

FLOOR-STOCK TAX ON DISTILLED SPIRITS

HEARING

BEFORE THE

COMMITTEE ON FINANCE UNITED STATES SENATE

SEVENTY-FIFTH CONGRESS

THIRD SESSION

ON

H. J. Res. 683

A JOINT RESOLUTION TO PROVIDE FOR A FLOOR TAX
ON DISTILLED SPIRITS, EXCEPT BRANDY

JUNE 8, 1938

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FLOOR-STOCK TAX ON DISTILLED SPIRITS

TUESDAY, JUNE 8, 1938

UNITED STATES SENATE,
COMMITTEE ON FINANCE,
Washington, D. C.

The committee met, pursuant to call, at 2 p. m., in the District Committee Room, Capitol, Senator Pat HARRISON (chairman) presiding.

(The committee had under consideration H. J. Res. 683, to provide for a floor stock tax on distilled spirits, except brandy, as follows:)

[H. J. Res. 683, 75th Cong., 3d sess.]

JOINT RESOLUTION To provide for a floor stock tax on distilled spirits, except brandy

Resolved by the Senate and House of Representatives of the United States of America in Congress assembled. That there shall be levied, assessed, collected, and paid a floor tax of 25 cents on each proof-gallon and a proportionate tax at a like rate on all fractional parts of such proof-gallon upon all distilled spirits, except brandy, produced in or imported into the United States upon which the internal-revenue tax imposed by law has been paid and which, on July 1, 1938, are held by a retail dealer in liquors in a quantity in excess of two hundred and fifty wine-gallons in the aggregate or by any other person, corporation, partnership, or association in any quantity and which are intended for sale for beverage purposes or for use in the manufacture or production of any article intended for sale for beverage purposes.

Each retail dealer in liquors and each person required hereunder to pay the floor tax shall within thirty days after July 1, 1938, make return under oath in such form and under such regulations as the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, shall prescribe. Payment of the tax shown to be due may be extended to a date not exceeding seven months after July 1, 1938, upon the filing of a bond for payment in such form and amount and with such surety or sureties as the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, may prescribe.

All provisions of law, including penalties, applicable in respect of internal-revenue taxes on distilled spirits shall, insofar as applicable and not inconsistent with this section, be applicable in respect of the floor tax imposed hereunder.

Passed the House of Representatives June 6, 1938.

Attest:

SOUTH TRIMBLE, *Clerk.*

The CHAIRMAN. Gentlemen, we have before us a joint resolution that was passed by the House providing for a floor stock tax on distilled spirits, except brandy. I have asked some of the gentlemen who are familiar with this matter to appear before the committee, and there are some requests by certain representatives of the industry. Any action that is to be taken on this joint resolution must be taken quickly.

Mr. Berkshire.

**STATEMENT OF STEWART BERKSHIRE, DEPUTY COMMISSIONER,
BUREAU OF INTERNAL REVENUE, TREASURY DEPARTMENT**

The **CHAIRMAN**. Will you give us your views with reference to this matter? I wish you would first make a brief explanation as to just what this joint resolution does.

Mr. BERKSHIRE. Gentlemen, it will be recalled that the Revenue Act of 1938 placed a tax on distilled spirits of \$2.25 a proof gallon, effective July 1, 1938. The present tax rate and the one which is now in force and will be until July 1 is \$2 a proof gallon.

Heretofore when the basic tax on spirits, and I understand also with respect to other commodities, has been raised there has likewise been a compensatory tax levied on floor stocks, stocks of liquors which are now in the hands of retailers, wholesalers, rectifiers, and also distillers which has been tax-paid and which will be on hand when the new tax rate becomes effective.

This resolution will place a tax of 25 cents, which would represent the amount of the increase which will be effective on July 1, 1938, on all distilled spirits which have been theretofore tax-paid and held on that day by any of these dealers.

Senator BROWN. When does the bill that we passed a couple of weeks ago take effect?

Mr. BERKSHIRE. On July 1, 1938. The idea being not only to tax and to obtain the revenue which this 25 cents will produce on the stocks which will normally be on the floors as of that date, but we think the most important purpose of such a resolution is to prevent excessive withdrawals of spirits between now and July 1 in order to avail themselves of the \$2 tax rate and save 25 cents a gallon. We are confident that that would occur, that there would be excessive withdrawals between now and July 1.

The **CHAIRMAN**. How much revenue is involved in this floor tax, if any? How much of a saving in taxes to the Government is there by virtue of the passing of this resolution?

Mr. BERKSHIRE. We think that the stocks on the floor would probably not produce more than \$4,000,000 or \$5,000,000, Senator, but we do think that the amount of liquor which they might withdraw anticipating the increase as of July 1 would be many times that much. We have estimated it would run in the neighborhood of \$12,000,000 to \$15,000,000.

The **CHAIRMAN**. The 25 cents increased tax was estimated to produce I think around \$21,000,000 or \$20,000,000.

Mr. BERKSHIRE. Something like \$19,000,000 or \$20,000,000, I think.

The **CHAIRMAN**. Was that an estimate of the Treasury Department?

Mr. BERKSHIRE. Yes, sir; I believe Mr. Magill stated that.

The **CHAIRMAN**. Did you take into consideration, in making that estimate, a loss by virtue of having no floor tax in the bill at that time?

Mr. BERKSHIRE. I think not. I think that that estimate was based on the amount of the anticipated withdrawals next year. I am satisfied it did not, Senator.

The **CHAIRMAN**. I see. Well now, it is your estimate that we will obtain how much more than the \$19,000,000 or \$21,000,000, estimated by virtue of the passage of this resolution?

Mr. BERKSHIRE. You will hold what you have got. You will supplement that by the collection of the amount which it will produce, collected from stocks normally on hand as of July 1, and it will prevent withdrawals in excessive amounts, and the amount which we will save will be included in that \$19,000,000. In other words, if \$19,000,000 is the amount we expect to collect from the 25 cents next year, that amount will be reduced to the extent of the amount of anticipated withdrawals between now and July 1. So you would not have \$19,000,000, but you would have some lesser amount.

The CHAIRMAN. Did the Treasury have anything to do with the drafting of this resolution when it was offered on the floor of the House?

Mr. BERKSHIRE. I do not think it did, Senator. Some two or three changes have been made in it since. I think that is a correct statement, is it not, Mr. Spingarn, that the Treasury had nothing to do with the drafting of the resolution?

Mr. SPINGARN (of the Treasury Department). Nothing at all.

The CHAIRMAN. Did the Treasury point out at that time that they ought to have a floor tax?

Mr. BERKSHIRE. Senator, I think at the time that the bill was originally introduced the Treasury had not. I think that is correct.

Senator TOWNSEND. Who introduced this resolution in the House?

Mr. BERKSHIRE. The first concurrent resolution was introduced, I think, by Mr. Robertson of Virginia. I suppose that was withdrawn for the reason that the tax bill went through, and this amendment was proposed by Congressman O'Neal.

The CHAIRMAN. What happened in the House when they struck out that 1 (b), I think it was, where they expected to get quite a revenue? They had to raise the revenue some way, and this was one of the methods that they employed, by the introduction of this amendment. At that time the Treasury took no position, is that not correct?

Mr. BERKSHIRE. That is correct, Senator.

The CHAIRMAN. They took no position when the matter came over to us?

Mr. BERKSHIRE. That is right.

The CHAIRMAN. We struck it out because we had raised what we thought was enough revenue from the flat corporation tax instead of the undistributed-profits tax. Then in conference, when we had to go back to the 2½ percent differential on the undistributed-profits tax, we had to accept this.

Mr. BERKSHIRE. Yes.

The CHAIRMAN. But it was in such a position that we could not apply the floor tax, with this amendment in the House bill, because it was subjected to a point of order.

Mr. BERKSHIRE. Yes.

The CHAIRMAN. Now the Treasury, even though it did not take a stand on it at those stages, does now take the position that there ought to be a floor tax?

Mr. BERKSHIRE. That is correct.

The CHAIRMAN. And they are now in favor of this proposition, and they took that position before the House Ways and Means Committee?

Mr. BERKSHIRE. Yes, sir; that is correct, Senator.

The CHAIRMAN. Now, may I ask you about the industry that is affected here? Are they pretty much in agreement with this resolution, that this floor tax ought to be imposed?

Mr. BERKSHIRE. I think that is demonstrated very definitely by the evidence produced before the Ways and Means Committee. It seemed that almost all branches of the trade were represented there and were urging the passage of this bill. I think that is a fair statement, Senator.

The CHAIRMAN. There is some opposition from some sources in the trade?

Mr. BERKSHIRE. I heard there have been some groups of retailers maybe here and there, although I believe that the heads of the retail organizations, after studying the bill, are now satisfied that they should have the floor tax.

The CHAIRMAN. Does anyone of the committee desire to ask any questions?

Senator WALSH. Would this involve increasing the force of Internal Revenue officers?

Mr. BERKSHIRE. We do not think it would, Senator. We handled it in 1934 without an increase, and I think we could again. We will just work the force a little harder.

Senator WALSH. Of course the floor tax then extended to other things than liquor.

Mr. BERKSHIRE. Of course it may require more men. I was only informed as to the tax on liquor.

Senator WALSH. I am quite sure there was an increase in personnel. It may not be due to this floor tax, but to some other floor taxes.

Senator BROWN. What is the reason for the exemption of brandy?

Mr. BERKSHIRE. Because the tax rate on brandy was not increased in the Revenue Act.

The CHAIRMAN. What is the reason for the exemption of 250 gallons?

Mr. BERKSHIRE. I take it it was the purpose of the Ways and Means Committee to relieve the small dealer. That was the class which seemed to be opposed to the resolution, and it was their thought that this exemption would relieve them, the 250 gallons being sufficient to exempt practically all the small retailers.

The CHAIRMAN. What position does the Treasury take with reference to that exemption?

Mr. BERKSHIRE. The Treasury takes the position, Senator, that that is excessive. We think 100 gallons would exempt certainly all of the retailers whom this tax would at least slightly affect in a financial way. Of course, they would all get the 100 gallon exemption whether they have 50 gallons or 100 gallons, or 1,000 gallons, and they would pay on the excess.

The CHAIRMAN. How many gallons does the ordinary retail liquor store carry?

Mr. BERKSHIRE. The package store, such as we see along the streets of Washington, would carry more than the average retail liquor dealer. I think that the evidence disclosed that they would have average stocks of 500 or 600 gallons, but the average retail liquor dealer, which would include all of the tavern keepers in country, and even hotels, unless it is a very large hotel, would not have even 250 gallons of liquor at one time.

Senator BAILEY. How much money would it raise? What would be the revenue?

Mr. BERKSHIRE. We had felt it would produce \$4,000,000 or \$5,000,000, Senator, but with this 250-gallon exemption to all retailers, that will be materially reduced. It might be reduced by one-half.

Senator BAILEY. There is only about \$2,000,000 involved?

Mr. BERKSHIRE. That is all it represents in taxes.

Senator LONERGAN. In the original revenue bill the Treasury made no recommendation for this tax, did it?

Mr. BERKSHIRE. The Treasury opposed the tax increase, so there was not any point in that.

Senator LONERGAN. The Treasury is not behind this resolution, is it? Originally was the Treasury behind the resolution?

Mr. BERKSHIRE. No, sir.

Senator LONERGAN. You say the Treasury wants it now?

Mr. BERKSHIRE. We think that that is the reasonable, normal, and proper thing to do.

Senator LONERGAN. Why?

Mr. BERKSHIRE. We feel not so much on account of the \$2,500,000 or \$3,000,000 or \$4,000,000 that it will produce, collected from normal stocks which will be on hand on July 1, but we believe, in fact we are confident that there will be excessive withdrawals between now and July 1 which would rob the Treasury of our anticipated income this year of \$12,000,000 or \$14,000,000.

Senator LONERGAN. Withdrawals from where?

Mr. BERKSHIRE. Withdrawals from bonded warehouses, to avoid the 25-cent increase.

Senator WALSH. Could not you apply this tax to the bonded warehouses and not to the retailers?

Mr. BERKSHIRE. No, Senator, I do not see how you could do that. There is not any tax until they withdraw.

Senator WALSH. So the wholesalers who can afford to stock up would deprive the Government of this tax later, when it is levied after July 1?

Mr. BERKSHIRE. Yes, sir.

Senator WALSH. And there will be a period of time when there will not be a tax collected?

Mr. BERKSHIRE. That is right.

Senator WALSH. Now, there would be a great shrinkage or loss from the bonded warehouses if the liquor were withdrawn between now and July 1, is not that correct?

Mr. BERKSHIRE. There will not be any purpose in withdrawing if the tax is on.

Senator WALSH. So that the withdrawals would have to come from bonded warehouses?

Mr. BERKSHIRE. That is where it would have to come from.

Senator WALSH. Why not make the tax just applicable to them? Is there any objection to that? Why not make the tax just applicable to them instead of these little fellows and having a lot of agents going around and taking account of stock?

Mr. BERKSHIRE. I do not see how you can do that.

Senator JOHNSON. Don't you almost do that with this exemption of 250 wine-gallons?

Mr. BERKSHIRE. You certainly take care of all the retailers with this 250-gallon exemption, and some others besides.

Senator JOHNSON. As I understood your testimony a few minutes ago, you stated that the loss in revenue you expect would be three or four times the \$5,000,000 estimate, on account of the withdrawals, and evidently that is the thing that has convinced you to be in favor of this bill; is that right?

Mr. BERKSHIRE. That, I think, is the primary purpose; yes.

Senator JOHNSON. Does not this 250-gallon exemption take care of it? If it does not take care of it why cannot it be raised to 300 gallons, or such a matter?

Senator WALSH. Some information has come to me that the average retailer has a stock of from 1,000 gallons to 1,300 gallons on hand. In fact one represented to me that this was trivial. One organization represented that this exemption was not valuable to the average retailer.

Mr. BERKSHIRE. The president of the package stores in the country is present. I think his testimony was it was in the neighborhood of 600 gallons.

Mr. STEINBERG. That is the average, that is striking the medium.

Senator WALSH. Are there very many that are less than 250 gallons?

Mr. STEINBERG. Only the fellows that sell by drink, the saloons.

Senator WALSH. Most of the package stores have more than that?

Mr. STEINBERG. Yes, sir.

Senator HERRING. This does not apply to stocks in State-owned stores?

Mr. BERKSHIRE. Yes, sir. I think so, very definitely. You refer to the exemption we are talking about now, Senator?

Senator HERRING. I am talking about the bill itself. Are you attempting to levy a tax on stocks in State-owned stores?

Mr. BERKSHIRE. That is right; yes, sir.

Senator WALSH. Of course, if there is a floor stock tax on liquor you cannot exempt State-owned stores any more than any other store.

Senator CONNALLY. Mr. Berkshire, under the general law when is the regular tax that is in effect now paid?

Mr. BERKSHIRE. When it is withdrawn from the bonded warehouse.

Senator CONNALLY. That is paid by the purchaser or the warehouse?

Mr. BERKSHIRE. That is paid by the distiller or the warehouseman.

Senator CONNALLY. The one who releases it?

Mr. BERKSHIRE. Yes, sir.

Senator CONNALLY. Why could not this apply, then, as well to wholesalers as it does to retailers?

Mr. BERKSHIRE. It does.

Senator CONNALLY. You do not say so. You say "held by a retail dealer."

Mr. BERKSHIRE. The exemption only applies to retailers, Senator; the tax applies to all of them.

Senator WALSH. If you put it on the bonded warehouses it would mean an increased tax on bonded liquor if they withdraw it at once, would it not?

Mr. BERKSHIRE. If you can make the 25-cent increase that is effective July 1 effective tomorrow, if that is what you mean, that will do it. That would be a good thing if we could do it.

The CHAIRMAN. Why was July 1 put in here instead of on the passing of the resolution?

Mr. BERKSHIRE. I could not say, unless that is the beginning of the fiscal year, and the increase went into effect as of that date. I do not know why it could not have been made upon the passage. As a matter of fact I made that suggestion, Senator, that it be made effective immediately, and I do not think this difficulty would have arisen. There might have been some excessive withdrawals just prior to the effective date of the bill even then, but it would not amount to so much. They would not have so much time to anticipate this increase.

Senator CONNALLY. Mr. Berkshire, it seems to me the language in this bill is rather confusing. I think it is indefinite. You provide 25 cents should be levied on all liquor produced in or imported into the United States upon which the Internal Revenue tax has been paid and which on July 1 is held by retail dealers in liquors. Up to there you do not get in anybody but retailers.

Mr. BERKSHIRE. I think we get them all.

Senator CONNALLY. Below that you say, "in a quantity in excess of 250 wine-gallons in the aggregate or by any other person, corporation, partnership, or association in any quantity," and so forth.

Mr. BERKSHIRE. It applies to liquor held by "any other person, corporation, partnership, or association."

Senator CONNALLY. They ought to make that clear, because that is not clear that that "or by any other person" refers back. These whisky fellows have all got smart lawyers and they will get around it if they can.

Mr. BERKSHIRE. I believe that will be all right. Mr. Spingarn, do you want to say anything about it? Do you think that is all right as it is?

Mr. SPINGARN. I think it is all right.

The CHAIRMAN. What is the proposition? The conversation is all down there and we cannot hear what you say.

Mr. BERKSHIRE. There is a point raised as to whether the language is such as to include the wholesalers in "or by any other person, corporation, partnership, or association."

The CHAIRMAN. On what line?

Mr. BERKSHIRE. Lines 11 and 12, on the first page. It might be better to say, I take it, on line 11 "or held by any other person," in order to clarify that language.

The CHAIRMAN. Are there any other questions to be asked of Mr. Berkshire? There are several witnesses here that represent various liquor interests.

Senator CONNALLY. It looks to me like 250 gallons is a pretty large exemption. In other words, the little fellow has a big advantage, he has 25 cents a gallon advantage over the other fellow that has to pay the tax. Why do you want to exempt him? Simply because it is so expensive to collect it?

Mr. BERKSHIRE. No, sir; we do not want to exempt him, Senator. The fact is they felt a lot of the small fellows might be hurt by this. They probably were not doing any too well anyway. Now, they will all be relieved a little, to the extent of 250 gallons. The big one will pay a tax on liquor in excess of 250 gallons.

Senator CONNALLY. I do not think we have any business to stimulate the retail whisky business. I do not think it is within the province of Congress to stimulate it.

The CHAIRMAN. If there are no further questions we will hear from some of the representatives of the industry.

Senator CONNALLY. I move we cut that down to 150 gallons.

The CHAIRMAN. We will go into executive session, Senator Connally, as soon as we get through with these witnesses.

Judge Covington, do you want to say anything on this matter?

STATEMENT OF J. HARRY COVINGTON, WASHINGTON, D. C.

The CHAIRMAN. Judge Covington, whom do you represent?

Mr. COVINGTON. My name is J. Harry Covington. My law firm is Covington, Burling, Rublee, Acheson & Shorb of Washington. Our firm is counsel regularly for Hiram Walker & Sons, Inc., which is an American company and which owns one of the largest distilleries in the United States at Peoria, Ill. For the purpose of this particular hearing, however, in order to conserve the committee's time, I am speaking for practically all of the distillers in the country who are either in the group of larger ones that produce 75 or 80 percent, or the group of smaller distillers. They are all in the Distillers Institute.

The distillers of the United States as a whole are for this measure.

Senator LONERGAN. Pardon me, Judge. Some distillers are not for this measure, though, is not that true?

Mr. COVINGTON. Senator, there is one distilling company, the American Distilling Co., which is not. I have seen a letter written by a very nice gentleman who is the chairman of the board. It is an amusing but utterly uninforming letter, in the sense that it is quite obvious he, with the best of intentions, does not really appreciate the problem involved in this matter of floor-stock tax.

There is nothing unusual, Mr. Chairman, about a floor-stock tax. An examination of the Treasury proceedings in dealing with excise taxes disclosed, insofar as our office has been able to conduct such an examination, that at any time when there has been imposed a manufacturer's excise tax, or there has been an increase in an existing manufacturer's excise tax. Then in order to accomplish what is an entirely equitable result there has been an identical compensatory tax recommended to be imposed upon the outstanding commodities already manufactured and in the course of distribution. Now, the reasons for that are two: First, if the tax goes into effect in the future, and there is no compensatory floor-stock tax, you have a large quantity of such commodities in the country enjoying a discriminatory price as against persons who, in the normal course of trade, have to buy the same commodity at the higher price caused by the tax. You also have something more, and I think that is what Mr. Berkshire really intended to indicate, you stimulate tax avoidance in that the person who can finance purchases of large quantities of the commodity quite naturally will undertake to buy in advance.

Whisky today is burdened with a \$2 tax and, after July 1 will be burdened with an additional 25-cent tax. That tax, in the aggregate, is considerably more than the initial manufacturer's cost of the whisky without the tax. It is the principal item, in other words, in the cost to the wholesale distributor who buys it. Now, being abundantly financed, one can well afford to get from the distiller very large quantities for stocks. Take the big department stores, for example. Macey & Co., to illustrate, in New York, which is one of the largest liquor sellers in the country, has an abundant opportunity to buy at a preferential price.

It really is a protection to the great mass of small retailers in the country to prevent that undue and unfair competitive situation which exists from an ability to finance purchases in that fashion. That to be for this resolution.

This proposed tax in reality does not come out of them in the ordinary course of trade, it is a part of the cost of operation, but the distillers want to preserve for themselves the largest range of distribution that they can have. It is very much better for a man who manufactures a commodity to have 100 distributors selling his product than just have 10 of them. He always tries to have innumerable outlets which make for the widest and most certainly reasonable distribution of his products.

The examination that our office made disclosed that in 1898, when the first substantial change in the tobacco tax was made in the United States there was a compensatory floor tax proposed. Incidentally it was the tax that produced the question as to whether or not there were any constitutional infirmities in the imposition of that type of tax on a commodity. It produced the famous *Potton case* in the Supreme Court of the United States in 1899.

In each instance in which liquor taxation had quite substantial changes, before the prohibition era, there was a floor tax imposed, compensatory in character, identical in amount; and in 1934, since prohibition, when the first raise in the existing tax was to be made, the act provided for a compensatory floor stock tax. The best illustration of it, because certainly regardless of whatever predilections we may have for or against the Agricultural Adjustment Administration processing taxes which subsequently were so extensively litigated in the Supreme Court of the United States, the economic features of that type of tax were very thoroughly gone into, is that when the processing taxes were proposed elaborate discussions concerning them took place before the Senate Committee on Agriculture and the Agricultural Department's economic experts made an extended explanation of the necessity for equity in trade and the imposition of a large range of compensatory floor stock taxes in respect to the manufactured commodities already in either the wholesalers' or retailers' hands, which were the type of commodities which were thereafter, as and when produced by the manufacturers, to be subject to the processing taxes. So it is not necessary to discuss the economics of this situation before you gentlemen.

There is only one thing more that I have to say, and that is about the proposal that Senator Walsh made a moment ago, the question that he raised, or the suggestion that he made. The fact is that no method of taxing the liquor in a bonded warehouse would effectuate the same purpose as this legislation.

Senator WALSH. If the law was made operative immediately, that would change the situation, would it not?

Mr. COVINGTON. That might change the situation, but it is too late to do that now.

Senator WALSH. In the customs administrative bill that is pending, where we have changed a few rates to correct decisions made by the customs court, we have provided the act becomes operative in 30 days. In this particular instance if the act becomes operative at once it would make quite a difference, would it not?

Mr. COVINGTON. That is true. You must remember this, though, in all types of rapidly moving commodities, the type of commodities in which the velocity of movement is great, that there is a large volume of those commodities outstanding, either in transit or in the hands of the distributors or retailers at any given moment. Of course it is a very difficult thing for the distiller to say just what amount that is. The Distillers Institute does have some fairly accurate statistics, and it is supposed that at any moment approximately 25,000,000 gallons of liquor have left the bonded warehouses and are unsold to consumers. Insofar as the distiller is concerned, he has discharged his obligation to the United States. The tax has been paid, and it has been removed from the bonded warehouse and is either in storage in a nonbonded warehouse ready for transportation or else is on bailment or has been actually sold.

Senator BROWN. You mean by that there would be \$6,000,000 of taxes involved?

Mr. COVINGTON. That is our best guess. That is the figure as to which Mr. Berkshire stated in his judgment it would be \$4,000,000.

Senator BROWN. It would be \$6,000,000 on 25,000,000 gallons that had left the bonded warehouses and was in the hands of retailers?

Mr. COVINGTON. Not retailers alone, I mean all varieties of whisky that had left the bonded warehouses.

Senator BROWN. That would not be covered by a tax on the whisky in the hands of the warehouse men?

Mr. COVINGTON. Not be covered by a tax on the whisky in the hands of the distiller.

Senator CAPPER. Judge, who is opposing this?

Mr. COVINGTON. Senator. I only know this: I think Senator Lonergan is familiar with one distilling concern which, for reasons which seem apt to it, is not for it. I do not recall that there were any important groups that were opposed to it at the time that the hearings took place before the House. I think there were some statements by one or two groups of wholesalers, and perhaps some retailers. I think it is a perfectly fair statement to say that, by and large, the distillers of the country, the wholesale distributors of the country and the retailers of the country, are for it.

Senator WALSH. When this was first proposed I got a large number of telegrams from retailers protesting it. Since then there have been some retractions on the part of some of the retailers' organizations, but there are still some retailers in opposition.

Mr. STEINBERG. There are a few. I think quite a few have changed their minds.

The CHAIRMAN. Why is the American Distilling Co. against this proposition?

Mr. COVINGTON. Senator, I can only repeat, I have no criticism of the American Distilling Co. I saw a letter signed by Mr. Tunney.

The CHAIRMAN. I had one communication objecting to it, that is all. I am just anxious to find out why they are against this proposition.

Mr. COVINGTON. My opinion is this, that Mr. Tunney, who I imagine does not devote a great deal of time to this particular business, is not familiar with the complexities of liquor taxation, because his letter was a perfectly straight-forward, high-minded argument against the propriety of an increase in the tax on whisky because the ultimate consumers are now paying too large a tax on liquor. He did not in this letter, certainly, grasp the fact that all that was sought to be done was to make an all-embracing imposition of that 25-cent tax increase which the Congress had already determined was appropriate. In other words, his letter was based on a thorough-going misconception.

The CHAIRMAN. Is not there an institute of liquor distillers?

Mr. COVINGTON. Yes, sir; and so far as I am informed there is no other member of the Distillers Institute against it.

The CHAIRMAN. Who represents that institute? Who is the head of the institute?

Mr. COVINGTON. Dr. Doran, the former Federal Alcohol Administrator.

Senator JOHNSON. Judge, these organizations, groups, and persons whom you are speaking for today, are they all in favor of this 250-gallon exemption, or what is their attitude about that?

Mr. COVINGTON. Their attitude is this: They believed at the time that this bill, that this joint resolution was introduced in the House, that the 50-gallon provision in the House was adequate. On the other hand, they did not believe that it was sufficiently important to have a controversy over the question of the enlargement to 250 gallons because it was their opinion, as it is limited to the retailer, that there is a very great misconception concerning the quantity that the innumerable small retailers will actually have in their possession, and that while the exemption is a 250-gallon figure, that the aggregate amount of the liquor which will be subject to the exemption is much less than would be supposed to be subject to it by a mere mathematical computation of the number of retailers multiplied by 250. In other words, it would be infinitely less than that.

Senator CONNALLY. Judge, will not a retailer immediately buy up to 250 gallons, or reduce to 250 gallons?

Mr. COVINGTON. Well, he could not reduce, Senator.

Senator CONNALLY. He might trade with his partner across the street and lend him 100 gallons. This would certainly be an inducement to every retailer who had 50 gallons to immediately buy 200 gallons more, because it would be free of this tax, and he would make 25 cents a gallon.

Senator CAPPER. Has anybody told us how much revenue this would bring in?

The CHAIRMAN. Yes; Mr. Berkshire has told us that.

Senator WALSH. Does the floor tax apply to distillers? They would have to pay the tax, would they?

Mr. COVINGTON. Surely.

Senator WALSH. Then would there be other tax?

Mr. COVINGTON. No, no.

Senator WALSH. There would be an increase to the consumer?

Mr. COVINGTON. Senator, the way that operates is this—

Senator WALSH (interposing). I understand it operates on the retailer and it operates on the wholesaler.

Mr. COVINGTON. Yes.

Senator WALSH. And it operates on the importer.

Mr. COVINGTON. Yes.

Senator WALSH. Then he would simply increase the price?

Mr. COVINGTON. Yes; he can. It operates on him. He gets no exemption. The process, Senator, is very simple. If you have a large distillery, such as we have in Peoria, the whole warehouse system is bonded. As a matter of fact, the theory of the bond for the purpose of distilling spirits in this country is a bonded area in which distilling operations take place. You cannot withdraw a single gallon for the purpose of transporting it in the channels of trade without you have paid the amount of Federal tax on it, whether it is \$2 or \$2.25. Now, in practice, as and when, from day to day, from week to week, and from month to month, there is the casing, barreling, and what not, getting it ready for actual shipments out at any part of the day, any part of the liquor from the distillery which has been withdrawn from bond comes in a general warehouse after the tax has already been paid, and it is simply waiting for shipment. As to that which thus remains in the distiller's hands this floor-stock tax will be as operative as it will be to the wholesaler or retailer.

Senator BAILEY. Am I right in the impression that this resolution, if passed, will impose a retroactive tax? He has paid his tax when he bought 600 gallons.

Mr. COVINGTON. No; because he has not paid the tax. It will, for the first time, put his specific quantity of liquor in a truly competitive situation.

Senator BAILEY. I get that point.

Mr. COVINGTON. He will not have paid the tax. The distiller pays the tax in all instances.

Senator BAILEY. Suppose I am a retailer and I bought 700 gallons and paid the tax of \$2, that is my normal purchase, but I get on the first of July 400 gallons more, the normal \$2 tax was paid prior to the effective date of the Revenue Act. There are 150 gallons on which I paid the tax, and now I must pay again, is that right?

Senator CONNALLY. Yes; that is right.

Mr. COVINGTON. You only pay 25 cents a gallon.

Senator BAILEY. It is retroactive on liquor purchased prior to the effective date. I get the argument that the gentleman makes, but we do not wish to impose a tax that operates retroactively.

Mr. COVINGTON. Senator, you are a very good lawyer. If you examine the *Patton case* to which I referred you will find that was precisely the question. As I stated, there was some doubt as to whether that which was denominated an excise tax could be made to operate, as it was said, retroactively.

Senator CONNALLY. Let me ask you, is it retroactive?

Mr. COVINGTON. No; it is not.

Senator CONNALLY. If you had sold that whisky and it was disposed of you could not tax it, but as long as the retailer has got it

in his hands it is not a retroactive tax, it is merely a tax on his right to sell that whisky, is that right?

Mr. COVINGTON. Surely. There are a variety of situations, Senator, in which the person owning property has it subject to all the infirmities of the changing tax rate. Suppose I own a house and the District of Columbia thinks it needs \$10,000,000 more money and the only way it can get it is by increasing the tax rate. It is my piece of property, formerly acquired when the tax rate was lower, and there is no difference in the case of personal property. If I have bought certain personal property and bought it at a price in which is incorporated a certain tax then if the tax is constitutional in other respects and is for the purpose of preserving, as you said in your argument, the equality of competition in all stages of that commodity, it has the effect of lifting up to me what, in effect, is the cost. There is no doubt about it whatsoever. As to whether or not it can be said that such a tax is properly a retroactive tax, the best I can answer is that the court said it is not.

Senator BAILEY. I was not thinking about the strict interpretation of the court in the matter with reference to the constitutionality of it. Your answer there would be on the question of when the transaction occurred. The excise tax would impinge whenever the transaction occurred.

Mr. COVINGTON. That is correct.

Senator BAILEY. What I have in mind, you have an exemption of 250 gallons. That is supposed to protect the man who has already paid the tax on 250 gallons, that is the philosophy of that exemption, but his normal stock is, we will say, 1,000 gallons, and he has bought that in good faith, and the \$2 tax is paid on that, collected by the distiller. Now, he comes in and pays a 25 cents tax additional. He gets 250 gallons off of that. That is 750 gallons. Would it not be the equitable thing to so fix it that the 25 cents a gallon would attach over and above his actual low requirements. That is to prevent the accumulation of stocks in advance of the effective date of the tax. I am talking of the legislative effect of the thing now.

Mr. COVINGTON. The best answer I can give to you is that the imposition of a boor-stock tax such as is now proposed accomplishes the result you refer to. From the date when that tax becomes effective, if imposed, there will be a liability for the additional 25-cent tax on all previously tax-paid whisky whether in the hands of the distiller, distributor, or retailer. The only whisky not subject to that tax will be 250 gallons of the stock in the hands of any retailer who has that much. The question is what are the practicalities of the situation. I think it is perfectly obvious that the House Members—we did not suggest it—arrived at this figure of 250 gallons in the Ways and Means Committee for what seemed to them to be the practical reasons. Just what they were I do not know. We did not, as I say, urge the 250-gallon exemption when we were urging the resolution.

Senator BAILEY. I do not know why you did not urge it. It is put in there for the purpose of fairness, is it not?

Mr. COVINGTON. There was a 50-gallon exemption.

Senator BAILEY. That was manifestly insufficient.

Mr. COVINGTON. Apparently, they thought so. Now, there is a wide divergence of opinion about that, and thousands of small retail-

ers thought 50 gallons was ample for them. The distillers were looking at this thing in a broad way, from the viewpoint of what was the equitable thing, and said if the Ways and Means Committee wants to fix it at 250 gallons they had no objection to it at all. It is a matter of legislative judgment. The only man I could get was the practical man in the organization, in the particular company for whom we are counsel, and he told us he thought every man that could fairly, in these days, be called the little fellow, was amply under the umbrella of 250 gallons.

Senator CONNALLY. Suppose a man had 500 gallons, how much tax would he pay?

Mr. COVINGTON. He would pay a tax on 250 gallons.

Senator CONNALLY. That is what I am asking about. It does not say the tax shall be paid on the amount in excess of 250 gallons, it says it shall be paid on liquor "held by a retail dealer in liquors in a quantity in excess of 250 wine-gallons."

Mr. COVINGTON. Senator, you have got to go along and read the grammatical construction of this sentence.

Senator CONNALLY. It is a badly drawn bill, if I have to say it. It is not clear.

Mr. COVINGTON. Senator Connally, may I interrupt you to say this: I am just told that this was determined by draftsmen to be appropriate, because it is a repetition of the precise provision in the 1917 act emanating from the Treasury, so that they must believe that the language was appropriate to accomplish the purpose.

Senator CONNALLY. Let me see. It reads, "that there shall be levied, assessed, collected, and paid a floor tax of 25 cents on each proof-gallon and a proportionate tax at a like rate on all fractional parts of such proof-gallon upon all distilled spirits, except brandy, produced in or imported into the United States upon which the Internal Revenue Act imposed by law has been paid and which, on July 1, 1938, are held by a retail dealer in liquors in a quantity in excess of 250 wine-gallons," and so on.

Mr. COVINGTON. "Or by any other person."

Senator CONNALLY. I am talking about the retailer. He is the only man who gets the exemption.

Mr. COVINGTON. Yes.

Senator CONNALLY. If he has 500 gallons why is not he taxed on 500 gallons under that language? I am asking you now. You are a lawyer.

Mr. COVINGTON. I appreciate that is a serious question. I should have no doubt, if I were still on the bench, that that is the appropriate language to use. It gives a specific exemption to the man who has 500 gallons, 5,000 gallons, or 10,000 gallons of 250 gallons, that 250 gallons be not subject to the tax and that all the remainder be subject to the tax.

Senator CONNALLY. You would have an appeal in your case if you did. You say you would give that as a judicial opinion. You would have an appeal in the case if you did.

Mr. COVINGTON. I was not immune to appeals. Occasionally cases were reversed and occasionally affirmed.

Senator CONNALLY. I do not see why you do not make the language plain. Why don't you make it plain instead of messing it all up?

Mr. COVINGTON. Let me say this: As a practical matter is not this the answer, though, that Mr. Berkshire, who was the first witness here, I happen to know is the man at the Treasury who is regarded as an authority on Federal Alcohol Administration—

Senator CONNALLY. I am for him; he is from my State.

Mr. COVINGTON. — he will be charged with the executive administration of it. He has the reputation of being a very high minded man, a capable official, and he has just stated that it is precisely the language which ought to be used to effectuate the purpose. Now, I do not know any way in the world to go about it at this time, to undertake to reconstruct that language. I would not have the temerity to undertake to rewrite that which the Treasury persons themselves say is the language which will effectuate the desired result.

The CHAIRMAN. Are there any other questions of Judge Covington? I have a list here of three or four other gentlemen who have asked to be heard. I do not know whether they want to appear now. We will have to go into executive session and get this matter straightened out this afternoon.

Mr. Steinberg.

STATEMENT OF WILLIAM STEINBERG, PRESIDENT, NATIONAL RETAIL PACKAGE STORES ASSOCIATION, NEW YORK CITY

Mr. STEINBERG. I just want to explain one phase of it. We had an occasion in this city about a month ago to have a hearing on credits. The States today limit the credit to retailers. In Kentucky you must pay cash, in other States they want 30 days and on. A month ago in this city the Federal Alcohol Administration had a hearing on credit. They want to supervise credit throughout the country uniformly, and the chairman of the Texas Commission was here and he stated at the hearing that the State of Texas being large, and so forth, it was very difficult of supervision. That same reason holds good in this tax exemption. A man who has a store in Texas might be very far away from the source of supply as a wholesaler and he might have in stock a great deal of whisky, not because he can sell immediately, but because he does not know how soon he can replace it.

There is a difference between the saloon, or the place where you buy the drink, and a package store. In a place where you buy a drink, if the man runs short of a certain brand he can pour a drink from a different bottle, but if someone walks in my store and asks for "X" brand, I must be in a position to give him the brand or else I lose a customer. That necessitates an amount of stock on hand at all times.

So at the hearing at the Ways and Means Committee at the House we discussed this thing probably for 20 minutes. I was questioned thoroughly on this matter. The conclusion was, however, that probably 600 gallons was the average stock of the retailer, the package-store keeper. That is the man who needs the protection of this bill, for this reason: Unfortunately we have in this business drygoods stores, department stores, chain stores, and so forth, they are not whisky people, they do not worry much about the future of the business, they do not worry about the legal element, they are selling whiskies the same as groceries or any other commodity. Their de-

sire is to do business and to attract, through whisky, people who will buy their other commodities, and use whisky for a stepping stone. So if you do not have a tax imposed upon the floor stock we have the condition where the large chain stores would have an advantage. Take in the State of Connecticut, the A. & P. is the strongest competitor we have there. We have 800 outlets. Six hundred belong to the association. They are small retailers. The balance is split up amongst the A. & P. and the Schulte chain stores. It would be a Roman holiday for the chain stores if there was no floor tax, because the small man cannot buy more than a month's supply. He is lucky if he can carry that, because he has to pay within 30 days in Connecticut. He hasn't any funds. The banks will not lend money on the liquor stocks, because there is no stability there, but the A. & P. can go out and borrow all kinds of money, because they have the facilities for groceries and other things.

Beginning the first of July, if the small retailer has to replenish his stock with new merchandise at the increased rate and the A. & P. and the other chain stores can sell at the old rate, there is a difference of about a dollar a case by the time it comes down to them, and it is a great advantage to the chain stores. They can advertise for 7 months and sell the liquor at a lower rate. We cannot prove it or disprove it, it might not be so, they might have run out of tax-paid merchandise a long time ago, but they have good advertising men and they use them for that purpose. That is the reason the small fellows, a great many of us, need this bill. We ask for protection.

We felt sure that the Ways and Means Committee were going to give us an exemption of 500 gallons. Mind you, this was not a request from us, this came voluntarily from the House. They thought, in all fairness, there should be an exemption of 250 gallons. I will tell you why. It is not so much a protection of the retailer, because we have no assurance on July 1, after this bill is passed, that the consumer will be asked to pay the difference. It might be the case where the distiller might not increase his price, but if the retailer pays his floor tax and the price to the consumer is not increased the retailer will have to bear the loss. So if you give him the exemption, if you exempt a certain amount of his stock we do not care whether the price is never changed, because it would not hurt us. That is the principal reason for the exemption.

First of all you have the fellow who hasn't got very much money; he hasn't got borrowing capacity, and you do not want to harass him. The small fellow would be hurt an awful lot if this provision was not put in there. So when the Ways and Means Committee compromised on 250 gallons in their own deliberation we felt we would be satisfied to go along.

Now, gentlemen, you know this session will be over soon. If there are any changes made now it will be another matter of conference, and we feel if there is any conference we are licked.

The CHAIRMAN. You are willing to accept the 250-gallon exemption?

Mr. STEINBERG. We are. We plead with you, leave the bill as it is, and pass it. It is the best solution possible.

The CHAIRMAN. What percent of the retailers in your association are asking for it?

Mr. STEINBERG. The only objection we have is from a small group. To my knowledge there are only about 90 stores in the United States who are opposed to it, and they are opposed to it, I feel I am qualified to say, for the reason that they have been instructed by certain wholesalers to go with them. A particular wholesaler in a certain section has an ax to grind. He thought if he opposed this bill it might have a nuisance value. Since I mentioned no names it does not matter. In this country, with a great number of retailers, the only ones on record are those few in that particular part of Massachusetts, and I think, if properly advised, they would not go along with the opposition either, but that is the only one, as far as the retail field is concerned, that have any opposition at all to this particular bill. So as far as we are concerned, it is practically unanimous.

The CHAIRMAN. Is there anybody here now that wants to say anything against this bill? Are there any witnesses here in opposition to this bill? I have the names of two other witnesses here, I do not know whether they want to be heard or not. Mr. Patterson, of the executive committee, Massachusetts Federation of Package Stores, Boston, Mass. Is he here?

Mr. STEINBERG. Mr. Patterson is here.

STATEMENT OF MATTHEW G. PATTERSON, EXECUTIVE COMMITTEE, MASSACHUSETTS FEDERATION OF PACKAGE STORES, BOSTON, MASS.

Mr. PATTERSON. I do not know that it is necessary for me to make a statement, because Mr. Steinberg covered the subject pretty well. The only reason I am here, we did have some opposition from Massachusetts, from a small group up there. In Massachusetts we have 1,100 package stores. This group claims they represent 300. I can truthfully say I am here representing more than 800 package stores, and they are all unanimous in their opinion that a floor tax is absolutely necessary for their welfare. Ninety percent of the package stores in Massachusetts are what we call small-business men, and I know that you gentlemen here are interested in the welfare of the small-business men.

With this floor tax, with the exemption of 250 gallons, there are very few of us going to be hurt. For instance, I took stock in my store last week and I find that I have 259 gallons of taxable merchandise in my store, and I think I am representative of most of the package stores in Massachusetts. Of course, in different sections of the country they may hold more. In New York, for instance, no doubt they do carry more merchandise than we do, but the average store, that is, 90 percent of the stores in Massachusetts carry approximately 250 to 300 gallons, and, as I say, with this exemption none of us would be hurt. We would be protected and in the future the industry will be well taken care of. That is all I have to say.

Senator CONNALLY. You will not only not be hurt, but you will be well benefited, will you not, because you will get 250 gallons of whisky without the tax?

Mr. PATTERSON. That is right, sir.

Senator CONNALLY. If anybody else buys any now they will buy without the additional tax.

Mr. PATTERSON. After July 1 they will have to pay the tax.

Senator CONNALLY. You have got it on hand now, you will be free of this two-bit tax, whereas if a new store starts here they will have to pay the two bits, the 25 cents.

Mr. PATTERSON. If they start up after July 1.

Senator CONNALLY. So it will really be a benefit to the little fellows.

The CHAIRMAN. Is Mr. Lourie here?

**STATEMENT OF HARRY L. LOURIE, EXECUTIVE SECRETARY,
NATIONAL ASSOCIATION OF ALCOHOLIC BEVERAGE IMPORTERS,
INC., WASHINGTON, D. C.**

Mr. LOURIE. I just want to say, Mr. Chairman, that the Alcoholic Beverage Importers Association, which represents 90 percent of the total number of importers in the United States, is manifestly in favor of the floor tax, and adopted a resolution to that effect early in May. I wrote you accordingly.

I want to add one thing, and that is in considering the resolution you gentlemen should bear in mind that the 250 gallons does not represent the total stock of the retail store. We have wines and other beverages which are not subject to the tax. All retailers, as I understand it, carry other items besides spirits. So in taking the stock in the store the only thing involved, of course, is the spirits itself and not the wines, beers, or whatever they may have.

The CHAIRMAN. All right, thank you. Does Mr. Martin want to be heard?

**STATEMENT OF JOHN G. MARTIN, PRESIDENT, G. F. HEUBLEIN &
BROS., HARTFORD, CONN.**

Mr. MARTIN. I have a short brief here that I would like to file. We are unanimously in favor of the floor tax.
(The brief referred to is as follows:)

Mr. Chairman and Members of the Committee: I am John G. Martin, president of G. F. Heublein & Bro., rectifiers, of Hartford, Conn. My firm was founded by my grandfather in 1875 and has operated continuously since that time with the exception of the prohibition years.

I speak with reference to House Joint Resolution 683. I speak on behalf of my own company, and to the best of my knowledge, on behalf of all the other rectifiers in the State of Connecticut (16 in number). From what I have been able to learn through the trade my interest in this floor-tax resolution is identical with the 350 or more independent rectifiers throughout the United States. We all want to see you favorably report this joint resolution for we believe it is of vital importance to our interests, to say nothing of the other branches of the industry, that a tax be placed on floor stocks in existence of the effective date of the increased excise tax on distilled spirits, July 1, 1938.

You have already been given a very able and eminently correct picture of the effect of no floor tax. I can add little or nothing to that and it is not my ambition to take up one moment more of your time than is necessary. I want to leave just one thought with you. Do not force the smaller units, manufacturing or otherwise, within the distilled spirits field to enter a race of withdrawals of distilled spirits prior to July 1, 1938, in an effort to avoid the increase then effective, because it will be most damaging and destructive to these interests. Most of us do not possess financial backing or have the means to tax-pay and withdraw distilled spirits in proportion to the amounts that will be tax-paid and withdrawn by the few wealthier corporations within the industry. That being the case we will be in a most disadvantageous position in

competing with these corporations. Our disadvantage will lie in the fact that as soon as our limited inventories are exhausted, we will be taxpaying at the rate of \$2.25 per proof gallon and attempting to sell our products in competition with distilled spirits which have been withdrawn at \$2 per proof gallon.

I therefore urge you on behalf of the rectifiers of Connecticut as well as the others throughout this country to recommend the adoption of House Joint Resolution 683.

Thank you.

Senator CONNALLY. Why is brandy excepted?

Mr. BERKSHIRE. The tax, of course, did not apply to brandy.

Mr. Chairman, there is one point I wanted to bring up. It is a mere matter of drafting. On page 2, line 5, with respect to the requirements that all dealers and others make a return under oath, setting forth their inventories, and so forth. We think that there is some question that under the present reading of that paragraph it is possible that all of these dealers, and others, might not be required to make this return. We think it is highly important that they all do make returns, whether they pay a tax or not. We will not, obviously, have the force to go out and inspect every dealer in the United States, there are 250,000, but if we have a sworn return from them we will have something definite.

The CHAIRMAN. You realize what the situation would be if we adopt any amendments?

Mr. BERKSHIRE. I understand that. It is suggested that the change that I will propose probably may not necessitate the bill going back at all.

The CHAIRMAN. It will have to go back if a change is made. Is this written now like you think it ought to be?

Mr. BERKSHIRE. That would be a considerable improvement, but we would endeavor to hold that that would all be required even without that requirement to file a return, but that amendment would make it clear.

The CHAIRMAN. I desire the record to show that Mr. Marshall F. Bannell, secretary and treasurer, Connecticut Wholesale Liquor Dealers' Association, Inc., of New Haven, Conn., and Mr. Vernal W. Bates, president of L. C. Bates Co., New Haven, Conn., had hoped to be present to testify in support of this joint resolution. They were called out of town, however, and were unable to be present. Both of these gentlemen wish the committee to know that they are in favor of the joint resolution.

The hearings are now closed and the committee will go into executive session.

(Whereupon, at the hour of 3:30 p. m. the hearing was adjourned.)