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SENATE

{ REPORT  
No. 983

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PROVIDING FOR THE REFUND OR CREDIT OF THE INTERNAL-REVENUE TAX PAID ON SPIRITS LOST OR RENDERED UNMARKETABLE BY REASON OF THE FLOODS OF 1936 AND 1937

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JULY 27 (legislative day, JULY 25), 1939.—Ordered to be printed

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Mr. BARKLEY, from the Committee on Finance, submitted the following

## REPORT

[To accompany H. R. 1648]

The Committee on Finance, to whom was referred the bill (H. R. 1648) to provide for the refund or credit of the internal-revenue tax paid on spirits lost or rendered unmarketable by reason of the floods of 1936 and 1937 where such spirits were in the possession of the original taxpayer or rectifier for bottling or use in rectification under Government supervision as provided by law and regulations, having had the same under consideration, report it to the Senate without amendment and recommend that the bill do pass.

The purpose of the proposed legislation is fully explained in the report of the Committee on Ways and Means, House of Representatives, which accompanied the bill, and which is attached hereto and made a part of this report.

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[H. Rept. No. 1268, 76th Cong., 1st sess.]

The Committee on Ways and Means, to whom was referred the bill (H. R. 1648) to provide for the refund or credit of the internal-revenue tax paid on spirits lost or rendered unmarketable by reason of the floods of 1936 and 1937, where such spirits were in the possession of the original taxpayer or rectifier for bottling or use in rectification under Government supervision as provided by law and regulations, having had the same under consideration, report it back to the House with amendments, and recommend that the bill, as amended, do pass.

The amendments are as follows:

On page 2, in lines 22, 23, and 24, strike out the words "and the Commissioner of Customs".

On page 2, in line 18, after the word "paid" insert the word "as".

#### GENERAL STATEMENT

The purpose of the bill is to authorize the refund or credit of the internal-revenue tax paid to the Government on distilled spirits lost or rendered unmarketable by reason of the floods of the Ohio River in 1936 and 1937 where such spirits were in the possession of the original taxpayer or rectifier for bottling or use in rectification under Government supervision as required by law and regulations. The bill merely extends to a restricted class of producing taxpayers, namely rectifiers, the same relief extended to other manufacturers of distilled spirits, since losses without fraud in a rectifying plant represent one if not the only situation in which taxes are not abated or refunded with respect to the manufacture of distilled spirits, and

gives to rectifiers the same relief now provided by law in connection with loss of spirits in distilleries and warehouses, in connection with loss or destruction of beer, in connection with loss of brandy in wine fortification rooms, and in connection with loss or destruction of tobacco.

If the proposed relief is to be extended, it is conceded that this or similar legislation is necessary.

The disapproval of H. R. 1648 by the Treasury Department, in the opinion of your committee, is unjustified and the objections and apprehensions set forth in the letter addressed to Hon. Robert L. Doughton, chairman of the Ways and Means Committee, by Acting Secretary of the Treasury, dated March 4, 1939, are unwarranted and unfounded, as will be conclusively shown by the committee's detailed analysis set forth later in this report. It would appear that the Department's views, as set forth in its letter, are based on a misconception of the facts and without full regard to the provisions of the laws and regulations affecting the production, warehousing, withdrawal, and distribution of distilled spirits.

The Department's letter, and the committee's analysis and comments thereon, are as follows:

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MARCH 4, 1939.

HON. ROBERT L. DOUGHTON,  
Chairman, Committee on Ways  
and Means, House of Repre-  
sentatives, Washington, D. C.

MY DEAR MR. CHAIRMAN:

(1) Further reference is made to your letter of January 23, 1939, requesting the comments or recommendations of this Department with respect to the passage of bill H. R. 1648, and such information and comments as I may care to make relative to the questions raised by Mr. Boehne in his letter of January 20, 1939, addressed to you and referred to me. The purpose of the bill is to provide for the refund or credit of tax paid on spirits lost or rendered unmarketable by reason of the floods of 1936 and 1937 where such spirits were in the possession of the original taxpayer or rectifier for bottling or use in rectification under Government supervision as provided by law and regulations.

The proposed legislation is solely for the relief of original

(1) The committee respectfully submits that the letter of March 4, 1939, of the Treasury Department commenting upon H. R. 1648 does not present any proper or convincing reason why the bill should not receive favorable consideration of Congress. The letter is apparently based on a misconception of the facts involved.

In the second paragraph, the Department states that the proposed legislation affords relief to original taxpayers and rectifiers while offering no relief for others who suffered the loss of, or damage to, their distilled spirits, thus resulting in discrimination between classes of persons whose liquor was lost and between losses involving liquor and other property. *This bill in no way proposes a relief for property loss.* The only relief suggested is in re-

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taxpayers and rectifiers whose distilled spirits were lost or destroyed, or rendered unmarketable or useless by reason of the floods, and offers or proposes no relief for others who, by reason of the same floods, suffered the loss of, or damage to, their distilled spirits. The proposed legislation, therefore, discriminates between the classes of persons whose liquor was lost or destroyed or rendered unmarketable or useless. It further discriminates between losses involving liquor and other property, in favor of the losses involving the former.

(2) The proposed legislation purports, on its face, to be a general relief bill for the benefit of a whole class of persons. This class is described in general terms only and might therefore reasonably be expected to be a large one. In fact, however, as set forth in Mr. Boehne's letter to you, the bill is substantially for the benefit of a single individual, the Seagram Co.

gard to *taxes* on spirits which had not entered the trade and commerce of the country, and the proposal would have the effect of placing a *rectifying house on the same plane as distilleries, internal-revenue bonded warehouses, breweries, wine fortification rooms, and similarly related manufacturing plants.* As to discrimination between classes, there is no discrimination except a discrimination which already existed and which this bill is designed to correct. There can be no relief for taxes on spirits that have already left the control of the Government and have gone into the ordinary channels of trade and commerce. The relief sought here is for taxes paid on distilled *spirits that were still in the custody of the Government* and which had not entered the normal channels of commerce. Thus, there is no discrimination of any kind.

(2) Secondly, the Department states that the proposed legislation purports to be a general relief bill and, in fact, is substantially for the benefit of a single individual. *The committee submits that whether there be 1 company or 10 makes no difference* in the face of the factual situation here involved. That there may not be other distillers and rectifiers in the same situation is merely an act of Providence. Further, in the very next paragraph of the Department's letter, they state that no statistics are available to indicate the amount of taxes paid on distilled spirits lost by reason of the floods and, if that is so, it does not seem proper to state that only one company is involved. Even if there is but one company involved, the committee repeats that if the cause is a meritorious one, the number of persons involved is of no importance.

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(3) There are no statistics available in the Department to indicate the amount of taxes paid on distilled spirits, wines, fermented malt liquor, and other property lost by reason of the floods while in the possession of dealers and others, but it can safely be assumed that during a flood of the proportions of those of the Ohio and Mississippi Rivers in January and February of 1937, such losses were of huge proportions.

It would, of course, present an administrative problem of great magnitude to enact legislation which would authorize the refund of all taxes paid on all property lost or destroyed during such floods. Such legislation would necessarily open wide the door to those of a mind to defraud the Government. The number of claims submitted and the volume of investigative work required on such claims would severely tax the resources of the Bureau of Internal Revenue.

(4) The proposed legislation contemplates the refund of taxes to those of two classes only to whom the tax-paid spirits may be traced through the records of the Bureau of Internal Revenue. In our opinion legislation designed to sanction refunds to those whose losses can be proved through the

(3) The Department states that it would present an administrative problem of great magnitude to enact legislation which would authorize the refund of all taxes paid on all property lost or destroyed during such flood. *In the first place, there is no thought or suggestion that a refund of all taxes be paid on all property lost in the floods.* Such is obviously impossible. However, distilled spirits have always been treated entirely differently than any other type of property. They are subject to special taxes, such as the rectification tax, which is found nowhere else. They are also subject to a supervision and control by the Government over their manufacture, storage, and sale, which is not the case in any other industry. Other special internal-revenue taxes collected by the Government, such as taxes on oleomargarine, rubber tires and tubes, firearms, etc., are collected when the articles are sold. That is not true with respect to distilled spirits on which the tax is levied and collected before sale. It can thus be seen that distilled spirits have always been treated apart from other classes of property subject to tax. In addition, all that is sought here is to have rectifying plants placed on the same level regarding losses of spirits as distilleries, warehouses, and similar manufacturing plants, which are now accorded the protection that this bill seeks for rectifying plants.

(4) The Department further states that this legislation contemplates a refund only to those who can trace losses by Government records. There is no attempt to set up a classification based on Government records. *The Government records are referred to only as proof that the Govern-*

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use of official records while denying authority to make refunds to those whose bona fide losses are not provable through the use of such official records is neither fair nor just. Enactment of this legislation either in the form proposed or if broadened to afford relief to all whose tax-paid property was lost or damaged, would create an undesirable precedent for other legislation for refund of taxes paid on property of all kinds which may be destroyed or damaged after tax payment and withdrawal from the custody and control of the United States.

(5) Property of all kinds is forever subject to loss and damage. Fires, floods, storms, and the hazards of transportation take a huge toll each year from the business people of the country. Many losses are covered by insurance but where not so covered the losses fall heavily and with undiminished force upon the persons whose property was lost or damaged. The United States cannot be an insurer of the tax paid liquor in the control of the distiller or rectifier any more than it can be the insurer of the buildings or machinery with which they prepare such liquor for the market. The distillers and rectifiers are, it seems, in no different position than the importer of fine fabrics whose property, after duty payment, was lost or destroyed by reason of the floods. Such an importer is in no different position than the manufacturer or possessor of fine domestic fabrics lost or destroyed in the same floods. There seems to be no easily discernible connection between the payment of the tax on liquor and the refunds or credits proposed by the bill. The liquors involved had been re-

*ment has control and custody of the spirits and to insure prevention of any possibility of fraud since losses are provable by Government records, as will be shown later.*

(5) The Department's letter then points out that property is forever subject to loss and damage. *That is granted, but no claim for property loss or damage is made here.* The Department states that the United States cannot be an "insurer of the tax-paid liquor" any more than it can be the insurer of the distillery and plant. It is respectfully submitted that no such suggestion has been made and a reading of the bill makes this obvious. The only purpose of the bill as above stated is to *relieve the unjust payment of taxes upon liquor which did not enter into the commerce of the country, and no claim whatever is made for property loss.* As a matter of fact, the Seagram companies suffered very substantial property losses in the floods in question. When the spirits which were in the rectifying house were lost, the spirits had to be replaced with other spirits upon which the excise tax had to be paid, so that in effect in addition to the property loss, there is what amounts to double taxation. The Department finally states that the spirits involved have been removed from the custody and control of the

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moved from the control and custody of the United States and, having entered into the commerce of the country, should be accorded the same treatment as all other objects of commerce.

(6) In his letter of January 20, 1939, addressed to you, Mr. Boehne propounded six questions, which I shall set down hereafter and discuss.

(7) "Is it true that all distilled spirits that are in rectifying plants are under the constant supervision and control of the Bureau of Internal Revenue?"

The answer to this question must be in the negative. Rectifying plants are constructed and operated in accordance with regulations promulgated by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury. Each rectifying plant consists of three departments, each of which departments may consist of one or more rooms or floors of a building. One of the departments is the "receiving room," another is the "rectifying room," and the third is the "finished products room." All distilled spirits or wines coming into the possession of the rectifier at the rectifying plant are required to be deposited in the receiving room and proper record thereof made. Distilled spirits or wines which are to be rectified are dumped into rectifying or mixing tanks pursuant to approval of applications for permission to rectify. Records are made of the spirits or wines and other materials dumped for rectification; of the volume of the rectified product; and of the packaging thereof in bottles, barrels, etc.

United States. *This is not correct and can be easily discernible in the following paragraphs.*

(6) With reference to certain questions asked of the Department by Representative Boehne, the Department has made certain answers thereto which it is respectfully suggested convey an erroneous impression of the true situation and are calculated to excite undue alarm.

(7) The first question was whether or not it is true that all distilled spirits in a rectifying plant are under the constant supervision and control of the Bureau of Internal Revenue. This question is answered in the negative, based on a most peculiar construction of the statute and regulations, the reason being, as stated, that spirits in a rectifying plant are under the control of the Government only during the daylight hours. The committee believes that if the Government were to maintain control of the spirits only during the daylight hours and give the rectifier complete freedom of access and operation during the other hours it would be equivalent to saying that the Government does not control at all. If there is justification for supervision and control during the daylight hours, that same justification would seem to require supervision and control during the other hours of the day. The Department makes the statement that the Government is interested in a rectifying plant only for three reasons: First, to insure collection of the rectification tax; secondly, to insure compliance with the law and regulations pertaining to containers; and, thirdly, to insure com-

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Neither the rectifying plant as a whole nor the processing tanks are locked, but the bottling tanks are so equipped as to permit locking of the inlets and outlets thereof, and the keys to the locks used in such places are in the possession of the internal revenue storekeeper-gager. Therefore, the proprietor of the rectifying plant has ready and free access at all times to the entire plant, and to the spirits and wines therein, with the single exception of the spirits or wines in the locked bottling tanks. The finished product, when bottled or barreled, is removed from the rectifying room to the finished-products room.

In addition to the processes of rectifying spirits and wines, and bottling such rectified spirits and wines, rectifiers receive, ordinarily, a large quantity of spirits and wines which they bottle without rectification. All spirits, rectified or unrectified, bottled in a rectifying plant are required to be in liquor bottles procured pursuant to joint resolution of June 18, 1934, and Treasury Regulations No. 13, and must bear the stamp required under the Liquor Taxing Act of 1934.

Aside from the control of the bottling tanks mentioned heretofore, there is no physical control of the rectifying plant except during the daylight hours when an internal revenue storekeeper-gager is on duty at the plant. The primary control of the rectifying plant is through the accounting system and audit of the storekeeper-gager's records and reports, plus periodic visits by inspectors.

The basic taxes on distilled spirits and wines which are handled by a rectifier have been paid, and the interest of the Govern-

pliance with the law in respect to strip stamps. Obviously, if the Government is interested for the three purposes mentioned, it should exercise control of the plant 24 hours a day. Regulations No. 15 relating to rectifying plants provide in article 9 that no operations shall be carried on at a rectifying plant on Sunday, or between sundown and sunrise on weekdays, *or at any time except in the presence of a Government officer, unless special permission is obtained.* Therefore, no operations may be conducted at a rectifying plant between sundown and sunrise without special permission. If this is so, how can it be said that the rectifier has *free* access to and use of his plant during all except the daylight hours? That provision alone refutes the Department's statement. The "access" may be "free," but the operations are not. Further, all spirits brought into a rectifying plant must be entered on Federal Form 45, as provided in Regulations No. 15, article 20. Article II of the same regulations provides that all spirits received must be stored in the receiving room of the rectifying plant and remain there until permission is obtained on Form 122 to dump the spirits. That does not mean that the permission need be obtained only during the daylight hours and that the rectifier may do as he pleases thereafter. Further, no spirits may be bottled or barreled off and removed unless and until either Form 230 or Form 237 is executed and approved by the Bureau of Internal Revenue. As further supervision, Government locks are required on all storage tanks and all bottling tanks, and no activity whatever is permitted or possible until the



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ment in the rectifying plant is threefold: (1) Collection of the rectification tax of 30 cents per proof gallon on spirits and wines rectified; (2) compliance by the rectifier with the law and regulations pertaining to containers; and (3) compliance with the law in respect of strip stamps on containers of spirits. Otherwise, the Government has no interest in the rectifying plant, and the rectifier is at liberty to use it, subject to regulations, whenever he wishes. It may be said very definitely, therefore, that the distilled spirits which are in a rectifying plant are under the supervision and control of the Bureau of Internal Revenue only during the daylight hours.

(8) "Is it true that through the Government records, every gallon of distilled spirits can be accounted for at all times so that any losses occurring in the rectifying plant will be provable by Government records?"

Government officer unlocks those tanks and approves of the various application forms. The Department seems to make much of the point that other than the control of the locked bottling tanks, there is no "physical control" of the rectifying plant. In addition to the locked tanks in the rectifying plant, the Bureau has and must exercise "physical control" of all spirits entered into and withdrawn from the plant by applications presented to and approved by the district supervisor. The "physical control" of spirits in a rectifying plant include "the presence of a Government officer" and are subject to greater degree of supervision and control than in a distillery. Regulations further provide (article XXXIII) that Government officers assigned to rectifying plants must, among other things, inform themselves fully of all requirements of law and regulations pertaining to the operation of such plants, check each operation to know that such operation is in accordance with law and regulations, *have the custody of all keys to the Government locks on the storage and bottling tanks and other equipment*, and generally perform their duties in a spirit of cooperation with the rectifier, but that they must "*perform their supervisory duties in all cases,*" and such duties require the officers to observe that the requirements of the law and regulations are complied with and that there is no loss of revenue to the Government.

(8) The second question is whether or not it is true that every gallon of distilled spirits can be accounted for at all times in a rectifying house by Government records so that losses are provable by Government records.

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In the light of the discussion of question 1 just above, the answer to this question is in the negative. In the answer to question 1 there was discussed the freedom of access to the rectifying plant, and it is that access which warrants the negative answer.

The Department answers this question in the negative, based on its reasoning in answer to the first question. The committee feels that this answer is entirely erroneous. Under Regulations No. 15 afore-mentioned, all spirits brought into a rectifying plant must be reported on Federal Form 45, which shows the date the spirits are received, the name and address of the person from whom received, the name of the producer together with the number and location of the plant, the kind of spirits, the number of packages, the Government serial numbers of the packages, the wine gallons and the proof gallons. This form is submitted to the district supervisor for his permanent records. Spirits can be dumped only after permission is requested and obtained on Form 122. This form shows the name of the producer, the registered number and location of the plant at which produced, the kind of spirits, the serial number of the package, the date the package was filled, the date of the last official gage, the contents in wine and proof gallons, the Federal stamps attached, all of the details with respect to dumping, namely, gross weight, tare, net weight, etc., and the date dumped. These forms, too, are filed with the district supervisor. All spirits to be bottled without taxable rectification may be bottled only after the filing and approval of Form 230. This form is an application for permission to dump and shows the serial numbers of the packages, the date filled, the date of tax payment, the kind and number of stamps, the regage, gross weight, tare, net weight, wine gallons, and proof gallons. This form must be certified by the

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Government officer assigned to the plant and approved by the district supervisor. All spirits bottled or barrelled after taxable rectification may be bottled or barrelled only after Form 237 is presented, the tax paid, and such form approved by the local supervisor. Form 237 shows the serial number of the packages or bottling tank, the gross weight, tare, net weight, wine gallons, proof gallons, and serial numbers of the rectifier's stamps. This, too, must be certified by the Government officer attached to the plant and must be approved by the district supervisor, after he collects the tax. After the bottling tanks are emptied, there must be a certification of the number of cases filled, size of bottles, number of cases, serial numbers on the cases, and all-similar data, which again must be certified by the Government officer in charge, accounting therefore for all the spirits put into the bottling tanks.

The committee does not believe that the Department can seriously mean to leave the inference that because the rectifier may have "access" to the plant after the "daylight hours" (and during the daylight the plant is conceded to be under the Government's supervision and control) some of the spirits may be removed of which no record will be made. It must, therefore, be acknowledged that all losses occurring in a rectifying plant can be proved and established by the records kept at such plant.

(9) "Is it true that the present laws provide for abatements or refunds of taxes on distilled spirits in case of loss or disaster without fraud or collusion in distilleries and warehouses and during transfers in bond, but there is

(9) The next question was whether or not the present laws provided for abatement or refunds of taxes on distilled spirits in case of loss or disaster without fraud or collusion in distilleries and warehouses and during trans-

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no provision for losses or casualties sustained in a rectifying house?"

It is not true that the present laws provide for refunds in the manner set forth in the question. Herein lies the point of distinction between the abatement provided by the present laws and the refunds which the proposed bill would authorize. In the case of losses in the distillery, the tax which attached to the spirits immediately they came into existence, while ascertainable at any time through audit of the distillery records, has not been ascertained. In the case of losses in the warehouse, and during transfer in bond, the amount of tax due has been ascertained as to each package, but the tax has not yet been paid. Distilled spirits on which the tax has not yet been paid, are in bond. If the object of the taxation is destroyed at distilleries and warehouses and during transfers in bond, there is in existence a very definite record of the quantity thereof and the tax due thereon, and, since no money has passed, it is possible, with a measurable degree of safety to the revenue, to forgive the tax in the manner provided by law and mark the records accordingly.

fers in bond. The Department states that it is not true that the present laws provide for "refunds" under such circumstances. An effort is then made to show the distinction between the abatement of taxes on losses occurring in distilleries, warehouses, and during transportation, and refunds such as proposed by the bill. The importance attached to Government records for the purpose of ascertaining losses is recognized by the Department, it being stated that, if spirits are destroyed at distilleries and warehouses and during transfers in bond, "there is in existence a very definite record of the quantity thereof and the tax due thereon, and, since no money has passed, it is possible with a measureable degree of safety to forgive the tax and mark the records accordingly." Attention should be called to section 2901 (b) of the Internal Revenue Code wherein it is provided that "when any distilled spirits are destroyed by accidental fire or other casualty without any fraud, collusion, or negligence of the owner thereof, after the time when the same should have been drawn off by the storekeeper-gager and placed in the internal-revenue bonded warehouse provided by law, no tax shall be collected on such spirits so destroyed, *or if collected, it shall be refunded* upon the production of satisfactory proof that the spirits were destroyed as herein specified." It is apparent, therefore, that the Department has overlooked this provision of law. The records kept at a rectifying plant are as detailed and complete, if not more so, as the records kept at distilleries and warehouses. If the records are complete and accurate, the committee feels that it is beg-

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ging the question to say that these records are satisfactory in connection with the abatement of taxes but not for the refund. It cannot be possible for records to be accurate for one purpose and not for another. In this same connection, it is interesting to note that when a transfer in bond is made from one warehouse to another at a distant point, the shipment is made by railroad car. The only "physical control" that the Government has over this car is the bond of the shipper and the records of the shipment. In the rectifying house, there is certainly more "physical control" than that and the records are fully as complete.

(10) "Is it not true that the present laws provide that after beer has been tax-paid and a loss occurs, or the beer becomes spoiled while still in the possession of the taxpayer, refund of the excise tax is permitted?"

The statement set up in this question is substantially true, but the allowance of the refund is hedged about by conditions which place the brewer whose beer has become spoiled in a situation which is vastly different from the situation of the beneficiary under the proposed bill. Section 327 of the Liquor Tax Administration Act (U. S. C., Supp. 111, title 26, sec. 1330b) provides for the refund mentioned.

\* \* \* Upon filing of a claim therefor by the brewer and proof by him to the satisfaction of the Commissioner that such beer, lager beer, ale, porter, or other similar fermented malt liquor (1) was fully tax-paid; (2) was lawfully removed from his brewery to his bottling house, on or after March 22, 1933; (3) never was removed from such bottling house, except in the process of de-

(10) It is admitted by the Treasury Department in answer to question 4 that present laws provide for the refund of tax paid on beer when such beer is lost or becomes spoiled while in the possession of the brewer. The Department argues, however, that "the allowance of the refund is hedged about by conditions which place the brewer in a situation which is vastly different from the situation of the beneficiary under the present bill," apparently because the beer "passes through a meter and the exact quantity thereof is a matter of record." It is not believed that greater accuracy can be credited to meters in a brewery than to the methods of gaging provided by law for the determination of the quantity, proof, etc., of distilled spirits by Government officers. Attention is called to the fact that the gaging of spirits in the rectifying house is under the direct supervision of a Government officer called a "storekeeper-gager" and he certifies to the quantities listed on the Forms 45, 122, 230, and 237. There can be no "hazard to the

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struction or for return to the brewery; (4) had become unsalable without fraud, connivance, or collusion on his part; and (5) was destroyed by him in such bottling house in the presence of a representative of the Bureau of Internal Revenue, or was returned from such bottling house to the brewery in which made for use therein as brewing material.

In the case of the brewer, the tax-paid article passes through a meter and the exact quantity thereof is a matter of record; it has not left the place in which it was bottled; and no allowance or refund is made to the brewer unless the destruction of the article is accomplished in the presence of a representative of the Bureau of Internal Revenue, or the tax-paid material is returned to the brewery for further use as brewing material. In either event, such representative ascertains the exact quantity so destroyed or returned, and that it is the article which passed through the meter. This type of refund presents practically no hazard to the revenue.

(11) "Is it not true that under the present law, taxes are remitted or refunded in the event of loss of brandy intended for fortification of wine from storage tanks in bonded warehouses or from steel drums filled therefrom while such drums are in such warehouse, and in the fortification room of a bonded winery, provided there is no negligence, fraud, or collusion?"

The answer to this question is in the affirmative, so far as concerns the remission or abatement of the tax. However, brandy intended for fortification, whether in the warehouse or in the fortification room of a bonded winery, is not a tax-paid spirit. If in a

revenue" in accepting the Government records kept at a rectifying plant, otherwise the entire system of Government records should be discarded. The proof demanded by the present bill to be filed in support of the refund claim is substantially the same as the proof demanded of brewers, viz, that (1) the internal-revenue tax on spirits has been paid; (2) that the spirits were in the possession of claimant at the time of loss; (3) that such spirits were lost or rendered unmarketable or useless by reason of damage sustained as the result of the flood conditions; (4) that the spirits so rendered unmarketable or useless have been destroyed; and (5) that claimant was not indemnified against such loss by any valid claim of insurance or otherwise. If proof of this kind is furnished to the satisfaction of the Commissioner, there can be no "hazard to the revenue."

(11) It is admitted by the Treasury Department in answer to question 5 that the present law provides for the remission or refund in the event of loss of brandy intended for fortification from storage tanks or drums in bonded warehouses and while stored in the fortification rooms of a bonded winery. It is argued, however, that brandy intended for fortification, whether in the warehouse or in the fortification room of a bonded winery, is not a tax-paid spirit, and therefore, the tax is remitted or abated instead of refunded. It is also stated that "the use of the word 'refund' is not strictly accurate because the tax is not paid immediately upon

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warehouse, the tax thereon is covered by the bond of the warehouseman and the lien of the United States for the taxes on such brandy attaches not only to the brandy but to the warehouse building. When brandy is withdrawn by a winemaker for fortification of wine on bonded winery premises, it is subject to a tax of 10 cents per proof gallon when used in the fortification of wines, or at the rate of \$2 per proof gallon if not so used, and the payment of the tax at either rate is governed by the bond of the winemaker.

The fortification room is under the lock of the United States, with the key thereto in the possession of its representative. The winemaker is afforded access to the spirits therein only in the presence of such representative; records of the winemaker's removal of the spirits are made by the storekeeper-gager; and the winemaker is required to account for the use of the spirits for fortification before it is charged to him at the 10-cent rate. The payment of the tax on brandy used in fortification is postponed, by statute, for a period of 18 months. In any event, complete Government records exist covering all brandy removed, and used, for fortification, and the losses allowed by law must be proved to the Commissioner before the tax on the spirits lost is remitted or abated. The use of the word "refund" is not strictly accurate because the tax is not paid immediately upon withdrawal for fortification, but is merely charged against the winemaker under his bond.

(12) "Is it not true that present laws provide for a refund of taxes paid on tobacco which is

withdrawal for fortification but is merely charged against the winemaker under his bond." If the use of the term "refund" is not "strictly accurate," the Congress must have been confused or in error for we find such terms in connection with losses of brandy in section 2901 (b) and section 3031 (b) of the Internal Revenue Code. Although, as stated, the tax on brandy used in fortification is 10 cents per proof gallon on the brandy used to be paid within 18 months from the date of notice of assessment, it is apparent that the Congress intended that the tax may be paid within the 18-month period and prior to its use in fortification and, if so paid, and the brandy lost or destroyed, such tax was to be refunded. A bonded winery or the fortification room in a bonded winery can be regarded as similar to a rectifying plant for the operations conducted in both places are carefully controlled by regulations and detailed records are prescribed. A rectifying plant, like a fortification room, is covered by a bond to insure payment of taxes.

(12) The last question was whether or not another precedent existed in that the laws provided

## TREASURY DEPARTMENT LETTER

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lost or destroyed while in the possession of the taxpayer?"

The procedure in respect of tobacco is such that the answer to No. 6 is substantially in the affirmative. The taxes on tobacco, snuff, cigars, and cigarettes are paid by stamps which have a money value. Section 1 of the act of May 12, 1900 (U. S. C., title 26, sec. 1424), authorized the Commissioner of Internal Revenue to make allowance for or redeem such of the stamps, issued under authority of the law, to denote the payment of any internal-revenue tax, as may have been spoiled, destroyed, or rendered useless or unfit for the purpose intended, or for which the owner had no use, or which through mistake may have been improperly or unnecessarily used, or where the rates or duties represented thereby had been excessive in amount, paid in error, or in any manner wrongfully collected.

By the act of March 3, 1931, it was further provided that internal-revenue stamps affixed to packages of tobacco, snuff, cigars, or cigarettes which, after removal from the factory or customhouse for consumption or sale, and which the manufacturer or importer withdrew from the market, might, under regulations prescribed by the Commissioner, be redeemed. It is to be noted (1) that the procedure in respect of tobacco, snuff, cigars, and cigarettes withdrawn from the market is not by way of a refund of the tax paid, but by a redemption of the tax stamps which have a money value, and (2) that the procedure (substantially a refund) is authorized by a statute which limits the redemptions to the tax stamps on the four commodities specifically named in the statute. The stamp placed on a

for a refund of taxes paid on tobacco which is lost or destroyed while in the possession of the taxpayer. The Department admits that this question must be answered in the affirmative. Apparently a distinction by the Department is attempted to be made on the ground that tobacco taxes are paid by stamps and that the refund takes the form of a redemption of the tax stamp. There can be no valid distinction proved between different methods of tax payment. Another distinction is attempted by the Department in that it is stated that the act covering tobacco grants all manufacturers and importers the privilege of redemption of tax stamps whereas the proposed bill grants relief to a single taxpayer. The committee believes that this objection had been adequately answered above.



## TREASURY DEPARTMENT LETTER

## COMMITTEE ANALYSIS

package of distilled spirits at the time of the withdrawal of the spirits from bond indicates exactly, as in the case of stamps for tobacco, snuff, cigars, and cigarettes, the amount of tax paid on spirits. As to the four commodities mentioned, the refund of the tax (redemption of the stamps) is accomplished under a statute representing the will of Congress whereby all manufacturers and importers of the four commodities were, in 1931, placed in the same position in respect of the privilege of redemption, whereas it is the purpose of the proposed bill to grant to a single taxpayer a privilege which has been denied others.

(13) Since the law is silent as to refunds of the distilled-spirits tax in cases where there have been destructions of tax-paid spirits, it follows that there can be no refunds without statutory authority therefor.

(14) This Department considers this bill, which is admittedly for the relief of one taxpayer in respect of losses of tax-paid spirits in a specified manner in certain years, to be in derogation of the general law applicable to all other taxpayers. It is our opinion that this bill ought not to be passed, and it is so recommended.

Mr. Boehne's letter is returned herewith.

The Department has been advised by the Bureau of the Budget that there would be no objection to the presentation of this report.

Very truly yours,

JOHN W. HANES,

*Acting Secretary of the Treasury.*

(13) The Department then states that since the law is silent as to refunds of the distilled-spirits tax in cases where there has been destruction of tax-paid spirits, it follows that there can be no refunds of the tax paid without authority therefor. If relief is to be granted, therefore, the necessity for this bill is admitted.

(14) The Department concludes its letter by stating that it believes this bill to be in derogation of the general law applicable to all other taxpayers. The committee believes that the purpose of this bill is to give a restricted class of producing taxpayers the same relief extended to other manufacturers of distilled spirits, since losses without fraud in a rectifying plant represent one if not the only situation in which taxes are not abated or refunded with respect to the manufacture of distilled spirits.

In conclusion, therefore, the committee find:

1. That a rectifying house is under the constant supervision and control of the Government.

2. That the relief sought by H. R. 1648 is for taxes only, not the property loss, on merchandise that was lost while in the custody and control of the Government, and not on merchandise lost after it had entered the normal channels of commerce.

3. That a complete and accurate record, certified by Government officers, is available covering every package of liquor that goes into or comes out of a rectifying house.

4. That the rectifier, therefore, is in no different position than a distiller or warehouseman, and it is mere oversight or unintentional neglect that the rectifier is not now afforded the relief granted to other manufacturers. Further on this same point, the rectifier in many cases is also the distiller, for most distillers operate rectifying plants in connection with their distilling operations. The rectifier, therefore, is not a strange creature to be considered completely apart from distillers.

5. That the proposed bill will not create but will follow a precedent.

6. That there is ample evidence of the precedents established in connection with loss of spirits in distilleries and warehouses, in connection with loss or destruction of beer, in connection with loss of brandy in wine-fortification rooms, and in connection with loss or destruction of tobacco.

The committee feel, therefore, that the relief sought is justified in law, equity, and common sense.

## MINORITY VIEWS OF HON. JERE COOPER ON THE BILL H. R. 1648

It is with regret that I find myself in disagreement with a majority of the members of the Committee on Ways and Means with respect to the bill H. R. 1648. In opposing the enactment of this bill I invite attention to the adverse report from the Treasury Department as stated in the following letter from the Acting Secretary:

TREASURY DEPARTMENT,  
Washington, March 4, 1939.

HON. ROBERT L. DOUGHTON,  
*Chairman, Committee on Ways and Means,  
House of Representatives, Washington, D. C.*

MY DEAR MR. CHAIRMAN: Further reference is made to your letter of January 23, 1939, requesting the comments or recommendations of this Department with respect to the passage of bill H. R. 1648, and such information and comments as I may care to make relative to the questions raised by Mr. Boehne in his letter of January 20, 1939, addressed to you and referred to me. The purpose of the bill is to provide for the refund or credit of tax paid on spirits lost or rendered unmarketable by reason of the floods of 1936 and 1937 where such spirits were in the possession of the original taxpayer or rectifier for bottling or use in rectification under Government supervision as provided by law and regulations.

The proposed legislation is solely for the relief of original taxpayers and rectifiers whose distilled spirits were lost or destroyed, or rendered unmarketable or useless by reason of the floods, and offers or proposes no relief for others who, by reason of the same floods, suffered the loss of, or damage to, their distilled spirits. The proposed legislation therefore discriminates between the classes of persons whose liquor was lost or destroyed or rendered unmarketable or useless. It further discriminates between losses involving liquor and other property, in favor of the losses involving the former.

The proposed legislation purports, on its face, to be a general relief bill for the benefit of a whole class of persons. This class is described in general terms only and might therefore reasonably be expected to be a large one. In fact, however, as set forth in Mr. Boehne's letter to you, the bill is substantially for the benefit of a single individual, the Seagram Co.

There are no statistics available in the Department to indicate the amount of taxes paid on distilled spirits, wines, fermented malt liquor, and other property lost by reason of the floods while in the possession of dealers and others, but it can safely be assumed that during a flood of the proportions of those of the Ohio and Mississippi Rivers in January and February of 1937 such losses were of huge proportions.

It would, of course, present an administrative problem of great magnitude to enact legislation which would authorize the refund of all taxes paid on all property lost or destroyed during such floods. Such legislation would necessarily open wide the door to those of a mind to defraud the Government. The number of claims submitted and the volume of investigative work required on such claims would severely tax the resources of the Bureau of Internal Revenue. The proposed legislation contemplates the refund of taxes to those of two classes only to whom the tax-paid spirits may be traced through the records of the Bureau of Internal Revenue. In our opinion legislation designed to sanction refunds to those whose losses can be proved through the use of official records while denying authority to make refunds to those whose bona fide losses are not provable through the use of such official records is neither fair nor just. Enactment of this legislation either in the form proposed or if broadened to

afford relief to all whose tax-paid property was lost or damaged, would create an undesirable precedent for other legislation for refund of taxes paid on property of all kinds which may be destroyed or damaged after tax payment and withdrawal from the custody and control of the United States.

Property of all kinds is forever subject to loss and damage. Fires, floods, storms, and the hazards of transportation take a huge toll each year from the business people of the country. Many losses are covered by insurance, but where not so covered the losses fall heavily and with undiminished force upon the persons whose property was lost or damaged. The United States cannot be an insurer of the tax-paid liquor in the control of the distiller or rectifier any more than it can be the insurer of the buildings or machinery with which they prepare such liquor for the market. The distillers and rectifiers are, it seems, in no different position than the importer of fine fabrics whose property, after duty payment, was lost or destroyed by reason of the floods. Such an importer is in no different position than the manufacturer or possessor of fine domestic fabrics lost or destroyed in the same floods. There seems to be no easily discernible connection between the payment of the tax on liquor and the refunds or credits proposed by the bill. The liquors involved had been removed from the custody and control of the United States and, having entered into the commerce of the country, should be accorded the same treatment as all other objects of commerce.

In his letter of January 20, 1939, addressed to you, Mr. Boehne propounded six questions, which I shall set down hereafter and discuss.

1. Is it true that all distilled spirits that are in a rectifying plant are under the constant supervision and control of the Bureau of Internal Revenue?

The answer to this question must be in the negative. Rectifying plants are constructed and operated in accordance with regulations promulgated by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury. Each rectifying plant consists of three departments, each of which departments may consist of one or more rooms or floors of a building. One of the departments is the receiving room, another is the rectifying room, and the third is the finished-products room. All distilled spirits or wines coming into the possession of the rectifier at the rectifying plant are required to be deposited in the receiving room and proper record thereof made. Distilled spirits or wines which are to be rectified are dumped into rectifying or mixing tanks pursuant to approval of applications for permission to rectify. Records are made of the spirits or wines and other materials dumped for rectification, of the volume of the rectified product, and of the packaging thereof in bottles, barrels, etc. Neither the rectifying plant as a whole, nor the processing tanks are locked, but the bottling tanks are so equipped as to permit locking of the inlets and outlets thereof, and the keys to the locks used in such places are in the possession of the internal revenue storekeeper-gauger. Therefore, the proprietor of the rectifying plant has ready and free access at all times to the entire plant and to the spirits and wines therein, with the single exception of the spirits or wines in the locked bottling tanks. The finished product, when bottled or barreled, is removed from the rectifying room to the finished-products room.

In addition to the processes of rectifying spirits and wines, and bottling such rectified spirits and wines, rectifiers receive ordinarily a large quantity of spirits and wines which they bottle without rectification. All spirits, rectified or unrectified, bottled in a rectifying plant are required to be in liquor bottles procured pursuant to joint resolution of June 18, 1934, and Treasury Regulations No. 13, and must bear the stamp required under the Liquor Taxing Act of 1934.

Aside from the control of the bottling tanks mentioned heretofore, there is no physical control of the rectifying plant except during the daylight hours when an internal revenue storekeeper-gauger is on duty at the plant. The primary control of the rectifying plant is through the accounting system and audit of the storekeeper-gauger's records and reports, plus periodic visits by inspectors.

The basic taxes on distilled spirits and wines which are handled by a rectifier have been paid, and the interest of the Government in the rectifying plant is three-fold: (1) Collection of the rectification tax of 30 cents per proof gallon on spirits and wines rectified; (2) compliance by the rectifier with the law and regulations pertaining to containers; and (3) compliance with the law

in respect of strip stamps on containers of spirits. Otherwise, the Government has no interest in the rectifying plant, and the rectifier is at liberty to use it, subject to regulations, whenever he wishes. It may be said very definitely, therefore, that the distilled spirits which are in a rectifying plant are under the supervision and control of the Bureau of Internal Revenue only during the daylight hours.

2. Is it true that through the Government records every gallon of distilled spirits can be accounted for at all times so that any losses occurring in the rectifying plant will be provable by Government records?

In the light of the discussion of question 1 just above, the answer to this question is in the negative. In the answer to question 1 there was discussed the freedom of access to the rectifying plant, and it is that access which warrants the negative answer.

3. Is it true that the present laws provide for abatements or refunds of taxes on distilled spirits in case of loss or disaster without fraud or collusion in distilleries and warehouses and during transfers in bond, but there is no provision for losses or casualties sustained in a rectifying house?

It is not true that the present laws provide for refunds in the manner set forth in the question. Herein lies the point of distinction between the abatement provided by the present laws and the refunds which the proposed bill would authorize. In the case of losses in the distillery, the tax which attached to the spirits immediately they came into existence, while ascertainable at any time through audit of the distillery records, has not been ascertained. In the case of losses in the warehouse, and during transfer in bond, the amount of tax due has been ascertained as to each package, but the tax has not yet been paid. Distilled spirits on which the tax has not been paid are in bond. If the object of the taxation is destroyed at distilleries and warehouses, and during transfers in bond, there is in existence a very definite record of the quantity thereof and the tax due thereon and, since no money has passed, it is possible, with a measurable degree of safety to the revenue, to forgive the tax in the manner provided by law and mark the records accordingly.

4. Is it not true that the present laws provide that after beer has been tax-paid and a loss occurs, or the beer becomes spoiled while still in the possession of the taxpayer, refund of the excise tax paid is permitted?

The statement set up in this question is substantially true, but the allowance of the refund is hedged about by conditions which place the brewer whose beer has become spoiled in a situation which is vastly different from the situation of the beneficiary under the proposed bill. Section 327 of the Liquor Tax Administration Act (U. S. C., supp. III, title 26, sec. 1330b), provides for the refund mentioned,

"\* \* \* upon the filing of a claim therefor by the brewer and proof by him to the satisfaction of the Commissioner that such beer, lager beer, ale, porter, or other similar fermented malt liquor (1) was fully tax-paid, (2) was lawfully removed from his brewery to his bottling house on or after March 22, 1933, (3) never was removed from such bottling house, except in the process of destruction or for return to the brewery, (4) had become unsalable without fraud, connivance, or collusion on his part, and (5) was destroyed by him in such bottling house in the presence of a representative of the Bureau of Internal Revenue, or was returned from such bottling house to the brewery in which made for use therein as brewing material."

In the case of the brewer, the tax-paid article passes through a meter and the exact quantity thereof is a matter of record; it has not left the place in which it was bottled; and no allowance or refund is made to the brewer unless the destruction of the article is accomplished in the presence of a representative of the Bureau of Internal Revenue, or the taxpaid material is returned to the brewery for further use as brewing material. In either event, such representative ascertains the exact quantity so destroyed or returned, and that it is the article which passed through the meter. This type of refund presents practically no hazard to the revenue.

5. Is it not true that under the present law, taxes are remitted or refunded in the event of loss of brandy intended for fortification of wine

from storage tanks in bonded warehouses or from steel drums filled therefrom while such drums are in such warehouse, and in the fortification room of a bonded winery, provided there is no negligence, fraud, or collusion?

The answer to this question is in the affirmative, so far as concerns the remission or abatement of the tax. However, brandy intended for fortification, whether in the warehouse or in the fortification room of a bonded winery, is not a tax-paid spirit. If in a warehouse, the tax thereon is covered by the bond of the warehouseman and the lien of the United States for the taxes on such brandy attaches not only to the brandy but to the warehouse building. When brandy is withdrawn by a winemaker for fortification of wine on bonded winery premises, it is subject to a tax of 10 cents per proof gallon when used in the fortification of wines or at the rate of \$2 per proof gallon if not so used, and the payment of the tax at either rate is covered by the bond of the winemaker.

The fortification room is under the lock of the United States, with the key thereto in the possession of its representative. The winemaker is afforded access to the spirits therein only in the presence of such representative; records of the winemaker's removal of the spirits are made by the storekeeper-gager; and the winemaker is required to account for the use of the spirits for fortification before it is charged to him at the 10-cent rate. The payment of the tax on brandy used in fortification is postponed, by statute, for a period of 18 months. In any event, complete Government records exist covering all brandy removed, and used, for fortification, and the losses allowed by law must be proved to the Commissioner before the tax on the spirits lost is remitted or abated. The use of the word "refund" is not strictly accurate because the tax is not paid immediately upon withdrawal for fortification, but is merely charged against the winemaker under his bond.

6. Is it not true that present laws provide for a refund of taxes paid on tobacco which is lost or destroyed while in the possession of the taxpayer?

The procedure in respect of tobacco is such that the answer to No. 6 is substantially in the affirmative. The taxes on tobacco, snuff, cigars, and cigarettes are paid by stamps which have a money value. Section 1 of the act of May 12, 1900 (U. S. C., title 26, sec. 1424), authorized the Commissioner of Internal Revenue to make allowance for or redeem such of the stamps, issued under authority of the law, to denote the payment of any internal-revenue tax, as may have been spoiled, destroyed, or rendered useless or unfit for the purpose intended, or for which the owner had no use, or which through mistake may have been improperly or unnecessarily used, or where the rates or duties represented thereby had been excessive in amount, paid in error, or in any manner wrongfully collected.

By the act of March 3, 1931, it was further provided that internal-revenue stamps affixed to packages of tobacco, snuff, cigars, or cigarettes which, after removal from the factory or customhouse for consumption or sale, and which the manufacturer or importer withdrew from the market might, under regulations prescribed by the Commissioner, be redeemed. It is to be noted (1) that the procedure in respect of tobacco, snuff, cigars, and cigarettes withdrawn from the market is not by way of a refund of the tax paid, but by a redemption of the tax stamps which have a money value; and (2) that the procedure (substantially a refund) is authorized by a statute which limits the redemptions to the tax stamps on the four commodities specifically named in the statute. The stamp placed on a package of distilled spirits at the time of the withdrawal of the spirits from bond indicates exactly, as in the case of stamps for tobacco, snuff, cigars, and cigarettes, the amount of tax paid on spirits. As to the four commodities mentioned, the refund of the tax (redemption of the stamps) is accomplished under a statute representing the will of Congress whereby all manufacturers and importers of the four commodities were, in 1931, placed in the same position in respect of the privilege of redemption, whereas it is the purpose of the proposed bill to grant to a single taxpayer a privilege which has been denied others. Since the law is silent as to refunds of the distilled-spirits tax in cases where there have been destructions of tax-paid spirits, it follows that there can be no refunds without statutory authority therefor.

This Department considers this bill, which is admittedly for the relief of one taxpayer in respect of losses of tax-paid spirits in a specified manner in certain years, to be in derogation of the general law applicable to all other taxpayers. It is our opinion that this bill ought not to be passed, and it is so recommended.

Mr. Boehne's letter is returned herewith.

The Department has been advised by the Bureau of the Budget that there would be no objection to the presentation of this report.

Very truly yours,

JOHN W. HANES,  
*Acting Secretary of the Treasury.*

My opposition to this bill is largely based upon the reasons appearing in this letter.

JERE COOPER.

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