

[CONFIDENTIAL]

REVENUE ACT, 1936

HEARINGS

BEFORE THE

COMMITTEE ON FINANCE UNITED STATES SENATE

SEVENTY-FOURTH CONGRESS

SECOND SESSION

ON

H. R. 12395

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

PART 7

MAY 16, 18, AND 20, 1936

Printed for the use of the Committee on Finance

UNREVISED



UNITED STATES
GOVERNMENT PRINTING OFFICE
WASHINGTON : 1936

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REVENUE ACT, 1936

SATURDAY, MAY 16, 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 Finance Committee room, Senate Office Building, Senator Pat Harrison presiding.

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

Also present: L. H. Parker, Chief of Staff, Joint Committee on Internal Revenue Taxation and members of his staff; Middleton Beaman, Legislative Counsel, House of Representatives; Arthur H. Kent, Acting Chief Counsel, Bureau of Internal Revenue, Treasury Department; C. E. Turney, Assistant General Counsel for the Treasury Department.

The CHAIRMAN. The committee will come to order. Mr. Beaman, on this foreign credit matter, let us turn to that and will you give us an explanation of it?

Mr. BEAMAN. That is section 231. You cannot pass on it very intelligently unless you have decided your policy about the domestic corporations. Let me tell you the situation; let me tell you what the present law is and what the House bill did to it.

Under the present law, a foreign corporation is taxed exactly like a domestic corporation, namely, subject to the graduated rate of 12.5 to 15 percent, but it is taxable only on its income from sources within the United States.

The House bill changes that and divides foreign corporations into two classes. The first class is a foreign corporation engaged in trade or business within the United States or having an office or place of business in the United States. That kind of a corporation is taxed under the House bill 22.5 percent of its net income from sources within the United States, flat, and without any undistributed profits tax or anything else attached to it.

A foreign corporation not engaged in trade or business in the United States and not having a place of business or an office in the United States is taxed only on its income from certain specified sources; roughly, interest, dividends, rents, and fixed or determinable annual or periodical gains. It does not include capital gains and the rate of tax on that kind of income is 15 percent, which is flat with no deductions whatsoever against it; in other words, it is practically a tax of 15 percent on their gross income from such sources. It is expected to be collected by withholding at the source.

Senator KING. The gross income instead of net?

Mr. BEAMAN. Upon those specified sources and with no deductions. It is contemplated that the probabilities are that in most cases the Treasury can by regulation exempt such corporation from making returns, because the amount withheld at the source collects the entire tax.

Senator COUZENS. Is there any change in foreign banks?

Mr. BEAMAN. Foreign banks under the House bill are taxable at 15 percent on the income from carrying on the banking business in the United States, and 22.5 percent on the portion of their net income derived from sources within the United States, other than banking business. If the foreign bank is not engaged in trade or business in the United States and not having an office or place of business in the United States, it is taxed like any other foreign corporation of that class, namely, 15 percent on its income from these certain specified sources.

The CHAIRMAN. What is the tax now on the foreign banks?

Mr. BEAMAN. The same as any other foreign corporation.

The CHAIRMAN. There is no distinction?

Mr. BEAMAN. No, sir; there is no distinction.

Senator GEORGE. What did you say the tax on the foreign corporations is now?

Mr. BEAMAN. The same as domestic corporations, except that their income that you put the tax on is only their income within the United States.

Senator GEORGE. But they are allowed deductions the same as domestic corporations?

Mr. BEAMAN. Yes. And this class of foreign corporations are taxed under the House bill 22.5 percent of their net income from sources within the United States, namely, those engaged in trade or business in the United States and having an office or place of business here, they are allowed the deductions just like the present law. But this flat 15 percent tax on what you might call the nonresident foreign corporations, that is a flat tax without any deductions.

The CHAIRMAN. If we should carry out the general theory on that and we should adopt an 18 percent flat, then we ought to put in 18 percent instead of 15 percent there on foreign banks?

Mr. BEAMAN. Yes, but you have a worse proposition than that. Are you going to tax a domestic corporation 18 percent and if it pays dividends to a foreign corporation, are you going to tax that 15 percent or 18 percent on top of that? That presents a question which is a very serious one. I do not know what you want to do about it.

Senator KING. Where you have a graduated tax of 12 plus up to 15 plus applicable to this same sort of a foreign corporation and it derives income from other sources—

Mr. BEAMAN (interrupting). They are only taxable on 10 percent of that. In other words, 90 percent of dividends received is a deduction.

The CHAIRMAN. Is that changed in this, the 90 percent proposition? That is changed, is it not?

Mr. BEAMAN. Under the House bill, all dividends are taxable.

Senator GEORGE. With no deduction.

Senator GERRY. How do the English do it, Mr. Beaman?

Mr. BEAMAN. I do not know. Perhaps Mr. Parker can tell you.

Mr. PARKER. They have already taxed the English corporation when dividends are paid. If you are a nonresident alien or corporation, there is no further tax.

Senator GERRY. They are taxed at the source?

Mr. PARKER. They really get 22.5 percent, because the foreign corporation would deduct that amount from the dividend check just the same as if it was a resident, but the nonresident cannot come in and get it refunded in case the tax is less than 22.5 percent.

The CHAIRMAN. This is a rather difficult matter here, this foreign credit business and foreign banks. Will you tell us a little more about it, Mr. Parker?

Senator LA FOLLETTE. Mr. Parker, in the first place, in order that the committee may have this in mind, as I understand it, it is the position of the Treasury, and I would like to know if you confirm that, that under the present method we are not getting nearly the tax that we ought to get from these foreign corporations, both resident and nonresident, to use Mr. Beaman's designations of them. Is that true?

Mr. PARKER. That is true. It is not because our taxes are not theoretically high enough on the foreigner and as a theoretical system it is all right, but it just does not work. I think you will readily see why that is, because under our present system—taking the individual first—

The nonresident alien individual is supposed to pay practically the same tax as the American citizen, except he does not get the same exemption, and he has to file a return and be taxed on that part of his income that comes from the United States just exactly as if he were a citizen. You can readily see that that is impracticable. You cannot expect a Frenchman to make out one of our income tax returns. We cannot do it ourselves without a lot of trouble, and if France taxed us in the same way and we happened to own stock in a French corporation, we would have great difficulty in making out a French income tax return. Even the English income-tax returns are very difficult to understand by an American. Instead of having one return, they have half a dozen of them that you have to fill out according to the different kinds of income; whether it comes from lands, et cetera.

So that while we get a few wealthy individuals to file returns, we do not get the amount of foreign returns that we should get. What we do get from the foreigner is largely what we get on the withholding. We do withhold in the case of all payments to these nonresident foreigners, in the case of interest, rents, and a lot of other fixed income. We do not withhold in the case of dividends, so that we have undoubtedly been losing a lot of money.

Senator COUZENS. How much, would you guess? Have you any idea?

Mr. PARKER. I have an idea that about \$66,000,000, at least, annually is being paid out to individuals or foreign corporations, and that at least half of that escapes taxation. So that if we withhold on \$33,000,000, even at the 10-percent rate, that is \$3,000,000 picked up right there. The last time we had the complete statistics of foreign income was about 1924. At that time from all of it we were only getting 6 or 7 million dollars. I think it will at least double under this system, although the rates do not look as high.

Senator KING. What is the character of the investments in the United States by foreigners?

Mr. PARKER. It is varied, but it is largely in stocks. It is estimated that about half of the income derived from investments comes from investments in American shares, in the stock of American corporations. The other half is in bond interest, rents, and royalties. The dividends make up just about half.

Senator KING. Have not their investments largely depended upon the insecurity that they felt toward their own Governments and their own financial structures? For instance, now that Blum has come into power, it is quite likely that there will be quite a flight of capital from France to the United States in the purchase of stocks, and if Baldwin should be overthrown there would be quite a flight of capital from Great Britain to the United States, and that capital would be represented by bonds and stocks purchased in United States corporations. Is it your idea that most of the investments by foreigners are in stocks and bonds, and that we do not have a system sufficiently tight enough to obtain from them the income which we should?

Mr. PARKER. We get the income all right from the bonds because that is withheld. I do not think we lose much of that, Senator. What we have been losing is the tax on dividends. Of course, in just one respect we have always treated a foreigner better than an American citizen. He is not taxable on Liberty-bond interest. That is not taxable to him. He is free from tax on that income.

Senator KING. Let me see if I understand it.

Mr. PARKER. But that is quite a usual provision.

Senator KING. One of my friends who has been in Europe for a number of years told me that almost daily in the two or three cities in which he had been, the table was used or the wireless to purchase so many shares of this stock or the other stock, and perhaps the next day they would sell it because there was a decline and had sustained a loss; or perhaps the next day they would purchase more because of a feeling that the stock was going higher. And yet it would be difficult to determine just where those transactions occurred and who were the owners and what the profits or the losses were. I was just wondering how you were able to reach it?

Mr. PARKER. The way this bill is drafted, it exempts the foreigner from his capital gains. The Treasury has had a lot of trouble with that. Under existing law a foreigner is taxable just the same as an American on his capital gains. For a long time the Treasury, knowing the difficulties, did not try to enforce that provision. I think that is a fair statement. I think they just did not try to enforce it.

About 2 or 3 years ago, the Treasury attempted to collect the capital-gains tax from the foreigners, and they met with only very limited success; in fact, they came almost to an impasse. They cannot get the records. They will try to get the information from an American broker, and of course, he will give the name of a foreign broker, and the foreign broker will write back and say that the laws of his government prevent him from disclosing the names of his clients; so that it has not been effective on the capital-gains proposition.

The CHAIRMAN. There should be a differential in taxes to be imposed in these two classes to which you call attention, should there not? In the bill it is 15 percent and 22.5 percent in the two classes: Should there or should there not be a differential if we should adopt the 18-percent flat rate or any flat rate?

Mr. PARKER. The letter from the Secretary of State seemed to lay down this principle. As far as possible he wanted to treat the foreign companies the same as American companies, where it could be done. He did not complain that we put the 22.5 percent on a foreign corporation instead of the new plan, because he realized that we could not apply the new undistributed profits tax to foreign corporations.

On the other hand, when it came to banks that we taxed a flat rate of 15 percent, the Secretary's letter did indicate that he thought we ought to tax a foreign bank at the same rate, that is doing business in this country.

The CHAIRMAN. Do you see anything against that proposition? Why should not the foreigner be taxed on the same basis as the American?

Mr. PARKER. When we can, but we cannot do it very well when it comes to this distribution of profits.

The CHAIRMAN. It looks as though the committee were veering a little bit away from the House bill. Won't you gentlemen prepare and have ready for us the proper amendments, leaving the percentage blank, but carrying out the idea there if the committee adopts a flat rate?

Mr. BEAMAN. Well, I do not know that we can. Senator, on that point we want to know first whether the committee is going to accept the policy laid down in the House bill or make a differentiation both as to the foreign corporation and the nonresident alien which has not been described yet.

Take the foreign corporation: The differentiation in tax upon the two groups that I described; one engaged in trade or business in the United States and having an office or place of business in the United States which pay under the House bill 22.5 percent on income from sources within the United States; and the other group—

The CHAIRMAN (interposing). Why was that put at 22.5 percent, and domestic corporations were put in the House bill at 15 percent?

Mr. BEAMAN. The domestic corporations were not put in the House bill at 15 percent.

The CHAIRMAN. Certain corporations were put in the House bill on an average of 15 percent. Banks, for instance.

Mr. BEAMAN. Yes; but you are now dealing with foreign corporations, manufacturing and operating; business corporations and not banks, who under the House bill are not subject to the undistributed-profits tax. In other words, they do not pay on the undistributed profits.

The CHAIRMAN. Here is a foreign corporation that has an office in this country and a place of business in this country and doing business in this country, and they pay the same rate that the domestic corporation does, and we put the further proposition in there that when there is any distribution that it shall be withheld in this country and they shall pay at the source. Why would that not get at the same thing?

Mr. BEAMAN. We do not do that. A foreign corporation engaged in trade or business here or having a place of business here, there is no withholding on the payments to it. I am not speaking now of the dividends that the foreign corporation pays. That is entirely another question, but the dividends received or the rent received, or anything else received by the foreign corporation that is engaged in trade or

business here, who has a place of business here, there is no withholding at the source. You are collecting your tax from that kind of a corporation just the same as you do a domestic corporation.

Senator COUZENS. To that extent we can make the law applicable to those as we do with our own corporations?

Mr. BEAMAN. Except when you come to the question of the undistributed-profits tax.

The CHAIRMAN. Let us get to that.

Mr. BEAMAN. If you do that, the House bill saw the impossibility of doing that, and so they simply put on this flat tax. Why they put that at 22.5 percent, is, I presume, because that is the rate that they thought was right. You might have three or four different people who might each have different notions as to what the rate should be.

The CHAIRMAN. If we follow that theory, we would put about a 25 percent rate on there.

Mr. PARKER. My reasoning would be this. With this new proposal which you made, we are always going to get 18 percent flat on the net income, and then in addition we are either going to get 5 percent if it is all distributed, 5 percent additional from the stockholder, or if the corporation keeps it, 7 percent. That is very little difference. It seemed to me if we taxed this foreign corporation 24 percent—you see, we will never get less than 23 and never get more than 25 from domestic corporation income. Take 24 percent figuring a 50-percent distribution, and that would be very defensible, and then the corporation would not have to withhold. You would get 24 percent out of the foreign corporation. Don't you think so, Mr. Beaman?

Mr. BEAMAN. I do not quite follow you, but that is a matter to discuss, in order to make recommendations to the committee; but the thing that I am interested in getting clear is, and on which I do want to make a statement as far as I and my office are concerned is this: Whether you wish to carry out the distinction made in the House bill dividing up the foreign corporations, as to whether or not they are engaged in trade or business in the United States or have an office or place of business therein.

On this particular occasion I am speaking entirely for my own office, Mr. O'Brien and myself, and not for the whole group as I usually do. We feel, and so told the Ways and Means Committee, and see no reason to change our minds, that what is meant by "engaged in trade or business in the United States" is too indefinite a standard to base such an important difference on. I do not know what it means and nobody else knows what it means, and the Treasury here does not know what it means, and the Treasury—when I say the Treasury I mean some of the men down the line, I do not mean the high officials—called attention to the ambiguity in the phrase and said it ought to be cleared up, but nobody knows how it ought to be cleared up.

It seems to me particularly important when you come to the non-resident alien individual. For the purpose of making my point, I will describe that briefly. Under the present law, a nonresident alien individual is taxed like a citizen, normal and surtax, but includes only in his income that from sources within the United States. In the House bill they divide nonresident alien up into two classes just like foreign corporations; those engaged in trade or business in the United States being subject to normal and surtax just as at present,

but those not engaged in trade or business in the United States and not having an office or place of business in the United States are, just like that corresponding class of foreign corporations, are subject to tax only on certain specified classes of income, interest, dividends, rents, and salaries, and things that are susceptible of determination on an annual basis.

Senator COUZENS. Do you mind an interruption? I was going to say, when a foreign corporation declares a dividend to its stockholders—

Mr. BEAMAN (interrupting). Senator, that is entirely a separate question and I do not want to get it mixed up with this, if you don't mind.

Senator COUZENS. You mentioned it awhile ago.

Mr. BEAMAN. That class of nonresident alien on that class of income were taxed 10 percent flat without any deduction and without, and probably in most cases, the necessity of filing a return, and all of that 10 percent is expected to be collected by withholding at the source.

Under the present law, the distinction between foreigners engaged in trade or business in the United States as opposed to those not so engaged, is found in connection with the withholding proposition; in other words, the law provides that on certain types of income they shall be withheld at the source in a certain amount if paid to a foreign corporation not engaged in trade or business in the United States or not having an office or place of business therein.

That is just as indefinite there as it is under the House bill, but the indefiniteness does not lead to the same serious consequences, because it simply means if it is not withheld, or is withheld when it should not be withheld and it is corrected on the return, there is no serious trouble; but here whether you are going to tax a man 10 percent or whether you are going to tax him normal tax and surtax running up to 75 percent, it seems to Mr. O'Brien and me that that is too serious a matter to let go with such a very ambiguous phrase, and it seems to me it is going to lead to enormous difficulties and litigation; and we just want to be on record as telling you as we did the Ways and Means Committee, that we cannot recommend any such distinction. How to make it any more definite we do not know. Probably with time enough it could be worked out.

But to build up a system of taxation based on such an ambiguous phrase does not seem to us to be sound administrative policy. That is why I say—you asked us a moment ago to get together and fix up the proper things which ought to be done, and by that you mean to work up the things that appear to us to be in such form as to commend themselves to you in determining your policy.

The CHAIRMAN. Has this been a very prolific source of revenue, Mr. Parker?

Mr. PARKER. No; it has not.

The CHAIRMAN. I do not see how you ever collect any.

Mr. PARKER. You do not get much; you get seven or eight million. In 1924 we got seven or eight million from foreign corporations and individuals all put together.

The CHAIRMAN. But you think that this proposition of collecting the dividends at the source would be helpful?

Mr. PARKER. I think it would be. I do not think any country has had good success in trying to get very much tax out of foreigners. The only way they get it is by withholding.

The CHAIRMAN. The principle of letting a foreign corporation that is doing business in this country off with less taxes than a domestic corporation does not appeal to me in principle.

Mr. PARKER. They won't have to do it under the new plan. Under the old plan, of course, 22.5 percent was about all that we could do. You could not go much higher.

Senator KING. Mr. Parker, we have invested in Canada large sums. There are perhaps several hundred corporations in Canada, the majority of the stock of which is owned by Americans. How do they treat us there in Canada?

Mr. PARKER. They deduct a flat 5 percent on individuals at the present time.

Senator KING. On the net income?

Mr. PARKER. No; it is withheld at the source.

Senator KING. Five percent of what?

Mr. PARKER. Of whatever goes out on the dividends. They withhold 5 percent. When you get a dividend from a Canadian company, there will be 5 percent deducted.

Senator KING. That is the only tax that is imposed?

Mr. PARKER. That is the only one. Of course, if we put on 10 percent, they may raise their rate to 10 percent, and that raises a rather interesting question, because the American investments in Canada are about four times the Canadian investments in the United States. If they raise their withholding rates to 10 percent, we are going to get less tax than we would if we had a 5-percent rate, as far as Canada is concerned, because we have a foreign tax credit, and that 5-percent tax paid by our citizens is a tax credit against the tax they pay to the United States. That being greater in volume, if their tax rate goes up, we are going to lose money by the 10-percent rate.

The CHAIRMAN. Take the countries of the world as a whole; how does it apply?

Mr. PARKER. Almost all of the larger countries that have an income tax withhold at the source.

Senator KING. What are their rates, generally?

Mr. PARKER. France withholds at 18 percent; Germany at 20 percent.

The CHAIRMAN. They cannot object if we withhold 18 percent.

Senator GERRY. What is England?

Mr. PARKER. England withholds at 22.5 percent. Of course, their system is entirely different from any other country.

Senator LA FOLLETTE. That is the practical effect of it there, is it not?

Mr. PARKER. That is the practical effect, because you do not have any right to get a refund.

Senator BLACK. When that dividend comes to an individual in this country, how is it treated?

Mr. PARKER. The English dividend?

Senator BLACK. An English corporation which withholds 5 percent at the source.

Mr. PARKER. If the dividend is \$100, you would get \$95 from the Canadian company. You would put into your income-tax return here \$100 and add it to your other income. You compute the tax.

If your total tax happened to come out at \$5 with this \$100 in income, you would take \$5 off of the tax and pay no tax, or whatever tax you did pay, the \$5 which you paid Canada would be deducted after you computed the American tax.

Senator BLACK. In other words, we give credit for the amount of tax paid by the individual through the corporate device in that country?

Mr. PARKER. That is right.

Senator KING. So the more taxes they impose upon their net or gross profits, the less the American stockholder would receive in dividends, and therefore the less tax he would have to pay.

Mr. PARKER. If the foreign countries have a higher rate than what we do, we do not allow the tax credit to exceed what the tax would be in this country. We have a limitation on that tax credit. For instance, if we had a flat income tax of 10 percent and some foreign country had a flat income tax of 20 percent, in spite of the fact that they paid 20 percent, we would only give them a tax credit of 10 percent on that income.

Senator COUZENS. Senator King is right, however, that the higher the rate is, the longer we continue this credit business, the less tax we get.

Mr. PARKER. In the case of Canada, that is true.

The CHAIRMAN. What did you think of the testimony of some gentleman who appeared before the committee who said that they had some smelting corporation in Mexico and that they were organized and doing business some years ago and because of some proclamation or some law of Mexico, they were unable to consolidate. I have forgotten all of the details, but it seemed to me that there was a good deal of force in the argument presented by that gentleman.

Mr. PARKER. That came about, I think in the case of a holding company under 27 (j) and that is the section I believe that under a different plan might not have to be retained.

Senator LA FOLLETTE. May I ask you, Mr. Parker, waiving aside for a moment the difficulties that Mr. Beaman has pointed out with regard to classification, do you or do you not regard the basic principle for the taxation of foreign corporations and nonresident aliens doing business in the United States as a step forward so far as the tax procedure is concerned and the results for the Treasury?

Mr. PARKER. I think so, Senator; yes, I do. I think it is a step forward in the practical way of handling the tax on foreign incomes.

The CHAIRMAN. You gentlemen prepare the proper amendments, and we will consider them when they come.

Senator COUZENS. I think they may prepare the estimate based on the theory that is in the House bill and let us consider it. I mean, the language.

The CHAIRMAN. Mr. Kent, we wanted you to take up and discuss this morning this refund proposition or have you discuss the windfall, with such suggestions and changes that you would make in view of the testimony and the criticisms. Have you anything to offer to us constructively on it?

Mr. KENT. Would you like to take up the windfall taxes?

The CHAIRMAN. Let us take up the windfall first.

Mr. TURNER. I am not ready to submit specific amendments, that is, drafts of language on these points, but I can if you want to run over a number of points that the witnesses made.

Senator KING. You are speaking of the windfall?

Mr. TURNEY. Yes.

Senator COUZENS. Let us have that, and then we can discuss the theory of drafting the specific legislation later.

Mr. TURNEY. One point that several of the witnesses touched on was the fact that this tax on the windfall income will apply to processors who may for the entire taxable year have had a net loss, who lost more on their business outside of the windfall period than the amount of the windfall, and their suggestion was that the tax in no case apply to an amount exceeding the taxpayer's net income for the entire taxable year. That is a question of policy, and also to some extent of constitutionality. It was considered by the Ways and Means Committee, and they decided that as a matter of policy, they wanted it to apply regardless of whether he had a net income and regardless of how much it was. They met the constitutional doubt by the separability provisions at the end of section 501.

Senator KING. Suppose the losses incurred during the year grew out of some transactions that were involved in the windfall?

Mr. TURNEY. You mean the same class of business?

Senator KING. The same class of business. Did they differentiate between that and losses that might come from some extraneous source?

Mr. TURNEY. No; they did not make that distinction, although I think that the question that is before you divides itself into two parts. You can go the whole way and say that you will allow as an offset against this windfall income, any loss of any character that the taxpayer had, or you can say that you will allow as an offset against this windfall income any losses that he had during the other part of the year on the same type of business.

Senator GEORGE. Mr. Turney, this has been suggested to me. I went over it very carefully with the textile people. Of course other people also are interested in this. They suggested "such special income tax however shall not be computed or assessed where no net income is derived by such person from transactions during the taxable year in the sale of articles with respect to which such excise tax was imposed, and in no event shall such special income tax exceed any such net income so derived after payment of the ordinary tax otherwise imposed with respect to the net income from such transactions."

In other words, they were restricting the question here, as I understand it, to profits or income made on transactions in the sale of articles with respect to which the excise tax was imposed?

Mr. TURNEY. Yes; that is right.

Senator GEORGE. And not to their general losses.

Mr. TURNEY. That is correct.

Senator GEORGE. In other lines of business that they were engaged in.

Mr. TURNEY. That would be the effect of that language.

Senator COUZENS. Let me assume in connection with what Senator George has said, suppose there was a processor that had nothing else but pork packing, and he had a loss, then I assume the tax would not apply, is that correct?

Mr. TURNEY. You are speaking of the House bill?

Senator COUZENS. Yes.

Mr. TURNER. The House bill would apply to him if he recovered any impounded money and had passed that tax on. It would apply to him even though during the other part of the year when the tax was not impounded he lost money on the pork-packing business.

Senator GEORGE. If on his whole operations in the meat-packing business he lost money, he would nevertheless be taxed under the House bill?

Mr. TURNER. Yes.

Senator GERRY. How can you show that? You might if he puts the price on the next day or something like that. How can you prove whether he passed it on?

Mr. TURNER. That is unquestionably a very difficult question. It is going to be the hard part of the administering of this bill, although the bill itself attempts to handle that question by laying down a presumption as to whether or not he passed the tax on, based on his gross-profit margin during the windfall period as compared with his gross-profit margin during a period when there was no tax.

Senator COUZENS. Have you anything else to say on that?

Mr. TURNER. That is all I have to say on that particular point.

Senator LA FOLLETTE. Let us go on to the other points.

Mr. TURNER. The next point that I think of is this: Under the House bill where the tax had been impounded on certain articles, and those articles had not been sold until after the termination of the tax, the House bill would nevertheless require an investigation of the question whether or not he passed the tax on in the case of the article sold after January 6. The textile people made the point, and we are inclined to think there is a good deal in it, that it is hardly fair to consider the possibility of passing the tax on after it ceased to be in existence, and that the thing ought to be cut off as of that date. I think we are inclined to agree with them on that.

The next point, and this was made by the cotton-textile people, is the difficulty of segregating this group of transactions to the income from which this tax relates and computing the net income of those transactions segregated from the rest of his business for the year. They pointed out the extent to which the business is intermingled and complicated by the various articles coming from one lot of cotton. They suggest an option to the taxpayer of computing his net income for this quantity of his sales by using his average net income for similar sales for the entire year.

It is impossible to tell whether that would make us money or lose us money. We are inclined to think it would not average very much different and it would eliminate a tremendous job both for the taxpayers and for the Government, and I think we are inclined to favor that suggestion.

Senator GEORGE. I am glad to hear you say that, because I think that is a practical suggestion. I imagine that applies to packers as well, because they have various products out of the same hog.

Senator KING. One witness testified, as I recall, that some 4,000 separate accounts were in a given business in the South that they would have to investigate because of the grades of cotton and so on, and it would be an absolute impossibility and would take several years with a large staff of bookkeepers to go out into all of those ramifications and ascertain the profits and the losses. Have you encoun-

tered in your investigations, difficulties analogous to those encountered by the witness?

Mr. TURNER. He is speaking of the problem under this tax, which I think is worse than anything we have encountered in the past.

Senator KING. You mean the House bill is worse than the problems you would have to encounter aside from this?

Mr. TURNER. All I mean to say is that with respect to this particular problem of picking out a group of transactions out of the year's business, I do not think in any case we have had to do that on any large scale, and there is no doubt that his point about the difficulty is very well taken.

Senator COUZENS. Have you given any consideration as to whether or not the taxpayer himself will take a refund of the processing tax he paid in August 1933 in lieu of making a claim for the stock he had on hand January 6, 1936?

Mr. KENT. I think that comes under title IV.

Mr. TURNER. Mr. Kent has considered that more particularly, and I think he can answer that when he takes up the later provisions.

Another point that has been made is that this question of whether or not he shifted the burden ought to be eliminated in the cases where the taxpayer has made a refund of the amount of tax to his customer. I think that point is well taken. It is really a defect in the mechanics of the bill as it was set up, which we will be very happy to straighten out.

Senator KING. You think he ought not to pay a tax if he made a refund?

Mr. TURNER. That is right. That was not the intent of the bill, and I think it would have reached the intended result, but by a great deal of unnecessary labor.

For the purpose of determining this question of shifting the tax, the House bill provides for a comparison, as I said, of his gross profit margin during the windfall period, with his average gross profit margin during the five taxable years preceding the imposition of the tax. The textile people contend that that 5-year period is unfair to them because it includes more bad years when they lost than it does good years when they made some income. They are very anxious to have that made 6 years so as to bring in 1927, which was a pretty good year. They also would like to be given the right to pick out of that 6-year period any years they want.

I think we would be afraid of that last thing but I do not think we would object to making it 6 years.

Senator WALSH. Why should that not be done?

Senator COUZENS. I think it should.

Senator GEORGE. Yes.

Senator KING. Have you prepared an amendment, or will you embody that in one?

Mr. TURNER. I have been working on some of these points. I have not any drafts with me to submit, but I will have them the first of the week.

The next point is this March 3 date limiting the deduction which they get for rebates to their customers of the amount of the tax. There has been a good deal of complaint about that, and I think that we would be quite willing to have that date extended to say 30 days after the enactment of the act and give them a chance to pass the money on.

Senator GEORGE. I think that is very, very just, because I called the attention yesterday of the committee to one of the largest textile manufacturers in Georgia who to my personal knowledge obtained the services of all of the available auditors and accountants that he could get immediately after the decision of the court, and decided first upon the repayment of all of the taxes in his hands or that had fallen into his hands, whether he had contracted or not, upon the broad basis that he had to deal fairly and justly and impartially between his customers, and they did not actually complete their computations until March 3 and were not able to make any remittances until after March 3, although they were working constantly on the program.

Senator COUZENS. The Treasury agrees with that?

Mr. TURNER. Yes, sir.

Senator KING. Keep that in mind in drawing your amendment.

Mr. TURNER. We were inclined to think at first that that would increase our administrative job under this thing, but while it does put us to the trouble of going to the person who gets the rebates to see whether or not it constitutes unjust enrichment to him, on the other hand the computations in the case of that middleman will not be as complex and difficult as they are in the case of the original processors; so we think we may not come out so badly on that point.

The cotton people have also suggested that in computing these margins for the purpose of determining this question of shifting the tax, they be allowed to use averages for the year's business, a similar point to the one made on the computation of net income, and we are inclined to think that that, too, is the best practical solution of a pretty bad situation.

Senator KING. Are there any other points you desire to make?

Mr. TURNER. The tire people have pointed out that there is a little quirk in this tax as follows: They were allowed to credit the processing tax against the tire tax under the 1932 act.

Senator GEORGE. They paid a 2½ tire tax?

Mr. TURNER. 2½ cents a pound on the tires, and they were allowed to deduct from the weight of the tires the weight of the cotton used in the tire if the cotton had borne the processing tax. The effect of their getting back the processing tax is automatically to increase the tire tax, so they do not get any windfall in those cases, and we are inclined to favor a provision which will give them an allowance for that situation.

Senator KING. That would be very difficult of ascertainment, however.

Mr. TURNER. I think that is one case, Senator, where there would not be much difficulty, because the automatic effect of recovering this cotton processing tax was to cause an equivalent increase in their tire tax. They just lost a reduction in the tire tax which they otherwise would have had.

Senator GEORGE. It amounted to reimposing the whole tire tax.

Mr. TURNER. Another point which I think is more a defect or an oversight in drafting is that under the House bill the provisions might result in a determination of unjust enrichment with respect to the impounding of the tax on articles which were exported or delivered for charitable distribution and that sort of thing, where the processor would have gotten a refund even though the tax had been valid.

We are inclined to favor a provision giving him an allowance for those cases, since there is not any real windfall there.

Senator WALSH. Are those the cases where the exporter received his refunds that were due him up to the time of the Supreme Court decision, and thereafter the Treasury suspended any more refunds?

Mr. TURNER. I think you have in mind one of the points that Mr. Kent is going to cover. That situation is involved here to this extent, that the amendment to the windfall tax that I was talking about will prevent those refunds which he did get during the tax period from being treated as unjust enrichment, since they were refunds contemplated by the system under the act.

In connection with this tax credit which is provided for in the bill to prevent double taxation of the unjust enrichment, the cotton textile people have suggested that they also be allowed a credit for State and local taxes on the income or money involved. I think we would be inclined to oppose that.

Senator COUZENS. Does that amount to much?

Mr. TURNER. I would not be in a position to say. Obviously it would vary from State to State, depending on what their tax system was and what their tax rates were.

Senator BAILEY. What method do you mean?

Mr. TURNER. First they point out that there will be some State income taxes in connection with the increase in their income resulting from the return of this impounded money.

Senator BAILEY. If they get an income and pay taxes on it and thereafter the income is taken away from them they would have the right to reopen the matter in the States, if they paid the tax, is that not correct?

Mr. TURNER. I think you are right, Senator, as far as I know about the State laws. I think it is probably safe to say they allow deductions for Federal taxes. So, as you see, there is a possibility of ironing out this point that they are complaining about with the States, rather than asking the Federal Government to do it all.

Senator KING. Perhaps they anticipate that the State books are closed and that the States might resist any effort to reopen the cases for the purpose of allowing them deductions.

Senator COUZENS. We can take care of that by future legislation.

Mr. TURNER. This situation is rather recent, Senator. I should not think that there would be much of that.

Senator KING. You may proceed.

Mr. TURNER. It has also been suggested that the due date of the returns on this tax for the first year ought to be later than the date provided for in the bill, which is 2½ months after the passage of the act. I think it is probably true that there will be a good deal of difficulty in getting these returns in by that date.

On the other hand, under the administrative provisions which are made applicable to this bill, the Bureau can and undoubtedly would give extensions up to 6 months, where they were needed. So I think the practical question is really whether you want to leave this the way it is and have interest run on this tax from the date provided for in the bill, the actual returns and payment being taken care of by extensions, or whether you want, in the bill, to extend the time or not, that is, whether you want to only put off the due date of the return or put off the date when the interest starts on the taxes.

Senator BAILEY. You mean the interest on the overdue taxes?

Mr. TURNEY. Yes; the 6 percent a year on overdue taxes.

Senator BAILEY. The overdue windfall taxes you are talking?

Mr. TURNEY. Yes.

Senator GERRY. In reference to that return, is there any special provision in this windfall tax that makes it different from the other?

Mr. TURNEY. The only thing that is specially provided for in the windfall tax on this point is providing for the due date of the return. It is to be, for the first year, 2½ months after the month in which the act is passed, since, under the general administrative provisions, it would have been due last March 15.

Senator BAILEY. What would the interest be in the event of dispute or litigation?

Mr. TURNEY. The interest on this windfall tax would be the same as on income taxes in general.

Senator BAILEY. There ought not to be any interest if the Government recovers. That would keep the Government down to an exact claim. If the claim is for \$2,000, for instance, the man does not have to pay interest on anything.

Mr. TURNEY. Take an exact case, for instance. If the man returns a certain amount and the Government claims \$2,000 more than he returned, and it is finally determined that the Government is entitled to \$1,500, the Government gets interest on the \$1,500, but not on the \$2,000.

Senator BAILEY. Suppose I owe you \$1,000 and you refuse it, and then the final adjudication is that it is \$1,000, why, I have stopped my interest. That is the law.

Mr. TURNEY. This bill would not change that in any respect.

Mr. KENT. I might say, Senator Bailey, that we have a regular procedure where a taxpayer admits that a portion of the deficiency is due, but is contesting the remainder; whereby he can waive appeal to the Board with respect to that portion and pay that amount and stop the running of interest, and then they go ahead and litigate the balance.

Senator BAILEY. If he tenders it.

Mr. KENT. We are glad to get any part of the additional amount as quickly as we can, as long as it does operate to prejudice the rights of the Government with respect to the balance.

Senator GERRY. What happens if instead of going to the Board he goes to the court?

Mr. KENT. In order to go to the court of course he has to pay the amount of the deficiency asserted in the 90-day letter, then he files a claim for a refund for all or some portion of it. If that claim is rejected he goes to court, and if his claim is either allowed by the Commissioner or sustained in the court he gets 6-percent interest on the amount of that claim from the date that the payment was made to the Government.

Senator WALSH. As I understand it, the taxes must be paid in 2½ months after the passage of the act.

Mr. TURNEY. Yes.

Senator WALSH. What further time did these witnesses request?

Mr. TURNEY. The suggestion was that it be made the sixth month after the month in which the act is passed, instead of the third.

Senator KING. Proceed.

Senator BAILEY. What provision do you make with respect to offsets in the suit? Suppose you brought that in to me and I made an offset by saying in the month preceding the act of the last Congress I paid you \$500,000 taxes, would you let me offset that?

Mr. TURNER. I would not think so, Senator.

Senator BAILEY. That is exactly the same proposition as a case between you and I in a civil case. Why should not the Government do the same thing? If you sue him you ought to allow him an offset.

Mr. TURNER. Well, I am not prepared to discuss the procedure in the civil suits. If you overpaid some other tax you are entitled to get that back with interest.

Senator BAILEY. Are you a lawyer?

Mr. TURNER. I am a lawyer.

Senator BAILEY. You agree that that is the rule of law, do you not? If you sue me I can offset your claim with something that you owe me.

Mr. TURNER. As I recall, obviously that depends on local law.

Senator BAILEY. That is common law. That is not written in any books, it is written in all the Supreme Court Reports of the United States and all the State Reports. A man always has an offset. If he did not there would never be an end to litigation. You would have to sue me for what I owe you and I would sue you for what you owe me, and the court says you can offset a counter claim.

Senator KING. I think in some States, Senator, a counter claim must have some germaneness to the transaction. You could not offset a tort against an action ex contractu.

Senator BAILEY. That is not this case at all.

Senator COUZENS. Let us proceed.

Mr. TURNER. This bill does not in any way change the existing procedure in income tax cases.

Senator BAILEY. What do you think about allowances for offsets?

Mr. TURNER. I would not think we ought to make any provision in connection with this tax for offsets which we would not allow against an ordinary income tax.

Senator BAILEY. Then we simply exert our arbitrary power to collect without allowing for the offset.

Mr. TURNER. Of course, Senator, if this, like other income taxes, goes to the Board of Tax Appeals it is not practical to provide that the taxpayer can make a claim of an offset for a processing tax refund, for instance, over which the Board of Tax Appeals has no jurisdiction and is the type of case which the Board of Tax Appeals does not consider at all.

Senator BAILEY. We have provided here for a means of recovery, by the Government, of taxes unjustly held, that are called unjust enrichment. Now, if the United States Government unjustly enriched itself through an unconstitutional tax why should not I have the same right as the Government? When the Government goes into court it ought to go in on an equality with the citizen.

Mr. TURNER. Of course, I think the first thing to keep in mind, in respect to this tax as any other, is that it will be a very exceptional case where the Government goes into court to sue the taxpayer for the tax. That must be handled by the usual machinery for the collecting of taxes. In this case the taxpayer has the right to petition

the Board of Tax Appeals for redetermination of the deficiency asserted.

Senator BAILEY. If I overpaid my taxes in 1934 and underpaid them in 1935 you come in and recover against me for 1935, and if I show that I overpaid in 1934 you give me a credit for that, don't you?

Mr. TURNER. Yes; that is right.

Senator BAILEY. That is the same principle.

Mr. TURNER. This bill does not apply any different principles to the recovery, assessment, and collection of this windfall tax than are applicable to income taxes in general.

Mr. KENT. I might say this, Senator: If your claim, or if the taxpayer's claim for refund of processing taxes were before the Bureau and were deemed by the Bureau to be a meritorious claim and were allowed so that there was a liquidation thereby of the amount due, then there would be a published decision put out stating that the taxpayer was entitled to a return on that amount. There would be no difficulty in arranging for the application of that amount against any other tax claim that the Government might have against the taxpayer.

If, however, the claim for refund of the processing tax were rejected on the ground that the taxpayer had passed on the burden of that tax under section 21 (d) to somebody else, you would have a different situation. Then he would have to go into the district court, or into the Court of Claims, and sue for that amount. So you would have his claim against the Government pending in one court and you would have the Government's claim, which he was resisting under the windfall tax, pending in the Board of Tax Appeals.

Senator BAILEY. Why not avoid that procedure and let him offset in the case that we are providing the machinery for it?

Mr. KENT. Of course, one case might be decided sometime before the other.

Senator BAILEY. Yes; but we can decide both cases here.

Mr. KENT. Of course if the Board of Tax Appeals had jurisdiction over both cases there would not be any difficulty.

Senator BAILEY. It would be the Commissioner here in the first instance, would it not?

Mr. TURNER. Yes.

Senator BAILEY. Put the authority in the Commissioner, with the right of appeal by petition. What I am driving at is the just disposition of the matter.

Mr. TURNER. In connection with the determination of the margins on these transactions, for determining whether or not the burden is shifted, the cotton textile people particularly have asked for a consideration of direct manufacturing costs, as well as material costs, in computing the gross profits.

Senator GEORGE. The direct cost?

Mr. TURNER. The direct cost of manufacture. As you recall, in discussing section 21 (d) the Secretary of Agriculture indicated that he was opposed to consideration of those items.

Senator COUZENS. And if the N. R. A. was in existence and in force at that time the condition ought to be considered.

Senator GEORGE. I think he indicated that some consideration should be given. There are other things affecting this margin of profit.

Mr. TURNER. Yes; and this bill does provide, after the presumption is applied on the basis of material costs only, the taxpayer can come in and rebut the presumption.

Senator GEORGE. That is not a conclusive presumption.

Mr. TURNER. No. The suggestion of the textile people is that the direct manufacturing cost ought to be a part of the presumption and not a part of the proof to rebut the presumption.

The CHAIRMAN. Mr. Turner, you are going to prepare these in writing, are you not?

Mr. TURNER. Yes, sir.

The CHAIRMAN. Some of these suggestions?

Mr. TURNER. Yes, sir.

The CHAIRMAN. So we can proceed along those lines.

Mr. TURNER. That is right.

The CHAIRMAN. We are trying to get some action early in the week.

Mr. TURNER. Yes. There are a number of rather minor points which I think can be taken up later.

The CHAIRMAN. Have you any suggestion as to any amendments that any member of the committee would want to have prepared?

Senator COUZENS. I think we have done that as we have gone along. I think we ought to hear from Mr. Kent now.

Senator GEORGE. Section 21 (d) is in the refund provision?

Mr. TURNER. Section 21 (d) is not in this bill at all.

Senator GEORGE. I know it is not in there, but are not you doing something about it?

Mr. TURNER. Yes. I think Mr. Kent can discuss that, along with the other refund question.

The CHAIRMAN. Yes.

Mr. KENT. I might say that a proposed revision of section 21 (d) has been before the subcommittee of the House Ways and Means Committee in recent days. We have had several conferences with them and I believe that that provision is likely to be reported out over there very soon.

I think what the subcommittee will try to do is write into the revision of 21 (d) essentially the same standards and prima-facie presumptions in dealing with this question of passing on that will appear in the windfall tax title as it is revised for consideration by your committee. The fundamental problem involved in the two cases is the same.

The situation, however, is different in this way: Under the windfall tax the Government is trying to collect the tax. In the other case the taxpayer is attempting to procure a refund of tax already paid to the Government. But the fundamental issue in both cases, if the principle of section 21 (d) is retained, is exactly the same. If he did not pass on the tax, if he absorbed the tax then there would be no windfall within the meaning of title IV, and, similarly, if he absorbed the burden of a processing tax that he had paid in 1933 or 1934, or the early part of 1935, then he is entitled to obtain a refund on the amount of tax apaid from the Government.

There have been several suggestions made during the course of the hearings before your committee with respect to changes that might be made in title IV. Some of those suggestions undoubtedly possess merit. I think if some of them had been made during the hearings

before the House Ways and Means Committee they would have been taken care of and would have been incorporated in the bill which came over here. But there were some suggestions or criticisms made in the Senate hearings which had not been made at the time the subcommittee's report was the subject matter of the hearings before the House Ways and Means Committee.

It is not surprising two or three situations have been overlooked, because it has been a very complicated situation that we have been dealing with.

One of the suggestions made with respect to section 601 of title IV, which deals with refunds under the Agricultural Adjustment Act on exports, deliveries for charitable distribution or use, and so forth, and which was approved by the Secretary of Agriculture in the statement read to your committee, is that the proof of payment be dispensed with in connection with the claims under 601, just as is done in connection with the floor stocks claims under section 602, and we see no sufficient reason why that change should not be made. I think that the situation is essentially the same in both cases, provided that processors in general are not included under section 601. If processors were brought under section 601 there would be great danger in that, because there is no reason, so far as I can see, for making a refund to a processor on the ground that he has exported the processed commodity or that he has sold that commodity to a charitable institution, if the processor himself never paid any tax. The Treasury never got any money out of that transaction and there is no theory, so far as I can see, upon which a refund could properly be made to such a processor. It would just be an out-and-out gift, with no reason for making it.

Moreover, a large number of processors who were exporting processed commodities never paid any tax under the Agricultural Adjustment Act. Right from the very beginning they were permitted to file bonds with the Treasury to secure the Treasury against loss of tax in the event that commodities destined for export were diverted from export and were sold in the domestic market.

There is a special provision involving four or five processors of cotton bags which has caused us a great deal of difficulty, and I am working on an amendment to section 601 which I think will take care of that situation, without opening up section 601 to claims by processors in general.

Senator WALSH. Which are left out and they really ought to be included?

Mr. KENT. That is correct. There were four or five of them that were caught in a very difficult position which was not of their creation, and in one way or another we certainly will try to take care of their situation in a fair manner.

Senator BAILEY. There were many cases under the Agricultural Adjustment Act where cotton was sold for export and the taxes were not paid?

Mr. KENT. Yes, sir.

Senator BAILEY. The incidence of the tax was at the breaker and they had to pay, unless they got an extension?

Mr. KENT. I am not intimately familiar with the details of the situation, because I had very little to do with it.

Senator BAILEY. I know that was the ruling. I recollect the phrase "the incidence of the tax was at the breaker."

Mr. KENT. There was a provision to that effect. It may have been in the regulations.

Senator BAILEY. They had 60 days thereafter in which to pay, then they could get extensions?

Mr. KENT. That is right. They could file a bond. If they had exported the goods in the meantime it would have been senseless to collect the tax with respect to the goods exported and then turn right around and refund it.

Senator BAILEY. They would not pay the money?

Mr. KENT. Well, I do not think they would. But the point is that is that if section 601 were broadened to include processors in general and at the same time the other amendment was adopted dispensing with any proof of payment of the tax, human nature being human nature, I am afraid that some of them would take advantage of the situation and file claims. I hope that there would not be many, but I believe that with a provision to take care of the peculiar case of these processors of cotton bags, and with an amendment of section 601 to incorporate a provision similar to that in 602, dispensing with proof of payment, that the meritorious objections to section 601 as it stands, which were made in the course of the hearings, would be well taken care of.

Senator COUZENS. Do you want to touch on the floor-stock tax? I would like to go in a minute.

Mr. KENT. Yes, sir.

Senator WALSH. Section 602?

Mr. KENT. Section 602. The principal suggestion that was made there was that an option be given to holders of floor stocks on January 6, 1936, to accept in satisfaction of their claims the amount of the original floor-stocks tax which was paid back in the summer and fall of 1933.

Senator BAILEY. Provided he had paid taxes on the floor stocks?

Mr. KENT. Yes, sir. Of course there would be some individuals or firms which had started up in business since that time and there would be other individuals and firms who were in business in 1933 but who had gone out of business since.

Senator BAILEY. What are you going to do about the variation in the inventory? A man might have a thousand bales of cotton and on January 6 he only had 500.

Senator COUZENS. They are going to suggest an option, Senator, at the election of the taxpayers.

Senator BAILEY. All right. Let us see how you work the option out.

Mr. KENT. I think I should say first that I have consulted with the men who are familiar with the situation in the Bureau of Internal Revenue and in the Department of Agriculture, and they are very apprehensive as to the effect of such a change if it were made. In the first place, they say that if this option were given what would happen would be this: Where their floor stocks on January 6, 1936, were materially smaller than they were back in 1933 they would exercise the option and take the refund of the tax originally paid. On the other hand, where their inventories on January 6 last were materially larger than they were back in 1933 they would take advantage of the provision of the bill as it now stands. So that the option in general would work very much against the interests of the revenue.

Now the principal argument, of course, which can be made for allowing such an option is that it would minimize very greatly the administrative difficulties. We know how much tax was paid back in 1933, and it is a very simple matter just to refund that amount, if that is what the law provides for. Deputy Commissioner Bliss, however, tells me that from private conversations that he has had in the past, before any legislation was suggested, with members of some of the groups that appeared in advocacy of that suggestion, he believes that the burden of the tax was passed on both in 1933 and in 1936. If the burden of the tax was passed on in 1933 they would not be able to obtain the refund of that tax under the provisions of section 21 (d), and if the burden of the tax was passed on last January, after the decision, they would not be able to get refunds under section 602 as it now stands.

Senator COUZENS. But your prior witness said that the probability of passing it on after January 6, 1936, was very remote.

Mr. KENT. Yes, Senator; I think that is probably true, and I was interested in that suggestion. I was just going to suggest if, in the windfall-tax provisions, the committee should deem it sound policy to, in effect, write into the law a presumption that no tax be passed on after the date of the decision in the *Hoosac case*, the administration of 602 could be very much simplified by writing a similar provision into it, in which case our only administrative problem would be to determine the amount of inventory on hand on January 6, inventory, that is, of goods which were subject to the tax, and to make a refund on that basis.

Now that will not be as difficult as it might seem, because the decision came at a pretty good time. The taxpayers who were on the calendar-year basis, and that includes most of them, will have taken inventory on the 1st of January, and you can add to the amount of that inventory the additions thereto shown by their invoices, and we can estimate without difficulty on the basis of their average volume of business, what the sales were, and what deductions should be made from the inventory on account of the sales.

You see, there were only two or three business days in between the first of the year and the date of the decision. If that change were made I think it would so greatly simplify the administration of this particular group of claims that there would be no particular advantage in allowing them the option which has been suggested.

Senator BARKLEY. Mr. Kent, could you prepare amendments along the lines suggested for the benefit of the subcommittee that has been appointed on this proposition, of which I happen to be chairman?

Mr. KENT. Yes, sir. I would be glad to do that. I have rough drafts of most of them in my papers at the present time. I believe that I have dealt with the major suggestions.

There is one other suggestion, or meritorious criticism, which has been made which would also be taken care of if the change that I have just referred to was made.

There were some groups of dealers came in who said that they would be able to establish—bakers of bread, for instance—that they had been changing their prices on account of the tax, that is, that they had absorbed the burden of the processing tax and therefore that there was never any occasion for them to make any reduction in their prices

after January 6 on account of the decision in the *Hoosac case*. Manifestly, we do not want to discriminate against them, and the bill, as it is framed at the present time, might have that effect.

One or two witnesses objected to subsection (h) on page 233, which reads:

In the absence of fraud or mistake in mathematical calculation the finding of fact and the decision of the Commissioner upon the merits of any claim under this section shall not be subject to review by any other administrative or accounting officer, employee, or agent of the United States.

They apparently were not aware of the fact that that is virtually identical with the provision in the general law which makes the determinations of the Commissioner with respect to refunds conclusive, so far as the administrative stage of the claim is concerned, except in cases of fraud or mistake in mathematical calculation. That is, the Comptroller General does not have the power, under the present law, and has not had for a good many years, to review the determinations of the Commissioner on refund claims on the merits.

Subsection (i) was also criticized by one or two witnesses. As I see it, that involves purely and simply a question of policy.

So far as the section 602 claims are concerned, there is no legal right of any sort in any taxpayer to claim or assert any claim for this type of refund against the Government of the United States. It is a special provision which the Ways and Means Committee thought was justified in the interests of fairness and sound public policy. Now the claims under this section run into the hundreds of thousands. Many of them are very small, and it is just a question of whether Congress deems it sound policy, under those circumstances, to throw a lot of these cases into court.

Senator GERRY. Does that refer to just the cases under this section?

Mr. KENT. Under this section. There is a similar provision also under section 601. I might say with respect to the cases under section 601 that the case is not quite so clear, because this section 601 really operates to reinstate or revive the rights which the taxpayers enjoyed under the Agricultural Adjustment Act before it was held unconstitutional. So there is that difference between the two sections. On the other hand, we never had any trouble in administering these export and charitable claims before the act was held unconstitutional, and I would not anticipate that we would have any more difficulty under section 601. The taxpayers were in general satisfied with the Commissioner's disposition of the cases.

The CHAIRMAN. Mr. Kent, you have all this matter prepared. I do not think we ought to take any action this morning on this proposition.

Mr. KENT. Yes, sir.

The CHAIRMAN. We will take it up early in the week, so that you will be ready on these estimates that you are working on and have them for us Monday morning.

Mr. KENT. Yes, sir.

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

(Whereupon, at 11:54 a. m., the committee recessed until Monday, May 18, 1936, at 10 a. m.)

REVENUE ACT, 1936

MONDAY, MAY 18, 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, Bailey, Clark, Byrd, Lonergan, Black, Gerry, Guffey, Couzens, La Follette, Metcalf, and Capper.

Also present: L. H. Parker and C. F. Stam, of the Joint Committee on Internal Revenue Taxation; Middleton Beaman, legislative counsel, House of Representatives; C. E. Turney, Assistant General Counsel for the Treasury Department; Lawrence H. Seltzer, Assistant Director of Research and Statistics, Treasury Department; Charles T. Russell, Deputy Commissioner of Internal Revenue.

The CHAIRMAN. Mr. Parker, what other questions are there? We discussed Saturday the unjust enrichment title, the refund title, and the foreign credit matter. What other propositions are there in this bill, not counting the question of undistributed-profits taxes?

Mr. PARKER. Of course you have named the most important ones. There were some other changes. One was in respect to complete liquidation of a corporation. We were informed, reliably, that there were a considerable number of holding companies that desire to liquidate. In the 1934 act we provided that on a liquidation of a corporation when the stockholder received his money in liquidation and that money was more than what the stock cost him he was taxed 100 percent on that gain.

Under the capital gains bracket system, you will remember that if you hold an asset over 5 years only 40 percent goes into income; if you hold it over 10 years only 30 percent goes into income. So we made a change in this section about complete liquidation which permits the stockholder to be taxed under the bracketed system set up in section 117. He pays the regular capital gains rate.

The severity of the present rate is so great that it just prevents liquidation. If you give them the capital gains rate they will liquidate and you will get in some money. When they have to pay on 100 percent of the gain that is just like an embargo.

The CHAIRMAN. Mr. Parker, in the case where individuals owned toll bridges and the State pays for them in taking them over, where there is a forced liquidation by statute, it seems to me that those people ought to be protected in some respect.

Mr. PARKER. I am of the opinion that under the facts given me the provision I just described would take care of the matter.

The CHAIRMAN. You think this new provision would take care of that situation?

Mr. PARKER. I think so. For instance, here is one of these toll-bridge companies, the company has sold the bridge to the State, we will say, therefore the company has now got the money, and they want to liquidate the company, they liquidate it and distribute it to the stockholders. Each stockholder will subtract from the amount he receives the cost of the stock to him, and that gain will be taxed under section 117, according to the length of time during which the shareholder has held his stock. So that if he held it over 10 years he will only pay a tax on 30 percent of the gain instead of 100 percent of the gain. We will get a tax, and we ought to get a tax, but I do think it is fair to tax them as a capital gain. We will give them that relief.

Senator CONNALLY. You mean it is fair to tax them on all of it in that taxable year? The rate might be much higher than it was in former years.

Mr. PARKER. That is the purpose of our bracketed rate. We only tax them on 30 percent of it, Senator, and that is the relief proposed in the bill.

Senator CONNALLY. I thought you advocated the tax on all.

Mr. PARKER. The present law taxes it 100 percent.

Senator CONNALLY. It does?

Mr. PARKER. Yes; that is so severe that it is just preventing liquidation.

Senator CONNALLY. Mr. Chairman, I may say that there was a party here the other day who was advocating the same principle relative to people holding mineral leases on oil and coal. They say they will not sell them, they will just keep them because they have to pay such a tremendous tax in the year in which they sell them.

Mr. PARKER. The provision that I have just described would not take care of your oil leases.

Senator CONNALLY. I understand that, but it is the same principle.

Mr. PARKER. It would be a similar principle. Of course they get that relief if they have held a lease now for over 10 years, but the trouble is, as you know, Senator, with oil leases that you cannot hold them.

Senator CONNALLY. You cannot hold them. Nobody has held them 10 years, because if you hold them 10 years somebody else has got all the oil long ago if you do not develop it yourself.

Mr. PARKER. I have no doubt that in a speculative industry like oil the high rate does prevent transactions. We used to have a provision in the 1918 act that limited the tax to 20 percent of the selling price, and then later on we limited the taxes to 16 percent of the selling price.

Senator CONNALLY. These parties advocated the reinstatement of that law, even if it goes higher than the old rate, but that we still have some limit on it so they can sell.

Mr. PARKER. Those rates look to me now as being too low.

Senator BAILEY. What is the rate you now propose?

Senator CONNALLY. He says if they hold it 10 years it is 30 percent.

Mr. PARKER. We tax the income at the same rate. It is a matter of how much of the gain you take over and put into the income.

Senator BAILEY. It depends on how much is allocated?

Mr. PARKER. That is right. Say that you have a share of stock for which you paid \$100 and you sell it for \$200, your gain is \$100. Now, if you have only held that stock for one year or less you are taxed on the whole \$100. That takes care of the speculative transactions.

Senator BAILEY. It is on the capital gains principle?

Mr. PARKER. That is the principle. Now if you have held this share of stock more than 1 year but not more than 2 years, then you take 80 percent of the \$100, or \$80, you put that in your income, and you are taxed on the \$80. That results, you might say, in cutting the rate down by one-fifth. Although you use the same rate it has the equivalent effect of reducing the tax on that particular portion.

Now, in the next bracket, 2 to 5 years you tax 60 percent. Five to 10 years you tax 40 percent, and more than 10 years you only include 30 percent of the gain in your net income.

Senator GEORGE. Mr. Parker, in the 1935 act we did provide for the tax-free liquidation of subsidiaries where more than 80 percent of the stock was owned by the parent company, or another corporation.

Mr. PARKER. That is correct.

Senator GEORGE. But there was no provision made that the assets, as distinguished from cash, would go over, as in the case of merger or consolidation, and a revaluation is required of those assets.

Mr. PARKER. That is true, and I understand it is a very difficult proposition.

Senator GEORGE. Well, this bill made no change in that regard?

Mr. PARKER. No; that has not been changed.

Senator GEORGE. It is a very difficult proposition. It prevents the liquidation of even a wholly owned subsidiary in many, many instances, because you have a fictitious value. The very minute that you dissolve one corporation and transfer the assets into the parent you have got a fictitious value, profit or loss, purely fictitious, on which you have the income liability.

Mr. PARKER. Of course, under a merger or reorganization where they do not come under this liquidation feature, we do take over the basis, whatever the basis for depreciation was, and so forth, that goes over, if it was a tax-free transaction.

Now, when this new provision was put in it was rather a hard thing to decide which way to do it. The way we did do it was if a parent dissolved a subsidiary it took the basis of the cost of that subsidiary's stock to the parent. So, of course, that put you in a rather involved situation in some cases. You have to take that amount of money and spread it over the assets of the subsidiary. Now, that amount of money will not coincide, of course, with the basis of this property in the hands of the subsidiary, and then it comes to the question of allocation.

Senator GEORGE. Take the ordinary case where you have got a patent right, trade name, or good will that has an immense increase in value, but it has the same assets, nothing more nor less; then you have got \$10,000,000 actual inventory, physical property value, that would result in a possible valuation over your valuation of say \$1,000,000, you have got a fictitious profit of \$9,000,000 right there. That prevents the liquidation if there is a change in national policy, and I think that is true with respect to the dissolution of the wholly owned or 80-percent-owned subsidiaries, and if there is a change in

the national policy with respect to the dissolution of personal holding companies it seems to me we ought to do the essential thing of allowing the assets, other than profits, other than earnings, and other than cash, the assets that were put over in the holding company in the first instance, to go back into the hands of the individual, and the assets that were put into the subsidiary in the first instance to go back into the hands of the parent company. In the long run, there could be no actual loss of revenue to the Government, it seems to me, and it would simplify all the corporate structures considerably.

Mr. PARKER. I understand that this section has not been very widely used, that we put in last year.

Senator GEORGE. It cannot be used, Mr. Parker. It cannot be used practically in a vast number of corporations that would really like to simplify their corporate structures. It just cannot be done, that is all, without a ruinous tax, because you have got immediately a high, injurious profit or loss, as the case might be. I do not see why we cannot simplify those things. The long-run effect might be advantageous to the Government, assuming we have had a change in our national policy with respect to subsidiary holding companies generally and personal holding companies as well. It looks like we ought to make it easy and practical for them to actually get out of the picture.

Take the case of personal holding companies. You have got personal holding companies created solely by controlling management, and if you want them to get out of the picture let them pass the property, these assets, back to the bank or the individual in the same proportion as they went into this holding company. I do not see how the Government, in the long run, can lose money on it.

Mr. PARKER. Well, they lose in some cases. Now, if you have a company that has paid a certain sum for the subsidiary's stock, say that is \$1,000,000 that they paid for the subsidiary stock, all the assets of the subsidiary, we will say, are worth \$500,000, that is the basis in the hands of the subsidiary; now, if they liquidate, the bases of those assets in the hands of the parent would be \$1,000,000. In other words, in that case we have a write-up. The assets should be only \$500,000 and now they are written up to \$1,000,000. In that case the taxpayer gets the advantage. He may have a much larger depreciation base now and get depreciation all over again.

On the other hand, if the reverse situation is true, where the parent has paid \$1,000,000 for the stock in the subsidiary but the basis of the property in the hands of the subsidiary is \$2,000,000, that forces a write-down from \$2,000,000 to \$1,000,000, we will say, as the depreciable assets and the taxpayer loses.

So you have both situations. It is true, though, that the other rule, the one that we did not put in the law, would be more workable because when you distribute a certain sum of money it is hard to tell how to allocate it. A certain portion might be allocated to plant and property, a certain amount to good will—and those different items come in there.

Senator GEORGE. In the case of a subsidiary that is wholly owned by the parent company, if it wants to get out of the picture, in view of our changed policy we ought to let it go out by putting its assets, not its earnings of course, other than its cash, actual earnings, back into the parent—and I can see no reason on earth that we have got to change

the national policy with reference to holding companies, especially personal holding companies, where you have got the personal holding company and it wishes to go out of the picture, that you cannot let it take its assets, where you can put them in the hands of the taxpayer, because that is what we seem to be driving at all the while—you have got a fictitious company, you have got a fictitious profit and loss, or capital gains and loss, wherever you revalue the assets in many corporations, but I am only speaking with reference to wholly owned subs, where the parent is the exclusive owner of all stock in the sub, it looks like the assets ought to go back, as in the case of these mergers or consolidations. It is a far more practical rule in the long run to work up.

Mr. PARKER. Did you want something worked out on that subject?

Senator GEORGE. I wish you would, Mr. Parker, because I just cannot see why we do not, in view of our changed policy, I do not see why we do not let them get out, make them get out in every way they can.

Senator COUZENS. I suppose what they had saved in the past as the result of the holding company scheme might be taken into consideration.

Senator GEORGE. Yes, I think so, Senator, in earnings.

Senator COUZENS. What it had saved between now and distribution ought to be considered too.

Senator GEORGE. Yes, sir.

The CHAIRMAN. I might say to the committee that I have received a letter from the Institute of American Meat Packers which was published in the papers yesterday, I received that this morning. It is a very voluminous letter. If any of the members of the committee want to have it read we will have it read. Perhaps most of you read it in the papers.

(The letter referred to is as follows:)

INSTITUTE OF AMERICAN MEAT PACKERS,
Chicago, Ill., May 16, 1936.

Hon. PAT HARRISON,
*Chairman, Committee on Finance,
Senate Office Building, Washington, D. C.*

SIR: We respectfully request that, in the interest of accuracy and fairness, the following information concerning the statement made in Secretary Wallace's letter of May 7 be read to the committee:

Notwithstanding the persistent efforts to make it appear that the proposed tax on unjust enrichment, so-called, is sound and that additional processing taxes on various foods, clothing, and other necessities of life would be desirable, the facts remain that—

(1) The processing tax on hogs and the use to which it was put in reducing hog production forced a number of pork packers into bankruptcy and brought hundreds of others to the brink of financial ruin.

(2) These others were saved from bankruptcy by the discontinuance of the tax.

(3) It is the general opinion in the industry that any successful attempt to circumvent the decision of the Supreme Court and wrest away from packers the impounded sums returned to them as a result of the Court's decision, would immediately force many small firms into bankruptcy and concentrate the packing business into fewer hands.

The foregoing facts are incontrovertible. They cannot be ignored—unless those promoting the so-called "tax on unjust enrichment" do not care how many small pork-packing companies they put out of business in accomplishing their aim.

The Secretary in his letter to you said: "Small packers were bound to have difficulty following the sharp reduction in hog supplies caused by drought. They

are always hard pressed by larger competitors in periods of falling hog supplies and rising hog prices."

Thus, the Secretary's letter made it appear that the processing tax program which it is asserted enriched pork manufacturers had no part in also impoverishing them.

The committee should be informed that the falling hog supplies were caused not only by the drought but also by the processing-tax-financed program of reducing hog production. In saying this, we are not raising the question of the merits of the program but the fact of its effect on the pork packing industry.

The Agricultural Adjustment Administration is on record in one of its publications ("Corn-Hog Adjustment", p. 54) as follows concerning factors affecting the 1935 market supply:

"The total reduction in hog production on all farms from 1934 litters, according to the December 1 report, now is expected to be about 35 percent or about 25 million head below the average production of recent years. The aggregate adjustment required of producers under the 1934 contract was approximately 13,000,000 head. A little over one-half of the total expected reduction, therefore, is represented by the contract requirements. * * *

It was not the drought which urged swine growers to sign contracts for reducing hog supplies and paid them for doing so. The processing tax collected from these pork packers was used to pay producers to raise 25 percent fewer hogs. Under such a program, as the Secretary has well said, small packers were forced to finance the destruction of their own businesses. The suggestion now is that no account should be taken of any losses accruing to these packers from the tax program but that any profit from it should be penalized—even if such a step destroys their businesses.

The Secretary also said:

"Farmers have an interest which is as great as that of any other group in provisions for adequate Federal revenues. This interest prompts a suggestion of excise taxes on certain agricultural commodities as a means of providing such revenues."

From this statement the committee should not get the impression that the live-stock producers of this country favor processing taxes on livestock. The committee should know that the leading organizations of the producers of livestock are strongly opposed to processing taxes on their products. The opposition of the producers of dairy cattle was so vigorous that dairy products were taken out of the list of commodities on which it was suggested that processing taxes be placed.

At the last convention of the American National Live Stock Association, held in January, the resolution governing the policy of that organization was the one adopted the year before as follows:

"Whereas it has come to the attention of this association from members of the Agricultural Adjustment Administration that there is no thought in Washington of levying a processing tax on cattle; therefore be it

"Resolved, That we do hereby express our appreciation to the Agricultural Adjustment Administration for this reassuring information to the cattle industry."

Subsequent to the last convention of the American National, the legislative committee and the secretary of the organization went to Washington and opposed any excise tax on cattle.

The National Wool Grower's Association, at its convention in January of this year, passed a resolution as follows:

"We are opposed to the laying of excise taxes on domestic livestock or the products thereof."

The National Live Stock Producers Association also is strongly on record in opposition to the proposed processing taxes on livestock.

In connection with the impression given by the Secretary's letter and chart that hog processors' margins were widened to include the tax, it should be noted that the Agricultural Adjustment Administration, after the tax had been in effect a long time, stated publicly that the hog processors' net margin had declined. Only a little decline when applied to a huge volume of operations may turn a profit into a loss.

In the chart, among other things, no consideration was given to the increased cost brought about by the packing industry's adherence to the wage scales set up under the President's Reemployment Agreement at the instance of the N. R. A. Moreover, the Secretary also fails to take into account the tremendous rise in unit costs, brought about by the reduction in volume of livestock; a reduction due to the A. A. A. crop reduction program and the drought. These two factors alone

under any circumstances would substantially increase the spread between what the packer paid for his livestock and what he received for the products thereof. In addition, since the incidence of the processing tax program there have been increases in the cost of transportation and in a wide variety of other incidentals of the cost of manufacture, all of which figure in the spread, but which Secretary Wallace ignores.

On the question of relative damage to larger and smaller pork-packing companies the number of firms engaged commercially in the pork-packing industry was obscured, apparently, by quoting the number of companies and individuals who paid processing taxes on hogs. By spreading a tax liability of \$40,000,000 over the slaughtering operations of 16,500 hog processors, so-called, the Secretary obtained an average of \$2,400 per taxpayer, implying that, except for 46 large packers, the remaining hog processors are only slightly affected. This is distinctly not the case. The committee should not get the impression that there are that many packers. A hog processor, as the Secretary uses the term, is presumably anyone who slaughters a hog.

If the Secretary will provide the committee with a complete break-down of his so-called liability figure, proceeding with the grouping of 46 packers at a time until 90 to 95 percent of the figure is covered, the following facts will be apparent:

1. That to make the volume and hence the tax liability of 46 packers look large, the Secretary has introduced more than 15,000 farmers, retailers, or other slaughterers of a relatively small number of animals, whereas the commercial pork-packing industry probably consists of less than a thousand companies.

2. That the hundred packers next in size after the 46 whom the Secretary mentions would find that their funds which the new bill would place in jeopardy would be far in excess of the \$2,400 average which the Secretary sets up by including thousands of the farming or retailing groups of the population in the packing industry.

Moreover, as the Secretary well points out, the fact of size does not justify the application of a different principle. The fact is that a very small packer may have had returned to him a very small sum, but that sum might represent a very large part of his working capital and might be much more vital to his continued existence than a larger sum would be to a relatively larger company.

The discontinuance of the processing tax averted wholesale bankruptcy of pork packers, whose capital had been impaired by the program, whose irritated customers had been driven to fish and other foods, whose foreign markets had been further reduced and whose businesses in scores of cases had been brought to the verge of bankruptcy by the hog-reduction program. It is the emphatic conviction of these packers that if their money, which was demanded from them as unpaid taxes but which the Court said should not be collected, is now torn away from them under another guise, their businesses, barely saved, again will be doomed.

Very truly yours,

INSTITUTE OF AMERICAN MEAT PACKERS,
WM. WHITFIELD WOODS, *President*.

Senator LA FOLLETTE. I do not see any reason, Mr. Chairman, for going over it again, especially that portion that deals with the imposition of the processing taxes. Anything that is pertinent to what we are doing is perfectly all right.

Senator COUZENS. I do want to say here there ought to be some effort to protect those pork packers. I do not know about the others. They make a reference to that. It is perfectly obvious if we intend to collect this so-called unjust enrichment tax that we cannot collect it, it would be putting them all into bankruptcy to collect a tax that you cannot collect in any event.

The CHAIRMAN. We have placed this letter in the record, and the clerk of the committee will be authorized to report to Mr. Woods, the president of this organization, that it was brought to the attention of the committee. I would like for those who are in charge of this particular section to read over this matter further and see if there are any new points raised.

Senator BAILEY. Mr. Chairman, did not you refer that to the sub-committee?

The CHAIRMAN. Yes; we referred that subject to the subcommittee. We will refer this letter to them, and also the experts handling this particular matter.

Senator BLACK. Mr. Chairman, in that connection it may be recalled that when the evidence came out about the large number of bankruptcies and failures I sought to obtain information on the facts in that connection, but without success. I then made a request on the Treasury Department that it give us the actual figures from the records, and I have those figures here, which I think should be placed in the record immediately following that. I think it would be very interesting to the committee, if they desire to see it.

The CHAIRMAN. That may be put into the record.

Senator BLACK. Yes; I would like to have this letter from Mr. Helvering in the record, with the table showing the failures in various classifications, with tax liability from \$1,000 on up.

Senator GEORGE. During what period?

Senator BLACK. 1935; the time when they said it was ruinous to all the packers.

The CHAIRMAN. Let it go in the record without objection.

(The letter referred to is as follows:)

TREASURY DEPARTMENT,
Washington, May 9, 1936.

Hon. HUGO L. BLACK,
United States Senate.

MY DEAR SENATOR: In accordance with your suggestion I have made an effort to secure the information relative to bankruptcies, discontinuances, and profits of the packing industry over a period of years.

I have been unable to find any readily available data as to the profits of the smaller meat packers or as to the number of such packers who may have discontinued business during the period the processing taxes were collected.

We have, however, in the Bureau, data relative to the amount of hog-processing-tax liability incurred by processors during the year 1935, segregated to show the number of processors in various classes predicated upon the amount of tax liability declared. We also have a record of all bankruptcy, receivership, and reorganization proceedings in which Federal tax liabilities are involved in any way which have been instituted and/or reported to the Bureau since September 1934.

For your information we have reviewed these records to determine how many hog processors were involved in such proceedings. Our records disclosed that out of 1,306 processors who reported hog-processing-tax liability for the fiscal year 1935 and whose returns accounted for all processors whose tax 1935 and whose returns accounted for 99.12 percent of the total tax liability disclosed, accounting for all processors whose tax liability was in excess of \$1,000, there have been but 28 bankruptcies, receiverships, or reorganizations reported to the Bureau.

A detailed statement classifying the above-mentioned hog-processing taxpayers in accordance with the amount of tax returned and showing the number of bankruptcies, receiverships, and reorganizations reported in each class is submitted herewith for your information and consideration.

Yours very truly,

GUY T. HELVERING, *Commissioner.*

Processing tax on hogs, fiscal year 1935

Tax liability	Number of processors	Total liability	Percent	Bankruptcy or receivership reorganization
Over \$20,000,000.....	2	\$51,527,374.05	29.68	0
\$10,000,000 to \$20,000,000.....	0	0	0	0
\$7,500,000 to \$10,000,000.....	2	17,890,209.92	10.31	0
\$5,000,000 to \$7,500,000.....	1	7,475,027.55	4.31	0
\$4,000,000 to \$5,000,000.....	1	4,356,398.20	2.61	0
\$3,000,000 to \$4,000,000.....	3	11,546,246.89	6.65	0
\$2,000,000 to \$3,000,000.....	5	12,422,211.67	7.16	0
\$1,000,000 to \$2,000,000.....	14	18,007,850.82	10.37	0
\$750,000 to \$1,000,000.....	5	4,270,465.95	2.46	0
\$500,000 to \$750,000.....	13	7,770,409.49	4.48	2
\$400,000 to \$500,000.....	10	4,421,850.67	2.65	0
\$300,000 to \$400,000.....	17	5,940,056.02	3.42	2
\$200,000 to \$300,000.....	20	5,047,318.26	2.91	3
\$100,000 to \$200,000.....	47	6,719,077.92	3.87	0
\$75,000 to \$100,000.....	30	2,610,022.70	1.50	1
\$50,000 to \$75,000.....	51	3,151,851.13	1.82	3
\$25,000 to \$50,000.....	111	3,897,160.86	2.24	5
\$16,000 to \$25,000.....	35	1,048,092.22	.95	0
\$10,000 to \$15,000.....	71	845,589.20	.49	2
\$5,000 to \$10,000.....	151	1,084,049.64	.62	4
\$4,000 to \$5,000.....	55	219,052.86	.14	1
\$3,000 to \$4,000.....	80	275,757.36	.16	1
\$2,000 to \$3,000.....	141	345,972.30	.20	1
\$1,000 to \$2,000.....	391	562,073.30	.32	3
Total.....	1,306	172,065,018.97	99.12	28

Senator BLACK. That might be a good idea, Mr. Chairman. I was greatly impressed by the facts. When they mentioned the bankruptcies I wanted to find out about the facts.

The CHAIRMAN. I am in receipt of a letter from Mr. Morill, the secretary of the Board of Governors of the Federal Reserve System, which I will put in the record.

(The letter referred to is as follows:)

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM,
Washington, May 16, 1936.

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

DEAR SENATOR HARRISON: In view of the fact that the Board of Governors of the Federal Reserve System is charged under the law with the responsibility for the supervision of holding-company affiliates of member banks and the granting of permits entitling them to vote the stock of such banks controlled by them, it desires to suggest for the consideration of your committee that the proposed Revenue Act of 1936 (H. R. 12395) exempt holding-company affiliates of member banks from tax on that part of their earnings which they retain in order to comply with the requirements of section 5144 of the Revised Statutes. Under the provisions of such section, holding-company affiliates are required to possess or accumulate certain amounts of readily marketable assets other than bank stock. There is enclosed a copy of a memorandum which discusses the matter in detail and contains a suggested form of amendment to the bill.

Very truly yours,

CHESTER MORRILL, Secretary.

SUGGESTED AMENDMENT TO REVENUE ACT OF 1936 (H. R. 12395) TO EXEMPT BANK HOLDING-COMPANY AFFILIATES FROM TAX ON THAT PART OF EARNINGS WHICH UNDER THE LAW THEY WOULD NOT BE PERMITTED TO DISTRIBUTE TO STOCKHOLDERS

Under the provisions of section 5144 of the Revised Statutes of the United States and section 9 of the Federal Reserve Act, the stock of a member bank controlled by a holding company affiliate cannot be voted unless the holding company affiliate has obtained a voting permit from the Board of Governors of the Federal Reserve System. It is also provided that no voting permit shall be granted except upon certain conditions, including requirements concerning readily marketable assets other than bank stock which must be possessed by the holding company affiliate on June 16, 1938, and/or acquired thereafter.

In the case of bank stock not subject to double liability held by a holding company affiliate, the amount of other readily marketable assets held by the holding company affiliate must ultimately be not less than 12 percent of the aggregate par value of such bank stock and, in the case of bank stock subject to double liability, the amount of other readily marketable assets held by the holding company must ultimately be not less than 25 percent of the aggregate par value of such bank stock.

The law also contains provisions limiting the dividends which may be paid by a holding-company affiliate after June 16, 1938, to 6 percent of the book value of its own stock unless it possesses the specified amounts of readily marketable assets other than bank stock.

Since Congress has determined that it is in the public interest to require holding-company affiliates to possess readily marketable assets other than bank stock and to restrict their right to pay dividends until such assets are accumulated, it does not appear to be in the public interest to tax earnings of holding-company affiliates which are retained by them in order to accumulate such assets. Also, under the proposed revenue act, banks will be subject to a tax on their earnings whether or not distributed. Therefore, earnings of holding-company affiliates derived from dividends on bank are earnings upon which a tax already will have been paid by the banks involved.

In view of these facts it would seem that holding-company affiliates should be exempted from tax on that portion of their earnings which the law requires them to retain. In short, holding-company affiliates should not be penalized for complying with the law.

Such exemption might be made by adding the following new section to the Revenue Act of 1936 (H. R. 12395):

"Sec. — *Credits of holding-company affiliates against net income.*—for the purpose of the tax upon the income of any holding-company affiliate, as defined by section 2 of the Banking Act of 1933, there shall be allowed as a credit against net income that portion of the net income of such holding-company affiliate which it retains in order to comply with section 5144 of the Revised Statutes."

The CHAIRMAN. What is the pleasure of the committee with reference to this letter? Suppose we turn it over to Mr. Parker, then we can get a further explanation, after they have studied the suggested amendments, and so on?

Mr. PARKER. All right.

The CHAIRMAN. Mr. Russell, you were to present some other matter here this morning.

Mr. RUSSELL. Senator, I have 10 or 15 of these consolidated groups that I have included in the list of 278 corporations. The employees of the Bureau worked on it yesterday, but I would rather have a little more time to go over the figures myself before I turn them over to the committee.

The CHAIRMAN. Is there any objection to giving them further time on that, Senator Byrd?

Senator BYRD. Beg pardon?

The CHAIRMAN. You and Senator Black were asking for this information and he requests to have a little more time to get this matter up.

Senator BLACK. I think they ought to get all the time they want.

The CHAIRMAN. You will have it by tomorrow, do you think?

Mr. RUSSELL. Yes, sir. I have the figures, Senator, but I want to check them over.

The CHAIRMAN. All right.

Senator BLACK. Mr. Chairman, if you will pardon me just one moment, I also asked the gentleman who testified for the packers, I have forgotten his name, the president, at the time when he reached the point about the number of bankruptcies, if he could give us definite information. I have received information also with reference to the same subject, and the suggestion was made that he hoped that the names of the companies would not be placed in the record, which I think is a very proper request, but it shows that the list of firms in bankruptcy was 11, the list of firms out of business was 4. For the 11 in bankruptcies he has, in parenthesis, "release of funds has restored most of these firms from insolvency." The firms against which liens were imposed were 12.

Senator GERRY. How many receivers were appointed, State receivers?

Senator BLACK. He does not state, Senator.

This was not complete and that is the reason I asked the Treasury Department to get me such information as they could. I would be glad to let you see this. This was what he gave us. The first was headed "List of firms in bankruptcies", and in parenthesis, "release of funds has restored most of these firms from insolvency." There are 11 of those. The next heading is "Firms out of business."

Senator CAPPER. Those 11 are not now in bankruptcy?

Senator BLACK. No, no; the next heading, "Firms out of business", he gives the names of four. In the next heading he says, "Firms against which liens were placed on account of processing taxes." There are 12 of those.

Senator GERRY. That is, his contention is that because they did not advocate the processing tax they were able to save those firms from going into bankruptcy?

Senator BLACK. You mean the 11?

Senator GERRY. Not the 11, I mean all of them. You said there were some that had liens.

Senator BLACK. Twelve that had liens.

Senator GERRY. They were able to pay those out if they did not have to pay this tax?

Senator BLACK. He does not state what happened, whether they paid them or did not pay them. I assume what he means is that there were liens placed against 12 only. I was very much surprised to see such a small list, and I would guess he would be wrong in that, because I imagine there would be more liens, but that is what he had set up. I think those figures ought to be placed in the record. I do not ask that the names be placed in.

The CHAIRMAN. You do not desire that these names go in the record?

Senator BLACK. No; he suggested that the names should not be made public. I think that is a very reasonable request, but I brought them along so that any member of the committee who wants to see them may see them.

The CHAIRMAN. On the question of the estimates on some of these proposals, Mr. Seltzer, you were to furnish us this morning an estimate on the last proposal that was made.

Mr. SELTZER. I have here the estimate on the Chairman's latest proposal.

Under the first proposition you "retain present capital stock and excess-profits taxes."

Under the second proposition you "repeal exemption of dividends from individual normal tax."

Under the third proposition you "impose 7 percent tax on undistributed adjusted net income of corporations."

Senator COUZENS. May I ask, can you not quote those estimates separately? I see where there are five different items here. Can you give them separately?

Mr. SELTZER. I can give them separately, but the separate allocations are rather rough.

The increase in the corporation statutory net income tax from the present graduated rate, 12.5 to 15 percent, to a flat 18 percent rate, would increase the revenues by \$244,000,000.

Senator BYRD. I beg your pardon, sir. Is that the first item or the second item?

The CHAIRMAN. That is the third item.

Mr. SELTZER. That is the first tax imposed here.

Senator LA FOLLETTE. No. 3 on this sheet.

Mr. SELTZER. Yes. The retention of the present capital stock and excess-profits taxes is responsible for \$168,000,000.

Senator GERRY. \$168,000,000?

Mr. SELTZER. That is right.

Senator GEORGE. Will there be no increase there?

Mr. SELTZER. That is the same as before. It is \$244,000,000 for the 18 percent corporation income tax.

Senator WALSH. How much is that an increase over the present rates?

The CHAIRMAN. You mean the capital stock tax?

Senator WALSH. No; no. 3, the 18 percent tax.

Mr. SELTZER. Under the present tax we estimate \$964,000,000 for the calendar year 1936, and with an 18 percent rate we estimate \$1,208,000,000, or an increase of \$244,000,000.

Senator COUZENS. You did not give us no. 2, "repeal exemption of dividends from individual normal tax."

Mr. SELTZER. That is bound up with no. 5, where you increase the rate. I can give you those separately in a moment.

The CHAIRMAN. I did not get the figures on no. 3.

Mr. SELTZER. \$244,000,000 increase.

Mr. PARKER. May I ask at this point if that contemplates the \$1,000 exemption, or any exemption on the graduated tax?

Mr. SELTZER. This is just as the memorandum has it.

Senator BYRD. What difference would that make? As I understood him there is proposed the incorporation of the idea of \$1,000 exemption for all corporations.

The CHAIRMAN. I do not know whether that was stated or not, but we talked considerably about corporations that had \$20,000 profit or less, that they be given \$1,000 exemption. Will you approximate for us about what difference that would make?

Mr. SELTZER. In our other schedules it run around \$30,000,000, but I would have to check to find out whether that would apply here.

The CHAIRMAN. I am very much surprised that we would only get \$244,000,000, I had an idea that we would get more money than that.

Senator BYRD. Mr. Parker estimated \$300,000,000, as I recall it.

Senator BARKLEY. How much do you estimate?

Mr. SELTZER. \$244,000,000.

Senator WALSH. The increase is almost 25 percent.

The CHAIRMAN. Yes, but I thought that we would get more money than what he shows in his estimates.

Senator GERRY. What section is that under, Mr. Chairman?

The CHAIRMAN. That is the third. Go to no. 4, Mr. Seltzer, "impose 7 percent tax on undistributed adjusted net income of corporations."

Mr. SELTZER. The adjusted net income is defined as the statutory net income less ordinary corporation income, and excess-profits taxes paid, plus 90 percent of dividends received, and the undistributed adjusted net income as adjusted net income less dividends paid.

The CHAIRMAN. What do you estimate on that?

Mr. SELTZER. We said that we could count on corporations under this proposal retaining approximately 50 percent of their adjusted net income. On that basis you would have an increase of \$225,000,000 from this 7-percent tax.

Senator GERRY. What is the total amount then?

The CHAIRMAN. He has not finished yet.

Mr. SELTZER. I have not yet finished.

The CHAIRMAN. Take an increase from 4 to 5 percent in the normal tax, what does that get you?

Mr. SELTZER. When you increase the normal tax, exclusive of applying it to dividends—to answer Senator Couzens—you get \$60,000,000, when you increase the normal rate from 4 to 5 percent. Then when you subject dividends to the normal rate of 5 percent you add another \$113,000,000, making an aggregate increase in revenues, under the fifth and preceding proposals, of \$642,000,000.

The CHAIRMAN. Now, let me get that.

Senator BARKLEY. What do you get under "five"?

Senator COUZENS. \$60,000,000 and \$113,000,000

Mr. SELTZER. You get \$60,000,000 plus \$113,000,000.

Senator BARKLEY. That is \$173,000,000?

Mr. SELTZER. Yes.

The CHAIRMAN. If you do not apply the 4 percent normal tax to the distribution of dividends you get only \$60,000,000?

Mr. SELTZER. That is right.

The CHAIRMAN. If you do apply it you get in addition \$113,000,000?

Mr. SELTZER. That is 5 percent normal.

The CHAIRMAN. 5 percent normal?

Mr. SELTZER. That is right.

Senator LA FOLLETTE. Is that on a full year basis?

Mr. SELTZER. That is on the calendar year basis.

Then, in Roman III:

If in addition to the foregoing, a tax of 35 percent were levied on that portion of undistributed adjusted net income in excess of 50 percent of the adjusted net income, the above estimated increase in revenue would be further increased by \$107,000,000.

The CHAIRMAN. How did you get that estimate?

Mr. SELTZER. You get an aggregate increase of \$749,000,000.

The CHAIRMAN. How do you figure that? Do you figure that concerns would retain 50 percent and more?

Senator LA FOLLETTE. I understand that you assume, under the proposal as submitted to you, that corporations could retain 50 percent without being induced to distribute, and for that reason you made that assumption in your estimates, is that correct?

Mr. SELTZER. We assume that under the present tax laws corporations reporting net income would pay out net cash dividends of about \$2,430,000,000. Now then, if you have a tax on retained earnings you get some increase in dividend distribution, depending, of course, upon the strength of the tax. In this case I believe that the distribution would be increased to about 50 percent. We estimated that in the aggregate corporations would not retain in excess of 50 percent at a cost of 35 percent, that is at a tax cost of 35 percent, hence it was reasonable to assume you would get roughly 50 percent distribution in the aggregate.

Senator BYRD. I did not get no. 2. How much would you get from that?

Senator LAFOLLETTE. \$113,000,000, if you raise it to 5 percent.

Senator BYRD. I see. When you added up the total you did not include, did you, the capital stock and excess profits tax?

Mr. SELTZER. No, no.

Senator GERRY. What was the increase under 4? I did not get that.

Mr. SELTZER. \$225,000,000.

Senator BLACK. What did you get under no. 3?

Mr. SELTZER. \$244,000,000.

The CHAIRMAN. Then, as a matter of fact, under the House bill you would get considerably more than you would under this bill, because you are repealing the capital stock tax after this year, which brings in \$168,000,000. That is out of the way. Then you get \$623,000,000 through the other process, and this way you get \$642,000,000, minus the \$168,000,000 of capital stock tax.

Mr. PARKER. These figures add up to \$810,000,000, Senator.

The CHAIRMAN. Where do you get that?

Mr. PARKER. That is if you add \$168,000,000 in here, you find that the total of these five figures that he has just given you is \$810,000,000. But that is not an increase, so we take off the capital stock tax and get \$642,000,000.

Senator BYRD. This plan brings in \$20,000,000 more than the House bill, approximately?

Mr. PARKER. Yes, Senator.

Senator CLARK. How much did you say no. 5 brings in, the increase in normal tax on individual income from 4 percent to 5 percent?

Mr. SELTZER. You get \$60,000,000, and when you apply it to dividends you get another \$113,000,000, or you get a net increase of \$173,000,000 by reason of increasing the normal rate from 4 percent to 5 percent.

Senator BLACK. What would you get from dividends if you simply applied the 4 percent normal instead of increasing it to 5 percent?

Mr. SELTZER. If you applied the normal rate of 4 percent on dividends you would reduce your yield by \$83,000,000.

Senator GEORGE. What would you get if you imposed on the undistributed adjusted net income 5 percent instead of 7 percent?

Mr. SELTZER. I might say that depends on whether you impose the surtax under III here, where you have a 35 percent tax on retained earnings in excess of 50 percent. If you do not have no. 3 we have to count on a smaller distribution of dividends. Would you like to have it both ways or one way?

Senator GEORGE. I would like to have it the other way.

Mr. SELTZER. Under no. 3?

Senator GEORGE. Yes, sir.

Mr. SELTZER. It would be a reduction from \$225,000,000 to \$161,000,000, if you reduce the 7-percent rate on undistributed net income to 5 percent.

The CHAIRMAN. You would get from \$225,000,000 down to what?

Mr. SELTZER. Down to \$161,000,000.

Senator GEORGE. How did you figure that? Would you mind telling me?

Mr. SELTZER. Beg pardon?

Senator GEORGE. Would you mind just saying briefly how you figure it?

Mr. SELTZER. Yes. We estimate that the undistributed earnings under the budget picture would be \$3,452,000,000. You apply a 5-percent rate to that and that gives you your gross-tax liability. Then you reduce that gross-tax liability by 6.8 percent to account for the regular difference between corporation-tax liability and collections, that is over a period of years we find that there is about that average difference between tax liability and collections, and that is how we arrive at the figure.

Senator GEORGE. I did not get that statement.

Mr. SELTZER. You did not get what statement?

Senator GEORGE. The 6.8 percent.

Mr. SELTZER. Over a period of years we find that the reported liability differs from tax collections by an average of around 6.8 percent, that is, collections are about 6.8 percent smaller than tax liability. So in making our estimates we always allow for that on corporation income. We get no such deduction for individual incomes because our experience does not show that it is necessary. But if you take corporation-tax liability and relate it to collections you find regularly that you get that difference.

The CHAIRMAN. You accounted for that in these estimates?

Mr. SELTZER. Yes, sir.

The CHAIRMAN. Did you apply the same rule with reference to your estimates in the House bill?

Mr. SELTZER. Yes. The statutory net income of corporations for the calendar year 1936 we estimated would increase by about 31 percent over the calendar year 1935. We estimated that the calendar year 1935 would show an increase of 41 percent over the calendar year of 1934—no, I beg your pardon. For the calendar year 1934 we had estimated that the statutory net income would show an increase of 41 percent over the calendar year 1933. Now, we used the same methods because we found that we were very nearly perfect in the 1934-1933 percent; we now have the returns in at the Bureau. Using the same methods of estimating we found that you could predict in 1936 an increase of about 31 percent over 1935. Now, about 1

percent of that would be due to a change in the law. That is, in 1935 we got 10 percent of intercorporate dividends included in statutory net, whereas previously such dividends had been excluded from statutory net. So that if you ignore that factor, that is, if you take that out, we anticipate about 30 percent increase in corporation statutory net income in 1936 over 1935.

Senator GERRY. How did you come out on your liquor estimates? Were you anywhere near in 1934?

Mr. SELTZER. Which year?

Senator GERRY. 1934.

Mr. SELTZER. Not the calendar year 1934. We had estimated a statutory net income at \$4,234,000,000.

The CHAIRMAN. You are talking about liquor now?

Senator CONNALLY. He is talking about liquor.

Senator GERRY. I know they gave me some figures on liquor in 1934 that I told them at the time were haywire, and they were. You were all off on your liquor estimates.

Mr. SELTZER. Because we haven't had any continuing experience on liquor.

Senator GERRY. But you could have had common sense on it. Some of the estimates you gave me were terrible.

The CHAIRMAN. Now, Mr. Seltzer, I asked the other day for an estimate on a proposition where you levy a flat rate of 15 percent, and where, on all corporations \$15,000 of net earnings is excluded, if they retained it, and I asked you for estimates between there and up to 50 percent, 40 percent, and 60 percent. What was your estimate on that?

Mr. SELTZER. We are still working on that estimate. We know at the minimum it is likely to reach a yield around \$600,000,000, but we will have to put that through the tax mill in order to get an accurate estimate. I might say that none of the estimates that we have offered so far, other than the one we offered this morning, has actually been put through our tax mill. We need usually about 48 hours for that. We have been attempting to give you overnight service on these other estimates in order that you might have a general idea of the magnitudes involved.

Senator WALSH. Mr. Chairman, may these estimates be submitted in writing?

The CHAIRMAN. Yes. I am very anxious to get this matter out of the way. We would like to have some plan sooner or later. We would like to have these estimates on the first proposition that we requested of you, namely, the 15-percent tax on statutory net income as now defined. Then between 30 percent and not in excess of 40 percent retained you put 30 percent on that amount, and between 40 and 50 you put 35 percent on that amount, and over 50 percent you put 45 percent on that amount, and on that you estimated \$552,000,000.

Mr. SELTZER. That, as I say, has not yet gone through our regular tax mill. If we had 24 hours we could put it through and get you a reliable estimate.

The CHAIRMAN. Well, the thing that is confusing me is that in these estimates where you leave it at 15 percent and put it at 18 percent there is not such a marked difference.

Mr. SELTZER. Under the House bill your first rate is something like 28½ percent applied to the first 14 percent of income retained.

The CHAIRMAN. Well, that will not take so long, will it?

Mr. SELTZER. If we had 2 days so we could line up the basic data then we could run off estimates for you in a hurry, but we have been kept so busy supplying overnight rough estimates that we have not had time to wind up our basic data, except the last proposal which you gave me last Friday night.

The CHAIRMAN. There is a proposal that Senator King requested you to give an estimate on. That is: Increase the corporate rate to 19 percent flat, with 4 percent recoupment to be retained by corporations.

Senator LA FOLLETTE. What does that mean?

The CHAIRMAN. I do not know what that means. Do you know what that means, Mr. Seltzer?

Senator CLARK. He means to levy a flat tax, then give them a rebate if they pay any dividends out of income.

The CHAIRMAN. I see.

Senator CLARK. The corporation gets a refund proposition.

The CHAIRMAN. Second, he wants to increase the corporate rate to 23 percent flat with 5 percent recoupment to be retained by corporations.

Senator LA FOLLETTE. Do you understand what that means?

Mr. BURGESS. Is that 5 percent of the amount retained or distributed?

Mr. STAM. What the Senator means is you impose the flat rate on corporations of 19 percent, or whatever rate he has in mind, and then when the corporation pays out the dividend to the shareholder it retains 4 percent of the dividend. In other words, it does not pay out to the shareholder the whole dividends but retains 4 percent of the dividends, and keeps that 4 percent itself. So the Federal Government always gets the flat rate of 19 percent, and as an inducement to the corporation to pay out the dividends in order to get this 4 percent recoupment, you see—it is an inducement to the corporation, because every time they pay a dividend out the corporation gets 4 percent recoupment of that dividend.

The CHAIRMAN. Then the shareholder would not pay the normal tax?

Mr. STAM. In effect he would be paying it, because the corporation, when it declared out the dividend say of \$100,000, it would keep 4 percent of the dividend itself and the shareholder would only get the dividend less that 4 percent.

Senator BARKLEY. That is just the same as a straight 15 percent tax on all net income, plus 4 percent additional on that which is not distributed.

Mr. STAM. It is an encouragement to the corporation to pay out the dividend.

Senator CONNALLY. Four percent of the part paid out?

Senator BARKLEY. They get back 4 percent. They pay 19 percent and then get back 4 percent on what they do pay out, which reduces that to 15 percent. So the result is it is a 15 percent tax on what they pay out.

Mr. STAM. It has the effect of reducing the corporate net if they do not pay the dividends out. It is an encouragement to the corporation to pay it out.

Mr. BEAMAN. Will you answer the question that Senator Barkley asked? I would like to get it answered. Is not the effect the same as 15 percent normal on a corporation plus 4 percent undistributed profits tax, except the scheme injects into it the element of withholding the source. I mean, the tax affecting the corporations is the same.

Mr. STAM. No; it is not. As far as the United States Treasury is concerned, the United States Treasury always gets the flat rate of 19 percent. If you impose the flat rate of 19 percent the United States Treasury always gets that. It is never reduced. But the corporation gets the benefit when the dividend is paid to the shareholder by retaining 4 percent of that dividend as recoupment. That is retained by the corporation. That does not affect the tax paid into the United States Treasury at all.

Senator BARKLEY. Then, as a matter of fact the shareholder who gets the dividend would pay 23 percent, that is, the corporation would pay 19 percent and the shareholder would be paying 23 percent, because the 19 percent would be taken out of the net earnings before distribution. Then after he was forced to get his the company would pay all except 4 percent more, which would increase his share of the tax to 23 percent.

Mr. STAM. That is if you took the 23 percent flat rate.

Senator BARKLEY. No; if you have the 19 percent flat rate. The corporation pays that 19 percent.

Mr. STAM. That is right.

Senator BARKLEY. Then it distributes dividends, say, up to 50 percent, the shareholder, after the 19 percent is taken out, is really paying 24 percent.

Mr. STAM. In effect it does this: Where the flat rate is 19 percent, 4 percent of that is really paid by the shareholder and 15 percent is paid by the corporation. That is really the effect of it.

Senator LA FOLLETTE. What I want to know is, before you turn this over to the actuaries for an estimate, whether they understand it.

Mr. BURGESS. Let me say that this is my understanding: A corporation has \$100 net income, it pays 19 percent of that \$100 or \$19; if it distributes 50 percent, or \$50, it has a recoupment on that \$50 of 4 percent, or \$2. So its total tax is \$17.

Mr. STAM. That does not affect this payment to the United States Treasury. It is still 19 percent.

Mr. BEAMAN. What I want to understand is, does he still pay 4 percent, whether he is subject to income tax or not?

Mr. SELTZER. That is the effect of it.

Mr. BEAMAN. In other words, as far as the stockholder is concerned, this is an excise tax, not an income dividends tax.

Mr. STAM. The idea was to limit the recoupment for dividends paid to other than corporations.

Mr. SELTZER. Whether they were subject to normal tax or not.

Mr. STAM. Corporations would not be subject to surtaxes.

Mr. SELTZER. That means you would tax dividends of charitable institutions, and the like also?

Mr. STAM. No, we said "persons other than corporations."

Mr. PARKER. It is something like the English system. If a corporation is going to tell you they sent you \$100 but they deduct \$4, you would only get \$96.

The CHAIRMAN. Let us take the third proposition that Senator King is asking for: Increase the corporate rate to 19 percent flat

with 5 percent recoupment to be retained by corporation. Now, he asked for a 19 percent flat with a 4 percent recoupment. He has asked for a 23 percent and a 19 percent with a 5 percent recoupment.

I would like to get an estimate on that. I want this brought up to date with the one that you had the other day, that you said was a rough estimate:

Mr. SELTZER. That is right.

The CHAIRMAN. Where all corporations can retain \$15,000 of their earnings.

Mr. SELTZER. On the 40-60 percent rates.

The CHAIRMAN. Now, keep that provision in mind there, about the 15-percent flat rate, and pay 40 percent on the part that is retained, let them pay on that part retained up and above the \$15,000 that they can retain, say, 10 percent, and if they retain more than 50 percent or above, 30 percent.

Mr. LINDOW. You said that up to 40 percent this 10 percent would apply?

The CHAIRMAN. Up to 50 percent.

Mr. LINDOW. And over 50 percent?

The CHAIRMAN. Over 50 percent put it at 30 percent.

Mr. LINDOW. The \$15,000 comes out of the first 50 percent?

The CHAIRMAN. Yes, that is to be retained for payment by all corporations, \$15,000.

Mr. SELTZER. In addition to that they can retain 50 percent?

The CHAIRMAN. Up to 50 percent, but they pay on the difference.

Mr. SELTZER. The \$15,000 is included in the first 50 percent?

The CHAIRMAN. Yes; all above that they pay the 30-percent rate. Figure your estimates on that proposition.

Senator BARKLEY. Which would raise the more money, the suggestion of an 18-percent flat rate with 7 percent addition on undistributed income or 17 percent flat rate with 8 percent additional on the undistributed net income?

Senator CONNALLY. You do not need to ask the experts that. The 8 percent, of course, would be most.

Mr. SELTZER. That is 17 percent flat and 8 percent of the undistributed net income?

Senator BARKLEY. Yes.

Mr. SELTZER. This 35 percent above 50 percent is out?

Senator BARKLEY. Yes. I want it as simply as I can get it.

The CHAIRMAN. There ought to be some penalty up in there. I do not care whether it is 60 or 75 or lower. There ought to be a meeting of minds. If we have a meeting tomorrow and we do not have the estimate we cannot vote as well and as intelligently as if we had the estimate.

Mr. SELTZER. Would it be possible to have the estimates submitted tomorrow afternoon instead of tomorrow morning?

The CHAIRMAN. Yes. We can do that. We will meet tomorrow afternoon. We will give you more time on the estimates if you need it, but we want to travel pretty fast here.

Do any of the Senators desire any estimate on any proposition?

Senator CONNALLY. Mr. Chairman, I would like to ask for an estimate on a matter that was submitted the other day, it is the estimate on 16 percent instead of 15 percent. That is very simple. All you have to do is to change that to 16 instead of 15.

Senator BYRD. We would like to have an estimate if the \$1,000 is exempt.

The CHAIRMAN. Of course that would only include corporations that earned less than \$15,000.

Senator BARKLEY. If it will not be too much trouble I would like to get figures showing the difference in total revenue by the suggestion I made a while ago, the 17 and 8 instead of 18 and 7, based on this sheet that you gave us this morning. I would like to have that, because if there is not too much difference in the amount of the total income the smaller percentage of the total would be a little bit easier on small corporations.

The CHAIRMAN. I have been very much impressed with the thought that over 90 percent of the corporations of this country make \$15,000 or less, and much less than 10 percent make over \$15,000. I do not see why we could not write in here, without any great loss of revenue, a provision to give those corporations that make less than \$15,000 the right to retain it, but if they fail to distribute it it is all right, and if they want to distribute it it is all right.

Senator CONNALLY. You would have to put the flat tax up pretty high if they did that, because you would lose very much in the \$15,000 class, if they are 90 percent of the corporations.

The CHAIRMAN. Why cannot you gentlemen, Mr. Seltzer and the others, figure out where we can get about \$623,000,000, about the amount that this bill would carry with this corporation proposition, through some process of calculating what the rate would have to be if you exempted all corporations from \$15,000 or less?

Mr. SELTZER. We could do that.

Senator LAFOLLETTE. You do not mean to exempt them from the normal tax?

The CHAIRMAN. I mean to exempt them from that amount, to permit them to retain that amount, and then put on a penalty after they get to 40 percent, or something like that.

Mr. SELTZER. We could do that.

Senator CONNALLY. You would have to tell them what the flat rate is.

The CHAIRMAN. I just give that in order to see if they can work it out. Figure it at 16 percent, 18 percent, 19 percent, or 20 percent. The total amount of revenue is the main proposition.

Senator BLACK. You mean graduated down?

The CHAIRMAN. Yes, graduated down, and make it moderate, say 40 percent, but when you get a corporation retaining more than 50 percent put the penalty on them pretty stiff. For instance, take General Motors. What was General Motors' earnings this year? \$100,000,000, was it not?

Mr. RUSSELL. I believe it was more than \$100,000,000.

Senator GERRY. How many stockholders do they have?

Mr. RUSSELL. I could not say, Senator.

Senator GERRY. We have not had any of those figures.

The CHAIRMAN. Senator Gerry, why ask that question? If a corporation makes \$50,000,000, or \$20,000,000, or \$10,000,000, it can retain, without any appreciable penalty, 30 percent of that amount. They are going to have a pretty good working capital when they retain that. A little corporation would find it difficult to go out and borrow any money.

Senator GERRY. That goes into the legal proposition too.

Senator BYRD. Mr. Chairman, if that plan is worked out you ought to also bring in your cushions, and so forth, and so on, for debts and other things.

The CHAIRMAN. I thought, Senator Byrd, a cushion would not be necessary if you make it \$15,000 and less.

Senator BYRD. There are some corporations that owe debts that have to be paid.

The CHAIRMAN. You do not have the heavy penalty proposition on the corporation that reserves 40 percent or less.

Senator BYRD. What if a corporation wants to put up a new plant? They will have this excess tax to pay.

Senator BLACK. Mr. Chairman, it has been suggested to me by Senator Couzens—

Senator COUZENS (interposing). The reason I handed it to you was that you received a letter from the Commissioner.

The CHAIRMAN. What is it, Senator Black?

Senator BLACK. I wanted to take up these names that we have here, which have not been put into the record. The statement is made that they have been restored to solvency by reason of the amount of the processing tax. I wanted to get the amounts of these processing taxes, and there was one other group, it has been explained where liens were placed against it, and I want to get the amount of the liens, the amount of the processing tax in each instance. I think it would be very helpful.

The CHAIRMAN. Mr. Russell, cannot you get this information for us? Will you just turn that over to him and tell him that is the request of the committee, that this information be given?

Senator BLACK. Yes.

(The remainder of the proceedings was not reported.)

The CHAIRMAN. We will recess until Wednesday morning at 10 o'clock.

(Whereupon, at the hour of 11:40 a. m. the committee recessed until 10 a. m., Wednesday, May 20, 1936.)

REVENUE ACT, 1936

WEDNESDAY, MAY 20, 1936

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

EXECUTIVE SESSION

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

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

Also present: L. H. Parker, Chief of Staff, Joint Committee on Internal Revenue Taxation, and members of his staff; Middleton Beaman, Legislative Counsel, House of Representatives; Arthur H. Kent, Acting Chief Counsel, Bureau of Internal Revenue; C. E. Turney, Assistant General Counsel for the Treasury Department; Lawrence H. Seltzer, Assistant Director of Research and Statistics, Treasury Department.

The CHAIRMAN. The committee will be in order.

Mr. Turney, we would like to hear from you.

Mr. TURNNEY. I have a mimeographed revision of the title. This draft shows with the underscoring the places where it differs from the House bill. The new matter is underscored. Since it is rather hard to do it on the typewriter, it does not show the House bill parts which are stricken out.

(The revised draft is as follows:)

CONFIDENTIAL

Title III showing possible amendments if it is decided to incorporate certain changes which have been suggested. Prepared for purposes of discussion.

(Italicized portions are either new matter or matter which differs from provisions of House bill.)

TITLE III—TAX ON UNJUST ENRICHMENT

SEC. 501. TAX ON NET INCOME FROM CERTAIN SOURCES.

(a) The following taxes shall be levied, collected, and paid for each taxable year (in addition to any other tax on net income); upon the net income of every person which arises from the sources specified below:

(1) A tax equal to 80 per centum of that portion of the net income from the sale of articles with respect to which a Federal excise tax was imposed

on such person but not paid which is attributable to shifting to others the burden of such Federal excise tax and which does not exceed such person's net income for the entire taxable year from the sale of articles with respect to which the Federal excise tax was imposed.

(2) A tax equal to 80 per centum of the net income from reimbursement received by such person from his vendors of amounts representing Federal excise tax burdens included in prices paid by such person to such vendors, to the extent that such net income does not exceed the amount of such Federal excise tax burden which such person in turn shifted to the persons to whom such reimbursement relates.

(3) A tax equal to 80 per centum of the net income from refunds or credits to such person from the United States of Federal excise taxes erroneously or illegally collected with respect to any articles, to the extent that such net income does not exceed the amount of the burden of such Federal excise taxes with respect to such articles which such person shifted to others.

(b) The net income specified in subsection (a) (1), (2), or (3) shall not include the net income from the sale of any article, from reimbursement with respect to any article, or from refund or Federal excise tax with respect to any article (1) if such article was not sold by the taxpayer on or before the date of the termination of the Federal excise tax; (2) if the taxpayer made a tax adjustment with respect to such article with his vendor; or (3) if the taxpayer would have been entitled to a refund from the United States of the Federal excise tax with respect to the article otherwise than as an erroneous or illegal collection (assuming, in case the tax was not paid, that it had been paid).

(c) The net income from the sales specified in subsection (a) (1) shall be computed as follows:

(1) From the gross income from such sales there shall be deducted the allocable portion of the deductions from gross income for the taxable year which are allowable under the applicable Revenue Act. The proper apportionment and allocation of such deductions with respect to gross income derived from such sales shall be determined under rules and regulations prescribed by the Commissioner, with the approval of the Secretary; or

(2) If the taxpayer so elects by filing his return on such basis, the total net income for the taxable year from the sale of articles with respect to which each Federal excise tax was imposed (computed without deduction of the amount of such Federal excise tax which was paid or of the amount of tax adjustments to purchasers) shall be divided by the total quantity of such articles sold during the taxable year and multiplied by the quantity of such articles involved in the sales specified in subsection (a) (1). Such quantities shall be expressed in terms of the unit on the basis of which the Federal excise tax was imposed.

(d) The net income from reimbursement or refunds specified in subsection (a) (2) or (3) shall be computed as follows: From the total payment or accrual (1) of reimbursement to the taxpayer from vendors for amounts representing Federal excise taxes included in prices paid by the taxpayer to such vendors or (2) of refunds or credits to the taxpayer of Federal excise taxes erroneously or illegally collected, there shall be deducted the expenses and fees reasonably incurred in obtaining such reimbursement or refunds.

(e) For the purposes of subsection (a) (1), (2), and (3), the extent to which the taxpayer shifted to others the burden of a Federal excise tax shall be presumed to be an amount computed as follows:

(1) From the selling price of the articles there shall be deducted the sum of (A) The cost of such articles plus (B) The average margin with respect thereto; or

(2) If the taxpayer so elects by filing his return on such basis, from the aggregate selling price of all articles with respect to which such Federal excise tax was imposed and which were sold by him during the taxable year there shall be deducted the aggregate cost of such articles, and the difference shall be reduced to a margin per unit in terms of the basis on which the Federal excise tax was imposed. The excess of such margin per unit over the average margin (computed for the same unit) shall be multiplied by the number of such units represented by the articles with respect to which the computation is being made; but

(3) In no case shall the extent to which the taxpayer shifted to others the burden of the Federal excise tax with respect to the articles be deemed to exceed the amount of such tax with respect to such articles minus (A)

any payments or credits to purchasers specified in subsection (f) (3) and minus (B) the amount of any increase in the tax under section 602 of the Revenue Act of 1932 for which the taxpayer under this section became liable as the result of the nonpayment or refund of the Federal excise tax.

(f) As used in this section—

(1) The term "margin" means the difference between the selling price of articles and the cost thereof, and the term "average margin" means the average difference between the selling price and the cost of similar articles sold by the taxpayer during his six taxable years preceding the initial imposition of the Federal excise tax in question, except that if during any part of such six-year period the taxpayer was not in business, or if his records for any part of such period are so inadequate as not to furnish satisfactory data, the average margin of the taxpayer for such part of such period shall, when necessary for a fair comparison, be deemed to be the average margin, as determined by the Commissioner, of representative concerns engaged in a similar business and similarly circumstanced.

(2) The term "cost" means, in the case of articles manufactured or produced by the taxpayer, the cost to the taxpayer of materials entering into the articles plus direct manufacturing costs; or, in the case of articles purchased by the taxpayer for resale, the price paid by him for such articles (reduced by the amount for which he is reimbursed by his vendor).

(3) The term "selling price" means selling price minus (A) amounts subsequently paid or credited to the purchaser on or before the thirtieth day after the date of the enactment of this Act, or thereafter in the bona fide settlement of a written agreement entered into on or before March 3, 1936, as reimbursement for the amount included in such price on account of a Federal excise tax; and minus (B) the allocable portion of any professional fees and expenses of litigation incurred in securing the refund or preventing the collection of the Federal excise tax, not to exceed 10 per centum of the amount of such tax.

(g) In determining costs, selling prices, and net income, the taxpayer shall, unless otherwise shown, be deemed to have sold articles in the order in which they were manufactured, produced, or acquired. Where the taxpayer's records do not show the quantity of a commodity taxable under the Agricultural Adjustment Act, as amended, entering into articles sold by him, such quantities shall be computed by the use of the conversion factors prescribed in regulations under such Act, as amended.

(h) If the taxpayer made any purchase or sale otherwise than through an arm's-length transaction, and at a price other than the fair market price, the Commissioner may determine the purchase or sale price to be that for which such purchases or sales were at that time made in the ordinary course of trade.

(i) Either the taxpayer or the Commissioner may rebut the presumption established by subsection (e) by proof of the actual extent to which the taxpayer shifted to others the burden of the Federal excise tax. Such proof may include, but shall not be limited to:

(1) Proof that the change or lack of change in the margin was due to changes in factors other than the tax. Such factors shall include any clearly shown change (A) in the type or grade of article or materials, or (B) in costs not considered in computing the margin. If the taxpayer asserts that the burden of the tax was borne by him while the burden of any other increased cost was shifted to others, the Commissioner shall determine, from the respective effective dates of the tax and of the other increase in cost as compared with the date of the change in margin, and from the general experience of the industry, whether the tax or the increase in other cost was shifted to others. If the Commissioner determines that the change in margin was due in part to the tax and in part to the increase in other cost, he shall apportion the change in margin between them.

(2) Proof that the taxpayer modified contracts of sale, or adopted a new contract of sale, to reflect the initiation, termination, or change in amount of the Federal excise tax, or at any such time changed the sale price of the article (including the effect of a change in size, package, discount terms, or any other merchandising practice) by substantially the amount of the tax or change therein, or at any time billed the tax as a separate item to any vendee or indicated by any writing that the sale price included the amount of the tax, or contracted to refund any part of the sale price in the

event of recovery of the tax or decision of its invalidity; but the taxpayer may establish that such acts were caused by factors other than the tax, or that they do not represent his practice during the period in which the articles were sold with respect to which there was imposed the Federal excise tax which was not paid.

(j) As used in this section—

(1) The term "Federal excise tax" means a tax or exaction with respect to the sale, lease, manufacture, production, processing, ginning, importation, transportation, refining, recovery, or holding for sale or other disposition, of commodities or articles, provided for by any Federal statute, whether valid or invalid, if denominated a "tax" by such statute. A Federal excise tax shall be deemed to have been imposed with respect to an article if it was imposed with respect to (or with respect to the processing of) any commodity or other article, from which such article was processed.

(2) The term "termination of the Federal excise tax" means, in the case of a Federal excise tax held invalid by the Supreme Court, the date of the decision of such invalidity.

(3) The term "refund or credit" does not include a refund or credit made in accordance with the provisions and limitations set forth in section 21(d) of the Agricultural Adjustment Act, as amended, or in section 621(d) of the Revenue Act of 1932.

(4) The term "tax adjustment" means a repayment or credit by the taxpayer to his vendee of an amount equal to the Federal excise tax with respect to an article (less reasonable expense to the vendor in connection with the nonpayment or recovery by him of the amount of such tax or in connection with the making of such repayment or credit) if such repayment or credit is made on or before the thirtieth day after the date of the enactment of this Act, or thereafter in the bona fide settlement of a written agreement entered into on or before March 3, 1936.

(5) The term "taxpayer" means a person subject to a tax imposed by this section.

(k) All references in this section to the purchase or sale (or to parties to the sale) of articles with respect to which a Federal excise tax was imposed shall be deemed to include the purchase or sale (or parties to the sale) of services with respect to which a Federal excise tax was imposed, and for the purposes of subsection (a) the extent to which the taxpayer shifted to others the burden of such Federal excise tax with respect to such services shall be presumed to be an amount computed as follows: From the selling price of the services there shall be deducted the average price received by the taxpayer (or performing similar services during the six taxable years preceding the initial imposition of the Federal excise tax in question. The balance (to the extent that it does not exceed the amount of the Federal excise tax with respect to the services minus any payments or credits to purchasers specified in subsection (f) (3)) shall be the extent to which the taxpayer shifted the burden of such Federal excise tax to others. If during any part of such six-year period the taxpayer was not in business, or if his records for any part of such period are so inadequate as not to furnish satisfactory data, the average price of the taxpayer for such part of such period shall, when necessary for a fair comparison, be deemed to be average price, as determined by the Commissioner, of representative concerns engaged in a similar business and similarly circumstanced. The presumption established by this subsection may be rebutted by proof of the character described in subsection (1).

(1) The taxes imposed by subsection (a) shall be imposed on the net income from the sources specified therein, regardless of any loss arising from the other transactions of the taxpayer, and regardless of whether the taxpayer had a taxable net income (under the income tax provisions of the applicable Revenue Act) for the taxable year as a whole; except that if such application of the tax imposed by subsection (a) is held invalid, the tax under subsection (a) shall apply to that portion of the taxpayer's entire net income for the taxable year which is attributable to the net income from the sources specified in such subsection.

Sec. 502. Credit For Other Taxes On Income.

There shall be credited against the total amount of the taxes imposed by this title an amount equivalent to the excess of—

(a) The amount of the other Federal income and excess-profits taxes payable by the taxpayer for the taxable year; over

(b) The amount of the other Federal income and excess-profits taxes which would have been payable by the taxpayer for the taxable year if his net income were decreased by the amount of net income taxable under this title.

SEC. 503. Administrative Provisions.

(a) All provisions of law (including penalties) applicable with respect to taxes imposed by Title I of this Act, shall, insofar as not inconsistent with this title, be applicable with respect to the taxes imposed by this title, except that the provisions of sections 21, 101, 131, 251, and 252 shall not be applicable.

(b) *Every person (1) upon whom a Federal excise tax was imposed but not paid, or (2) who received any reimbursement specified in subsection (a) (2), or (3) who received a refund or credit of Federal excise tax, shall make a return under this title, which return shall contain such information and be made in such manner as the Commissioner, with the approval of the Secretary, shall prescribe. For any taxable year ended prior to the date of the enactment of this Act the return shall be filed, and the total amount of the taxes shall be paid, not later than the fifteenth day of the third month after the date of the enactment of this Act, in lieu of the time otherwise prescribed by law.*

(c) If the Commissioner finds that the payment on the due date of any part of the amount determined by the taxpayer as the tax would impose undue hardship upon the taxpayer, the Commissioner may extend the time for payment of any such part not to exceed two years from the due date. In such case the amount with respect to which the extension is granted shall be paid on or before the date of the expiration of the period of the extension, and the running of the statute of limitations for assessment and collection shall be suspended for the period of any such extension. If an extension is granted the Commissioner may require the taxpayer to furnish a bond in such amount, not exceeding double the amount with respect to which the extension is granted, and with such sureties as the Commissioner deems necessary, conditioned upon the payment of the amount with respect to which the extension is granted in accordance with the terms of the extension. There shall be collected, as a part of any amount with respect to which an extension is granted, interest thereon at the rate of six per centum per annum from the expiration of six months after the due date of the tax to the expiration of the period of the extension.

SEC. 504. Taxable Years to Which Title is Applicable.

The taxes imposed by this title shall apply only with respect to taxable years ending during the calendar year 1935 and to subsequent taxable years.

SEC. 505. Application of Title to Possessions.

With respect to the following income, the tax under this title shall be in force in any possession of the United States; such tax shall (without regard to the residence or citizenship of the taxpayer) be collected by the appropriate internal revenue officers of such possession; and the proceeds thereof shall accrue to the general government of such possession: (A) Any income specified in subsection (a) (1) or (3) of section 501 if the Federal excise tax with respect to the articles in question accrued in such possession; and (b) any income specified in subsection (a) (2) of section 501 if the reimbursement specified therein relates to articles sold in such possession by the taxpayer under this title and if the geographical scope of the Federal excise tax in question extended to such possession. Income taxable as provided in this section shall not be otherwise taxable under this title. In applying section 501 to such income, the gross income and deductions shall be determined in accordance with the Federal Revenue Act applicable to the taxable year. In applying section 502 to such income, income taxes paid to such possession shall be deemed to be Federal income taxes.

The CHAIRMAN. Now, will you go ahead and explain it?

Mr. TURNER. The first point is on the first page at the end of paragraph 1. I think this is one of the questions of policy which Senator George referred to.

The CHAIRMAN. Take it and explain it in original language, and the change.

Mr. TURNER. The original language is the part which is not underscored. That imposes a tax of 80 percent on the net income from the articles with respect to which the tax was imposed but not paid, to

the extent that the tax was passed on with respect to those articles; that is, it takes into consideration only that part of his year's processing business on which he did not pay the tax.

The new language which is added there would limit the base of the tax to his income for the entire year from the processing business. That is, if he had a loss in his processing business during the part of the year when he paid the tax, that would be allowed as an offset against this unjust enrichment.

Senator GEORGE. That is the big question of policy involved in this.

The CHAIRMAN. He must have made money first?

Senator GEORGE. Under the House bill, he did not have to make any money during the year, but if he had this particular income which was tax-imposed but not paid by him but collected out of his customers, that is treated as a separate item of income and is taxable 80 percent.

Senator HASTINGS. What I want to inquire about is this. Suppose a processor had a retail business; in other words, he had a combination processing and something else, does this apply only to his income from his processing?

Mr. TURNER. The amendment which is in this draft would apply only to the processing business.

The CHAIRMAN. You have confined it to that?

Mr. TURNER. Yes, sir.

The CHAIRMAN. The other part of his income has nothing to do with this provision?

Senator LA FOLLETTE. From other lines?

Mr. TURNER. That is right.

Senator LA FOLLETTE. That is excluded?

Mr. TURNER. That is right.

Senator HASTINGS. Just treated as though it were a separate corporation?

The CHAIRMAN. The committee is unanimous on that proposition?

Senator GEORGE. That is a question of policy.

Senator LA FOLLETTE. That is a question of policy, one which the full committee has to decide.

Senator GEORGE. There were two questions in it which the full committee must decide. Of course if that should be accepted by the full committee—that suggestion—or if it should be rejected, some other slight redrafting would be necessary, would it not, Mr. Turner?

Mr. TURNER. Do you refer to the extension provision?

Senator GEORGE. No.

Mr. TURNER. If this particular point is rejected, all you have to do is to leave the House bill as it was.

Senator COUZENS. Could you give us a concrete example?

Mr. TURNER. A concrete example would be, say that a miller who was on a calendar-year basis for income-tax purposes. He started having his tax impounded, say, the 1st of July, so that he did not pay the processing tax for the last half of the year, but did pay it for the first half of the year. Under the House bill, you would look only from the income standpoint to the processing during the last half of the year. If when he got his money back from the

court, in case it was impounded, if without paying the tax he had a net income from the last half of the year, and looking at that half of the year alone he would be taxed 80 percent on the unjust enrichment part of that income without regard to whether or not he had lost money or made money on the milling business during the first six months of the year.

The CHAIRMAN. You take the whole year into consideration?

Mr. TURNER. That would be the effect of this amendment.

The CHAIRMAN. Yes; this amendment.

Senator GEORGE. Yes; that would be the effect of it.

Senator BLACK. Does it take the whole business?

Senator LA FOLLETTE. Just the part of the business that applies to the milling.

Senator BLACK. How is it possible in most of these businesses to distinguish between them? You take the packers, for instance, who were here. Would this limit the application merely to pork? What I am wondering is whether the books are kept in such a manner that it is possible to distinguish between the part of the business that relates to pork alone.

The CHAIRMAN. If you cannot distinguish, it seems to me that there would be difficulty right away.

Mr. TURNER. As far as possible, we believe it is possible to work that out from his books.

Senator KING. Did not one of the witnesses testify that there would have to be several thousand computations, as many as 40,000?

Mr. TURNER. That relates to another point on which we are making a recommendation. That was the difficulty of tracing—it was cotton which the witness spoke of—of tracing a bale of cotton into all the individual articles which were made from it. I do not recollect that any of the witnesses contended that it would be hard to separate their processing business from the rest of their business if they had any.

Senator BLACK. Whether they contended it or not, let us take the processors in pork and beef. They have that number of employees. Some of them work a half an hour on one thing and half an hour on another. They have a president, a vice president, and they have officers. All of their overhead expense, practically, is of people who give their time and attention to the entire business.

Senator COUZENS. But they must have some system of cost accounting to separate those items.

Mr. TURNER. The bill provides for the allocation of the deduction, and in the type of thing that you speak of, where all of a man's time is not put on the processing business, it would be necessary to prorate the salary of the man, or whoever was involved.

Senator BLACK. I was interested in that. I asked a man yesterday who is not in the packing business but who is in another business, so I asked him about the packing business as an example. I have asked several, and I have found that in the main those that I have talked to said that it would be very difficult to distinguish between that part of the business on which the processing tax was paid, and that part on which it was not. It is going to cause a great deal of complication.

Senator COUZENS. They would not have a very good accounting system if they did not know what their goods were costing them.

Senator LA FOLLETTE. They would have to know it, to put the price on it.

Mr. TURNER. That is necessarily involved in this tax, whether you give this offset or not.

The CHAIRMAN. Suppose you cannot get together on the facts with the packer or the miller. What is the next step which the Government will take?

Mr. TURNER. Of course, the taxpayer will make his return on the basis which he thinks is proper. The Commissioner or, rather, the revenue agents will investigate the case and make their conclusions, and if the Commissioner does not agree he will send out a notice of deficiency in tax. Then it is a question of negotiation with the taxpayer or an appeal to the Board of Tax Appeals.

The CHAIRMAN. You will proceed just as you do in other cases?

Mr. TURNER. Just as in any other income tax.

Senator HASTINGS. I would like to put an example and see if I understand it. Suppose you could show that a corporation had a \$100,000 profit by reason of this tax, what you would call unjust enrichment.

The CHAIRMAN. Is that for the whole year?

Senator HASTINGS. Yes. But he also showed in that business an \$80,000 loss.

Mr. TURNER. The other part of the year when he paid the tax? Is that what you mean?

Senator HASTINGS. I do not necessarily separate it.

The CHAIRMAN. Say on July 1 it showed one thing and from July 1 on, for the balance of the year, that last year, that he had shown a gain of \$100,000 and a loss, say, of \$80,000 for the first 6 months?

Senator HASTINGS. What I wanted to know was whether you took the 80 percent of the 20 that he had left.

Mr. TURNER. The House bill would take 80 percent of \$100,000.

Senator HASTINGS. I understand that. You would take 80 percent of the 20?

Mr. TURNER. I probably ought to say right now that the Treasury is not very favorably inclined to this offset, but the effect of the amendment, if I understand your example, would be to limit the tax to 80 percent of the 20.

Senator LA FOLLETTE. As I understand it, it was recognized in the House that there was a serious constitutional question here, and in order to protect it they put in a separability clause?

Mr. TURNER. That is right.

Senator LA FOLLETTE. And while it may appear that it would be more equitable to follow the policy suggested in this amendment we are now discussing, will you please point out to the committee, as you did to the subcommittee yesterday, the fact that this will not work equitably in some cases?

Mr. TURNER. If you apply it simply to the unjust enrichment, in a sense you are treating everybody alike, because you are taxing them that unjust enrichment, which is the basis of this tax, and not looking at any facts outside of the unjust enrichment. If you start giving an offset for losses outside of the unjust enrichment period, the question immediately comes up how far you are going to go. If you give it for the taxable year, it operates pretty accidentally

between different taxpayers according to the extent to which their taxable year corresponds with this unjust enrichment period. Some of them will be on a calendar-year basis and will have practically no opportunity for an offset. Others will be on a fiscal-year basis, so that the unjust enrichment will fall into 2 taxable years, and the effect will be to give them an offset for losses during a big part of the year before the tax and the peak of another year after the court's decision.

The CHAIRMAN. What percentage within the calendar year and what percentage within the fiscal year, if you know?

Mr. TURNER. Generally speaking, the great majority of taxpayers are on a calendar-year basis. I cannot vouch for this fact, but I know that one of the millers was complaining to me that he was on a calendar-year basis and would get practically no benefit from this sort of a provision and, according to him, most of the other millers were on a fiscal-year basis and would get a good deal of benefit from the offset for losses during the period following the tax. Whether that is true or not, I cannot say.

Senator KING. Take a case where the vendor of pork and lamb and various other kinds of meat commingled them, so to speak, together, and perhaps sold his pork at a less price than he perhaps would have been warranted under the market in order to increase the sale of his other marketable meats and, as a result of the whole transaction during the year, there was a loss and it was impossible to distinguish just where the loss occurred, whether it was in the increased overhead or in the diminished price at which he sold the pork to increase the sale of the others, or bad management or what, what would be the situation?

Mr. TURNER. Your example simply shows the difficulty of working out the accounting problems involved in this thing, and about all that can be said is that we think we will be able to work them out with a good deal of fairness.

Senator KING. You will just take a sword and cut the Gordian knot?

Mr. TURNER. I do not think we can use too much of a sword on taxpayers.

The CHAIRMAN. The subcommittee that had this provision up—Senator George, you were chairman of it. Do you believe that this change is for the better?

Senator GEORGE. I am inclined to think so. However, I have talked with various people. The packers say frankly that it won't help them at all.

The CHAIRMAN. How about the little packers?

Senator GEORGE. The little packers claim it won't help them primarily, but I do not see why it would not help them. The big packers say it will not help them. They want it for 3 years, they want to carry the loss over for the subsequent year to the tax. They say that is the only thing that could help them. The textile people tell me that it won't seriously affect them. Perhaps there is a weak unit here and there on the verge of bankruptcy or receivership that made no profits at all, although they did get a little "windfall" tax. They might be slightly helped, but they say for the most part during the taxable year in which they had this refund coming back to them or impounded these taxes, that they all did show some

actual profit, big or little, and they do not think it will affect them very much.

Senator CLARK. The "windfall" tax is going to help a lot of these little packers.

Senator GEORGE. I thought it would help the little packers more than anyone else.

The CHAIRMAN. Senator, did you give any thought to the question of the offset on the part of the processors, as to whether he could apply it to the fiscal year or to the calendar year?

Senator GEORGE. No; we gave no thought to that.

Senator LA FOLLETTE. I do not think we should consider that, Mr. Chairman, because in every case the Government will take a licking. I think that we ought to set the policy on the basis where we think that the greatest equity lies, and then it will have to fall as the incidence of business require.

The CHAIRMAN. The reason I asked that question was in view of what he said, that some miller had stated it would help some and not help others.

Senator LA FOLLETTE. If you permit a taxpayer to take the option, it does not seem to me that it will be just to the Government, assuming that you are going to impose this tax.

Senator GEORGE. Within the taxable year in which he receives it, within the calendar year in which he received it, would seem to me to be the only basis on which you could apply it. I do not think you could give an option. To my mind, this is the strongest consideration. Perhaps the poor business man had lost during a part of his calendar year, and he nevertheless impounded these taxes and got them back, but he had a net loss on his whole year's transactions. To give him the benefit of this amendment here is to give to the unsuccessful business enterprise an advantage that you do not give to the successful man who has properly managed his business and shown a little profit. In other words, here are two men that are getting back a refund of the taxes. One by good business management has shown profits during the year, and the other has not shown them. One escapes the tax altogether and the other has to pay it. That, to my mind, is the strongest consideration against it. That is, assuming you are going to impose this tax.

I think I should state that, because I made inquiry of all of the groups that are affected by it. Most of them think it ought to be put in, although the large packers say it does not help them and does not affect them at all.

Senator GERRY. How will your amendment affect the little pork packers in the case we had?

Senator GEORGE. I think it would probably help them.

The CHAIRMAN. Is there any other provision that you have suggested here that goes to relief of the little packer?

Senator GEORGE. We have suggested only one other thing, and that is we have suggested the principle applied to the payment of estate taxes be applied to all payments under these windfall taxes; that is to say, we have suggested lodging in the Commissioner the discretion to allow these payments in installments over 1 or 2 or 3 years if necessary, in order to prevent the bankruptcy of these people who, if they were called upon to pay this windfall tax at once, undoubtedly would suffer greatly.

The CHAIRMAN. You have given them the opinion for 3 years? Senator GEORGE. Did you put in 3 years, Mr. Turney?

Mr. TURNNEY. I put in 2 years.

Senator GEORGE. Of course, that is a matter for the committee.

The CHAIRMAN. The estate taxes are 10 years.

Senator GEORGE. We were suggesting that same principle. That is the only thing that the subcommittee had thought of as being in the nature of relief, particularly to the small packers, and maybe other processors who were weak and who received a considerable sum of money now as measured by their total assets. To make them pay it all at once or within 1 year, we certainly feel would result in receivership in some instances.

The CHAIRMAN. What interest would you suggest under that deferred payment?

Mr. TURNNEY. Six percent.

Senator KING. We are paying 6 percent to those that get refunds from the Government.

Mr. TURNNEY. Yes, sir.

Senator KING. That ought to be cut, it seems to me. Perhaps not in this bill, but in some subsequent measure.

Senator COUZENS. Senator Black had the list of concerns yesterday, or the other day, that were in bankruptcy or on the edge of bankruptcy, and some of them saved from bankruptcy through the decision of the A. A. A., and in those cases there were large accumulated taxes that were not paid because they were unable to be paid. Is the cancelation of those contemplated?

Mr. TURNNEY. To the extent that the invalidation of the tax resulted in the wiping out of assessments that would constitute unjust enrichment under this bill?

Senator COUZENS. Assuming that prior to the decision of the court, a packer, exclusively a hog packer—I will use that example because he had no way of offsetting his losses in that particular business—he had accumulated a back tax of a couple of hundred thousand dollars and had not been able to pay the Government because he did not have it to pay, and the Government took possession of his plant, the receipts of the plant. That was done in some cases, was it not?

Mr. TURNNEY. I could not say for certain.

Senator COUZENS. Is there anybody here that knows whether that was done?

(No response.)

Senator COUZENS. I understood it was done, but I may not be accurate.

Mr. TURNNEY. I know that the statement was made in the hearing.

Senator BLACK. There are liens on file on some of them.

Senator COUZENS. When the Court decided the case, all of that debt was canceled, was it not?

Mr. TURNNEY. Yes, sir.

Senator COUZENS. So this does not only apply to the particular money that was put into the Court when the case was being contested, and impounded, but it applies to all of the accumulated taxes prior to that time because of the inability of the corporation to pay. That is all canceled. Would that be computed in the unjust enrichment taxes?

Mr. TURNER. Yes, sir; that would be treated the same as any other tax that was not paid.

Senator COUZENS. You are going to find not only the list that Senator Black had, but you are going to find thousands of others that cannot pay it, and I just wondered what the Government procedure was going to be in a case of that sort.

Senator GEORGE. This is the true picture. In many instances the processor on whom the tax was imposed did not have the ready cash; and through the leniency or indulgence extended by the tax collector, he carried the processing taxes until they accumulated into considerable sums. There are instances within my knowledge where some small meat packers were unable to pay the tax and did not pay it because they did not have the money to pay it, and accumulated a sum that is now equal to practically all of their assets, and certainly they cannot pay those taxes if they are forced to pay them now; and they saved their tax, of course, by virtue of the decision of the Court.

Senator HASTINGS. Would the accounts show, in the suggestion Senator Couzens made, that those companies made a profit during those years but just could not get enough money together to pay these taxes?

Senator GEORGE. Presumably, Senator Hastings, they were operating on some profit, and they were passing on the tax to the consumer if they could. There is no doubt in the world that and presumably they did pass it on, or part of it.

Senator HASTINGS. If they made a profit, this section here would not relieve them, but if they did not make a profit it would relieve them.

Senator GEORGE. That is true. This section here would mollify the harsh provision on the taxpayer that he must pay 80 percent of this windfall profit of tax that he did not pay the Government, and yet passed on, or the tax that he had impounded in court and finally got back and yet passed on, and would not treat it as a separate item of income, but would merge it with all of his income during that taxable year, from the particular articles made from the commodity on which the processing tax was imposed.

Senator CLARK. Is not this the fact, that in the case of a lot of little packers, that they were not able to pass on the tax in competition with the big packers? That they had to go out and pay a much higher price for the raw product than the big packers did, and at the same time had to compete with the big packers in selling their finished or processed goods, and were not able to pass this tax on, and at the same time this windfall tax raises what amounts to a conclusive presumption that they did pass it on?

Senator LA FOLLETTE. I do not think that is a fair statement.

Senator GEORGE. That is their contention, Senator Clark. We do have some of the changes made in subsequent parts of this title that will mollify that harsh, arbitrary rule to some extent.

Senator KING. If they can show, in other words, that they did not pass the tax on—

Senator GEORGE (interposing). If they can show that, they would not be liable, of course.

Senator KING. Several persons have spoken to me in regard to this matter, and some have written that their alleged profits con-

sisted of bills receivable or accounts receivable which they never received and therefore they had no profits. On their books they showed a profit, but they had trusted and given credit in several instances, my recollection is, to the persons who owed them very large sums and who had gone into bankruptcy.

Senator LA FOLLETTE. When the taxpayer came to make out his return, he would do in this instance just as in any other instance as though he had any losses of that nature; he could, of course, get deduction for that.

Mr. TURNER. That is right; he would get the bad-debt deduction.

Senator COUZENS. What Senator Clark said is substantially true. These big packers had a multitude of things, beef and sheep and lambs and hogs, and they were not relying on hog packing to base their profit or the success of their business, so that when this went into effect there were literally thousands of packing concerns that only pack hogs, and they had to go out and compete with the big fellows in buying the hogs because of the scarcity; then they had to go out and compete with the big packers in selling, and the big packer did not rely upon the sale of this one product to make a profit, so he put the price down to a point where he could get the business, and the little fellow could not do that because he had nothing to offset the losses in the hog division of his business. It is perfectly absurd to think that you can take those and lump them all in one classification.

Senator LA FOLLETTE. Of course, Senator, if in that process, and in order to meet the competition of the big packer, he absorbed the tax, he won't be liable under this windfall provision.

Senator COUZENS. If you use the rule that as I understand is in the bill, or was in the bill, of fixing the differential between the spread of what he paid for his goods and what he sold them for, if that is the yardstick, he won't be protected under this provision, and that is the yardstick that I understand is proposed to determine whether he did pass the tax on or not, and that is an inequitable yardstick.

Senator HASTINGS. That is what the Treasury Department suggested as the easy way to determine it.

The CHAIRMAN. Is it possible to define it, dividing this into two classifications of the large and small packer?

Mr. TURNER. I do not see how you can.

The CHAIRMAN. I do not, either.

Senator GEORGE. The subcommittee could see no way, and the smaller packers suggested a graduated tax. That, of course, would in time be treating it just as ordinary income. That is what it would amount to.

Senator HASTINGS. This suggestion here is certainly some improvement anyway.

Senator BLACK. Frankly, Mr. Chairman, I clearly do not understand it. I would like to find out.

Senator GEORGE. Mr. Turner, will you please explain just what it is that this change means?

Senator BLACK. May I ask one or two questions which would clarify it in my mind?

Mr. TURNER. Certainly.

Senator BLACK. If a profit is made of 1 percent or 10 percent, there is no difference so far as the proposition of the tax is concerned, under this amendment?

Mr. TURNER. You are speaking of the ratio of profit to gross sales?

Senator BLACK. Yes.

Mr. TURNER. This bill makes no difference.

Senator BLACK. The amendment?

Mr. TURNER. Neither the amendment nor the bill.

Senator BLACK. This is a tax on the amount of unpaid processing taxes. That is really what it is.

Mr. TURNER. To the extent that the taxes were passed on.

Senator BLACK. To the extent that they were passed on. You have a provision here, a provision which I do not quite understand. If there is a loss by the company, is there any tax imposed under this amendment?

Mr. TURNER. Under the amendment, if there was a loss on the processing business for the entire year, there would be no tax imposed.

Senator BLACK. If there is a profit, how much tax is there? Is it limited to the amount of profit made?

Mr. TURNER. Under the statement of the amendment it would be limited to the amount of profit made on the processing based on the entire year.

The CHAIRMAN. Eighty percent.

Senator BLACK. And you do attempt to limit it in those figures to the part of the income which came from the particular thing processed?

Mr. TURNER. That is right.

Senator BLACK. Suppose it covered all of the goods and did not merely cover the processing part, then would that not automatically bring about what they have been speaking about, a relief to the small packer who is engaged, for instance, only in packing pork, and who is not, like the larger packer, engaged in various other types of business?

Mr. TURNER. If the small packer who was only packing pork and has no other business, it would not make any difference whether it was limited to that business or not, if that is all of the business he had. To the people who have other lines of business, it would be, I think, purely accidental whether taking into account all of their business, if the rest of their business was profitable, they would be better off, not taking it into consideration, and if they had losses in their other line of business, of course, they would be better off in taking those into account.

Senator BLACK. And you believe that you can figure out the differences from the books of account?

Mr. TURNER. I have been advised by the accountants in the Bureau that they think this can be done.

Senator BLACK. Suppose a man here has not paid the tax to the Government but has paid it back to his purchaser. What effect is he in here? This does not eliminate him?

Mr. TURNER. He is taken care of by a later provision.

Senator BLACK. In this bill?

Mr. TURNER. In that bill; yes.

The CHAIRMAN. It seems to me that the subcommittee has made a very wise suggestion here. All in favor of this particular amendment will say aye.

(The amendment was agreed to.)

The CHAIRMAN. Now go to the next.

Mr. TURNER. The next amendment, paragraph 2 on page 1, consists entirely of rewording the paragraph for clarification without any change in substance. That is the paragraph which taxes the middleman who got a rebate of the amount of the tax from the processor, although he had passed it on to his customer. There is no change in substance there.

Senator KING. Do you think that is workable? Have you any data that show the feasibility of that?

Mr. TURNER. Well, it is like the rest of the bill, Senator. It is something entirely new. I think it is only fair to say that there is probably less difficulty there than in the case of the processor.

The CHAIRMAN. The House bill did not treat with the middleman?

Mr. TURNER. This is in substance the same as the House bill.

The CHAIRMAN. You think this is all right, Mr. Turner?

Mr. TURNER. Yes, sir.

The CHAIRMAN. All in favor of that amendment will say aye. That includes what?

Senator GEORGE. All of no. 2.

The CHAIRMAN. That takes in the latter part of page 1 and the first five lines of page 2.

All in favor signify by saying aye.

(The amendment was agreed to.)

The CHAIRMAN. Now, paragraph 3.

Mr. TURNER. Paragraph 3 is a new provision. It is technical in nature and actually has no application to the processing tax aspect of this thing. It is necessary because this bill relates to unjust enrichment not only from the processing taxes, but from any other excise tax, and relates to unjust enrichment by way of rebates as well as by way of nonpayment.

The House bill was set up on the theory that when a refund was made, the income should be computed by a redetermination of the net income for the year in which the tax was paid, disallowing the deduction for the tax paid.

This change would treat the refund as income and compute the unjust enrichment for the year in which the refund was made.

The state of the law for general income-tax purposes on the treatment of refunds of taxes which have been deducted for prior years is somewhat doubtful, but this change in the bill conforms to the practice which is the one which the Bureau of Internal Revenue now thinks is correct and would like to follow.

The CHAIRMAN. Without objection, then, no. 3 will be agreed to.

Senator COUZENS. Does that include subsection (b), too?

Mr. TURNER. No, sir. That is down to that subsection.

Senator KING. You said "other excise taxes." To what did you refer?

Mr. TURNER. This title in terms relates to unjust enrichment with respect to any Federal excise tax. That term is defined to mean, generally speaking, the excise taxes with respect to manufactured

articles and commodities of the sort which are ordinarily passed on to the purchasers.

Senator WALSH. I have a memorandum given to me which states that there are more than 200 different articles under certain provisos on which Federal excise taxes are imposed at the present time, and some of the more important of these are automobiles, tires, candy, radios, refrigerators, chewing gum, tobacco, liquor, gasoline, oils, and so forth. Also such service as telegraph, telephone, radio, cable facilities, safe-deposit boxes, electric energy, and many others. Would this provision apply to all of these?

Mr. TURNER. That is right, it would.

Senator WALSH. They all have to make returns?

Mr. TURNER. They only have to make returns when they get the refund of one of those taxes, or fail to pay one of those taxes.

Senator HASTINGS. It does not apply, generally, to having paid these taxes in the past, and the question whether they passed them on in the past.

Mr. TURNER. I won't apply to anyone who paid his Federal taxes and does not get a refund.

Senator KING. I do not understand that yet.

Senator CONNALLY. Suppose on an automobile, for instance, he paid the excise tax and passed it on to the customer and they afterward got a refund, does it apply?

Mr. TURNER. That is right.

Senator CONNALLY. You would make him show how much he paid out of that particular source of revenue?

Mr. TURNER. That is right.

Senator CONNALLY. And you tax him 80 percent of that?

Mr. TURNER. That is right.

Senator GEORGE. It applies generally and not merely to these particular processing taxes?

The CHAIRMAN. Without objection it will be agreed to.

Mr. TURNER. Subsection (b) excludes from the computation of this unjust enrichment three classes of cases. The first one is the most doubtful. I think the second and the third are quite clear.

Senator KING. You mean doubtful as to constitutionality?

Mr. TURNER. No. The first one involves some question of policy, and that is the case where the taxpayer had the articles on hand on the date the tax was terminated, that is January 6, 1936, in the case of the processing taxes. Some of the witnesses objected to bringing in the articles which were not sold during the taxable tax period, for two reasons.

First, they say that there is no logic in talking of passing on a tax after the tax ceased to be in existence. Second, they point out that they may have some of these articles on hand for years, and that the thing ought to be cut off for that reason to keep the computations from going on forever.

Senator GEORGE. Under this (b) what the taxpayer sold is merchandise, and after the tax was declared invalid, that does not come into the picture.

Mr. TURNER. That would be the effect of class 1.

The CHAIRMAN. That it would not have any effect if he sold it after the law was declared unconstitutional.

Senator GEORGE. Yes. The House bill seems to cover that period immediately following the invalidation of the tax, as I understand it.

Mr. TURNER. That is right.

Senator GEORGE. And this takes that out, because after the tax is declared illegal and void, of course they would not pass on the tax even though they made profit on the goods, or substantially the same profit. It seems to me at least that that contention on the part of the taxpayer was entirely valid.

Senator CONNALLY. That is the theory that we are letting them have refunds on floor stocks and other things that they had on hand, all the tax automatically went off.

Mr. TURNER. Of course, the floor stock refund provisions of the House bill gave that refund only when the taxpayer showed that he has cut his prices. To some extent the House bill and the refund provisions recognized the possibility of passing the tax on after it ceased to be in existence.

The CHAIRMAN. I do not see how he could pass it on after it ceased to be in existence.

Senator BLACK. It seems to me it is very unsound for us to proceed on the windfall tax on the basis that they passed it on, and then after the tax is repealed, to say that they are still passing it on. The trade and business is free from the effect of the tax. It might be a psychological effect.

Senator LA FOLLETTE. As I understand the question, the contention of the Department of Agriculture was that many of these people had fixed a price on their goods that included the tax, and that they continued that for a period after the tax was declared unconstitutional. In other words, that as a matter of fact, they were still including a computation of the tax in the sale price of their commodities to the customers even though the tax had been declared invalid, and as I understand it, that was the reason that the House had this provision in it.

Senator CONNALLY. Is that not such an intangible thing that you could never enforce it? Why bother with it?

Senator LA FOLLETTE. I was simply trying to present, so that the committee could have it, the theory behind both of these suggestions; the one that the House made and the one that is now contained in subsection (b).

Senator KING. Presumptively when the tax was stricken down, some would cease to pass it on and prices would automatically adjust themselves to the situation.

The CHAIRMAN. Wherever there was competition, it would seem to be impossible to pass it on after the tax was declared unconstitutional. All right, now let us proceed.

Mr. TURNER. Clause (2) is a provision which the Treasury is inclined to favor as really an oversight in drafting the original bill. That is the provision which excludes the cases where the taxpayer has repaid to his customer the amount of the tax which he had passed on to him.

Senator KING. Are there many cases of that kind?

Mr. TURNER. Yes; that has been done very widely.

The CHAIRMAN. The House bill permitted that, did it not?

Mr. TURNER. The House bill took care of it by allowing an offset of that amount against the amount of the burden which was shifted

as computed. This really merely simplifies the procedure. You do not have to make any computations at all.

The CHAIRMAN. Now, take no. 3. What is that?

Mr. TURNER. No. 3 excludes any income from articles with respect to which the taxpayer would have been entitled to a refund even though the tax had been valid; in other words, the exports and the charitable distributions.

Senator COUZENS. And sales to the Government?

Mr. TURNER. Yes. I think that is a proper provision.

The CHAIRMAN. Without objection (b) will be agreed to. Now, go to (c).

Mr. TURNER. (c) is the provision for computing the net income from the part of the business with respect to which the tax was not paid. Paragraph (1) is substantially the provision in the House bill which says that it shall be computed by apportioning deductions to the gross income from those sales.

The CHAIRMAN. So that (1) is just the same as the House bill?

Mr. TURNER. Yes.

The CHAIRMAN. Proceed with no. 2.

Mr. TURNER. Paragraph (2) is an attempt to simplify that problem which is very difficult, and that is what some of the discussion has related to, by giving the taxpayer an option to compute that net income on the basis of his average net income per bushel of wheat or per bale of cotton for the entire taxable year, and it will very much simplify the problem.

The CHAIRMAN. You mean the calendar year?

Mr. TURNER. For the taxable year, whether it is the calendar year or the fiscal year.

Senator LA FOLLETTE. That is the point you brought up, Senator King, and the witness testified how many computations would have to be made.

Mr. TURNER. This is the provision they asked for to take care of that, and we are inclined to think it is a good idea.

The CHAIRMAN. Without objection no. 2 will be agreed to.

Senator KING. Have you conferred with any of those who made that complaint about the mysterious qualities of this provision, so that they are more or less satisfied with it?

Mr. TURNER. Of course, I have not submitted this language to them. I had the language which they suggested, and I am sure that this language carries out the policy that they were asking for.

Senator KING. Senator Bailey and Senator George should be able to advise us as to textiles.

Senator GEORGE. This raises the whole question of what Senator Clark said about the packers, and what Senator Couzens said about it, and what others have said in regard to other processors. The whole theory under which it is determined that they did not pay the tax and yet passed it on is rather arbitrary, and it may result in casting upon a taxpayer an impossible burden to show that he did not pass it on, but this does simplify it. This option to the taxpayer does unquestionably simplify his accounting and does make his task easier and makes it possible for him to show what actually happened in his business, without going through each invoice and following down the raw material down to the sale made of the processed article.

Senator LA FOLLETTE. On the other hand, also it has the advantage of simplifying the problem from the point of view of the Treasury if the taxpayer elects to use this method.

Senator GEORGE. And undoubtedly they will so elect. All of the textile people say they will elect this because, irrespective of how it cuts, it will be to their interest to do it, and it is the only method by which they can really present it.

Senator BLACK. That would meet the situation suggested by the leather people also, does it not?

Senator GEORGE. Yes. I think all of them favor this simplification of it or this option given to them. So far as I know, all of the processors who have talked with me seemed to think that this would be helpful both to the Government and to them.

The CHAIRMAN. Mr. Turney, here is a letter on this proposition from the American Hospital Association [reading]:

In behalf of the hospitals of the American, Catholic, and Protestant Hospital Associations, which our committee represents, we wish urgently to request that the Finance Committee of the Senate modify the provision contained in section 501 (e) 3 of H. R. 12395, covering refunds such as may be made to hospitals, as the ultimate consumer, by processors from excise taxes recovered by them through order of the Supreme Court.

A number of these processors have expressed their desire to pass on to our hospitals, the hospital's share of these recovered excise taxes, as soon as they can be assured legally that they will not be called upon to pay them a second time. Section 501 (e) 3 provides that this must have been done prior to March 3, 1936, or a bona-fide written agreement entered into prior to that date. Our hospitals, I regret to say, have not received these refunds and do not have such a written agreement.

It is my understanding that your Committee has under consideration the liberalization of this section; such as the advancement of this date. Accordingly on behalf of our hospitals, we sincerely request that some such amendment be made to the present bill whereby these processors will be given the opportunity to make proper refunds to hospitals, before the taxes provided for in this bill become effective.

Charitable hospitals, as you know, have received no direct Federal aid toward the needed hospitalization that they have given to those on relief. Their employees' wages have been reduced, their plants have depreciated and they have gone into debt in order to render this service. They now ask that provision be made so that they can obtain the refund of these excise taxes to which they originally were entitled under the A. A. A.

Have you read this communication?

Mr. TURNNEY. Yes.

The CHAIRMAN. That has been taken care of?

Mr. TURNNEY. Yes.

Senator GEORGE. That relates to the date of March 3.

The CHAIRMAN. Without objection, No. 2 on page 3 will be agreed to.

Now (d).

Mr. TURNNEY. The changes in paragraph (d) are purely clerical. They are in the nature of cross-references to the new paragraph (3) on page 2.

The CHAIRMAN. You have suggested those?

Mr. TURNNEY. Yes.

The CHAIRMAN. Without objection they will be agreed to. How about (e) on page 4?

Mr. TURNNEY. (e) Is the provision for computing the extent to which the tax was passed on. The change there is to give the tax-

payer an optional method of computing that on the basis of averages for the year. It is a provision which the textile people and the milling people particularly asked for, and which we favor because it will simplify it.

The CHAIRMAN. That takes in all of (e)?

Mr. TURNER. Yes, sir.

The CHAIRMAN. Without objection that will be agreed to. How about (3) on page 5?

Mr. TURNER. There is one little thing at the end of (e) which is new, and that is giving them credit for the amount by which the tire tax was increased on account of the invalidation of the processing tax.

The CHAIRMAN. You suggested that, I understand?

Mr. TURNER. Yes, sir.

The CHAIRMAN. And that was presented to us?

Mr. TURNER. Yes.

The CHAIRMAN. Now, no. (3).

Mr. TURNER. The next substantial change is on page 5 with respect to the tax-year period. The House bill provided for computing this passing on the tax by comparing the margin during the wind-fall period with the gross margin and with the 5-year period preceding the tax. The cotton textile people in particular have asked that that 5-year period be made 6 years in order to include 1927, which was a good year, and to balance what they claim is the unfavorable effect of using 1928 to 1932.

The CHAIRMAN. What did the Treasury think about it?

Mr. TURNER. Well, as far as the fairness is concerned, there seems to be a good deal to their contention. Of course, the longer the period is made, the more extended our investigation has to be. However, if the committee thinks that the equities demand the lengthening of the period—

The CHAIRMAN (interrupting). Was the subcommittee unanimous on that?

Senator GEORGE. Yes; I think so.

The CHAIRMAN. Without objection it will be agreed to. What is the next one?

Mr. TURNER. In paragraph (2), beginning at the bottom of page 5 or at the top of page 6, there has been written in a provision which the cotton people asked for, which takes into account in computing their presumption as to how much tax was passed on, the direct manufacturing costs.

Senator COUZENS. That would cover the extra cost of the N. R. A.?

Mr. TURNER. Yes, sir. The House bill allowed the direct manufacturing cost to be shown as evidence to rebut this presumption. This change would take into account in computing the presumptive shift of the tax, and I do not think that we are inclined to oppose that change.

The CHAIRMAN. Without objection that will be agreed to. Now, no. (3)?

Mr. TURNER. That is a provision with respect to the March 3 date.

Senator GEORGE. That was the point that was raised in the Hospital Association letter that was read.

Senator BYRD. In determining the direct manufacturing costs, you take a large packer—would he be required to keep separate costs for the hogs or the cattle, or can he put it all in together?

Mr. TURNER. All through this tax it is necessary for this purpose and other purposes to apportion deductions of which the direct manufacturing costs are one, to the taxed articles. In the case you mention it would be pork.

Senator BYRD. Wouldn't that be practically impossible because with cattle there was no processing tax, and with sheep there was not. A large packer handles all of those things. It seems to me it is to the advantage of the big packer and the disadvantage, as Senator Couzens says, of the small man who handles hogs alone.

Senator COUZENS. As I pointed out previously, Senator, I think any kind of an institution must keep a cost accounting system, and he must have a cost basis which involves a distribution of the manufacturing costs, and he would ordinarily have that, in any event.

Senator BYRD. It seems to me it would be most difficult to segregate the overhead costs of Armour & Co. on hogs alone.

Senator COUZENS. They must do it in order to get their costs.

Mr. TURNER. It is necessary as to the overhead costs, of course, to prorate them according to the volume of the various packers.

Senator CONNALLY. Most modern packers would have a separate hog account, would they not?

Mr. TURNER. I should think so, for their own accounting system.

Senator CONNALLY. They would want to know whether they are making money on the hogs or losing on the hogs.

Senator BYRD. But there are a lot of overhead costs.

Senator CONNALLY. They would prorate those.

Senator LA FOLLETTE. It is inherent in the business, otherwise they would not know anything about their business if they did not have a cost accounting system. The packers can tell you about what everything costs except the squeal.

Senator BYRD. I think that is very true, providing you had taxes on all the other articles that they handle. In this instance, only the hogs were taxed. Cattle and other things were not taxed.

Senator GEORGE. In reality, this does not inject a new principle. It simply brings it under the equation.

Senator BYRD. I do not object to it; but it certainly gives them a chance to apportion the costs.

Senator KING. I think that the entire effort to enforce this, while I think these people that have an unjust enrichment ought to refund to the Government, but it simply means, I think, a vast amount of work to the Treasury, and a large amount of employment for expert accountants and lawyers, and the result will be quite unsatisfactory to everybody.

The CHAIRMAN. Without objection, we will agree to it. The next?

Mr. TURNER. The next change relates to the March 3 date in the House bill.

Senator COUZENS. You have extended that to the thirtieth day after the enactment of the act?

Mr. TURNER. Yes; it allows all rebates made after 30 days of the enactment of the act, and after that if it relates to a contract which they had on March 3.

The CHAIRMAN. And the contract was the closed date of March 3?

Mr. TURNER. Yes, sir.

The CHAIRMAN. Without objection, that will be agreed to.

Senator BLACK. Does it still have to be in writing?

Mr. TURNER. All rebates up to 30 days after the date of the enactment of the act that are actually made will be actually allowed, whether there was any contract or not.

The CHAIRMAN. Let us take (g).

Mr. TURNER. The first change there is simply a clerical change to clarify the provision.

The new sentence added was suggested by some of the accountants in the Bureau and is to this effect, that where the taxpayers' records are not sufficient to show the quantities of commodities going into particular articles the amount shall be computed by the conversion factors which were used for these purposes under the Agricultural Adjustment Act.

The CHAIRMAN. Without objection, that will be agreed to.

(h), there is no change.

Now, (i).

Mr. TURNER. The words added there are a clerical change. Since labor costs are shifted over into a presumption, they are excluded by those words.

Senator KING. Where you say there is no objection, you mean to the House bill? Does that mean that the Treasury Department is satisfied with the phraseology and with the entire principle announced in the House bill dealing with these questions?

Mr. TURNER. These amendments include all the changes in wording which we have to suggest to the House bill.

The CHAIRMAN. And this is also the recommendations offered by the subcommittee that studied the proposition?

Senator GEORGE. Yes.

The CHAIRMAN. The next?

Mr. TURNER. The next is at the top of page 9. That first change is a shift in the position of the underscored words to clarify it and no change in substance.

The CHAIRMAN. Without objection, that will be agreed to.

Mr. TURNER. Paragraph (2) is a definition of the term that was used on the first page, the termination of the tax, and it is defined to mean where the tax was held unconstitutional, the date it was so held.

The CHAIRMAN. Without objection, it will be agreed to.

Mr. TURNER. Paragraph (3) is the definition of refund or credit, which excludes refunds and credits made in accordance with section 21 (d) of the Agricultural Adjustment Act or 621 (d) of the 1932 Revenue Act.

Senator COUZENS. That straightens out what the taxpayers were alarmed about in the House bill where it seemed to exclude all refunds which were not excluded in 21 (d) of the A. A. A.

Mr. TURNER. Yes; that is taken care of in these amendments.

The CHAIRMAN. Without objection they will be agreed to.

Mr. TURNER. Paragraph (4) is a definition of the term "tax adjustment", which has been used to refer to these rebates to customers, and it is drafted in accordance with the other provisions of this March 3 date.

The CHAIRMAN. Without objection it will be agreed to. Now, (k) on page 10.

Mr. TURNER. Those changes are purely clerical and allow an offset for the rebates made to the purchaser.

The CHAIRMAN. Without objection it will be agreed to.

Mr. TURNER. The changes on page 11 inserting the words "the other" are purely clerical.

The CHAIRMAN. Without objection, it will be agreed to.

Mr. TURNER. The change on page 12 requires every person who has had his taxes impounded or did not pay them or who got a rebate from a processor or who got a refund of one of those taxes, to file a return and show whether or not he passed the tax on. It will be helpful in administering it.

The CHAIRMAN. Without objection, that will be agreed to.

Mr. TURNER. Paragraph (c) on page 13 should be underscored. It is not. That is a new provision which Senator George spoke of.

Senator LA FOLLETTE. Will you read that, please?

Mr. TURNER. Yes. It is a provision for the extension of time for the payment of the tax, modelled after the estate tax provision.

The CHAIRMAN. This is rather important.

Senator GEORGE. I was disposed to think that we might allowed them three or four years. Where you take a case of a half a million dollars or a million dollars to be repaid. It is discretionary. Of course it is left within the discretion of the Commissioner, and he will safeguard the interests of the Treasury if he does grant the extension, but I think this is the one way of softening the blow to the man who is going to pretty nearly if not altogether shoved over into bankruptcy if he has to pay this tax in 1 year.

Senator LA FOLLETTE. I would like to have it read, Mr. Chairman, because this has been drafted since the subcommittee meeting, and we agreed on principle, but this is the language to carry it out, and we have not had a chance to see it.

Mr. TURNER. The provision is as follows [reading]:

(c) If the Commissioner finds that the payment on the due date of any part of the amount determined by the taxpayer as the tax would impose undue hardship upon the taxpayer, the Commissioner may extend the time for payment of any such part not to exceed 2 years from the due date. In such case the amount with respect to which the extension is granted shall be paid on or before the date of the expiration of the period of the extension, and the running of the statute of limitations for assessment and collection shall be suspended for the period of any such extension. If an extension is granted the Commissioner may require the taxpayer to furnish a bond in such amount, not exceeding double the amount with respect to which the extension is granted, and with such sureties as the Commissioner deems necessary, conditioned upon the payment of the amount with respect to which the extension is granted in accordance with the terms of the extension. There shall be collected, as a part of any amount with respect to which an extension is granted, interest thereon at the rate of six per centum per annum from the expiration of six months after the due date of the tax to the expiration of the period of the extension.

Senator HASTINGS. I do not think that helps them at all. If he has to give that bond to pay the money, he can go and borrow it from the bank just as well as he can give the bond. This is a bond to pay money; it is not a bond for faithful services or anything of that sort.

The CHAIRMAN. If there was not some security put up, in the meantime they might get rid of any property they had left and go out of business.

Senator GEORGE. That is in the discretion of the Commissioner. Of course, he might exact—and he probably would if he thought the interests of the Treasury would suffer—he might exact the security.

Senator HASTINGS. He does not have to?

Senator GEORGE. No.

Senator LA FOLLETTE. It is only in the case where the Commissioner thinks there is danger of the Treasury not collecting the tax. He is not compelled to do it. If the discretion is to be exercised, it seems to me you can also trust the officer exercising it to use his discretion with regard to whether he will require a bond or not, and I think it is fair to assume that he would only require it where he thought the interests of the Treasury were in jeopardy.

Senator COUZENS. Where the assets might be liquidated?

Mr. KENT. May I make an observation on that that I think might be of some value? This provision is similar to the one contained in section 272 with relation to the extension of time to pay other taxes. Under that section, also, the Commissioner has discretion to take a bond.

I have been rather intimately connected with the administrative matter for extensions of time under that section and where the condition of the taxpayer is such that it is impossible for him to obtain a bond we have accepted such security, other forms of security, as the nature of the taxpayer's situation would permit him to give; in other words, it has been that what we have tried to do is simply to be sure that the situation from the point of view of collecting will not be any worse at the end of the period of extension than it was at the beginning.

Senator HASTINGS. Mr. Chairman, I thought he was compelled to give the bond. I see now that it is a matter of discretion with the Commissioner.

Senator GEORGE. I think this period of 2 years might well be extended to 4 years, because it is still in the discretion of the Commissioner, and it gives him some leeway.

Senator COUZENS. I move that that be done.

The CHAIRMAN. Why can we not agree on 3 years?

Senator COUZENS. As long as it is in his discretion, why not leave it as a maximum of 4 years?

The CHAIRMAN. Mr. Kent, it requires a bond in double the amount—that is the present law?

Senator CONNALLY. It is discretionary.

The CHAIRMAN. Do you think we ought to have it double the amount?

Senator GEORGE. Not exceeding double the amount. That leaves it within his discretion to put it at less.

The CHAIRMAN. The amendment is to give him 4 years?

Senator CONNALLY. I second Senator George's motion to make it 4 years. It is discretionary, anyway.

Mr. KENT. On the income tax, we can grant an extension not to exceed 30 months.

Senator CONNALLY. Make it 3 years, then.

Senator COUZENS. Well, make it 3 years.

The CHAIRMAN. Is it agreeable to the committee to make it 3 instead of 2?

Senator GEORGE. I move that it be 3 years.

The CHAIRMAN. All in favor will say "Aye."

(The motion was adopted.)

Senator COUZENS. May I draw the witness's attention to the second line on page 13? Should that not be the amount determined by the Commissioner instead of the taxpayer?

Mr. TURNER. Of course, the amount which is due with the return is the amount shown on the return as the tax. If the Commissioner determines more to be due, that is a deficiency; and under this bill, the general provisions for extensions of time with respect to deficiencies would be applicable.

Senator COUZENS. Does that language cover the amount when the taxpayer determines the less amount of tax than is due? I did not understand why you should put this in there as "the taxpayer." I think it should be not the taxpayer, but also what the Commissioner determines.

Senator KING. It takes some time for the Commissioner to make an investigation, and to ascertain that a larger sum is due. There might be a hiatus of several months.

Senator BARKLEY. Why is it necessary to put in here these three words, "by the taxpayer"?

Mr. TURNER. If the committee thinks this same period can be allowed for the extension of deficiencies—

Senator BARKLEY (interposing). Why not leave out the words "by the taxpayer"?

Mr. TURNER. I would like to have a chance to check into the best way to say it.

Senator BARKLEY. As you suggest, Senator Couzens, that sounds as though it leaves it all up to the taxpayer. Of course, in making out his preliminary return, he fixes what he thinks is due. That is subject to approval by the Commissioner, and he may find there is some more due. I suppose this is intended simply to cover the preliminary return, and a taxpayer himself who in the first instance does determine what he owes.

Mr. TURNER. Yes; under this provision the extension provided for here would be applicable only to the amount of tax contained on the return, and deficiencies would be governed by the general provision. It would be possible to make it apply to both if the committee so thinks.

The CHAIRMAN. Look into it, Mr. Turner, and see how that should be worded.

Senator GEORGE. I think it should be applied both to the amount shown and the amount determined.

The CHAIRMAN. Without objection that will be agreed to. Now, section 505.

Mr. TURNER. Section 505 is the provision which makes the windfall tax applicable to any possessions. A similar provision was in the House bill. It has been redrafted generally to make it clearer that the windfall tax applies in a possession only when the excise

tax in question was made applicable there. As to the most of the excise taxes, the possessions are all like foreign countries.

The other change is substantial and provides that the windfall tax applicable in the possessions shall be collected by the Internal Revenue Department of those possessions, and they shall keep the proceeds. That seems to be a sound principle, because the processing taxes, to the extent that they apply in the possessions were turned over to those possessions, and also because our Federal Internal Revenue Bureau has no adequate machinery for collecting these taxes in the possessions.

The CHAIRMAN. Without objection that will be agreed to.

Now, let me ask you this. How much less revenue by virtue of that modification will be involved? We expected to get \$100,000,000, did we not, out of the windfall?

Mr. TURNEY. It was close to \$100,000,000; that was the estimate. The changes which would result in lost revenue are first, the offset for the losses during other parts of the year. I imagine we could give you some kind of an estimate on that. I am not prepared to do it now.

The CHAIRMAN. Well, the committee wanted just a rough estimate.

Mr. TURNEY. I could not even do that. I would have to turn that question over. There are several other changes which would affect the revenue, but not to any great extent.

The CHAIRMAN. Get us up some idea about it.

Senator GEORGE. I question whether the first change will seriously affect the revenue in any way.

The CHAIRMAN. This last amendment giving them 3 years is going to affect the immediate needs.

Mr. TURNEY. Yes; it would affect the amount collected in the first year.

Senator COUZENS. That is only optional, anyway.

Senator KING. I think that those who can pay, will pay, rather than be taxed the 6 percent in there, because if they have any financial standing, they can borrow the money from the banks at very much less. It would be the poor people.

The CHAIRMAN. The subcommittee has done a very good job on this. Thank you, Mr. Turney, very much.

Without objection, this amendment as amended will be agreed to.

Now, let us get to the refund proposition.

Senator BARKLEY. On the refund, the special committee has gone over that title and has made some revisions. Mr. Kent advises me that they have not got the amendments here yet. Are you going to have a meeting this afternoon?

The CHAIRMAN. Yes; we will.

Senator BARKLEY. They will be ready this afternoon. If it goes over until tomorrow, we can have them in mimeograph form in a complete new title like this, which is much more easily understood, but we are not ready to make the suggestion this morning, because the experts have not gotten the draft completed.

The CHAIRMAN. Let us take up this foreign-credit proposition and get it out of the way.

Mr. Parker, will you address yourself to that?

Mr. PARKER. There are a number of sections here dealing with foreign corporations. We have been over that ground once. Do you want to start from the beginning?

The CHAIRMAN. We want to get it straightened out this morning.

Senator KING. Let me ask one question. Mr. Parker, are you familiar with the testimony of Mr. Birnhauer, of Amsterdam, who made a statement before the Ways and Means Committee?

Mr. PARKER. Yes, sir.

The CHAIRMAN. He appeared before our committee also.

Senator KING. I was not here.

The CHAIRMAN. I think before we get into that, I should read a letter from the State Department on this foreign-credit matter. This need not go on the record.

(Off the record.)

Senator HASTINGS. Does not that foreign tax depend a good deal upon the general policy that you are going to adopt?

The CHAIRMAN. Yes; it is related to whatever rate we may agree upon.

Senator HASTINGS. Does it not also depend upon whether you are going to follow the general policy set down by the House, or whether you are going to do what has been suggested here in your last proposal? Let us ask Mr. Parker about it.

The CHAIRMAN. Mr. Parker, do you think you could handle this matter before knowing just what we are going to do with reference to corporate taxes?

Mr. PARKER. I do not think you can handle the complete situation until that question of policy is determined.

Mr. BEAMAN. I think that is subject to this modification, and I think Mr. Parker will agree with me. You cannot settle intelligently the foreign-corporation situation until you have settled the domestic corporation, but I see no reason why you cannot settle in advance, whether or not you are going to make the change in the taxation of the nonresident alien individuals as the House bill did. As far as I know, that has nothing whatsoever to do with the corporation except as it affects one narrow point about taxation of dividends. If that can be left over, it can be disposed of afterward.

But the general taxation of nonresident alien individuals can be settled independently of the other. Mr. Parker may differ with me, but that is the way it looks to me.

Mr. PARKER. I think that is correct.

(Off the record.)

The CHAIRMAN. Now, Mr. Parker, will you proceed?

Mr. PARKER. In France, the income tax is imposed on a schedular basis and will have a different rate on the income from salaries and compensation for services, than what they do on income from investments, for instance. I am not acquainted with all of the details, but I believe they have as many as four or five different schedules for the levying of the assessment of their income taxes, so their rates on nonresident aliens may vary somewhat in proportion to the rates on the French citizens, depending upon the source from which the income is derived. It runs as high as 18 percent in some instances.

The CHAIRMAN. Mr. Parker, will you give to the committee, first, just a picture of what is proposed to be done?

Senator KING. May I ask one question? I suppose it is conceded that both in Canada and in Paris and in London particularly, and perhaps in Berlin, on exchanges and the bourses of those countries, American securities are bought and sold and American stocks and bonds are largely dealt in?

Mr. PARKER. That is correct.

Senator KING. And foreigners likewise make investments in the United States?

Mr. PARKER. That is right.

Senator KING. Buying here over the counter and through the stock exchange, and that there are some foreign corporations located here in New York and elsewhere, and there are foreigners who are non-residents who do business not through a corporation here, that is, not through their own corporation, but other organizations. I just want to get that fact noted.

Senator WALSH. Have we many foreign corporations paying taxes?

Mr. PARKER. There is a fairly substantial number. I cannot remember offhand; I think it is about 2,000.

Senator LA FOLLETTE. Mr. Parker, I suggest that you confine yourself to the nonresident alien individual now, because I think it is pretty generally conceded that we cannot determine how we are going to treat foreign corporations until we know what we are going to do with the domestic corporations. Let us take up this alien individual.

Mr. PARKER. Very well. Under existing law, the nonresident alien individual is taxed the same as an American citizen except he is disallowed the exemption, such as credit for dependents, and so forth, but he comes under the normal tax and he comes under the surtax at least theoretically, and he is supposed to file a return exactly the same as an American citizen. The tax on him, therefore, is whatever tax is provided for. At present, of course, it is in the 1934 act with its 4-percent normal rate and the surtaxes going to 60.

Senator HASTINGS. He does not include in that any income except what he gets in this country.

Mr. PARKER. The income upon which he is taxable under our system is that derived from sources within the United States under section 119.

Senator HASTINGS. If he has \$100,000 which he gets from his income at home, he, of course, does not include that.

Mr. PARKER. That is not included in his income. You just take the income from sources within the United States.

Senator KING. Just like Americans who deal in London or elsewhere. We do not include the profit we have made there in Canada or elsewhere.

Mr. PARKER. That is right. Of course, it is obvious that you are getting small sums of money in the United States and we have no really effective method of making them file returns, so that we have a system in the existing law which provides for a deduction of the tax at the source; that is, a person paying a foreigner in this country withholds a certain percentage of the tax and remits that to the Government—leaving out of account this tax-free Government-bond proposition, which is an exception. The general theory is this under existing law, you withhold the normal tax of 4 percent

on interest, rents, compensation, and other fixed and determinable incomes, as stated in the law. We do not withhold on dividends.

There is no question in my mind but that we have been losing a considerable amount of money due to the failure of our law to require withholding on dividends. Of course, the theory of not withholding on dividends was because they were not subject to normal tax either in the hands of our own citizens or of the foreigner.

Senator KING. I understood you to say that you withhold the normal tax?

Mr. PARKER. No; we do not withhold on dividends. We withhold on interest, rents, royalties, and such things as that.

Senator BLACK. Do you mean if anyone pays anything to a foreigner, he is supposed to withhold—

Mr. PARKER (interposing). Four percent.

Senator BLACK. For wages or salary or anything like that?

Mr. PARKER. That is right.

Senator BLACK. Is that done very much?

Mr. PARKER. Oh, yes. That is done on that type of income. I suppose there is some escape. I am talking about the nonresident alien solely. I am not talking about the resident alien.

Senator CONNALLY. The resident alien pays just like anybody else.

Mr. PARKER. He pays just the same as a citizen of the United States.

Senator KING. Doesn't that need a little clarification? The reason I make that suggestion is that here only a few days ago some man brought to my attention the fact that he was representing an English or a French house—I have forgotten which—and he lived in a foreign country and would come over just once or twice a year and take orders, and it required him to stay here about 2 weeks, and they required him to make a statement as to what his share of an annual salary for that 2 weeks would be and what his share of the commissions would be that he would derive, and they wanted to tax him on that and compelled him to make a return.

Mr. PARKER. Of course, we could not compel the employer living in London to withhold the tax, but we say, "Here, if you have made any income in the United States, you should pay." I think myself it is going too far. No other country attempts to do such a thing.

Senator KING. If you should go to England to sell Ford automobiles and would be there a couple of weeks selling them, applying that principle you had to return in Great Britain the salary you had and the commissions that you had made.

Mr. PARKER. You would not pay in Great Britain unless you had been there 3 months.

Senator KING. I mean, applying the same principle that was applied to the person that made the statement to me.

Senator HASTINGS. Just to illustrate that point: That was a small corporation that employed an expert living in Canada and they paid him a final fee of \$6,000. They did not know anything about this law. Two or three years afterward when their income-tax return was examined, they had to pay on this particular person's share of tax that he ought to have paid, because they, under the law, were supposed to have withheld it.

Mr. PARKER. We make the withholding agent responsible for the tax.

Senator HASTINGS. They could not get it back from him because he had gone.

Mr. KENT. There is a provision in the present law, section 19, defining income from sources within the United States, which provides that compensation for labor or services performed within the United States shall be deemed income from sources within the United States. I think some of the cases to which reference has been made are simply absurd. I think it is really beneath the dignity of this Government to hold a commercial representative who has been here negotiating commercial contracts for 3 or 4 weeks, up at the port in order to squeeze a few dollars out of him, but our agents do it. We cannot very well tell them in Washington that they are violating the law in doing so, and it is a very difficult situation to deal with.

Senator KING. In a case I referred to, the man was here 2 weeks, and they asked him to make a return and pay, and he was here trying to find a market for our goods. He wanted to buy goods here, and he wanted to sell goods in return.

Mr. KENT. And on the other hand, one thing that makes the situation rather difficult to deal with is this: You may have some English pugilist or German pugilist or theatrical star coming over here and being here for 2 or 3 months and making \$100,000 or \$200,000 out of their activities in this country, and the feeling there is that we ought to get some tax out of it. So it is rather difficult to frame an amendment even which will draw the line of distinction and let out the cases that you want to exclude without letting out some that you want to include.

Senator KING. Joe Louis is going over to Germany soon to fight, and if he gets a million dollars there they will tax him.

Mr. KENT. On that same principle, on page 180, section 211, is the new plan which states the tax on non-resident alien individuals. The nonresident alien individuals are divided into two classes. The first class is treated in subsection (a) and the second class in (b). The first class are those that have no United States business or office; that is, if they are not carrying on business in the United States, and have no office or place of business therein.

Senator KING. Are you speaking of the individuals now?

Mr. KENT. Yes; that is the heading.

The CHAIRMAN. How do you collect that 10 percent?

Mr. PARKER. We put 10 percent on all of his income, and it includes dividends as well as interest, rents, salaries, wages, premiums, annuities, compensations, and so forth. The tax is 10 percent. The man collecting that tax is taken care of in section 143, and the important part of that is subdivision (b) on page 145 [reading]:

All persons in whatsoever capacity acting, having the control, receipt, custody, disposal, or payment of interest—

I am skipping a part of it, but that will give you the general idea—pay to persons not engaged in business in the United States and not having an office or place of business therein, must withhold on dividends, rents, salaries, wages, premiums, annuities—

and so forth. That 10 percent is withheld by the person in this country who makes the payment to the nonresident alien individual.

Senator KING. I should like to say—this is off the record.

(Off the record.)

Mr. PARKER. The other class are the nonresident aliens who are engaged in a trade or business in the United States that have a place of business or office in the United States. In other words, if an Englishman has an office in New York City and is carrying on an importing business, then he is taxed not this 10 percent, but he is taxed just like an American citizen with the exception that these exemptions which I pointed out and which are rather unimportant in the larger incomes are excluded. Or, he is also taxed in the same manner if he has an office or place of business in the United States.

Senator BLACK. What is the line of distinction between the illustration that Senator King gave? Here is a teacher who teaches for a year. Suppose she came over here and taught 2 weeks, would she then be considered a nonresident alien securing an income here, or would she come under the other basis of one engaged in business? I do not yet get the line of distinction.

Mr. PARKER. I believe if the foreigner came over and stayed 2 weeks, that there should be a withholding there.

The CHAIRMAN. Suppose some Frenchman came over here and stayed here for 6 months and made \$500 a month, whether he was in Hollywood or what not, where would he pay his income tax?

Mr. PARKER. He would pay his tax right here, and he would have to have an income-tax clearance receipt before he left the country.

The CHAIRMAN. He would also have to pay an income tax in France, would he not?

Mr. PARKER. Yes; he would.

The CHAIRMAN. Suppose an American went over doing some kind of a gymnastic act in England or France or Germany and made \$500 a month; to whom would he pay the tax?

Mr. PARKER. He would pay the tax to England, but then when he was taxed here he would get a tax credit up to the amount of the rate of the United States tax.

The CHAIRMAN. He would have to pay here, but there would be a credit on it for the amount that he paid in the other country?

Mr. PARKER. That is right.

The CHAIRMAN. What rate do these people who are doing business in this country or have a principal office in this country pay under this (b)?

Mr. PARKER. They pay just the same rate as an American citizen would pay with whom they may be competing. Exactly the same on the income derived from sources within the United States.

The CHAIRMAN. It says "without regard to the provisions of subsection (a)."

Mr. PARKER. Subsection (a) is a flat 10 percent, and when you say taxed without regard to that it means you go over to the general provisions of the bill with regard to tax on individuals.

The CHAIRMAN. Of course, we have kept this withholding rate in the past because of the comity between countries.

Mr. PARKER. I do not think it has been so much on that account.

The CHAIRMAN. They could retaliate, could they not?

Mr. PARKER. They could, but most of the important foreign countries are withholding at a greater rate than that now on our citizens. Our theory, I think, was that we would withhold at the normal rate of tax. We taxed the foreigner just the same as our citizens paid, our withholding rate was the normal rate on the assumption that

they would have to pay that anyway, and then they might have to pay more. If you collect all of that income together—

The CHAIRMAN (interposing). That is 4 percent?

Mr. PARKER. Four percent under the present law.

The CHAIRMAN. You propose to raise it to 10 percent?

Mr. PARKER. Ten percent flat, but they get some compensating advantages. One of them—and perhaps the most important—is that the House bill proposed to exempt the foreigner from capital gains because the Treasury has found it practically impossible of collection, practically impossible to trace the transactions and impossible to get the capital-gains tax in any substantial number of cases, and that same thing is also true of the hedging transactions, which I think you will remember in the last act there was considerable complaint about before the committee. I forget whether it was the 1935 act or the 1934 act, but they claimed it was forcing foreigners to deal, for instance, in cotton on the Liverpool market and instead of dealing on the New York market.

The CHAIRMAN. Is it your opinion that the provisions with reference to withholding 10 percent on these foreign people and withholding that at the source, is a fair provision?

Mr. PARKER. I think it is not so much a question of being fair as it is a question of getting a reasonable revenue under the arbitrary rule which will work and which will bring us in more revenue, but will not be out of line on the foreigner.

The CHAIRMAN. How much does the Treasury estimate it will get by virtue of this increase?

Mr. PARKER. I believe the Treasury estimated only about \$4,000,000 additional from our new foreign tax system, but personally I feel that estimate is very low.

Senator HASTINGS. What do you think about putting the foreigner in the same position as the American citizen if he filed an income-tax return, but if he failed to file one, then place him under the 10 per cent?

Senator LA FOLLETTE. The difficulty with that, Senator, would be that the person or the corporation responsible for withholding at the source would not know whether he had done it or not.

Senator HASTINGS. Let him withhold the 10 percent. Let that provision apply of withholding the 10 percent, but give the foreigner who comes in and files a return—put him on the same basis as the American citizen.

Mr. PARKER. I think that would be objectionable for this reason, Senator. It creates an option. If a man had \$100,000 income in the United States, he would pay the 10 percent or \$10,000 instead of filing a return, because if he filed a return he would pay \$30,000. On the other hand, a foreigner that only had \$2,000 of income, he would file the return because he would only pay 4 percent or \$80 on it instead of paying \$200.

Senator HASTINGS. I do not believe the amount is sufficient to warrant criticism of this Government along that line, myself.

The CHAIRMAN. They say that we are getting less now than these other countries, as a general rule.

Senator KING. I did not hear the testimony of Mr. Cohen and others, and if I may be pardoned, Mr. Chairman, for my own information, Mr. Cohen of New York, representing Canadian investors, in

his statement pointed out that the Canada withholding tax is only 5 percent, and that a heavier American withholding tax will result in actual loss of revenue to the United States. Mr. Hansard, representing the Amsterdam Stock Exchange in his statement before the committee stated that there was no scientific basis for the 10-percent rate, and that the proposed rate of a flat tax of 10 percent on the gross income on foreigners will in all probability have a most detrimental effect upon foreign investors in the United States. The withholding tax plan in the case of the nonresident alien income in the pending bill is an improved step in the right direction, but the withholding rate should be moderate; furthermore, due to the fact that the withholding rate is applied to the same kind of items of annual or periodical income, the withholding flat rate should be uniform with respect to both individuals and corporations.

The CHAIRMAN. It was pointed out there, Senator King, that that gentlemen who represented the Amsterdam people, that before the House Ways and Means Committee he said that he thought a 10-percent rate was fair. That is my recollection of it.

Senator KING. That was Dr. Brenhauer. But Mr. Cohen said that in Canada they only imposed a tax of 5 percent.

Mr. PARKER. That is true. It seems to me if you go below 10 percent and go to 5 percent, that that might be fair enough in some instances, but if you did that, that you would have to put some limitation on. For instance, if a foreigner got over \$20,000 income, then he must file a return, and then you would have to make a third classification here of foreigners and make those that got over \$20,000 subject to the tax, because when you go that low we are giving too much relief. There are some rather large taxpayers that pay a very considerable tax, up around \$100,000 or \$200,000. The 10 percent is going to cut their tax in half, but to cut it down to a quarter, cut it down 75 percent, it seems to be going too far, even though we would get a little more revenue on the aggregate. Don't you feel that way, Mr. Kent?

Mr. KENT. Yes. I believe we can say this much, that in essence this proposal for a change in our system of taxing nonresident aliens is substantially similar to the system which is in effect in the more important foreign countries. How they can fairly criticize the United States Government for shifting over to substantially the same principles as they are following in the collection of taxes from nonresident alien individuals, is a little difficult for me to see.

Senator KING. Could we not differentiate between contiguous countries, between Canada and Mexico from those that are not contiguous?

Mr. PARKER. That would be possible, although the information comes to me rather indirectly that the State Department would be rather apprehensive of giving a better rate to contiguous countries. Canada, of course, is in this position—Canada has a very real economic reason for keeping this withholding tax low, because Canada is a developing country. It is trying to attract capital from other countries, and to develop its natural resources, and I doubt very much whether Canada would be inclined to retaliate against the United States.

If I may have this off the record—

The CHAIRMAN. The reporter need not take this.

(Off the record.)

Senator KING. Going over 6 or 8 or 9 years, or at least under the present law as long as it has been operating both as to foreign corporations and individuals, by and large have the laws worked fairly satisfactorily and justly?

Mr. PARKER. I should say that they have not. That the existing rate is necessarily discriminatory in its operation, because we have to depend to such a large extent upon the honesty and the voluntary cooperation of the nonresident alien in collecting the tax, and that has been particularly true with respect to the capital gains provisions of the statute. A Frenchman or an Englishman signs an order to his broker, a New York broker, to buy some stock for him on the New York Stock Exchange. Later on he sells it and he makes a gain out of it. It is not the sort of a situation where it is practicable to withhold the tax and we have an enormous amount of difficulty. It has upset business relationships, it has thrown our brokers into a panic whenever we have tried to make a real effort to collect those taxes and we got them in a few cases, but in scores or hundreds or thousands of other cases we do not get them at all. And I believe that has been the experience of other countries.

Great Britain takes 22.5 percent of the dividends of a British corporation going to American citizens. It amounts to that. It allows no refund, no readjustment of any sort, although it does allow such refunds and readjustments in the case of its own nationals.

The CHAIRMAN. Let us get this out of the way so that we won't have to discuss it this afternoon again. Without objection, you will draw an amendment then, and it is agreed to along the lines of 10-percent withholding on these foreigners, and that they be given credit, foreigners of contiguous countries, on these dependent provisions, and that the rate that we adopt on these corporations shall apply.

Mr. BEAMAN. I do not understand that, Senator.

The CHAIRMAN. If foreign people are doing business in this country they should be applied the same yardstick that Americans are.

Mr. BEAMAN. Just the residents?

The CHAIRMAN. I am just talking about the residents. If they have a principal place of business and all of that. That was the idea in the bill.

Mr. BEAMAN. Then you are taking the House bill with two changes; you are giving the residents of contiguous countries credit for dependents, which the House bill denies them.

The CHAIRMAN. That is right.

Mr. BEAMAN. And you are making the rate of withholding—on the tax too, or just withholding? Are you going to tax this Canadian nonresident 10 percent and withhold it for him?

Senator KING. I am not ready to vote on this.

The CHAIRMAN. Then we will take it up this afternoon. We will meet in the District of Columbia room in the Capitol.

(Whereupon, at 12 o'clock noon, a recess was taken until 2 p. m. of the same day.)

AFTER RECESS

(The hearing was resumed at 2 p. m., in the District of Columbia Committee Room, Capitol Building.)

The CHAIRMAN. Mr. Parker, will you continue about this foreign credit matter?

Mr. PARKER. In the 1924 act, we had a normal tax of 4 percent, and 8 percent. When it came to withholding on a resident alien, we withheld at 8 percent, except in the case of residents of contiguous countries, and there it was 4 percent that was withheld.

The CHAIRMAN. What would be your reaction to 10 percent being withheld except residents of contiguous countries, and in that case it be 5 percent?

Mr. PARKER. I think we can do it, if you want to do it. It is a question of policy.

The CHAIRMAN. The only fear that I have about it is that you get criticism of discrimination.

Mr. PARKER. There is one practical reason for doing it, and it is a selfish reason. Under the present state of the law, we would get more tax if we continued it at 5 percent instead of 10 with Canada, if Canada should retaliate and put on a 10 percent rate. The reason for it is this, that our residents receive from Canada something like four times the amount of income that Canadians receive from our country. We have a foreign tax credit, and of course the more they tax our people, that reduces our tax on the income they get from that foreign source, and since the volume is greater coming into the United States than going out, you would probably lose money if they retaliate. Of course if they leave their rate on at 5 percent, which they have now, that is different. They have a 5 percent rate now.

Senator KING. For how long a time did we have the 4 percent discriminating, if you call it discrimination, between contiguous countries and other countries? Wasn't it for many years?

Mr. PARKER. We were not discriminating.

Senator KING. I do not call it discriminating, but a difference.

Mr. PARKER. Since the 1921 act. Of course, when we had the 1934 act and went back to a 4 percent flat rate, then we did not have any difference in the rate, and that distinction was no longer made.

Senator KING. Between 1921 and up until the time we went back to that other rate, so far as you know was there any protest from any foreign country?

Mr. PARKER. I have never heard of any.

Senator KING. You had not heard of any?

The CHAIRMAN. How much would this credit to dependents amount to?

Senator LA FOLLETTE. You would not do both, would you?

Senator KING. We have done both. They are getting that now.

The CHAIRMAN. That is in the present law, is it not?

Senator KING. Yes.

Mr. PARKER. That is right.

Senator LA FOLLETTE. If you give them a half rate, I don't know why you should give them a credit for dependents.

The CHAIRMAN. In measure of percentage, how does that compare with just giving them a credit for dependents? Not giving them both?

Senator COUZENS. What is the objection to letting the law stand where it is?

Senator LA FOLLETTE. You mean so far as taxing these nonresident aliens?

Senator COUZENS. Yes.

Senator LA FOLLETTE. It is this. This is not on the record—

(Discussion off the record.)

Mr. PARKER. The theory of our existing law is to tax a foreigner practically the same as the American resident except that we give them a \$1,000 exemption and no credit for dependents, and no marriage status except in the case of contiguous countries, where we give them credit for dependents, but not for marriage status.

Under this bill, it is different. We have a tax here of 10 percent or 5 percent, if you please, but I do not think that when we send dividends to a man or interest to a man with this flat tax, that he should get any exemptions at all. I do not think we should bother with deductions.

Senator LA FOLLETTE. I do not, either.

Mr. PARKER. But I think that this \$1,000 will apply to any earnings that he makes in the United States in services or in wages that come from the United States, to have it apply to that part of his income.

Senator KING. Do we have any considerable number of American citizens who are working in Canada?

Mr. PARKER. Yes; we have a considerable number. I think Senator Couzens would know more about that in Detroit, of the men in the lumber regions. I know that we have a great many in New York that come down for certain seasons of the year.

Senator COUZENS. We have a great many more high-priced executives living in America and working in Canada than the other way around. They have no high-priced executives working in America and living in Canada.

Senator KING. If we have any considerable number of Americans working in Canada, they allow them an exemption of \$2,000 and \$200 for dependents. So it is as broad as it is long. Senator Couzens, haven't we, by and large, in lumber and in aluminum and in other activities there, nearly as many American working people as Canada has over here in Detroit?

Senator COUZENS. No. There are many more Canadians in American than there are Americans in Canada.

Mr. PARKER. We have divided nonresident aliens into two classes, the first of which are not engaged in business in the United States and do not have a place of business or office herein, and the second of which is composed of those individuals which are engaged in trade or business in the United States or do have an office or place of business therein. It seems to me that this thousand dollars in the case of the ordinary foreigner and the thousand dollars plus the personal exemptions in the case of contiguous countries should, of course, be confined to that class of nonresident individuals; that is, they are engaged in business here. They come over here for a short time. They have not become residents here. But those are the ones that

ought to have the exemption. We did not have that distinction before; we did not divide the nonresident into two classes. That is all there is to it then. It is just confined to that one class. It won't have any effect on wealthy people in Canada who may have some investments here. They are not coming here for work, but it will let out your loggers and the people, perhaps, working in the automobile factories up around there.

Senator COUZENS. They do not get enough income to worry about taxes.

Mr. PARKER. But, Senator, if we do not put that in, the employer will have to withhold at the source.

The CHAIRMAN. What page is that, Mr. Parker?

Mr. PARKER. Page 146.

The CHAIRMAN. Yes.

Senator KING. Mr. Chairman, I would like Mr. Kent's view on this matter if he cares to express it, as a matter of policy. If he is willing to divorce himself from the position of expert and speak as a policy man.

The CHAIRMAN. Mr. Kent has stepped out for a moment.

Mr. PARKER. You see, in 146, this withholding of these payments of wages and so forth is required with nonresident alien individuals, whether they are engaged in business here or whether they are not engaged in business here. That is rather serious. If a man has a job here for 2 or 3 months and you have to withhold on him, if we do not have that exemption, of course he would be caught with a pretty high tax.

Senator KING. I have made up my mind with respect to the question of exemptions. It bothered me. But as to the 5-percent tax, we are getting four times as much from Canada from our investments there as the Canadians are getting from us, so that if we should make it 10 percent and they should raise it to 10 percent, we would lose a good deal of money.

Mr. PARKER. In other words, if our citizens get \$200,000,000 annually from Canada, and they tax that at present at 5 percent, that is of course \$10,000,000. If they tax at 10 percent, that would be \$20,000,000. That additional \$10,000,000 would be taken off the tax bill. Our citizens would put that into their income, and they would compute the tax, and then we give them a tax credit which would take this tax right off again. Therefore, we lose on what goes out.

The CHAIRMAN. I would be fearful of the 10 and 5 except for the present law they have there.

Mr. PARKER. They have not got it in the present law, but they did have that up to 1934. We came back to one normal rate of 4 percent, so we did not make any differential.

The CHAIRMAN. Why would not 10 and 5 be right?

Mr. PARKER. Five percent is the same as Canada is withholding from us.

The CHAIRMAN. You say other countries are withholding much more than that?

Mr. PARKER. To Germany we can say, "You withhold at 20 percent", but Canada only withholds 5 percent.

The CHAIRMAN. How much does England withhold?

Mr. PARKER. You might say they withhold at 22.5 percent.

Senator LA FOLLETTE. That is the practical effect of it.

The CHAIRMAN. Why can we not agree on 10 and 5? Ten percent for all countries except contiguous countries, and make that 5 percent?

Senator KING. I favor that.

The CHAIRMAN. Is there any objection to that?

(Discussion off the record.)

Mr. BEAMAN. Do you want to keep the House bill, tax them 10 percent plus on all income from these specified sources, and withhold the 10 percent except in the case of residents of contiguous countries, where it should be 5 instead of 10?

The CHAIRMAN. That is what we want. Is there any objection to that arrangement with reference to that? If not, that will be agreed to.

And the other class where they are doing business in this country, they are going to be taxed the same as Americans, so we cannot fix that rate definitely until we have agreed on it later. Is that right?

Mr. BEAMAN. What are you going to withhold then?

The CHAIRMAN. What is withheld on those people in this bill?

Mr. BEAMAN. Ten percent.

The CHAIRMAN. If they have a place of business here and they are taxed so much, why can you not collect it all?

Mr. BEAMAN. The present law withholds, and the House bill does.

The CHAIRMAN. How much does the present law withhold?

Mr. BEAMAN. Four percent normal tax. But this House bill is entirely different. It takes up the normal tax and surtax.

The CHAIRMAN. What does the House bill withhold?

Mr. BEAMAN. Ten percent.

Senator KING. What was it from 1921 to 1934?

Mr. BEAMAN. I don't remember. When they had 4 percent on a citizen resident, they had 6 percent nonresident, except to contiguous countries, and applied a different rate to salaries, and something on top of something, and it was very complicated.

(Discussion off the record.)

Mr. BEAMAN. I understand then that the rate of withholding on all residents of Canada and Mexico is 5 percent, no matter whether they are taxable under the flat tax or whether they are under the normal and surtax?

The CHAIRMAN. What is your suggestion, Mr. Parker?

Mr. PARKER. I just want to point out one more thing that I think helps. You may wonder why if a man comes over from Canada and works in a logging camp for 3 weeks and gets \$30 a week, or \$90, that we would withhold 5 percent or 10 percent on him and have the employer take that out of his salary. We fixed that so that won't have to be done. We have this \$1,000 exemption for these people that are working here engaged in business here, so we put this in on page 146 [reading]:

Under regulations prescribed by the Commissioner with the approval of the Secretary, may be exempted from such deduction and withholding the compensation for personal services of nonresident alien individuals who enter and leave the United States at frequent intervals.

So that may help there if the Commissioner wishes to make regulations.

The CHAIRMAN. Why should favoritism be given to people who live without the United States and who are working on jobs in the United States?

Mr. PARKER. We are not giving them any favoritism; we are taxing them the same as the American citizen, and a little bit more. It is simply to avoid the confusion of taking 5 percent or 10 percent off of a man's salary, and then have him make a return, and then have to give it back to him. Suppose a man goes over every day, for instance across the river into Detroit in an automobile factory, and his total salary is \$1,000 a year. He is employed. Why make his employer withhold \$50 on him when he knows very well that he is going to get a refund of that amount. We will have to come in at the end of the year to have him get his \$50 back. It is just unnecessary, because the Commissioner, for instance, could provide if the total annual salary of a man is not over \$1,000, I think he could be relieved to the point where he would pay more than \$1,000 a year.

Senator CLARK. In the case you state, Mr. Parker, a man coming over and working in an automobile factory in Detroit—there are a large number of unemployed in Detroit. If the employer is put to some little trouble about the matter of employing alien employees, it might have the effect of more or less encouraging him to employ American citizens, might it not?

Mr. PARKER. It might, but I have rather the impression, Senator, that there are more of our people that go over to Canada, or almost as many that go over to Canada to work as there are Canadians coming over here, so it is just reciprocity. Perhaps Canada is giving a great many of our citizens work to do.

Senator CLARK. If that is true, that answers my argument.

Senator COUZENS. Windsor is the only place that I know about. There are not as many going to Canada as there are coming over from Canada into the United States. There are more high priced executives go from America to Canada operating the Canadian plants, and they have none coming from Canada in here operating American plants.

The CHAIRMAN. Are we agreed on this, that it is going to be 5 and 10, 5 percent withheld on those nonresidents in contiguous countries, and 10 percent on others?

Senator KING. Mr. Kent, are you familiar with this proposition and how it worked out under the 1921 to 1934 act, where there was a discrimination—if that is the proper term—or at any rate where the tax imposed at the source by Canada was the same as that which we imposed, because we have had more coming in that was going out. Did you have any trouble over that? Was there any protest made by other countries because these contiguous countries had a little advantage?

Mr. KENT. I never heard of any.

Senator KING. Was there any difficulty in working it out?

Mr. KENT. No.

Senator KING. No administrative difficulties?

Mr. KENT. No.

Senator KING. Were there any administrative difficulties in dealing with the workmen who were living in Canada and who came across the line and would go back at night or at the end of the week, and a lot of Americans went across the line?

Mr. KENT. No more difficulties than administering any other provision.

Senator KING. In view of the fact that we sent a large number of high-priced executives there and they should withhold at the source based upon high-priced salaries, do you think that we would gain more or lose more in balancing the accounts between employees working in the United States and those working in Canada?

Mr. KENT. I think this is undoubtedly true, that there is more American income coming out of Canada than there is Canadian income going out of the United States. I do not know just what the exact figures are, but the difference is considerable. Of course, I do not know whether there would be any incentive if you had a preferred rate in favor of Canadians, for nationals of other countries who have their securities held by Canadians, and thereby get an advantage on the lower tax rate. There is always that possibility if you have a difference in the rate structure.

Senator KING. But we had a difference in the rate structure prior to 1934. Did you have any of that?

Mr. KENT. Not to any extent that I recall.

The CHAIRMAN. Without objection that will be agreed to by the Committee, the 5 and the 10 percent, and the rate will be fixed later on those that are doing business here.

Mr. BEAMAN. Just a moment, Senator. Did you decide under the present law a nonresident alien individual has an exemption of a thousand dollars whether married or single, and he has no credit for dependents unless he is a resident of Canada or Mexico? Is that what you want? The House bill changes that. They took away the dependents and took the personal exemption to apply only to compensation for personal services.

The CHAIRMAN. I do not think these people in foreign countries should have any further exception. Just leave it to the difference between 10 and 5 and leave dependents out.

Senator KING. Canada allows a married man an exemption of \$2,000 and a credit of \$200 for children, to our citizens.

Mr. KENT. May I say that my attention was recently called to a provision in the Canadian law which contains a possibility of retaliation if this credit for dependents is taken out of the act?

Senator KING. Because they give us \$200 there.

Mr. KENT. I think they were somewhat concerned about that up there. As a matter of fact, they seemed to me more concerned about that than they did about the 10 percent rate.

The CHAIRMAN. What do you think ought to be done about that, Mr. Kent?

Mr. KENT. I think myself that the present law might very well be continued in effect. The present law gives Canadians and Mexicans a \$1,000 personal exemption and the additional for dependents.

Mr. BEAMAN. It gives all nonresidents \$1,000.

The CHAIRMAN. In other words, the nonresidents of all countries have the same privileges that Canada and Mexico have?

Mr. BEAMAN. You are talking about credits for dependents. Let us stick to that alone. Under the present law, the nonresident alien does not get a credit for dependents except the residents of Canada and Mexico, who do get it. The House bill kicked it out, so that

no nonresident alien gets any exemption for dependents whether he lives in Canada or wherever he lives.

The CHAIRMAN. With respect to Canada and Mexico, they are on the same footing with every other country.

Mr. PARKER. Under existing law, this \$1,000 is allowed to all men, no matter whether they come from Germany, France, Italy, or anywhere. Contiguous countries get credit for dependents in addition. That applies to whether they work in the United States or whether they never saw the United States and are just clipping coupons up in Canada, and from those that are just clippings coupons up in Canada and are not engaged in trade or business in the United States, we are taking \$1,000 away, and we are taking the credit for dependents away under the structure of this bill. So we are taking all of that away from them, and I think that is the biggest part from the revenue standpoint, and the only thing we are retaining here is a \$1,000 exemption and the credit for the dependents for those that are engaged in trade or business here or have an office and place of business. Is that not right, Mr. Beaman?

(Discussion off the record.)

Mr. PARKER. Under the existing law, if a banker in Canada gets \$1,000 interest from the United States, they will withhold on it under existing law unless he files an exemption certificate or he can come in and get a refund on that tax which is withheld, because there is an exemption of \$1,000. I do not think you ought to continue that exemption. I think that this \$1,000 and this credit for dependents in the case of contiguous countries should be confined to those that are doing business here, or at least have an office and place of business in this country.

Mr. BEAMAN. Suppose they are working here?

Mr. PARKER. If they are working here they are engaged in business here, I assume.

The CHAIRMAN. Let us settle this proposition. We have discussed it long enough. Let us get down to other matters. We had settled on the proposition of making a differential of 10 and 5.

Mr. PARKER. I think so, but on this other thing I feel rather strongly that just because a man has \$10 income from the United States and we turn around and give him a refund because he got less than a thousand dollars from the United States and he has never been to the United States—

The CHAIRMAN (interposing). I do not think you ought to do that. Is that in this bill?

Mr. PARKER. No; but I wish the committee would take an action here than would produce that result.

Senator KING. Let me see if I understand. There are two men living in Canada; one comes across and works and goes home at the end of the week or at the end of the month. The other just has his business in Canada, and he gets \$1,000 interest represented by coupons. You think that he ought not to get an exemption of \$1,000, whereas the man that crosses the line and working here ought to get it?

Mr. PARKER. Yes.

Senator KING. I agree with you.

The CHAIRMAN. Without objection, draw the amendment carrying out that idea. Is there anything else on this matter? Do you understand now what we are after?

Mr. BEAMAN. Mr. Parker does, and that is all right.

Senator BARKLEY. Mr. Chairman, I think we will have our mimeograph revision of title IV in a few minutes. It is on the way up, and we will be ready a little later in the afternoon.

The CHAIRMAN. We have these estimates here, and there is no use taking them up until all of the members are here. Is there any minor matter that we might take up? Is the subcommittee on that insurance matter ready to report?

Senator LONERGAN. We have a report on the one item but not on the second, because they are preparing an amendment.

The CHAIRMAN. Will you proceed, Senator Lonergan?

Senator LONERGAN. The amendment is [reading]:

SEC. 401 (c) of the Revenue Act of 1932, as amended, is amended to read as follows:

"(c) For the purposes of this section, the value of the net estate shall be determined as provided in Title III of the Revenue Act of 1926, as amended, except that (1) in lieu of the exemption of \$100,000 provided in section 303 (a) (4) of such act, the exemption shall be \$40,000—

That is the present law—

and (2) there shall be deducted from the value of the net estate as thus determined, the proceeds of life insurance policies payable to (and received by) the Treasurer of the United States in trust for the payment of estate, inheritance, succession, legacy, or other death duties levied by the United States against or with respect to the estate of the decedent, exclusive of any excess over the amount of such taxes, which excess shall be accounted for (without interest) to the executor or administrator of the decedent for the benefit of the persons entitled thereto; provided, however, that the proceeds of policies on which the premium-paying period is less than 10 years shall not be deductible and that, in any event, the amount deductible as aforesaid shall not exceed \$1,000,000."

You remember, I think it was Mr. Hull appeared before the committee on this, and of course, it merely provides in substance that a man may have a policy issued on his life payable to the Treasurer of the United States for a given sum for the purpose of paying the death taxes on his estate. The policy, we will say, is \$400,000, and the taxes amount to \$310,000, and that is the sum that the United States Government will get. They will get it immediately.

Up in my section of the country it would require, in most cases, the liquidation of a plant, and that would mean to put it under the hammer. Most of these businesses sell for about 20 cents on the dollar, and it would take probably 2 or 3 or 4 or 5 years to even get the 20 cents on the dollar.

I think it is a meritorious proposal. It means quick and sure money to the United States Government without any doubt about it. I think that the exemption ought to be given when the taxpayer makes the sacrifice of raising the money to pay the premium, that that is the sum of money that he pays, and that is the tax that he pays, and he is displaying good citizenship and making it possible for quick and full payment to the United States Government.

I think it is meritorious and I believe it ought to be passed.

Senator CONNALLY. You do not take that out of the amount of the tax, but you deduct that from the net value of the estate?

Senator LONERGAN. Yes; that is the idea. Now, the Government gets the money immediately.

The CHAIRMAN. Let us have an illustration, Senator Lonergan. Suppose you had a man that was worth roughly \$10,000,000. He takes out an insurance policy to see that his estate taxes are paid.

Senator LONERGAN. That is right.

The CHAIRMAN. Is there any limitation to the amount that he shall take?

Senator LONERGAN. The limitation would be \$1,000,000.

The CHAIRMAN. That is the limit?

Senator LONERGAN. Yes, sir.

The CHAIRMAN. In paying these insurance premiums, is that a deductible item in his income tax?

Senator LONERGAN. No.

Senator CONNALLY. He would not pay on \$10,000,000. He would pay on \$9,000,000, and that policy would come off the tax.

The CHAIRMAN. That would reduce the tax considerably, would it not? If you reduce it from \$10,000,000 that the estate was worth, and take off \$1,000,000 for this insurance policy, reducing it to that amount, it would reduce the taxes considerably.

Senator LONERGAN. That would happen probably one time in a million instances. We are talking of the average man who has acquired a business. In my section that business would be worth, we will say, from \$200,000 to \$500,000, and the average man who has an industry in my State, if he died tonight, his family would be unable to procure the funds, and it would be necessary for the United States Government to step in there and sell that property under the hammer, and they would lose everything. It would result in a great loss.

Senator LA FOLLETTE. They have 10 years now in case of hardship.

Senator LONERGAN. That would not improve conditions very much where we came to a force sale of industry.

The CHAIRMAN. Why do you take it out of the value of the estate? That is the point I am asking you about.

Senator LONERGAN. What do you mean by taking it out of the value of the estate?

The CHAIRMAN. If a man carries a \$50,000 insurance policy on an estate of \$500,000; where the estate would be ordinarily put in at \$500,000, you would take the \$50,000 and put it in at \$450,000 which would reduce the taxes?

Senator LONERGAN. That is correct.

The CHAIRMAN. Why do you take the insurance policy from the value of the estate?

Senator LONERGAN. Because the taxpayer will be giving quick and sure payment to the United States Government, and he makes the sacrifice in raising the premium. It might be a year and it might be 10 years. He is really paying the tax. He is making the supreme sacrifice.

Senator HASTINGS. You offer it as an inducement for him to make arrangements to pay the tax quickly after his death?

Senator LONERGAN. Yes; and the tax will be paid; whereas in the average case, that is, the average case with which I am familiar, the

United States Government would not collect. The money would not be there.

Senator LA FOLLETTE. We are collecting a lot of money now, Senator.

The CHAIRMAN. Would you not get at the same results if you allow the premiums on such a policy deducted for that particular purpose to be deductible items on the income tax? Why would you not get the same results?

Senator LONERGAN. I would not say that. Supposing I had my life insured this afternoon for \$50,000, a new policy, and the premium, \$3,000; and supposing in a week from today I die. For that \$3,000, my estate would get \$50,000.

Somebody has suggested—I think it was one of the Treasury men to whom I talked—he said, “Why not deposit these insurance premiums or deposit Government bonds?” A man would have to live a century in order to accumulate a fund that would enable his estate to pay the taxes due the United States if his estate was in that situation.

Senator CONNALLY. How would it do if the premiums were deducted from the gross estate rather than the policy? Would that not be fair?

Senator LONERGAN. No; I would not say so.

Senator CONNALLY. He gets back all that he paid out.

Senator LONERGAN. That does not make any difference; he is making a sacrifice.

If you will bear with me, I will read what the insurance organization prepared; the gentleman who appeared before us. [Reading:]

Take the case of a man whose net worth—after all permissible deductions—is \$700,000. Suppose he has life insurance amounting to \$150,000, all of which he makes payable to the Treasurer of the United States under and in accordance with the proposed amendment. The amendment would not exempt this insurance in its entirety; the exemption is limited to such amount as is necessary to cover the tax liability of the estate, any balance over and above that amount being taxable as heretofore. As the tax in this case would be \$100,804, only that much of the insurance would be exempt. The balance of the insurance, amounting to \$49,100, would be included in the taxable estate accounting for \$11,204 of the total tax due.

ADVANTAGES

1. From the point of view of the Federal revenues the great advantage of the proposal lies in the fact that it would assure prompt payment, in full, of many assessments which must now be written off in whole or in part—due to posthumous depreciation or dissipation of assets, etc.—or collected only after numerous extensions.

In fact, it would assure payment in advance since the estate tax is not due until 15 months after death. In the interim, the Government would have the use of the money without interest.

2. From the point of view of the taxpayer, the advantages are obvious. The proposal would afford an opportunity to provide against the disastrous consequences of necessitous liquidation to cover Federal death duties.

As the law now stands, life insurance taken out to pay these taxes is itself taxable; it is included in the taxable estate with the result that the tax burden is sharply increased—the reward of prudent forethought is the imposition of an additional levy.

Then they offer other reasons.

I believe, gentlemen of the committee, that you will approve of this proposal. I favored it for at least a year. We adopted it in the Senate 1 year ago, and it was taken out in conference.

The CHAIRMAN. This is an important proposition. We have these people here from the Treasury with these estimates. Suppose we hear from them.

Senator BARKLEY. Mr. Chairman, I think we can report on our capital refund title, or would you rather go ahead with these estimates?

The CHAIRMAN. Let us take these estimates up first.

Senator LONERGAN. I understand from the Treasury people that they suggest that we do nothing at this time to tax mutual benefit insurance companies.

(Discussion off the record.)

Senator LA FOLLETTE. As to the question of taxation of insurance companies and reopening it in connection with this bill, it is a complicated question, it is a technical question, and we have spent a tremendous amount of time on it in the last revenue bill. This involves some 2,600 mutual companies and some 4,000 stock companies in the fire-insurance business, and if you open this thing up without any hearings, you are going to have a long controversy, and since the tax is not involved from the point of view of revenue, and that is what we are driving for here, I think it should not be opened.

Senator GERRY. How much revenue would you get out of taxing these companies?

Mr. KENT. At the most, under the plans we had in view, we would get a corporate tax on income from \$160,000,000 or \$170,000,000 on the investment of securities. A limited number of the companies have not been earning, apparently, all of the excess of premiums or assessments collected other than the amounts used for the payment of losses or setting up the proper reserves to their property owners, but have been keeping back some of it and have been creating fairly large investment reserves from which they are deriving a substantial income, and that is the one thing in which we are chiefly interested, but I feel that Senator La Follette has stated the situation fairly. They really should be given a chance to be heard and present their side of it before any action is taken.

The CHAIRMAN. Mr. Kent, you and Mr. Parker will please run over in your minds the thought of applying the capital stock tax if we continue it, and apply it on the stock of these corporations writing fire insurance, and to put it on the reserves of the mutuals. I understand there are a great many mutuals that build up a surplus or reserve. Perhaps something can be worked out whereby we can get some revenue out of that without hurting anybody or getting into this competitive situation.

Senator LA FOLLETTE. If you open that up, you are just going to have an irresistible demand for hearings on both sides of this proposition. It has not been testified to before this committee. It was all thrashed out in the 1934 revenue act. We had to come back and have hearings after we got the bill on the floor. You are just fixing to delay your bill here a couple of weeks if that happens.

The CHAIRMAN. Mr. Seltzer, have you the last estimate that I asked you for?

Mr. SELTZER. That is still in the works, Mr. Senator.

The CHAIRMAN. The one that I asked for first then, where they are exempted for \$15,000 and under.

Mr. SELTZER. All of the plans that contemplate a \$15,000 exemption are still in the works, because that particular provision is very difficult to work out.

Senator KING. Are the two plans that I asked for estimates, prepared?

Mr. SELTZER. We have those here.

The CHAIRMAN. I have this one here, no. A6 [reading]:

1. Impose 15 percent tax on statutory net income as now defined.
2. Repeal present capital stock and excess-profits taxes.
3. Define adjusted net income as the statutory net income less ordinary corporation income taxes plus 90 percent of dividends received. Define undistributed adjusted net income as adjusted net income less the dividend credit, and, a special credit of \$15,000, which is allowed all corporations. Impose a tax on undistributed adjusted net income equal to the sum of the following:

Forty percent of the amount of the undistributed adjusted net income which is not in excess of 50 percent of the adjusted net income.

Sixty percent of the amount of the undistributed adjusted net income which is in excess of 50 percent of the adjusted net income.

II. Estimated revenue, calendar year 1936

Estimated increase in revenue over present law.....	\$1,024,000
Reduction due to special credit of \$15,000 given all corporations...	204,000,000
Estimated increase in revenue.....	730,000,000

Senator COUZENS. I understood you to say that all of those 15 percent credits were still going through the mill?

Mr. SELTZER. It happens that this particular proposal containing only two rates was fairly easy to calculate, even though it had this \$15,000 exemption. It is much different where you have a series of graduated rates.

The CHAIRMAN. This would give \$730,000,000?

Mr. SELTZER. That is right.

The CHAIRMAN. Let me ask you in explanation of this: This provides for 40 percent of the undistributed adjusted net income which is not in excess of 50 percent of the adjusted net income?

Mr. SELTZER. Correct.

Senator KING. I am opposed to that. I am opposed to any plan that contemplates a tax on undistributed profits.

The CHAIRMAN. I would suggest, Mr. Seltzer, that you take up these different plans. You have copies of each of them.

Mr. SELTZER. The first plan that we discussed was plan A6 of which I believe all of you gentlemen have a copy.

The next schedule that I should like to discuss is A3.

Senator CONNALLY. That is the one I submitted.

Senator GERRY. Has A6 been explained?

The CHAIRMAN. Do you want to ask any question about it?

Senator GERRY. What is the 90 percent of dividends received? You take 10 percent off of any dividends received?

Senator CONNALLY. That does not change the law any; that is the present law. That is intercorporate dividends, and they make up for that, as I understand it, by charging 1.5 percent on the 10 percent, do they not, Mr. Kent?

Mr. KENT. Fifteen percent on the 10 percent.

Mr. SELTZER. Ten-percent intercorporate dividends are included in the statutory net income.

The CHAIRMAN. Any other questions?

(No response.)

The CHAIRMAN. What is the next one?

Mr. SELTZER. A3.

Senator CONNALLY. That is the second one that I submitted, Mr. Chairman. The first I submitted was 10 and 13 and 16 and 20.

The CHAIRMAN. Will you read A3?

Mr. SELTZER (reading):

1. Repeal present capital-stock and excess-profits taxes.
2. Impose 16-percent tax on statutory net income as at present defined.
3. Repeal exemption of dividends from normal tax on individuals.
4. Define adjusted net income as the statutory net income less ordinary corporation income taxes plus 90 percent of dividends received. Define undistributed adjusted net income as adjusted net income less the dividend credit. Impose a tax on distributed adjusted net income equal to the sum of the following:

0 on first 20 percent of the undistributed adjusted net income.

20 percent of the amount of the undistributed adjusted net income which is in excess of 20 percent and not in excess of 40 percent of the adjusted net income.

25 percent of the amount of the undistributed adjusted net income which is in excess of 40 percent and not in excess of 60 percent of the adjusted net income.

32 percent of the amount of the undistributed adjusted net income which is in excess of 60 percent and not in excess of 80 percent of the adjusted net income.

40 percent of the amount of the undistributed adjusted net income which is in excess of 80 percent of the adjusted net income.

II. Estimated revenue, calendar year 1936

Net estimated increase in revenue, \$633,000,000.

Senator CONNALLY. I want to ask you, Mr. Seltzer, why you made me an original estimate of \$690,000,000 and this shows \$633,000,000?

Mr. SELTZER. Before we can get an official final Treasury estimate, we have a conference of Treasury officials. They go over the whole matter. These estimates, we think, substantially are correct, but they have not been reviewed at the Treasury. We give them to you as fast as we can get them for your information, to give you an idea of the general order of magnitude.

Senator CONNALLY. This one now is a more mature one than the one you gave me the other day when you had \$690,000,000?

Mr. SELTZER. Correct.

Senator HASTINGS. I think they do pretty well to give you an estimate of any kind.

The CHAIRMAN. What you have done is to give a flat rate of 16 percent?

Mr. SELTZER. That is right.

The CHAIRMAN. And various percentages up to 80 percent of the adjusted net income?

Mr. SELTZER. Yes, sir.

Senator COUZENS. I am not going to be satisfied with this kind of an estimate until we know where it comes from. I would like to know what part comes from the 40-percent tax.

Mr. SELTZER. I have not with me here a break-down of that, because we spent the last 48 hours getting out 10 of these estimates. If you will give us sufficient time, we will give you all of the detail that you might desire on any of these.

Senator COUZENS. You have not a break-down here now?

Mr. SELTZER. Not here.

Senator COUZENS. I am not criticizing, but I just offer that as a reason why no determination can be made until we know where this money comes from; in what bracket.

Senator BYRD. There should be no trouble in getting a break-down, because they must have it before they can give the total.

Senator COUZENS. It is a determining factor of what rate we adopt.

Senator BARKLEY. We are not reading any of these for action. Let us get some more of them.

The CHAIRMAN. The next is A8.

Mr. SELTZER (reading):

1. Repeat present capital-stock and excess-profits taxes.
2. Repeat present exemption of dividends from normal tax.
3. Impose 15-percent flat tax on corporation statutory net income as now defined.

4. Define adjusted net income as statutory net income plus 90 percent of intercorporate dividends received less corporation income taxes. Define undistributed adjusted net income as adjusted net income less dividends paid, and, in the case of corporations with adjusted net income of less than \$20,000, a special credit for \$1,000. Impose tax on undistributed adjusted net income equal to the sum of the following:

Nothing on the first 20 percent of the undistributed adjusted net income.

Fifteen percent of the amount of the undistributed adjusted net income which is in excess of 30 percent of the adjusted net income.

Thirty-five percent of the amount of the undistributed adjusted net income which is in excess of 30 percent and not in excess of 50 percent of the adjusted net income.

40 percent of the amount of the undistributed adjusted net income which is in excess of 50 percent of the adjusted net income.

II. Estimated revenue, calendar year 1936

Gross estimated increase in revenue over present law.....	\$358,000,000
Estimated reductions due to special credit given small corporations.....	35,000,000
Estimated net increase in revenues.....	323,000,000

The CHAIRMAN. Any questions on that one?

(No response.)

The CHAIRMAN. The next is A7.

Mr. SELTZER (reading):

1. Impose 15-percent tax on statutory net income as now defined.
2. Repeat present capital-stock and excess-profits taxes.
3. Define adjusted net income as the statutory net income less ordinary corporation income taxes plus 90 percent of dividends received. Define undistributed adjusted net income as adjusted net income less the dividend credit, and, in the case of corporations with adjusted net incomes less than \$20,000, a special credit of \$1,000. Impose a tax on undistributed adjusted net income equal to the sum of the following:

0 of the amount of the undistributed adjusted net income which is not in excess of 30 percent of the adjusted net income.

30 percent of the amount of the undistributed adjusted net income which is in excess of 30 percent and not in excess of 40 percent of the adjusted net income.

35 percent of the amount of the undistributed adjusted net income which is in excess of 40 percent and not in excess of 50 percent of the adjusted net income.

45 percent of the amount of the undistributed adjusted net income which is in excess of 50 percent of the adjusted net income.

II. Estimated revenue, calendar year 1936

(In millions of dollars)

	Dividends exempt from normal tax on individuals	Dividends subject to normal tax on individuals
Estimated increase in revenue over present law.....	416	571
Reduction due to special credit given small corporations.....	35	35
Estimated net increase in revenue.....	381	536

Senator KING. In view of the large amount which you say will be available for taxation as net return on net profits, seven billion plus, it seems to me that your 571 is very much less than should be obtained with those rather high taxes upon those graduated brackets. Are you quite sure that that figure is accurate?

Mr. SELTZER. I am quite confident that it is. It has gone through regular processes.

Senator KING. You get over \$200,000,000 from your 15 percent on statutory net income.

Mr. SELTZER. You mean extra in addition to what we now get?

Senator KING. Yes.

Mr. SELTZER. We calculated the other day if we raised the statutory net income tax to 18 percent we would get an additional \$244,000,000. In this case you have it at 15 percent.

Senator KING. What do you figure you will get with 15 percent?

Mr. SELTZER. I have not got the figure here. It will be a relatively easy matter to calculate.

Senator CLARK. Suppose you calculate it.

Senator KING. That is not graduated. It is a flat 15, as I understand it.

Mr. SELTZER. Yes. Right now we get about 13.39 effective rate on the total statutory net under present law, even though the top rate is 15 percent.

The CHAIRMAN. Now, go to the next one.

Mr. SELTZER. The next is A2 [reading]:

1. Impose 15 percent tax on statutory net income as now defined.
2. Repeal exemption of dividends from individual and normal tax.
3. Define adjusted net income as the statutory net income less ordinary corporation income taxes plus 90 percent of dividends received. Define undistributed adjusted net income as adjusted net income less the dividend credit. Impose a tax on undistributed adjusted net income equal to the sum of the following:

Nothing on first 20 percent of the undistributed adjusted net income.

10 percent of the amount of the undistributed net income which is in excess of 20 percent and not in excess of 40 percent of the adjusted net income.

13 percent of the amount of the undistributed adjusted net income which is in excess of 40 percent and not in excess of 60 percent of the adjusted net income.

16 percent of the amount of the undistributed adjusted net income which is in excess of 60 percent and not in excess of 80 percent of the adjusted net income.

20 percent of the amount of the undistributed adjusted net income which is in excess of 80 percent of the adjusted net income.

II. ESTIMATED REVENUE, CALENDAR YEAR 1935

Estimated net increase in revenue if present capital stock and excess-profits taxes are repealed, \$400,000,000.

Net estimated increase in revenue if capital stock and excess-profits taxes are retained at present rates, \$546,000,000.

The CHAIRMAN. Which is the next?

Mr. SELTZER. A5. A5 is the following [reading]:

1. Impose 16-percent tax on statutory net income as now defined.
2. Repeal exemption of dividends from individual and normal tax.

Define adjusted net income as the statutory net income less ordinary corporation income taxes plus 90 percent of dividends received. Define undistributed adjusted net income as adjusted net income less the dividend credit. Impose a tax on undistributed adjusted net income equal to the sum of the following:

- 0 on the first 20 percent of the undistributed adjusted net income.
- 10 percent of the amount of the undistributed adjusted net income which is in excess of 20 percent and not in excess of 40 percent of the adjusted net income.
- 13 percent of the amount of the undistributed adjusted net income which is in excess of 40 percent and not in excess of 60 percent of the adjusted net income.
- 16 percent of the amount of the undistributed adjusted net income which is in excess of 60 percent and not in excess of 80 percent of the adjusted net income.
- 20 percent of the amount of the undistributed adjusted net income which is in excess of 80 percent of the adjusted net income.

II. ESTIMATED REVENUE, CALENDAR YEAR 1936

Net estimated increase in revenue if present capital stock and excess-profits taxes are repealed, \$465,000,000.

Net estimated increase in revenue if capital stock and excess-profits taxes are retained at present rates, \$500,000,000.

The CHAIRMAN. The next is which?

Mr. SELTZER. A-4 [reading]:

1. Repeal present capital-stock and excess-profits taxes.
2. Impose 15-percent tax on statutory net income as at present defined.
3. Repeal exemption of dividends from normal tax on individuals.
4. Define adjusted net income as the statutory net income less ordinary corporation income taxes plus 90 percent of dividends received. Define undistributed adjusted net income as adjusted net income less the dividend credit. Impose a tax on undistributed adjusted net income equal to the sum of the following:

- 0 on first 20 percent of the undistributed adjusted net income.
- 20 percent of the amount of the undistributed adjusted net income which is in excess of 20 percent and not in excess of 40 percent of the adjusted net income.
- 25 percent of the amount of the undistributed adjusted net income which is in excess of 40 percent and not in excess of 60 percent of the adjusted net income.
- 32 percent of the amount of the undistributed adjusted net income which is in excess of 60 percent and not in excess of 80 percent of the adjusted net income.
- 40 percent of the amount of the undistributed adjusted net income which is in excess of 80 percent of the adjusted net income.

II. ESTIMATED CALENDAR, CALENDAR YEAR 1936

Net estimated increase in revenue, \$570,000,000.

Senator CLARK. We are not getting anywhere toward consideration by having these things put in in this sort of manner. I suggest that the Treasury report all that the Treasury is to submit. All that this witness is doing is to authenticate the exhibit that are being put in.

I suggest that they all be put in at one time, and then we will go into executive session and consider them.

(Discussion off the record.)

The CHAIRMAN. Have you any other estimates?

Mr. SELTZER. There are two other types of proposals. These previous schedules have uniformly included a flat tax on statutory net income and a surtax on a supertax on undistributed net income.

Senator KING. It is not a supertax.

Mr. SELTZER. Call it what you like, as far as these others are concerned. Your proposal, Senator, differs from the others in confining itself essentially to a flat corporation income tax.

Senator King's proposal no. 1 is:

1. Impose 23-percent tax on statutory net income of corporations as now defined, of which 5 percent would represent a prepayment at the source of the normal tax on dividends, and 18 percent would represent the tax to be paid by the corporation as such.

2. Capital stock and excess-profits taxes to be retained.

3. No supertax on undistributed earnings.

4. Normal tax raised from 4 to 5 percent.

II. Estimated revenue, calendar year 1936

Estimated increase in revenue over present law by reason of 23-per cent rate on statutory net income-----	\$579,500,000
Estimated addition due to increase in normal rate from 4 to 5 percent-----	60,000,000
Estimated net increase in revenue-----	639,500,000

Senator King's proposal no. 2 is as follows:

An alternative proposal whereunder the normal tax would be retained at 4 percent, but the rate on corporation statutory net income would nevertheless be 23 percent, of which 4 percent would represent a prepayment at the source of the normal tax on dividends, and 19 percent would represent the tax to be paid by the corporations as such, is estimated to yield \$579,500,000 over the revenues estimated in the Budget.

There is this that might be said about Senator King's proposal. When you levy a tax on the corporation, that includes a prepayment at the source on dividends, you raise the question whether you wish now to tax the dividends received by tax-exempt institutions and tax-exempt individuals which would be involved in this proposal unless you otherwise provided for a recoupment by them.

The CHAIRMAN. What have you done with reference to the estimate? Have you excluded that?

Mr. SELTZER. No; we have taken this as given to us.

Senator KING. There would be no recoupment from those institutions?

Mr. SELTZER. None whatever.

Senator CLARK. That same charge on charitable institutions is contained in the House bill, is it not?

Mr. SELTZER. You cannot say dogmatically that it is contained in the House bill, because the tax is paid by corporations and their stockholders. If the corporation distributes all of its earnings, its stockholders who were tax-exempt as individuals because their incomes were not big enough or were tax-exempt institutions, would pay no tax.

Senator CLARK. I am just asking for information. Under the House bill, in the case of an institution such as you describe, a charitable organization, if they accumulated a surplus, under the House bill they would be taxed, would they not?

Mr. SELTZER. If the companies in which they held stock interests retained earnings?

Senator CLARK. Yes.

Mr. SELTZER. True.

The CHAIRMAN. Will you read the other estimates that you have?

Mr. SELTZER. The next is C-1 and C-2, which are the proposals of Senator George.

C-1 is as follows:

1. Impose a tax of 25 percent on corporation statutory net income as at present defined, except that each corporation will receive a credit against the income subject to tax of 40 percent of the amount of dividends it pays.

2. Repeal present capital stock and excess-profits taxes.

3. Repeal exemption of dividends from the normal tax on individuals.

II. ESTIMATED REVENUE, CALENDAR YEAR 1936

Estimated net increase in revenues, \$641,000,000.

Mr. SELTZER. When you work out this proposal, Senator George, you find out in fact that it amounts to this: A 15-percent tax on statutory net income as at present defined, and then a flat 10-percent tax on the retained earnings of corporations.

Senator GERRY. How does that work out? Just on the general basis of a certain number of corporations.

Mr. SELTZER. If you were to take these figures and work out an arithmetical illustration, that is what you would come out with.

The CHAIRMAN. In other words, it is the same thing as imposing a flat rate of 15 percent and putting a flat rate of 10 percent on the retained earnings?

Mr. SELTZER. Yes; a straight 15 percent on the statutory net, and a straight 10 percent on undistributed.

Senator LA FOLLETTE. If you are going to go at this thing at all, it is a very simple way of doing it, because as far as the bill is concerned, you do not have any complicated schedules or anything else. That is the plan that Mr. Parker discussed the other day. I do not think the committee has given it very much consideration, but as a compromise—

Senator GEORGE. C1 and C2 are both predicated on the same principle, but have different rates.

Senator HASTINGS. Let us find out how the thing works out, from the witness.

The CHAIRMAN. Let Mr. Parker explain it.

Mr. PARKER. Suppose you have \$100,000 of adjusted net income. If you declare no dividends at all, you will just pay 25 percent tax or \$25,000. That is your maximum tax.

Suppose that you have a \$100,000 adjusted net income and you have a 10 percent dividend declaration of \$10,000, you get a credit of 40 percent, of \$10,000.

Senator CONNALLY. You have a net income of \$100,000?

Mr. PARKER. Yes; and you declare \$10,000 in dividends. And pay \$10,000 in dividends. Your credit is 40 percent of what you pay in dividends or \$4,000. Then you have \$96,000 subject to tax and

at the same rate. You apply 25 percent to the \$96,000, which would be \$24,000. That presents then a rate of 24 percent on your whole \$100,000.

Suppose now that you declare \$40,000 in dividends. You have 40 percent credit, which is \$16,000. \$16,000 from \$100,000 is \$84,000, which is subject to 25 percent tax, which is \$21,000, or 21 percent. If you declare out just half in dividends, \$50,000, then your dividend credit of course would be 40 percent of that, or \$20,000, with \$20,000 from \$100,000 is \$80,000, and your tax of 25 percent on \$80,000 is \$20,000, or just 20 percent.

That is with a distribution of only 50 percent of your income, which is much less than the average, your rate is 20 percent.

If you declare everything out, your dividend credit of course becomes 40 percent of \$100,000 or \$40,000, which subtracted from \$100,000 leaves \$60,000. 25 percent of \$60,000 is \$15,000, which is just what your corporation is paying today.

Senator LA FOLLETTE. One advantage of this that I do not think you have pointed out, Mr. Parker, is that as far as the simplicity of this bill is concerned, you simply impose your flat tax and then provide for this credit in your credit section, and that is all there is to the bill.

Senator KING. In other words, if they pay 25 percent, that is the maximum.

Mr. PARKER. That is the maximum.

Senator KING. And they are not compelled to make distribution of dividends at all.

Senator CLARK. In other words, Mr. Parker, it has this one advantage, that every corporation pays at least 15-percent minimum?

Mr. PARKER. That is the minimum tax.

Senator CLARK. Instead of starting at the bottom and scaling up, you start at the top and come down the other way, so that each corporation gets an increasing credit as they pay out in dividends, but every corporation—and this is important, because we have considered some corporations who under the House bill would not pay any taxes at all—every corporation will pay at least the present flat tax of 15 percent.

Mr. PARKER. That is correct. And I think that it will encourage distribution by reducing the rate to a reasonable amount.

Senator KING. It will amount to practically 15 percent flat plus 10 percent on undistributed.

Mr. PARKER. If you want to put it that way, I could work it out almost the same as though you start at 15 percent and put 10 percent on.

Senator KING. I would rather it be a flat tax than a tax on undistributed profits.

Senator BYRD. What percent would you have to give credit for here if you just had a normal tax of 5 percent, and in order to make the difference between, that is the 5-percent additional tax, how could you work it that way?

Mr. PARKER. I do not know that I just got your question. This estimate was based on the same normal tax as we have got now.

Senator BYRD. I understand that. But some of us, at least I have the view that the tax on undistributed surplus should not be in

excess of the normal tax. Could you plan to work it out along that line, assuming you have a normal tax of 5 percent?

Mr. PARKER. I do not think you could get much money.

Senator BYRD. If you retain the present capital stock and excess-profits taxes you probably have enough.

Senator CONNALLY. Senator George, your plan is essentially a graduated rate, working backward instead of forward.

Senator GEORGE. Substantially that. This is what Mr. Parker suggested. I wanted to see how they would look, because I think they have decided advantages.

Senator CLARK. It is obvious in any case, an increase in the normal tax.

Senator BYRD. As I understand it, Senator George, you are not favoring this plan? It just gives us the information?

Senator GEORGE. No; I favor the original proposal that made of a flat tax plus the normal on undistributed profits.

Senator CLARK. I favor this more than any scheme I have heard yet.

Senator GERRY. What does your capital stock and excess profits bring in?

Mr. PARKER. \$168,000,000.

Senator GERRY. Suppose you had what Senator Byrd suggested?

Senator GEORGE. We had that estimate yesterday.

Senator KING. Mr. Parker, as I read this so-called plan C-1 it contemplates repeal of the present capital-stock and excess-profits taxes and repeals the exemption of dividends from the normal tax on individuals.

Mr. PARKER. The individual would be subject to the 4-percent normal tax on dividends. I really think that the individual does not appreciate that exemption. I admit that theoretically your normal tax ought to be exempt. That is the theory, and that is correct, but theory and revenue sometimes do not mix too well, and it makes a big difference whether you subject these dividends to normal tax.

Senator KING. Let me just give an illustration of one of the plans which I suggested: 23-percent flat corporate rate with 5-percent recoupment.

(1) Net income (with no intercompany dividends).....	\$100,000
(2) Corporate tax.....	23,000
(3) Balance after corporate tax.....	77,000
(4) Dividends payable.....	50,000
(5) Amount of dividend withheld at source and kept by corporation (5 percent).....	2,500
(6) Dividend received by shareholder.....	47,500

Under this plan the Federal Government will always collect from the corporation the flat corporate tax of 23 percent, which, in the illustration given, amounts to \$23,000. However, because of the 5-percent recoupment provision, in case dividends are paid, part of this tax will be borne by the shareholders and recouped by the corporation. In the illustration given, the tax of 23 percent, although paid by the corporation into the Federal Treasury, is divided between the corporation and its shareholders as follows:

Tax of 23 percent.....	\$23,000
Amount recovered by corporation from shareholder through 5-percent recoupment.....	2,500

Tax actually borne by corporation.....	21,500
Tax actually borne by shareholder (2.5 percent).....	2,500

If the corporation distributed all of its net income, namely \$100,000, in dividends, its tax burden will be \$18,000 or 18 percent and the shareholders' tax burden will be \$5,000 or 5 percent.

Senator BARKLEY. The day before yesterday the Treasury officials reported a net income of \$642,000,000 on the plan suggested by Senator Harrison. That is a flat 18-percent tax plus 7 percent on that retained.

Mr. SELTZER. And raising the normal rate to 5 percent.

Senator BARKLEY. In that connection, I asked you to figure on what the difference would be between a 17 percent flat rate and 8 percent on the undistributed. Did you get that?

Mr. SELTZER. That is being worked out now.

Senator KING. There are two others that I suggested. They have not been worked out yet. The chairman is not here, and I would like to ask if there is anything else, gentlemen, that you wanted to take up at this time? The chairman will be here in a few minutes.

Senator BLACK. The plan C2 is the same as C1 except a different rate?

Senator GEORGE. Your flat starts at 30, and you get a 50 percent credited on dividends paid instead of 40 percent. That is the only difference.

Senator KING. Will you explain C2?

Mr. SELTZER. 1. Impose a tax of 30 percent on corporation statutory net income as now defined, except that each corporation will receive a credit against the income subject to tax, of 50 percent of the amount of dividends it pays.

2. Repeal present capital-stock and excess-profits taxes.

3. Repeal exemption of dividends from the normal tax on individuals.

II. ESTIMATED REVENUE, CALENDAR YEAR 1936

Estimated net increase in revenues, \$835,000,000.

That plan differs from the first in this respect. Your flat tax is 15 percent as it is in the first, but your surtax on withholding earnings instead of being 10 percent is the equivalent of 15 percent. That is why you get so much more revenue.

Senator BLACK. That surtax reaches its peak, of course, when they distribute the least.

Mr. SELTZER. We cannot work it out for surtax and individuals separately.

Senator BLACK. I meant when the corporation distributes the least it reaches its 30 percent.

Mr. SELTZER. Of course, your revenue figure is always a net balance under this proposal.

Senator KING. Are there any other matters pending the arrival of the chairman?

Senator CONNALLY. Most of these repeal the capital stock and excess profits. If you retained that, we would get considerably more revenue?

Mr. SELTZER. Yes.

Senator KING. My view is that we ought to retain those.

Senator BLACK. Under C1, if we did not repeal that, we would get about \$771,000,000.

Mr. SELTZER. It varies in every schedule.

Senator CONNALLY. Depending upon the amount you take out.

Senator BARKLEY. I would like to bring up our report on the refunding, title IV. We are ready to report on it.

Senator KING. If there is no objection, we will proceed with that.

Senator BARKLEY. Will you have these others by tomorrow?

Mr. SELTZER. I doubt it, because none of our people have had any sleep last night.

Senator KING. We will proceed, then, with title IV.

Senator BARKLEY. There is no use of reporting on this unless it is disposed of.

Senator LA FOLLETTE. Let us dispose of it.

Senator BARKLEY. I do not think any controversies will arise over it.

Senator GEORGE (presiding). Proceed, Senator Barkley.

Senator BARKLEY. The committee met and spent all yesterday morning goes over these suggested changes with reference to the refunds under sections 601 and 602 and we amended section 601 (a) by striking out the parentheses on page 229, lines 19, 20, and 21, and a new section 603 added, which appears on page 8 of the mimeographed copy, as follows:

SEC. 603. The proclamations, certificates, and regulations prescribed by the Secretary of Agriculture under the Agricultural Adjustment Act, as amended, in effect on January 5, 1936, insofar as not inconsistent with this act, are hereby made applicable for the purpose of determining the amount of any refund or payment authorized under sections 601 and 602.

The object of that is simply to preserve those regulations under which this tax was collected and use them as a yardstick by which they are to be refunded. It is clearer and simpler than having the parenthetical statement on page 1. I would like to have that amendment adopted.

The CHAIRMAN. If there is no objection, it will be adopted.

Senator BARKLEY. On page 2, subsection (b) from 601 has been rewritten. The language underscored there is the language that is changed. As passed by the House, section 601. (b) provided that no refunds under section 601 shall be made to the processor or other person who paid the tax with respect to the articles on which the claim is based. Because of the situation existing with respect to manufacturers of large cotton bags, both processors and nonprocessors, it is deemed advisable to permit the adjustment of all claims under section 15 (a) whether filed by processors or nonprocessors. Accordingly, an exception has been written in in the first sentence of section 601 (b) applicable to refunds to section 15 (a).

(The same is as follows:)

(b) Except for refunds under section 15 (a) of the Agricultural Adjustment Act, as reenacted herein, no refund under this section shall be made to the processor or other person who paid or was liable for the tax with respect to the articles on which the claim is based. No refund under this section shall be allowable to any person with respect to any articles where such person prior to January 6, 1936, paid an amount as tax under the Agricultural Adjustment Act, as amended, by taking as a credit against such amount an

amount otherwise allowable as a refund with respect to such articles under sections 15 (a), 15 (c), 16 (e) (1), 16 (e) (3), or 17 (a) of said act. No refund under this section shall be allowed to any person except to the extent that he establishes that he has not received, and is not entitled to receive, reimbursement of such amount from the processor or other vendor with respect to the articles on which the claim is based. No claim under this section (except claims of processors under section 15 (a)) shall be disallowed on the ground that the tax with respect to the article or the commodity from which processed has not been paid.

Senator BARKLEY. That language is put in there to take care of the manufacturers of cotton bags. There are only five of them. They were not only manufacturers of cotton bags, but also processors, and as the bill passed the House they could not file a claim for refund as manufacturers but had to do it as processors.

We have amended this so that now they can file their claim as manufacturers of these cotton bags, just as the rest of the manufacturers who are not processors.

Senator CLARK. May I ask the Senator from Kentucky if there is any discrimination under the amendment which he is proposing, which I have not had a chance to examine, against the manufacturer of cotton bags on the ground that he was not to be a processor?

Senator BARKLEY. None at all. They are put on the same basis.

Senator GEORGE. That also takes care of the sales to charitable institutions, Mr. Kent?

Mr. KENT. Yes.

Senator GEORGE. That is clear now, that is all clear now?

Mr. KENT. Yes.

Senator GEORGE. And sales to the Government itself?

Mr. KENT. Yes; that is all clear.

Senator GEORGE. As well as the processors?

Mr. KENT. Yes.

Senator BARKLEY. I move that that section be adopted.

The CHAIRMAN. Without objection, it will be adopted.

Senator BARKLEY. There is no change in (c), (d), or (f). We have included them here to make it a whole.

Subsection (g) reads as follows:

(g) Section 16 (e) (1) of the Agricultural Adjustments Act, as reenacted by subsection (a) of this section, is amended by striking out "subsequent to June 26, 1934" and by inserting in lieu thereof "on or after June 1, 1934."

The CHAIRMAN. Without objection, that will be agreed to.

Senator BARKLEY. On page 4, section 602 (a), relating to floor stocks as of January 6, 1936, there is added the words "with respect to the articles on which the claim is based."

Senator GEORGE. Is that a limitation in any way?

Senator BARKLEY. No; not beyond the original limitations as passed by the House, but this clears it up somewhat.

The CHAIRMAN. Without objection, that will be adopted.

Senator BARKLEY. Subsection (b) on page 4, we have changed some language down in lines 17, 18, 19, 20, 21, and 22.

In clause (1) the words "will not", occurring in lines 20 and 21 of page 231, have been deleted and the phrase "is not entitled to receive" substituted. The phrase "will not" is ambiguous in that it may be construed as requiring a weighing of possibilities. The words "processor or other vendor" have been inserted in line 21, for purposes of clarification.

In other words, this simply clears up an ambiguous phraseology in the House.

The CHAIRMAN. Without objection, those changes will be agreed to.

Senator BARKLEY. Clause (2), beginning on line 22 of page 231, does not take into account the case of claimants who did not increase the sale price of the articles because of the tax burden and who, accordingly, might not be able to reduce the price of the articles because of the invalidation of the taxes under the Agricultural Adjustment Act. Clause (2) has been reworded to provide for this situation.

It simply is reworded to carry out what was evidently the original intention, but it is done better under this language than it was in the House bill.

Senator CLARK. There is no change in substance?

Senator BARKLEY. No. I think I had better give the balance of the explanation.

In order to expedite the consideration of claims, a sentence has been added to the end of section 602 (b) which would permit the claimant, with the approval of the Commissioner, to submit as part of his claim—in lieu of a detailed schedule of articles, purchases, sales prices, and sales—an affidavit setting forth the total amount of tax burden passed on to him, the total amount of such burden for which he has been reimbursed or is entitled to reimbursement, the total amount that he has included in the sales prices of his articles, and the total amount of the tax burden which the claimant has borne himself. It is felt that the inclusion of such a provision will expedite the consideration of meritorious claims, will relieve the Bureau of a heavy administrative burden in such cases, and will relieve claimants in many cases of a heavy evidentiary burden. At the same time, if the Commissioner has reason to believe that the claimant has submitted a false affidavit, or has other reason for inquiring into the accuracy of the claim, the Commissioner will have full authority to cause necessary investigations to be made and to put the claimant on strict proof of his claim. The latter would require a detailed break-down of all transactions relating to purchase and sales of the articles upon which the claim is based.

The object of that is to permit the Commissioner on the filing of an affidavit by the claimant in setting out all of these facts, to go on and pay the amount. It simplifies the proceeding with respect to the claim, but if he has any suspicion about it or there is any ground to believe that the claimant has made a false statement or a false affidavit, he can hold it up and go into it in detail, but the Bureau believes that this language would eliminate a lot of unnecessary delay and technicalities with respect to the presentation of the claims.

Senator CLARK. It does not change any legal rights?

Senator BARKLEY. No, it does not; but it gives the Commissioner a freer hand in passing on claims on the prima-facie evidence submitted on behalf of the claimant.

Senator BLACK. And it gives the claimant a freer hand?

Senator BARKLEY. Yes.

Senator GEORGE. Let me ask you this question. I do not know whether you have already dealt with it or passed it in the bill or whether you are coming to it, but I would like to know is it required

that before any person shall be entitled to a refund with respect to merchandise on hand and sold after the date of January 6, that he must have reduced the price of that merchandise?

Mr. KENT. All that he has to do in his affidavit, if he can honestly say in his affidavit that he absorbed the burden of the tax and he did not pass it on, then prima-facie the Commissioner can go ahead and allow his claim, unless there is reason to believe that that is not the situation. In other words, it may be that in some lines the prices were not reduced after January 6 because of other competitive factors entering into the picture.

Our object has been to give the Bureau leeway to do with these claims, to deal with them, as thoroughly and expeditiously as possible. Thousands of them will be claims for small amounts, where the cost of making an exhaustive investigation into all of the facts would be out of all proportion to the amount of the claim.

Senator GEORGE. But you do not cut off the theory that he may have passed on the tax after the date of the decision of the court?

Mr. KENT. That is right.

Senator GEORGE. As we did when we were arriving at this "wind-fall" tax.

Mr. KENT. Yes.

Senator GEORGE. I was personally in hopes that you might find it feasible to do that. It seems to me it would simplify it. All right, Senator BARKLEY.

Senator BARKLEY. There is no change in subsection (1) and (2), but we have added a new subsection (3) to define the term "sale price."

It is as follows:

(3) The term "sale price" includes the price at which the claimant actually sold the article or articles prior to the date of the filing of his claim, or if the article or articles have not been sold, the price at which he is offering the same for sale on the date of the filing of his claim.

It was thought necessary to provide a definition there of "sales price", and this definition seems to cover the situation.

Senator GEORGE. That conforms with the provisions of the act?

Senator BARKLEY. Yes.

Senator GEORGE. Without objection, then, it will be adopted.

Senator BARKLEY. Subsection (2), at the bottom of page 6 of the mimeograph, we have added this provision [reading]:

No payment shall be made under this section in connection with any article with respect to which a refund has been allowed or credit has been taken under the Agricultural Adjustment Act, as amended, or a refund has been allowed or is allowable under section 601 of this title.

Senator GEORGE. What does that do?

Senator BARKLEY. It prevents the possibility of duplicate payments.

The CHAIRMAN. There is no need for these gentlemen from the Treasury Department to stay here this afternoon?

Senator BARKLEY. No.

The CHAIRMAN. Then there is no need of them staying any further.

Senator BARKLEY. In section 602 (f), clause (3), we have added the words "processed from sugar beets and sugarcane", in the first

sentence of that clause, so that it reads "direct-consumption sugar processed from sugar beets and sugarcane."

Senator CONNALLY. Should that not be "or" instead of "and"?

Senator BARKLEY. Yes; it should be "or."

In section 602 (f), line 4, strike out the phrase "wholesale floor stocks of"; on line 5, after the word "sugarcane", insert "and held in other than retail stocks."

Senator GEORGE. What is the purpose of that? Is that where it is held for use other than sales, as in candy manufacture?

Mr. KENT. That was deemed desirable to maintain the proper distinction between the retail floor stocks and other than retail floor stocks. Wholesale stocks does not necessarily include all stocks other than retail floor stocks. You have some intermediary processor, for instance, who might not be described as wholesale jobbers but who are themselves manufacturers, but they are manufacturing articles or commodities that have already been processed and on which a tax has already been paid or for which someone was liable. It is merely a clarifying change.

Senator GEORGE. Without objection, we will pass on to the next one.

Senator BARKLEY. We have added also a new section 604. We have already passed on section 603.

Section 601 covers the same subject matter as the first part of section 21 (d) (2), which should be repealed to avoid confusion and a possibility that two statutes relating to the same subject matter may be operative. It simply makes it clear that we have not got two statutes which might seem in conflict on the same subject.

Senator LA FOLLETTE. I move the section, as amended, be approved.

Senator BARKLEY. In that connection, I wish to say that the subcommittee discussed the possibility of a revision of section 21 (d) of the Agricultural Adjustment Act, for this reason: The House Ways and Means Committee are now considering a revision of section (d), along with two or three other administrative sections of the present law. When they will make a report on that independent bill, none of us know; but we thought that if the departments and the subcommittee, in working out a revision of section 21 (d) that is satisfactory, in time to offer it as an amendment to this bill, instead of having to pass a new bill—that we could either bring it before the full committee and have approval of it, or bring it before the floor as an amendment. We could offer this revised section 21 (d) on the floor if it cannot be worked out in time to put it in the bill here. It is better to do it without having to pass two bills.

With that exception, this is a complete report of the subcommittee.

Senator GEORGE. Let me make this inquiry: It has been brought to my attention that in many instances raw sugar is purchased, not for the purpose of resale but for the purpose of manufacture into candy or soft drinks or otherwise. Is that taken care of in this bill? Do you recall that objection? The House bill seemed to have made no actual provision for that sort of thing.

Mr. KENT. The reason for that was this: In drafting title IV, we endeavored to take as our objective giving this group of claims substantially the same rights that they would have enjoyed had the

taxes imposed by the A. A. A. been terminated by proclamation of the Secretary of Agriculture rather than by an adverse judicial decision. No provision was made for the cases to which you refer in the A. A. A. as amended, largely for this reason, that the administrative difficulties and complexities involved in determining the amount of sugar in a few pounds of candy or in a case of canned peaches are so out of proportion to the amount involved that the cost of administering those claims would be simply disproportionate.

Senator GEORGE. I meant stocks on hand. Stocks of sugar held by the processor, by the manufacturer, on which he has paid the processing tax, and he has the actual stocks of sugar on hand. It runs into large figures.

Senator CONNALLY. If he paid the tax and has it all on hand, he will get it all back.

Senator GEORGE. He would not get it back because of the drop in the price.

Mr. KENT. He would get it if it is held in the form of direct-consumption sugar.

Senator GEORGE. I do not mean where it has been put into a soft drink and that product is unsold, but I mean where the stocks are on hand.

Mr. KENT. I am reassured on that point by Mr. Bolton of Commissioner Bliss' office, who has worked on this, that they have been taken care of, because it does provide for the refund of direct-consumption sugars which are in floor stocks.

Senator GEORGE. What are the conditions attached to the refund on that particular item?

Mr. KENT. Just the same conditions as applied when it was floor stock. They file their affidavit and show their inventory.

Senator GEORGE. They do not have to show a sale of it?

Mr. KENT. No.

Senator CONNALLY. What do you mean by "direct-consumption sugar?"

Mr. KENT. It simply means sugar in a form which could be consumed without further process.

Senator BARKLEY. If they had had that sugar in store and decided not to put it into candy or canned peaches, it could be sold for ordinary consumption?

Mr. KENT. Exactly.

Senator BARKLEY. And they would get the refund just as if it had not been intended for candy?

Mr. KENT. Exactly.

Senator CLARK. May I ask the chairman of the subcommittee a question? It deals with another matter.

Senator COUZENS. Will you pardon me, Senator? This deals with this subject. The testimony before the committee was to the effect that many of the retailers desired to get a refund of their August 1933 payment and not be compelled to take an inventory as of January 6, 1936. Was anything done with that?

Senator BARKLEY. We discussed that at great length, Senator, and we found we ran up against this difficulty: If you provide for the refund of the amount of tax paid in the fall of 1933, in a great many cases you will be refunding a tax that was passed on. It could not

be passed on on some things, like a shirt or a pair of socks, where the price was marked; but this refund section applies to flour and other products of wheat which was sold in bulk, to all sorts of products of cotton and meats, and so on. To refund the amount of the tax they actually paid on the stock there, you would be refunding a considerable amount that was passed on.

In addition to that, many concerns were in business in the fall of 1933 who were not in business on January 6, 1936, and vice versa. Other people have gone into business since August 1933—situations of that kind. So we decided to make an effort to work out some alternative which would take into consideration the concerns in business in 1933 and still operating on January 6, 1936, with approximately still the same amount of business or stocks that they had on hand on both dates; but in trying to do that, we ran up against the insuperable administrative difficulties and have not been able to do it. Mr. Kent can tell you about that more in detail.

Senator COUZENS. Mr. Kent, in previous testimony, frankly admitted the great administrative difficulty of taking all of these items and determining the amount due based on the January 6, 1936, situation. Yet it was plainly known to the Government that the tax was paid in August 1933. I got a letter this morning from a constituent who said that in August 1933 he had \$150,000 worth of floor stock and on January 6, 1936, he had \$300,000 worth of floor stock, but he would be willing to take his refund as of August 1933 even though it was smaller, to save all of the delay and trouble of trying to determine the tax, because of the difficulties that would be incurred both by the Government and himself in determining the amount of tax that might be refundable on the basis of the 1936 inventory. I think that is an unanswerable argument, and I just do not get the point why it cannot be worked out.

Senator BLACK. May I make this statement as a member of the subcommittee. I favored and I do favor if anything can be worked out, a plan whereby we can give an optional settlement, letting the option rest with the Bureau, as to a settlement on the basis of the floor stock paid originally, and we requested and probably they are going to work on it, as the Senator stated. We have asked them to work on that; and whether or not there could be an amendment drawn up in such a way that the businesses that are going businesses, as the Senator said and continued to go on until January 6, that we could work out a plan whereby that could be done in such a way that the Bureau itself could exercise the option to let them do that. In that way I believe we would avoid probably two or three thousand long drawn-out contests, and would strengthen it in one way by adding a provision which does permit the taxpayer to figure it up for himself and then let the Bureau go over that, and unless it is suspected that there is some fraud or something of that kind, let that be accepted. That is in the amendment which we have adopted.

Senator BARKLEY. It is on page 5 of the mimeograph. The object of that is to permit the claimant to file an affidavit setting out all of the information bearing on the claim, the amount passed on to him and passed by him and so on, and unless there is some suspicion there is fraud in it, the Commissioner will accept that and pay the claim. But he has authority to hold it up and make a

detailed investigation if on the face of it it bears evidence of any fraud. That will simplify from a half to three-quarters of these cases and dispose of them. But I will say that this matter is not foreclosed, Senator.

Senator LA FOLLETTE. Mr. Chairman, I would like to alter my motion. I moved that the schedule as amended and the report of the subcommittee be adopted. I modify that by moving that it be adopted subject to these matters—

Senator BARKLEY (interposing). It is not necessary to do that. If we can work out something, we will bring it in.

Senator LA FOLLETTE. There might be some other details of draftsmanship and other small matters. I just want to leave it open so that we do not have to move for reconsideration, but that it be tentatively adopted with that reservation.

Senator CLARK. Subsection (b) of section 601 is what I was going to inquire about. I think the chairman of the subcommittee is thoroughly familiar with the subject of the large cotton bags in which 35 companies are engaged, and only 4 are included in subsection (b) as originally written, apparently for some purpose, in the Department of Agriculture. They are punishing the manufacturers of cotton bags who might also be processors. I think the amendment clearly takes care of that, except that I am apprehensive about some language. It reads:

No refund under this section shall be allowed to any person except to the extent that he establishes that he has not received, and is not entitled to receive, reimbursement of such amount from the processor or vendor with respect to the articles on which the claim is based. No claim under this section (except claims of processors under section 15 (a)) shall be disallowed on the ground that the tax with respect to the article or the commodity from which processed has not been paid.

As far as the rule established in that language is concerned, I am entirely in sympathy, because my information is that these people have not received any refund; but I am just apprehensive of the language in the amendment, simply on the ground of the testimony of the Secretary of Agriculture the other day, which to my mind undertook to set up a standard of proof and make it impossible for anyone to prove that he had received the refund, or on the whole matter of processing taxes. I simply would like to ask the chairman of the subcommittee, who is more familiar with it than I am, whether there is anything else in this act which will modify this language; in other words, if this language would be submitted to the court as a mere matter of approval, I would be perfectly willing to rely on that, but if there is anything else in the language along the line of the testimony of the Secretary of Agriculture setting up presumptions and things of that sort, I would not be willing to take this language.

Senator BARKLEY. I think there is nothing else in the bill anywhere that is in conflict with this. So far as the Secretary's testimony is concerned, I do not recall all of it in detail, but this provision has with it the idea that a man cannot collect from two sources. We have tried to provide that he could not collect twice.

Senator CLARKE. The testimony of the Secretary of Agriculture was to set up a right and then provide insuperable obstacles against obtaining the right.

Senator BARKLEY. I am satisfied there is nothing else in the bill which would modify this.

Senator BLACK. May I make a statement in regard to this? I submitted this amendment myself to the Treasury Department on account of the discrimination. I found that both the Agricultural Department and the Treasury Department favored doing away with this discrimination against these particular processors, and am sure that this does not in any way take away from their rights, and there is nothing in the bill that does. I think the bill was drawn in good faith, following largely what these bag people had drawn themselves, which I submitted to the Treasury Department, and I am sure they are absolutely protected.

Senator BARKLEY. Furthermore, the formulas that you probably have in mind and those that you have discussed with the Treasury have relation to section 21 (d) of the Agricultural Act, and there is no formula here.

Senator BLACK. The Secretary of Agriculture made a very strong argument for this particular kind of payment. It was the windfall tax. This does not come under the windfall tax. This comes under a different classification where they were promised to be paid back, and the Secretary of Agriculture argued in favor of that.

Senator CLARK. I made my living for a great many years trying lawsuits, and I could not in a million years set up and prove a claim against the insuperable obstacles which were set up by the Secretary of Agriculture, as I understood from his testimony.

Senator GEORGE. Where the tax is under \$10 you do not pay them back anything?

Senator BARKLEY. No; we do not; not under \$10.

Senator GEORGE. I do not imagine many fall within that class, but it does seem to me that we should give those people who paid a small amount of tax like that, where you do not want to go back into all of the accounting, let them have back what they paid if they are still in business.

Senator CONNALLY. It is bad psychology to say that because a man's claim is small that he cannot have it. I think it would be better to say that we will pay all under \$10.

Senator GEORGE. Pay all that paid that when the law went into effect.

Senator LA FOLLETTE. How many are there under \$10?

A VOICE. About 75,000.

Senator COUZENS. I would rather leave that whole language out and not make it look ridiculous. Many, many thousands will never even make the claim.

Senator BARKLEY. That is true. There is no doubt about it, but there is a large number that will make the claim of these little amounts \$1, \$1.50, \$2, and \$3.

Senator COUZENS. I think the psychology is bad and the trouble involved is disproportionate.

Senator BARKLEY. This language was in the old bill and we are simply carrying it along.

Senator COUZENS. I make a motion that we leave out that reference to the \$10 in this amendment.

Senator CONNALLY. I second the motion.

Senator BARKLEY. As far as I am concerned, I do not care one way or the other about it. We followed the statute as it now exists. I do not know how much administrative trouble it would be putting the Bureau to, to pay all of these little claims. It is surprising sometimes how much trouble a man will go to to collect \$4.90 where if it were \$15, he would not go after it.

Senator CONNALLY. The Government goes after these small amounts.

Senator GEORGE (presiding). All in favor will signify.

(The motion was lost.)

Senator COUZENS. I will reserve the right to bring it up again when we have the full committee present.

Mr. KENT. May I request permission of the committee to put in titles on two or three of these new sections that were interpolated, and make any clerical changes that are necessary?

Senator GEORGE. Yes; you can insert the title and make the changes in the numbers of the sections.

If there is nothing else, we will adjourn.

Senator BLACK. Before we leave, I understand that there is some information here which we should have either this afternoon or tomorrow morning, which the committee has heretofore asked for, on certain consolidated reports that Senator Byrd had asked for, and certain packers' information that I asked for at the request of another member of the committee.

Senator CLARK. I move that the committee receive the information at 10 o'clock tomorrow morning.

(Whereupon, at 4:45 p. m., an adjournment was taken until 10 a. m., Thursday, May 21, 1936.)