[CONFIDENTIAL]

REVENUE ACT, 1936

HEARINGS

BEFORE THE

COMMITTEE ON FINANCE
UNITED STATES SENATE

SEVENTY-FOURTH CONGRESS

SECOND SESSION

ON

H. R. 12395

AN ACT TO PROVIDE REVENUE, EQUALIZE TAXATION, AND FOR OTHER PURPOSES

PART 10

MAY 26 and 27, 1936

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REVENUE ACT, 1936

TUESDAY, MAY 27, 1936

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

EXECUTIVE SESSION

The committee met, pursuant to adjournment, at 10 a. m., in the committee room, Senate Office Building, Senator William H. King presiding.

Present: Senators King (acting chairman), Bailey, Walsh, Connally, Byrd, Couzens, La Follette, Guffey, Lonergan, Gerry, Metcalf, Black, and Capper.

Also present: L. H. Parker, chief of staff, Joint Committee on Internal Revenue Taxation, and members of his staff; Middleton Beaman, legislative counsel, House of Representatives; John O'Brien, assistant legislative counsel, House of Representatives; Arthur H. Kent, acting chief counsel, Bureau of Internal Revenue; C. E. Turney, assistant general counsel for the Treasury Department; L. H. Seltzer, assistant director of research and statistics, Treasury Department; W. R. Johnson, Bureau of Customs, Treasury Department.

Senator KING (acting chairman): The committee will be in order. Senator Byrd, are you willing to go forward with the proposed amendment of section 102?

Senator LONERGAN. While we are waiting for Senator Byrd to present his amendment, can we dispose of a matter which will take only a moment? The other day Senator Couzens offered an amendment to an amendment which I offered having to do with the issuance of insurance policies to pay death taxes. Senator Couzens has agreed to withdraw the amendment which he offered. It has to do with the issuance of policies following the adoption of the law, and confining it to that. That has been withdrawn by Senator Couzens.

Senator KING. Let the experts take cognizance of that.

Senator COUZENS. That had relation to the retroactive feature of Senator Lonergan's amendment, and I see the objections to putting that amendment in and not making it retroactive. I withdraw my proposal.

Senator KING. You understand that, Mr. Parker?

Mr. PARKER. Yes, I understand the way the thing was adopted by the committee in regard to this insurance for paying estate taxes, that there was inserted in there, language which would require any such policy to be taken out after the date of the enactment of the act.

Senator LONERGAN. That is withdrawn.

Mr. PARKER. You want the existing policies included?

Senator LONERGAN. In other words, my amendment will be adopted without amendment.

Senator KING. Do you understand, Mr. Parker?

Mr. PARKER. I understand.

Senator KING. Senator Byrd, are you ready to proceed with your amendment?

Senator BYRD. Yes. All I have to suggest is, that I was wondering whether it would not be well to increase the 30 percent to some extent and make it 40 percent.

Senator KING. To increase the amount. That when 40 percent is withheld, then the application of the amendment which was suggested by Mr. Parker should apply. It was 30 percent; if 30 percent reserves were retained, then they must make a statement as to the purpose for which they were to be used. Senator Byrd suggests that it be 40 percent instead of 30 percent.

Senator BYRD. They are already penalized for what they do, 7 percent.

Senator COUZENS. I have no objection if the Senator wants to make that as an amendment, but I do want to make this amendment, extending the statute of limitations as applying to section 102, to 5 years instead of 3. It seems to me that if these companies are going to file with the Bureau of Internal Revenue the purposes for which they hold these earnings, and state the reason, that the Commissioner of Internal Revenue has to have a longer time in which to check them up to see whether they had complied with their promises for which they are going to use these excess reserves, and the statute of limitations ought to be extended to 5 years. I offer that as an amendment to the amendment.

Senator BYRD. Do you not think that 4 years would be long enough? The only objection to it is that this thing hangs over the heads of the corporations, and they do not know what is going to happen to them.

Senator COUZENS. Otherwise, you will have no adequate time to check up on the promise. Now we are granting them leeway because of certain promises they make as to what they are going to use the funds for. It is my judgment that in that case, if we grant them that privilege, we ought to give the Commissioner of Internal Revenue, adequate time to check what they do to see that they live up to their promise.

Senator BYRD. Do you not think that 4 years is enough?

Senator COUZENS. I won't argue about it, but I think 5 years is better.

Mr. PARKER. I would like to ask a question about that policy. The ordinary statute is 3 years.

Senator COUZENS. I understand.

Mr. PARKER. The Commissioner determines the income, we will say, within a 3-year period. Later on he finds that during the 5 years, that he wants to apply section 102. Are you going to allow him to make adjustments in the income? We have some bad cases like that.

For instance, a man might have reported in his return $100,000 of net income. On a reaudit, even after it has been passed once, 4 years afterward, the Commissioner, on account of court decisions or what not, will say that this man instead of the amount being $100,000 is $1,000,000. Do you want to take into account $100,000 in adjustments in income that would make it look as though a lot more money had been accumulated?

You see, oftentimes income is shifted from 1 year to the other, and you get a million dollars too much in 1 year and a million dollars too little in the other year. It is a little hard for me to see just what you want to do there. Probably you just want to open it up for the purpose of the surtax and you want the Commissioner to stick to his prior determination of the net income?

Senator COUZENS. I only want to have the 5 years apply for checking up the promises of the taxpayer as to what he wants to use this specific retention for. That is the only purpose I have in asking for an extension of the statute of limitations. I do not desire to distrub any other figures or any other conclusions reached by the Commissioner of Internal Revenue, except as they are changed by the nonuse of these reserves.

Mr. BEAMAN. Supposing, Senator, that it appeared that the corporation had an accumulated surplus of $100,000. Now, they file a return showing an income this year of $10,000, and they retained $3,000, or rather, they distributed $7,000. Four years later, the Commissioner finds that the true net income for that year was $150,000 instead of $10,000. If that had been shown in the first place, he might have thought that the distribution of $7,000, which resulted in an accumulation of $143,000, was perfectly unreasonable, but he thought that the retention of $3,000 in the return was perfectly reasonable.

Now, if he knows the facts, the Commissioner of course would like to go back and say that that retention was unreasonable on the basis of the true net income for that year.

That is another angle to it other than keeping of the promises. I take it that the corporation back there must have known that it had that money, but it may be perfectly honestly or dishonestly they thought that it belonged in some other year.

It is awfully difficult, I believe, when you have a tax—it is not as if this were a separate tax all by itself with a separate return and everything. This is a surtax on top of the flat taxes and all included in the one return and all a part of one tax.

Senator KING. It may hold up the settlement for 7 years.

Mr. BEAMAN. It is very difficult, and I think it will take a lot of thought to find out just what effect it would have.

Senator COUZENS. I think the purpose of section 102 is to prevent these things, and I think that stiffening it up will perhaps eliminate all of these controversies with respect to the holding of undue reserves, and especially in these family holding companies and so on which this section is particularly aimed at. When a taxpayer, having reserved an unnecessary amount, knowing that he promises, because of the concessions he gets to carry out his program, he will carry out his program or will not make it, and I am of the opinion that the Department will find very few cases result in a possible penalty because of misrepresentation.

I do not see any objection to putting it in the law, and if it does not work, we can change it at some other time, but at least we should do the best we can to stiffen up section 102 to prevent misrepresentations for which the reserves are held. I will agree to the suggestion of Senator Byrd that we make it 4 years.

Senator KING. Forty percent, and 4 years?

Senator LA FOLLETTE. Just a minute on that 40 percent. I would like to make this suggestion to the committee. I realize that when you come to fix an arbitrary amount out of which the statement is to be required, it is a little difficult, but the fact is that in some corporations and in certain situations where they already have large accumulations, 30 percent even may be an excessive retention. It is my understanding that it is not an uncommon thing for deficiency letters to go out under the existing section 102 to corporations that have withheld less than 30 percent, and it seems to me that all you are asking for here is a statement of their reasons for the retention, and that it would be a mistake to increase this 40 percent for many of the corporations.

Senator COUZENS. The only purpose that I understood Senator Byrd made that proposal is because the present law does not assess the 7 percent on undistributed earnings, so he raised the amount to compensate for that additional 7 percent on the undistributed earnings.

Senator LA FOLLETTE. But there is not any penalty attached to this thing. It simply requires the corporation to file the statement as to the reasons for its retentions if it is above 30 percent, and I think if you take individual corporations—I have not any figures in mind now—but I think you will find a large number, if we knew all the facts about them, that we would say that a 40 percent retention in 1936 was excessive or that there ought to be some explanation of it, and since it is simply filed as a matter of information to the Department, and I think will operate to the benefit of the taxpayers as well as help to some extent to reach those that are not retaining their reserves for the purposes that they allege they are being retained for, I cannot see any reason why we should increase the amount from 30 to 40. I think 30 percent is plenty high enough.

Senator BLACK. I want to state that I fully agree with Senator La Follette. It has been my understanding that every member of the committee was of the opinion that there are many corporations who are abusing this particular privilege, and there can be no injury done by simply requiring them when they withhold 30 percent to make a report of it, and certainly there can be a great many, as Senator La Follette said, where 30 percent might be withheld wholly for the purpose of preventing distribution of that much income. Since we are not doing anybody any injury, and every member of the committee wants to expose these abuses wherever they occur, I want to vote against changing it from 30 to 40 percent.

Senator BYRD. Take the case of a corporation that in perfectly good faith made a report that they wanted to retain their earnings to build a new plant, and then a year later by reason of some other situation which they could not foresee, could not build the plant, and they are on record as wanting to retain a part of their earnings to build this plant and then are unable to do it.

Senator COUZENS. If you put that kind of a loophole in the law, everybody will have some scheme about building a plant.

Senator BYRD. I do not want a loophole in the law, but at the present time, as I understand, corporations are distributing 70 percent of their earnings; that is the average. In my judgment, there is going to be a stimulation by reason of this 7-percent tax on it, and I thought it was fair to increase it to 40 percent, and they do not have

to make these reports until after they have retained 40 percent or more.

Senator KING. Is there any further discussion? We will vote on the amendment first. Those favoring 40 instead of 30 will say, "aye"; contrary, "no."

(The acting chairman announced that the "noes" have it.)

Senator BYRD. I would like to have a raising of hands.

Senator BLACK. Suppose we take a record vote.

(A record vote is taken.)

Senator KING. It is 9 to 6. The amendment is agreed to.

The next is on the change of the statute of limitations from 3 to 4 years. Those favoring the amendment to strike out three and insert four will say "aye"; contrary "nay".

(The acting chairman announced that the "ayes" have it.)

Senator KING. Now, the question is on the amendment as perfected. Those in favor, "aye"; contrary "nay".

(The acting chairman announced that the "ayes" have it.)

Senator BLACK. I voted "aye" because I intend later on to try to put it back to 30.

Mr. BEAMAN. Through some oversight, apparently, all of these years, on that section 102 and its predecessors, the language has been used speaking of gains and profits to accumulate. All the rest of the act everywhere else uses the phrase "earnings and profits." I do not think anything ever was intended any different here. We therefore suggest that you use the phrase "earnings and profits" here instead of "gains and profits," accompanied by the statement in the report that it was not intended to change the law, but simply to make it uniform with the rest of the law.

Senator COUZENS. Is there any objection to the proposed amendment? The Chair hears none and it will be agreed to.

Mr. BEAMAN. Subsection (e) on page 81 provides that this surtax on the amount improperly retained shall not apply if all of the shareholders of the corporation, even though they do not get the money, include their distributive shares and pay a tax on it as though they had gotten it. Obviously the Government gets its share and the corporation is relieved.

There is a little quirk to it, however. If the shareholders of the wicked corporation are corporations, they include all of their distributed shares in their gross income, but they immediately take out, at least for the purpose of the 18 percent tax, they take off 90 percent of it so that the Government is not getting the tax by the shareholders taking it, but that they would have gotten it if the corporation had not accumulated.

Senator COUZENS. It seems to me that that is a very objectionable provision for the reason that the stock may change ownership and the next man get it and have to pay.

Mr. BEAMAN. The best thing we could think of would be to say that this subsection allow that corporation to escape taxes if the shareholder did take it all, but that that provision should not apply if more than any percentage you want to fix—Mr. Parker suggested 10—if more than 10 percent of the stock of the corporation was owned by other corporations.

Senator LA FOLLETTE. I should think that that would fix it.

Senator COUZENS. Is that agreed to? If there is no objection, that proposal will be agreed to.

Is there anything else, Mr. Beaman?

Mr. BEAMAN. No.

Senator BAILEY. I will bring forward at this time the amendment that I proposed on last Friday. At the time I proposed it, Senator Connally proposed an additon to it, and it was agreed at the time that his addition and my amendment would be considered together and be rewritten, and the proposition has been rewritten, and I understand it has been approved by the representatives of the Treasury. What is your attitude in the Treasury? Senator Connally handed me this [indicating] with the statement that the Treasury said that it was satisfactory. Who was it?

Senator CONNALLY. A man by the name of Ward who is interested in the matter, and he has consulted the Farm Bureau and practically everybody interested, and they are in favor of the amendment.

Senator BAILEY. I will read the amendment. It is—

Title V—Amendments to prior acts.

SEC. 701. Tax on certain oils.

The first sentence of section 601 (c) (8) of the Revenue Act of 1932, as amended, is amended to read as follows:

"(8) Whale oil (except sperm oil), fish oil (except cod oil, codliver oil, and halibutliver oil), marine animal oil, tallow, inedible animal grease, and fatty acids of any of the foregoing oils or fats and the salts of any such oils, fats, or fatty acids; all the foregoing, whether or not refined, sulphonated, sulphated, hydrogenated, or otherwise processed, and any merchandise, combination, or mixture containing a substantial quantity of one or more of such oils, fats, fatty acids, or salts, 3 cents per pound; olive oil and sesame oil, classified under paragraph 1732 of the Tariff Act of 1930, perilla oil, sunflower oil, rapeseed oil, kapok oil, hempseed oil, and fatty acids of any of the foregoing oils and the salts of any such oils; all the foregoing, whether or not refined, sulphonated, sulphated, hydrogenated, or otherwise processed, and any merchandise, combination, or mixture containing a substantial quantity of one or more of such oils, fats, fatty acids, or salts, 4½ cents per pound; perilla seed, hempseed, rapeseed, sesame seed, kapok seed, 2 cents per pound."

Senator CONNALLY. You have left out fish scrap, fish meal, and other marine animal scrap and meal.

Senator BAILEY. I am doing that on purpose. I will explain that. I have left out tung oil as a matter of courtesy to the chairman of our committee who is absent and sick. He requested me to leave it out, and I think I consented on last Friday that I would do so.

Senator KING. Is what you are reading the printed amendment?

Senator BAILEY. I am reading the new amendment. I am explaining at this time that I have omitted tung oil because the chairman of the committee, Senator Harrison, made that request. While I did not agree absolutely to it, I am perfectly willing in his absence to agree to strike it out. It is of some importance but not of sufficient importance to justify me pressing it in his absence.

I have left out fish scrap, fish meal, and other marine animal scrap and meal for this reason. They are new matter, and the point has been made here and was made on yesterday with respect to Senator Capper's amendment, that that opened up the tariff question. I do not and did not propose to open up the tariff question. All I am doing is perfecting the 1934 act. I wish to be perfectly consistent about that.

Senator COUZENS. May I find out from the Senator from North Carolina in what manner the Treasury Department interprets that word "substantial quantity" in these various items?

Senator BAILEY. The words "substantial quantity" is defined. It means 10 percent or more by quantity. That is section 703 reading:

"The words 'substantial quantity' when used in sections 701 and 702 mean 10 percent or more by quantity."

Section 702 relates to processing tax on certain oils, and is as follows:

The first sentence of section 602½ (a) of the Revenue Act of 1934, as amended, is amended to read as follows:

"(a) There is hereby imposed upon the first domestic processing of coconut oil, palm oil, palm-kernal oil, or fatty acids of any of the foregoing oils (whether or not such oils or fatty acids have been refined, sulphonated, sulphated, hydrogenated, or otherwise processed), or the salts of any such oils or fatty acids, or any combination or mixture containing a substantial quantity of any one or more of such oils, fatty acids, or salts with respect to any of which oils, fatty acids, or salts there has been no previous first domestic processing, a tax of 3 cents per pounds to be paid by the processor."

Senator COUZENS. That is the present law?

Senator BAILEY. That is amending the 1934 act.

Senator CONNALLY. It is practically the same law.

Senator KING. But increasing the tax?

Senator CONNALLY. No, it does not change the tax. But if you read on, you will understand why.

Senator KING. That is all there is in section 702 of the amendment as tendered.

Senator CONNALLY. I think there are some other provisions in there about paying money to the Philippine Treasury.

Senator BAILEY. I am coming to that. This is merely perfecting the act and putting it in language that will prevent the breach of the purpose of the 1934 act by further defining the matter.

Senator KING. Let me see if I understand you; I was called out. Section 702 which you have just read, subdivision (a) is the same as the existing law?

Senator BAILEY. I am taking Senator Connally's word for that.

Senator CONNALLY. I do not say it is identical in language, but the substance of it is the same as we put on 2 years ago in the 1934 act.

Senator KING. They have not added any commodities that were not in that act, or increased the rate?

Senator BAILEY. I think not.

Senator CONNALLY. I do not think so.

Senator BLACK. Have you a statement which will give us a clear picture of the difference between this act as amended and the original act?

Senator BAILEY. I gave that for the record, and I have the record here before me. I will go into that.

Section 703 which I have read previously in response to Senator Couzens query, is as follows:

The words "substantial quantity" when used in sections 701 and 702 mean 10 percent or more in quantity.

Senator KING. That is entirely new, is it not?

Senator BAILEY. Yes, that is a definition of "substantial quantity." That is new.

Senator CONNALLY. Let me go back there a minute, Senator King. Just as I said a moment ago, section 602½, which is amended by 702, in the present act it provides for the levy of 3 cents a pound on coconut

oil, sesame oil, palm oil, palm kernel oil, or sunflower oil. The reason sunflower oil is omitted is because Senator Bailey carries it in another section, but in this 602½, it was provided that these oils originating in the Philippine Islands, we should pay the money to the Philippine Islands, and that is what I am trying to get rid of.

Senator BAILEY. That brings me then to section 704.

Senator BLACK. Before you leave that, Senator, may I ask some questions? In reading that, you left out sesame oil.

Senator CONNALLY. No, I did not. The present act has sesame oil in it. It is omitted here because Senator Bailey, as I understand it, has it in somewhere else.

Senator BAILEY. I put that under the tax section which I just read.

Senator BLACK. Instead of under the processing?

Senator BAILEY. That is right. Now section 704 is as follows:

So much of subsection (a) of section 602½ of the Revenue Act of 1934, as amended (relating to the processing tax on certain oils), as reads "All taxes collected under this section with respect to coconut oil wholly of Philippine production or produced from materials wholly of Philippine growth or production, shall be held as a separate fund and paid to the treasury of the Philippine Islands, but if at any time the Philippine government provides by any law for any subsidy to be paid to the producers of copra, coconut oil, or allied products, no further payments to the Philippine treasury shall be made under this subsection" shall not be effective with respect to taxes collected on account of processing after the date of the enactment of this act.

This is Senator Connally's amendment, if you care to make a statement on that.

Senator CONNALLY. The point is that they have attacked in the courts the levying of this tax, on the theory that we had no power to levy and turn the money over to the Philippine Treasury. What we propose to do here is simply to repeal that provision and pay the money into the United States Treasury, and then if Congress desires to reappropriate a similar amount to the Philippines, that can be done.

Senator WALSH. Is there a prospect of the courts finding it illegal and thereby throwing out the tax?

Senator CONNALLY. I understand one of the subordinate courts one of the district courts somewhere has so held. I am trying to fill up that gap. That is all that that is.

Senator KING. It is not your purpose, Senator, is it, to deprive the Philippine Islands of the benefit of any tax imposed?

Senator CONNALLY. No. I say it is my purpose to do this, to repeal this doubtful provision, and then if Congress wants to grant the money, to hand it over to the Philippines, they can do that in a general appropriation bill, or in any other way that they see fit; but this directs that it be turned over to the Philippines; it earmarks the tax, in other words.

Senator COUZENS. You think that is unconstitutional?

Senator CONNALLY. I am fearful because one court has already held that it is.

Senator BLACK. Is there an injunction out against it?

Senator CONNALLY. No, I do not think there is an injunction. The Treasury can tell you that.

Senator KING. I think it would be tremendously disturbing to the Philippines.

Mr. KENT. I think there was an injunction issued against the payment of the amount to the Philippine Government.

Senator CONNALLY. That may be. It is not my disposition to take it away from the Philippines, but if it is knocked out, the Philippines won't get it and we won't get it either. If the court holds the act invalid, what good will it do the Philippines? It won't do their treasury any good, but if we do fill up this crack, if Congress wants to hand the money to the Philippines, all right.

Senator KING. I fear that it will create a great deal of perturbation in the Philippine Islands.

Senator CONNALLY. You would be amazed to know that this act has not resulted in a very material reduction of coconut oil which the Philippines are selling, and they are getting a great deal more pay for this coconut oil than they did. I have the statistics here to show that their imports are being affected very slightly, but they are getting more for it than they did before.

Senator WALSH. Senator Bailey, will you continue with your amendment?

Senator BAILEY. I have about finished. Section 705 is as follows:

Effective on the day following the date of the enactment of this act, the last sentence of subsection (a) of section 602 (1–2) of the Revenue Act of 1934, as amended, is amended by striking out the comma following "imposed" and by striking out "but does not include the use of palm oil in the manufacture of tin plate."

Change title V to title VI and change sections 201, 702, and 703 to 801, 802, and 803.

Senator WALSH. I would like to ask Senator Bailey and Senator Connally both what effect this amendment if adopted will have upon the price of these commodities to the consumers?

Senator BAILEY. I cannot make a definite statement, but I will make a very frank statement. It is intended that the price to the consumers shall be raised. If that was not the intention, I do not know that I would have the proposition here.

Senator WALSH. To what extent?

Senator BAILEY. I think to a very modest extent, but it will raise it sufficiently to enable the American farmer and the American fishermen to carry on. If you do not aid them, they will have to quit. They cannot stand this competition.

Senator CONNALLY. Let me suggest to Senator Walsh: In the case of a lot of these commodities, it won't raise it at all, but the point is this: We put excise taxes and other taxes on certain of these oils, and they immediately switched and used other oils as substitutes, which in effect evaded the effect of the tax. What Senator Bailey is doing is providing for the taxation of some of those substitute oils.

Senator BAILEY. That is right. In putting the tax, for example, on tallow at the same rate that it was on the other oils. We were getting 245,000 pounds of tallow into this country prior to the passage of the 1934 act, and that leaped from 245,000 pounds to 245,000,000 pounds. The whole business concentrated on that substitute. They could have used the tallow in competition with all foreign products. Of course it brought the price down here.

There were other oils which we did not take in the 1934 act, and they were immediately substituted for those upon which we put the tax. I am supporting the amendment upon the ground that it covers the very materials on which we levied the taxes in the interests of our farmers in the beginning.

Senator WALSH. What is the rate on tallow at present?

Senator BAILEY. One-half of 1 cent.

Senator WALSH. What do you propose to make it?

Senator BAILEY. Three cents.

Senator KING. Do you call your amendment a tariff tax or an excise?

Senator BAILEY. They call it an excise tax; insofar as I am concerned, if you put a tax on an import into this country, I think we have always called it, according to the Constitution, an impost. However, that may be, let it go as a tariff tax.

In the first portion of the bill, we have put a tax on the importation of articles into this country in competition with the farm products, and I think it is properly classified according to the way we have done things here for a hundred years, it is a tariff tax.

Senator KING. Senator, do you think it is wise for us to embark upon the policy in this bill of levying additional excise taxes? If we start with tallow, where are you going to end?

Senator BAILEY. Let me say that we are not proposing to levy additional excise taxes. We are extending the taxes levied in the 1934 act over certain substitutes which are being shipped in, because we did put a tariff tax on the original articles. It is not extending the act; it is extending the purpose of it so as to make it more embracing, but it is not a new tariff act, and I have cut out here fish scrap, fish meal, and other marine-animal scrap. I cut that out because that would be breaking new ground.

If our proposal were entirely new, I would leave those in; I think they should be, because it is a good thing, but all I am trying to do is to stop the gaps in the 1934 act; and if you do not do it you are going to find the price of cottonseed and cottonseed oil and soybean and soybean oil, tallow, hog fat, all going down under the competition of the foreign nations. If you wish to do that, all right, so far as I am concerned.

The President gave us an example the other day when he lifted the tariff on the importation of textiles from Japan. I am just doing the same thing here. We cannot stand still the balance of the year and see these prices go down. Cottonseed has fallen 50 percent already. Soybeans have fallen 35 percent.

Senator KING. Do you contend that that is the result of importations?

Senator BAILEY. There is no doubt about it.

Senator KING. Because of competing commodities?

Senator BAILEY. There is no question about it, and the whole fat proposition has gone down, and the oil proposition, because of this importation of 245,000,000 pounds of tallow into this country.

Senator KING. Where did it come from?

Senator BAILEY. It came from all over the world; from the Argentine, where you have your main production; and from Asia as well; and it comes also from Germany.

Senator CONNALLY. When we first put this excise tax on these coconut and other oils, cottonseed responded instantly to $12 a ton, but as soon as they learned how to use these substitutes, it began to recede.

Senator WALSH. What increased imports have there been other than tallow?

Senator BAILEY. I will be glad to give you that.

Senator KING. While the Senator is getting that, may I read a letter that came to me and came to the chairman of the committee. It came from the National Paint, Varnish, and Lacquer Association, and the Linoleum and Felt Base Manufacturers Association.

Senator CONNALLY. All of which have good tariffs on them.

Senator KING. This communication is as follows [reading]:

There are two items in the Bailey amendment, a tax of 4½ cents per pound on imported tung (china wood) oil—

I understand that tung has been left out [continues reading]—

and a like tax on perilla oil—which seem to be without merit and will actually work harm to American agriculture and industry. Tung and perilla oil are not used in the edible industry; they do not compete with dairy products, nor do they compete with fish oils.

The request for the tax on these items comes from the American flaxseed farmer who desires to have the drying-oil market diverted as much as possible to the use of linseed oil, which is a product of flaxseed. The American flaxseed farmer is amply protected by a 65-cent tariff and yet he is unable to supply half of our national requirements.

The Department of Agriculture attributes failure to attain greater American production to a combination of physical causes, such as frosts, grasshoppers, and the drought. Under the new Soil Conservation Act a bonus of 20 cents per bushel will be paid to the flaxseed farmers, and yet the Department of Agriculture hopes that this aid, together with a 65-cent tariff, will merely bring American flaxseed production back to the point where half of our requirements are raised in this country.

Every pound of domestic flaxseed that is grown is readily absorbed by the market at a fair price (present market price is $1.68 a bushel). Advocates of these taxes point to the fact that perilla and tung oil are coming into the United States in increasing quantities, which is quite true, but so is foreign flaxseed being imported in increasing quantities. Last year more than 17.5 million bushels of flaxseed were imported which, when crushed, will yield in excess of 300,000,000 pounds of oil. In 1934, domestic production of flaxseed dwindled to slightly more than 5 million bushels (due to the drought) and naturally it was necessary to import greater amounts of foreign oil which did not displace but supplemented American linseed oil.

Perilla oil, which to some degree competes with linseed oil, contains a higher iodine value, i. e., has greater drying properties, and has been used in the paint and varnish and linoleum industries in combination with soybean oil, which is low in iodine value. Virtually all of the soybean oil consumed in this country is of domestic production, and soybeans are raised in more than 20 States. As stated, soybean oil finds a ready market in the above industries when combined with perilla. In 1935 approximately 18 million pounds of domestic soybean oil were used in the paint and varnish and linoleum industries, largely in combination with perilla oil. Thus, a tax on perilla would curtail its use and at the same time close one of the large outlets for the consumption of soybean oil.

The next paragraph deals with tung oil, and it is not necessary to read that.

The communication continues:

It is incontrovertible that the taxing of these two oils will penalize progress and tend to suppress the manufacture of superior products.

The problem of the flax grower is not merely the competition of various oils, but also the ever-pressing competition of nonoil-bearing products, and the loss of markets for products carrying drying oils. Lacquer and synthetic enamels have supplanted varnish in the important automobile industry, and lacquer is widely used on furniture.

The paint industry has contributed over $139,000,000 in a flax-development program. It encouraged the development of the soybean industry. It introduced tung plantings. It is now securing cooperation of experiment stations in extensive experimental perilla plantings.

We approve of an American market for the American farmer. We have also attempted to find an American farmer to supply the American market.

There is every reason to believe that additional taxes on drying oils will not result in greater production of flaxseed but, instead, will seriously burden the paint, varnish, and linoleum and felt-base industries, with a resultant shifting of purchases from the Orient to a greater degree than ever before to Argentine.

Senator BAILEY. May I now respond to the inquiry of the Senator from Massachusetts? I have a table here and it is in the record. The tallow imports were as follows:

	Pounds
1931	1,671,000
1932	501,000
1933	238,000
1935	245,725,000

It jumped from a low of 238,000 pounds in 1933 to a high in the last year of 245,725,000. It went up a thousand times.

Senator WALSH. What do you claim is the reason?

Senator BAILEY. Because of the substitution of these articles on which we placed our duty. Perilla seed figures are as follows: 13,000 pounds in 1931, and 72,000 pounds in 1935. That is multiplied by about five or six.

Senator CONNALLY. What did these paint people do before they got the perilla?

Senator BLACK. May I ask if that is the oil that I read in your statement that you placed in the record, that there was one oil which had escaped taxation simply by transferring the point at which the raw product was processed? I believe that was perilla, was it not?

Senator BAILEY. I am not sure.

Senator KING. This paint and varnish and linoleum is addressed solely to tung and perilla.

Senator BAILEY. Let us be perfectly plain about it. These manufacturers get all of the protection they want, but when the farmer wants a little, they all come up with a thousand excuses. So far as I am concerned, I will vote against giving them a dollar as long as they are unwilling to give the farmer his share of protection. That is one of the troubles in this country. I have very little patience with their attitude. If they will come in here and take all of the tariff off of their products, I will take it all off of these farmers. But they won't stand for it; they want it all. That is no way to run a country.

I have a list of the others——

Senator KING (interposing). May I interrupt you right there, Senator?

Senator BAILEY. Flaxseed jumped from 14,000,000 to 17,500,000. Now, what has happened with cottonseed oil? That is a most singular thing. It appears that none was imported into this country in 1931, 1932, and 1933, but last year there were 166,678,000 pounds of cottonseed oil shipped into this land of cotton.

If we want to stand still and see the foreign nations ship their cottonseed oil into this country and depress the price, we can stand for it, but here is the point. Last year cottonseed brought $18 to the bale of cotton. I mean to say, the farmer got $60 for the lint and about $18 for the seed, and it was the greatest help in the world. There is 1,500 pounds of seed in each bale of cotton. It has gotten to be a very valuable thing.

Senator CONNALLY. That may be what it is in North Carolina, but it is a thousand pounds in Texas.

Senator BLACK. I do not see cottonseed oil in this amendment.

Senator BAILEY. I think I have it in here. If we have not, we ought to have it. That has come in notwithstanding the 3 cents a pound we have.

Your soybean cake has jumped from 39,000,000 pounds in 1931 to 107,000,000 in 1935. That is a jump of about three times.

Your copra cake has jumped from 7,400,000 pounds in 1932 to 102,000,000 pounds. That is a multiplication of 12 or more than that—nearly 15 times.

Senator CONNALLY. In other words, if they put a tax on coconut oil, they switch over to cakes.

Senator BAILEY. Cottonseed cake was 1,500,000 pounds in 1931 and is 15,000,000 now.

Senator KING. Where does that come from?

Senator BAILEY. Cotton is produced in 57 different countries. India is the principal producing country outside of ours, but Brazil is developing herself and Russia is developing. You can sit perfectly still and let the world come over here and take our domestic market away from our farmers. If we want to do that and have a free-trade country, all right; but if you are going to have any protection for manufacturers, it does not lie in the mouth of the manufacturer to come up here and say that the farmer shall not have his share. That is my proposition.

The amendment is drawn not to write a new tariff, but simply to extend the duties on these substitutes which have been used to break down the act that a Democratic Congress and the Democratic administration passed in 1934. I am not breaking any new ground. I have stricken out fishmeal and fish scrap. A little further I have stricken out tung nuts and tung oil. That is out of courtesy to the absent chairman.

I ask that the bill be favorably considered, and I hope you gentlemen will pass it as a constructive and necessary and very fine piece of legislation. If you do not, your soybean market and your cottonseed market and your general American fat market will go all to pieces.

Senator KING. I feel it my duty to invite the attention of the committee to a memorandum from the Secretary of State.

Senator CONNALLY. Was that not read once?

Senator KING. No; this refers to the Bailey amendment.

Senator CONNALLY. Then this is something else?

Senator KING (reading):

Proposal: To maintain, in some cases, and increase in others, existing import taxes on a long series of oils and fats: (1) Continue 3 cents per pound tax on whale oil, fish oil, marine-animal oil; (2) impose 3 cents tax on tallow and greases, in addition to existing tariff (½ cent per pound on tallow); (3) increase tax on sesame oil and sunflower oil from 3 cents per pound to 2½ cents (no tariff on these as present if denatured); (4) impose for the first time import taxes, 4½ cents per pound on inedible olive oil, perilla oil, tung oil, rapeseed oil, hempseed oil, and kapok oil; (5) impose tax of 2 cents per pound on perilla seed, hempseed, rapeseed, sesame seed, kapok seed, tung nuts; (6) impose tax of ⅝ cent per pound on fish scrap and fish meal; and (7) continue present processing taxes (3 cents per pound) on coconut oil, palm oil, and palm kernel oil (additional 2 cents tax on coconut oil from countries other than the Philippine Islands and other United States possessions.)

The proposal is obviously one to set up a solid, highly restrictive tax front against imports of fats and oils by plugging up all the cracks now existing.

Arguments against: These are both general and specific as to particular oils.

A. Broad arguments: Taxing these products or increasing taxes on some of them:

1. Runs directly counter to our program to reduce trade barriers and diminishes faith of foreign countries in our good intentions.

2. Reduces foreign purchasing power for our exports and invites retaliation and renunciation of present treaty commitments.

3. Threatens to create shortages of types of materials especially adapted to certain uses in soap-making and to force costly and burdensome readjustments upon industrial consumers and to burden ultimate consumers as well.

4. Impedes restoration of foreign markets for lard, not only through reduction of foreign purchasing power, but, more specifically, by diverting on to world markets much larger quantities of oils (e. g., whale oil) which compete in foreign countries with American lard.

B. Specific arguments as to particular items:

1. Tallow: Imposing a tax of 3 cents per pound on tallow, in addition to present tariff of ½ cents per pound would:

(*a*) Normally have no appreciable effect on domestic tallow prices, because imports, normally, are too small to affect appreciably the domestic price structure.

(*b*) Would tend to raise prices materially at this time because of continued large importations of tallow resulting from the drought and high import taxes on whale oil and palm oil, which are the chief competitors with tallow in soap making. But even under present conditions, livestock producers would receive little, if any, benefit because of (1) uncertainty as to how far, if at all, the tallow renderers would pass the benefits along to the producers and (2) fact that, in any case, the effect on the price of a steer is small. For a 1,000-pound steer containing 70 pounds of tallow, if the price of tallow rose by the full 3 cents tax and half the benefit eventually got to the cattlemen, the amount would be $1.10. Both these assumptions are overgenerous.

(c) Would complicate our commercial relations with Argentina, Uruguay, Australia, and New Zealand, from which tallow imports have been coming.

(*d*) Would be especially untimely in relation to Australia, because of delicate situations right now. Australia has authorized imposition of licensing restrictions on imports from the United States, to effect closer balance of trade, but has not yet imposed licenses. We imported $1,323,000 of tallow from Australia in 1935. Suddenly to tax tallow at this time might well precipitate licensing action against our exports. (Imports of tallow will doubtless gradually subside in any event, but the complicating effects of a tax at this time will be no less on that account).

(2) Whale oil: Reenacting the tax on whale oil runs directly counter to all the considerations which weigh in favor of repealing this tax, which are familiar. (See below.)

(3) Perilla oil and tung oil: These are drying oils used largely or exclusively for specialized purposes. For tung oil there is no oil substitute produced in the United States. It is a waterproof oil. The domestic tung industry is negligible; imports, from China and Hong Kong, have always been substantial ($13,131,000 in 1935). Perilla oil is used especially for high-gloss varnish, but when blended with slow-drying soya bean oil, competes with linseed. But free entry of perilla oil:

(*a*) Enhances outlet for domestic soya beans.

(*b*) Contributes to Japanese purchasing power for our cotton and other products.

(*c*) Checks substitution of synthetic (cellulos) paints for oil paints.

(4) Rape-seed oil: Used, normally, in reciprocating-type marine engines. Other uses in 1935 due to high prices. To impose tax on this would burden marine interests and, ordinarily, have no compensating advantages for other interests.

Senator BYRD. Does the Secretary want the tax on whale oil repealed?

Senator KING. I have not read it. There is a statement here by Mr. Paredes, resident commissioner of the Philippines to the United States. It seems to me that we ought to do him the courtesy, inasmuch as this is affecting his country, to consider it. What are your views, gentlemen? I have not read it.

Senator WALSH. Are we going to meet this afternoon?

Senator KING. I think so.

Senator CONNALLY. I do not object to having it read for the record.

Senator BAILEY. I do not think it is necessary to reply to that statement from the State Department. The questions will always be whether the Congress is to raise the tax or run the commerce of this country, or somebody else. I am in favor of the Congress doing it. That is a constitutional obligation. They have a strange idea that they can build up American trade by letting those people compete with our farmers, and at the same time we try to give the farmers tariffs on domestic trade. Why not give the farmer the tariff the same as anyone else gets, to start with?

Senator CONNALLY. May I just say a word, and I am through? We fought this thing out 2 years ago and we put it on. It did the farmers a lot of good, but the soap people and others immediately set about finding a way to evade the tariff, and they did so by bringing in a lot of these substitutes and then treating them chemically and making comparably the same article that they made before. This amendment in substance does not bring within the law any new subject-matter. True, it brings in other names of the oils, but basically they are the same thing.

I know that in the case of cotton seed, the price went up from about $18 to about $30 a ton in a little while after this law went on the books, but gradually since that time they have been evading it by bringing in these 245,000,000 pounds of tallow in a year where they did not import any, to speak of, before.

The simple question is, do you want to treat the farmers and agriculture like we are treating the manufacturers? Not fully, but only a little smidget; just give them a little smidget.

Of course, that letter from the Secretary of State sounds like a brief from the importers. He had to have all of the argument and technical data about what perilla oil will do, and he got it from the interests that go over there and throw it on his desk.

Senator BLACK. May I ask, what is the tax on oleomargarine?

Senator CONNALLY. 10 cents a pound.

Senator GUFFEY. There are two taxes on it; one on the white and one on the colored.

Senator BAILEY. I think that is correct.

Senator GUFFEY. Senator Bailey, as you state your amendment, it is to tie up some loopholes in the present law and also some abuses under the present law. There is a tax on palm oil. There is nothing said about palm-oil refuse, and for 18 months the Treasury Department did not tax palm-oil refuse. Last October they started to tax palm-oil refuse. It is the refuse from palm oil used in tinplating. I am wondering if you can cover that in this amendment of yours?

Senator BAILEY. I did not have that expression, but I will be glad to add it. Let me get the facts before you regarding the purposes of the bill that I have introduced.

Due to the various improvements, experiments and developments, it has been definitely determined that fats and oils of different types are interchangeable one with the other. The whole proposition is that we have reached a point under the development of chemistry where an oil is oil and a fat is fat. You can put your tariff on this one or on that one, and if you do not put it on the third one, you have not anything. They can be reduced by hydrogenation to the elementary oil. This bill simply extends it to correct the gap.

I am willing to accept that——

Senator CONNALLY (interposing): No; I cannot go with you on that. My amendment provides specifically in that regard. Tin plate has a high tariff, and why should it get all of the free importations and not have a tariff on what it uses?

Senator GUFFEY. For 18 months they did not put a tariff on. It is on not through the act, but through a ruling of the Treasury Department.

Senator CONNALLY. They got this amendment in that it does not include the use of palm oil in the manufacture of tin plate.

Senator KING. Senator Copeland wishes to have his amendment considered.

Senator BAILEY. May I have mine considered independent of his?

Senator KING. Out of respect to the Philippine representative, we should hear his statement if we do not let him testify. They are in trouble enough now over economic disturbances, and I feel that this amendment is going to be very serious as affecting them psychologically as well as economically. I suggest that we take a recess until half past 2.

Senator WALSH. I submitted an amendment dealing with mutual investment trusts on which I would like to have the opinion of the Treasury Department.

Senator BAILEY. I would like to have a vote on my amendment. It is being delayed and delayed and delayed. Can we not have a vote, Mr. Chairman?

Senator KING. I am the servant of the committee. I prefer to wait until 2:30.

Senator BAILEY. For what purpose, may I ask?

Senator KING. I want to read this statement of Mr. Paredes, and the statement of Senator Copeland.

Is it desired that you take a vote now or at 2:30?

Senator BAILEY. I have just made my statement and I would like to get the thing off my hands.

Senator CONNALLY. Make it 2:30.

Senator KING. Without objection, the committee will meet at 2:30 this afternoon in the District of Columbia Committee room in the Capitol.

(Whereupon, at 12:15 p. m., a recess was taken until 2:30 p. m. of the same day.)

AFTERNOON SESSION

(The committee met at 2:30 p. m., pursuant to the taking of a recess at noon.)

Senator KING (presiding). The committee will be in order. Senator Bailey, a few other Senators may come in and then we will be ready to vote.

Senator Copeland is here and he has to go. Have you any objection to his presenting his matter now?

Senator BAILEY. Not a bit.

Senator KING. The committee will hear you, Senator Copeland.

Senator COPELAND. Mr. Chairman and gentlemen, the thing that I am asking you to do is to repeal the 3 cents per pound excise tax on inedible whale oil.

Last year the Senate accepted an amendment I offered to this same effect, and this was dropped out of the tax bill in conference. The reason it was dropped out was because the farmer organizations were opposed at that time, fearing that imported whale oil might compete with American fats and oils in the American market. On account of that opposition, a compromise bill was introduced and it is here now, that this whale oil shall be rendered inedible by denaturing so that it cannot possibly be used as a food product.

You have on file here a letter from the Agricultural Department and also from the Treasury Department favoring this proposal. The Agricultural Department points out the fact that it is greatly to the advantage of the American farmer who is producing oil to have this inedible oil brought in for soap-making purposes, because when the tax is so high that it cannot come in, it is consumed in Norway. They use it in making a substitute for butter, and so it is a food product in Norway, and by reason of the fact that it is used as a food product over there, there is a lesser demand for butter and lard from our country, and, as I say, that fact is pointed out by a letter from the Department of Agriculture dated February 1 and addressed to the Secretary of State.

One paragraph states:

> The general views of the Department of Agriculture regarding the tax on imported marine animal oils were summarized in the departmental memorandum in May 1935. This memorandum was published in the Congressional Record of August 15, 1935.

There is a very full report in that copy of the Record, because at that time I was urging the committee to accept this amendment, which it did do.

> These views are that as a whole there is little or no benefit to American agriculture from an excise tax on imported whale oil, but on the contrary a possibility that this tax may work actual harm to some branches of agriculture. While there has been some changes in the factual situation since that time—

last year—

> they have not been such as to affect materially the conclusions expressed in our earlier survey.

Without taking the time of the committee, the Agricultural Department gives eight reasons which they have developed very fully in favor of the amendment, which I am asking you to adopt.

The Secretary of State, in a letter to Senator Harrison urges the repeal of this tax and the admission of the amendment which I am proposing to the bill, and calls attention to the bill in this way:

> There is left no cause for fear of damage to any branch of American agriculture by the removal of the tax in question.

And it goes on to quote the letter which I have just read from the Secretary of Agriculture and asks:

> May I call particular attention to statements in the second paragraph that this tax may work actual harm to some branches of agriculture if it is not enacted.

That is, if it is left out because of the reasons that I have stated, because it will cut off a demand for edible butter and other farm products, lard, and so forth. The Secretary continues:

> In submitting this material to the consideration of your committee, I wish to reiterate that this tax will, if continued, seriously hamper our efforts to improve commercial relations with Norway and possibly create new difficulties. The tax has also become the subject of representations by the British Government.

And he makes reference to a letter from the British Ambassador referring particularly to Newfoundland, where there is a production of whale oil which if shipped in here, will permit the sale of very many American products, products from which they have recently lowered the tariff. He speaks particularly of motor cars, marine motor engines, flour, oil, skins, rubber boots, rope and nets, and so forth, and urges also that this tax may be taken off of whale oil in order that there may be some use for it here.

I am quite convinced, as has been pointed out by the Treasury Department in another letter to the committee, that it would not be enough simply to take the tax off of whale oil, because if that were done, there would be a lot of edible whale oil sent in here, but there should be, as is suggested in this letter of May 19 to Mr. Harrison from the Secretary of State—referring to Mr. Bailey's amendment—that a modification might be made there to read as follows:

except codliver oil, cod, halibut oil, sperm oil, and except whale oil rendered unfit for use as food or for use in the manufacture of food products by denaturing, under customs supervision at the port of entry, by such means as shall be satisfactory to the Secretary of the Treasury, and under regulations to be prescribed by him.

That would insure that whale oil that is brought in would be denatured, and it would not be used for edible purposes in the United States, and I strongly urge that this may be done.

The committee last year accepted the amendment even without the denaturing provision, and I believe that with that, there could be no possible objection.

Senator KING. Why was it stricken out in conference, do you know?

Senator COPELAND. Yes; because, as I said a moment ago, the agricultural interests at that time thought that it would interfere with them. The Secretary of Agriculture in his letter says, no, it would not, but this gives a double assurance if it is denatured that it could not possibly be competitive of any American edible product.

Senator BYRD. It competes with fish products, does it not?

Senator COPELAND. No. The whale is a little different animal; he is a mammal. But the other fish oils that the Senator from Virginia has in mind are not competitive; whale oil is not competitive with them.

Senator BYRD. That information I get is that it is. They think that this amendment will be disastrous to them.

Senator BAILEY. We are not here taking taxes off. I am putting taxes on. I think if you get into the business of taking taxes off, you are breaking new ground. All oils are competitive, no matter from what source derived. You can take whale oil and reduce it to fill some of the demand for tallow. An oil is an oil, and the processing just changes its character.

That is our difficulty about this act. They put in substitutes for articles on which we placed the excises, and we are just moving out to get those substitutes. That is the whole principle that we are following. You, Senator, are asking to make an exception and take a tax off that is already on. If you do that, you are violating a principle on which I started. My principle is not to take any taxes off, but simply extending the act.

Senator COPELAND. You are putting the taxes in your amendment.

Senator BAILEY. We are putting taxes on these substitutes.

Senator COPELAND. But you are making some exceptions in your amendment.

Senator BAILEY. We excepted sperm oil as a matter of grace. We did not have anything else to do about it. We excepted codliver oil. There is a perfect basis for that exception. There is no substitute for codliver oil; it is not competitive and it is not a food.

We have excepted sperm oil, but you have all of the balance of the whale to make oil out of. You can make just as much oil out of the carcass of the whale as you can out of any similar tonnage of meat.

Senator COPELAND. The point I have in mind is if this is done, there will be an increase in our income from Norway, because there will be a market for our products, and subsequently they will be shipping other things in here and buying our products, too.

Senator BAILEY. That whole theory that we have to take our products of the farm or the sea and have them compete with foreign countries in order that those foreigners may buy our manufactured products, does not go with me at all. If you are going to take the tariff off and create a market, let us take it off the manufactured products and let them buy our cotton. I will go with you on that. We have traded the tariff proposition against the farmer for a hundred years. Now, let us trade a little bit for him and give him a fair show.

Senator COPELAND. Here you have your Department of Agriculture which urges that this be done.

Senator BAILEY. I may recognize that, but that does not affect my mind at all. I do not think the Department of Agriculture knows any more about agriculture than this committee does. And I do not believe we get our legislation properly when we go down the street to get it. The Congress is the sources of laws in America. Those people give us information and we make the laws.

Senator BLACK. Senator, I intended to ask this: After this oil has been treated in the manner that you have mentioned, what is it used for?

Senator COPELAND. Making a certain type of soap, and that is all. That is all. If I were discussing the general type of oils, I would make an argument about rapeseed oil which is used in making oil for heavy machinery and all that sort of thing, but that is not my job.

But this particular thing, if that is brought in, it gives us a cheaper soap of a certain type, where the whale oil is particularly valuable in its manufacture, and by having it denatured it could not be competitive in this country at all with agricultural products. On the other hand, if these quantities are shipped from Norway and from Newfoundland, there will be a demand there for butter and lard there from the American farmers.

Senator KING. Is there anything further to be said by either proponent or opponents of this amendment?

Senator BAILEY. I ask for a vote.

Senator BLACK. I wanted to find out before we voted—I asked the question this morning—I have never yet fully understood the difference between the law as it is and the law with reference to this amendment. Just what oils are added to what?

Senator BAILEY. This adds certain oils—I won't be certain which ones—but we put in oils and fats and salts of other such oils and getting into chemical changes.

Senator CONNALLY. We had it on the processing before, and they have evaded that by partly processing it before it came in. This is broadened so that it is still subject to the tax.

Senator BAILEY. It simply stops the gaps in the old law; that is all.

Senator BLACK. The reason I ask is just in connection with what Senator Copeland has said. I voted against the tax on oil originally. I am perfectly willing since the tax is on, to vote to include those oils in that different category that have evaded the tax by processing in a foreign country. I am perfectly willing to vote for the amendment to that extent, and I was trying to find out if it went any further than that. I would vote to repeal the whole thing today, but with it in effect, I am perfectly willing to vote to prevent the evasion by the processor.

Senator BAILEY. That is exactly what we are doing.

Senator COPELAND. What you are trying to do, Senator Bailey, is to increase the tax from 3 cents to 4½ cents a pound, is it not?

Senator BAILEY. On the whale oil, the tallow and the inedible animal grease there is an increase.

Senator CONNALLY. The Secretary of Agriculture says it is 1½ cents.

Senator BAILEY. There is an increase, for instance, on tallow from the present one-half cent a pound to 3 cents.

Senator COPELAND. May I ask you why you except sperm oil?

Senator BAILEY. I will tell you I do not know why they except sperm oil. It was excepted before, and we excepted it again. We do not want to change it. There is no evasion along the line of sperm oil. This bill is meant to stop the gaps, and that is not a gap. Sperm oil is a peculair oil, and is used very largely by the airplanes. It is a very fine type of oil, and I do not think it is competitive in the lubrication field as these other oils are.

Senator COPELAND. Now, Senator, your amendment, as I understand it, reads this way:

> Whale oil except sperm oil, fish oil except cod oil, codliver oil, halibut-liver oil—

Senator BAILEY (interposing). That is medicinal.

Senator COPELAND. Yes. Marine animal oil, and then tallow and so forth. Now, this is what I am urging upon the committee, that Senator Bailey's amendment be changed to read this way:

> Fish oil except cod oil, codliver oil, halibut-liver oil, marine animal oil except denatured whale oil for inedible use and except sperm oil—

because you have already used that language, and then go on with tallow, and so forth.

Senator BAILEY. That just takes the denatured whale oil out, and the moment you do that, another one will want to put denatured rapeseed oil in.

Senator GUFFEY. And denatured coconut oil.

Senator BAILEY. If a man denatures it and ships it in here, it is still competing.

Senator KING. I would like to hear from Mr. O'Brien. I am not quite satisfied with the situation as presented. That does not mean to say that I am not satisfied with the clarity of the expressions, but I would like Mr. O'Brien to just tell us what this does; what change it makes in the existing law.

Mr. O'BRIEN. As Senator Bailey has pointed out, there is added in this amendment to section 601 various substances which are generally considered fatty acids, salts of those oils which now are not

classifiable under that paragraph, and which it was intended, I suppose, as Senator Bailey says, to include in 1934 in that paragraph.

In addition, the amendment does this, with respect to sunflower oil, it takes that material out of section 602½ of the Revenue Act of 1934, which levies a processing tax on sunflower oil, which processing tax is at the rate of 3 cents per pound, and here imposes an import tax at the rate of 4½ cents a pound.

Senator KING. What would the effect of that be?

Mr. O'BRIEN. The effect of the change is that there is no processing tax on sunflower oil in the United States. That article is subject to duty at the rate of 4½ cents, whereas under the present law it is subject to a processing tax at the rate of 3 cents.

In addition to that, denatured olive oil which now is not subject either to a processing tax or to an import tax under section 601 (c) (8) is subject to a rate of duty that—I think it is—3 cents a pound under that amendment.

In the case of sesame oil, that oil is now subject to a processing tax of 3 cents a pound under section 602½. That oil is taken out of 602½ and put in this paragraph except that this paragraph goes not to all sesame oil, but to denatured sesame oil as specified in one of the paragraphs of the Tariff Act of 1930.

Furthermore, the amendment removes the exemption from processing tax of palm oil used in the manufacture of tin plate. Under the present law, palm oil used in the manufacture of tin plate is not subject to the 3 cents a pound processing tax but is under this amendment.

As to the Philippines, I think that has been explained.

As far as the treatment of the various commodities named in this amendment, I think that is a summary.

Senator KING. It takes a number of them out of the processing tax provision and puts them on the tariff?

Mr. O'BRIEN. Yes.

Senator KING. Taking it by and large, would it increase the price or the duties or the revenue in any way, or decrease it?

Mr. O'BRIEN. To the extent that new materials are included, of course there is more revenue if they will be imported.

To the extent that there is a difference between a 3 cents per pound processing tax on sunflower oil and a 4½ cents a pound import tax on sunflower oil, there is that difference in tax treatment.

Senator KING. The result is to make them all higher priced?

Mr. O'BRIEN. Not all. A number of them, for instance coconut oil and palm-kernel oil, are treated just exactly as they are in the present law.

Senator GEORGE. They are not affected at all.

Senator KING. I mean those that are affected.

Mr. O'BRIEN. I was naming those as to which there was a change in the law.

Senator BLACK. As the law is, as it is now written, has it tended to operate in such a manner that it was a constant inducement to process the oils outside this country and thereby evade the payment of the tax in this country?

Mr. O'BRIEN. I cannot answer that. I have heard that said, but I have not been concerned with the administration of the law.

Senator BLACK. Is there a witness here who does know?

I do not know, but it seems to me as I understand it, that has happened; they put a processing tax on the raw product and then simply processed them before they brought them into this country, and accomplished two results, as I have understood it and as I gathered from what I had read. The first result was that they processed it in the country abroad, which deprived us of the benefit of the processing in this country. The second was that it necessarily reduced the taxes in this country, because they did not have to pay a tax on it in this country.

Mr. KENT. I think I can clarify that a little bit by telling you something of what happened after the taxes imposed by section 602½ went into effect. Of course, it was known for some little time before the act became a law that something of the sort was going to happen. Some of the big soap manufacturers forthwith imported a vast quantity of coconut oil into this country and saponified it. That is a chemical process by which the chemical oil is broken up into fatty acids and glycerine, and the material can be pressed into bars and sold as a rather crude soap.

Moreover, the question arose as to what the situation under the act would be if instead of treating the coconut oil after it came in to this country, it was saponified in the Philippines, the glycerine was drawn off and the fatty acid residue was imported into the United States.

Senator CONNALLY. That is, tax free?

Mr. KENT. Tax free. We studied the matter very carefully and we could not find—I think we went as far in our regulations as we possibly could—but we could not find in the act any statutory warrant for imposing a tax on the fatty-acid residue when it came into this country because all of our chemists advised that these fatty acids were not coconut oil, that they did not contain a substantial quantity of coconut oil, that they were chemical derivatives of coconut oil, but that since this treatment had been applied to the oil, the glycerin had been drawn off, and you had something that was from a chemical point of view, entirely different from coconut oil. I do not know how much of these fatty acids were actually shipped into this country. They were not equipped, I was informed, to do that on a large scale. It would require a considerable capital investment to set up these treatment plants in the Philippines and other countries, and people hesitated to make that capital investment because they feared that as soon as Congress became acquainted with the situation, the law would be amended to take care of the situation and deprive them of any advantage. But there unquestionably was that danger if the situation had not been met last year.

Senator BLACK. The figures placed in the record show that there has been a very large increase in the importation of certain oils on which a processing tax was not imposed, and which they processed abroad.

Mr. KENT. Yes; I think it was even more than that. The tax was not imposed with respect to certain oils that could be used as substitutes for coconut oil and various other oils that were taxed.

Senator BLACK. Does not that give a decided advantage even between the products of the different countries?

Mr. KENT. Yes. And, of course, since there was no tax levied with respect to such oils, you did not have to subject them to any particular treatment abroad. The oils themselves could be brought into this country free from the tax and processed here.

Senator CONNALLY. Let me state some instances right there. We put a tax on coconut oil which is made from copra?

Mr. KENT. Yes.

Senator CONNALLY. When they put that tax on there, what did they do? They brought in copra cakes from the Philippines which theretofore had come in 7,000,000 pounds, and instead of 7,000,000 they brought in 102,000,000, because they could take this copra cake and put it through a chemical process and get the same elements out of it as they did on coconut oil. We had a processing tax on coconut oil but none on copra cakes, but they brought those in and evaded the tax. That is what they did.

Senator KING. Are you ready to vote on Senator Copeland's amendment to repeal the tax on whale oil now existing?

Those favoring the motion say "aye"; those opposed "no".

(The vote is taken.)

Senator KING. The "noes" have it.

Before voting on Senator Bailey's motion, I think we should hear from Mr. Paredes. He came to appear before the committee this morning and I told him that we were not conducting open hearings. I will ask now that the clerk read his statement.

(The same is as follows:)

MAY 23, 1936.

Hon. PAT HARRISON,
Chairman, Committee on Finance, United States Senate,
Washington, D. C.

DEAR SENATOR: I am informed that a proposal has been made to the State Committee on Finance to amend the existing statute with respect to the coconut-oil tax to provide that the revenue from such tax be paid over into the United States Treasury, rather than to the Philippine Commonwealth as at present provided for.

On behalf of my Government and the 14 million people who for 30 years have lived in faith and confidence and cooperation in and with American policies, I hope you will oppose any such unjust proposal.

It would destroy the basic reciprocal relationship between the Philippines and the United States which has for years been productive of progress, growth, and prosperity in both the islands and the United States. It is in direct contravention of every statute passed since the establishment of our reciprocal relationship including the provisions of the present Tariff Act and previous measure having to do with this subject.

You will recall that when the Philippine Independence Act was passed we assumed that during the 10-year pendency of that act the relationships established would, with certain inequalities removed, remain in force and effect.

We were confident of this mutuality of understanding not only because of the friendly attitude of Congress during the consideration of the independence measure but, again, because of the statement of President Roosevelt with respect to the inequalities which might be found in the Independence Act. In approving that act, you will recall, he pointed out the act, you will recall, he pointed out the hope of removing these inequalities.

It will be noted that the coconut-oil tax was contained in an act passed subsequent to the Independence Act. And the act was passed over the objection of the Philippine people and its representatives.

The burden of this tax falls heavily upon the vast number of people in the islands engaged in the growth and production of coconuts. The absorption of this tax, or a substantial portion of it by them was inevitable, and this came at a time when we were entering upon the very heavy and serious responsibility of an extended autonomy preparatory to ultimate independence.

The President of the United States at the time again called the attention of Congress to the inequity of the coconut-oil tax.

The only compensatory feature of this tax is the provision that the revenue derived from the processing of Philippine coconut oil is to be paid over to the Philippine government.

If that compensation is removed, then the tax becomes not only an inequity but an absolute unjust burden upon the second largest industry of our islands—an industry built up largely through the theory of reciprocal relationship with the United States over the past 30 years. It was in the spirit of cooperation that our Philippine people upon the suggestion of the American Congress agreed that our markets be thrown open to the free access of the respective countries.

It is inconceivable that the American Congress would at this time remove the only semblance of justice in the entire coconut-oil provision.

I cannot understand how in the face of a Presidential opposition to the coconut-oil tax itself there could now be levied upon our people the unthinkable provision of removing the revenue from this tax from our Government. Aside from its violation of the long-established principle set forth in the tariff and other acts over many years, it would establish definitely an attempt on the part of the United States to profit financially out of what has been a misfortune to the islands as found in the coconut-oil tax itself.

We were hopeful that your Committee on Finance would, as a matter of fact, remedy the injustice already done and approve the compromise proposal contained in what is known as the Guffey-Dockweiler bill under which the coconut-oil tax would be limited to oil processed for edible purposes. This would protect the dairy products as well as the cotton-seed-oil interests and the various other vegetable-oil interests of the United States 100 percent, and leave to the Philippine coconut-oil industry the industrial field wherein the domestic products of the United States are but negligently consumed.

To find now that a proposal which not only does not contemplate that modicum of relief but is on the other hand an aggravation of our troubles, is something which we are unable, after our long period of mutuality and cooperation, to understand.

Your attention is invited to the reciprocal provision of the Tariff Act of 1930 which is similar, or identical, to the provisions of previous tariff acts from the date of our establishment of our free trade relationships to which policy Congress and administrative officials of the United States have always adhered, and to which we respectfully call your attention and consideration.

We attach copies of President Roosevelt's statements (1) approving the Independence Act, and (2) urging the defeat of the coconut-oil tax.

We hope that you and your committee will do what you can to defeat this unprecedented proposal and, in fact, we confidently hope for your favorable consideration of the relief which we seek through the amendment of the present coconut-oil tax confining it to those produces consumed in the industrial processing field.

Very respectfully yours,

QUINTIN PAREDES,
Resident Commissioner of the Philippines to the United States.

QP:cl.

[H. Doc. No. 272, 73d Cong., 2d sess.]

ENACTMENT OF LEGISLATION FOR INDEPENDENCE OF PHILIPPINE ISLANDS

Message from the President of the United States transmitting a recommendation that legislation be enacted to the effect that the Philippine Islands shall be granted their independence. March 2, 1934.—Referred to the Committee on Insular Affairs and ordered to be printed

To the Congress:

Over a third of a century ago the United States as a result of a war which had its origin in the Caribbean Sea acquired sovereignty over the Philippine Islands, which lie many thousands of miles from our shores across the widest of oceans. Our Nation covets no territory; it desires to hold no people over whom it has gained sovereignty through war against their will.

In keeping with the principles of justice and in keeping with our traditions and aims, our Government for many years has been committed by law to ultimate independence for the people of the Philippine Islands whenever they should establish a suitable government capable of maintaining that independence among the nations of the world. We have believed that the time for such independence is at hand.

A law passed by the Seventy-second Congress over a year ago was the initial step, providing the methods, conditions, and circumstances under which our promise was to be fulfilled. That act provided that the United States would retain the option of keeping certain military and naval bases in the islands after actual independence had been accomplished.

As to the military bases, I recommend that this provision be eliminated from the law and that these bases be relinquished simultaneously with the accomplishment of final Philippine independence.

As to the naval bases, I recommend that the law be so amended as to provide for the ultimate settlement of this matter on terms satisfactory to our own Government and that of the Philippine Islands.

I do not believe that other provisions of the original law need be changed at this time. Where imperfections or inequalities exist, I am confident that they can be corrected after proper hearing and in fairness to both peoples.

May I emphasize that while we desire to grant complete independence at the earliest proper moment, to effect this result without allowing sufficient time for necessary political and economic adjustments would be a definite injustice to the people of the Philippine Islands themselves little short of a denial of independence itself. To change, at this time, the economic provisions of the previous law would reflect discredit on ourselves.

In view of the fact that the time element is involved, I suggest that the law be amended as I have above suggested and that the time limit for the acceptance of the law by the proper authorities and by the people of the Philippine Islands be sufficiently extended to permit them to reconsider it.

For 36 years the relations between the people of the Philippine Islands and the people of the United States have been friendly and of great mutual benefit. I am confident that if this legislation is passed by the Congress and accepted by the Philippines, we shall increase the mutual regard between the two peoples during the transition period. After the attainment of actual independence by them, friendship and trust will live.

FRANKLIN D. ROOSEVELT.

THE WHITE HOUSE,
March 2, 1934.

[H. Doc. No. 388, 73d Cong., 2d sess.]

COCONUT OIL IMPORTATION FROM THE PHILIPPINE ISLANDS

Message from the President of the United States transmitting a request for reconsideration of that provision of the revenue act, which relates to coconut oil. May 28, 1934.—Referred to the Committee on Ways and Means and ordered to be printed

To the Congress of the United States:

Early in the present session of the Congress the Philippine Independence Act was passed. This act provided that after the inauguration of the new interim or commonwealth form of government of the Philippine Islands trade relations between the United States and the Philippine Islands shall be as now provided by law. Certain exceptions, however, were made. One of these exceptions required levying on all coconut oil coming into the United States from the Philippine Islands in any calendar year in excess of 448,000,000 pounds, the same rates of duty now collected by the United States on coconut oil imported from foreign countries.

It is, of course, wholly clear that the intent of the Congress by this provision was to exempt from import duty 448,000,000 pounds of coconut oil from the Philippines.

Later in the present session, the Congress in the revenue act imposed a 3-cent-per-pound processing tax on coconut oil from the Philippines. This action was of course directly contrary to the intent of the provision in the independence act cited above.

During this same period, the people of the Philippine Islands through their legislature accepted the provisions of the independence act on May 1, 1934.

There are three reasons why I request reconsideration by the Congress of the provision for a 3-cent per pound processing tax.

First, it is a withdrawal of an offer made by the Congress of the United States to the people of the Philippine Islands.

Second, enforcement of this provision at this time will produce a serious condition among many thousands of families in the Philippine Islands.

Third, no effort has been made to work out some form of compromise which would be less unjust to the Philippine people and at the same time attain, even if more slowly, the object of helping the butter and animal-fat industry in the United States.

I, therefore, request reconsideration of that provision of the revenue act which relates to coconut oil in order that the subject may be studied further between now and next January, and in order that the spirit and intent of the independence act be more closely followed.

FRANKLIN D. ROOSEVELT.

THE WHITE HOUSE, *May 28, 1934*.

Senator KING. Gentlemen, I make an appeal in behalf of the Philippines. You know as well as I the hardships that they are encountering, the vicissitudes that are attending their embarking on a new government. We defeated them the other day, very properly, in regard to the gold clause and repealed the act which they thought was just, and now to administer this blow again, the effect will be very unfortunate.

The President indicated his opposition to the bill which we passed at the last session of Congress. I cannot speak for him, but I assume that he would feel just as strongly now in regard to this matter as he did then. I think we ought to eliminate, and I suggest to my friend from North Carolina, to eliminate from the amendment anything relating to the Philippine situation.

Senator BAILEY. I do not feel like doing that. I have two remarks to make. The Philippine Islands have for about 5 years been Uncle Sam's favorite project, and I am a little bit tired of that.

The other question is this: Whether we are to run this country in the interests of American agriculture or whether we will run it in the interests of agriculture of the Philippines. They have gotten their independence on a basis—I am willing to go along with them and help them—but we cannot help them at the expense of the American farmer and the American people. I do not feel like yielding to the suggestion, much as I think of our acting chairman. They come up here every time we have anything and they want a lot of special privileges. At the same time, they want independence.

Senator KING. We have had special privileges there. We have prevented them from finding foreign markets for their products. We compelled them to trade with us. We have prevented them for years from finding a market for their surplus products, and to that extent inhibited them in securing that stability and that economic independence essential to the maintenance of their government, where so many problems are to be encountered.

Senator CONNALLY. Mr. Chairman, may I say just a word? Senator Bailey is not really responsible for that portion of that amendment. He and I merged our two amendments into one amendment, and I am responsible for that relating to the Philippines.

We have got a tax on Philippine oils, and it probably is going to stay there, because I do not believe the Congress would knock out that clause on the ground that the money would go to the Philippine treasury; but that is a very real issue, and the people interested want it removed. I have no objection on earth about paying the proceeds of this tax to the Philippines if Congress wants to do it, just as now.

But in answer to Senator King, this act is not operating in any serious injury to the Philippine Islands. From January 1933 to

October 1935 the records show that the Philippines are getting more now for the coconut that they are sending to the United States than they did before the tax went on.

Senator GEORGE. It has improved their price?

Senator CONNALLY. It has improved their price.

Senator GEORGE. That is the ground that I took. Their price has been improved, and they have not been hurt. I think it highly questionable that the court decision which has been brought to our attention will be followed by the Supreme Court. It looks to me like the Supreme Court would say that we had a right to differentiate in dealing with the Philippines. But that is a danger of the amendment being thrown out on that ground. It certainly does not work any injustice if they get back the money, and it has helped their prices of oil. Their prices are greatly helped because they have a differential of approximately 2 cents on that oil. It gives them the market.

Senator LA FOLLETTE. I think that the Nye amendment obtained a great many votes in the Senate for section 602½ which it would not have obtained otherwise. Personally, I think it would be a mistake to raise that issue again in connection with this amendment. The Senator knows that I supported the amendment before and I want to support it now, but I do think it is going to cause a lot of controversy, and I do not know what the outcome will be, because I am satisfied from my own knowledge that there were a number of Senators who voted for it before——

Senator CONNALLY (interposing). The Senator understands that I am not hostile to that now. I do not object to the money going to the Philippines.

Senator LA FOLLETTE. I understand. But you understand that the contingency of an appropriation and all of that is very uncertain. This is just the decision of a district court, and it seems to me that under all of the circumstances you would be wise to eliminate this repeal from the amendment, and then if the decision as finally reached by the Supreme Court is adverse, you can always remedy the situation as the time comes.

Senator CONNALLY. May I briefly put some of these figures in the record? In December 1935 the value of coconut oil shipped into the United States from the Philippines was $8,555,000. From January to October 1935, after the tax went on, it was $10,000,000. Copra and coconut oil, valued for 17 months before the tax, was $20,000,000, and an average of $1,206,000 monthly.

After the tax went on, for 16 months, they shipped in $22,000,000 worth; $2,000,000 more in 16 months than they did in the 17, and the answer is that they are getting a better price. They are not shipping as much in, but they are getting more money out of it. As explained by Senator George, they have a favorable differential. We are still giving them that.

I want to suggest to Senator King that under this law we are still favoring the Philippines because we are giving them a differential.

Senator GEORGE. We give them our market. We buy their stuff, and in dollar value they are not hurt.

Senator CONNALLY. They are benefited. I do not say that the tax did it, but still the conditions are such that they are getting more money now than they did before; and that is one thing. We are giving them, as the Senator suggested, absolutely the American

market by reason of this differential, and I rather agree with Senator Bailey. This balance sheet has not all been on the side of the Philippines. We have spent millions of dollars there. They wanted their independence and we have given it to them. Let them stand on their own bottom.

Senator GEORGE. There is another thing, that it adds considerably to the revenue.

Senator BLACK. May I suggest in line with what Senator La Follette has said, that it seems to me that that letter is worthy of consideration. I had thought originally that this law had been enjoined and the taxes impounded.

Senator CONNALLY. The money is impounded, and it keeps it from going to the Philippines.

Senator BLACK. I had thought that they had enjoined it so that they help up the tax.

Senator GEORGE. In view of the decision, they won't pay any more tax.

Senator BLACK. They have not done it. I am very frank to state that I did not know how I was going to vote. I have decided, as far as the oils are concerned, it is almost stupidity simply to have an excise tax in such a matter that it favors certain oils over other oils, and it also encourages processing the oils out of this country in order to evade the tax. I personally would like very much to see you eliminate that part of the amendment which repeals the provision of law which is known as the Norris amendment.

Senator KING. I should be glad if that were done.

Senator CONNALLY. There is a very substantial danger that you lose it all.

Senator BLACK. This district court evidently did not go very far. They did not impound the tax, as they did in the processing taxes.

Senator CONNALLY. They simply enjoined that part of it going to the Philippines.

Senator GUFFEY. The chances are we will be in session again before the Supreme Court decision.

Senator KING. Senator O'Mahoney is here. Do you want to present any matter to the committee at this time, Senator?

Senator O'MAHONEY. I wanted to be present when there was any consideration given to sugar.

Senator KING. The subcommittee has disposed of it.

Senator O'MAHONEY. It was my understanding that I was to be called before the subcommittee.

Senator KING. I beg your pardon, Senator. We will hear from you now. We had representatives of the sugar people from the West, and I will state very briefly that their opinion was that the bill was not wise, certainly they did not favor any legislation until the House had acted or Congress had acted and established a quota. They were opposed to any tax until a quota bill.

Senator O'MAHONEY. I think that is the general feeling with respect to that, but the probability is that some satisfactory legislation will be developed which will preserve the quota system. In fact, I think it is of the utmost importance that that should be done.

Senator KING. So far as the facts were presented before the subcommittee, they reached the conclusion to report to the full committee adversely pending, of course, any action that was taken on the quota.

Senator O'MAHONEY. That is a qualified report?

Senator KING. Yes. And all of the witnesses were favorable to that. They said they did not want any tax bill until a quota was established. That, in substance, was their view.

Senator O'MAHONEY. With that understanding, would it not be possible for the committee to report that tax provision to the Senate so that it would have the advantage of coming to the Senate from the committee, otherwise it would have to be presented on the floor, and that would be a disadvantage in the closing days of the session.

As a matter of fact, it would be perfectly easy for the committee to kill the tax bill if it became evident that the quota system could not be effectuated.

Senator COUZENS. May I say something? I listened to all of the testimony this morning, and the committee was quite unanimous that this should not be tied on this bill, this processing tax for sugar, but if a processing tax were desired, it ought to be taxed on to the quota bill in the House where this matter should arise anyway.

Senator O'MAHONEY. That could not be done, Senator, because that would immediately raise the same constitutional question which resulted in the invalidation of the processing tax in the *Hoosac Mills case.*

Senator COUZENS. There is no disposition in the bill that we have here of processing tax.

Senator O'MAHONEY. No; but your suggestion, as I understand it, was that the processing tax should be attached to the quota bill. The A. A. A. legislation was knocked out in the Supreme Court because the processing tax was a part of that legislation.

Senator COUZENS. No; it was knocked out because of the use of the money. We were not determining to what purposes the processing tax would be used, so it would not come under the A. A. A. decision.

Senator O'MAHONEY. While that is technically correct, the joining of these two measures in one bill would be fraught with great danger, and I think probably would invalidate the beneficial effects of the quota system.

Senator COUZENS. I want to say that so far as I am concerned, and I think the committee was quite unanimous this morning, that we are going to do everything we can to defeat this processing tax from going into this revenue bill. I am only speaking for the subcommittee.

Senator GEORGE. We are quite satisfied that it will lead to a long debate and will prolong the discussion of this bill in the Senate several days.

Senator O'MAHONEY. Does that mean then, that the equivalent of Senator King's statement a moment ago is really not the mind of the committee?

Senator COUZENS. We are only determining about this particular bill. We are not determining upon the merits of a processing tax as such.

Senator O'MAHONEY. I understand that. But if it had been represented to this committee that the quota legislation had been satisfactorily worked out, would the committee then feel that it would proceed with a recommendation for a processing tax on sugar?

Senator KING. I do not think, Senator O'Mahoney, that we could decide that now. I think that we will have to rest on the facts that transpired.

Senator O'MAHONEY. If I understood you statement, the committee came to the conclusion that it would not recommend the processing tax until it had some assurance with respect to the quota system?

Senator COUZENS. That is quite correct.

Senator O'MAHONEY. I am trying to determine what the facts are.

Senator COUZENS. We decided that we would not recommend to this committee the incorporation of the processing tax in this bill.

Senator O'MAHONEY. May I inquire upon what ground that was based?

Senator COUZENS. So far as I am concerned, and I think we had a unanimous agreement on it, it was that we were not going to deal with the merits of a processing tax on sugar at this time, and therefore we would not recommend it to be put into this revenue bill.

Senator O'MAHONEY. Well, you see, Senator, that impales us on both horns of the dilemma, so to speak.

Senator COUZENS. Do you want the processing tax?

Senator O'MAHONEY. What I am anxious to do is to preserve the quota system and to preserve a system whereby the growers of sugar beets and sugarcane may have the benefits of the legislation which was recommended by this committee in 1934. Now we are confronted with this situation, that this committee now says that we cannot have the processing tax until we have the quota system.

Senator COUZENS. The committee did not say that.

Senator O'MAHONEY. We cannot have the quota system unless we have the processing tax.

Senator KING. The committee did not say that. Speaking for myself, when this bill is taken to the Senate and reported by the committee, and the House has taken such definite action with respect to the quota system as to make it possible and feasible and constitutional for us to attach to the bill a provision in regard to taxation, I should favor it. But the information before us was—all of the witnesses said in effect that they did not want us to report the bill out with a quota system undetermined, because they did not want any taxation system until they had a quota.

Senator O'MAHONEY. I hope that the committee has the same view that you have, Senator King.

Senator KING. I do not know what the view of the committee is, and we have not passed upon the report of the subcommittee yet, and I am sure as far as I am concerned, full opportunity would be given for the further presentation of that matter to the full committee.

Senator O'MAHONEY. When that comes, I would be very glad to be advised.

Senator KING. Yes. Now, are we ready to proceed with regard to the oil matter?

I wanted to move to strike out the word "perilla." I think in the light of the testimony that we ought not to include perilla. It stands in the same category as tung oil, and there are a number of industries depending upon it very largely, the linoleum and others, that it seems to me that that ought to be excluded from the bill.

Senator BAILEY. Senator, I will just give you the information. In 1931, the amount of perilla oil that came into this country was 13,285,000 pounds. In 1935 it was 72,327,000 pounds. We passed the act in 1934. When we passed the act in 1934, the amount was 25,164,000 pounds. It jumped in 1 year by way of escaping the force of that act to 72,000,000.

Senator KING. Do you think that is quite an accurate way of presenting it? We New Dealers are boasting of enormous advances in industry, the increase of production and factories and mills and so forth. You got back to 1931 when of course the importations were light.

Senator BAILEY. We have just gotten back to 1931, according to the index. The New York Times had that last Sunday, and to make it accurate we had gotten back to July 1, 1930, according to that chart. That is in the Investment Outlook. That would not account for it.

Senator BARKLEY. I would like to know how this 72,000,000 that is imported compares with the domestic production of comparable oils for which it is a substitute. It does not mean anything to make the comparison unless it has an appreciable effect on something that it takes the place of.

Senator KING. I would also like to ask the Senator, if he has any definite information as to what oils produced in the United States are comparable to tung oil and perilla and their use in varnishes and lacquers and linoleum? Whether we have anything that is comparable to perilla.

Senator BAILEY. I have no information about that except that these oils certainly have come in by way of substitution since we passed the act.

Senator KING. Can you say for substitution for varnishes and linoleum, because the increase in paints and varnishes and linoleum in the last 2 or 3 years has been very great.

Senator BAILEY. Nothing sufficient to account for this increase in this oil.

Senator COUZENS. May I say, can the Senator inform me what this perilla takes the place of in this country?

Senator BAILEY. I really do not know.

Senator COUZENS. Why do you object if you do not know what it takes the place of?

Senator GUFFEY. This increase is due to the fact that it is now used with soybean oil. In the linoleum industries and other industries they take a greater percentage of perilla oil, and that is what increases its use.

Senator KING. Because we use more soybean oil that it is used with?

Senator GUFFEY. Paint and varnishes used about 20 percent of the entire soybean output in 1935.

Senator BARKLEY. In other words, this soybean oil makes desirable the use of perilla oil as a mixture, because it dries faster and it is used in paints and varnishes.

Senator BAILEY. I am perfectly willing to have a vote on it, of course; but I have had an argument of the sort made by these paint and varnish and linoleum people on every oil. I have never heard the linoleum people say that their tariff be reduced. They just do

not want to pay any tariff, but they want to get all of the protection that they can.

Sentor CONNALLY. I want to say that the National Grange, the American Farm Bureau, the American Cotton Cooperative, and the National Dairy organizations are all of them for these taxes.

Senator COUZENS. They do not urge Perilla in there particularly, do they?

Senator KING. All in favor of the motion which is submitted by the chairman to strike out Perilla from this bill will say "Aye"; contrary "No."

The motion is agreed to.

Senator LONERGAN. At the request of Senator Moore, I move that sulphate of olive oil and olive oil be stricken from the bill, and I desire to place into the record a statement which Senator Moore sent to me in support of this motion.

(And the same is as follows:)

MEMORANDUM SUBMITTED BY J. A. COULTER, VICE PRESIDENT, COLGATE-PALMOLIVE-PEET CO., JERSEY CITY, N. J.

There will be an amendment offered in the Senate Finance Committee on Monday morning by Senator Bailey of North Carolina, to the tax bill, H. R. 12395, which proposes to place excise taxes ranging from 3 to 4½ cents per pound on a number of oils and fats.

While we object to the amendment as a whole this company will be gravely affected by the enactment of one in particular of the excise taxes proposed in Senator Bailey's amendment. We refer to the proposal to place an excise tax of 4½ cents per pound on "olive oil * * * as included in paragraph 1732 (the free list) of the tariff Act of 1930".

The proposal is to place a 4½-cent per pound excise tax on sulphur olive oil, which is inedible and while now on the free list sells at 7½ cents per pound (a fair average price). This would force us to pay 12 cents per pound for the essential ingredient of our chief selling brand of toilet soap, which must compete with soaps made from coconut oil and palm oil, the prices of which oils, excise tax paid, is 6¾ cents per pound. This would mean the practical elimination of our chief brand of toilet soap from the market.

The sulphur olive oil which we use is entirely of inedible nature. It is called sulphur olive oil because it is obtained from the press cake which results from the pressing of olives to produce edible oil by the use of a solvent called carbon bisulphide. The resulting oil contains approximately 50 percent free fatty acids as well as the green coloring matter known as chlorophyll, which with traces of the solvent used render impossible its usage for edible purposes. There is no record of its ever having been used for any purpose other than the manufacture of toilet and textile soap.

The average annual importation over the past 10 years has been 42,400,000 pounds per annum. The imports in 1935 were 34,000,000 pounds. About two-thirds of the imports are used in the manufacture of soap employed in the textile industry where it is required because of its easy solubility in water at low temperatures and quick rinsing properties.

The burden of this tax with respect to the oil mentioned and affecting a specific industry, is greater than the entire value of the Atlantic coast production of fish oil, which interest, we understand, is chiefly interested in this legislation. The only fish from which is produced oil of commercial importance along the Atlantic coast is the menhaden. The value of the entire production in 1934 (last year of record) was $704,000, according to Statistical Bulletin No. 1133 of the Bureau of Fisheries. The Bureau of Fisheries divides this production as follows:

New York, New Jersey, Delaware, and Georgia	$283,828
Virginia	248,041
North Carolina	72,960
Florida	99,170

In addition to the above there were odds and ends of various fish oils, the total value of which was $200,000 in 1934, the last year of record.

Under no circumstances can olive oil be considered to be in competition with fish oil in soap or any other industry because of the totally divergent characteristics of the two.

From the foregoing it may be seen that the levying of this tax will affect seriously one of the important industries of your State and we urge that every possible effort be made by you to oppose such enactment.

Respectfully submitted.

COLGATE-PALMOLIVE-PEET CO.,
J. A. COULTER, *Vice President.*

Senator BAILEY. You do not want to strike the word "sulphated", Senator Lonergan, because it relates to all of the other oils, do you?

Senator LONERGAN. Only insofar as it relates to olive oil.

Senator BAILEY. If you strike out "olive oil", you will get what you want.

Senator KING. Are you ready for the vote on that?

Senator COUZENS. What are the reasons for striking it out?

Senator BAILEY. Why not say "olive oil, except sulphated olive oil"? If I consent to one, there will be another amendment to each one.

Senator KING. I do not understand the amendment in the light of the amendment which has now taken the place of it.

Senator LONERGAN. Do you want me to read the long statement of Senator Moore?

Senator LAFOLLETTE. No, we do not.

Senator COUZENS. Can you not tell us the reason for it without reading the statement?

Senator KING. Then all in favor of the motion will say "aye"; contrary "no."

The noes have it and the motion is not agreed to.

Senator LONERGAN. On page 2, line 13, I move to strike out "rapeseed."

Senator KING. Have you any statement to make in support of that?

Senator LONERGAN. It is just for marine oil. I talked with Senator Bailey about it yesterday. Do you feel that you can modify that?

(Discussion off the record.)

Senator KING. Those in favor of the motion say "aye"; contrary, "no."

The noes have it and the motion is not agreed to.

Senator CONNALLY. Mr. Chairman, I want to accommodate myself as much as I can to the views of the members on this Philippine proposition.

Senator KING. I wish you would let that go out.

Senator CONNALLY. I have this thought: Let us go ahead and repeal this, and then let us put in a new section authorizing the appropriation to the Philippines of the same amount.

Senator COUZENS. That is a very difficult process to go through every year. I do not see your insistence upon repealing the present law.

Senator CONNALLY. Because the courts have declared it invalid.

Senator COUZENS. That is not a final decision. We will be back here in 6 or 7 months.

Senator KING. The chairman moves to strike out section 704. Are you ready for the question?

Senator CONNALLY. I very much hope that the committee won't do it.

Senator KING. It strikes out the Philippine proposition and leaves the present law. Those in favor of the motion say "Aye"; those opposed "No."

Senator BAILEY. Let us have a roll call.

(The roll is called, and the motion prevailed, 9 to 6.)

Senator LA FOLLETTE. The question now is on the amendment as amended. Let us have a roll call on that.

Senator CLARK. Mr. Chairman, I have just come into the hearing. I have been in the Senate. I understand the last vote was taken on the question——

Senator KING. Striking out the whole provision of the Philippines and leaving the present law.

Senator GEORGE. That part of the amendment which gave it to the Philippine Treasury.

Senator CLARK. I understand the amendment was to strike out the provision of the present law by which the amount of the coconut oil tax is given to the Philippine Government. I desire to be recorded against that amendment.

Senator LA FOLLETTE. You want to give it to the Philippines as it is now?

Senator CLARK. Yes.

(The roll is called, and the motion prevailed, 11 to 5.)

Mr. TURNEY. We would like to have permission for the Treasury to submit a revision of this amendment which would iron out some conflicts between it and the amendment which was passed last year, or rather some overlapping.

Senator BAILEY. Providing you do not change the tenor of this.

Senator KING. You are speaking now of the amendment as passed?

Mr. TURNEY. Yes. There are some provisions in this amendment which overlap the amendment which was passed last year and would cause some confusion. Mr. Johnson from the Customs Bureau can explain to you some of the difficulties which we would still have in administering this thing, and if the committee would like to consider incorporating those in the amendment——

Senator KING. Shall we take those up?

Senator LA FOLLETTE. I think it would be wise.

Senator KING. Mr. Johnson, we will hear from you.

Mr. JOHNSON. Our difficulties in administering this bill are to determine——

Senator KING (interposing). You understand the action which has just been taken?

Mr. JOHNSON. Yes.

Senator KING. Proceed.

Mr. JOHNSON. Section 402 of the Revenue Act of 1935 is somewhat similar to this bill and overlaps it in several respects. One purpose of our revision will be to eliminate those overlapping and perhaps to consolidate section 402 of the Revenue Act of 1935 with this amendment so as to give them full effect.

One of our difficulties is that the rate of tax on certain commodities is very difficult to determine. These products are processed in foreign countries, the processed products are assembled and reprocessed, and that goes on through several different stages, making the retracing of those things practically interminable. Of course, what

we would like is to have rates stated for each of the products, but that is, I understand, an impracticability from your point of view.

If you could authorize a determining of the rate on the basis of the facts ascertainable from the merchandise itself at the time of importation, we would have something we could deal with.

Senator LA FOLLETTE. Give us an example of what you mean.

Mr. JOHNSON. Glycerin, a product largely used in medicine and hospital services in the United States, is derived from innumerable oils. When it is imported in the state of glycerin, it is absolutely impossible to determine by examination of the glycerin whether that came from the city garbage or from one of these taxable oils. We have to trace the thing back. It is produced, some of it, in Russia, some in Switzerland, and some in Germany.

Senator CLARK. You mean it is impossible for you to determine from examination of the finished product?

Mr. JOHNSON. I won't say that it is impossible, but it is as near to it as anything that has come within our experience.

Senator KING. The cost would be very great?

Mr. JOHNSON. Enormous. On importations of glycerine during the effective period of the act of 1935, I do not think any importation has been finally liquidated. We have not reached yet a determination of what the rate is. When the rate is determined, I think it will be very low.

One of our largest problems right now would be solved if you would give us a special rate for glycerine or specially exempt it from the tax. Glycerine is sometimes made directly from the oil as a primary product, more frequently it is made from waste.

Senator BAILEY. How many articles have you like that?

Mr. JOHNSON. We have two.

Senator BAILEY. What is the other one?

Mr. JOHNSON. Whale fish. It is a peculiar product, very small in quantity, used principally in the making of composition flooring such as you have in the new Department of Labor Building. I do not know of any use other than that which it has at all. Until that use was discovered, it was thrown away as waste.

Senator BAILEY. What is it used as?

Mr. JOHNSON. Composition flooring, flooring for large public buildings where they lay the flooring something in the way that you lay cement, as I understand it. It is a resilient binding material.

Senator BAILEY. So far as I am concerned, when it comes to those small matters, if he wishes to make a special rate, he can leave glycerine and this whale fish out, and that is going to interfere with the operation of the law.

Mr. JOHNSON. One of our solutions would be to eliminate from the tax altogether all products which are derived from a waste, that is, where a waste is derived from the taxable oil and then from that waste a new product is created. If a waste comes in between a manufactured stage, you would disregard that. The compensatory tax would be small, anyway.

Senator KING. The waste would have to be, however, of oil?

Mr. JOHNSON. We would have no question if it is produced from some other material that is not within the scope of this tax. Our problem is first finding out whether it is produced from taxable oil, and then how much of it is so produced.

Senator KING. Your problem is what ameliorating provision should be contained in this act so that if waste came in which you knew came from some oil or some fatty substance, you would not be compelled to ascertain from which oil it came, but would give to it a customs duty quite different from pure oil or fatty oil itself?

Mr. JOHNSON. Yes.

Senator BLACK. How would you know it came from waste?

Mr. JOHNSON. As well as we know that it came from any other oil. We know that glycerine may come from garbage or hog oil, coconut oil, or several of these oils, and it is commercially so produced in several of these countries.

Senator BLACK. Why can you not name them if there are only two of them?

Mr. JOHNSON. We have had this tax in operation for only 9 months, and those have immediately come up. We do not know how many others are coming along. We may have some problems elsewhere that are not described.

The point I am making is that under the present law the tax would be small.

Senator KING. Could you prepare an amendment to submit to Senator Bailey and Senator Connally for their consideration, dealing with that, and also with these overlappings so that they can be properly integrated?

Mr. JOHNSON. Yes, sir. I have perhaps two other items.

Senator BAILEY. Just so that you do not interfere with the principle.

Senator GEORGE. You had better put a small tax on, otherwise you will have a small loophole.

Mr. JOHNSON. Could we have the bill expressly state that the tax imposed upon derivatives which are not expressly enumerated in your amendment——

Senator KING (interposing). Give an illustration.

Mr. JOHNSON. Glycerine I will have to use over again.

Senator CLARK. Is that the only one you have?

Mr. JOHNSON. No; we have others. Soap is one. Soap comes in if it is subject to a tax according to the derivative of its components. The list is limitless.

Senator LA FOLLETTE. What do you propose to do about it?

Senator CLARK. It seems to me it would be a strange thing if it is limitless, if the only one you can give here, the only one that you can think of is glycerine. If it is limited to glycerine, say glycerine, and if there are some others, let us know what they are.

Mr. JOHNSON. My present discussion is not on eliminating the tax.

Senator CONNALLY. What you mean is if there is a tax on coconut oil, then any derivative of that oil, if that oil originated in other countries, shall be relatively taxed just like the oil would be. Is that what you mean?

Mr. JOHNSON. At the present time any product more than 50 percent in value of which is a derivative derived from one of these taxable oils, bears an import tax equivalent to the tax which would have been paid upon the quantity of oil represented by that component of the imported article.

Senator CLARK. What do you propose to do with the amendment?

Mr. JOHNSON. To get rid of the value basis which requires these elaborate researches in foreign countries, and to provide that the tax shall apply to the imported article proportionately to the components in the article derived from the oil.

Senator CLARK. I understood your testimony to be in the case of glycerine, which is the only illustration you have used, that you cannot tell whether it is derived from one of these taxable oils or garbage or from some other thing.

Mr. JOHNSON. We can from examination of the article itself.

Senator CLARK. Just a minute. Why would you proceed under the rule that you propose rather than under the present law?

Mr. JOHNSON. Under the present law we have to determine the quantity, and having determined the quantity, we have to determine the value of the quantity, and we have to trace that back in some cases to more than one process.

Senator CLARK. Under your proposed rule as I understand it—if you cannot determine the quantity originally, how can you possibly determine a portion?

Mr. JOHNSON. In the present case, you already have to determine everything that I propose to continue to be determined.

Senator CLARK. You have to determine the quantity?

Mr. JOHNSON. Yes, sir.

Senator CLARK. And you say it is impossible to determine quantity?

Mr. JOHNSON. From examination of the imported article.

Senator CLARK. Then you come in here with an amendment by which you propose to set up portions, and I do not see how it is physically or mentally possible to set up portions unless you first determine the quantity.

Mr. JOHNSON. Exactly. But I say there is one element that we have not quoted. I say we cannot determine from imported glycerine by examination of the glycerine itself what it is derived from. We require statements on the foreign invoices——

Senator CONNALLY (interposing). Why do you not draw the proposed change? Draw the regular one and one like you want it, and we can vote on it when you come back.

Mr. JOHNSON. I will do that. The question of glycerine is a collateral question. If my proposal is adopted, the rates on glycerine and these products derived from an intermediate waste will be enormously increased.

Senator CLARK. Give us a list of some of these other products that you are talking about. You say they are innumerable, and all that you are able to cite up to date is glycerine.

Mr. JOHNSON. Everything you use glycerine in.

Senator CLARK. Give us a list of those.

Mr. JOHNSON. Yes, sir.

Senator CONNALLY. Mr. Chairman, I want to bring up one little matter; it won't take but about a minute. I have a little amendment later on coming up relating to the admission tax on community or cooperative concert associations. It has been a matter of dispute whether they were taxable or not. There is a delegation of these people, artists and others outside, and they do not want a hearing. Out here is Mr. Zimbalist, the famous violinist; Mr. Fischer, secretary of the American Musical Artists Association; Mr. Charles Hackett,

of the Metropolitan Opera; and Mr. Lawrence Tibbett. I should like to bring them in here and present them to the committee.

Senator KING. Any request made by the Senator is a command. Are there any further amendments?

Senator COUZENS. Mr. Chairman, on section 602 (f) in the bill, it provides that no payment under this section shall be made with respect to wholesale flour stocks, of articles processed from wheat, sugar beets, or sugarcane except—then come the exceptions—flour, prepared flour, and cereal preparations, and so forth. I would like to add the word "gluten" in there, because it really is processed and comes from wheat, and I have a mill in Michigan, one of the few exclusive manufacturers of gluten, and I think if there is no objection—I have talked with the officials, and there seems to be no objection to including that word.

(At this point the delegation referred to by Senator Connally were introduced to the committee, and there was informal discussion of the proposed amendment relating to admission tax, et cetera, with respect to community, civic, or membership concert courses or series.)

Senator COUZENS. My motion was to include gluten in section 602 (f).

Senator KING. Is there any objection?

Mr. PARKER. The Treasury may know something about it.

Senator LA FOLLETTE. Is this a refund?

Mr. PARKER. A refund of floor stocks which they have on hand. There are certain exceptions which are granted refunds in section 602 (f).

Senator COUZENS. I want to put gluten in there because it comes under the same heading as flour.

Senator KING. All in favor of the motion to include the word "gluten" will say "aye"; contrary, "nay."

(The motion was agreed to.)

Senator CONNALLY. With respect to the amendment in favor of which this delegation appeared, here is the present law, the Revenue Act of 1926, as amended by the Revenue Acts of 1928 and 1932, title V, section 500, of the act of 1926, subsection (b):

> No tax shall be levied under this title in respect of (1) any admissions, all the proceeds of which inure (A) exclusively to the benefit of religious, educational, or charitable institutions, societies or orgnizations, societies for the prevention of cruelty to children or animals, or societies or organizations conducted for the sole purpose of maintaining symphony orchestras and receiving substantial support from voluntary contributions, or of improving any city, town, village, or other municipality, or of maintaining a cooperative or community center moving-picture theater if no part of the net earnings thereof inures to the benefit of any private stockholder or individual.

What they want to insert is, after the words "moving-picture theater", the following: "or a community, civic, or membership concert course or series."

Senator COUZENS. I support the motion.

Senator KING. All in favor, "aye"; contrary, "no."

(The motion was agreed to.)

Senator LONERGAN. I have several matters here, and I talked with Mr. Parker and Mr. Beaman about them.

The first is, on page 166, after line 9, add a new paragraph as follows:

7. The amount received as dividends from a domestic corporation where the tax on such corporation under this title equals fifteen per centum or more of its net income in excess of the credit, if any, provided in section 26; and—

I will ask Mr. Parker to make a statement on that.

Mr. PARKER. It is proposed to add a new tariff which would decline the net income of a life-insurance company as to gross income less the amount received as dividends——

Senator LA FOLLETTE (interposing). I thought that we had decided, after careful consideration, that we were not going to upset this base of life-insurance taxation.

Mr. PARKER. All there is to this amendment is that the amount received as dividends from a domestic corporation where the tax on such corporations under this title equals 15 percent or more of its net income in excess of the credit, if any, provided in section 26—what they are asking for, as I see it, is that they do not want to be taxed on the intercompany dividends.

Senator LA FOLLETTE. If we are going into this business, we will be here 2 weeks.

Senator COUZENS. If that goes through, I am going to offer an amendment to tax all of their earnings outside of their reserves required by State laws.

Senator LA FOLLETTE. I think it is a great mistake to open this life-insurance matter.

Senator KING. As many as favor the motion made by the Senator from Connecticut will say "aye"; those opposed, "no."

(The motion was rejected.)

Senator LONERGAN. Now, I will offer this amendment:

On page 171, after line 6, add the following new paragraph:

"7. The amount received as dividends from a domestic corporation where the tax on such corporation under this title equals 15 per centum or more of its net income in excess of the credit, if any, provided in section 26."

Mr. PARKER. That is the same thing.

Senator KING. As many as favor the amendment just proposed by the Senator from Connecticut will say "aye"; opposed, "no."

(The vote was taken, and Senator King announced that the "noes" have it.)

Senator LONERGAN. I want to ask a question about this amendment that was submitted by Mr. Ferguson, of the Seth Thomas Clock Co.

Mr. PARKER. These are old companies——

Senator KING (interposing). Yes; we have had that before. One makes money, and the other does not.

Mr. PARKER. When section 351 was originally drafted, we had the consolidated return in all; and under the 1934 act, there was introduced into the Senate this parent operating company of the Seth Thomas Clock Co. and the Western Clock Co. in their relation to section 351. When the consolidated return was stricken out, that made them taxable. This is an operating holding company really, and they have some difficulties in declaring dividends with one company losing and the other making money. There is merit in the situation, but it is difficult.

Senator CLARK. In other words, they want to retain the Seth Thomas name as an advertisement and not pay taxes on it as an asset.

Senator COUZENS. We had the same condition when we examined the Treasury. We found that this publisher of the Saturday Evening Post was making an enormous amount of money on it and losing on the Public Ledger, and he was transferring his profits from the Saturday Evening Post to the Public Ledger and obviating taxes. That was one of the main arguments that made us dispose of these consolidated returns. Hearst was doing the same thing with his rotogravure section.

Senator CLARK. In other words, if we write an exemption for every particular company like that, you will have to write five or ten thousand specific exemptions.

Senator LONERGAN. I remember when Mr. Ferguson appeared before us a year ago, that the committee felt that there was great merit in his question, and I feel so now.

Senator KING. As many as favor the motion will say "aye"; those opposed, "no."

(The vote is taken, after which Senator King announced that the "noes" have it.)

Senator LONERGAN. Mr. Parker, yesterday I gave to Mr. Johnston an amendment that was submitted to me by Mr. Julian Curtis. I would like to have that presented.

Mr. PARKER. He represents the Spalding Sporting Goods Co. and suggests an amendment to section 609 of the Revenue Act of 1932, which imposes a tax on sporting goods. That sporting-goods tax includes a great many articles, not only sporting goods proper, but clothes and uniforms and things of that nature. It is very short. To get an idea, I will read what is in the existing law:

> Tennis rackets, tennis-racket frames and strings, nets, racket covers and presses, skates, snow shoes, ski, toboggans, canoe paddles, polo mallets, baseball bats, gloves, masks, protectors, shoes and uniforms, football helmets, clubs, lacrosse sticks, balls of all kinds, including baseballs, footballs, tennis, golf, lacrosse, billiard, and pool balls, fishing rods and reels, billiard and pool tables, chess and checker boards and pieces, dice, games, and parts of games (except playing cards and children's toys and games), and all similar articles commonly or commercially known as sporting goods.

Mr. Curtis makes the claim that clothing should come out, and that baseballs and footballs which are used by the youth of the country shall not be taxed.

Senator KING. Why?

Mr. PARKER. His argument is that, for instance, a State or a city or a county school can buy baseball uniforms and can buy baseball gloves, and all of that, if the school does it as a municipal matter. They of course are exempt from tax, but all private schools and religious schools and what not have to pay it.

Senator LA FOLLETTE. There may be some merit in it, but I make the point of order that it falls under the category which the committee said that it would not consider.

Senator KING. As many as favor the motion will say "aye"; those opposed, "no."

(The vote is taken, after which Senator King announced that the "noes" have it.)

Senator LONERGAN. The next is the case of Mr. Arthur M. Marsh, a Bridgeport lawyer.

Mr. PARKER. This is an amendment proposing a change in the estate-tax law. The decedent dies and leaves certain trust funds.

Under existing law, the widow can receive income from that trust if it is drawn up in a certain way. She does not pay the tax on it, but the other beneficiaries, like the son, pay a tax, and it is a question which ought to be taxed.

Senator KING. What is the present law? Who pays the tax now?

Mr. PARKER. In this particular case that he is arguing about, the sons have to pay the tax, and the widow gets the income.

Senator LA FOLLETTE. I do not think we have the time to go into the question and decide whether the son or the widow should pay it.

Senator KING. Are you ready for the question? As many as favor the motion of the Senator from Connecticut will say "aye"; those opposed, "no."

(The vote is taken, after which Senator King announced that the noes have it.)

Senator LONERGAN. I have just one more. This is a proposition asking for the repeal of that sentence which was put in section 101 in respect to taxing corporations which reads as follows:

> And no substantial part of whose activities is participation in partisan politics or in carrying on propaganda, or otherwise attempting to influence legislation.

Mr. PARKER. That was put in the law here a couple of years ago to catch a few companies that we thought were getting funds and using those funds improperly to influence legislation. It affects other organizations. It affects an organization, for instance, like an association to prevent the employment of child labor, and it is probably catching some people that you do not want to.

I would like to hear what Mr. Kent has to say about it.

Senator KING. Would it affect those who are seeking to obtain increased pensions and increased agricultural benefits?

Mr. PARKER. It would cover almost everything. If part of the activities of an association are to influence——

Mr. KENT. We are having some very difficult cases to arise under that section. Propaganda is one of these polemic terms which is used as one of the things you do not like to use yourself, and it is almost impossible to set up any precise standards that would get the cases that one would like to get and should be gotten, that won't sweep in a lot of cases that should not be included. The most troublesome kind of a case that we are having is that there have been several foundations set up in the country for the purpose of making factual studies, and on the basis of those studies presenting to legislatures resolutions and making recommendations as to legislation.

Senator CLARK. And some of those foundations have spent great sums of money in trying to influence the action of Congress; for instance, like the Carnegie Foundation trying to take the United States into the League of Nations. It seems to me this amendment is very properly directed to such organizations.

Mr. KENT. I am not expressing any opinion on the policy of it. In some of these cases, however, your organization or representatives of the organization will be called before a committee and will present the results of their studies, and maybe asked, or the study itself may lead up to some conclusions as to ways and means oftentimes involving legislation, in which the problems there studied can be corrected. Of course, the moment they undertake to make recommendations to a legislative or congressional committee, they are in point of fact

attempting to influence legislation, at least to us it is difficult to administer the statute on any other basis.

Senator COUZENS. Do you have any difficulty with any child-welfare organizations? I understand that there is one in New York that has been ruled taxable under this provision of the law, and it does seem to me that there ought to be some possible language which would exclude those dealing directly with child welfare. I do not see how an organization, a nonprofit organization devoted entirely to the welfare of children, should necessarily be called a lobbying organization because they desire legislation which will protect the child.

Mr. KENT. I am not acquainted with the specific case, but I should not be surprised, Senator Couzens, if that were true.

Senator METCALF. I have a letter from a child-labor organization which has been in existence for a long time in Providence, and they were wondering if they came under it. I do not think they have any money that can be taxed.

Senator KING. Suppose there is an organization, as there is I am told, which is doing all it can to propagate atheism. While I am very much opposed to atheism, I do not think it is any of my business if a dozen of you get together and form an organization to propagate that, or agnosticism or any other form of religious belief. It is not any of my business.

Senator LA FOLLETTE. This is a question, as I understand, of the exemption from tax.

Senator CLARK. That is absolutely true. It is not trying to prohibit anybody from getting together in any sort of an organization they please, but it is well known to all of us that some of these organizations have officers who receive very handsome salaries and they spend a great deal on overhead. This is a question whether we shall exempt them from a tax. It is not an attempt to prevent them from doing anything that they want.

Senator BARKLEY. Contributions are made to these organizations by people who deduct them from their income tax.

Mr. KENT. That is where the shoe pinches, because most of these organizations will not themselves show any profit and there is no profit being realized from their operations. They can file an income-tax return and it would be probably in most instances a nontaxable return, but in order for contributors to the organization to get a deduction from their income returns for such contributions, it must be an organization that qualifies for exemption under section 1016, I believe, under the statute, and of course this qualifying phrase appears in that section of the statute.

Senator COUZENS. I have here an amendment which would include with the others, the cases of legislation directed specifically to the care or protection of children, or legislation relating to the treatment of prisoners, the sick, the aged, or other unfortunate dependent or delinquent persons. I do not know whether that is too broad, but they do have in there the point I particularly raised, the point with reference to the protection of children. I think in those cases contributions ought to be exempted.

Senator CLARK. On the aim directed to the improvement of industrial conditions, the du Ponts, for instance, could come in and make a very moving plea to the Treasury Department that the American

Liberty League was, according to their view, directed to the improvement of industrial conditions, and exempt the contributions. According to the viewpoints of those particular gentlemen, it would be so, I take it. A great many of us would very violently, I assume, differ with them in that conclusion, and it seems to me almost impossible to draw an exemption as far as the few organizations that are really devoted to the abolition of child labor and conditions of that sort—I do not think there are any of us that would not be glad to exempt them. The tax on them would be very small and we are likely to leave a loophole that all of the propaganda organizations in the country can go right through it.

Senator COUZENS. May I suggest to leave off the language relating to organizations looking to the improvement of industrial conditions. I offer that as an amendment; I do not think it should be included. All that this proposal does is to permit the contributions to these organizations to be deducted from their income tax.

Senator KING. Is the amendment in concrete form?

Senator LONERGAN. Will your amendment cover the whole thing, Senator?

Senator COUZENS. No. I say that labor is too controversial. This amendment would include, with the others, the cases of legislation directed specifically to the care or protection of children, or legislation relating to the treatment of prisoners, the sick, the aged, or other unfortunate dependent or delinquent persons. Of course, that would carry with it the last provision of the act which points out that there is to be no profit to anybody in connection with these organizations.

Senator KING. Those in favor of the amendment will say "aye"; those opposed "no".

(The vote is taken, after which Senator King announced that the amendment was carried.)

Mr. BEAMAN. If that is carried, I have some questions to ask. Do you want that to apply to all of the five or six places in the law, or just the one that Senator Lonergan mentioned?

Senator KING. We are advised by one of the experts here that the amendment in one place does not do any good; it must be half a dozen places.

Mr. BEAMAN. The important place is in the place where it gives the individual a deduction for contributions made. It is also in the estate tax and in the gift tax sections, and also in other places. I suppose you want it in all of those places?

Senator CLARK. What was the last vote? I did not understand that it had been carried.

Senator KING. It was carried.

Senator COUZENS. Let us have the vote over again.

Senator KING. Those in favor will signify by saying "aye"; those opposed, "no."

(The vote is taken, whereupon Senator King announced that the noes have it and the amendment was rejected.)

(At the request of Senator Lonergan, the following documents in connection with the amendments proposed by him are made a part of the record:)

MEMORANDUM RE MUTUAL SAVINGS BANKS

1. How does the act operate on mutual savings banks? That is to say, does the act place a burden upon mutual savings banks which heretofore did not exist?

2. The tax on undistributed income is based on the theory that such income could have been and should be distributed by way of dividends to stockholders. However, "bank holding companies" may be required by regulatory supervising public authorities to refrain from distributing income for the purpose of building reserves to absorb losses in one or more of the affiliate banks. This situation is different from the usual corporation situation which is withholding income in that it is being held on account of statutory provisions or by direction of public supervising authorities. The public has an interest in requiring or directing that such income be withheld. There is attached hereto a suggested amendment which will cover this situation and also a supporting statement which sets forth the arguments in detail for the amendment.

3. The House bill purports to impose a tax on the full amount of dividends received by corporations including "bank holding companies." My understanding is that the position of the Finance Committee is to strike out the effect of the House bill in this respect. A "bank holding company" is merely an agency or conduit through which dividends from the affiliate banks are paid to the persons entitled to the same.

The tax on this agency or conduit results in a double taxation of bank dividends from the viewpoint of the stockholders in the "bank holding company". Heretofore it has been a long-established principle of taxation not to impose a tax on dividends received on the theory that the tax has already been paid from the corporation's earnings. In the Revenue Act of 1935 this principle was slightly modified in that 10 percent of such dividends received by corporations became subject to taxation. The universally accepted principle of avoiding double taxation should be adhered to and no further encroachments upon this principle should be countenanced. The House bill completely ignores this principle that double taxation should be avoided. Unless the Senate Finance Committee's position in this respect is insisted upon in the conference, there will be established the obnoxious principle of double taxation for the same income. This would have a serious weakening effect upon the banking structure for the reason that "bank holding companies" represent more than 10 percent of the entire banking system of the country.

SUGGESTED AMENDMENT

"That such part of the net income of any 'holding company affiliate' of a member bank of the Federal Reserve System as defined by Section 2 of the Banking Act of 1933 (U.S.C., Title 12, Section 221a) shall be rated as distributed income, (1) which such affiliate retains and invests in readily marketable assets in compliance with, or in anticipation of compliance with, the provisions of Section 5144 of the Revised Statutes (U. S. C., Title 12, Section 61) or (2) which such affiliate by direction or under the advice of the Board of Governors of the Federal Reserve System, the Comptroller of the Currency or the Federal Deposit Insurance Corporation, so invests, retains, or contributes towards the strengthening of the capital structure of any affiliated bank, (3) which such affiliate retains as required by agreement with the Reconstruction Finance Corporation restricting the dividends of such affiliate."

It would seem that this amendment might properly be incorporated in section 26 of the bill, "Credits of corporations against net income", in section 27,"Corporation for dividends paid", or by the addition of a new section.

IN RE [H. R. 12395]: SECTIONS 26 OR 27 CONFLICT WITH BANKING ACTS RELATIVE TO HOLDING COMPANIES

Under the bill there is treated as undistributed income subject to tax, income which bank holding companies are required to retain, either by Federal law, by Federal supervisory and regulatory authorities acting pursuant to law, or by agreements made with the Reconstruction Finance Corporation. This treatment defeats the purpose of the statutory and regulatory provisions.

For the reasons hereinafter set forth, this purpose would be better served if the part of the net income of bank holding companies which cannot be distributed by reason of these requirements were treated as distributed income.

There are in the United States approximately 100 bank holding companies, whose affiliated banks have approximately $5,000,000,000 in deposits. They are located principally in the South, in Florida, Georgia, and Tennessee, on the Pacific coast, in the Northwest, centering about Minneapolis and St. Paul, in the Central West, in Wisconsin and Ohio, and also in Utah, New York, and Massachusetts.

The Banking Act of 1933 dealt with bank holding companies principally in three respects. (See section 19, revising section 5144 of the Revised Statutes.)

(1) By requiring them to build up reserves of readily marketable assets and limiting the payment of dividends by them to 6 percent per annum while such readily marketable assets are below specified amounts.

These reserves were intended to be used for three purposes:

(*a*) To replace capital in affiliated banks;

(*b*) To pay losses incurred in such banks;

(*c*) To meet individual liability imposed on any shares of stock held by the holding company.

Actual experience has shown that it has been necessary for these holding companies in many cases to save their affiliated banks by contributing funds to them for new capital, taking out losses, etc. In some cases where the assets of holding companies were practically exhausted by these contributions, they have borrowed from the Reconstruction Finance Corporation to secure the necessary funds to protect the depositors of these affiliated banks.

(2) By providing that holding companies cannot vote the stock owned by them in member banks without first obtaining voting permits from the Board of Governors of the Federal Reserve System.

The issuance of such voting permits is conditional upon agreements made with the Federal Reserve Board, which provide for examinations by the Comptroller, the Federal Reserve Board and compliance by the holding companies and their affiliated banks with recommendations made following such examinations.

The result is that under such agreements, said supervisory authorities can, in practical effect, prevent the distribution of income by the holding companies to their stockholders.

(3) By providing for the purchase by the Reconstruction Finance Corporation of preferred stock of the banks themselves and loans by the Reconstruction Finance Corporation to be holding companies, under agreements between such banks or companies and the Reconstruction Finance Corporation.

Unless such part of the net income of holding companies as cannot be distributed by reason of these statutory and regulatory provisions under existing Federal laws is treated as distributed income, bank holding companies will find themselves in this position: Their affiliated banks will have paid the 18-percent tax, the holding companies will pay a tax on the bank dividends received by them to the extent the same are not distributed (which may make the holding companies liable for 7 percent on the very reserves which the Federal law requires them to set up) and thus the very purpose of the banking acts and what Federal supervisory authorities are seeking to accomplish under such acts will be defeated.

To avoid this result under the new tax bill, and in fairness and justice to the bank holding companies which otherwise would have to pay a tax on undistributed income on the theory that it could be distributed by way of dividends to their stockholders, but which in fact by law they cannot so distribute, the following amendment is suggested:

"That such part of the net income of any 'holding company affiliate' of a member bank of the Federal Reserve System as defined by section 2 of the Banking Act of 1933 (U. S. C., title 12, sec. 221a), shall be treated as distributed income, (1) which such affiliate retains and invests in readily marketable assets in compliance with, or in anticipation of compliance with, the provisions of section 5144 of the Revised Statutes (U. S. C., title 12, sec. 61) or (2) which such affiliate by direction or under the advice of the Board of Governors of the Federal Reserve System, the Comptroller of the Currency or the Federal Deposit Insurance Corporation, so invests, retains, or contributes toward the strengthening of the capital structure of any affiliated bank, (3) which such affiliate retains as required by agreement with the Reconstruction Finance Corporation restricting the dividends of such affiliate."

It would seem that this amendment might properly be incorporated in section 26 of the bill ("Credits of corporations against net icome," in sec. 27), "Corporation credit for dividends paid", or by the addition of a new section.

Income Taxation on Trustees and Beneficiaries of Trust Funds

(Memorandum submitted to Senator Augustine Lonergan of the Finance Committee, United States Senate, April 9, 1936)

OBJECT OF THIS PROPOSAL

The purpose is to make sure, by a slight amendment of section 162 of the Revenue Act of 1934 (suggested form below), that recipients of income bear their own income taxes.

Section 162 does not now cover a certain class of cases, generally involving the widow beneficiary of a testator, but equally applicable whether widow, son, daughter, or a stranger.

The Government in these cases loses revenue, and the tax becomes payable out of the trust fund itself, not out of the person receiving the income.

The loss of revenue is explained below.

GROUNDS FOR PROPOSED AMENDMENT

As the revenue act and the court decisions now stand, it appears that in this certain class of cases income is received from trust funds, and will continue to be so received, by beneficiaries who nevertheless escape income taxation thereon.

This is the class in which a testator creates a trust fund and gives to a legatee a fixed annual amount to be paid out of the income of the fund, but adds the provision that in case the income shall fall short of that amount, the deficit shall be made up out of the capital.

This last provision causes the trouble. The second circuit, in (*Mrs.*) *Eva F. Warner* v. *Commissioner* (66 Fed. (2d) 403) has decided that the beneficiary goes free of income taxation, though receiving, out of income, $50,000 per year. Certiorari was refused by the Supreme Court.

Meanwhile the Board of Tax Appeals has decided that the trustee for Mrs. Warner must pay income tax on the income distributed to her (*Bridgeport-City Trust Co., trustee* v. *Commissioner*, 32 B. T. A. 1181 (now on appeal)). This is a grossly unjust result. The trustee, if so taxable, must pay the tax either out of the surplus income of the trust fund, or out of the capital. Both the surplus income and the capital belong to other members of the family. Why should they bear the tax on Mrs. Warner's income?

Similar and related litigation is going on in various courts throughout the country.

LOSS OF REVENUE TO GOVERNMENT

This loss may occur in two ways:

(1) Since section 162 in its present form (and it was the same in preceding revenue acts) is ambiguous, or fails to hit the above situation, the Internal Revenue Bureau has in many cases assessed the wrong person and the statute of limitations has run. This may occur again.

(2) The recipients of such income usually have other income, and if income from the trust fund should be added, as it ought, the beneficiary's income would be raised into higher brackets. If, on the other hand, such taxation is to fall on the trustee, the latter would be a separate tax entity; the income so distributed, having nothing to be added to it, would remain in a lower bracket, and would pay at the corresponding lower rate.

This condition would run for years in many cases, because such trusts usually last for the life of the beneficiary.

FORM OF AMENDMENT

The following amendment of section 162 is suggested to cure the above injustices and doubts:

Revenue Act of 1934: Add to section 162 a new subsection (d):

"(d) The deduction allowed by subsection (b) of this section shall apply to income distributed or distributable to any beneficiary by direction of any will or deed of trust, whether or not the beneficiary is entitled to a fixed amount per annum and whether or not said fixed amount is required to be paid out of capital in default of sufficient income, such deduction to be allowed only to the extent of income so distributed or distributable, and the amount so allowed as a deduction to be included in computing the net income of the beneficiary."

THIS AMENDMENT DESERVES ACTION

This amendment, during the past year or two, has been duly studied. It has been discussed with Senator Harrison somewhat and with Senator Walcott while he was in office, also with Messrs. Hill and Treadway of the Ways and Means Committee and with several representatives of the Treasury and Internal Revenue Bureau, including Mr. B. H. Bartholow, Mr. Ralph D. Brown, Professor Magill, and others. Mr. L. H. Parker, of your joint committee staff is especially familiar with it. The injustice done to taxpayers and the loss of revenue have been recognized, but the multitude of other revenue questions has prevented action

It now becomes of greater importance with higher rates of tax and with dividends becoming subject to normal tax.

COURT DECISIONS

The pertinent decisions and others are analyzed and quoted in a memorandum dated October 22, 1934, and then submitted to Mr. L. H. Parker. A copy will be furnished if you so desire.

Following is a very brief summary:

If the bill contains an unqualified gift of, say, $50,000 per year payable annually, or in other words, a pure annuity, chargeable against the entire estate like an ordinary legacy, the petitioner trustee would not be entitled to deduct it as against income received, even though, during any particular year, it had paid the annuity out of income. This is because it would have been a gift of capital, like an ordinary legacy. (*Burnet* v. *Whitehouse*, 283 U. S. 148; *Helvering* v. *Pardee*, 290 U. S. 370.)

If, on the other hand, the gift by will is the entire income of a particular fund, even though the capital is bequeathed to others, the beneficiary would pay the tax and the estate or trust would be free of it (*Irwin* v. *Gavit*, 268 U. S. 161; *Helvering* v. *Butterworth*, 290 U. S. 365).

Coming closer to the present question, if the testator gives, say, $50,000 per year for life to his widow and adds to this annuity authority to his executors or trustees to either (1) buy an annuity for her, or (2) set aside securities from his estate sufficient to provide $50,000 per year in income, and the latter course is elected by them, the beneficiary would be liable to the tax, and the estate or trust entitled to deduct the payment to her, as against income received from such fund (*Heiner* v. *Beatly*, 17 Fed. (2d) 743, affirmed 276 U. S. 598, by the Supreme Court "on authority of *Irwin* v. *Gavit*", *supra*).

But if the testator, instead of authorizing his executors to set up such a fund, establishes the fund himself by a specific list of securities in his will, and makes a gift to the legatee of a fixed sum per annum payable out of the income of that particular fund, exactly as in *Heiner* v. *Beatly*, *supra*, but makes deficit in income chargeable to capital, difficulty arises. In *Irwin* v. *Gavit*, *supra*, the beneficiary's income from the fund was, to be sure, an indeterminate amount while in the *Beatly case* it was a fixed sum. Both cases, nevertheless, decided that the beneficiary was the person to be taxed. This demonstrates that the ground was that in both it was a gift of income.

In *Irwin* v. *Gavit*, *supra*, in which the petitioner received surplus income from a fund but had no other title or interest in the corpus, the court said:

"The money was income in the hands of the trustees and we know of nothing in the law that prevented its being paid and received as income by the donee."

Nevertheless, *Warner* v. *Commissioner*, *supra*, exempts the beneficiary purely on the ground that since the $50,000 may become payable out of capital, the gift is the same as an unqualified annuity, and by implication the trustee would have to bear the tax (that is, charge it to other members of the family who own the capital and surplus income of the fund. The Board of Tax Appeals has ruled likewise, and since the Supreme Court has refused to review the *Warner case*, legislation seems necessary to cure this unfair and unfortunate situation.

Both the capital and the surplus income belong to other members of the family and it would seem unconstitutional for that reason to take the tax out of them (*Hoeper* v. *Tax Commissioner*, 284 U. S. 206). That which is not due process of law under the fourteenth amendment is equally not due process under the fifth.

This argument may perhaps beg the question, but there can be no doubt that the result shocks the conscience. It is clearly unfair that when specific income is collected, held, administered and distributed, as such, to a recipient beneficiary

the latter should nevertheless be able to shift her income tax to the shoulders of others who derive no benefit from it.

Respectfully submitted.

ARTHUR M. MARSH.

BRIDGEPORT, CONN.

CONNECTICUT FEDERATION OF LABOR,
May 13, 1936.

Hon. AUGUSTINE LONERGAN,
Washington, D. C.

DEAR SIR: I am writing you in regard to the the United States revenue bill of 1934. An amendment has been introduced which adds to the usual wording of section 101, paragraph 6 of this bill specifying certain types of organizations' contributions which were exempt from the Federal income tax, the following clause:

"and no substantial part of whose activities is participation in partisan politics or in carrying on propaganda, or otherwise attempting to influence legislation."

The effect of this clause is to penalize organizations engaged in legitimate work for the protection or welfare of children if they attempt to influence legislation, and this will do much harm to many of our organization that are engaged in trying to secure the passage of proper legislation.

Such organizations as the National Probation Association, the Child Welfare League of America and the National Child Labor Committee and others will suffer as a result of this clause, and every means should be taken to see that this clause is taken out of the 1936 bill.

I understand that this bill is now before the Senate Finance Committee of which you are a member. I urge that you do everything you can to see that this clause is eliminated so that these organizations will not be hindered in their work to secure social and other legislation beneficial to the working people and the masses in this country.

Sincerely yours,

JOHN J. EGAN,
Secretary-Treasurer, Connecticut Federation of Labor.

Senator BYRD. I have been asked to present an amendment—I have no interest in it at all, but it seems to me it is to correct an injustice. As I understand it, the law now is that these leased wires that transmit news to the newspapers are not taxed, but the leased wires whereby a radio station transmits its news to stations over the country is taxed. Mr. Parker has gone into it, and a man named Digges appeared before the committee. I am a newspaperman, and naturally there is competition between the two, but it seems to be unjust where the wires are used exclusively for the transmission of news, to give relief to newspapers and then tax the radio.

Senator LA FOLLETTE. Then let us tax the newspapers.

Senator KING. Do you offer an amendment, Senator?

Senator BYRD. I would like Mr. Parker to explain it. This present bill does not exempt the newspapers. It is the same old law.

Mr. PARKER. In the 1932 act, we put a tax on telegraph messages, telephone messages, radio messages, and a tax on leased wires. The rate of tax varied a little; it ran from 5 to 10 percent on the average.

In subdivision (b) of that particular section, they exempt from tax the messages or the leased wire tax which would otherwise be payable in a case of the messages sent in the dissemination of news by the public press.

This amendment does not by any means propose to exempt all radio broadcasting profits or anything like that; it simply proposes to take off in the case of two or three companies that have gone into business since the 1932 act—this business was not in existence at that time—these companies which give you daily news bulletins over

the radio. They have leased wires, and they have a central place for collecting the news, perhaps, and they send these messages out to the various broadcasting stations, and they get paid for that service and they have to pay a tax on it.

I understand that the total tax of these two or three companies does not exceed $25,000 a year. At present it is a small business and not an exceptionally profitable one. It is a matter of whether or not you want to put them on a consistent basis with the newspaper.

Senator CLARK. What would be the result if instead of taking the tax off radio, you put it on the leased wires? We can be consistent that way just the same as the other way.

Mr. PARKER. I would say we would probably pick up $250,000 at least instead of losing $25,000. I think that is very conservative.

Senator CLARK. I propose that as a substitute, Mr. Chairman.

Senator BARKLEY. What is the amendment?

Mr. PARKER. The amendment is to insert after certain words "where the word public press is used", they propose to insert "or for radio broadcasting stations." And that the words "or by radio" be inserted after the words "the dissemination of news through the public press."

Senator KING. As many as favor the motion will say "aye"; those opposed "no."

(The vote is taken, after which Senator King announced that the noes have it and the amendment is rejected.)

Senator KING. Mr. O'Brien, will you please explain this amendment offered by Senator Wagner?

(The amendment proposed is as follows:)

[H. R 12395, 74th Cong. 2d sess.]

AMENDMENTS Intended to be proposed by Mr. WAGNER to the bill (H. R. 12395) to provide revenue; equalize taxation, and for other purposes, viz:

On page 3, in the table of contents, strike out the following: "Sec. 120. Unlimited deduction for charitable and other contributions."; and strike out "Sec. 121." and in lieu thereof insert "Sec. 120.".

On page 40, line 16, strike out "animals;" and insert "animals.".

On page 40, lines 17 to 19, strike out the following: "to an amount which in all the above cases combined does not exceed 15 per centum of the taxpayer's net income as computed without the benefit of this subsection."

On page 40, lines 22 to 24, strike out the following: "(For unlimited deduction if contributions and gifts exceed 90 per centum of the net income, see section 120.)"

On page 42, lines 13 to 15, strike out the following: "; to an amount which does not exceed 5 per centum of the taxpayer's net income as computed without the benefit of this subsection."

On page 42, line 20, strike out "section 121" and in lieu thereof insert "section 120".

On page 127, beginning with line 16, strike out down to and including line 2 on page 128.

On page 128, line 3, strike out "Sec. 121" and in lieu thereof insert "Sec. 120".

Mr. O'BRIEN. Senator Wagner's amendment proposes to eliminate that part of the provision of the present law which relates to the deduction for charitable purposes which limits that deduction to 15 percent of the taxpayer's net income in the case of an individual, and to 5 percent of the taxpayer's net income in the case of a corporation; in other words, what he wants to do is this, to permit the corporation or an individual to take the entire amount of his charitable deduction and make a deduction against his net income.

Senator KING. As many as favor the amendment offered by Senator Wagner say "aye"; opposed "no".

(The amendment was rejected.)

Senator KING. Senator McNary has offered the following amendment.

(The amendment is as follows:)

[H. R. ——, 74th Cong., 2d sess.]

AMENDMENT Intended to be proposed by Mr. MCNARY to the Revenue bill of 1936 (H. R. ——), viz: At the proper place insert the following new section:

SEC. —. Effective only in the case of taxable years beginning after December 31, 1935, paragraph (1) of section 25 (b) of the Revenue Act of 1934, as amended, is amended to read as follows:

"(1) *Personal exemption.*—In the case of a single person, a personal exemption of $1,000; or in the case of the head of a family or a married person living with husband or wife or a married person not living with husband or wife but who actually supports and maintains such husband or wife, a personal exemption of $2,500. A husband and wife living together or a husband and wife not living together but one of whom is actually supported and maintained by the other, shall receive but one personal exemption. The amount of such personal exemption shall be $2,500. If such husband and wife make separate returns, the personal exemption may be taken by either or divided between them."

Mr. O'BRIEN. The effect of that amendment is to permit a married man's personal exemption not only in the case in which the husband and wife are living together, but also the case in which they are living apart but one is supporting the other.

Senator KING. As many as favor the amendment will say "aye"; those opposed, "no".

(The amendment is rejected.)

Senator KING. Yesterday John W. Haussermann's clarifying amendment to section 251 was postponed for consideration until today. Who will explain it?

Mr. BEAMAN. It was postponed with the idea that we would look at it and make a recommendation and report. We have not yet considered it because we have been considering these other things.

Senator KING. You are not ready to report?

Mr. BEAMAN. No.

Senator KING. Please do so tomorrow.

Senator CLARK. What is it about?

Mr. BEAMAN. I can explain it to you. Section 251 of the bill provides that a domestic corporation or an individual citizen of the United States, if he derives 50 percent of his income from the active conduct of a trade or business in a possession, then you seek to inquire if having thus qualified, if he derived more than 80 percent of his income from sources within a possession, and if you find the second and the first both, then he is taxable only on his income on sources within the United States just like a nonresident alien.

This man says that for the purpose of determining whether 50 percent of his income shall come from sources from the active conduct of a trade or business in a possession, you ought to include the amount of dividends he receives from a corporation if he is running the corporation—or something or other, I don't know just what—and that is what we have not had the time to look into. He says if he is working for the corporation, if he is devoting 100 percent of his time to running the corporation and then he gets a dividend, you might

say that the dividends just as much as his salary are derived from the active conduct of the business.

Senator KING. Dividends from the same corporation?

Mr. BEAMAN. Yes. If he is devoting 2 weeks out of every year to it, the query is, Where are you going to draw the line? Or, if you can draw a line?

Senator GERRY. Is that not the case of where the individual who is doing business in the Puilippines does not have to pay, he is exempt from the tax, but if it is a corporation he pays the tax?

Mr. BEAMAN. The corporation does not.

Senator GERRY. But he pays if it if he gets it from dividends, and he does not if it is an individual.

Senator KING. Mr. Kent, have you any views on that?

Mr. KENT. I have not anything in addition to what Mr. Beaman has stated. There may be some element of quota involved there, but the problem is one of devising the limitation.

Mr. BEAMAN. It is complicated by the fact that supposing he does get some dividends, you cannot take it that the day that he receives the dividends he happens to be running the corporation.

Senator KING. It is the view of the Chair that the matter, if any Senator desires to offer it on the floor, may do so.

Senator LA FOLLETTE. Let us vote on it now.

Senator KING. We do not know enough about it.

Senator BARKLEY. I move that the amendment be postponed indefinitely.

Senator LA FOLLETTE. I second the motion.

Senator KING. Those in favor, aye; those opposed, no.

(The motion was agreed to.)

Senator CLARK. Mr. Chairman, in connection with the amendment proposed by Senator McNary and which we voted down, I move to reconsider that. As I understand the purport of it now, it seems to me to be a very sensible amendment.

Senator KING. The Chair announces that by unanimous consent it will be reconsidered and reported. Mr. O'Brien, will you make a statement on it, please?

Mr. O'BRIEN. The proposed amendment provides that in the case of a single person, a personal exemption of $1,000, or in the case of the head of a family or a married person living with a husband or a wife, or a married person not living with a husband or a wife, but who actually supports and maintains such husband or wife, a personal exemption of $2,500. That a husband and wife living together, or a husband and wife not living together but one of whom is actually supported and maintained by the other, shall receive but one personal exemption and the amount of such personal exemption shall be $2,500. If such husband and wife make separate returns, the exemption may be taken by either or divided between them.

Senator CLARK. I am frank to say that I do not see why a man who is supporting his wife, even though they are not living together, should not have the same exemption.

Senator KING. Is there not some difficulty there in ascertaining whether he is supporting her? Does it involve a good deal of administrative matter?

Senator COUZENS. If you put that in, you should put in the single man supporting his mother and father.

Senator KING. Are you ready to vote on the question?

Mr. KENT. I would like to call attention to one perhaps minor difficulty, but the last clause of this section provides that if such husband and wife make separate returns, the exemption may be divided between them.

Senator METCALF. That is what the present law is now.

Mr. O'BRIEN. With respect to that, there is no change.

Senator KING. As many as favor the amendment will say aye; those opposed no.

(The amendment is rejected.)

Senator KING. Senator Pope desires to bring up this amendment to section 604 and section 608 of the Revenue Act of 1932, as amended, that those sections are hereby repealed and the following substituted—

that there is hereby imposed upon the following articles sold by the manufacturer, producer, or importer a tax equivalent to 3 percent of the price for which so sold, articles made of fur and the hides or pelt of which any such fur is the component material or chief value.

Senator LA FOLLETTE. As I understand it, and I would like to know from Mr. Kent if that is correct, I understand that there has been a great deal of difficulty in administering this fur-tax business. It has been very difficult for the industry and very difficult for the Treasury, and as I understand it, this is not any proposition to take the tax off, but it is a proposition to state the section in a more workable form. Is that correct?

Mr. TURNEY. It reduces the rate and eliminates the exemption of $72.

Senator CLARK. As a matter of fact, it costs almost as much to collect this fur tax as it brings in in revenue, does it not?

Mr. KENT. Yes, sir. Any exemption that is imposed in that fashion would be likely to create the same difficulty. You see, it is exempted in the wholesale price if it is not over $75. If it is $75.01, the rate applies not merely to the excess over $75, but to the entire amount. The result has been that it has operated to put a wholly artificial pressure upon prices, and all sorts of schemes have been resorted to to take advantage of the exemption. For instance, you have a fur coat that formerly wholesaled for $125 and a muff that went with it for $25. What they will do now is to bill the coat at $74.50 and the muff at $74.50, everybody getting out from any tax unless our agents succeed in checking the thing up and soaking them.

Senator LA FOLLETTE. This proposes to take the exemption out.

Mr. KENT. And a flat 3-percent rate straight through. It is estimated I think that the 3-percent tax would yield as much.

Senator GERRY. What is the tax now?

Mr. KENT. Five.

Senator KING. The secretary advises me that a number of people from New York want to be heard. They are opposing the amendment which has been offered by Senator Pope.

Senator BARKLEY. Mr. Chairman, if this amendment or similar amendments are adopted here, it embarrasses a great many of us who have told people interested in other things that these matters are not going to be taken up. I have refrained from offering amendments of this sort, because I thought we were not going to go into it. If you are going to adopt this changing the basis of the presnt excise tax, how can I excuse myself for not offering some amendments on things that other people are asking me to offer?

Mr. KENT. I may say, Senator, that I am not appearing in advocacy of this proposal. If it had been proposed to open up the field of excise taxation at this time, I think the Department would have had a recommendation to make of its own with respect to this situtión, because of its administrative features, but, of course, when we were asked to report upon a specific bill, naturally the Department stated its view.

Senator BARKLEY. I understand that.

Senator KING. Mr. Kent, may I ask this question? Suppose we continue the present law, can you not fairly administer it and meet the situation in a reasonably fair way to dispose of it all?

Senator LA FOLLETTE. The difficulty is with this exemption of $75. You can see how many different ways there are to get around that.

Mr. KENT. You would have the same situation if you exempted from the manufacturers' excise tax on automobiles all automobiles selling at the factory at a price of under $500 or $600.

Senator LA FOLLETTE. Every manufacturer that could possibly do it would try to get under it by selling you half a car now and half a car at another time.

Senator COUZENS. I think this is a good amendment, because it really does not affect the excise tax to the extent of Government revenue.

Senator KING. We have another suggestion to modify the excise taxes on jewelry of all kinds.

Gentlemen, are you ready to vote on this proposed amendment?

Senator METCALF. Does it not make it simpler for them to do business, and does it not make it simpler for you to put this in?

Mr. KENT. That is the representation that has been made by many people in the fur trade.

Senator METCALF. I am inclined to think it is a good thing.

Senator KING. There are demands to be heard by opponents of the amendment if we propose to legislate.

Senator METCALF. We have not the time, and I think it should be left to our judgment.

Senator KING. I do not know enough about it without a hearing. Are you ready for the question? As many as favor the motion will say "Aye"; those opposed "No."

(The amendment is rejected.)

Senator KING. Senator Schwellenbach offers the following amendment:

[H. R. 12395, 74th Cong., 2d sess.]

Amendment intended to be proposed by Mr. SCHWELLENBACH to the bill (H. R. 12395) to provide revenue, equalize taxation, and for other purposes, viz: On page 219, between lines 7 and 8, insert the following new title:

TITLE II—MANUFACTURERS' EXCISE TAXES

SEC. 401. TAX ON JEWELRY, ETC.

Effective fifteen days after the date of the enactment of this Act, section 605 of the Revenue Act of 1932, as amended, is amended by adding at the end thereof the following new sentence: "If the vendee of the manufacturer, producer, or importer uses any article enumerated in this section as material in the manufacture or production of, or for use as a component part of, any article to be manufactured or produced by the vendee, then for the purposes of this title the vendee shall not be considered the manufacturer or producer of any such article or articles, but no credit or refund shall be allowed or made to the vendee under section 621, as amended."

SEC. 402. TAX-FREE SALES.

Effective fifteen days after the date of the enactment of this Act, the last sentence of section 620 of the Revenue Act of 1932, as amended, is amended to read as follows: "The provisions of paragraphs (1) and (2) shall not apply with respect to tires or inner tubes or articles enumerated in sections 604 and 605 relating to the tax on furs and jewelry."

Have you anything to say, Mr. Kent, on that?

Mr. KENT. I am not acquainted with it.

Senator KING. I understand from the clerk it just came in this morning.

As many as favor the adoption of the amendment will say "aye;" those opposed, "no."

(The amendment is rejected.)

Senator METCALF. There is a case in regard to these investment corporations that seems to work great harm and would almost put them out of business, and Senator Walsh has asked them to get up an amendment to cover that, and as he is not here, I want to ask that it be put in in the morning.

Senator KING. Very well. Have you any administrative matters, Mr. Parker?

Mr. PARKER. Here is something from Senator Hayden.

Senator KING. Will you explain it?

Mr. PARKER. Senator Hayden asked for an amendment to section 101, adding a new paragraph exempting "corporations operating reclamation projects under contract with the United States."

In existing law, on one of the exemption provisions, there is already an exemption for ditch and irrigation companies 85 percent of whose income is used to pay expenses and losses. It appears that this company does not come in that category, and they point out that they have a contract with the United States to build certain dams and they point out that all of this property belongs to the United States.

I will quote one line from their letter:

I am enclosing these Budget estimates to show what seems to be the absurd position of the association paying income tax and at the same time having to levy an assessment.

This is the Salt River Valley Water Users Association of Phoenix, Ariz.

Senator LA FOLLETTE. Have you looked into it?

Mr. PARKER. I have not had time to look into it.

Senator LA FOLLETTE. This one company may have a very good case, but there may be thousands of them, for all we know. We ought to know what we are doing before we do anything about that.

Senator COUZENS. Let Senator Hayden bring it up on the floor.

Senator KING. Without objection, such procedure will be suggested.

Senator COUZENS. May I ask if you have made the subcommittee's report on sugar?

Senator KING. The subcommittee, consisting of Senator Couzens, Senator George, and myself, had hearings this morning, and a number of witnesses testified, all of whom as I recall, stated in substance they were not in favor of the tax unless there should be legislation with respect to the quotas, that the two synchronized and so integrated that one without the other would not bring about the desired results.

The committee, at least a majority of the committee, believed that it was unwise to introduce into this bill the tax features of the proposed amendment.

Senator COUZENS. May I add to that?

Senator KING. Yes.

Senator COUZENS. There also was an almost unanimous agreement that sugar itself should not be picked out alone for a processing tax; in other words, it is the most used and the cheapest commodity that we have, so far as calories is concerned, and that it is unfair to pick out a commodity so much used and the only one that, of all of the agricultural products, has not a surplus.

Senator KING. I did not quite assent to that view.

Senator COUZENS. I was just telling what the witnesses said.

Senator KING. I think the witnesses indicated that if they could get a quota, they would favor a bill if they would get benefits.

Senator LA FOLLETTE. I have no objection to voting subject to reconsideration.

Senator KING. As many as are in favor of adopting the report will say "aye"; those opposed "no."

(The report was adopted.)

Senator KING. I want to put into the record my analysis of the statement made by Mr. Seltzer in reply to the statement which we put into the record on Friday. Without objection it will be inserted in the record.

1. In my statement of yesterday I asked the Treasury experts the question as to whether they applied the effective corporation tax rate under existing law to a statutory net income of 7,200 million dollars (the amount estimated by Mr. McLeod to be the statutory net income for the calendar year 1936, p. 36 of the House Ways and Means Committee hearings) in estimating the amount of tax for 1936 under existing law, namely, 956 million dollars. They answered this question in the affirmative. I then asked the Treasury experts why they had not also followed this same method and applied an 18 percent rate to this 7,200-million-dollar base in order to estimate the revenue from a flat corporation tax of 18 percent. I pointed out that if this method was followed, we would have additional revenue of 302 million dollars as compared with their estimate of 215 million dollars, or a gain of 87 million dollars. They stated that I should have made an allowance of 6.8 percent to take care of that part of the tax which might be uncollected.

I wish to point out that such an allowance is exceptionally high and should in no case be more than 1 or 2 percent. The statutory net income of 7,200 million dollars is the amount reported by corporations on their returns. I understand that the Treasury collects about 99 percent of the tax reported by corporations on their returns. It is only when deficiencies in income tax are taken into account that the percentage of collections drops as low as 95 or 94 percent. Therefore, if we are going to reduce our estimated 1936 tax by 6.8 percent we should add to our tax base the amount by which deficiencies in income tax of corporations exceed refunds, credits and abatements in respect of that year's tax. Since this was not done, I do not feel that the Treasury has shown that their low estimate on this 18 percent flat rate is justified.

I also pointed out that both Mr. Helvering and Mr. Oliphant stated in hearings before the House Ways and Means Committee (p. 24 and p. 653, respectively, of House hearings) that if existing rates of corporate taxes were increased to 25½ percent, we could obtain the

620 million dollars permanent revenue required under the President's message. The Treasury experts attempt to qualify this statement by pointing out that it was probably made without giving any weight to the effect of such a rate upon reducing dividends distribution, and, therefore, reducing the tax liability of the individual shareholders.

I wish to point out that the record shows that this statement was made upon consultation by Mr. Helvering and Mr. Oliphant with their actuaries, and was in answer to a question as to what increase in the corporate rate would be required to produce the 620 million dollars requested by the President. This was an estimate as to additional revenue over existing law and clearly did not contemplate any reduction in taxes under existing law through lack of dividend distribution. I quote both Mr. Helvering's statement and Mr. Oliphant's statement from the House hearings:

Mr. HELVERING. The revenue-producing alternatives that might be offered in lieu of the proposed taxation of corporate incomes on the basis of withheld earnings appear to be distinctly inferior to the subcommittee's proposal as respects equity or administrative feasibility. To raise an equal sum of additional revenues through an increase in the present corporation income tax, it has been estimated that a rate approximating 25½ percent would be necessary. * * *

Mr. LAMNECK. You said that the rate to raise an equal amount of revenue would have to be 25.5 percent, if we raised revenue at the present rate. * * *

Mr. OLIPHANT. As I said to you, when you get into figures you get me beyond my depth. I am advised by the statistical staff of the Treasury Department that makes the estimates that 25.5 percent would be necessary (p. 653, House hearings).

I also pointed out that a flat corporation tax of 18 percent plus a 7-percent tax on undistributed profits should produce as much, if not more, than a flat 25.5-percent rate. This was due to the fact that the base of the 7-percent tax would be increased by intercorporate dividends which were not included in the estimate arrived at in applying the 25.5-percent rate to the statutory net income of existing law. According to Mr. McLeod (p. 56 of House hearings) there are about $1,000,000,000 in intercorporate dividends which are not taxed under existing law and which were not included in computing the revenue from the flat 25.5-percent rate. The amount of revenue to be derived from including such dividends in the tax base will more than offset any loss in revenue due to the allowance of the 18-percent tax as a deduction in computing the base subject to the 7-percent undistributed-profits tax. The Treasury estimated that the allowance of this deduction will cost $75,000,000, reducing the revenues from the 7-percent tax from $292,000,000 to $217,000,000. However, this loss will more than be made up by the enormous increase in the 7-percent tax base due to the inclusion of intercorporate dividends.

I feel assured that I am very conservative in stating that the Treasury has underestimated the revenue to be derived from the Senate Finance Committee plan by over $100,000,000.

We will recess now until tomorrow morning at 10 o'clock.

(Whereupon, at 5 p. m., the committee recessed until tomorrow, Wednesday, May 27, 1936, at 10 a. m.)

(Subsequently, the meeting was postponed until 2 p. m.)

REVENUE ACT, 1936

WEDNESDAY, MAY 27, 1936

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

The committee met in executive session, pursuant to adjournment, at 2 p. m., in the committee room, Senate Office Building, Senator William H. King presiding.

Present: Senators King (acting chairman), George Walsh, Barkley, Connally, Bailey, Clark, Byrd, Lonergan, Black, Gerry, Guffey, Couzens, La Follette, Metcalf, Hastings, and Capper.

Also present: L. H. Parker, chief of staff, Joint Committee on Internal Revenue Taxation; C. F. Stam, counsel, Joint Committee on Internal Revenue Taxation; Middleton Beaman, legislative counsel, House of Representatives; John O'Brien, assistant legislative counsel, House of Representatives; Arthur H. Kent, acting chief counsel, Bureau of Internal Revenue; C. E. Turney, assistant general counsel for the Treasury Department; W. R. Johnson, Bureau of Customs, Treasury Department; L. H. Seltzer, Assistant Director of Research and Statistics, Treasury Department.

Senator KING. The committee will be in order.

Mr. Kent, you had a matter here to present, as I recall, in regard to amending section 161.

Mr. KENT. I find that I was under a misapprehension. That amendment is not the one that I had studied. Could you defer action on that?

Senator KING. Mr. Parker, have you any technical matters or procedure matters that you desire to bring before the committee?

Mr. PARKER. There is that Mather estate matter that Senator Couzens asked for a report upon.

Senator COUZENS. I did that at the suggestion of Senator Buckley.

Senator KING. Are you ready to report on it?

Mr. PARKER. I would ask Mr. Stam to make a report on it.

Senator COUZENS. Have you anything drafted?

Mr. STAM. We have something drafted. This is what happened: This decedent, when he died—before his death he made a lot of pledges to go to charitable organizations and universities and hospitals, and so forth, and after his death, they held that those pledges constituted an enforceable obligation against the estate. There was some wrangle in the Treasury Department as to whether or not they were deductible for inheritance-tax purposes, and the estate finally decided that it was to their best interest to incorporate, because the estate did not have enough money to satisfy all of these obligations at

one time; and they thought if they incorporated, then they could take the income of the corporation and gradually pay off these obligations.

Under section 351, the personal holding company section, we allowed a deduction for debts incurred prior to January 1, 1934. These liabilities were incurred by the estate prior to January 1, 1934, but the corporation papers were not taken out until after January 1, 1934, so that the corporation really did not incur this indebtedness until after January 1, 1934, because when they took over the estate, they assumed all of the indebtedness of the estate; but the Bureau rules that the corporation, not being in existence prior to January 1, 1934, did not incur this indebtedness prior to January 1, 1934, and therefore they did not get this deduction which is allowed by section 351.

Senator KING. Was it held that it could not even be a de facto corporation?

Mr. STAM. It was not in existence; the papers were not taken out.

There were two amendments that were suggested. One amendment was to allow these deductions in full to the corporation because they had actually been incurred by the estate prior to January 1, 1934. The experts considered that and thought that that might be a little broad.

Then the other amendment provided that to the extent that the amounts of these deductions went to charitable organizations or hospitals which are exempt from taxation under the pending law, that they would be allowed the deduction. That would give the estate or the corporation partial relief, but it would not give it full relief, because some of these debts were in the form of notes held by banks and did not go to charitable institutions.

Mr. PARKER. This exemption is not to exempt them from the regular corporate tax. It is just in respect to the section 351 tax?

Mr. STAM. That is right.

Mr. PARKER. Which is an additional surtax. There is not any proposal to exempt them from the 18-percent or even the 7-percent tax.

Senator COUZENS. Have you the language of the second proposal?

Mr. STAM. I think Mr. Beaman has that.

Senator LA FOLLETTE. Can you tell us whether there are likely to be any other similar cases?

Mr. STAM. It is pretty well limited, because in the first place the debt has to be incurred by somebody prior to January 1, 1934, and assumed by the corporation after that date. In the second place, the debt has to be as the result of pledges or gifts made to charitable organizations and hospitals, so it is pretty well restricted.

Senator LA FOLLETTE. In other words, you do not think that there are other estates in a similar situation which could take advantage of it by incorporation now?

Mr. STAM. No; we did not.

Senator KING. Mr. Beaman, have you the amendment?

Senator METCALF. How would it be in a man's will when he leaves something to a hospital?

Mr. STAM. If they did that prior to January 1, 1934, and then later the estate was incorporated after January 1, 1934, this situation would

arise, because the estate would have to pay off those obligations in the will.

This amendment provides that we allow deductions for gifts paid to charitable organizations or hospitals for the purposes of section 351, and we add to that deduction section this clause [reading]:

> Including in the case of a corporation organized prior to January 1, 1936, to take over the assets and liabilities of the estate of a decedent, amounts paid in liquidation of any liability of the corporation based on the liability of the decedent to make such contributions or gifts to the extent that such liability of the decendent existed prior to January 1, 1934.

Senator COUZENS. I think that is a good amendment. I talked to Senator Bulkley about it. I am not his advocate, but I did promise to look after it for him here, and I brought it up at Senator Bulkley's request. I do not think that that does any material damage to the Treasury, and I do think it helps out this particular situation very much. I move its adoption.

Senator KING. Mr. Kent, what do you think of it?

Mr. KENT. I collaborated yesterday in the preparation of the amendment. I have no objection to offer.

Senator KING. Are there any remarks? As many as favor the adoption of the amendment say "aye"; contrary, "no."

(The vote is taken, and Senator King announces that the motion is carried.)

Senator GEORGE. Mr. Parker, have you anything on liquidation worked out?

Mr. PARKER. We have made considerable progress on liquidation, and in respect to many of the points are in agreement on something which would accomplish what we believe is your idea. There are one or two points that still are not agreed upon.

Senator GEORGE. You are not ready to report on it yet?

Mr. PARKER. If we could have one more day I think we could present something that would meet what we understand you want done.

Senator COUZENS. May I ask the chairman if the minority is going to have any information as to what we are going to do about the revenue-raising features of this bill, because it seems to me that that is the fundamental of the whole question in getting this matter cleared up. I do not want to sit here as a minority member day after day if you gentlemen of the majority have made up your minds about the kind of tax that we are going to impose.

Senator KING. Speaking for myself, there has been no conclusion reached other than those conclusions which have been expressed here in our votes, and our Republican brethren will have their say just as loud and as long as any Democrat has the say in the formulation of the bill.

Mr. Kent, you had a matter to present. Are you ready to do so now?

Mr. KENT. Senator Walsh has another amendment which he has been waiting to present with respect to a somewhat similar situation. I may say that I am well acquainted with the general situation with which this particular amendment deals.

Senator KING. His amendment?

Mr. KENT. The one that you have there, and also the other situation, but that I had not, previous to this afternoon seen—no copy of it came to my attention—and I have had no opportunity to examine the text of the proposed amendment to see whether it establishes a proper basis of classification.

This problem is essentially one of a classification once the policy question which is involved is passed upon.

The situation with which the amendment deals is this: There are a large number of investment trusts. They vary considerably in point of detail. They subdivide into two general classes, which are referred to by the terms "management trust" and "fixed trust", although the line between them is a rather shadowy one. In general, the difference between the two classes of cases is this: In your investment trust on the fixed type, the trust instrument itself defines with considerable particularity the sort of investments or even the specific securities in which the trustees may invest the trust funds.

Moreover, in the trust of the fixed type, there are usually limitations upon the power of the trustees to reinvest funds derived from the sale of securities held in the portfolio.

With your management type of trust, the powers of the trustees are much broader. They are usually with respect to both the types of securities in which they can invest and with respect to the sale of securities already held and the investment of the proceeds in other securities.

These investment trusts have grown. They began to develop in the late twenties, and they have grown and expanded quite rapidly in recent years. They do provide a medium for investors to obtain the benefits of diversification of risk and the spreading out of the risk of losses over a larger area.

Under the recent decisions of the courts, reflected in our Treasury Regulations, these trusts are now included in the association as defined in section 801 of the revenue act and are taxable as corporations.

Now, they say that that imposes a very heavy burden upon them, that they are simply agencies for a group of persons to get together and invest their funds in diversified securities, collect the income, and redistribute the income to the certificate holders.

Senator COUZENS. Does what you are discussing have any bearing on what that banker testified before the committee with respect to these little trusts in trust companies?

Mr. KENT. No; the problem there is really somewhat different, although it has elements in common with this situation. What they wanted there was leeway to pool the resources of these small trusts they are administering and invest them so as to get the benefit of diversification.

These investment trusts, of course, do very much the same thing. There is that marked similarity between them, but the action taken with respect to the common trust fund the other day would not cover this situation.

Senator BAILEY. There is no analogy between the common trust and an investment trust. An investment trust is something with stockholders, and the common trust has no such element.

Mr. KENT. Yes; the only point of similarity is that the investment trust does provide a method where it is possible to invest funds of a number of people to get the benefits of diversification.

Senator BAILEY. I have no special interest in it. What do you propose to do with respect to an investment trust?

Senator LA FOLLETTE. Mr. Kent is not proposing to do anything, but the Senator from Massachusetts and the Senator from Rhode Island brought it to his attention and asked for a discussion on it.

Mr. KENT. What these people are asking for, Senator, is simply this: In the case of these investment trusts which are not incorporated entities, they are asking that the law be amended so as to classify them as strict trusts, take them out of the classification of associations under section 701 (a) (2) of the House bill, which simply continues the present law on that, in order that the income upon their certificate to the certificate holders will not be diminished by the collection of the flat corporate rate from the trust itself.

Senator COUZENS. What do they pay now?

Mr. KENT. They would pay now from 12.5 to 15 percent.

Senator COUZENS. Under existing law?

Mr. KENT. Under existing law; depending upon the volume of their income.

Senator COUZENS. They do not want to pay the 18 percent, is that right?

Mr. KENT. That is right; they want to be classified as strict trusts, in which case if they distribute all of their earnings to the certificate holders, the income will be taken up in the returns of the individual holders.

Senator COUZENS. I do not think we should make any exception in a case like this any more than we make an exception in any other investment.

Senator METCALF. This puts them all out of business.

Senator COUZENS. A jump of 3 percent?

Senator METCALF. Perhaps 3 percent would not, but a larger percentage would. Most of these people, they tell me the average is not over $3,000 apiece, and these people take up 10 or 12 different kinds of stock and they pay it out in dividends.

Senator COUZENS. If a man has $3,000 in any other kind of a corporation, his corporation would pay the 18 percent. I do not see why they should be excepted in this case.

Mr. KENT. I am not certain that Congress actually intended to include them, or that this situation was considered when the association definition was written into the act. As a matter of fact, until comparatively recently they made their returns as trusts and were taxed upon that basis, and as the result of these recent court decisions, they have been swept into the association group and are now being taxed as corporations.

Senator KING. What would you call them if they are not corporations?

Mr. KENT. They are trusts. They are not trusts of the traditional type; they are really a modern development.

Senator LA FOLLETTE. They are not regulated in any way either, are they?

Mr. KENT. Under this amendment which has been proposed, the treatment of them as trusts will be limited to those cases in which they are subject to the supervision or regulation of the Government of the United States or any State or Territory thereof or of the District of Columbia, and by the terms of the trust instrument, the beneficiary may at any time withdraw his share of the trust property or its equivalent in cash, and by the terms of which there is provided a method for the diversification of investments.

Senator LA FOLLETTE. You have not had much time to go into this?

Mr. KENT. I have not really had time to consider the text of the amendment itself.

Senator KING. Is there any other feature that you are ready to report upon in the act?

Mr. KENT. Senator Walsh has an amendment—I thought I had a copy of it with me but it seems to have escaped me—which would apply to so-called mutual investment corporations. I think that I had better let him present that.

Senator KING. Then you will examine into that and let us hear from you as soon as you possibly can.

Senator COUZENS. May I ask of the chairman if we are going to work along on the assumption of the standing of our action of a few days ago in our previous vote, of 18 percent and 7 percent. If we are, I want to raise the question of cushions on the 7 percent on undistributed earnings. If we are not going to stick to that, we might as well not discuss it now, because it is only a waste of time.

Senator KING. I do not know that I can answer for the committee. I think several members of the committee are ready to adhere to that view. As to whether there has been any change or will be any change or any change is desired with respect to the matter just mentioned, I would not care to express an opinion. I think you can assume that we will go right along.

Senator LONERGAN. Mr. Chairman, are we not to be furnished with figures this afternoon?

Senator KING. I assume that the Senator refers to an informal discussion last evening?

Senator LONERGAN. Yes.

Senator KING. It was understood that the Treasury would furnish some figures or estimates during the day, and I am advised that they are on the way here now.

Senator COUZENS. In other words, that is another plan which contemplates our abandoning the plan already adopted, is that correct?

Senator KING. I do not know exactly what the figures will be, but I assume that it will call for the modification of the existing plan. Here is Mr. Seltzer now.

Mr. Seltzer, as the representative of the Treasury, have you any figures to submit, and if so, from whom?

Mr. SELTZER. Here are two estimates that we were asked to prepare.

Preliminary estimate

	Additional revenue (million dollars)
1. Repeal capital stock and excess profits tax	$168
2. Impose present corporate tax rate (12½ percent to 15 percent) on statutory net income as defined in present law, which includes 10 percent of intercorporate dividends received	
3. Define adjusted net income as the statutory net income less corporate income taxes plus 90 percent of dividends received. Define undistributed adjusted net income as adjusted net income less the dividend credit, less a special exemption of $15,000 to all corporations. Impose a tax on undistributed adjusted net income equal to the sum of the following: 25 percent on the amount of the undistributed adjusted net income which is not in excess of 20 percent of the adjusted net income; 35 percent on the amount of the undistributed adjusted net income which is in excess of 20 percent and not in excess of 40 percent of the adjusted net income; and 45 percent of the amount of the undistributed adjusted net income which is in excess of 40 percent of the adjusted net income.	
Yield of such tax on undistributed adjusted net income and of surtax on dividends to individuals	790
Total additional revenue	622

	Additional revenue (million dollars)
1. Retain capital stock and excess profits tax	
2. Impose present corporate tax rate (12½ percent to 15 percent) on statutory net income as defined in present law, which includes 10 percent of intercorporate dividends received	
3. Define adjusted net income as the statutory net income less corporation income taxes plus 90 percent of dividends received. Define undistributed adjusted net income as adjusted net income less the dividend credit, less a special exemption of $15,000 to all corporations. Impose a tax on undistributed adjusted net income equal to the sum of the following: 15 percent on the amount of the undistributed adjusted net income which is not in excess of 20 percent of the adjusted net income; 25 percent on the amount of the undistributed adjusted net income which is in excess of 20 percent and not in excess of 40 percent of the adjusted net income; and 40 percent of the amount of the undistributed adjusted net income which is in excess of 40 percent of the adjusted net income.	
Yield of such tax on undistributed adjusted net income and of surtax on dividends to individuals	$630
Total additional revenue	630

If the percentage of intercorporate dividends now subject to corporate income tax be increased from 10 percent to 13⅓ percent, the additional yield would be $5,000,000. If from 10 percent to 16⅔ percent, the additional yield would be $10,000,000.

These estimates assume no changes in existing law other than those cited above and that the new bill will contain provisions which will prevent any avoidance of the above taxes.

Senator KING. Will you proceed, Mr. Seltzer, if you care to make any explanation?

Mr. SELTZER. We were asked to prepare two additional amendments summarized in this mimeographed sheet.

On the left-hand side of this sheet, you have a proposal whereunder you would repeal the existing capital-stock and excess-profits taxes; you would retain the present corporation taxes with their graduated rates; you would define adjusted net income as statutory net income less corporation income tax paid, plus 90 percent of dividends received; you would define the undistributed adjusted net income as adjusted net income less the dividends paid and less a special exemption of $15,000 for all corporations. Then you would impose a tax on the undistributed adjusted net income after these credits and exemptions equal to the sum of the following: 25 percent on the amount of the undistributed adjusted net income which is not in excess of 20 percent of the adjusted net income; 35 percent on the amount of the undistributed adjusted net income which is in excess of 20 percent not in excess of 40 percent of the adjusted net income; 45 percent on the amount of the undistributed adjusted net income which is in excess of 40 percent of the adjusted net income.

The total additional revenues we estimate would amount to $622,000,000, after allowing for the repeal of the existing capital-stock and excess-profits taxes.

On the right-hand side you have a somewhat different proposal. Under this proposal you would retain the existing capital stock and excess profits taxes and you would have somewhat lower rates on undistributed adjusted net income.

No. 2 under this proposal is the same as it is under the other.

Under no. 3, the rates would be 15 percent instead of 25 percent on the first 20 percent of the adjusted net income not distributed. Then they would amount to 25 percent instead of 35 percent on the next 20 percent saving, and the top rate would be 40 percent instead of 45 percent on the balance of the undistributed adjusted net income.

The estimated additional revenues under this second proposal amounts to $630,000,000.

We were also asked to estimate what additional revenues would be received in the event of changes in the treatment of the intercorporate dividends. At the present time, as you know, 10 percent of dividends received by a corporation are included in the statutory net income, whereas 90 percent is allowed as a deduction. One of these proposals was to increase from 10 to 13⅓ percent the proportion of dividends received by corporations that would be included in the statutory net income subject to the regular corporation income tax. The other, if the proportion of such included dividends be 16⅔ percent as compared with the present 10 percent.

We estimate that you would get an additional $5,000,000 if you raised the percentage of dividends received by corporations included in the statutory net income from 10 to 13⅓ percent, and the additional revenues would be $10,000,000 if you raised the percentage to 16⅔ percent from the present 10 percent.

Senator BLACK. May I ask you a question? In these two estimates, what consideration if any was given to the debts and obligations of corporations?

Mr. SELTZER. No consideration whatever was given.

Senator GEORGE. You provide no cushions?

Mr. SELTZER. These figures mean just what they say here. We assumed no other changes than these that are specified here.

Senator BLACK. In other words, that does not provide any so-called cushions of any kind?

Mr. SELTZER. No.

Senator GEORGE. This treats all corporations the same, banks, trust companies, insurance companies, and so forth.

Mr. SELTZER. You have this cushion that is included here. Every corporation may retain $15,000.

Senator GEORGE. Yes; I know that. This treats all corporations, banks, trust companies, insurance companies, all the same.

Mr. SELTZER. It does with this qualification, that as I pointed out the other day, the revenue estimates would remain substantially unchanged if you treated banks and insurance companies as they are treated under the existing law, because as I pointed out, the amount of taxable income of banks and insurance companies has been for some years now almost insignificant.

Senator GEORGE. I understand. I am just making inquiry.

Mr. SELTZER. Yes.

Senator GEORGE. You do not take into consideration here the normal tax on dividends?

Mr. SELTZER. No; there is no normal tax on dividends in either of these proposals.

Senator GEORGE. Because you are taking that up with your surtaxes? Is that the idea, or have you abandoned that?

Senator BLACK. We have had figures on that, have we not?

Mr. SELTZER. I beg your pardon?

Senator BLACK. The figures we have had heretofore on the normal tax on dividends would be substantially the same?

Mr. SELTZER. Oh, yes.

Senator BLACK. If we should decide to impose them.

Mr. SELTZER. Whereas, under the Budget estimate, we estimated that a 4-percent tax on dividends would yield an additional $90,000,000 under either of these two proposals, the application of the normal tax to dividends would yield substantially in excess of $90,000,000, because it is supposed it would encourage far more liberal distribution of corporate earnings.

Senator GERRY. What do you mean by "substantially"?

Mr. SELTZER. If we had a few minutes, I could calculate that. You see, the 4 percent normal not being involved in either of these two propositions, we made no calculation for it.

Senator LA FOLLETTE. Could you give us an approximation shortly of what it would be?

Mr. SELTZER. Yes; we could.

Senator BLACK. May I ask you another question before you do that? As I understand it, then, so far as banks and insurance companies are concerned, according to the judgment of the Treasury Department, this estimate would remain approximately the same whether you applied this law to them or applied the changed rates that appear in the bill now?

Mr. SELTZER. Well, so far as the corporations' statutory net income taxes are concerned, it does not make much difference, because as I said, the taxable income of banks is relatively small. That, ipso facto, makes the undistributed net income of banks small.

Senator BLACK. Then, is the question that I asked you, correct, that the fact that you treat banks and insurance companies the same as you treat the others makes substantially no difference in your estimates?

Mr. SELTZER. That is correct. About 5 or 6 million.

Senator BLACK. Let me ask you another question. Would it be practicable to estimate what income the Government would receive from this present plan that you have if the bill provided that the income which was needed to pay off contractual obligations of the corporations during the year, and obligations which had been assumed under their bonds, on outstanding stock issues or any other necessary obligations——

Senator KING (interposing). Extending over some period of time as well as in the current year?

Senator BLACK. Extending over a period of time. Would it be possible for you to estimate and take that into consideration and give a reasonably accurate estimate as to what we could obtain from that plan, providing for those payments and those obligations?

Senator BYRD. Before you answer that, I want to understand whether that includes an ordinary debt.

Mr. SELTZER. Do you mean commercial debt?

Senator BYRD. Yes.

Senator BLACK. All this includes debts.

Senator BYRD. You said, a contractual obligation.

Senator BLACK. This is a tax on profits, is it not?

Senator BYRD. I just want to get it clear.

Senator BLACK. This is not on gross income.

Mr. SELTZER. Senator Byrd's question is important for this reason. A commercial debt, ordinary bank debt and debt to suppliers is a revolving debt that is never paid off. You do not look to net income to pay off that type of debt; you look to your gross receipts for that, and hence it is important to us whether commercial debts of that category would be given special treatment.

Senator BYRD. Furthermore, whether a deed of trust would be included in it.

Senator BARKLEY. They are not included in the category of debt-ridden corporations as defined under this bill.

Senator BYRD. The debt-ridden corporation in the House bill in my judgment is totally inadequate, because that only gave relief to a corporation that had debts in excess of its capital, and that was a bankrupt company.

Senator BLACK. Could you provide an estimate, or is it possible to provide an estimate, either on the basis of the present 12½ to 15 percent or some other graduated scale, superimposing upon that a graduated tax on undistributed income, not counting that undistributed income, however, until the payment of the necessary contractual obligations, either by notes, bonds, or stock obligations?

Mr. SELTZER. Including commercial debts?

Senator BLACK. I did not ask you about commercial debts now.

Mr. SELTZER. The possibility of producing a reliable estimate in that connection depends very importantly on what kind of checks you would insert against the abuse of such privilege. In the House bill we did not have to allow very much of a loss because of the cushions for debt-ridden corporations, because if you will recall, a corporation could use earnings to retire debt only if it paid 22.5 percent on the amount of earnings so used.

Well, now, when we sit down with ourselves and say "What is going to be the effect of that cushion provision" we have to say that corporations that could retire debt only at a tax loss of 22.5 percent would in most cases seek to refinance their debts rather than to use earnings to retire those debts. They might, of course, indirectly do so, they might sell additional stock to their stockholders——

Senator BLACK (interposing). What I want to get at is this. There is an idea on the part of some of the Treasury Department people that it is wholly and completely impossible to give us an estimate with those cushions, and I simply want to know whether or not it is or is not. I am not prepared to discuss the House bill.

Mr. SELTZER. I am inclined to say that the possibilities in this respect depend very largely upon the type of cushion provision that you include.

Senator BLACK. I mean the type of cushion provision that we permit a corporation to pay the debt that it owes during the year, or part of the debt that it owes to discharge a part of its bonds that are due if there were some due, or the interest thereon, or to discharge any stock obligation or any other outstanding contractual obligation that it assumed. I am not including now the commercial indebtedness that runs from year to year.

Mr. SELTZER. Without any penalty whatever?

Senator BLACK. What I want to know is, without any discussion of anyt[illegible]g else connected with the House bill or this bill or any other bill, whether the Treasury can or cannot give us an estimate which will be reasonably certain—not to the dollar—but can we get an estimate of that kind on a provision of that type.

Mr. SELTZER. Well, as I tried to say, if you make the use of earnings for debt retirement possible at a tax cost sufficient to discourage unnecessary use of that cushion, you have one situation, but——

Senator BLACK (interposing). Let me ask you this. Suppose we assume that there is no discharge necessary where the debt or obligation is due, or where there is a partial payment due, and suppose there are some of us who want to draw a bill—let us suppose we want to draw a bill, and I want to know if it can be done or if it cannot be done. To draw a bill providing for a base tax of 12.5 to 15, or 12.5 to 16, or 12.5 to 18, and we want that bill then to provide that before we consider taxation on undistributed income, that the corporation should first have a right to discharge the obligation that it ought to discharge, that it owes.

Senator CONNALLY. Senator Black, in all fairness to these experts, they cannot form an estimate on a general statement like you make, to let them pay all debts that ought to be paid. One man would think one thing and one man would think another, and I think in fairness to them, you are introducing such a variable element there that it makes it impossible for them to get any estimate of it. You have to say $25,000 or $150,000, or some definite standard before you can expect an estimate.

Senator BLACK. I am not talking about a definite exemption; I am talking about a bill which would provide—and nobody could be definite about it because we would have to assume that it would have to be drawn in such a way as to take that into account.

Senator CONNALLY. When you speak of estimates, you have to be definite.

Senator BLACK. I am not asking for an estimate; I am just asking if such an estimate can be made and such a bill drawn.

Mr. SELTZER. We did make an estimate in connection with the House bill that provided cushions of the character that you mentioned. We were able to make an estimate of the character that you suggest, but that possibility was due in no small measure to the specific provisions of the House bill. I believe that is what Senator Connally has in mind.

Senator BLACK. Of course we would draw specific provisions or we would not have any bill. What I want to get at is, if we draw the specific provisions permitting them to pay what they owe during the year, and we start off on a basis of 12.5 to 15, or any other amount, and then we fix a definite graduated scale but we provide specifically in the bill the terms under which the obligations shall be paid—what I want to know is, I see no reason why the Treasury Department cannot give us an estimate and I think they can.

Mr. SELTZER. I say in general if you want a general answer to a very general question, the answer is yes, and the answer is illustrated by our estimate in connection with the House bill, but the reliability of another estimate would depend again upon the particular provisions that is, if you were to propose, Mr. Senator, a certain series of cushions with rates attached, we might feel that there was so much play in those particular provisions that we could not give you a close estimate.

On the other hand, you might impose another series of questions in which there is far less play, in which case I feel confident of my ability to give you a close estimate.

Senator BYRD. Isn't this true, that the question that Senator Black has asked takes in much more territory than the House bill?

Mr. SELZTER. Decidedly.

Senator BYRD. Because the House bill confined these debt-ridden corporations to those corporations that owed more than their capital, and they pay 22.5 percent. The question that Senator Black asked, and that I would also like to know, is in regard to any debt that may be properly payable within that year. Take a deed of trust of a corporation and say they have 5 years in which to pay it, and whether they can prorate it so much in each of the 5 years and pay no surtax.

Mr. TURNEY. Any whatever?

Senator BYRD. Any whatever. When it is applied to that debt. That is the question Senator Black wanted the answer to, and I would like to know the same thing, if you can furnish it. Frankly, in my judgment it cannot be done.

Senator KING. It could not be done. Can I ask one question of you, and this is a political question rather, perhaps what might be called a scientific-expert question to be propounded to an expert. Has the Treasury Department any idea as to what a cushion is, and have they defined cushions, and have they defined cushions with respect to the corporations that are in debt and have various classes of debts?

Mr. SELTZER. That is essentially, I take it, a legislative matter.

Senator King. I think so.

Mr. SELTZER. And certainly my own division does not do that.

Senator KING. I was wondering whether in the Treasury Department or outside of the Treasury Department your division had been asked to define what "cushions" were, and what provisions should be made to meet cushions, and with what particularity should they be surrounded so that there could be no evasions or no injustices.

Mr. SELTZER. I cannot speak for the whole Treasury Department, but I can speak for myself personally. I have not been asked to do that.

Senator KING. Is there any other question?

Senator BYRD. Is Mr. Seltzer going to attempt to get that information up, or can it not be furnished?

Senator LA FOLLETTE. He cannot give you any estimate until you tell him what your cushions are going to be.

Senator KING. Senator Bailey, have you any questions to ask of the expert in regard to this matter?

Senator BAILEY. In regard to those new schedules?

Senator BYRD. On the cushion question.

Senator KING. No; in regard to the estimates.

Senator BAILEY. This proposition here does not contain the proposition that I thought we were going to consider. Let me say one thing that strikes me as being of the essence of it. I do not think that I would ever consent to putting a tax of 20 percent or 25 percent on the first earnings of a corporation. Here is a tax of 25 percent on the income which is not in excess of 20 percent.

Senator BARKLEY. That is after deducting $15,000.

Senator BAILEY. I understand that, but that $15,000 is a very small sum. There ought to be a fundamental exception as to earnings. We begin to tax earnings on top of a tax. A man might not make enough earnings to pay a dividend and yet he would have to pay this tax. What I think at the outset is that that is not in accord with what we are supposed to be discussing.

And, secondly, I do not think if you adjust it according to cushions, you will get as much money as we propose to get under the law that we practically agreed upon.

Senator BARKLEY. I think this is in accordance with what we requested the Treasury to get. The only difference between it and the one we were considering is that that proposal repealed the capital-stock tax and excess-profits tax.

Senator BAILEY. I understood we were to make some proper allowances for debtor corporations and some corporations that had contracts with respect to the payment of dividends, and reservations of profits, and provisions with regard to banks, and provisions with regard to insurance companies. If you make those provisions, you do not get as much out of this plan as you got out of the plan that we have developed up to date. Our first task is to get somewhere around $650,000,000 to $670,000,000. This won't do it.

Senator KING. Are there any other questions to be asked of Mr. Seltzer?

Senator CONNALLY. I would like to ask Mr. Seltzer this. I notice in the next to the last paragraph here you say that if the percentage of intercorporate dividends now subject to corporate income tax be increased from 10 percent to 13⅓ percent, the additional yield will be $5,000,000; and 16⅔ percent, $10,000,000. Suppose we just advance that sum of 10 percent, 2½ percent; how much additional revenue would it bring in?

(Discussion off the record.)

Senator CONNALLY. I understand then, about $10,000,000.

Senator BARKLEY. As I understood, the statement was made that for every 1-percent additional tax you put on this 10 percent, it would bring in $100,000,000.

(Discussion off the record.)

Senator CONNALLY. Suppose we raise that rate to 13.5, instead of 12.5, to 16, we get a right considerable amount of money there, do we not?

Mr. SELTZER. Yes.

Senator CONNALLY. That is 1 percent. You would get about sixty or seventy million right there, would you not?

Mr. SELTZER. You would not gain that much; no.

Senator CONNALLY. We would get a considerable amount right there by raising that rate from 13.5 to 16, and retaining the graduation. I should say that, roughly, you would get at least fifty million right there, and whatever you picked up there, and whatever you picked up on the normal tax, would serve to reduce these brackets.

Senator GERRY. I would like to ask a question if everybody is finished. I would like to know what a million-dollar corporation that has earned a million dollars in a year would pay under both plans.

Mr. SELTZER. If it retained what percentage?

Senator GERRY. If it retains the whole amount.

Mr. SELTZER. If it retains everything?

Senator GERRY. Everything. I want to know what it would pay under these two plans.

Senator CONNALLY. That is a simple matter of calculation.

Senator GERRY. I would like to have it calculated.

Mr. SELTZER. It will take about 5 minutes.

Senator GERRY. And put it in the record. I think we are entitled to know that. That is the picture.

Senator KING. Any other questions?

Senator GERRY. Under this first plan it is 55 percent, is it not?

Mr. SELTZER. You would have to make assumptions with respect to dividend receipts, and so on.

Senator GERRY. No dividend receipts. It is 15 plus 40; is it not?

Senator CONNALLY. It is not 40 on the same amount.

Senator GERRY. I see. The thing that will really answer the question is this tax on a million dollars of earnings.

Senator BYRD. It would run around 55 percent on a million-dollar corporation.

Senator WALSH. May I inquire if in this latest estimate that has been submitted you have included all of the provisions of the House bill relating to the computation of net income?

Mr. SELTZER. You mean the regular provisions of the law?

Senator WALSH. All the cushions.

Mr. SELTZER. What is not included there is approximately $37,000,000 of special provisions with respect to the liquidation of foreign corporations, and the taxation of nonresident aliens. If you take over those provisions of the House bill, you would add about $37,000,000 to these two estimates.

Senator WALSH. They are not included?

Mr. SELTZER. They are not included in these statements.

Senator WALSH. But we practically decided to include those, so that is $37,000,000 more.

Mr. SELTZER. Oh, yes.

Senator WALSH. But are all the cushions included?

Senator LAFOLLETTE. They are not included.

(Discussion off the record.)

Senator KING. While the experts are making their calculation which has been requested, Mr. Kent has a proposition.

Mr. KENT. We were asked to report upon an amended draft of the receivership sections of the bill. We had worked out this amended statement for your consideration. Of course, the undistributed-profits tax would not apply to these corporations. [Reading:]

Domestic corporations which for any portion of the taxable year are in bankruptcy under the laws of the United States or are insolvent and in receivership in any other court of the United States or any State, Territory, or the District of Columbia.

Senator GEORGE. You would apply only the flat rate?

Mr. KENT. Yes.

Senator GEORGE. Is there any objection to this amendment?

Senator LA FOLLETTE. Do you give them the year under which they come out, in that?

Mr. KENT. Yes.

Senator LA FOLLETTE. Do you think it would have any material effect upon the revenue if you gave them 2 years?

Mr. KENT. Yes; I think it would. Under this, if they go into receivership during the taxable year or come out of receivership during the taxable year, they are treated as corporations in receivership for that year. One change that we made in here was to limit this favored treatment to corporations which are in receivership and which are insolvent.

It was pointed out the other day—I should say by the way, that it was our purpose to write into the committee report a statement that the term "insolvent" here used, is used in the broad sense to include cases where the corporation may have in excess of its liabilities assets, but which are in such frozen condition that it cannot meet the claims of its creditors. Of course, if they come out during the middle of the year, this does give them a little breathing spell. It would be pretty hard to make an exact estimate, of course, of just what the effect of that will be.

Senator LA FOLLETTE. The only thing that I was impressed with is the fact that there are some of these corporations, where they come out of receivership, there is an adjustment which they make with their creditors or bondholders, and there may be the situation that unless they have a little time wherein they could make these adjustments, that they could not get out of receivership at all.

Senator GEORGE. If there is no objection, this amendment is approved.

Is there another one?

Mr. KENT. The other one has already been presented.

Senator GERRY. I have an amendment that Senator Van Nuys asked me to introduce for him. I think I had better read the explanation first, and then the amendment.

MEMORANDUM PERTAINING TO REFUND OF EXPORT DRAWBACKS

Certain packers exported meat to foreign countries and thereby became entitled, under section 17 (a) of the Agricultural Adjustment Act to the refund of a processing tax placed upon such exported meat.

The right to this refund is known as export drawback.

The reason for export drawbacks was to enable the exporting packers to sell on foreign markets, at the lower foreign prices, and yet to suffer no loss; in other words, the export drawbacks were to equalize the lower foreign with the higher domestic prices, and thus the exporting packers could hold their foreign markets and thus handle more commodities.

Refunds of export drawbacks were being allowed to the exporting packers, being the consignors named in the bills of lading, until January 6, 1936.

However, due to routine administrative delay in passing upon claims for export drawbacks, many such claims had been made but were not allowed, or, if allowed, had not been paid by January 6, 1936. Also, some large packers (like John Morrell of Ottumwa, Iowa) were paid export drawbacks though they obtained injunctions against payment of processing taxes; while other packers were paid no export drawbacks at all.

The exporting packers relied upon the promise of the Government to refund, made under the Agricultural Adjustment Act, in making such exports. They have this argument based upon considerations of fairness and consistency which should entitle them to permission for refund in the present tax bill; if the spirit of the Agricultural Adjustment Act should be so observed as to justify the retention of processing taxes paid, and the recovery by means of a "windfall Tax" of impounded and returned processing taxes, then also its spirit should be sufficiently respected to permit the completion of refund of export drawbacks, the right to which was earned by packers in reliance upon the promise of the Government to make such refunds.

If such export drawback refunds are not permitted, then the exporting packers will not only lose the amount of processing taxes paid and impounded but they will be penalized for having relied upon and followed out the Agricultural Adjustment Act in the exporting of goods, for which they earned export drawbacks.

This situation can be recognized and the exporting packers can be treated consistently and fairly if subsection (b) of section 601, be amended by adding to the first sentence the underscored words following:

Senator GEORGE. I think that has been covered, but you can read the amendment.

Senator GERRY. I will read the amendment then.

(b) Except for refunds under section 15 (a) of the Agricultural Adjustment Act as reenacted herein, no refund under this section shall be made to the processor or other person who paid (or was liable for) the tax with respect to the articles on which the claim is based, unless such processor or other person was the consignor in the exportation.

The remainder of section (b) to remain unchanged from the Senate draft.

Senator GEORGE. Is that not covered, Mr. Kent?

Mr. KENT. I do not really understand that situation, because if these people are not processors who paid the processing tax, they are certainly taken care of by section 601, and if they are processors, all that they have to do——

Senator GEORGE (interposing). I thought they came along with the big bag people.

(Informal discussion.)

Senator GERRY. Would you like to look into that and report back?

Mr. KENT. Yes.

Senator GEORGE. Are there any other amendments to be considered by the committee?

Senator BAILEY. Are you ready for the amendment on oils and fats? You will recall it was adopted yesterday. It was referred to one of the representatives of the Treasury for redraft, and he has redrawn it, and I think it is all right. If the committee desires me to read it, I will read it. He has changed the structure, but he has not changed the meaning or intent. He has made some adaptations to the existing law that are necessary, but the purpose and effect of the amendment is not altered. He used the word "article", and I have added "merchandise or combination."

It is further provided here:

Notwithstanding the provisions of subsection (a) of this section, the first domestic processing of sunflower oil or sesame oil, imported prior to the effective date of this title, shall be taxed in accordance with the provisions of section 602½ of the Revenue Act of 1934 in force on the date of the enactment of this act.

I think that is very wise. The other provision is not exactly new, but it is different from what we had:

All taxes accrued or paid under section 402 of the Revenue Act of 1935 on the importation of glycerin or stearine pitch shall be remitted or refunded under such regulations as the Secretary of the Treasury may prescribe.

You recall that on yesterday the statement was made about the difficulty of ascertaining the duties on that subject, and they never have been able to resolve it, so the effect of this bill will be to remit those duties and end those controversies, but the expert tells me there is nothing in it anyhow.

I will offer the amendment and state that it is in accordance with the amendment that I offered yesterday, but it is probably in much better form.

(The amendment submitted by Senator Bailey is as follows:)

TITLE V. AMENDMENTS TO PRIOR ACTS

SEC. 701. TAX ON CERTAIN OILS.—The first sentence of section 601 (c) (8) of the Revenue Act of 1932, as amended, is amended to read as follows:

"(8) Whale oil (except sperm oil), fish oil (except cod oil, cold-liver oil, and halibut-liver oil), marine-animal oil, tallow, inedible animal oils, inedible animal fats, inedible animal greases, fatty acids derived from any of the foregoing, and salts of any of the foregoing; all the foregoing, whether or not refined, sulphonated, sulphated, hydrogenated, or otherwise processed, 3 cents per pound; olive oil and sesame oil, provided for in paragraph 1732 of the Tariff Act of 1930, sunflower oil, rapeseed oil, kapok oil, hempseed oil, fatty acids derived from any of the foregoing, and salts of any of the foregoing; all the foregoing, whether or not refined, sulphonated, sulphated, hydrogenated, or otherwise processed, 4½ cents per pound; any article, merchandise or combination, 10 per centum or more of the quantity by weight of which consists of, or is derived directly or indirectly from, one or more of the products specified heretofore in this paragraph or in section 602½ of the Revenue Act of 1934, as amended, a tax at the rate or rates per pound equal to that proportion of the rate or rates prescribed in this paragraph or such section 602½ in respect of such product or products which the quantity by weight of the imported article derived from such product or products bears to the total weight of the imported article; hempseed, rapeseed, sesame seed, and kapok seed, 2 cents per pound."

SEC. 702. PROCESSING TAX ON CERTAIN OILS.—(a) The first sentence of section 602½ (a) of the Revenue Act of 1934, as amended, is amended to read as follows:

"(a) There is hereby imposed upon the first domestic processing of coconut oil, palm oil, palm-kernel oil, fatty acids derived from any of the foregoing oils, salts of any of the foregoing (whether or not such oils, fatty acids, or salts have been refined, sulphonated, sulphated, hydrogenated, or otherwise processed), or any combination, merchandise, article, or mixture containing a substantial quantity of any one or more of such oils, fatty acids, or salts with respect to any of which oils, fatty acids, or salts there has been no previous first domestic processing and no import tax has been paid under section 601 (c) (8) of the Revenue Act of 1932, as amended, a tax of 3 cents per pound to be paid by the processor.

"(b) Notwithstanding the provisions of subsection (a) of this section, the first domestic processing of sunflower oil or sesame oil, imported prior to the effective date of this title, shall be taxed in accordance with the provisions of section 602½ of the Revenue Act of 1934 in force on the date of the enactment of this Act."

(c) The last sentence of section 602½ (a) of the Revenue Act of 1934, as amended, is amended by striking therefrom the last comma and the words, "but does not include the use of palm oil in the manufacture of tin plate."

SEC. 703. MISCELLANEOUS PROVISIONS.—Nothing in section 601 (c) (8) of the Revenue Act of 1932, as amended, shall be construed as imposing a tax in contravention of an obligation undertaken in any trade agreement heretofore entered into under the authority of section 350 of the Tariff Act of 1930, as amended, or as imposing a tax on the importation of glycerin or stearine pitch or on the importation of any article by reason of any component or such article derived directly or indirectly from a waste not named in section 601 (c) (8) of the Revenue Act of 1932, as amended. Section 402 of the Revenue Act of 1935, is hereby repealed. All taxes accrued or paid under section 402 of the Revenue Act of 1935 on the importation of glycerin or stearine pitch shall be remitted or refunded under such regulations as the Secretary of the Treasury may prescribe.

SEC. 704. EFFECTIVE DATE.—The provisions of this title shall be effective on and after the thirtieth day following the date of the enactment of this Act.

Senator GEORGE. Without objection it will be agreed to.

Senator BLACK. I should like Mr. Seltzer to submit an estimate where the present corporation income tax rate, retain the present capital stock and excess profits tax, impose a normal tax on dividends of 4 percent, exempt the first 20 percent of the adjusted net income, impose a 20-percent rate on the next 20 percent retained; impose a 30-percent rate on the rest retained.

Alternatively, the same thing except that you exempt the first 30, and then the other two steps.

Then, a third alternative, wherein in addition to the 20 and 30 percent exemptions, you have $15,000 additional exempted.

I think that on the theory that it will get something before us which would contain what I would consider the most practical cushion we could get. I think it is the best kind of a cushion, and I believe some of them have to get cushions.

Senator GEORGE. In order that we may make some progress, I move that this committee report the bill as it has thus far been builded in this committee. I do not care to press it tonight, but I want to lodge that motion. If anybody has any substitute, let them have them ready.

Senator CLARK. You mean to report the bill including the provisions that we adopted some 10 days ago?

Senator GEORGE. Yes.

Senator KING. But postpone vote until tomorrow, and that does not preclude the offering of any substitutes.

Senator BLACK. In order that there may be no misunderstanding about the 18 to 1 vote some days ago, I stated at the time what my position was.

Senator KING. Are there any other amendments or suggestions to be offered?

Mr. KENT. There is one matter that I ought to bring up here in connection with Senator Lonergan's amendment. It merely refers to the phraseology of the amendment at one point:

Provided, however, That the proceeds of policies on which the premium-paying period is less than ten years shall not be deductible.

We are informed that you can get almost any arrangement for the payment of premiums that you want, and that under this provision it would be possible to have the policy in which 90 percent or 99 percent of the total premium was paid in the first year, and the balance of the premium, the small amount remaining, was spread out over the 10-year period.

It was our thought that what the committee probably had in mind was that those 10-payment policies should be that the premium under such a policy should be substantially equal in amount, otherwise it would be virtually the same as permitting a single premium policy to be written for the purposes of this amendment.

I merely bring that up for the consideration of the committee, and inquire whether you would wish to have the experts modify the language of the amendment in such a way as to provide not only for a 10-payment policy, but also that the premiums for each year of the 10-year period should be approximately equal in amount.

Senator LONERGAN. What is the advantage in that, Mr. Kent?

Mr. KENT. The advantage is this. You could have a man who is very ill, and you would expect him to die. If he will pay a high enough premium, he can get a policy from an insurance company. For instance, he thinks he may die next year, and he has a large estate, and he wants a million dollar policy, and if he will pay a high enough premium so the insurance company could be certain that it is not going to lose money on it, he can get a policy, and a mere proviso that it should be written as a 10-payment policy would not affect the situation very much because the policy could provide for the payment of all but a very small amount of the total premium at the time the policy was written, and the purpose of the safeguarding clause would be substantially defeated unless that possibility were eliminated.

Senator LONERGAN. I would like to have action on that deferred until tomorrow.

Senator LA FOLLETTE. I think it should be eliminated. I move that it be changed so that it will provide for approximately 10 equal premiums.

Senator LONERGAN. And I ask to have action deferred until tomorrow.

Senator KING. There is no objection, then.

Are there any other amendments or suggestions?

(No response.)

Senator KING. Are there any administrative changes, Mr. Parker?

Mr. PARKER. No; we have no more ready. We may have one or two more to submit before we get through.

Senator KING. The committee will stand adjourned until 10:30 o'clock tomorrow morning.

(Whereupon, at 4 p. m., a recess was taken until the following day at 10 a. m.)