

January 16, 1970

PAUL W. MCCrackEN, CHAIRMAN  
HENDRIK S. HOUTHAKKER  
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MEMORANDUM FOR D. P. MOYNIHAN

Subject: Proposed FAB (Family Assistance Bank)

The financial difficulty encountered by the Family Assistance Plan is due to failure to understand the problem in a sufficiently business-like or, more precisely, bank-like way. The fact is that there are no poor people in the United States. There are only some people who are terribly illiquid; that is, they have no money. Moreover they face capital markets that are highly imperfect; that is, they can't borrow.

The Federal Government should correct this imperfection in the capital markets. For one thing, the imperfection is largely due to Federal action in outlawing slavery. Moreover, if all of these people came to the capital markets to borrow it would seriously interfere with the Treasury's financing, as well as make the capital markets pretty dirty.

The obvious solution is to establish a Family Assistance Bank. The FAB would lend to people on the same schedule and conditions provided for benefits under FAP. However, the debtors would be expected to repay in proportion to their future incomes. For example, they might pay 10% of any years' income in excess of \$10,000 but not exceeding \$20,000 and 20% of any income in excess of \$20,000 until their debt had been repaid with interest. To keep the whole thing business-like, interest should be charged at the prime rate. If the debtor died with some debt outstanding, that debt would be cancelled, just as we cancel the income tax obligation of people who die with unrealized capital gains. When any debt is cancelled the Treasury would make a

contribution of equal amount to the FAB, thus keeping the capital of FAB unimpaired. This contribution would be considered a budget expenditure, and is the only part of the operation that would appear in the budget. If the program is confined to families with minor children these expenditures would not appear in any large amount for quite a few years.

FAB would raise money by selling its own securities with a Federal guarantee. The Treasury would manage the offerings.



Herbert Stein  
Member