before the post-war-delivery contract is signed. It selects sales finance agencies and local collection agencies in accordance with standards established by the Federal Reserve Board. It prints payment books for distribution to sales finance agencies. The Bank maintains ledger accounts for sales finance agencies charging each agency with payment books issued and anticipated collections and crediting it with collections transmitted.

When the contract forwarded by the Dodge dealer in York reaches the Federal Reserve Bank of Philadelphia, it should be filed alphabetically to determine whether the same person has applied for additional cars. When the completed ledger card is received from the Commercial Credit Company, the card should be audited and the alphabetical file again checked for multiple applications. If the record is satisfactory, it issues a paid-up certificate for a \$1,000 automobile which certificate is sent to the Dodge dealer for delivery to the purchaser.

When the certificate is finally exchanged for a Chevrolet automobile, and the dealer has deposited it with his bank, the Federal Reserve Bank of Philadelphia accepts the certificate at its cash value, credits that sum to the account of the bank which forwarded the certificate and charges the account of the United States Treasury with the withdrawal of the same amount.

1/11/43

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MINUTES OF BOARD MEETING

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December 22, 1942, 11:00 A.M.

East Wing, White House

Present: The Director (Presiding)
Miss Perkins
Mr. Smith
Mr. McNutt
Mr. Green
Mr. Flanders
Mr. Bell (Acting Secretary of Treasury)
Mr. Hill (Acting Secretary of Agriculture)
Mr. Taylor (Acting Secretary of Commerce)

1. Mr. Henderson discussed with the Board the proposed rationing of canned foods, describing the procedures which had been agreed upon. Mr. Henderson stressed the necessity of training retail distributors in the mechanics of point rationing, with its accompanying scheme of rationed banking.

The question was raised whether hoarding was not stimulated by advance announcement of such rationing programs. Mr. Henderson said no, particularly if the proper appeal was made to the public. In view of the fact that the processors and distributors must be familiarized in advance with point rationing, rumors and "leaks" would almost certainly reach the public, thereby stimulating hoarding. In order to stop such runs, it will be necessary, Mr. Henderson stated, to announce the program in advance, thereby placing the pressure of public opinion against the tendency to hoard. Furthermore, Mr. Henderson stated, consumers will be required to declare their stocks of canned goods on hand, and these stocks will be deducted from the individual's allotment.

The Director suggested that, particularly in small communities, it would be desirable to use the schools, and especially the high school students, to assist retailers in checking inventories and filling out the necessary forms in connection with new rationing procedures.

2. The Director stated that, in view of the present difficulty experienced by millers in obtaining free wheat for domestic flour consumption, he was prepared to cooperate with the Price Administrator and Secretary of Agriculture in meeting this situation. Action to be taken would include an increase in the present flour ceilings, together with a program of economies in the distribution and baking of bread, designed to absorb these increases and thus to prevent any increase in the price of bread. The increased ceiling price of flour would permit the millers to purchase wheat at a price approximately 90% of parity, and it is believed that this price would attract enough wheat to meet the needs of the miller industry.

Mr. Henderson expressed complete willingness to cooperate in such a program, but doubted whether it would afford a lasting solution to the problem or would prevent an eventual increase in the price of bread. In the past, he pointed out, the millers' margin has averaged about 35¢ per barrel. The new ceiling price would make this the maximum margin, thereby reducing the average to approximately 60¢ per barrel. This will squeeze the small miller and create pressure for relief. In addition, according to Mr. Henderson, the effect of the proposed economies would not be uniform throughout the baking industry, and some bakers will be subject to a squeeze, thereby creating an additional pressure for price adjustments. Furthermore, Mr. Henderson expressed the opinion that, in view of the Congressional agitation for increased parity prices, the farmers might hold their wheat in anticipation of still greater returns, thus continuing the existing flour shortage and forcing further increases in prices.

The Director agreed that the difficulties pointed out by Mr. Henderson were great, but felt that the proposed program certainly deserved a trial. Mr. Flanders was of the opinion that any increase in the price of bread would be extremely unfortunate, especially from a psychological standpoint, and suggested that even a subsidy would be preferable to such an increase. Mr. Henderson stated in reply that there was already in existence an enormous and indefensible wheat subsidy by virtue of the Congressional prohibition against the sale of government owned wheat stocks at less than a full parity price.

3. Mr. Henderson discussed the question of government policy with respect to subsidies designed to hold down the cost of living. He pointed out that the profit margins of the industry are great and that in many sectors of the economy there is ample margin to absorb a considerable increase in production costs. The institution of general price control has given elbow room for some increases, particularly those which are designed to increase the production of essential commodities. The principal pressure in this direction has, according to Mr. Henderson, come from a desire to obtain additional raw materials; and the question to be faced in this connection is whether to use price increases or subsidies to draw out marginal production. In the case of lumber, price increases were allowed, and in the case of non-ferrous metals, subsidies are being used. The same question is now presented in connection with increased overtime payments resulting from an extension of the work week in the coal industry. In this case Mr. Henderson stated that price increases will be relied upon rather than subsidies.

Up to the present time, Mr. Henderson continued, the decision as to when subsidies shall be used has to a considerable degree been made without any general government policy. The outstanding example of this is the present

- 4 -

subsidy for the transportation of gasoline to the east coast by tanker. It was generally agreed that this subsidy was highly questionable. Yet, Mr. Henderson pointed out that it was the only subsidy ever considered by his office against which there had been not a single Congressional protest. Mr. Henderson went on to state that the enormous sums thus used, if diverted to most justifiable purposes, could have prevented many of the most painful increases in living costs during the past six months.

Mr. Henderson also pointed out the existence of a difficult problem in connection with the effect of price ceilings, together with increased costs, upon marginal firms, particularly in the transportation field and the retail field. Even though considerable fat may exist, in the form of high profits, this fat is not equally distributed over a particular industry; and thus, when costs increase, the number of marginal producers increases. This problem will become particularly difficult when the present adjustment procedures under the general maximum price regulations are superseded by dollars and cents ceilings.

Despite the difficulties involved, Mr. Henderson expressed the opinion that subsidies should, as a general rule, be used to prevent increases in the price of any major cost of living item. Price increases inevitably pyramid and disarrange the economy, cause additional demands for increases in wages, and continue the inflationary spiral. Mr. Henderson pointed out that no country engaged in the present war has been able to avoid the substantial use of subsidies for this purpose.

However, he expressed the firm view that before subsidies were used, every alternative should be exhausted, including the institution of economies in processing and distribution. He stated that already the Office of Price Administration has assisted in the institution

of many economies in retailing, and also called attention to the program for grade labeling of canned goods. Subsidies, in any case where used, should, said Mr. Henderson, be afforded only to those firms which can prove a need for them, and should not be extended generally throughout an industry irrespective of need. Disregard of this criterion is one of the basic flaws in the present gasoline subsidy.

Mr. Green called attention to the fact that the enormous increase in the volume of such industries as transportation and distribution should permit the absorption of considerable cost increases.

Mr. Ball stated that in general the Treasury was opposed to subsidies, since they add to the income stream, thereby increasing inflationary pressures, and create political pressure groups. In general, he stated that the Treasury favored limited subsidies to those situations in which it was necessary to draw out marginal production or to hold down the price of a major cost of living item.

Mr. Henderson agreed with the position of the Treasury. He also called attention to the fact that wide-spread rationing might leave certain of the lowest income groups in the possession of purchasing power insufficient to utilize their full rations. In this case, two alternatives would be presented: Either to permit the sale of rationed coupons by the lowest income groups, or to provide some form of subsidy to permit them to purchase their full quota.

Mr. Smith pointed out that the parity concept, embodied in the price control legislation, is in itself a subsidy; and that the result of this subsidy is to force certain prices up, thereby creating the necessity for additional subsidies. The five basic parity crops directly effect only 30% of the total farm income, and the parity concept for those crops may actually harm some of the producers of those commodities which account for the remaining 70%.

Mr. Smith stated that the present wheat policy of the government, forced by legislative enactment, is the prime example of this tendency; and runs counter to all reason.

The Director then read extracts from a memorandum distributed by Mr. O'Neal, expressing firm opposition to the use of any subsidies designed to hold down food costs.

4. ~~Mr. Henderson~~ called attention to a memorandum distributed by him, describing the course of the cost of living during recent months. He stated that the facts as contained in this memorandum were especially important in view of the current effort in Congress to abolish the power to impose retail price ceilings, and to compel reliance upon the power to fix prices for certain basic manufactured products, with control over distributor's margins. Mr. Henderson stated that the memorandum submitted by him demonstrated a conclusive necessity for the power to control prices at retail; and that the cost of living was not brought under control until this power was exercised. The translation of these ceilings into dollars and cents basis can ease the burden of this control in many cases, but the power will always be necessary if the cost of living is to be held stable.

The Board adjourned at 1:30 to meet again on January 8, at 11:00 A.M.

Copies sent to:
Bell, Gaston, Haas,
Paul, and White

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE FOR EMERGENCY MANAGEMENT

(Secretary has ~~not~~ seen.) OFFICE OF ECONOMIC STABILIZATION
WASHINGTON, D. C.

JAMES F. BYRNES
Director

December 18, 1942

My dear Mr. Secretary:

Enclosed are the Minutes of the last Board meeting. Our next meeting will be held on Tuesday, December 22nd, at 11:00 a.m.

We shall discuss:

1. Recent changes in food prices (Mr. Henderson).
2. Basic policy for use of subsidies in wartime (memorandum enclosed).

Sincerely yours,

James F. Byrnes
Director.

Hon. Henry Morgenthau,
Secretary of Treasury,
Washington, D. C.



THE UNDER SECRETARY OF THE TREASURY
WASHINGTON

December 11, 1942.

MEMORANDUM ON MEETING OF THE ECONOMIC STABILIZATION COMMITTEE

Most of the time of the meeting was spent in discussing subsidies for dairy products and the program submitted by Secretary Wickard. There is attached his statement, the main points of which were discussed by him.

One point that is up for immediate decision is the question of subsidies for cheese manufacturers. Chairman Byrnes said that it was estimated that these subsidies would take about \$20 million and he had put a limit on expenditures of \$25 million. He also indicated that all of the products of the dairy industry would be up for subsidies and it was estimated that the total cost would be somewhere in the neighborhood of \$435 to \$450 million.

swb



MINUTES OF BOARD MEETING

December 11, 1942, 11:00 A.M.

East Wing, White House

Present: The Director (Presiding)
Mr. Bell (Acting Secretary of the Treasury)
Mr. Wickard
Mr. Jones
Miss Perkins
Mr. Smith
Mr. Eccles
Mr. Henderson
Mr. Davis
Mr. McNutt
Mr. Green
Mr. Patton
Mr. Flanders

General discussion of the principles which should underlie subsidies was postponed to a future meeting, subsidies being discussed only in connection with the proposed dairy products program.

Mr. Wickard pointed out that, with respect to agricultural commodities, a considerable body of opinion among the potential beneficiaries of subsidies -- the farmers -- is hostile. Nevertheless, he stated, support prices adequate to secure needed production will require either subsidies or higher retail price ceilings. Mr. Wickard expressed the opinion that there is no other alternative if the necessary quantities of critical agricultural commodities are to be produced. Yet, he asserted, the Congress is still strongly predisposed against subsidies. It may be possible to reduce the amount of money required for subsidies by instituting economies in the processing and distribution of farm commodities. This would, in many cases, markedly alter the accepted systems of distribution and would therefore meet with considerable opposition. Hence, Mr. Wickard cautioned against

expecting too much relief in the distributive economies.

The dairy situation, Mr. Wickard pointed out, vividly illustrates the convergence of all these issues.

The Department of Agriculture has set a production goal of 122 billion pounds. This, Mr. Wickard believes, is the most dubious of all of the Department's goals, largely on account of the critical labor shortage in dairy farming. The Department will attempt to meet this goal by an intensive production drive in each county, undertaking to find what farmers will need in order to handle additional cows and produce additional quantities of milk. The Department will also, for the first time, offer stable year round support prices, so that farmers will be able to know just what price they can expect to get for their products at any time in the year. In general, prices to both farmer and consumer will remain at October levels, with some necessity for adjustment in certain special areas. There will, however, be one nation-wide exception -- a subsidy on cheese which will cost between \$20 and \$25 million. The Department, according to Mr. Wickard, has also taken steps to stop the slaughter of dairy cattle in certain localities by offers to purchase dairy cows at fair prices for resale to other farmers.

The War Manpower Commission has also directed deferment of essential dairy workers; and the procurement agencies have ordered government contractors not to hire such workers. The Department of Agriculture, in cooperation with the War Manpower Commission, has also instituted a program for the recruitment, training and transfer of farmers from unproductive areas, thus making them available to supply the shortage of labor in more productive dairy centers. Even these measures, however, will not be sufficient to

relieve the manpower shortage; and Mr. Wickard expressed the opinion that it will be necessary to recruit women for this type of work.

One additional problem, Mr. Wickard stated, is the maintenance of an adequate supply of fluid milk, particularly in those areas where population has suddenly and recently increased, or in those areas from which supplies have been drained off into such localities. In such areas, increases in the price of fluid milk are necessary to secure adequate supplies, ~~and~~ if either subsidies or increases in retail prices are to be avoided, it will be necessary to effect substantial economies in milk distribution, through the standardization of bottles, the zoning of deliveries, and increase of store sales. This problem is especially difficult in New York and Chicago. A subsidy is already in effect for the New York area, but should be eliminated if it is possible to institute sufficient economies.

The Director emphatically expressed the opinion that such economies must be instituted quickly, in view of the strong opposition to subsidies upon the part of Congress, and requested the help of Mr. Green in securing the help of organized labor.

Mr. Henderson pointed out that the practices of both labor and management in the dairy industry are deeply involved, and that these practices have grown up through years because of the necessity of developing strong collective bargaining relationships between workers and powerful nation-wide dairy corporations.

Mr. Wickard stated that, as part of the dairy program, cheese will be rationed along with meats. On the other hand, there will be no necessity for the nation-wide rationing of milk. In certain areas where the population has increased faster than supply, local rationing may be necessary.

Miss Perkins inquired whether it would not be possible to carry out an educational program, discouraging milk consumption upon the part of able-bodied adults, especially in view of the fact that milk consumption has been encouraged in the past by advertising and other educational methods. Mr. Wickard replied that such a program had failed to reduce the consumption of meats to any substantial degree, and expressed scepticism as to the possibility of using voluntary methods to reduce consumption.

Mr. Patton pointed out that butter has much less nutritive value than milk and cheese, and he inquired as to what measures are being taken to convert dairy resources away from butter production. Mr. Wickard replied that this is the purpose of the cheese subsidy, but pointed out that the limited cheese-making facilities reduce the extent to which conversion can be induced. Mr. Patton also emphasized the necessity of some measures to guarantee the minimum levels of subsistence to those persons who, in case of rationing, would not have sufficient purchasing power to utilize their portion of the rationed commodity.

There followed a general discussion as to the point system of rationing, and other related problems.

Mr. Green stated that a review of the proposed program had convinced him that it would be desirable to institute subsidies for milk. Other members of the Board emphasized the difficulty of securing Congressional approval, but Mr. Green stated that, since milk is essential to the maintenance of health and efficiency, subsidies would be especially desirable as an alternative to price increases.

Mr. Flanders stated that, in his opinion, there were other alternatives. If arrangements are made, he stated, to preserve the necessary minimum supply of manpower on the dairy farms; if sufficient labor-saving machinery

is made available to the farmer; and if the most efficient methods of production and distribution are used, it will be possible to secure the necessary products without increasing prices to consumers or without large subsidies.

Mr. Patton stated that the problem was not simply one of subsidies, but of furnishing adequate funds to finance the expansion of production, particularly on the family-type farm. We have, he stated spent billions of dollars from the public Treasury to finance the expansion of industrial facilities, but have made only the most ineffective efforts to provide adequate resources for medium and small farmers to expand their productive capacity, thereby utilizing to the fullest degree our agricultural manpower.

Mr. Flanders agreed that methods of increasing the efficiency of existing agricultural manpower should be given greater consideration.

Mr. Smith and Mr. Henderson both urged that, at a meeting of the Board in the near future, there should be a discussion of the general principles which would govern the use of subsidies in wartime.

The meeting adjourned at 1:25 to meet again on Tuesday, December 22, at 11:00 A. M.

Statement of Secretary of Agriculture Claude R. Wickard to Board
of Economic Stabilization

Friday, December 11, 1942

THE DAIRY PROGRAM

Dairy products provide some of the most important nutrients in our food supply. A comprehensive program has been developed in cooperation with other Federal agencies to get maximum production and utilization of our milk supplies to meet civilian, military, and lend-lease requirements.

The Farm Production Program

- a) A goal of 122 billion pounds of milk - 2 billion above the previous all-time record - the maximum feasible production in view of manpower and cow numbers.
- b) A farm by farm and county by county drive among farmers to achieve that goal.
- c) A price support program through continuous offer to buy manufactured products at ceiling levels - the first time in history that dairy producers have been assured stable prices.

Prices of manufactured dairy products have been stabilized at September-October levels. By agreement with OPA, prices will be supported at not less than 46 cents per pound for 92 score butter, Chicago basis, 27 cents per pound for No. 1 American cheese, Plymouth (Wisconsin) basis, 14.5 cents for roller and 14.5 cents for spray process dry skim milk, extra Midwest basis, and a comparable price for evaporated milk, f.o.b. plant basis, to be announced. Consequently consumers should experience no further price rises in most of these products. In the case of cheese, the OPA ceiling price for American civilians will remain at the present level of 23½ cents per pound (Plymouth basis). The cash returns to farmers at this price would be far below returns from other products. Since cheese has one of the highest

priorities for domestic, military, and lend-lease requirements, the high cheese production is being maintained by a subsidy which returns to farmers the equivalent of 27 cents per pound, while maintaining the wholesale price at 23 $\frac{1}{4}$ cents Plymouth basis.

d) A simple but workable program to keep good dairy cattle from being slaughtered by standing offers to buy good dairy cattle at prices higher than their beef value. These cattle will be sold to other farmers.

e) More milk cans, rationed among farmers, to make possible increased deliveries of whole milk.

f) A Nation-wide manpower program has been launched to retain skilled workers on essential dairy farms, to recruit and place workers on dairy farms. Demonstration training programs have begun as well.

Marketing and Distribution Programs

a) With the cooperation of other Federal agencies, the Department is exploring the possibility of undertaking to direct the flow of milk from producers to processing plants, so as to reduce hauling distances, and assure maximum production of dry milk, cheese and the more essential dairy products.

b) The Department with the cooperation of other agencies will seek to achieve greater efficiencies and increased standardization in distribution of fluid milk in urban markets, so as to limit the costs of distribution and the pressure for further price rises.

c) It will increase and re-locate facilities for dry skim milk production in the Midwest so as to reduce the volume of skim milk wasted or fed to livestock.

- d) A program will be developed to conserve for human food and livestock feed, the supplies of whey not now being conserved.
- e) All steps necessary will be taken to maintain at the highest level possible our production of cheese and dry whole and skim milk, as well as milk for fluid consumption.
- f) Maximum production and marketing of other dairy products will be encouraged, consistent with the priority requirements for the civilian, military, and lend-lease needs. Tin allocations for evaporated milk will be limited, though this should not reduce civilian supplies appreciably.

Supplies in Relation to Requirements

Our production goal is 122 billion pounds for 1943 - an all-time record. Military and lend-lease requirements will total at least 18 billion pounds, as compared to about 7 billion pounds in 1942. If our goal is achieved, civilian supplies will not exceed 104 billion pounds, compared to nearly 113 billion in 1942. Increased National purchasing power and employment is creating further demands on the civilian supply. Relative shortages of meat and coffee result in attempts to buy more cheese, milk and other dairy products. With their present purchasing power, consumers would increase their milk and dairy product consumption by at least 15 percent. Even the maximum feasible production for 1943 will be at least 18 to 20 billion pounds below what consumers would like to buy.

We cannot meet the military and lend-lease requirements and permit this at the same time. Consequently we have taken and may take further action to assure best possible utilization of our supplies and be sure of meeting all war requirements.

Conservation and Limitation Measures

- a) Through a WPB order, cream is limited to 19 percent butterfat - whipping cream is out for the duration.
- b) The butterfat and milk solid content of ice cream is now limited under a temporary order, so as to conserve these supplies for more important uses. A permanent order will be issued.
- c) 90 percent of the spray process dry skim is now reserved for government requirements and supplies of roller process milk are being released to bread bakers and other commercial users of milk solids.
- d) Approximately 20 million pounds of storage butter are now held for government use.

e) Government requirements of cheese are so large that supplies for civilians cannot exceed two-thirds of the 1941 consumption. Consequently cheese is to be rationed along with meat.

f) In some milk areas, especially where population increase has been rapid or military camps have created unexpected demands, the supply of fluid milk may not keep up with demands. Whenever this becomes evident, the Department will recommend a local rationing program to divide the available supplies equitably.

Under this program we can feel confident that all essential needs of our domestic population will be met and at the same time our military forces and Allies will receive their minimum requirements. The cooperation of many groups - farmers, processors, distributors, labor leaders and housewives - will be necessary. We have every reason to expect that they will cooperate and that this vital food will be able to do its war job.

December 10, 1942

To: Hon. James F. Byrnes
From: Leon Henderson
Subject: Public Policy on Government Subsidy Payments

1. We Have Obtained Control of the Price Structure.

In order to prevent a run away price and cost situation, it was necessary for the Government last spring to bring the entire price and cost structure under control. Selective control of prices gave way to the General Maximum Price Regulation, to greatly extended rent control, and to the development of wage and salary stabilization. By these and subsequent actions we have brought under price control 90 percent of the cost of living, and virtually all wholesale prices except those of finished combat items and subassemblies. These measures broke into the spiralling inflationary movement which was under way at that time and permitted us to bring the price situation under control.

2. Limited Price Increases May Now be Permitted to an Extent Consistent with the Maintenance of Control.

The attainment of control does not, however, end our job. Now that control has been attained it is necessary to manage prices, that is, do the more refined job of administering prices in such a way as to facilitate the war production program and the general requirements of the war economy. The original assertion of control over the inflationary price spiral required a rigid and inflexible attitude towards prices. So long as there was any question about the control of the explosive inflationary forces, the price instrument could not be used to promote the objectives of the war economy.

Price administration, on the other hand, requires a certain flexibility which could not be risked until control was assured. Successful administration permits of some upward movement. But the permissible upward movement must be sufficiently small so that it does not have repercussions on farm prices and wage rates which would in turn react on the price level, set off the spiral again, and endanger our control.

3. Although the Price Structure is Now Under Control, the Forces Making for Cumulative Increases Remain Present.

Our price ceilings are being subjected to the pressure of increasing costs of production and distribution. These pressures will persist and increase because of war dislocations, regardless of our ability to stabilize raw material prices, or wage rates, or transportation rates.

(a) The drive to secure an adequate volume of raw materials means pressing on marginal sources of supplies, the use of which would not be economical under normal circumstances. It means in many cases the substitution of new, and more costly raw materials for those normally used.

(b) The drive to attain full use of facilities means the utilization of facilities that are less efficient than those now in use.

(c) The withdrawal of 10 million men from the labor force by the end of 1943 will require not only a drastic shift of workers from industry to industry with attendant problems of retraining, but the introduction into the labor market of an almost equal number of nonworkers. Output per man hour must be expected to diminish and labor costs per unit of output to increase.

(d) Transportation costs must be expected to increase as a result of the rerouting of traffic, the delays due to congestion, and increased maintenance costs.

(e) Beyond these cost increases there are others which must result from the commitments the Government has made with respect to parity in the field of agricultural prices, and the elimination of substandards and inequalities in the area of wages.

4. In General There is Elbow Room for the Absorption of Substantial Cost Increases.

In the field of industry corporate profits before taxes averaged \$4½ billion in the period 1936 to 1939. In 1941 they amounted to \$14 billion. This year they will total at least \$19 billion. In agriculture also net income of farm operators, that is, income after all expenses, has increased from \$4½ billion in 1939 to \$9-3/4 billion this year. This is \$1 billion in excess of the peak rate raised in 1919.

5. There Will Nevertheless be Many Situations in Which Profits Will not Permit the Absorption of Cost Increases.

This is true of the marginal output of many industries, output which is essential to the war effort. Even though the bulk of an industry's output is being produced under favorable conditions, some part may be produced at costs higher than the price ceilings. It is also true for distribution of essential civilian commodities in particular areas, and for the production of specific commodities whose ceiling prices will be insufficient to cover direct costs, even though the profits of industries from the production of other commodities may be generally favorable. In these cases the returns to producers must be increased if the production and distribution of goods essential to the war effort is not to be impaired.

6. Returns to Producers Can Be Increased Either by an Increase in Prices or by Subsidies. Price Increases Should Be Avoided for Commodities Which Bulk Large in the Government's or Consumer's Budget.

(a) Price Increases. Where major cost-of-living items are directly or indirectly affected, industry-wide price increases should be avoided. (1) Such price increases expand the profits of firms whose profits are already more than adequate at the same time that they provide relief to those firms which need it. (2) It is difficult to prevent the pyramiding of such price increases throughout the price structure. (3) The administrative difficulties of adjusting the whole series of interrelated prices are formidable. (4) Finally, an increase in the cost of living makes it extremely difficult to avoid an increase in farm prices and wage rates, with consequent reactions on prices. If further increases in farm prices and wage rates are permitted, we will again be involved in an upward price-cost spiral. The prices of significant cost-of-living items must, therefore, be firmly held, lest our control of the price structure be jeopardized.

(b) Subsidies. In the case of such items producers' returns must be increased by subsidies wherever such an increased return is necessary to maintain the essential production or distribution. Such subsidies will cost consumers and the Government a fraction of the original cost increase in contrast to price increases which cost the consumer and the Government more than the cost increases.

7. Conditions for the Granting of Subsidies.

(a) Subsidies should not be used to meet increases in the cost of producing or distributing commodities which have only a minor direct or indirect effect on the cost of living. Such cost increases may be met by price increases without raising the cost of living sufficiently to threaten our control.

(b) Subsidies should be provided only for the production and distribution of goods essential to war production or to the maintenance of the health and efficiency of the civilian population. Wherever it is deemed advisable to encourage continued production of non-essential commodities, price increases rather than subsidies are indicated.

(c) All possible cost economies should be required before subsidies are granted. This condition means not only that waste and extravagances must be eliminated; it means also that positive programs must be adopted to standardize or simplify output, concentrate production to secure optimum operations, and cut costs in other ways. Such economies are necessary not only to protect price ceilings, but also to secure maximum use of our resources for war. Sufficient economies will not be attained by any automatic processes. Positive and vigorous Government programs are needed.

(d) Subsidies should be granted only to those firms which still need them after having made all possible cost economies. They should be granted on an industry-wide basis only when the profits of producers of the bulk of an industry's output are at unreasonably low levels. Unless subsidies are confined to the firms which need them, a substantial part of the saving associated with the subsidy device will be lost, and the cost of subsidies will approach that of price increases.

12/10/42

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Photostats to:

Mr. Bell
Mr. Gaston
Mr. Paul
Mr. White
Mr. Haas

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE FOR EMERGENCY MANAGEMENT
OFFICE OF ECONOMIC STABILIZATION
WASHINGTON, D. C.

*Mr. Bell will
attend.*

JAMES F. BYRNES
Director

December 8, 1942

My dear Mr. Secretary:

The Board will meet on Friday, December 11th, at
11:00 a.m.

We shall discuss:

1. Government policy with respect to subsidies designed
to hold down the cost of living (memoranda previously submitted by
Messrs. Wickard and O'Neal).

2. Proposed dairy products program (memorandum to be
submitted at meeting by Mr. Wickard).

We should be glad to have an expression of your views
on any aspect of either of these subjects, if you have not already
expressed them.

Sincerely yours,

James F. Byrnes
Director.

Hon. Henry Morgenthau,
Secretary of the Treasury,
Washington, D. C.



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COPIES TO: Bell, White, Gaston,
Paul, and Haas

12/7/42

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE FOR EMERGENCY MANAGEMENT
OFFICE OF ECONOMIC STABILIZATION
WASHINGTON, D. C.

December 5, 1942

JAMES F. BYRNES
Director

Dear Mr. Secretary:

I am enclosing six copies of the Minutes of the last Board Meeting. The next meeting will be held Friday, December 11, 1942 at 11:00 A. M.

Very truly yours,

James F. Byrnes
Director.

6 Encls.

Honorable Henry Morgenthau
Secretary, Treasury Department
Washington, D. C.

MINUTES OF BOARD MEETING

The Economic Stabilization Board met on Friday, November 27, at 11:00 A.M.

Present: The Director (presiding), Mr. Wickard, Mr. Jones, Mr. Eccles, Mr. Smith, Mr. Henderson, Mr. Davis, Mr. Murray, Mr. Patton, Mr. Johnston, and Mr. Lubin.

Mr. Henderson discussed the necessity for rationing essential articles of food and clothing, on the basis of a memorandum previously circulated. He emphasized the increasing recognition that rationing is an obviously integral part of a comprehensive economic stabilization program. Any effort to stabilize the cost of living must, he pointed out, include provision for the fair distribution of essential goods which are in short supply. This is necessary in order to maintain the productivity and the morale of the civilian population, thereby insuring adequate munitions and other supplies to the armed forces and to our allies. Despite this recognition, Mr. Henderson stated that there is still strong resistance to rationing upon the part of many people.

Mr. Henderson expressed the opinion that our large inventories of consumer goods, accumulated in 1941, have confused the popular understanding of this problem. Despite the fact that our production of consumer goods has been declining, incomes have increased; and, more important, retail purchases have gone up. The result has been to reduce our stock-pile of consumer goods to a very low point, and the pressure of purchasing power on limited supplies has been intensified by the imposition of general retail price ceilings. As shortages appear, there will be increased acceptance of rationing by the public, stated Mr. Henderson.

He also pointed out that the vastness of this country prevents any slavish duplication of foreign rationing systems. For instance, in the rationing of fuel oil, our Government has attempted to distribute the supply on a "tailored" basis rather than by some more automatic method. The object of this, according to Mr. Henderson, was to cut down on the consumption by larger houses, though this might involve a risk of public opposition.

Mr. Henderson also pointed out that public reactions vary according to the commodity which is involved. For instance, there was full public acceptance of the necessity for tire rationing, and yet resistance to the rationing of mileage through control of gasoline. Therefore, each commodity requires special study in order to devise a system of rationing which will best fit the national need and best obtain public acceptance.

There is one universal characteristic of all rationing systems, said Mr. Henderson -- a rationing currency or card. It has been the difficulty of preparing these rationing books which has often caused delay in the institution of rationing programs. These delays have occurred in mailing, in parcel post, and in printing.

Meats, with the probable inclusion of cheese, will be rationed on a point basis, thereby preserving the largest possible range of consumers' choice. Butter, on the other hand, will probably be grouped with other fats and oils in a similar system.

In answer to inquiry by the Director, Mr. Henderson stated that the Office of Price Administration does not have authority at present to determine what commodities shall be rationed. This authority is now vested in the various industry branches of the War Production Board.

Mr. Murray inquired of Mr. Henderson whether the cost of food stuffs had not risen enormously in recent months. Such increases, according to Mr. Murray, will have a pronounced effect upon wage demands in the future. Mr. Henderson replied that, though there have been sharp increases during the past year, the rate of increase has been rapidly decelerating, and almost all foods are now coming under price control. Only fresh fruits and vegetables will remain uncontrolled. In answer to a further question by Mr. Murray, Mr. Henderson stated that only eight or nine percent of food prices is now free from ceilings. When this statement was questioned by Mr. Murray, it was agreed that Mr. Lubin would prepare a memorandum upon this subject for discussion at a future meeting of the Board.

Mr. Patton asked whether the recommendations of the Food Requirements Committee for the rationing of food were not subject to review by the industry branches in the War Production Board. Mr. Wickard stated that as a practical matter this was the case, and blamed some of the delay in instituting rationing programs upon this fact. Mr. Patton expressed the opinion that the food industry branches of the War Production Board were, in a large measure, under the domination of food processors who would tend to oppose rationing.

The Director asserted that these delays, with the attendant publicity and welter of conflicting statements, constituted one of the most important difficulties in setting up a successful rationing policy. Mr. Henderson agreed, referring to the fuel oil situation as a typical example.

Mr. Patton inquired whether rationing could be utilized as a means of control over general expenditures. Mr. Henderson replied in the affirmative, but said that no alternative could obviate the necessity for specific rationing.

The Director again inquired of Mr. Henderson as to what can be done to speed up the preparation of rationing programs. Mr. Henderson replied that freer authorization by the Budget Bureau for advance planning would be helpful, as well as some effort to overcome the printing bottleneck. At present, Mr. Henderson stated, preparations can be made only after a formal decision to ration a particular commodity or group of commodities. The Director expressed the opinion that perfection and fool-proof mechanisms must be sacrificed to speed and simplicity. For example, he cited the use of safety paper in the preparation of rationing books.

Mr. Smith requested Mr. Henderson to prepare and circulate a brief memorandum on the objectives of rationing so that the Board members could agree upon a set of common principles. He also agreed to have the Bureau of the Budget prepare a similar statement setting forth in detail the procedure by which a rationing program is now determined upon and put into effect.

Mr. Eccles expressed general agreement with the position taken by Mr. Henderson. To emphasize the magnitude of the job, he cited figures on increases in department store sales in various localities, averaging about 25 percent for the entire country. Mr. Eccles also emphasized the necessity of parallel action in the field of manpower, production and fiscal policy as necessary in order to minimize the difficulties of rationing and to relieve the pressure on supplies of consumer goods. Nevertheless, he strongly emphasized that he saw no possibility of avoiding the rationing of essential food and clothing, and favored the institution of these measures at once.

Mr. Patton agreed with Mr. Eccles. He also strongly urged the necessity of centralizing control over the entire field of production,

manpower and civilian economic policy, as recommended in the joint statement of Senators Truman, Pepper, and Kilgore, and Representative Toland. Mr. Patton requested that these recommendations be discussed at a future meeting of the Board.

Mr. Murray also agreed with what Mr. Eccles and Mr. Patton had previously said. He urged the importance of maintaining civilian control over production, procurement, manpower, and economic policy. He further expressed the opinion that so long as procurement remained in the control of the military side of the Government, it would be very difficult to formulate an effective production and manpower program.

Mr. Davis agreed with the recommendations of Mr. Henderson, favoring immediate action. Mr. Davis emphasized the importance, along with rationing, of assuring the people that a minimum supply of essential goods will be planned for and guaranteed. He also urged the necessity of adequate publicity to acquaint the people with the necessity for rationing.

Mr. Eccles agreed with these suggestions, pointing out that the maintenance of minimum civilian requirements was equally as important as providing for the needs of the armed forces. The Director and Mr. Henderson expressed accord. Mr. Henderson asserted that in some cases the Army was planning its production program without adequate consideration of essential civilian needs.

Mr. Johnston stated that people in Government must stop talking and do some straight thinking. He agreed with remarks previously made as to the necessity of maintaining civilian control of the economy. He also held the opinion that the Director of Economic Stabilization must assume more power and responsibility. He further stated that in his opinion the Director should make greater use of the Board members. The Director agreed

with this recommendation, stating that it was his intention to submit various rationing programs to the non-governmental members of the Board for their review and endorsement prior to any public announcement of the various rationing measures.

Mr. Johnston pointed out that it was important for the Board members to help in selling these necessary measures to the general public.

The Board adjourned at 1:45 P.M. to meet again on Friday, December 11, 1942, at 11:00 A.M.

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