

[EXECUTIVE SESSION COMMITTEE PRINT]

# REVENUE ACT, 1936

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## 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

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### PART 2

APRIL 27, and 28, 1936

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Printed for the use of the Committee on Finance



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# REVENUE ACT, 1936

MONDAY, APRIL 27, 1936

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

The committee met in executive session, pursuant to adjournment, at 10 a. m., Senate Finance Committee room, Senate Office Building, Senator Pat Harrison presiding.

Present: Senators Harrison (chairman), King, George, Walsh, Barkley, Connally, Bailey, Black, Gerry, Guffey, Couzens, Keyes, La Follette, Hastings, and Capper.

Also present: Guy T. Helvering, Commissioner of Internal Revenue, Treasury Department; Herman Oliphant, General Counsel for the Treasury Department; Arthur H. Kent, Acting Chief Counsel, Bureau of Internal Revenue; George C. Haas, Director of Research and Statistics, Treasury Department; A. S. McLeod, Statistician, Treasury Department; C. E. Turney, Assistant General Counsel for the Treasury Department; L. H. Parker, Chief of Staff, Joint Committee on Internal Revenue Taxation, and members of his staff; Middleton Beaman, Legislative Counsel, House of Representatives.

The CHAIRMAN. All right, Mr. Parker.

Mr. PARKER. We come to the question of the tax on foreign corporations and nonresident aliens in the bill, and, with your permission, Mr. Beaman will explain that.

The CHAIRMAN. All right, Mr. Beaman, to simplify it for us, tell us just what the present law is.

Mr. BEAMAN. That is just what I was going to do, Senator. We shall take up first, if you will, the foreign corporations.

The CHAIRMAN. You put the foreign corporations on the basis of banks and insurance companies?

Mr. BEAMAN. No, Senator. I will start out by telling you the present law. Under the present law the foreign corporation is taxed exactly like the domestic corporation, the same rate of tax, but it includes in its gross income only income from sources within the United States, whereas, the domestic corporation includes in its gross income the income from all sources.

This bill divides the foreign corporations into two categories. First, those who are engaged in trade or business within the United States, or have an office or place of business in the United States. Those foreign corporations the bill taxes 22.5 percent on all their income from sources within the United States. In other words, it is exactly like the present law as to that class of corporation, except the rate is put up to 22.5 percent.

A foreign corporation not having an officer or place of business in the United States and not engaged in trade or business in the United States is taxed 15 percent on certain specified sources of income, of

course, from within the United States, and those are, generally speaking, interest, rents, dividends, and the fixed or determinable annual periodic payments, not including things like capital gains, the kind of income on which the withholding is now required.

The CHAIRMAN. Give us an illustration of that.

Mr. BEAMAN. Where they get interest on the bonds of a domestic corporation, or where they get dividends from the stock of a domestic corporation, or they get rent.

The CHAIRMAN. Take a foreign corporation that has no office in this country, its business is wholly in the other country except it owns some stock here.

Mr. BEAMAN. If it does business here, Senator, it is taxed in the other category, 22.5 percent on all its income from sources in the United States. If it has no business here, we will say, for example, it is an investment trust in London. If it has in its portfolio stock in domestic corporations, bonds in United States corporations, and draws its income from those sources, it is taxed 15 percent on the income from those sources.

The CHAIRMAN. On what it makes in this country?

Mr. BEAMAN. On what it makes in this country, 15 percent flat, without any deductions against this income. The tax is expected to be collected largely by withholding. Of course, the corporation is liable for the tax. If the withholding agent does not take it out, the corporation is still liable for the tax, and there is a provision in the bill that the commissioner, under regulations, can exempt foreign corporations in this category from the requirement of filing returns to such an extent as he finds advisable. I think if the withholding system works well there will be no need for feeling worried about it, because the tax has been collected; there will be no deduction. It is a flat 15 percent on this class of income.

Senator COUZENS. The matter will be aided, though, if the Commissioner will be sure that he has adequate returns, whether they file a return or not.

Mr. BEAMAN. Sure. That is all there is to the foreign-corporation provision.

Now, the nonresident alien individual under the present law again is treated just like a resident of the United States subject to normal and surtax, but only on his income from sources within the United States.

Senator COUZENS. He is not required to file returns?

Mr. BEAMAN. He is required to file returns.

Senator COUZENS. He is?

Mr. BEAMAN. Under the present law I am speaking of.

Senator COUZENS. Do we require a return to be filed by an alien resident, a resident who lives abroad?

Mr. BEAMAN. I think there is some trouble in getting the tax out of him. Theoretically he is supposed to file a return. Of course, if he has property in this country you can collect the tax.

This bill makes a very decided change in that system. Here again the field of nonresident alien individuals is divided into two classes, like the foreign corporation. Those who are engaged in trade or business in the United States, or have an office or place of business in the United States remain subject to the normal and surtax just as

the present law on all the income from sources in the United States and is subject to the duty to file a return just the same as at present.

The CHAIRMAN. That is on the business in the United States?

Mr. BEAMAN. That is on all their income from sources within the United States, whatever it may be, whether from the business in which they are engaged here or their investments. A nonresident alien individual who is not engaged in trade or business in the United States, or has not an office or place of business here, is taxed a flat rate of 10 percent on the same items of income that I just told you that the foreign corporation was taxed 15 percent on; in other words, dividends, interest, rent, salaries, wages, and all fixed or determinable annual payments, not including capital gain.

The CHAIRMAN. Why is he taxed 10 percent?

Mr. BEAMAN. Senator, I cannot go into that. Mr. Parker can tell you later on. I just want to explain to you what it is.

The CHAIRMAN. I just wanted to know what the reason advanced was for fixing that 10-percent rate.

Mr. BEAMAN. It seems to be obvious that the committee thought that was the fair rate.

Senator GEORGE. What is the present rate?

Mr. BEAMAN. The present rate is the rate applying to him under the normal tax and surtax, just like the resident individual, except that there is no tax on income from other than sources within the United States.

Senator GEORGE. Yes.

Mr. BEAMAN. Now, this 10-percent tax on nonresident alien individuals contemplated by the Ways and Means Committee will be collected in almost every instance by the withholding at the source, and again the Commissioner is given power, under regulations, to exempt these people from filing a return. They have no deductions against these items and so there is no particular need for a return if the withholding agent has done his duty and withheld and collected the tax.

Senator COUZENS. Is there any penalty on the agency if it does not collect the tax?

Mr. BEAMAN. Oh, yes; it is liable for the tax.

Senator COUZENS. How do you get service on him?

Mr. BEAMAN. If he has an office here you can get him.

The CHAIRMAN. If he does not have an office here, how do you get service on him?

Mr. BEAMAN. If he does not have an office here, the only thing you can do is to levy on the property that you can find here. The result is at the present time that there are a great deal of taxes from nonresident aliens that we are not getting. Practically about all we get is by withholding from the fellows not engaged in business here. At the present time the withholding rate in the case of the nonresident alien is 4 percent. Of course, this bill withholds at the same rate as the rate of our tax on him, namely, 10 percent.

Senator COUZENS. In other words, if he owned a lot of United States Government bonds we could not collect any surtax from him?

Mr. BEAMAN. You mean United States bonds?

Senator COUZENS. Yes.

Mr. BEAMAN. They, of course, are not subject to tax.

Senator COUZENS. Yes; but they are subject to surtax.

Mr. BEAMAN. Not in the hands of the nonresident alien.

Senator COUZENS. Not in the hands of the nonresident alien?

Mr. BEAMAN. No.

Senator CONNALLY. Why?

Mr. BEAMAN. Because the Congress said they could not be taxed.

Mr. KENT. There was a provision to that effect in the victory-loan law.

Senator GERRY. How can you collect the surtax on the nonresident?

Mr. BEAMAN. If he has any duty, under the law, to file a return and you assess the tax on the return, and if he has got any property, you distrain on the property. As I say, it does not work so well. In other words, we are not getting the tax, I am informed, out of these people that we ought to.

That is what I say, that it was one of the compelling reasons in the Ways and Means Committee of getting at least 10 percent out of the people that have no place of business here, getting at least 10 percent by withholding.

Senator GERRY. What I am getting at is what you would collect under the surtax is the amount of property that he has here.

Mr. BEAMAN. That is right.

Senator COUZENS. If he has a railroad bond there would be no way of withholding at the source; there is no way of collecting the tax.

Mr. BEAMAN. The railroad withholds the tax when he cashes the coupon.

Senator COUZENS. If it is a bearer bond?

Mr. BEAMAN. Everybody has to file a certificate when they cash a coupon.

Senator COUZENS. Even on the present bonds?

Mr. BEAMAN. Oh, yes. The bank will not take the coupon you deposit unless there is a certificate attached to it showing the ownership.

Senator GERRY. Do not the English collect the surtax on the nonresident alien, or the tax on the nonresident alien on the amount he spends?

Mr. BEAMAN. I do not know, sir. Does anybody know?

Mr. PARKER. What is your question again, Senator? Do not the English collect a tax on the nonresident alien? If he resides in the country more than a certain length of time on what he spends?

Senator GERRY. Yes.

Mr. PARKER. Yes; if he resides there. The nonresidents do not get any credit, of course, like the residents do in respect to the British corporate tax paid at the source. The residents, when they get a dividend from an English corporation, 22.5 percent being withheld at the source, get a credit for that against their tax.

Mr. BEAMAN. There is one further change.

Senator BARKLEY. What page are you on?

Mr. BEAMAN. I am not discussing any particular page, Senator. Under the present law the nonresident alien individual has a personal exemption of \$1,000, whether married or single. He has the credit for dependents only if he is a resident of a contiguous country, Canada or Mexico. This bill, in the first place, takes away the credit

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for dependents from the resident of Canada or Mexico. It keeps the personal exemption of \$1,000. The personal exemption can be used only as against the part of the net income attributable to compensation for personal services. If his income is from other sources than personal services he gets no personal exemption at all.

Now, that disposes of the changes, with one exception. You notice, as I said several times, that these foreign corporations and non-resident aliens, are taxable only on their net-income sources within the United States. The present law, in which this bill makes but one change of importance, lays down numerous rules to determine that, and under the present law one of those rules is this: Suppose a shareholder in a foreign corporation, whether that shareholder be an individual or another corporation, receives dividends from a foreign corporation which derives income from United States sources. The present law lays down the rule that if the foreign corporation paying the dividend derived for the 3-year period preceding more than 50 percent of its gross income from sources within the United States, then all the dividend it pays out shall be considered as income in the hands of the shareholders from sources within the United States.

For instance, suppose the foreign corporations under the present law derives 60 percent of its income from sources within the United States, and it declares out a \$100 dividend; the present law says the whole \$100 is income from sources within the United States.

That did not meet with the approval of the Ways and Means Committee, and they have changed it in two respects. First, they changed the 50 percent to 75 percent, so that a foreign corporation must derive 75 percent of its gross income over the 3-year period preceding, and then when it declares out the dividend there is considered as income from sources within the United States only the same proportion of the dividend as the income of the corporation from sources within the United States. In other words, if a foreign corporation gets 80 percent of its income from sources within the United States and declares out \$100 dividend, \$80 of that dividend is considered income from sources within the United States.

Senator CONNALLY. But if it is under 75 percent?

Mr. BEAMAN. Under 75 percent, that is not prorated.

Senator CONNALLY. That is not fair, is it?

Mr. BEAMAN. I am not arguing that.

Senator CONNALLY. I understand that. That is not just, it seems to me.

Senator COUZENS. Have you had any difficulty under the existing law where you collected the whole 100 percent?

Mr. BEAMAN. There have been, Senator, great complaints, and justly so. In fact, most of us feel there is very serious legal objection to doing it. Simply because a corporation makes 51 percent of its income from sources within the United States, to say the foreign stockholder is going to be taxed on the whole \$100 dividend he gets, when only \$51 of it came from the United States is, I think, very doubtful.

Senator COUZENS. How long has that been the law? It seems to be wholly inequitable.

Mr. BEAMAN. That has been the law for quite awhile; since 1921, I think. There have been great objections to it, and the objections have been getting louder and louder.

The CHAIRMAN. What is the view of the representatives of the Treasury?

Mr. BEAMAN. They are heartily in accord with this thing.

The CHAIRMAN. They are in accord with what the House did?

Mr. BEAMAN. I think so. Is that right, Mr. Kent?

Mr. KENT. In a general way. There may be one or two changes that we would want to suggest when the committee comes to consider the specific provisions of the bill. We are in favor of the general principles of this plan, largely for the reason that the collection of foreign taxes, taxes from nonresident alien individuals who are personally beyond our reach, has proven to be extremely difficult and rather ineffective from a revenue point of view. It does not work out uniformly. We have to rely largely upon the honesty or the willing cooperation of the nonresident individuals, and that is impossible to obtain in a great many cases. We believe that, taken as a whole, the plan which is set forth here will benefit the Government from a revenue point of view. We will get more money and we will get it more easily than we have been able to do under the present system..

The CHAIRMAN. You apply the same theory, then, that we apply, to reduce the rate in order to collect more revenue?

Mr. BEAMAN. That is right. I might say also that this plan corresponds, in a general way, while there are differences in detail, with the plan which other countries having an income-tax system have come to; that is, they do not in general rely upon returns as a method of collecting the taxes from nationals of other countries, particularly on investment income derived from the taxing country. They have relied mainly upon imposing a certain rate of tax and withholding that tax as far as possible at the source.

Mr. BEAMAN. May I say right in that connection, Senator, that it is not entirely a reduction in tax. In some cases it is an increase in tax.

Mr. KENT. Yes; that is true.

Mr. BEAMAN. For instance, in the case of a foreign corporation, engaged in business here, the bill puts a rate of 22.5 percent on it. Of course, that is an increase in the rate. The rate on foreign corporations not doing business or having an office is about the same as the present law.

In the case of a nonresident alien individual, those doing business here, this bill leaves them as they are now, subject to the normal and surtax. Those who are not engaged in business here, who are subject to this 10-percent flat rate, of course, if they are deriving a large income, would, under the present law, be subject to surtaxes. It is a lowering of the theoretical rate. As to whether or not it is a lowering of the actual rate, it may be, as to some particularly honest men who have been in the habit of filing returns and paying surtaxes, I think there is good ground for believing that it is, in effect, a raise on them. In fact, we withhold 10 percent on them rather than the present rate of 4 percent.

The CHAIRMAN. You say you are making it more liberal; you are raising the 50-percent proposition to 75 percent?



Mr. BEAMAN. That is just in one narrow provision.

Senator KING. You mentioned the foreign corporation. As you may know, in Mexico, for instance, most, if not all, of the Latin-American States have a provision where a foreign corporation may not operate within those countries. Take Chile, take Mexico. So what do the mining companies, big and little, who have an interest in Mexico do? What are the men compelled to do, particularly in Mexico, in view of that situation? They have got to organize a Mexican or Chilean corporation, then they have got to put all the stock, every share of it, in the possession of those respective governments, and the corporation here has to become a holding company, has to advance the money and the operations are conducted there. Now, what would you do in a case of that kind? All the dividends are declared in Mexico, but they are the result of capital which has been furnished by the foreign company here. The smelting companies and mining companies have, as it is required there, perhaps two or three corporations to operate a mine, and all the stocks of the corporations are deposited as collateral with the respective governments in which those corporations operate, and the holding company is in the United States. Supposing they declare a dividend there, what happens?

Mr. BEAMAN. The dividend comes to the holding company?

Senator KING. The dividend comes to the holding company.

Mr. BEAMAN. If it is included in the income they pay a tax according to the bill.

Senator KING. It would be practically confiscatory, would it not?

Mr. BEAMAN. I do not quite see why. Why is it confiscatory any more than if the holding company had a subsidiary in New Jersey?

Senator KING. Of course you have heavy taxes down there that you have to pay.

Mr. BEAMAN. They have a credit for foreign taxes. This bill does not disturb the present law in that respect.

If there are no further questions about the foreign corporations and nonresident alien individuals, there are two very narrow and restricted classes of corporations to which the bill gives only a 15 percent rate, instead of bringing them under the new plan, and they are, first, the corporations who are dealt with in section 251 of the present law and in this bill. The present law provides that a domestic corporation conducting an active trade or business in one of our possessions, say Puerto Rico, and gets 50 percent or more of its income from the conduct of that trade or business, it has passed the first examination for the purposes of coming under the provision. The second examination is: Did it derive 80 percent or more of its gross income from sources within that possession? If it does it is treated under the present law practically like the foreign corporation, namely, it is taxable only on its income from sources within the United States.

The CHAIRMAN. That is section 261?

Mr. BEAMAN. Section 251.

Senator BARKLEY. Page 189.

Mr. BEAMAN. Now, that kind of corporation did not seem to the Ways and Means Committee to be very well susceptible to treatment under the new plan. Therefore they have taken them out and given

them a 15 percent flat rate instead of dealing with them under the new plan.

The second class that the 15 percent flat rate was given to is the China Trade Act Corporation which, under the present law, was given a special exemption or credit, and I will be glad to explain it if you like. It is very complicated, but the situation is such, technically, that it seemed almost impossible to work out and bring them under the new bill. Therefore the committee recommended to give them a 15 percent flat rate. I will be glad to explain to you, if you desire, how it comes about, and what the trouble is.

Senator COUZENS. You might explain it. I would like to know about it.

Mr. BEAMAN. All right.

Senator CONNALLY. What do they pay now under the present rate?

Mr. BEAMAN. I will explain that.

Senator BARKLEY. The definitions there in sections 1, 2, and 3 are a little confusing. It pays 80 percent or more in the case of the citizens of the United States.

Mr. BEAMAN. We are only dealing now with the corporations. There is no change in the citizens. What I was saying, this refers to the corporations only.

Senator BARKLEY. "Gross income" means only gross income from sources within the United States?

Mr. BEAMAN. That is right.

Senator BARKLEY. It says:

If 80 percent or more of the gross income of such citizen or domestic corporation (computed without the benefit of this section), for the 3-year period immediately preceding the close of the taxable year (or for such part of such period immediately preceding the close of such taxable year as may be applicable) was derived from sources within a possession of the United States.

That seems to state here an identical condition, but you have got two different percentages there.

Mr. BEAMAN. As I say, in order to get to first base under section 251, Senator, you must get 50 percent of your income from the active conduct of the trade or business, not from holding investments in one thing and another, but the active conduct of the trade or business. Now, when you get to first base doing that then to get further you have got to prove that 80 percent of your gross income from all sources came from sources within that possession. For instance, a corporation investment trust in New York which got 100 percent of its income from Puerto Rico through investments in Puerto Rican corporations, which did nothing but sit in New York and clipped the coupons and cashed the dividend checks, is not entitled to this relief, because it has not gotten to first base to get 50 percent of its income from there, in fact, none of the income came from the conduct of its business there.

Senator BARKLEY. The 80 percent does not apply unless numbers (2) and (3) apply?

Mr. BEAMAN. That is right. Now, as to these China Trade Act Corporations. Under the present law the rate of tax on them is the same as any corporation, on their net income, but the law provides that they are given as a special credit against that net income an amount which equals the same proportion of their net income from

China as the par value of stock owned by a certain class of people. I will come to that later, if you want me to.

To get the idea through your head, as the proportion of the blue-eyed stockholders bears to the entire amount of stock. For instance, if the corporation's net income was \$100, and \$80 of that came from sources within China, you now look and find that the blue-eyed stockholders are 50 percent of all the stockholders, therefore, they get a credit against the \$100 of 50 percent of the amount of the income from that source, which is \$40. So they get the credit against the \$100 of \$40, which we will assume is taxed at the 15-percent rate, that results in a reduction in tax of \$6. Is that clear? I will say it again.

Senator COUZENS. What about the brown-eyed stockholders?

Mr. BEAMAN. The law says they get a credit for that same proportion of \$80, namely, income sources within China, as the par value of the stock owned by the blue-eyed stockholders bears to the whole.

The CHAIRMAN. Where do you get the expression "blue-eyed"?

Mr. BEAMAN. There is a whole list of them here.

The CHAIRMAN. Where do you get the term "blue-eyed stockholders"?

Mr. BEAMAN. That is just descriptive.

Senator CONNALLY. Are these stockholders living within the United States? What makes them blue-eyed?

Mr. BEAMAN. I want you to get the effect first. I will come to that a little later. That is the way the credit is computed, if you follow me. There is a tax saving of \$6.

Now, the law further provides that in order to get that \$6 tax saving the corporation must distribute to these same blue-eyed stockholders a special dividend over and on top of all of the dividends equal to the \$6, or if it distributes this special dividend to the blue-eyed stockholders to the extent of \$3 then the corporation only gets a \$3 tax saving.

Senator CONNALLY. In other words, they give back to the blue-eyed stockholders what they save on the tax by reason of the blue-eyed ones being in favor of the tax?

Mr. BEAMAN. That is right. Now, it seems apparent from that set-up that the new plan does not fit it, because how much of the tax was saved depends on how many dividends were distributed, and whether you should count the special dividend in that instance. It just seems perfectly hopeless to try to think that through. Inasmuch as the amount of revenue, derived from these corporations anyway was not very great, it did not seem to the committee it was wise to complicate the law further by applying the new plan, so they gave them a 15-percent flat rate. If the corporation or the stockholders are blue-eyed, and all the income sources are in China they do not pay any tax at all under the present law. I think the total amount of money collected from that source is less than \$200,000. One hundred and eighty thousand dollars is my recollection of the total.

Now, Senator, you wanted to know who the blue-eyed stockholders are:

Persons resident in China, the United States, or possessions of the United States, and (2) individual citizens of the United States or China, wherever resident.

Senator BARKLEY. Where is that?

Mr. BEAMAN. Page 194. That is the present law.

Senator CONNALLY. That gets pretty nearly everybody, does it not?

Mr. BEAMAN. Very much so. It does not get a Frenchman living in Paris.

Senator GERRY. What page is this?

Mr. BEAMAN. Page 194 is the list of blue-eyed stockholders.

I think that completes everything in title I, Senator, that needs to be explained at this time. Mr. Parker already called attention to section 351 of the present law.

Senator CONNALLY. Under this law a blue-eyed person, either a German, Frenchman, or anybody, if he lives in China and owns stock, he gets the benefit of this exemption?

Mr. BEAMAN. The corporation gets it.

Senator CONNALLY. The corporation gets it; then it is rebated back to him? It may be an Englishman or anybody else?

Mr. BEAMAN. As I say, the present law is set up so that the corporation does not pay much tax.

Senator BARKLEY. There is no change there anyway from the present law, is there?

Mr. BEAMAN. No; no change whatsoever.

Senator KING. I think we should keep in mind the reason why we give an apparent benefit privilege to these Chinese corporations if the stockholders are in the United States. The English, and all European nations were setting up corporations there and were getting a large amount of trade, and the Americans were not so advantaged, so we passed the law to encourage them, to protect American capital, Americans who made investments in China.

Senator BARKLEY. It is an effort to create another revenue for getting rid of some of our surplus products.

Senator KING. To encourage trade and commerce between the two countries, instead of having Great Britain and Germany getting all the foreign trade in the Orient. We wanted to get a part of it, and this Chinese Trading Act was the outgrowth of the investigations which were made.

Mr. BEAMAN. Title II of the bill, on page 228, deals with the capital-stock and excess-profits taxes. It has reduced the rate of the present capital-stock tax.

The CHAIRMAN. Mr. Parker referred to that the other day.

Mr. BEAMAN. Then I do not need to repeat it now.

The CHAIRMAN. I think he explained that the other day.

Mr. HELVERING. Mr. Chairman, if the committee would like to take this suggestion, I would like to have the statistician of the Treasury discuss this survey on this tax before we start on the windfall and the other amendments.

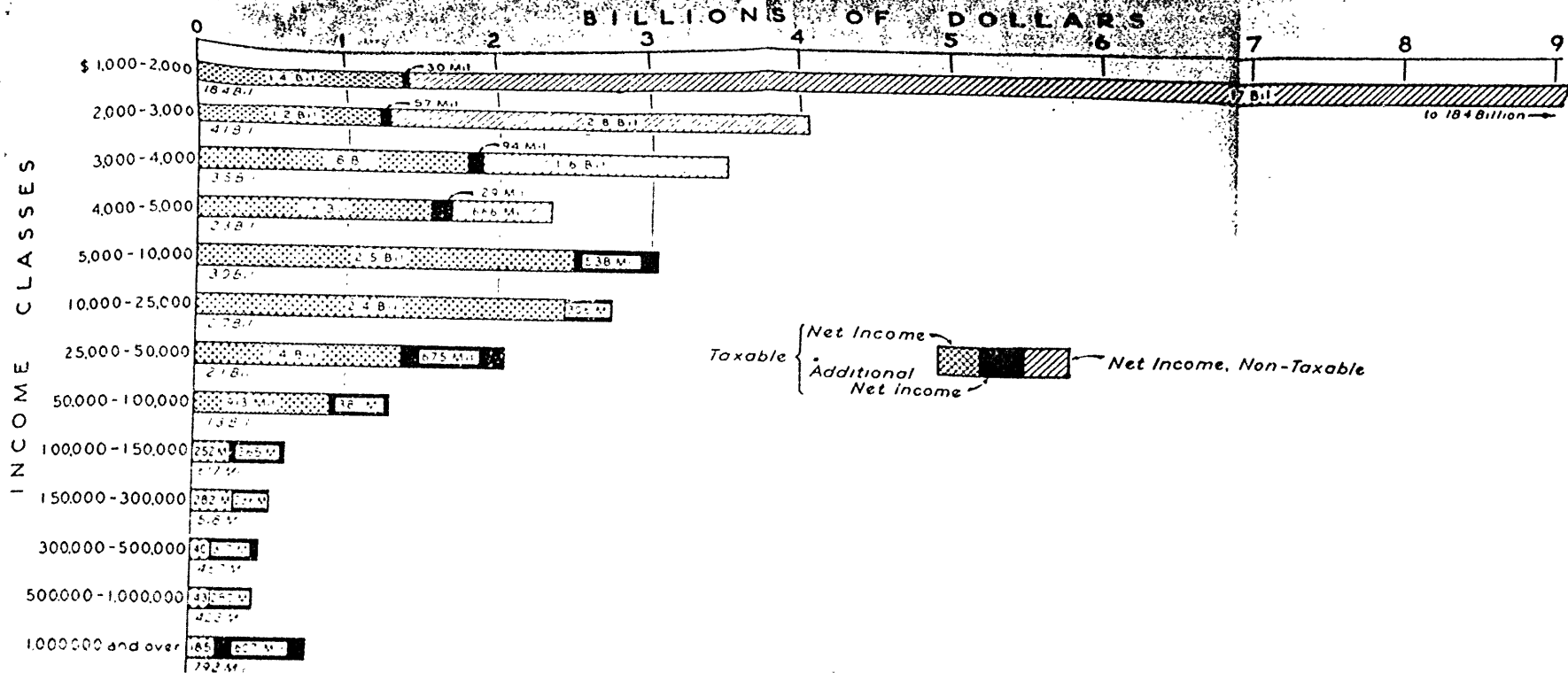
The CHAIRMAN. Yes; let us take up one subject at a time.

Mr. McLEOD. We are going to distribute small copies of this chart and the statistical data which underlies the basis of the estimates.

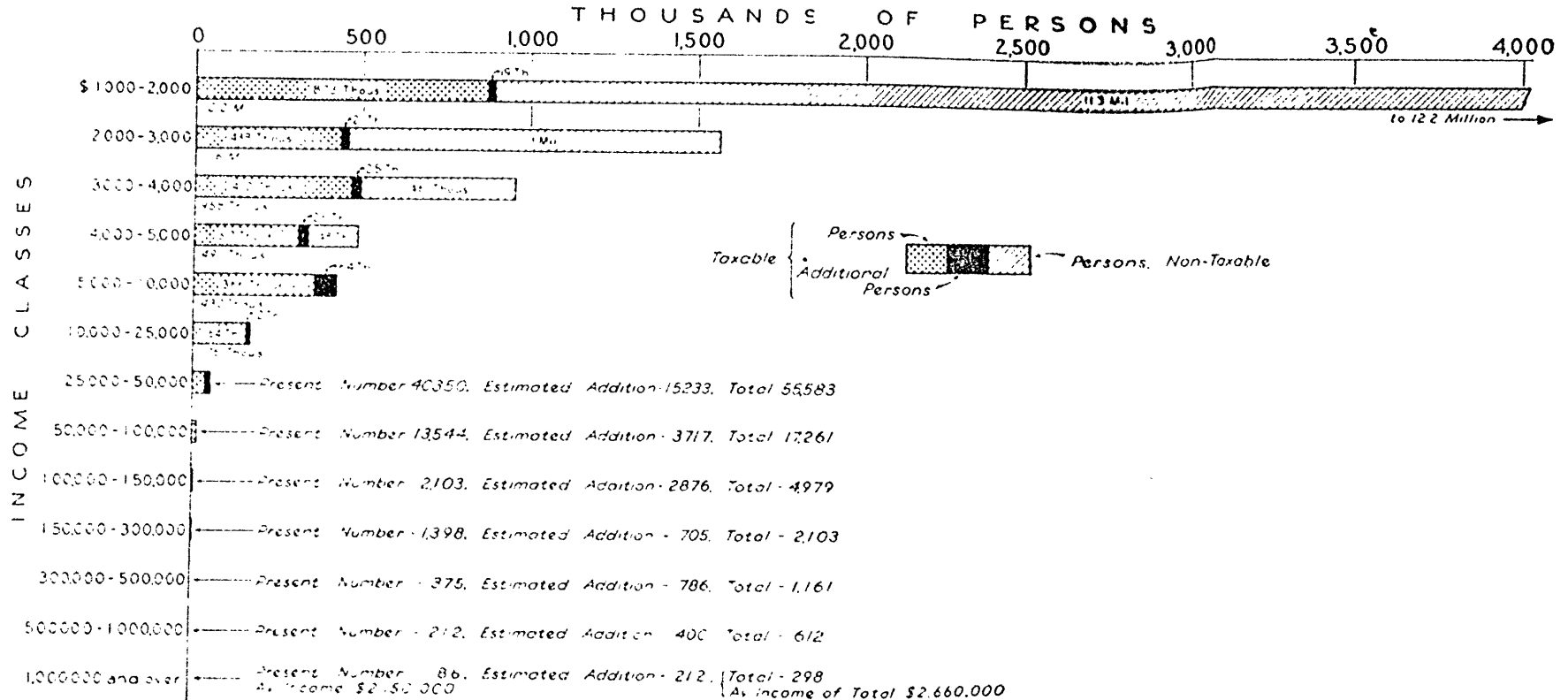
The CHAIRMAN. All right.

(The chart and table referred to is as follows:)

# DISTRIBUTION OF INDIVIDUAL NET INCOME



# NUMBER OF INDIVIDUALS IN EACH CLASS



\*Estimated increases if all corporate earnings were distributed

Note in income classes less than \$5,000 only, there are additional "non-taxable" persons or net income which are not shown

*Estimated number of individuals and distribution of individual net income by net-income classes, calendar year 1936*

Net income classes (thousand dollars)	Number of individuals				
	Taxable under present law	Additional taxable <sup>1</sup>	Nontaxable under present law	Additional nontaxable <sup>1</sup>	Grand total
1-2.....	873,000	18,772	11,312,228	44,000	12,248,000
2-3.....	438,000	21,206	1,110,794	44,000	1,614,000
3-4.....	472,000	24,830	461,170	32,000	990,000
4-5.....	317,000	26,494	147,506	21,000	512,000
5-10.....	365,711	63,868	-----	-----	429,579
10-25.....	163,989	12,203	-----	-----	176,192
25-50.....	40,350	15,233	-----	-----	55,583
50-100.....	13,644	3,717	-----	-----	17,261
100-150.....	2,103	2,876	-----	-----	4,979
150-300.....	1,398	705	-----	-----	2,103
300-500.....	375	786	-----	-----	1,161
500-1,000.....	212	400	-----	-----	612
1,000 and over.....	86	212	-----	-----	298
Total.....	2,687,768	191,302	13,031,698	141,000	16,051,768

Net income classes (thousand dollars)	Net income (in millions of dollars)				
	Taxable under present law	Additional taxable <sup>1</sup>	Nontaxable under present law	Additional nontaxable <sup>1</sup>	Grand total
1-2.....	1,379	30	16,968	66	18,443
2-3.....	1,215	57	2,778	110	4,160
3-4.....	1,787	94	1,614	112	3,607
4-5.....	1,650	129	666	95	2,440
5-10.....	2,499	538	-----	-----	3,037
10-25.....	2,445	306	-----	-----	2,751
25-50.....	1,371	675	-----	-----	2,046
50-100.....	913	381	-----	-----	1,294
100-150.....	252	365	-----	-----	617
150-300.....	282	236	-----	-----	518
300-500.....	140	317	-----	-----	457
500-1,000.....	143	280	-----	-----	423
1,000 and over.....	185	607	-----	-----	792
Total.....	14,101	4,016	22,026	383	40,585

<sup>1</sup> Assuming that all corporate earnings were distributed.

<sup>2</sup> Exclusive of \$370,000,000, the estimated additional amount which would be distributed to tax-exempt institutions, etc.

The CHAIRMAN. All right, Mr. McLeod, you may proceed.

Mr. McLEOD. Last October and November, when we prepared the Budget estimate we estimated the amount of individual income and the amount of corporate income for the calendar year 1936. At that time we estimated a tax liability of \$1,132,000,000 on the basis of 1936 calendar incomes, of which \$964,000,000 was from the corporate tax, \$163,000,000 was from the capital surtax and \$5,000,000 was from the excess-profits tax.

Now, under this bill we propose to repeal each of those taxes and substitute a tax which would be based upon the undistributed net income of the corporations.

The question arises as to how, when we repeal \$1,132,000,000 of revenue through those taxes, we could raise that amount of money and \$620,000,000 additional revenue. This chart points out how this would result, assuming 100-percent distribution of 1936 corporate earnings to individual stockholders.

Now, the small chart which you have there, which is a duplicate of this large chart—

The CHAIRMAN (interrupting). Mr. McLeod, before you state that, how near did your estimate come this last year on the various incomes?

Mr. McLEOD. Well, last July we made our last estimate of individual and corporate income for the calendar year 1935. March of this year is the first indication we get in the form of collections as to the accuracy of those estimates, and we collected about 1 percent more than we estimated, that is, the individual income taxes and corporate taxes were 1 percent more than estimated.

The CHAIRMAN. That is about as close an estimate as you have experience on any of these tax proposals?

Mr. McLEOD. I think it is. It came out very closely this year.

Senator KING. I did not quite understand you, Mr. McLeod. Is it your proposal that we collect \$1,300,000,000, approximately, from corporate and individual income taxes for the past and six-hundred-and-some-odd million in addition, so your proposal is that we collect practically \$2,000,000,000?

Mr. McLEOD. My proposal is this, that we have estimated as a tax liability for the calendar year 1936, \$1,132,000,000 from corporate taxes.

Senator BARKLEY. Under the present law?

Mr. McLEOD. Under the present law. That would apply to corporate taxes, capital-stock taxes, and excess-profits taxes. Now, in addition to that we estimate \$1,153,000,000 from the individual income taxes. We propose to repeal all the corporate taxes and through this proposal, through the proposed bill, raise \$1,132,000,000 that we are giving away and \$620,000,000 additional revenue.

On this chart we are pointing out how that would occur, assuming that 100 percent of the corporate earnings in 1936 were distributed to the individual shareholders in that year.

Now, the small chart which you have there is a duplicate of this. It is not in colors, but the yellow in this legend corresponds to the black on that small chart, the blue corresponds to the double hatching on the left, which represents the taxable net income, and the red, which corresponds to the single hatching on the small chart, represents the nontaxable net income. Nontaxable net income is not involved in the estimate.

Senator BARKLEY. Let me ask you there: Taking the \$1,132,000,000 which you now get, plus \$620,000,000, makes a total of \$1,752,000,000 that you have got to raise. Is that out of the corporation tax or out of all of the taxes included in this bill?

Mr. McLEOD. That is out of the corporate taxes, exclusive of all other taxes.

Senator BARKLEY. Exclusive of windfall, excess-profits taxes or anything else?

Mr. McLEOD. That is correct.

Senator KING. That does not include the supposed increased individual income tax?

Mr. McLEOD. The only increase in the individual income tax would be that attributable to the changes in the rates under the 1935 act. Individual income-tax liability is estimated at \$1,153,-



000,000 for the calendar year 1936 and this figure is exclusive of the estimated increase under this bill.

Senator KING. You are assuming that the individuals would receive a larger income?

Mr. McLEOD. That is right.

Senator KING. You are assuming that under this bill because of the dividends which would be distributed to them.

Mr. McLEOD. That is correct.

Senator KING. Therefore you are assuming that the income tax for the next year will be larger than the income tax under the present laws?

Mr. McLEOD. That is correct. I might summarize that by saying that we estimate, if this became effective and if 100 percent of the corporate earnings were distributed, that individuals would receive about \$4,768,000,000 in additional income in the form of earnings from the corporate earnings which we estimate would be withheld from the shareholder in the calendar year 1936, and that is the basis of the additional revenue. Of that \$4,768,000,000 we estimate that \$4,015,000,000 would become taxable in the hands of the individual shareholders.

Senator LA FOLLETTE. Under existing law?

Mr. McLEOD. That is correct, under existing law.

Senator LA FOLLETTE. In other words, assuming 100 percent distribution, if you apply the present normal and surtaxes to that 100 percent distribution you expect to get somewhere around \$625,000,000 of additional taxes?

Mr. McLEOD. Of additional taxes over what we estimate under the present law, that is correct.

Senator KING. As a predicate for those estimates you would actually know the number of stockholders in all of the corporations which you say have these large earnings to distribute, and then ascertain the holdings of the individual stockholders, so that you could determine whether or not they fall under the surtax provisions of the existing law, or whether they are confined only to the normal tax, or whether they are taxable at all?

Mr. McLEOD. I was coming to that. We have a record every year of how dividends fall in the individual-income brackets. We know how much net cash dividends were paid out to the stockholders—to the individuals. We also have a record for the latest available year of the number of individuals who actually received dividends and the income bracket in which they fell.

Now, there is nothing new in making this estimate. The only new factor is that which is involved in estimating the total amount of corporate income. Each year when we prepare the Budget estimate we have to estimate the various sources of income to individuals, wages, salaries, rent, royalties, dividends, capital gains, and so forth. So the only new problem that is involved here is one of magnitude.

Senator GERRY. Do you know how much you would get from each class of corporation—by that I mean small corporations of under \$10,000—how much they pay out in dividends, or how much they would pay out?

Mr. McLEOD. We know the net income by income classes of the various corporations, running from the small brackets up to the

highest brackets, and from that we can estimate the total amount of net income and the probable amounts that would be distributed. We do not know just exactly how much dividend is distributed by corporations in each of the net-income classes, but we know how much dividend is distributed by all the corporations, and from our knowledge of the distribution of these dividends into individual shareholders' hands we have a pretty good picture of how this bill would work out.

Senator GERRY. As to these corporations that come under this \$10,000 class, have you estimated how much they would distribute in income, the small corporations?

Mr. McLEOD. If there were no such bill as this bill?

Senator GERRY. No; under this bill.

Mr. McLEOD. We have made various assumptions as to amounts distributed. This particular illustration is based on 100-percent distribution by all corporations, whether large, small, or intermediate.

Senator GERRY. I understand that. I mean, have you gone further and broken it up so that you know how much each class would distribute? In other words, you take the small corporation that you are talking about here, which you have got in the bill, of \$10,000. Do you know how much that distributes as compared with other corporations?

Mr. McLEOD. We do not know exactly how much they distribute.

Senator GERRY. Have you got any approximate estimate of how much they distribute?

Mr. McLEOD. That varies from year to year.

Senator GERRY. I mean, on the same basis that you have worked this out. You must have a basis to work this out for all of them.

Mr. McLEOD. But we did not work it out necessarily by the size of each corporation.

Senator GERRY. Well then, you haven't got any figures on that, showing that the amount of distribution by small corporations is a certain amount?

Mr. McLEOD. We do not know exactly how much they distribute.

Senator GERRY. Have you got any approximate estimate on that?

Mr. McLEOD. On the small corporations?

Senator GERRY. Yes.

Mr. McLEOD. No; we have not.

Senator GERRY. Do you know how many stockholders the small corporation has?

Mr. McLEOD. I do not know that.

Senator GERRY. Have you got any figures on that at all, that is, as to the different grades, the different sets?

Mr. McLEOD. As to the percentage that the various-sized corporations distribute?

Senator GERRY. Yes; and how much they distribute.

Mr. McLEOD. We do not have that for each size of corporation, because we did not believe it was necessary in making the estimate to have that material.

Senator COUZENS. If you state a different rate for the \$10,000 group, don't you have to have an estimate for that?

Mr. McLEOD. We have provided a special set of rates for corporations with net incomes under \$10,000.

Senator COUZENS. If you have no figures as to the distribution of those \$10,000 corporations, how do you fix the estimate of revenue in that group?

Mr. McLEOD. Oh, yes; we have the amount of the net income by those corporations under \$10,000.

Senator COUZENS. That is what the Senator from Rhode Island is trying to get.

Senator GERRY. That is what I am trying to get.

Mr. McLEOD. I thought you were emphasizing how much dividends they distributed.

Senator GERRY. I am trying to find out how much they had and how much they would distribute under this bill, in the different classes.

Mr. McLEOD. Yes; we have a table which, I believe, was placed in the hearings of the House Ways and Means Committee, which shows by various brackets the amount of income and the number of corporations in those brackets. That has been released.

Senator GERRY. And the amount which you distribute under this?

Senator LA FOLLETTE. I assume it is 100 percent.

Senator GERRY. I am taking his table. The Senator from Michigan stated what I had in mind.

I would like to ask another question: Do you know how many stockholders there are in those different groups?

Mr. McLEOD. We do not know how many stockholders there are in those different groups, we only know how many individuals received dividends, by income brackets, from all corporations.

Senator KING. As I understand, you are predicating your figures upon the assumption that there will be 100 percent distribution of dividends. Now, supposing that many of these corporations would retain, for expansion of business or other legitimate purposes, say, 10, 15, 20, 30, or 40 percent of their net income, then the amount which you say would be received would, upon the theory that the 100 percent is distributed, not be accurate, would it?

Mr. McLEOD. The amount that would be received by the individual stockholders would, of course, be less, but we have rates adjusted on the amounts retained, that is, the corporate rates which the corporation would pay based upon the amount it retained, and we know upon the basis of the amounts that would be distributed under those percentages of retention what the tax would be to the individual stockholder. Up to 30-percent retention there is very little difference in revenue. Above 30 percent there is considerable increase in revenue to the Federal Government.

Senator GEORGE. In other words, the corporate rates on the retention you figure will get you the same revenue. In one instance you get part of it out of the corporation, whereas, when there is 100-percent distribution, you get it all out of the individual stockholders?

Mr. McLEOD. That is correct.

Senator LA FOLLETTE. Mr. McLeod, as I understand, what really happens is that by subjecting these corporate profits to taxes, assuming 100-percent distribution in the hands of the individuals, you get about \$625,000,000 of additional revenue as the result of stopping the avoidance of surtaxes and applying the normal tax to dividends?

Mr. McLEOD. That is right. In other words, most of the revenue that would result under this plan would come from the higher surtax brackets, which I will point out later on this chart.

Senator LA FOLLETTE. Taking the amount that would be taxable under existing law, which I understood you to say was about \$4,015,000,000, what percentage of those corporate profits would fall into the hands of or be distributed into the hands of individual income-tax payers who now pay in excess of 16 percent?

Mr. McLEOD. I am going to present another chart to point that out.

Senator LA FOLLETTE. I do not wish to interrupt your chain of thought.

Mr. McLEOD. I think it would be clearer in the form of another chart.

Senator LA FOLLETTE. Very well.

The CHAIRMAN. You may proceed.

Mr. McLEOD. Now, the blue section of the upper deck of the chart, this being the income class, and the horizontal bars representing the amounts of net income in billions of dollars, in the blue section of the chart are the amounts of income subject to tax under present law which we have estimated for the 1937 Budget. The blue section represents the additional income, net income, which would fall in the various brackets as the result of this proposed bill.

Mr. PARKER. No; the yellow.

Mr. McLEOD. The yellow, rather.

Senator LA FOLLETTE. The black on this small chart.

The CHAIRMAN. You mean the yellow corresponds to the black?

Mr. McLEOD. The yellow corresponds to the black on your chart. Now, the red section merely represents individuals having net incomes which are not taxable under present law because of personal exemptions, credit, and so forth.

Now, as the result of this proposed bill, assuming 100-percent distribution, we estimate, for example, in the first bar, \$1,000 to \$2,000, one and four-tenths billion dollars of net income and only \$30,000,000 additional taxable income as the result of the increased distribution of dividends.

In the next bar we estimate one and two-tenths billions under present law.

Senator LA FOLLETTE. That is \$2,000 to \$3,000?

Mr. McLEOD. That is right, in the class of \$2,000 to \$3,000. \$57,000,000 of additional income would become taxable as the result of the increase in dividend distribution.

I might say that the lower section of the chart, which has the same income class gradation, shows the number of individuals who would be taxable under present law as to those various brackets, and the additional number of persons who would become taxable as the result of the increase in the dividend distribution.

For example, in the first bar—\$1,000 to \$2,000—we estimate, under present law, there would be 873,000 individuals taxable. As the result of the proposal we estimate only 19,000 additional individuals would become taxable in that income class.

In the second bar corresponding to the \$2,000 to \$3,000 income, we estimate 438,000 individuals would be taxable under the present law, and under the proposal there would be 21,000 additional taxpayers.

Senator COUZENS. That is represented by the red, is it?

Mr. McLEOD. That is represented by the yellow. The yellow represents the additional, and the red represents nontaxable individuals, nontaxable income.

Now, in the next class, \$3,000 to \$4,000, we estimate 1.8 billion dollars of net income taxable under present law, or 472,000 individuals. As the result of the proposed bill there would be \$94,000,000 additional taxable income in that class, and that would be represented by 25,000 additional taxpayers.

In the next class, \$4,000 to \$5,000, under present law there was 1.6 billion dollars estimated as taxable income, and \$129,000,000 additional income as the result of the proposal. The number of individuals would be 317,000 under present law, and only 26,000 additional taxable persons.

In the next bracket we are getting into the surtax bracket, \$5,000 to \$10,000. There was estimated, under the present law, 2.5 billion dollars. Under the proposal there would be \$538,000,000 additional taxable income, and the number of persons involved would be 366,000 under the present law and 64,000 additional persons. Now, the additional amounts begin to get considerably larger, because that is where you begin to get your dividends in volume.

In the next bracket, people having an income of \$10,000 to \$25,000, there was 2.4 billion dollars estimated under the present law and \$306,000,000 additional taxable income. The number of persons involved in the \$10,000 to \$25,000 class are 164,000 under the present law and 12,000 additional persons under the proposed bill.

In the next bracket, \$25,000 to \$50,000, there was estimated 1.4 billion dollars of taxable income under the present law, and \$675,000,000 additional taxable income as the result of the proposal. In the lower brackets the number of persons becomes so small that we printed it out. Under the present law there would be taxable 40,350 persons and an estimated additional number of 15,233.

In the next bracket, \$50,000 to \$100,000, there was estimated \$913,000,000 taxable income under the present law and \$381,000,000 additional as the result of the proposed plan. The number of persons involved under the present law are 13,544, and an estimated additional number of 3,717 would become taxable.

In the next bracket, \$100,000 to \$150,000, there was estimated \$252,000,000 taxable income under the present law and \$365,000,000 of additional income under the proposed plan. The number of persons get smaller as you go down, and there would be estimated under the present law, 2,103 persons; and an additional number of 2,876 would become taxable.

In the next bracket \$150,00 to \$300,000, there was an estimated income of \$282,000,000 under the present law and \$236,000,00 of additional income under the proposed plan. In other words, the additional income in that bracket gets pretty close to the present income. The number of persons are 1,398 under the present law and an additional number of 705 under the proposed plan.

In the bracket \$300,000 to \$500,000, under the present law there was estimated \$140,000,000 of taxable income and an increase in taxable income of \$317,000,000 under this proposal. In other words, the additional income is considerably in excess of the present income. In that particular class the number of persons under the present law;

in the \$300,000 to \$500,000 class, is 375 and the estimated additional number is 786, under the proposed plan.

The next class is \$500,000 to \$1,000,000.

The CHAIRMAN. May I ask right there—you have got a larger number of additional persons in the \$300,000 to \$500,000 bracket than you have in the \$150,000 to \$300,000, because in the \$300,000 to \$500,000 you have 786 and in the \$150,000 to \$300,000 you have 705.

Mr. McLEOD. That is correct.

In the next class, \$500,000 to \$1,000,000, we estimated \$143,000,000 of income under the present law and \$280,000,000 of additional income in the proposal, and the number of persons estimated under present law are 212, and the additional number are estimated at 400.

Senator BARKLEY. Following this little chart, I do not see where you set out the additional taxable income.

Mr. McLEOD. The yellow bar, which, in your chart, is black.

Senator BARKLEY. Are you referring to the top chart or the bottom now?

Mr. McLEOD. I have been shifting by brackets. I first referred to the top chart and then referred to the corresponding income class below, to show the number of people involved.

Senator KING. Which one are you describing now?

Mr. McLEOD. I just discussed the \$500,000 to \$1,000,000 class. You will notice in the upper deck there is \$143,000,000 of income, and estimated as the result of the proposal \$280,000,000 of additional income. That will be shown by the heavy black section in your chart.

Senator BARKLEY. Making a total of \$423,000,000?

Mr. McLEOD. That is correct. Now, if you go down to that same income class in the lower deck on the chart—that is, \$500,000 to \$1,000,000—you will notice written out the present number of 212 taxable persons in that class—that is, under the present law—and as the result of the proposed distribution we estimated an additional number of persons of 400, or a total of 612 persons.

Now, in the last group, \$1,000,000 and over, under the present law there was estimated \$185,000,000—that is, the last income class in the upper deck—and \$607,000,000 of additional income under the proposed distribution. That, you will notice, is considerably in excess of the amount of income estimated under present law. Now, in the lower deck, the last income class, \$1,000,000 and over, there was estimated, under present law, 86 persons, and under the proposal an additional number of 212, or a total of 298.

Now, I will explain what I believe is the significant thing this chart demonstrates. We have estimated that if all corporate earnings were distributed in the calendar year 1936, there would result about \$4,015,000,000 of additional taxable individual income and that 191,302 additional persons would become taxable. The major reason for the larger increase in revenue is because an individual in this class of \$25,000 to \$50,000, we will say, has \$25,000 of income, of which \$15,000 was dividends; and if the dividends should be doubled on the securities he is holding, he would receive \$15,000; that would take him up to the \$50,000-income class. Now, he would not be quite out of this bracket; but if we say he got \$25,000 additional dividends, he would move from this bracket of \$25,000 to \$50,000 into

\$50,000 to \$100,000. That means his surtax jumps considerably, so that the average tax on the additional amount of income distributed results in a large increase in revenue.

That is especially true when you get up into the higher classes where the surtax rates are high and where the majority of the people in those classes receive their income in the form of dividends.

Take this group of \$1,000,000 and over—today we estimate they will receive \$185,000,000 of income. Now, most of that will be in the form of dividends. If they were to get all the dividends that would otherwise be retained in the corporations in which they have an interest, they would be paying on that additional amount \$607,000,000—about 70 percent. That surtax is many times the rate of 16 percent which they would be paying on the \$607,000,000, if it were not distributed.

Senator LA FOLLETTE. In other words, when you say "16 percent" you mean the average corporate tax under existing law that would be applied to this revenue which is now retained in corporations?

Mr. McLEOD. That is correct; the capital-stock, excess-profits, and income tax. In other words, there is \$670,000,000 retained by the corporation in the form of undistributed earnings that is not paid out; the stockholders are paying, in effect, 16 percent on that. If it flowed out to their individual income brackets they would be paying several times that rate in the form of a surtax rate on that portion of the corporate earnings.

Senator WALSH. I can understand how the individual number of persons paying additional taxes increases in every bracket from the \$1,000 bracket to \$1,000,000 and over, but I cannot quite understand why the number of additional nontaxable individuals increases in the bracket from \$1,000 to \$5,000.

Mr. McLEOD. The nontaxable?

Senator WALSH. Yes. The nontaxable persons increases in the \$1,000 to \$2,000 bracket, 44,000 persons; from \$2,000 to \$3,000, 44,000 persons; from \$3,000 to \$4,000, 32,000 persons; and in the bracket of \$4,000 to \$5,000 it increases 21,000 persons. Under that there is an increase in the nontaxable group.

Mr. McLEOD. Would you like me to explain that?

Senator WALSH. Yes; I would like to have you explain that as to why there is an increase in the nontaxable group. I supposed this distribution of income would make more taxable individuals.

Senator BARKLEY. It is not shown on the chart. What Senator Walsh has reference to is the table. From \$1,000 to \$2,000 you have nontaxable under the present 11,312,228, and under this new plan you propose to add 44,000 to that.

Senator WALSH. I thought you were reducing the number of nontaxables.

Mr. McLEOD. There are people who report a net income of less than \$1,000, and that appears in the statistics of income, although we do not include it here. Now, they receive some dividends. As the result of the increase in dividends they are moved up into a higher bracket, so they appear as nontaxable individuals in those particular brackets.

Senator WALSH. They are really not exempt from taxation, except they are moved up into the higher brackets, and in those brackets they are not taxable?

Mr. McLEOD. That is right; they are still nontaxable. They move into the higher bracket of income.

Senator WALSH. How much is the increase of the total number of taxable individuals as compared to the present law?

Mr. McLEOD. Under present law we estimate 2,687,768 taxable persons. As the result of this proposal there will be an increase of 191,302 persons.

Senator WALSH. And the additional nontaxable persons in these groups is 141,000?

Mr. McLEOD. That is correct.

Senator WALSH. So the difference between that number and the 191,000 represents an increase in individuals who become taxable under this plan?

Mr. McLEOD. No; the additional number of persons who become taxable under this plan are 191,302. The 141,000 merely represents people who are just shifted up. They get a higher income; but still, because of personal exemptions, they remain nontaxable.

Senator BLACK. What is the amount of increased taxable assets under the new plan?

Mr. McLEOD. Increased taxable income?

Senator BLACK. Yes.

Mr. McLEOD. \$4,015,000,000 would become taxable.

Senator BLACK. You figure you would get how much additional as compared to the present taxes?

Mr. McLEOD. We estimate we will get \$1,752,000,000 additional, but part of it is normal tax on dividends that is already being received. The \$1,752,000,000 does not come entirely out of the \$4,015,000,000, because the bill proposes to tax all dividends or subject them to the 4-percent normal tax.

Senator BLACK. That is the gross revenue, \$1,752,000,000?

Mr. McLEOD. That would be the additional revenue.

Senator BLACK. You figure we will get that much more in additional revenue?

Mr. McLEOD. No; we estimate we will get \$620,000,000 in additional revenue.

Senator BLACK. I understand.

Mr. McLEOD. Under the bill there will be \$623,000,000 additional revenue, because of another factor.

Senator BAILEY. Have you taken into account the losses from sales of stock?

Mr. McLEOD. Beg pardon?

Senator BAILEY. Have you taken into your calculations the losses upon sales of stock? Did you offset those losses to the increase in taxable income?

Mr. McLEOD. You mean the individuals would sell stock to avoid these taxes.

Senator BAILEY. Take a man there who would be in the \$100,000 group—he would be squeezed out into that yellow strip of \$365,000,000, which becomes taxable at a very high rate; it no longer pays him to hold the stock; the taxes would be so high that he would convert it to bonds. Now, when he throws the stock on the market, it goes down, and somebody takes a loss, probably everybody who has got stock. Then take a man has who got stock in a corporation that



has money, that has a big surplus; compare him with the man who has got stock in a corporation that owes money; the stock in the corporation that owes money is taxable at a different rate than the stock in the corporation that does not owe any money; there may be a transfer there, a sale on one hand and a purchase on the other, but a loss will be taken, in my judgment. Now, have you taken into your calculation the losses, say, this year, that will occur from the adoption of this act, this tax system—the losses in the holdings of stock? This whole thing is based on the stock.

Mr. McLEOD. That is correct. The losses, I would say, on the average, would be insignificant.

Senator BAILEY. You do not think that that would cause a sale of stock?

Mr. McLEOD. It might cause a sale of stock, but the sale of stock today, at the present market, would result, on the average, at considerable profit.

Senator BAILEY. It would at the present market, but suppose I begin selling and the market should break?

Mr. McLEOD. Of course, if you assume that this proposal would result in a considerable decline in general business activity, that is a different proposition.

Senator BAILEY. Why would not it result in a decline if I were to convert my holdings into United States bonds at  $2\frac{1}{2}$  or 3 percent? I would get much less than that, because you would get me out into these high brackets where I would pay 72 or 75 percent.

Mr. McLEOD. Of course, that is continuously going on all the time to some extent.

Senator BAILEY. That is not going on now like it would go on under this, because this is not the law now. I am not opposing your plan; I just want to know how you would explain it.

Mr. McLEOD. I would like to explain that in this way: The wholly tax-exempt securities that can be purchased would be State and municipal. For the past 5 years there has been practically no increase in the amount of those issues. Moreover, the yield on the short-term Government bonds is low. For instance, 6 months' Treasury bills are selling at one-eighth of 1 percent and the 5-year notes are selling from  $3\frac{1}{8}$  to  $3\frac{3}{8}$ .

Senator BAILEY. The yield on the long-term paper is greater.

Mr. McLEOD. But those securities are not exempt from surtaxes.

Senator BAILEY. The yield on the long-term bonds is now under the surtax plan, and under this schedule they fall right into the dividend brackets.

Senator COUZENS. In other words, a stockholder that sells stock that is yielding 4 or 5 percent to buy Government paper that yields  $2\frac{7}{8}$  loses an enormous amount of money because of the surtax applied to the Government bonds, so there would be no purpose, Senator Bailey, in doing what you suggest.

Senator BAILEY. If the rate is the same I will agree with you.

Senator COUZENS. The rate would be substantially the same.

Senator BARKLEY. He would lose more in income than he would save in taxes.

Mr. McLEOD. In other words, if that were done in wholesale lots, the yield would change considerably. If there is one share of stock

sold by an individual in the higher brackets and someone is buying that, the income does not disappear unless the total income declines, which would mean the total corporate earnings would decline. You might get some slight shifting to lower brackets, but not enough to make a considerable change in the revenue picture.

Senator BAILEY. Take the State or municipal bonds, the Government pays such low rates that it is not worth while buying the State, municipal, county, or local bonds.

Mr. McLEOD. The average rate on municipals today is in the neighborhood of  $4\frac{1}{2}$  percent on bonds which have been outstanding for a long period. New issues are as low as  $2\frac{1}{2}$  in some instances, but not higher than 4. The tax that the individual pays as the result of the tax on capital gains in those higher brackets would no doubt more than offset the advantage he would try to obtain through the sale of securities. The tax on capital gains would probably boost him into a still higher bracket than he is now in. If he sold securities that he bought within a year he would pay a tax on 100 percent of his gain. If he bought them 2 years ago he would pay on 80 percent. If he bought them 5 years ago he would pay on 60 percent of their value. You have to hold them over 10 years to pay a tax of less than 30 percent. So that provision is enough to stop any considerable amount of liquidation.

Mr. HAAS. There is another point that I would like to take up, and that is this. I am inclined to believe that there might be an elevating influence on the stock market for these reasons:

The first is you will have a stock selling on the stock exchange that is earning, say, \$7 and that is not being distributed, and you have stock in some corporation operating the same industry, assume, as a hypothetical illustration, that is earning the same amount, but distributes \$6 of the seven; the earnings which are distributed are always valued in the market higher than earnings not distributed, so as dividends go up you tend to get a higher valuation on the earnings of the company.

Senator BAILEY. You will, provided you cannot find another investment somewhere else. Say he is going to get 7 percent but that is all going to be taxed, he is going to get out of the way of that if he can.

Mr. HAAS. If there is a place for him to go to.

Senator BAILEY. All right.

Mr. HAAS. And the other thing is that the more dividends that a corporation distributes the less this corporation tax will be, and therefore the higher its earnings will be, the earnings actually will be higher, therefore the market values of the stock will be higher. The only place they can go to theoretically would be to State and municipal bonds.

Senator BAILEY. How about real estate?

Mr. HAAS. The only thing I could answer there, Senator, is under the present schedule you have this experience, you have high rates in these upper brackets. What has been the experience to date? There is an equilibrium point that you can reach where it does not pay you to shift any more.

Senator BAILEY. I was wondering whether you have arrived at an equilibrium point. Now, look at the map there and see what happens

in those yellow places. You squeeze a great deal of income out into higher brackets.

Mr. HAAS. If he makes earnings on real estate, Senator, he will pay the same rate.

Senator CONNALLY. If he did that he would have to buy lower income stuff.

Mr. McLEOD. We have estimated, you see, in consideration of these factors, under the 1935 act only 86 people with incomes above \$1,000,000. Now, in 1929 there were 513 of those individuals. We have estimated an increase of 212. We will suppose it does not quite reach 212—that may be, but we believe this estimate is conservative, it may go above that—it would mean an increase in returns here somewhere, and here [indicating] it might be still lower. That is, a man cannot so subdivide his total income as to bring it down into the very smallest bracket.

Senator BAILEY. If he tries to distribute it by gift you have the gift tax.

Mr. McLEOD. That is right.

Senator BAILEY. You have got in the bottom bracket \$607,000,000 squeezed out into the \$1,000,000-income bracket.

Mr. McLEOD. \$607,000,000; that is correct. Of course, when general business activity was considerably higher than it is at the present time there was a much larger amount of income in those particular brackets.

Senator BAILEY. You add immensely to the annual income of the very wealthy classes in that chart.

Mr. McLEOD. They have got the income at the present time. It only means the income is appearing in the form of individual tax brackets, but the income rests in the corporations today. There is no difference in the income, it is only a question of who actually receives it for the purpose of taxation. What this means is that an individual would pay a tax on the income he received in the form of dividends but he would still be free to reinvest in that corporation, or in any other corporation, if he so desires. He has paid a tax on it in proportion to his income.

Senator BAILEY. \$607,000,000 is in the corporate treasury that pays a tax of 15 percent under the present bill?

Mr. McLEOD. That is correct.

Senator BAILEY. That is, a man with a million-dollar income, since he gets over a million dollars he pays 72 percent?

Mr. McLEOD. It is not quite that high. \$5,000,000 I think is where the top rate is.

Senator BAILEY. What is it for \$1,000,000?

Mr. McLEOD. I will have to get the schedule.

Senator COUZENS. To get these results you have to go back and analyze the source of the income to all the income taxpayers, or all those filing returns, is that not correct?

Mr. McLEOD. That is correct.

Senator COUZENS. After you have gone back to say, one individual taxpayer, you have had to analyze the source of his revenue, and assume he maintains the same source of revenue, you fixed these brackets on that basis?

Mr. McLEOD. That is correct.

The CHAIRMAN. All right; proceed, Mr. McLeod. Is there any other explanation as to that chart?

Mr. McLEOD. No; I think we have covered this chart, pointing out that it merely shows where the additional amount of income would fall; what bracket it would fall into to provide the large amount of additional revenue.

Senator LA FOLLETTE. Mr. McLeod, do you know what average corporations over a period of years usually withhold?

Mr. McLEOD. Well, they have withheld varying amounts. Over a 10- to 11-year period they average about 30 percent. In some years it was very high and in other years it was considerably lower, but it averaged around 30 percent of the compiled net profits.

Senator LA FOLLETTE. Under this bill, assuming that average, would corporations as such pay more or less than they are paying now?

Mr. McLEOD. Corporations above \$10,000 could keep a little more than 31 percent of their current earnings and pay less tax, or pay no more than they pay today. If they should keep as much as 30 percent they would pay only 15 percent. If a small corporation kept no more than 40 percent of its current earnings it would pay no more tax than it does under the present law.

Senator LA FOLLETTE. In other words, we would be getting this additional revenue of approximately, according to your estimate, somewhere around \$623,000,000 from those who have been, as the result of being squeezed out from corporations, that have been withholding more than the average?

Mr. McLEOD. That is right. At the present time they would be withholding considerably more than the average.

Senator LA FOLLETTE. Who are they mostly?

Mr. McLEOD. Well, a considerable amount of that income I believe is in the large income, closely held corporations, or it may be in the minority controlling interest of a large corporation, where the stock has been placed in another corporation in order to avoid the high taxes which would apply under the 1935 act, but a considerable part of that income comes from large income, closely held corporations.

Senator LA FOLLETTE. Where they get the advantage of paying, on the average, about 16 percent instead of paying on what they would pay in their income brackets, if the abnormal amount of profits that they have been withholding in the corporation were forced out under this bill into their hands, where it would fall into their income brackets.

Mr. McLEOD. If it were paid out to the stockholders, they would have considerably more to pay in the form of surtaxes than they do in the form of corporate taxes.

Senator LA FOLLETTE. In other words, those in the upper brackets who are holders of stock in these closely held corporations, or in corporations where they have a sufficient minority interest so they can have a great influence on the policy of the corporation, under the existing law have an inducement to hold excessive amounts of profits in the corporation in order to avoid their surtaxes?

Mr. McLEOD. That is true. It would be much more profitable to them to hold the profits in the corporate form.

Senator COUZENS. Have you an estimate of the aggregate number of such corporations?

Mr. McLEOD. I do not have it at the moment.

Senator COUZENS. Have you it available in the Treasury?

Mr. McLEOD. I might. I am not positive as to the exact number of such corporations.

Senator COUZENS. You have in the Treasury, however, a record of the groups that have held more than 30 percent, or whatever they have held, over a period of years, have you not?

Mr. McLEOD. Well, we have the averages available in the Treasury. That would require a considerable amount of work to get the number of individual corporations over a long period of time that have kept above or below a certain actual percentage.

Senator COUZENS. Well, now, that is very important. I do not know how much time the committee wants to give to it, but it is necessary, it seems to me, because I understand the philosophy of this is to reach particularly those corporations who have kept above the average, and we should know if we are going to affect the whole corporate distribution, the number of corporations that are to be particularly affected by this bill.

The CHAIRMAN. How long would it take you to get that up?

Mr. HAAS. It is a question of machine tabulation. It is quite a job. It is not a thing of a day or a week. It is going to take considerable time.

Senator COUZENS. How long?

Mr. HAAS. I would not be able to estimate it, Senator, without going through it with some of my people to size it up.

Senator COUZENS. Can you do that tomorrow?

Mr. HAAS. Tomorrow I can let you know.

Senator COUZENS. I think it is very important.

Senator HASTINGS. In that connection I would like you to state just what the present revenue law provides with respect to corporations withholding for reserve more than is normal. Isn't there some penalty now in the revenue law?

Mr. McLEOD. I think section 351 takes care of personal holding corporations, where the corporation has been accumulating surpluses for the purposes of avoiding taxes.

Mr. PARKER. Then of course we also have section 102 that adds an additional surtax if the Commissioner can show that that corporation has been formed or availed of for the purpose of preventing the imposition of the surtax on the shareholders.

Senator HASTINGS. Is anybody prepared to say for the Treasury Department whether that has been effective, and if so to what extent, and explain why it has not been effective, if that is true?

Mr. McLEOD. I think that was taken up by Mr. Kent and Mr. Helvering earlier in the hearing.

Senator COUZENS. It is in the record.

Mr. KENT. I would be glad, if it is not in the record, to supply you with a memorandum which we prepared for the House committee showing our experience in cases arising under section 102, which is the present section corresponding to the earlier section 104 and still earlier section 220. Of course, we have no way of estimating to what extent that section has been effective by way of moral pressure which was exerted. We do know that, so far as our experience in cases which have actually arisen under this sec-

tion where deficiency letters have been sent out is concerned, it is not very satisfactory.

Senator COUZENS. In other words, in an operating corporation you would have to substitute the judgment of the Commissioner for the board of directors?

Mr. KENT. That is right, Senator.

Senator HASTINGS. I understand it is in the record.

The CHAIRMAN. You might furnish that memorandum, though, if you haven't already stated it.

Senator GEORGE. Mr. McLeod, I want to get this statement accurately, that on the average all corporations might retain or reserve 30 percent of their annual earnings.

Mr. McLEOD. That is what experience indicated over a 10- or 11-year period.

Senator GEORGE. With no increase in the actual payment of taxes, no increase over the 15 percent, above the present rate?

Mr. McLEOD. This rate is probably the highest we have had for several years.

Senator GEORGE. Did you say that on the average corporations could reserve 30 percent of their annual earnings without an increase over present rates?

Mr. McLEOD. Oh, yes; they would be paying 1 percent less.

Senator GEORGE. They would be paying 1 percent less?

Mr. McLEOD. They would be paying 15 percent under the law. On the average they are now paying a little more than 16 percent in excess-profits tax, corporate income tax, and capital stock tax. On the average it would be more than 15, it would probably run about 16 percent.

Senator GEORGE. In the case of smaller corporations you said they might retain approximately 40 percent?

Mr. McLEOD. A little better than 40 percent and pay no more tax than they do under the present law. If they retain as much as 30 percent, on the average they would be paying only one-half as much tax as they do under the present rate, that is, the small corporation, the corporation under \$10,000 net income.

Senator GEORGE. The small corporation?

Mr. McLEOD. That is correct. It pays 7½-percent tax on its adjusted net income for a retention of 30 percent.

Senator CONNALLY. Now he pays 13¾ to 15 percent.

Mr. McLEOD. Well, the \$10,000 corporation would approximately pay about 13 percent.

The CHAIRMAN. Twelve and one-half to 15 percent now.

Senator CONNALLY. As I understand it you ordered the preparation of this material on the question of Senator Couzens?

The CHAIRMAN. They are going to make an investigation and will give us a report tomorrow on how long it will take.

Senator CONNALLY. I do not think we ought to burden them with that, if it is merely to get the names of these corporations, I think that is wholly immaterial if the statistics already in their possession show the average.

The CHAIRMAN. They will give us a response on that tomorrow.

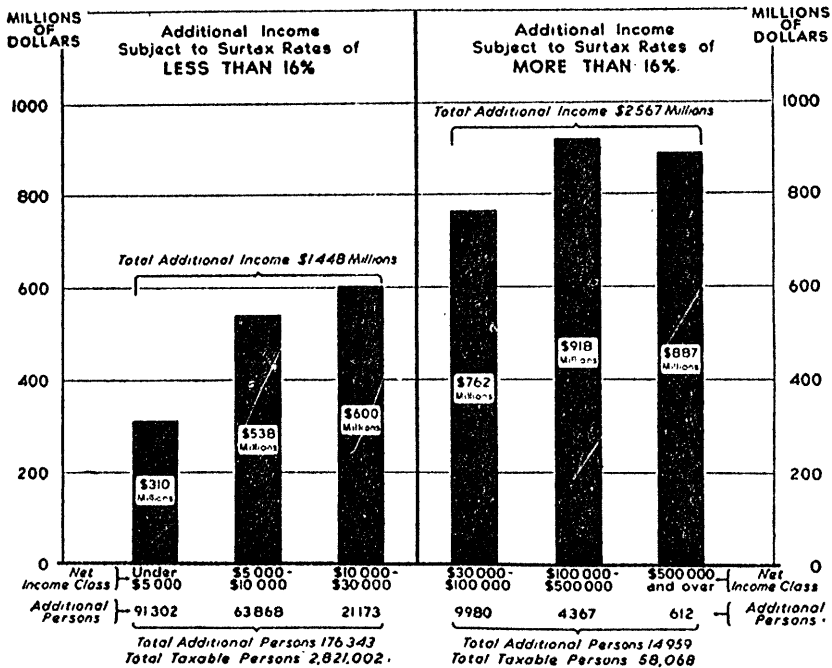
Senator LA FOLLETTE. Do you have copies of the chart which you are now to explain?

Mr. McLEOD. I do not have copies of this chart, but we could provide copies of it.

Senator LA FOLLETTE, I wish you would.

Mr. McLEOD. The black part on this chart that you now have before you expresses the proposition in a little different way. Here we have taken the additional income that would result from 100-percent distribution of corporate income by the bracket under \$5,000; \$5,000 to \$10,000; \$10,000 to \$30,000; \$30,000 to \$100,000 to \$100,000 to \$500,000; \$500,000 and over, and we show the additional income subject to

**ADDITIONS TO TAXABLE INCOMES OF INDIVIDUALS**  
Assuming All 1936 Estimated Corporate Earnings Were Distributed



surtax rates of more than 16 percent, 16 percent being about the average rate that corporations are paying today, and the additional income subject to surtax rates of less than 16 percent.

Now, to summarize the chart, of the total \$4,015,000,000 which we estimate under the present law will be withheld by corporations, \$1,448,000,000 would fall in individual-income brackets under \$30,000 if distributed. In other words, the surtax rate on the incomes below \$30,000 would be considerably less than the 16 percent which that income is now paying in the corporate form. There would be \$2,567,000,000 of the total \$4,015,000,000 which under the proposed plan would be paying considerably in excess of the 16 percent which that income is now paying in the corporate form.

Senator LA FOLLETTE. What percentage is that of the taxable total?

Senator CONNALLY. About 37½ percent—no, it is more than that.

Senator LA FOLLETTE. It would be about 64 percent, would it not?  
Mr. McLEOD. That is 64 percent of the total additional income.

Senator LA FOLLETTE. Can you tell me how many taxpayers there would be?

Mr. McLEOD. Well, the total additional persons that would fall within those brackets would be 14,959.

Senator LA FOLLETTE. And what percentage is that of all the taxpayers?

Mr. McLEOD. Well, that would be a little more than half of 1 percent of all the taxpayers. That, I would like to point out, is only the additional number of persons that move into that group of \$30,000 and over. There would be a total taxable number of persons in that group of about 58,000.

Senator LA FOLLETTE. Well, now, if I understand this chart, it would appear that there is an inducement for the taxpayers in the higher brackets who are in a position to influence the withholding of excess earnings, so to speak, because the earnings, so far as they are concerned, pay on the average around 16 percent, and they do not pay in their surtax bracket rates, whereas the stockholders in those same corporations, let us say, who fall in the class under \$30,000 are paying a rate of 16 percent on those excess profits withheld in the corporation, so to speak, but if they were paid out to them they would be paying a less rate than 16 percent, is that correct?

Mr. McLEOD. They would be paying on the average a surtax of about 4 percent.

Senator LA FOLLETTE. In other words, the stockholders in these classes of corporations, the corporations that have the practice that we are now discussing, are given a licking by the taxpayers in the higher brackets because they do not get the benefit of the lesser taxation that the taxpayers in the higher brackets get when this excess is held in the corporation.

Mr. McLEOD. That part of it which is due to that particular function of that particular group of corporate management, that is true.

Senator LA FOLLETTE. In other words, there is a great inducement, under the present law, for taxpayers in the higher brackets who own the stocks to use their influence, or their control, to withhold excessive amounts of profits rather than having them distributed, because they get the benefit of paying at the flat rate of around 16 percent, whereas the taxpayers in the brackets under \$30,000 who own stocks in these corporations are penalized to that extent, and under this proposal that the committee is now considering they would pay a lesser tax on those earnings if they were distributed than they pay on them as individual incomes.

Mr. McLEOD. That is correct. Now, that is well illustrated by what happened during the depression, I think. For instance, if you had this amount of income held under the control of a certain corporate management to avoid the highest surtaxes, assuming that the highest surtaxes were in effect at that time, they could pay that out during the periods of depression when they were taking probably severe losses on securities and other forms of income which dropped severely, and they would pay considerably less surtaxes



than they would at the time the income was earned. There is no doubt that that occurred in the past periods, and it would probably occur under the present law.

Senator CONNALLY. In other words, they offset their dividends with their losses on sales of stock and shrinkage of values, therefore that would be the period in which to take the dividends.

Mr. McLEOD. I think it would be good sense to do that. If one had a large amount of income and he paid a high surtax rate on it and did not require it he could hold it in the corporate fund and pay 16 percent and pay the income tax when the income-tax rates were reduced, or when there was considerable shrinkage in other forms of income, one could pay the income out and pay a much smaller tax than at the time it was actually earned.

Senator GERRY. They could not do it under the present law, could they?

Mr. McLEOD. They could not keep it in the corporate form.

Senator GERRY. No; they could not get the deductions.

Mr. McLEOD. Under present law?

Senator GERRY. Yes.

Mr. McLEOD. No; they would be limited to the amount of their gains plus \$2,000, but that would not affect the company if they had a great shrinkage in other forms of income, they could pay this corporate surplus out and pay a considerable less tax than if they paid it out the year it was earned, on top of the other income which they already had.

Senator GERRY. They could not deduct the losses under the present law?

Mr. McLEOD. Only to the extent of the gains plus \$2,000.

Mr. HAAS. They could deduct actual operating losses, they could balance actual operating losses over a period of years which an individual is not allowed to do. The corporation, by selecting a class of disbursement, could take that advantage, which is very substantial.

Senator GERRY. That would not affect the individual so much, it would affect the corporation.

Mr. HAAS. It would affect the corporation, but the income to be distributed actually would shrink because of that, you see. They balance the losses of 1 year against another year's income.

Senator GERRY. What he is talking about is the question of the advantage to the individual. He spoke about the fact that they could take tax deductions. That loophole has been plugged under the present statute.

Mr. HAAS. I thought he was leading up to this other escape.

Senator GERRY. No; he was leading up to just this one thing. I was correcting him in the statement he made, that is what I was doing.

Senator HASTINGS. I should like to inquire whether you have any calculations as to the number of people that will pay a tax to the Federal Government under this new law who did not pay a tax before.

Mr. McLEOD. We estimate 191,302 additional taxable individuals, and that would be chiefly people who, because the dividend being exempt from tax at the present time, plus personal exemptions, credit, and earned income credits, do not fall in the taxable class.

Senator HASTINGS. Have you any estimate as to the amount that the 191,000 persons would pay?

Mr. McLEOD. I do not have it here. The amount that the 191,302 persons would pay would be relatively small. That would be people in the lower-income brackets.

Senator HASTINGS. And if the person in the lower bracket holds only preferred stock on which he now pays no income tax, and that preferred stock has a fixed dividend, that stock becomes that much less valuable to him because of the fact he will have to pay a tax on it; is that correct?

Mr. McLEOD. He pays a tax on that. In the case where the individual is getting a certain fixed return on the investment and no more than would result to him from this plan through corporate distribution, he would be paying more tax than he does at the present time.

Senator HASTINGS. That is, if the person had no income except \$50,000 of preferred stock on which he had an income of \$3,000, now he would pay no tax and under this law he would pay \$120; is that correct?

Mr. McLEOD. Four percent; that is correct.

The CHAIRMAN. Is that about all you want to say about that chart?

Mr. McLEOD. That is all.

Senator BAILEY. Senator, would not he get an increase in his income?

Senator HASTINGS. Not on his preferred stock.

Senator BAILEY. If it is common stock he might get more.

Senator HASTINGS. If it is common he might offset it by the increase, but the preferred stock would not have any increase because it is fixed.

Senator LA FOLLETTE. Mr. Chairman, I would like to suggest that the first chart we had under discussion should be printed in the record in black and white for reproduction purposes, and that the second chart be furnished and put in the record also.

The CHAIRMAN. That will be done.

Mr. KENT. Senator, may I make a short statement?

The CHAIRMAN. Yes.

Mr. KENT. You asked us to find out whether there were any tax provisions in the trade agreements which would have to be taken into account in connection with the amendment to the statute to preserve the French Treaty and other treaty obligations, if any.

The CHAIRMAN. That was in this provision on treaty?

Mr. KENT. That is right. We have made inquiry, and we are informed that there are no tax provisions in any of the trade agreements other than those relating to tariff rates.

The CHAIRMAN. The committee will recess until 10 o'clock in the morning.

(Whereupon, at the hour of 12 noon, the committee recessed until 10 o'clock, Tuesday, Apr. 28, 1936.)

# REVENUE ACT, 1936

TUESDAY, APRIL 28, 1936

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

The committee met in executive session, pursuant to adjournment, at 10 a. m., in the committee room, Senate Office Building, Senator Pat Harrison presiding.

Present: Senators Harrison (chairman), King, George, Walsh, Barkley, Connally, Byrd, Black, Gerry, Couzens, Keyes, La Follette, Metcalf, and Capper.

Also present: Guy T. Helvering, Commissioner of Internal Revenue, Treasury Department; Herman Oliphant, general counsel for the Treasury Department; Arthur H. Kent, acting chief counsel, Bureau of Internal Revenue; George C. Haas, director of research and statistics, Treasury Department; A. S. McLeod, statistician, Treasury Department; C. E. Turney, assistant general counsel for the Treasury Department; L. H. Parker, chief of staff, Joint Committee on Internal Revenue Taxation, and members of his staff; Middleton Beaman, legislative counsel, House of Representatives.

The CHAIRMAN. The committee will come to order. Mr. McLeod, did you finish yesterday?

Mr. McLEOD. I did, Senator.

Senator KING. Mr. Chairman, I want to have inserted in the record a few paragraphs from the report made by the Joint Committee on Internal Revenue Taxation in 1927 by Mr. Parker, of the staff, found on pages 54 and 55 of their report.

The CHAIRMAN. That may be included in the record.

(The matter referred to is as follows:)

The most obvious objection to such a tax is the burden which it places on legitimate and proper business expansion. As a business expands not only does its plant and property increase but a larger working capital is required and it is desirable that reasonable accumulations of profits necessary for the expansion and stability of corporations should not be unduly burdened. A tax placed only upon the unnecessary accumulation of capital instead of upon the total accumulation involves many of the difficulties inherent in section 220 and is certainly an impracticable solution of the problem. It is believed that a tax on the total accumulation of profits by corporations is not desirable, because in many cases it might cause the taking of unwise distributions and prevent the accumulation of a reasonable and proper surplus.

*Taxation of dividends to the recipient.*—Another method, which would prevent any large amount of tax evasion by incorporation, would be to allow the corporation to deduct from taxable income the full amount of dividends during the taxable year in cash or in property and to tax such dividends to the stockholders at the full normal and surtax rates.

This would, of course, be a fundamental change in the structure of our present Revenue Act and should not be made without careful study. There might be noted as objections to such a method:

1. It would decrease the total revenue because much income now subject to the corporation income tax would be distributed to individuals paying a low rate of tax or no tax at all. Such a plan, therefore, requires a general readjustment of tax rates.

2. It would probably increase the difficulties of collection, since there would be many small sums to be collected from the many stockholders instead of large sums from the corporations.

3. It is open to the same general objection as an undistributed earnings tax since it might encourage unwise distributions.

There can be claimed as advantages for such a method:

It would be an automatic check on evasion of surtaxes by incorporation as there would be a tax, otherwise not payable, remaining on the income which the corporation did not distribute.

It would go far to make possible an important simplification of the tax law, for if dividends were taxed on the same basis as other income means might be found whereby the present normal and surtax rates could be combined into one graduated scale of rates for individuals.

*Partial deduction for corporations on account of cash dividends.*—A third method, and the one which is recommended, is to allow the corporation a deduction in computing net income equal to, say, 20 percent of the excess of dividends paid over dividends received, the deduction in no case to be more than, say, 25 percent of the corporation's taxable net income before such deduction. In this computation no account should be taken of stock dividends. This method appears to be of such a nature that it can readily be applied to the present structure of our revenue act.

An illustration will show how this plan would operate:

If a corporation having a net income of \$1,000,000 distributes cash dividends of \$500,000, it will get a deduction of 20 percent of \$500,000, or \$100,000. The taxable net income will then be \$900,000 instead of \$1,000,000, and the tax at 13½ percent will be \$121,500 instead of \$135,000, a saving in corporate tax of \$13,500. The effect upon the corporation income-tax rate will, of course, depend upon the proportion of income distributed as dividends. Based on the present corporation income-tax rate of 13½ percent, this would result as follows:

	Percent
If total net income is distributed, the tax would be equivalent to that produced by a present tax rate of.....	10.80
If one-half of the net income is distributed, the tax would be equivalent to that produced by a present tax rate of.....	12.15
If no distribution is made, the tax would be equivalent to that produced by a present tax rate of.....	13.50

The CHAIRMAN. All right, Mr. Helvering.

Mr. HELVERING. There are two titles in the bill that have not been gone into, titles III and IV. Title III is on the windfall tax, and title IV the two sections as to the refund on floor stocks, export and charitable institution funds, and Mr. Turney of the Treasury Department will present that.

The CHAIRMAN. We will take that up. Is there some other question before we start on an explanation of this windfall tax?

Mr. HELVERING. We might reverse this order I suggested, by having Mr. Kent go into sections 601 and 602, which have to do with the little reclassification, before taking up the windfall.

Senator KING. Just before we go into that, what amount do you get now from the tax on corporations, and from income taxes?

The CHAIRMAN. Mr. McLeod, will you give us those figures again?  
Mr. McLEOD. Under the present law we have estimated for the calendar year 1936, including the capital stock tax and excess-profits tax, and the income tax \$1,132,000,000.

Senator KING. That is from corporations alone?

Mr. McLEOD. That is correct.

Senator KING. Now, what is it from individuals?

Mr. McLEOD. \$1,153,000,000.

The CHAIRMAN. And under this bill you would get \$623,000,000 more, is the estimate.

Mr. McLEOD. That is correct.

The CHAIRMAN. Not counting the windfall tax?

Mr. McLEOD. Yes.

The CHAIRMAN. All right, Mr. Kent, you are on what section now?

Mr. KENT. Title IV, beginning on page 240, section 601. If I may, I will make a preliminary statement as to how this title happens to come into the bill.

The decision of the United States Supreme Court holding the Agricultural Adjustment Act unconstitutional, created certain very special and rather unanticipated situations.

I will take up section 602 first, as I believe that really comes first in logical presentation of the matter. The amendments to the Agricultural Adjustment Act which were enacted into law last summer, contained a provision for refund of floor-stocks taxes in the event the act should be held unconstitutional. They are not adequate to cover the present situation, however.

At the time those amendments were enacted into law, it was not anticipated that the major portion of the processing tax would be tied up by injunction as it is, and would be impounded in court.

Senator GEORGE. Can you tell me why we did not anticipate that?

Mr. KENT. I don't know exactly, as I had practically nothing to do with that. For some reason, however, and I am not familiar with just what happened in connection with the legislation, section 21 (d) (2) limited the refund of floor-stock taxes in the event the Act was held unconstitutional, to those cases in which the tax upon the original processing had been paid into the Treasury.

Now, as you gentlemen know, nearly \$200,000,000 of such processing taxes were tied up and impounded in these injunction suits, and after the decision of the Supreme Court such amounts were refunded in toto to the processor, so that with respect to the major portion of the floor stocks that were on hand on January 6 no processing taxes had actually ever been paid into the Treasury.

However, there was this additional fact that embarrassed the members of the House Ways and Means Committee—

Senator KING. You mean embarrassed them in connection with this?

Mr. KENT. Yes, sir. Many of the persons who held the floor stocks were not the original processors, they were the intermediate processors, the jobbers and retailers, and they had paid in most instances a price for these goods which included the amount of the tax, because, although these processors who brought the injunction suits had succeeded in preventing the actual payment of the taxes into the Treasury, nevertheless, in order to protect themselves against the possible contingency of a Supreme Court decision sustaining the constitutionality of the act, they continued in most cases to charge a price for their products, which included the amount of the tax.

The result was that this large number of dealers, jobbers, and so forth, who had floor stocks on hand on January 6, 1936, had paid a price which included the amount of the taxes. As soon as the deci-

sion was handed down, in most lines at least, there was a rather rapid and almost immediate adjustment of prices; therefore, they were unable in many instances, to sell the products on hand to the consumers at a price which would enable them to recoup the amount of taxes they had paid theretofore.

Unless some provision is made by way of provision for refunds in that situation, the amount of the taxes represents a dead loss to these persons. That is the purpose of section 602.

Senator KING. Would it be a fair illustration, if before the President sent in the message which eventuated in this bill, I had gone into the stock market and bought a lot of shares of stock, not anticipating that this bill would be before us, not anticipating its good effects or bad effects, but after the bill was passed it was contended that the bill operated to cause a great fall in the stock which I had bought, do you think Congress ought to recoup my losses; or, suppose I had gone out and bought a lot of agricultural commodities.

Mr. KENT. I do not think so, Senator, because I do not think Congress could very well assume the obligation of repairing all sorts of collateral and incidental injuries.

The additional fact which I intended to call to your attention, that the Agricultural Adjustment Act, as amended, contained a provision that in the event the processing taxes should be terminated by proclamation of the Secretary of Agriculture, refunds should be made to the holders of floor stocks as of the date of the termination of the tax. That went along with the provision which was inserted in the original act, you will remember, imposing a floor stock tax equal to the processing tax, on floor stocks which were on hand at the time the processing tax went into effect.

The purpose of that floor-stock tax was to take care of the competitive situation and to make certain that on and after that date all products to which the tax applied should go into the channels of trade equally taxed.

For the same reason it was thought fair in that legislation to provide, in the event the processing tax should be terminated in the manner provided by the act, that refunds on floor stocks should be made in order that such commodities might at that time move into the channels of trade equally untaxed.

The termination of the processing tax, of course, occurred by virtue of a judicial decision rather than by the administrative proclamation of the Secretary of Agriculture, but the practical situation which resulted therefrom is essentially the same, and it was the purpose of section 602 to take care of that situation.

The CHAIRMAN. Let me ask you, so that I can get it clear in my mind, because it is not now, what we did, we imposed a floor tax, but a great many of the people that should pay the tax did not pay it into the Government?

Mr. KENT. That is right; about \$237,000,000 was tied up.

The CHAIRMAN. How much was paid to the Government in these floor taxes?

Senator GEORGE. Do you mean the floor tax was not paid to the Treasury?

Mr. KENT. No; that floor tax that was imposed at the time the processing tax went on, was collected substantially in full, about \$98,000,000.

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The CHAIRMAN. That was paid?

Mr. KENT. Yes, sir; that was paid.

The CHAIRMAN. But there was a lot of processing taxes people paid out in the price they paid the original seller for the commodities?

Mr. KENT. That is right.

The CHAIRMAN. And the price is fixed along that basis?

Mr. KENT. That is right.

The CHAIRMAN. But some \$200,000,000, I believe, was paid under the injunction?

Mr. KENT. Yes, sir.

The CHAIRMAN. What was the amount of taxes paid?

Mr. KENT. \$956,000,000, I think, is the full amount.

Mr. HELVERING. That was during the period that the processing tax was in effect.

The CHAIRMAN. Now, this \$200,000,000 we propose to collect in another clause?

Mr. KENT. Yes, sir.

The CHAIRMAN. That has nothing to do with this?

Mr. KENT. That is correct.

Senator GEORGE. This deals only with the floor stocks?

Mr. KENT. This deals only with the floor stocks on hand January 6, 1936.

The CHAIRMAN. This refund is to the original parties who sold it?

Mr. KENT. It is to the persons holding the floor stocks on January 6, 1936, other than the processor or other person, who paid or was liable for the tax.

The CHAIRMAN. In other words, it is not a double tax?

Mr. KENT. Not at all.

Senator LA FOLLETTE. As I understand it, this is simply the reverse of the situation that occurred at the time the tax was imposed?

Mr. KENT. That is right, Senator.

Senator LA FOLLETTE. When the tax was imposed those who had goods on hand that had not paid the tax, had to pay some tax equal to the processing tax?

Mr. KENT. Yes; that is correct.

Senator LA FOLLETTE. Now, instead of the tax being terminated by proclamation of the Secretary of Agriculture, the tax is terminated by a decision of the Supreme Court?

Mr. KENT. Yes, sir.

Senator LA FOLLETTE. And this is a provision to refund to those who had goods on hand, presumably in the price of which the tax had been figured, so that they can obtain a refund and be on a competitive basis with those who do not have to pay the processing tax because of the Supreme Court decision?

Mr. KENT. That is correct. In other words, the aim of section 602 is to place these persons in substantially the same position they would have occupied under the Agricultural Adjustment Act as amended, had the processing tax been terminated by proclamation of the Secretary of Agriculture instead of by the adverse decision of the Supreme Court of the United States.

Senator KING. Let me give another illustration, I am not clear on it yet. Suppose a broker in my State, who purchased canned goods and agricultural commodities, had ordered from New York, or from the factories, or from those who had the stocks, \$10,000

worth, say, of goods which he had on hand at the time this decision was made, and he had paid for those goods, and, of course, there had been carried into the goods, doubtless, the increased price by reason of the processing tax—

Mr. KENT. Yes, sir.

Senator KING. He sells those goods at perhaps a little less than he otherwise would have sold them in view of this decision; is he to be reimbursed?

Mr. KENT. He is; to the extent that the sale price of the goods of January 6 was diminished by the amount of the tax he had paid, in the price he paid for the goods.

Senator GEORGE. Is this refund to be made for the processor?

Mr. KENT. No, sir.

Senator GEORGE. He does not get any back under this section?

Mr. KENT. If he gets it, it will be under section 21 (d), not under this section.

Senator GEORGE. The merchant who has the stock on hand, would be entitled to file his claim for refund?

Mr. KENT. Yes, sir.

Senator GEORGE. That is all there is to these sections you are referring to?

Mr. KENT. Yes, sir.

The CHAIRMAN. How much will that be?

Mr. KENT. It is estimated that the refunds under section 602 would run in the neighborhood of \$35,000,000.

Senator GEORGE. Will you state to us simply, what the remedy is, that he is provided with?

Mr. KENT. I will explain this as simply as I can. Section 602 (a) provides that there shall be paid to any person who, on January 6, 1936, held for sale or other disposition any article processed wholly or in chief value from a commodity subject to processing tax, an amount as provided in subsection (b), but it specifically excludes from the benefits of this section the processor or other person who paid or was liable for the tax.

Senator BLACK. May I ask a question before you leave that?

Mr. KENT. Yes, sir.

Senator BLACK. It is my understanding and, in fact, I was told by a cotton-mill operator who came up here to discuss this feature, and I told him he could probably come before the committee later if he desired to do so, that at least a large number of processors such as he had agreed by contract to refund this tax to the people who had it on their floor, and that under this provision, as he understood it, it would require the tax to be refunded to his purchaser, when as a matter of fact he had paid his purchaser the difference.

Mr. KENT. No; that is not true, Senator, because under subsection (b) of this section, in the parentheses, it is provided: "to the extent that the claimant has not received and will not receive reimbursement for such burden from the vendor." That is, if the jobber or the wholesaler or the retailer has been made whole, or under a contract will be made whole, then he is not entitled to any benefits under this section.

Senator BLACK. What about the man who has made him whole under that, the operator by this subsection (b)?



Mr. KENT. He does not come under this section, as he is here governed by section 21 (d).

Senator BLACK. Where is that?

Mr. KENT. That is in the old Agricultural Adjustment Act as amended. Section 21 (d) is the section which is intended to govern the claims of processors or other persons who paid the tax.

Under that section, if they are able to prove that they really absorbed the burden of the tax themselves, they would be entitled to a refund of the amount of the tax which they had paid.

Senator BLACK. His statement which he put in writing, at my request, I have downstairs, and I did not bring it because I did not know this was coming up, but as I understand he will want to bring it up later. The people who had attempted to observe the law and had not taken advantage of the injunction, and he did not, but paid the tax up to the last minute, and he understands that he is excluded under here because he is an original processor, and that as a matter of fact, as this is written it would give the benefit of the refund to the people who had defied the law and declined to give it to the people who had observed it.

Mr. KENT. No; I do not think that is the intention, because this section has nothing to do with the processor or persons who paid or were liable for the payment of the taxes. They are the persons who brought the injunction suits, they are the persons at whom the tax imposed by title III, which Mr. Turney will explain, is directed, and as far as their right to refund is concerned, their situation is governed by section 21 (d) of the Agricultural Adjustment Act.

This is only intended to take care of certain cases where, unless some special statutory provision is made for them, the persons affected will suffer a dead loss by reason of the invalidation of the Agricultural Adjustment Act.

Senator BLACK. What about the flour stock of the processor who has refunded and who has paid the tax up to the last minute?

Mr. KENT. He will not have the slightest difficulty, in my judgment, in establishing a right to a refund under section 21 (d).

I may say, by way of information, it is proposed to suggest in another connection certain changes in section 21 (d), in order to make it more feasible of administration, but that section is the section which is intended to cover the cases of processors.

If a processor had paid a tax on flour, for instance, prior to January 6, 1936, and he still has the flour on hand on January 6 and has not sold it to anybody, manifestly he has not passed on the burden of the tax to anyone else.

Senator BLACK. Suppose he has sold it, however, and agreed, at the time he sold it, and had to, on account of these injunctions, that he would refund the tax.

Mr. KENT. If he got it back?

Senator BLACK. No; they had an ironclad agreement, and they have paid out this money.

Mr. KENT. I have seen a number of those agreements, Senator, and none I have seen have gone any further than to provide that if in one way or another the processor got back the amount of the tax for which he was liable, he would make reimbursement.

Senator BLACK. I haven't the contract, but as I recall it was provided if it was held illegal, after the injunction was issued, like this

man had in a contract which provided that if the law was held unconstitutional they would make refund to the purchaser of the amount of the tax, that being true they have paid it, as he says they have, exactly the same as they had paid it to the Government so that their floor stock is included, and you include the floor stock of others, who paid the taxes as you say, there would be a discrimination against them, which section 21 (d) might take care of.

Mr. KENT. Even so, that would be one of the problems which it would seem to me should be covered by section 21 (d).

Senator WALSH. May I make an inquiry?

Mr. KENT. Yes, sir.

Senator WALSH. I understand inventory was taken of all property for the purpose of levying the floor tax.

Mr. KENT. Yes, sir.

Senator WALSH. Then, in a particular establishment, let us say, commodities were valued at \$10,000, and between that time and January 6 of this year that merchant disposed of \$8,000,000 of those commodities, leaving \$2,000 upon which he paid the tax. He can obtain refund for that amount.

Mr. KENT. Yes, sir.

Senator WALSH. And this does not include goods he bought since, because they were taxed at the source?

Mr. KENT. No, Senator; it does not include any goods in which the person seeking the refund is the person who paid the tax.

This provision is intended to take care of certain persons who would not otherwise be taken care of at all, who have not paid any tax to the Government, but have in effect borne the burden of the tax, because of the increased price which they paid to the processor, but paid by the processor in the price of the goods they have.

Senator BARKLEY. This bill does not deal at all with the refunds under the Kerr-Smith Act?

Mr. KENT. No, sir.

Now, subsection (b) states the method in which the amount of refund to which the claimant is entitled shall be computed. It states that it shall be equal to the processing tax which would have been payable with respect to the commodity from which the article was processed, if it had been processed on January 5, 1936, but not in excess of (1) the amount of the burden of the tax with respect to the article which was shifted to the claimant in the price he paid for the article; that is, if he bought his products from a processor who actually himself absorbed the burden of the tax.

Senator GEORGE. Or one-half of it?

Mr. KENT. That is right.

Senator GEORGE. He could only get what he had absorbed in his purchase price?

Mr. KENT. That is right. And with the further limitation to the extent that the claimant has not received and will not receive reimbursement for such burden from the vendor; that is, in some lines of industry repayment has been made.

In other words, we are not going to let him obtain a refund from the Government if he has already been made whole in the other way.

Senator GEORGE. That seems entirely equitable.

Mr. KENT. Yes, sir; it further provides the refund shall not be in excess of (2) the amount by which the claimant reduced the sale

price of the article on account of the invalidation of the taxes under the Agricultural Adjustment Act as amended.

We are told in many lines of trade in commodities and products to which the processing tax applied there was a very immediate readjustment of prices subsequent to the decision in *Hoosac case*.

In the case of flour, for instance, the wholesale price dropped almost without delay—almost the next day—by an amount which practically equaled the amount of the processing tax on that commodity.

Senator KING. Let me ask you a question, if I may.

Mr. KENT. Yes, sir.

Senator KING. I do not quite understand all of the ramifications. Suppose I had been a merchant in a mining camp and I anticipated a great development in the camp, mines should be opened up and smelters opened up, and I overstocked with canned goods, let us say, upon which the processing tax had been paid; that I bought \$50,000, instead of a reasonable amount, and when this tax decision came subsequently, the mining company did not develop, the smelter did not open up, and it was evident that I had exercised very poor judgment, and had on hand \$25,000 worth of those goods; would I be entitled to relief?

Mr. KENT. And which you would only be able to sell and dispose of at a considerable loss to yourself?

Senator KING. Yes; would I be entitled to relief?

Mr. KENT. Only to the extent that the price at which you were able to sell them would be reduced by the removal of the processing tax.

Senator KING. Then I can see litigation without end.

Mr. KENT. I think we have taken care of that, Senator, in a later section.

Subsection (c) simply contains a couple of definitions.

Subsection (d) requires the claim to be filed under this section by January 1, 1937, in conformity to regulations prescribed by the Commissioner with the approval of the Secretary, and placed upon the claimant the burden of establishing the facts upon which his claim is based.

Senator CONNALLY. Will you not run into the proposition that a lot of them will claim they have not disposed of the goods?

Mr. KENT. That is taken care of in the provision of the bill which defines the term "sale price" as meaning either the price at which the article was actually sold prior to the filing of the claim, or the price at which it is being offered for sale.

Senator KING. Let me get one more illustration, if I may, and I beg the pardon of the committee. In my State we have a large number of canning establishments. They paid more for the tomatoes and beans and peas than they otherwise would have paid by reason of the Agricultural Adjustment Act, and after the decision the price went down. They had paid, maybe, for tomatoes \$50, whereas probably, if it had not been for the Agricultural Adjustment Act they would have only paid maybe \$40. How are they to adjust that? And who shall pay it?

Mr. KENT. Of course, that particular product was not under the processing tax, but if you will assume a product that was—

Senator KING. All right; assume some that were, then, on the same problem; who would pay for it?

Mr. KENT. It is probably true that in some instances at least there was some pyramiding as the result of the tax: that is, a processor would not only add on the amount of the tax, but a little more if he was able to do so, a common phenomenon in connection with tax on transactions, such as sales, but this section would not allow relief in any case in excess of the actual amount of tax which the statute has imposed.

If there was a dollar processing tax on a barrel of flour, for instance, which was in somebody's floor stock on January 6, the refund with respect thereto in no case could exceed that one dollar; in other words, it is not proposed to make any reparation for any consequences that were incidental or collateral to the economic workings of the act.

Senator CONNALLY. You could not do it any other way?

Mr. KENT. No, sir; we would simply be at sea.

Senator GERRY. Would you explain the necessity for any of the sections of the Agricultural Act which you referred to?

Mr. KENT. Yes, sir; I would be glad to do that. There would be only one or two sections that are relative to this.

It is proposed to limit the claim allowable under this section to those of \$10 or over, for the practical reason that with claims less than that, the cost of administration is out of all proportion to the amount involved both from the point of view of the claimant and the Government.

Moreover, by virtue of the fact that this relief is not relief which the law requires, it is proposed to make the determination of the Commissioner with respect to claims filed under this section final, and not subject to judicial review.

Unless some such provision is written into the law there is no principle of law upon which any such claim could be successfully invoked against the Government, and this relief, if it is written into the law as finally enacted, is to be justified on grounds of equity and public policy alone.

For the same reasons it is provided that no interest shall be allowed in connection with any payments made under this section.

Senator GERRY. Are there other sections in which the decision of the Department is final?

Mr. KENT. In the case of special assessment, except that where a review by the Board of Tax Appeals was allowed, but there was no judicial review.

Senator GERRY. Where was that?

Mr. KENT. That was in connection with the wartime excess-profits tax. There is plenty of precedent for making the administrative decision final in the payment of what in one sense is a gratuity.

Senator CONNALLY. This is a comparatively simple thing compared with the windfall.

Mr. KENT. Yes, sir; and there is no question that can be presented under section 602 which is not involved, in perhaps a more complicated way under section 21 (d) of the Agricultural Adjustment Act as amended.

Section 601 is intended to take care of a somewhat different situation. The Agricultural Adjustment Act as amended contained cer-

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tain sections providing for so-called refunds where commodities and products with respect to which a tax was due, or a tax was paid were exported from the country, or were delivered to a charitable institution, and certain other provisions providing for refunds on floor stocks where a processing tax should be decreased in amount or should be suspended upon a certificate by the Secretary of Agriculture for certain reasons which were stated in the act.

The invalidation of the Agricultural Adjustment Act has created such doubt as to the present legal status of those provisions that the Treasury Department has felt unable to continue with the making of refunds to which persons would otherwise be entitled under those particular sections. It is estimated there is about 10 or 11 million dollars altogether involved in them.

Senator GEORGE. The sale of goods to the Government is also included?

Mr. KENT. Yes, sir; that is included in this case of charitable goods.

It is proposed in section 601 to reenact the particular provisions of the Agricultural Adjustment Act to which I have referred for the sole purpose, however, of allowing refunds in accordance therewith in the specific cases.

In other words, this enables us to go ahead and liquidate that much of the wreckage resulting from the invalidation of the act.

Senator COUZENS. With respect to this section where you say no refund is permitted under any circumstances, I understand that is taken care of in the Agricultural Adjustment Act.

Mr. KENT. In section 21 (d), or at least it will be taken care of in a revised form of the section which will be submitted later for consideration.

Senator COUZENS. That has created some misunderstanding, and I want to have something gotten up and put in there to take out that misunderstanding, because many persons do not go back to the Agricultural Adjustment Act to read this act, and without going back to the Agricultural Adjustment Act it shows certain persons are not permitted to make claim.

Mr. KENT. We tried to cover that by saying no refund under this section shall be made, not that no refund shall be made anywhere, but that no refund shall be made under the authority conferred by this section.

The other provisions of the section with respect to the date of filing of claims, the finality of the Commissioner's determination, the nonallowance of interest, are similar to those contained in section 602.

Just a word about subsection (g) on page 231, that is intended to correct what we are amply convinced was an inadvertance, or a legislative error made a year or two ago in the amendment of the Agricultural Adjustment Act.

Legislative history clearly indicates that Congress intended to write in the date June 1, 1934, but by some mischance wrote in June 26, 1934, instead. The result was to cut off the allowance of a few meritorious claims for refund arising out of the suspension of the processing tax such as on large cotton bags, and it is simply the purpose of that section to remove this impediment.

Mr. HELVERING. Title III has to do with the windfall tax, and Mr. Turney will explain that, on page 231.

Mr. TURNER. This title imposes a tax of 80 percent on the unjust enrichment, or what has been called the windfall, resulting to certain processors and certain dealers from the unconstitutionality of the Agricultural Adjustment Act, the impoundment of taxes last year, and the nonpayment of taxes outstanding at the time the act was held invalid.

I might say the title is general in terms and applies to similar situations in connection with any excise tax, but I take it for the purpose of this discussion it is just as well to talk in terms of the processing tax.

The tax applies to two classes of persons. The first are those covered by subsection (a) (1) on page 231, the processors who last year either had the tax impounded and got it back when the act was held invalid, or who had not paid part of their processing taxes at that time.

In the case of those persons the bill provides that there shall be determined the net income which they made from the sale of the articles with respect to which the tax remained unpaid. Then the tax of 80 percent applies to that net income from the sale of those articles to the extent that such net income results from passing on the tax to other people.

Subsection (a) (2) applies to the dealers who bought articles at prices including the processing tax and who, under these contracts which have been mentioned, received refunds from their vendors for the burden of those taxes, in cases where they had gone ahead and passed the tax on to their customers.

In those cases the bill provides for determining the net income which they realized from this reimbursement from the vendors, and the 80-percent tax applies to that net income to the extent they have passed the processing taxes on to their customers.

It only applies where they have in effect collected the amount of the processing-tax burden twice, once from their customers and once from the processor who originally passed it on to them.

The CHAIRMAN. Why do you fix this percent?

Mr. TURNER. The Ways and Means Committee did that.

The CHAIRMAN. What was the reason of fixing that instead of 90 percent?

Mr. TURNER. The original proposal was to make it 90 percent, and I think the committee had some fears that the tax might be held unconstitutional because 90 percent amounted to confiscation. I think they felt it was better to go to 80 percent, which would be safer from attack of that sort.

Senator GEORGE. I suppose they took into consideration the expense of litigation?

Mr. TURNER. That point was also made, that after all these processors had been put to a good deal of expense in connection with these processing taxes, extra bookkeeping, accounting, and that sort of work.

The CHAIRMAN. And the lawyers' fees?

Mr. TURNER. The lawyers' fees are in here as a special deduction, but limited to 10 percent.

Senator CONNALLY. They will be put to some expense in meeting the requirements of the Treasury in collecting refunds, also?

Mr. TURNER. Yes, sir.

Senator CONNALLY. Some of these impounders make the claim that a part of it, if not all of it, was absorbed, can the Treasury be able to determine in this kind of cases whether the tax was absorbed, or to what extent it was absorbed?

Senator GEORGE. The burden will be on the claimant, will it not?

Mr. TURNER. Yes, to the same extent the burden is on the taxpayer in ordinary income-tax cases when the Commissioner makes a determination against him.

Senator GEORGE. Is there a provision here that if the processor who impounded the taxes, went into court, and did not pay it to the Treasury, but nevertheless paid the amount of that fund over to his vendees, is he protected?

Mr. TURNER. Yes; that is covered here.

Senator GEORGE. He is allowed a credit where he has made an actual bona-fide payment?

Mr. TURNER. Where the rebate was made on or before the date of the President's message or pursuant to a contract entered into on or before that date.

Senator GEORGE. Suppose they have come since?

Mr. TURNER. That is only if it is made under such a contract.

Senator GEORGE. Suppose it is not made under a contract, but is a bona-fide payment, such as, take the textile people, whether they do have a contract or not, they have got to pay it, and if they do not pay it, the customer will buy from somebody else.

Mr. TURNER. There was a representative of the textile people who appeared before the Ways and Means Committee, and objected to the time limit on the rebates to their customers.

Senator GEORGE. That is obviously unjust, because if it is an actual bona-fide payment, it seems to me he ought to have credit for it.

Mr. TURNER. I think the objection to that is that these processors have known since March 3 that they might become liable for this tax, and to permit them to go ahead and make all of these payments to their customers, simply gives them a wide-open opportunity to buy goodwill at the expense of the Government.

The CHAIRMAN. Would not practically all of them do it?

Mr. TURNER. I haven't any doubt that if the limitation were taken off, every processor who thought he was likely to be liable for this tax, would prefer to give the money to his customers.

Senator GEORGE. It is not a question of preference; if he stays in business he has got to do it, and he has done it as a matter of fact, and is doing it today, and there is no way out for him. It seems to me if it is a bona-fide payment actually made to somebody since the passage of the act, he ought to have credit for it, and then you can get it in the hands of his vendee, if he passes it on.

Mr. TURNER. Of course it is more difficult for the Government to collect the 80-percent tax from all his customers.

Senator GEORGE. It will be difficult to make the collection anyway.

Senator WALSH. There was, as I understand, some loss to the Treasury.

The CHAIRMAN. We lost about \$10,000,000, I believe.

Mr. KENT. It was about 5½ percent, because when we had the 90-percent rate there was a provision allowing a deduction for attorneys' fees up to 15 percent, and when the rate was reduced to 80 percent the allowance was reduced to 10 percent, so that there was an offset that way.

Mr. TURNER. Subsection (b) provides for determination of the net income from sale of the articles with respect to which the processing tax was not paid. It provides for the proper allocation of deductions to the gross income from that source, and subsection (c) lays down a similar rule for determining the net income which the dealer realizes from reimbursement from his vendors.

Subsection (d) gives the rule for determining, the prima facie, the extent to which the taxpayer under this section shifted the burden of the processing tax to his customers.

The rule laid down there is a comparison of his margin, or the difference between the selling price and direct cost of materials or of the article with his average margin determined on the same basis during the 5 years preceding the tax period.

In paragraph (3), page 233, provision is made for credit of refunds which he may have made to his purchasers to offset the tax passed on to them.

Subsections (f) and (g) on page 234 are minor rules to facilitate these determinations. Subsection (f) provides for the first-in-first-out rule in fixing the costs and selling prices of articles in cases where they cannot be definitely shown.

Subsection (g) covers the case of dealings through affiliated corporations where fictitious prices may have been set up and provides that the Commissioner shall determine a fair price.

Subsection (h) provides that either the taxpayer or the Commissioner may overcome this prima facie rule which is set out in subsection (d) by proof of the actual extent to which the taxpayer shifted to others the burden of the processing tax.

The subsection enumerates certain types of proof which can be taken into consideration to determine this extent, but does not limit either party to this type of proof.

Subsection (i) defines the term "Federal excise tax."

As I said before, this title does not relate only to the processing tax but relates to all Federal excises which are of the sort which the taxpayer ordinarily shifts to other people.

Senator COUZENS. Give us an example of what kind of a tax that would be.

Mr. TURNER. Any sales tax; for instance, a tax under title IV of the Revenue Act of 1932; the cotton-ginning tax under the Bankhead Act would be another one. That tax was imposed on the ginner for the ginning of the cotton, but he, of course, took it out of the producer in the price he charged.

Senator CONNALLY. Is that the requirement he had to have a tag on the bales and had to pay about \$20 for it?

Mr. TURNER. Yes; the tax was paid by means of bale tags.

Senator CONNALLY. That would not hurt the ginner provided he got it out of the man who bought the cotton; is that right?

Mr. TURNER. That is right.

Senator CONNALLY. And in all cases, of course, he did?



Mr. TURNER. Yes; and if under those circumstances the ginner gets a refund from the Government, he is just as unjustly enriched by getting that refund, unless he pays it back over to purchaser, as any of these processors under the Agricultural Adjustment Act.

Senator GERRY. Is there an appeal from these decisions of the Department?

Mr. TURNER. Yes; this title is an income tax, and is subject to all of the administrative provisions of the income-tax law. The taxpayer will file a return showing his determination of the tax. Those returns will be audited by the Commissioner, and if he finds more tax due, he will issue a notice of a deficiency, and the taxpayer can then go to the Board of Tax Appeals or pay the tax and sue for refund, and the procedure will be exactly the same as that with respect to the ordinary income tax.

Senator BLACK. I assume this will apply to the tax on oils?

Mr. TURNER. That is right.

Senator BLACK. I understand there has been an injunction granted against that.

Mr. TURNER. Yes; that is correct.

Senator CONNALLY. The coconut oil?

Mr. TURNER. Yes, sir.

Senator CONNALLY. That was appealed, and was sustained by the District Supreme Court yesterday, but I do not know what the Supreme Court of the United States will hold.

Mr. TURNER. Of course, even in the case of a tax which is not held unconstitutional, there may be a situation where the taxpayer will get a refund on something not taxable which he thought was taxable.

Senator CONNALLY. Under this windfall there is no provision for getting back these taxes on cotton under the Bankhead Act?

Senator GEORGE. No.

Senator CONNALLY. Why would not the windfall do it?

Mr. TURNER. The windfall tax will apply with respect to the processing taxes in these cases where the tax was never paid by the processor. It will apply to any refunds that may be made of the ginning tax.

In subsection (j), page 236, the bill expressly provides that while in general this windfall tax applies to cases where the taxpayer gets a refund, as far as the Agricultural Adjustment Act taxes are concerned, and the manufacturer's excise taxes under the 1932 act, it does not apply where the taxpayer gets a refund of those taxes in conformity with section 21 (d) of the Agricultural Adjustment Act or section 621 (d) of the 1932 act, which sections permit refunds only when the taxpayer can show he absorbed the burden of the tax.

Subsection (k) is a provision in the nature of a definition which provides that the language used previously in the title with reference to sales of articles and commodities shall be deemed to include sales of services where the tax was imposed with respect to a service rather than an article.

Subsection (l) on page 237 is a special separability clause.

As the main part of the section is drafted it applies to the unjust enrichment arising out of the sale of these particular nontax-paid articles, to the extent the taxes are passed on, without any offset to the taxpayer for losses sustained on any other business or during any other part of the year.

In the Ways and Means Committee there was considerable question raised as to the validity of an income tax which picked out of the taxpayer's business for the taxable year a special group of transactions and computed the net income on the basis of those transactions without any offset for losses outside of those transactions.

The Ways and Means Committee decided that as far as policy was concerned they wanted to do that, and they thought there was enough argument for its validity to justify them in doing that, but they wrote in here a provision to the effect that if this broader application of the tax was held invalid, then the tax should nevertheless apply, but with an offset for losses from other transactions.

Senator CONNALLY. That is in order to avoid a court's decision?

Mr. TURNER. That is in order to avoid a court holding the entire thing unconstitutional because it is too broad in its application.

Senator BARKLEY. Of course, that gives to this particular class of taxpayers a right which is not enjoyed by the rest of them, to offset losses on general transactions. I am not objecting to it, but it is putting them in a little different class.

Mr. TURNER. You mean the ones who have losses outside of this part of their business?

Senator BARKLEY. Yes.

Mr. TURNER. Yes; that is true; and this provision only applies if it is necessary to apply it in order to save the constitutionality of the tax.

Section 502 is a provision for crediting against this tax the amount of any other income tax which is attributable to the same income.

For example, this tax applies to a part of the net income at the rate of 80 percent. The taxpayer might be an individual in a fairly high surtax bracket so that his regular income tax, which is computed on his entire income, including this income, would be increased by, say, 50 percent of that amount, and you would have a total of 130 percent tax attributable to this unjust enrichment.

Therefore, section 502 provides a method of crediting against this 80 percent the portion of the other income tax which is attributable to this windfall part of the income, and therefore in effect this part of his income bears the 80-percent tax and no other tax.

Senator CONNALLY. The effect of that is to segregate this and not include it in the tax on any other income.

Mr. TURNER. That is substantially it. Technically it is done by leaving the other income tax alone and reducing this tax.

Senator BARKLEY. Getting back to section 501, if this law shall be declared invalid this income is just put in the general pot of his income and taxed according to the general tax laws without regard to this section; is that true?

Mr. TURNER. No; under subsection (1), if the court says you cannot tax this income without giving him credit for losses outside of this section, this tax still applies to the windfall income, but limited by his total net income for the taxable year.

To give an example, assuming a man was in the milling business and had his tax impounded during part of the year and made, say, \$1,000 windfall by reason of the unconstitutionality of the Agricultural Adjustment Act, but on the product with respect to which he paid the tax he lost \$500, the main part of the section would tax

the \$1,000 windfall without any offset for that \$500, but if the court should hold that you cannot tax a part of the net income which is in excess of his entire net income, then the section would apply to the \$1,000 limited by the \$500 which he made for the entire taxable year on all of his business.

In other words, the provision would, if it were held applicable, give an offset for any net loss on the taxpayer's other transactions.

The CHAIRMAN. Why would not the same rule apply to this next section you are reading from, where in applying the processing tax for the fellows in the higher brackets he should be separated from the other. Isn't that a special class where it does not apply generally?

I am just wondering on that proposition whether the same rule would apply.

Senator CONNALLY. The point there is if you take the 80 percent out of this and throw it into the other income and tax it again, you would make it more than 100 percent of the windfall taxes.

Mr. TURNER. Of course, as to section 502, its operation will be dependent on what is finally held as to the scope of the main tax.

The CHAIRMAN. In other words, it is removing discrimination, and the other you put it in, except the proposition we are in the bigger class of people and you make it apply separately, but you apply that to all of them whether large or small, don't you?

Mr. TURNER. Of course, whatever the court holds as to the scope of the main tax, it will apply as far as legal effect is concerned, to everybody alike. There will be a practical discrimination in a sense, between those who have outside losses and those who do not.

Senator BARKLEY. Is it true that whatever the court might hold there will be some tax levied on this amount of money?

Mr. TURNER. That is correct, but the application of subsection (1) to particular taxpayers would reduce their tax or perhaps exempt them, if they had no net income on their entire year's business.

Senator CONNALLY. Taking your illustration of a moment ago where a man makes \$1,000 windfall, and has a \$500 loss on the outside, what you would do, would be to take off \$500 and assess it 80 percent against the other?

Mr. TURNER. Substantially, yes, you determine his windfall at \$1,000, and if you determine his entire income for the year to be \$500, the \$1,000 would be limited by the \$500, so that the tax would be 80 percent of \$500 under subsection (1), if the court held the tax could not constitutionally apply to the \$1,000.

Senator CONNALLY. Then, the tax would be \$400?

Mr. TURNER. Yes. Section 503 makes applicable to this tax the administrative provisions applicable to regular income taxes, with special provision for the due date of the taxes and the returns for taxable years ending before the date of enactment.

Section 504 makes the tax retroactive to any taxable year ending during the calendar year 1935 or any subsequent taxable year. That makes it sufficiently retroactive to cover all of these cases where the processing taxes were impounded last year.

The CHAIRMAN. That includes the year 1935?

Mr. TURNER. It includes the year 1935 and every fiscal year which ends in 1935. It is conceivable it will apply to fiscal years begin-

ning February 1, 1934, and ending January 31, 1935. That would be the earliest year to which it could apply.

Section 505 makes this tax applicable to Puerto Rico and the Philippine Islands because processing taxes were applicable in those possessions, and there were some outstanding processing taxes down there.

Senator CONNALLY. How about the District of Columbia?

Mr. TURNER. It is applicable to the District of Columbia as shown on page 239, line 18.

Senator CONNALLY. Yes, I beg pardon, I didn't see that.

Mr. TURNER. I think that covers the entire title unless there are some more questions.

Senator BLACK. Do you have a proposed amendment of section 21 (d) in connection with this same thing?

Mr. TURNER. I have not been working on that, Senator. I think Mr. Oliphant probably can answer that.

Mr. OLIPHANT. There are a number of problems there, on which the Department of Agriculture, the Department of Justice, and the Treasury Department are working.

Senator WALSH. I would like to know how you estimate the returns from this tax at a hundred million dollars a year, on what basis?

The CHAIRMAN. How about that, Mr. McLeod?

Mr. McLEOD. We have a distribution in the Bureau of Internal Revenue, showing the number of concerns involved and the amount of taxes, and we determine the net income or deficit of those corporations for the previous year, and making adjustments in earnings for the current year we arrived at an approximation which we believed was fairly conservative, and we wrote that down, allowing a factor of safety in view of the statistical data we had, which amounted to around a hundred million dollars, but the actual statistical data indicated a higher figure.

The CHAIRMAN. You estimated the increased revenue by virtue of this bill, including the windfall and the corporation tax at \$723,000,000. Is that right?

Mr. McLEOD. Including the capital-stock tax, it would be more than that.

The CHAIRMAN. The capital-stock tax runs until 1937, I believe—what is the date it runs to?

Mr. McLEOD. We collect everything on the capital-stock tax in the fiscal year 1937, the first 3 months of the fiscal year 1937.

The CHAIRMAN. Then, taking off whatever the capital-stock tax would be, it would be \$723,000,000; is that correct?

Mr. McLEOD. Yes; that is correct.

The CHAIRMAN. But with the capital-stock tax as written in this bill going until 1937, you would estimate how much?

Mr. McLEOD. \$803,000,000, including the capital-stock tax and the excess profits. There would be probably an additional amount of excess profits we have not included.

The CHAIRMAN. There was one phase, Mr. McLeod, you did not discuss yesterday in all your demonstration on the board there, and your estimates, they were based on complete distribution of earnings to the stockholders, and then you discussed about the retention of

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certain reserves; what is your estimate on these reserves that this bill permits with these various taxes, 15, 22½, and so forth, on the surplus; does that change your estimate in any respect?

Mr. McLEOD. By reason of the corporation retaining 30 percent in the form of surplus and paying out 55 percent in dividends, and paying a tax of 15 percent we found practically no difference between 100-percent distribution and 30-percent retention, because of the rates we applied on the total net income based on the percent retained plus the tax we get on dividends paid; with the two working together, we get about the same figure up to 30 percent.

Above 30 percent retention we gain, because then the rate of corporation tax, depending on the percentage retained, rises more rapidly.

Senator COUZENS. Yesterday I asked for some information with respect to the number of corporations that the Treasury had in mind to reach when they suggested this method of taxation. Have we any information in connection with that?

Mr. McLEOD. We have looked into that, and it would probably take about 4 days, but we might shorten that by working nights. All of the cards have to be run through the machines.

Senator COUZENS. Do you think you could have it in 4 days?

Mr. McLEOD. Yes; we are working on it now, as a matter of fact.

Senator COUZENS. Do you intend to give it to us?

Mr. McLEOD. I do.

Senator LA FOLLETTE. Mr. Chairman, is there any question about there being any misunderstanding between the Senator from Michigan and the Treasury officials about the data required? I was confused about it, but perhaps they have talked it over since.

The CHAIRMAN. I do not think you can get in 4 days all of the data he requested. What is it you were getting in 4 days?

Mr. McLEOD. We were going to get all corporations reporting for a calendar year over a million dollars net income, which would include about half of the total corporate net income, and amount to about 500 to 600 corporations. That sample would provide the greater part of the net income of the corporations and cut down the work to a great extent. Otherwise we would have the tabulations to run for about 250,000 corporations.

Senator COUZENS. That may cover the question, but when the Treasury Department apparently advised the President this was a good scheme, they had certain information before them to predicate this scheme, and I would like the same sort of information the President had or you had when this plan was proposed. Do I understand that you are preparing substantially what the President had when he proposed this plan?

Mr. McLEOD. We had not, of course, the number of individual corporations that retained more or less than 30 percent. We had a picture of all corporations' net income and deficit corporations, and the amount of net income that had been retained in the form of surplus, and the amount that had been paid out over a period of years, but not broken down by the number that retained, say, 30 percent, and the number that retained 40 percent, and the number that retained 50 percent.

Senator COUZENS. I did not contemplate that, but I did contemplate you would have the same information you had and which

you gave the President when you planned this scheme, and I would like to have that information. Is that available?

Mr. McLEOD. Yes; everything we have has been already inserted in the hearings before the Ways and Means Committee, and we can provide similar tables.

Senator COUZENS. If you can direct my attention to what particular tables you refer to in the House hearings I will not ask you to duplicate it here.

Senator LA FOLLETTE. I am interested yet in just what it was Mr. McLeod was proposing to do in response to the request of the Senator from Michigan.

Senator CONNALLY. Mr. McLeod was called upon today to report just what he could furnish in the limited time.

Senator LA FOLLETTE. I understood that, but I would like to get it clearer in my own mind just what they are proposing now to run through these calculating machines or whatever they are, and what that data will show when it is assembled. Would you mind restating your proposal, Mr. McLeod?

Mr. McLEOD. The proposal is to take all corporations in the country that reported over a million dollars of net income, and that would include probably one-half of the total net income.

Senator LA FOLLETTE. Reported by corporations?

Mr. McLEOD. Yes. It would include say between 500 and 800 corporations. Then, we propose to take certain items on their income statements which would indicate the percentage of their income retained in the form of surplus or paid out in the form of dividends, and run a frequency table on that, and show the number of corporations that retained 25 percent, the number that retained 35 percent, the number that retained 50 percent, and so on, as a sample of the entire corporate income.

Senator GERRY. Would that tell you, for example, the number of corporations that come under the \$10,000 class?

Mr. McLEOD. It would not tell anything about the small corporations, it would include only the large corporations which provide a great bulk of the income.

Senator GERRY. Have you any statistics showing how many corporations there are in the \$10,000 class?

Mr. McLEOD. Yes; we have a detail.

Senator GERRY. And the number of shareholders they have?

Mr. McLEOD. We do not have the number of shareholders.

Senator GERRY. So that you do not know whether these corporations are simply corporations that are not doing any work at all, and not paying any income?

Mr. McLEOD. We know how many corporations there are.

Senator GERRY. I am not asking that, but I am asking the \$10,000-a-year corporations included in your basis. I want to find out how you arrive at the basis. You know how many \$10,000-a-year corporations there are?

Mr. McLEOD. Yes.

Senator GERRY. You know the capitalizations?

Mr. McLEOD. We could determine that, but we haven't the stockholders that they have.

Senator GERRY. You do not know how many stockholders they have?

Mr. McLEOD. We do not.

Senator GERRY. Do you know how much average dividends they pay out?

Mr. McLEOD. Not for the particular class of corporations, but we know it for all corporations.

Senator GERRY. I am not asking that, but just this particular class.

Mr. McLEOD. We have not considered that.

Senator GERRY. Then apparently you have not given any careful study to the \$10,000-a-year corporations, you have just taken it as a figure?

Mr. McLEOD. I think not, Senator. We have sufficient data for the basis of this estimate.

Senator GERRY. You have sufficient data for your estimate as to what your total income will be if you take all corporations in?

Mr. McLEOD. All income classes.

Senator GERRY. What do you mean by that? I am trying to find out if you have got a class of corporations that had \$10,000 a year. You say you have that data, but apparently you have not any statistics on how many stockholders there are in that class of corporations, and how many people will be benefited.

Mr. McLEOD. That is correct we do not have the number of people.

Senator GERRY. Have you got anything on a higher class, for example, \$50,000 corporations, have you anything on that?

Mr. McLEOD. The number of stockholders?

Senator GERRY. The number of stockholders and how much they pay out in dividends or anything else.

Mr. McLEOD. No; we do not have that.

Senator GERRY. You have not split up your corporations at all as to their size, have you?

Mr. McLEOD. Yes; as to size of net income. We have split them up as to the number of corporations that have an income of one to two thousand, two to three, five to ten, and so on, up to a million to five million, and five million and over. We have the corporations and the net income.

Senator GERRY. Then you have the number of corporations that have a net income and you have gone into the number of corporations that have a net income so much, and you have that schedule?

Mr. McLEOD. That is correct, and we could present that in a table.

Senator GERRY. I am not clear on that, and I would like to get it clear how you arrive at your statistics.

Senator WALSH. I should think if you were getting the number of corporations with an income of less than \$10,000, you would get it by adding the number of corporations of one to two, two to four, four to six, and eight to ten.

The CHAIRMAN. He has all of the information the Senator desires, as I understand, except the number of stockholders.

Senator GERRY. I am trying to find out just how they get at how many shareholders there were in these classes.

Senator BARKLEY. That would not appear in the Treasury reports.

Senator GERRY. I just wanted to find out what they did in that connection.

Senator CONNALLY. The stockholders change from day to day.

Senator GERRY. Of course that is true, and there is nothing to that.

Mr. McLEOD. I have a table here of which I would be glad to provide a duplicate which shows the number of corporations having income under \$1,000, two to three thousand dollars, three to four thousand dollars, and the amount of income in those classes.

Senator GERRY. But you have not broken that up into whether those are corporations of a certain size or not?

Mr. McLEOD. You mean by size of capitalization?

Senator GERRY. Yes; on your taxation basis.

Mr. McLEOD. That would not be necessary except in case of excess-profits taxes. This is corporations of a certain income.

Senator COUZENS. Could we have that put in the record?

Senator BARKLEY. Is that shown on the two tables you discussed yesterday?

Mr. McLEOD. No; that shown on the tables yesterday was the number of people receiving incomes, the size of the income, and the dividends.

Senator COUZENS. Mr. Chairman, may we have that put in the record?

The CHAIRMAN. Yes; that table may be placed in the record.

(The material referred to is as follows:)

*Estimated total corporate net income and number of returns by net-income classes, calendar year 1936, corporations reporting net income*

Net-income classes (thousands of dollars)	Total corporate net income (millions of dollars)	Number of returns	Net-income classes (thousands of dollars)	Total corporate net income (millions of dollars)	Number of returns
Under 1.....	28	76,923	25 to 50.....	295	9,397
1 to 2.....	55	42,799	50 to 100.....	383	6,240
2 to 3.....	86	38,904	100 to 250.....	571	4,229
3 to 4.....	54	17,764	250 to 500.....	499	1,628
4 to 5.....	41	10,496	500 to 1,000.....	557	906
5 to 10.....	152	24,466	1,000 to 5,000.....	1,336	744
10 to 15.....	119	11,032	5,000 and over.....	2,929	209
15 to 20.....	104	6,820			
20 to 25.....	99	5,029	Total.....	7,308	257,586

Mr. OLIPHANT. Other agencies, as I understand, attempted to compile the number of stockholders.

The CHAIRMAN. What other agencies?

Mr. OLIPHANT. I think the Federal Reserve Board has some information on it, and the Department of Commerce, and the Securities Exchange Commission.

Senator GERRY. Why can't we put that in the record?

The CHAIRMAN. That may be put in the record when it is prepared.

Senator GERRY. I would like to ask the expert another question. You put the tax at 30 percent, did you, on a certain class of corporations, 27 percent on a distribution of 30 percent?

Mr. McLEOD. The 15 percent tax runs this way. Corporations above \$10,000 pay 4 percent if they retain 10 percent, and if they retain 20 percent they pay—

Senator GERRY. Wait a minute, state that again, please.



Mr. McLEOD. On an adjusted income of a corporation having more than \$10,000, it has the choice of paying a certain tax on the income, depending on the percentage of the net income it has retained in the form of surplus, or the other way around, it can compute its tax depending on the amount distributed to stockholders. If a corporation retains 10 percent of the adjusted net income, the tax is 4 percent. A corporation with an adjusted net income of \$100,000 could retain \$10,000 and pay a tax of \$4,000.

Senator GERRY. All of that goes right into your table?

Mr. McLEOD. Yes.

Senator GERRY. Now, what I am trying to get at, what was the rounding in the amount of earnings in the size of the capitalization of the corporations on your basis of making this up.

Mr. McLEOD. That illustration has nothing to do with the basis of this.

Senator GERRY. And what you do not know is the number of the people who are stockholders?

Mr. McLEOD. We know the number of people it will affect of those who pay income taxes, which is shown on the table we presented.

The CHAIRMAN. Thank you, Mr. McLeod; I think that is all.

This will close these proceedings and the committee will meet Thursday morning at 10 o'clock.

(Thereupon at 11:55 a. m. the committee adjourned until Thursday, Apr. 30, 1936, at 10 o'clock.)