[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 9

MAY 22, 23, AND 25, 1936

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REVENUE ACT OF 1936

FRIDAY, MAY 22, 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, 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; John O'Brien, assistant legislative counsel, House of Representatives; Lawrence H. Seltzer, assistant director of research and statistics, Treasury Department.

The CHAIRMAN. The committee will come to order.

(There was a general discussion which, by direction of the chairman, was off the record.)

The CHAIRMAN. Mr. Seltzer is now here. Mr. Seltzer, have you the estimate on the proposal no. 7 comprising retained capital-stock tax and excess-profits taxes, repeal of exemption of dividends from individual normal tax, impose 4-percent tax on corporation statutory net income as at present defined, and imposing a 7-percent tax on undistributed adjusted net income of corporations? What would be the estimate on that?

Mr. SELTZER. I had this computed for you on Monday with other provisions inserted.

The CHAIRMAN. You had it with the normal tax increase from 4 to 5 percent, and you had $642,000,000?

Mr. SELTZER. That is right.

The CHAIRMAN. If you leave the 4 percent as it is, what would it be?

Mr. SELTZER. We figured $244,000,000 from the corporation rate raised to 18 percent, and we figured $255,000,000 from the 7-percent tax on undistributed earnings.

Senator BYRD. But that does not tax the tax.

Mr. SELTZER. No.

The CHAIRMAN. We do not want to tax the tax.

Mr. SELTZER. That is what you did in the proposal that I took home with me yesterday.

Senator LA FOLLETTE. You may disregard that.

The CHAIRMAN. Give us now the figures on this proposition here.

Mr. SELTZER. You would get, as I say, $244,000,000 from the corporation tax at 18 percent. That is without any allowance for

small corporations. You would get $255,000,000 from the 7-percent tax on undistributed earnings. You would get $90,000,000 from the normal tax on dividends at 4 percent. That is all you would get.

Mr. BEAMAN. May I just ask one question? I am asking in ignorance. Should that estimate be increased a little bit because of the impulse on corporations to distribute, which is a little bit bigger than it was under proposal no. 7; in other words, they were faced with the proposition of paying 7-percent tax by that or having their stockholders pay a 5-percent tax. Now they are faced with a proposal of paying a 7-percent tax or having their stockholders pay a 4-percent tax. Is that not a little more inducement to distribute and should you not add a little more for that?

Mr. SELTZER. Well, there is a little, a slight added inducement to distribute, but on the other hand there is less corporate income left to distribute because you have raised your corporation rates from 12.5 to 15 percent, to a flat rate of 18 percent.

Mr. BEAMAN. You have that under your proposal no. 7.

Mr. SELTZER. Yes; that is right.

Senator COUZENS. Mr. Beaman is working on the assumption, however, that the added distribution under this proposal will bring more individual income tax. That is something we have not any estimates on.

Senator BLACK. May I ask if these estimates you have given us do not include what the committee agreed on with relation to the exemption of $1,000?

Mr. SELTZER. No.

The CHAIRMAN. How much is that? We have one estimate where that was about $32,000,000, I believe.

Senator CONNALLY. Have you an estimate on what we did yesterday?

Mr. SELTZER. Yes; I have an estimate on that and on nothing else.

Senator LA FOLLETTE. I think it would be interesting to have it.

Senator BYRD. You have a differential now of 7 and 4 instead of 7 and 5, therefore it is some incentive to the corporation to distribute its earnings. To what extent have you allowed for that?

Mr. SELTZER. We felt that the only safe thing to do was not to allow anything for that, and for this reason. The increases in the surtax rates on individual incomes that were incorporated in the 1935 act go into effect for the first time in connection with the calendar year 1936 on individual incomes. Those rates are very substantial, and we did not feel that it was safe to figure on a 7-percent tax of which either 4 percent or 5 percent would be counterbalanced by a tax on the individual, as a sufficient incentive to stimulate additional dividend distribution.

Senator BYRD. Have you considered the retention of the excess profits tax of $168,000,000? Is that considered in your estimates?

Mr. SELTZER. Yes.

Senator BYRD. What is the total then?

Senator CONNALLY. That is not over the present levy; we have that now.

Senator LA FOLLETTE. Are you now giving the committee the estimate on what was done yesterday?

Mr. SELTZER. I would like to, if that is what you wish.

Senator LA FOLLETTE. Let us have it for the record.

Senator BYRD. Should we not get the total of this other first?

The CHAIRMAN. There is $559,000,000 on this, less an estimated $30,000,000 on the $1,000 exemption on $20,000 of earnings.

Mr. SELTZER. In connection with proposal no. 7, we did not compute any allowance for an exception for small corporations.

Senator COUZENS. Did you not in your testimony the other day here estimate that the $1,000 exemption would mean a difference of $30,000,000?

Mr. SELTZER. I said, as I recall it, that in several of the schedules that we had worked out, that that happened to be the loss. I also said, I think, that you cannot make a mechanical transference of a loss under one schedule to a loss under another schedule—any other schedule.

Senator COUZENS. I remember, when we were discussing the question whether we would have a $3,000 exemption or a $1,000 exemption, you made the estimate without regard to what any other taxes might be, and that that exemption would mean a loss of approximately $30,000,000 to the Treasury.

Mr. SELTZER. That is not my understanding. I may have given you that impression.

Senator COUZENS. I do not hold you to it, but that is my recollection.

The CHAIRMAN. I have an idea that in one of these tables it was $30,000,000 or $32,000,000.

Senator LA FOLLETTE. But he made it clear that that could not be transferred.

Senator WALSH. What would it be?

Senator LA FOLLETTE. He must know what the other rates are before he can tell.

Senator GEORGE. It was estimated on the proposal that the chairman suggested here.

Senator BLACK. Is there not one difference in this estimate than the one suggested by Senator Byrd? Did not no. 7 also inlude an increase to 5 percent on individual incomes?

Senator BYRD. Yes.

Senator BLACK. So that if we got no. 7, we would have to eliminate whatever we got from the increase to 5 percent, and we would also have to eliminate the exemptions to the corporations.

The CHAIRMAN. He has eliminated that in his estimate.

Senator BLACK. I did not so understand. On your estimate, did you eliminate the increase of normal tax and put it back at 4 percent?

Mr. SELTZER. Do you refer to the estimate under no. 7?

Senator BLACK. Yes.

Mr. SELTZER. I gave you a rough figure for the difference, I believe, that that would make. I said if the normal tax were cut to 4 percent, the yield would be reduced by $88,000,000, approximately.

Senator BLACK. You are not able to give us even an approximate estimate of the reduction on account of the exemption that the committee voted yesterday?

Mr. SELTZER. I would very much prefer not to. It is not safe to do that.

Senator BLACK. If it were $30,000,000, as has been stated, understanding that you say that that might not apply at all, but if it were

$30,000,000, what would we get simply by the 7 percent that is suggested?

Mr. SELTZER. Perhaps you would get a better idea if I would tell you what happened under your proposal yesterday.

Senator BLACK. I think we could get it later. I am very anxious to get it, but I am anxious to see if any of us could get an approximate idea.

Senator BYRD. It is $559,000,000, and $30,000,000 from that would be $529,000,000.

Senator CONNALLY. Why not let Mr. Seltzer give what he did yesterday?

The CHAIRMAN. That does not take into consideration straightening out section 102, and it does not take into consideration the fact that you put 7 percent on the undistributed income.

Senator HASTINGS. Let us get what the estimate is on what we did yesterday.

The CHAIRMAN. On that, as I gather it, it is $529,000,000 on no. 7.

Senator BLACK. With what left out?

The CHAIRMAN. As I understand, he says that the 18 percent, they figured $244,000,000, imposing the 7 percent on the undistributed adjusted net income would give $255,000,000, and then $90,000,000 on the normal tax which you would get. That gives $559,000,000. Take $30,000,000 off, roughly, for the $1,000 exemptions of the $20,000 of earnings of corporations, the small corporations, would give you $529,000,000.

Senator BLACK. What was the $90,000,000 for?

The CHAIRMAN. Today they do not have a 4-percent normal tax, and this would add $90,000,000.

Senator BYRD. What about strengthening section 102? Have you an estimate on that?

Senator LA FOLLETTE. You cannot expect them to make an estimate unless they know how you are going to strengthen it.

Mr. SELTZER. The proposal I got from you yesterday, and I read it before I left, was—so that that I might make sure that I was not in error—was something like this: Impose an 18-percent tax on corporation statutory net income as now defined, except that corporations with net incomes of $20,000 or less deduct an exemption of $1,000 from net income in arriving at statutory net income. That would automatically exempt that $1,000 from both taxes.

Second, repeal the present exemption of dividends from normal tax on individuals.

Third, impose a 7-percent tax on undistributed adjusted net income of corporations. Adjusted net income is defined as statutory net income plus 90 percent of dividend income. Undistributed adjusted net income is defined as adjusted net income less dividend paid.

On that basis, with no other changes in the law, and assuming that all of the loopholes or possible loopholes that arise in connection with the House bill would be stopped up, you would get, we estimate, $596,000,000.

The CHAIRMAN. There is a difference then between $529,000,000 and $596,000,000?

Mr. SELTZER. I would not like to say that that would be the difference, Mr. Chairman, because it is not possible to make anything resembling an accurate computation of the loss, right out of your head.

Senator LA FOLLETTE. Does that include the retention of the excess-profits and the capital-stock tax?

Mr. SELTZER. Yes; there being no change in that respect. You see, we would get $214,000,000 additional from the corporation income tax. We would get $292,000,000 from the 7 percent tax on undistributed earnings.

Senator CONNALLY. I thought you estimated the other day $244,000,000 on the 18 percent.

Mr. SELTZER. But you have now exempted $1,000.

Senator CONNALLY. Yes. And that would be the $30,000,000.

Mr. SELTZER. And there was $90,000,000 from the normal tax applied to dividends, making the aggregate increase $596,000,000.

The CHAIRMAN. That includes the capital-stock tax being retained?

Mr. SELTZER. Yes; that would represent net increases over existing loss.

Senator WALSH. If you increased that 18 percent to 19 percent, how much more would you get?

Mr. SELTZER. I cannot make a rough estimate.

Of course, I might point out that so far as the corporation tax proper goes, this estimate here shows a yield of about $5,000,000 in excess of that in the House bill on the corporation tax proper, and the normal tax applied to dividends. The House bill got $591,000,000 from the normal tax from dividends and from the taxes on corporations. The balance of the $623,000,000 of the House bill was made up by other measures.

Senator GEORGE. What are those?

Mr. SELTZER. For example, a 10 percent tax levied at the source on dividends paid to nonresident aliens. We figured we would pick up perhaps $4,000,000 in that. Then they had a provision which would encourage the liquidation of personal holding companies. A number of personal holding companies exists that hold cash or other assets abroad, that the House committee was informed would like to dissolve and bring their money home, but they do not want to do so if they have to pay 100 percent of the capital gains that they have realized, if those would be subject to the ordinary taxes.

As I understand it, the House bill provided in effect that these holding companies might dissolve and the assets be distributed, and the capital gains taxed on the same basis as individual capital gains are taxed. The longer the assets were held, the lower the proportion of the gains subject to tax; that is, assets held for more than 10 years, only 30 percent of the gains on such assets would be subject to tax, but Mr. Turney or one of the other lawyers could explain better the precise provisions in this respect than can I.

We would pick up, I believe, about $33,000,000, we estimated, not permanently—not a recurring item, but during the next year, from such a provision.

Senator CLARK. How much do those taxes amount to?

Mr. SELTZER. We thought we would pick up about $33,000,000 from this liquidating provision.

Senator BYRD. And the nonresident aliens, $4,000,000, which makes $37,000,000?

Mr. SELTZER. Yes.

Senator BARKLEY. The liquidating part would be over in 1 year?

Mr. SELTZER. Yes.

Senator BARKLEY. You would not have any more than that?

Mr. SELTZER. That would be over within a year or two. There were some other provisions that resulted in some slight deductions, so that you got a net balance of about $623,000,000 in the House bill.

Senator BYRD. How much of the House bill of $623,000,000 came from the same sources that we are figuring on now?

Mr. SELTZER. $591,000,000.

Senator BARKLEY. Is there any reason why those miscellaneous small items should not be kept in this bill, to which Mr. Seltzer has been referring? Even though it is temporary. I would prefer to have a permanent basis, myself.

Senator GEORGE. My recollection is that we kept the one with reference to the dissolution of personal holding companies.

Mr. PARKER. That is right; we did.

Senator GEORGE. The trouble about it all is that we start here to impose a tax to get so much money without regard to a principle involved.

Senator BLACK. I thought, Senator George, that you had a proposal to do away with that liquidating provision?

Senator GEORGE. No; I carried that over. I think we did reduce the amount applying to the nonresident aliens. Did we not make a reduction there on the House bill?

Mr. PARKER. Just from Canada and Mexico, but we figured that would increase the revenue rather than decrease it.

Senator CONNALLY. Under the plan yesterday we would get $599,000,000?

Mr. SELTZER. $596,000,000 is what our figures worked out to.

Mr. PARKER. Could I ask one question? I cannot understand, Mr. Seltzer, on this proposal C1 that we had the other day, you estimate $641,000,000 additional revenue. That was with 25 percent flat and 40 percent of the dividends paid allowed as a deduction. It did not change the normal tax and contemplated a repeal of the present capital-stock and excess taxes. The plan that was put in yesterday, that you estimate $596,000,000 on, contemplates the retention of the capital-stock and excess-profits tax, and still when I compute the tax of those two plans, compared on the amount of dividend distribution up to 100-percent distribution, I find that the proposal yesterday is more tax, and therefore I am at a loss——

Mr. SELTZER (interposing). You get more tax from which?

Mr. PARKER. I get more tax from the proposal yesterday than I did for the plan C1. I am at a loss to account for that difference.

Senator COUZENS. I cannot either, because there was some $168,000,000, as I recall, lost by the repeal which was proposed in C1 or C2.

Senator GEORGE. I did not understand that myself.

Senator COUZENS. Now it seems to me, if that is not repealed, that this $168,000,000 ought to be added.

Senator CONNALLY. He is only giving the additional revenue. We have that already.

Senator COUZENS. Yes, but that was true with C1 also.

Senator GEORGE. You are proposing to do certain repealing there, and yet on the plan C1 that I asked for an estimate on, they estimated $641,000,000. We were doing away with the capital stock entirely, doing away with excess profits tax entirely, and were not increasing the normal.

Senator CONNALLY. You were doing this, though; you were adding a flat 25 percent with these deductions, which would probably bring in a good deal more money than what we did yesterday.

Senator LA FOLLETTE. Will you just take a look at these figures, the comparison, and forgetting the rates for a minute, see what the actual burden of the tax is? Compare it with no. 7 and the proposal of yesterday.

Mr. SELTZER. You are confining this, Mr. Parker, to the taxes on corporations, are you not, in this comparison?

Mr. PARKER. That table shows the tax on the corporations, yes.

Mr. SELTZER. Well, of course, that probably explains why you were not able to satisfy yourself. You cannot apply rates mechanically and get proportionate revenues, because the form of the tax has an enormous influence upon your revenues. If you make a tax purely contingent upon retention of earnings in business, you do stimulate distribution, and we find when earnings are distributed, the average rates to which they are subjected in our individual income tax schedules are sufficiently higher to produce greater revenues than a flat tax, say, of 18 percent on corporation income would. That is the explanation.

If you recall, Mr. Parker, this plan put a 10-percent tax in effect on retained corporate earnings. It also included, if I recall correctly, a tax on a tax, as does this proposal which we call C3. You had a much more powerful inducement to distribution than you have under C3. That is why we got greater revenues.

Senator COUZENS. It seems to me that we are wasting an indefensible amount of time on a 25, 30, or 40 million dollars of income, instead of trying to do equity. In view of the fact that we are spending billions of dollars without considering $40,000,000, which goes out of the window in 30 seconds, we are spending days and days here and doing injustices to raise $40,000,000. It just seems wholly indefensible. Let us build an equitable tax bill and take whatever revenue we get and see what the experience is.

Senator WALSH. Let us vote on principles first.

Senator HASTINGS. It seems to me we are approaching the thing in an entirely wrong manner by trying to find out how much a certain plan will raise. Let us do the equitable thing to the corporations and see what that will raise, and then go to some other place and find whatever else they insist they must have as their revenue.

(Discussion off the record.)

The CHAIRMAN. I will put the question. All those in favor of fixing an 18-percent flat rate and a 7-percent tax on that part retained by the corporation and undistributed will say "aye."

Senator COUZENS. I do not think they ought to be together.

The CHAIRMAN. All in favor of the first proposition, then, will say "aye."

(The motion carried.)

The CHAIRMAN. The 18 percent provision is carried. Now, all in favor of the 7-percent surtax on that part that is retained by the corporation and undistributed will say "aye."

(Discussion off the record.)

The CHAIRMAN. Will you explain that, Mr. Parker?

Mr. PARKER. In the House bill, you will find that in defining undistributed net income you not only took off dividends paid, but

they took off the tax; that is to say, when you say the amount retained, if you have $100,000, and you are going to pay 18 percent on that, that is $18,000. There is $82,000 left. Everybody is agreed apparently that this 7-percent rate or whatever rate it may be, if you keep it all, that 7 percent for example is going to apply to the $82,000. If it does apply to that, you are going to pay some $5,700 on that.

After you have paid that tax, then you have not got $82,000 left, and therefore you have not got $82,000 retained; you only have less than $77,000 to put into surplus.

The House even went so far as not to agree to that proposition of a tax on a tax, and that is why you have the complicated schedules in the House bill. You wanted to make the amount retained the actual amount that was passed to surplus net.

I assume that the committee, in order to get simplification, and that was explained in the first part of this discussion a number of days ago, that in order to get simplification, that we would not go to the point of that second tax on a tax, which I have just explained.

Senator GEORGE. There would not be the necessity of that so much when you have not got your graduated rates on the undistributed part?

Mr. PARKER. I do not think that would be a necessary refinement, no.

The CHAIRMAN. What this committee wants to do, as I judge it, is that if there is $100,000 made and they first pay $18,000 flat, if they want to distribute of that $25,000, that goes out. Then whatever is retained is the difference between the $25,000 and the $82,000, and on that, 7-percent tax is paid. That is what we want to get at. We want to remove all of these frills.

Senator BYRD. I want that written up and put in the record so that there won't be any question about it.

The CHAIRMAN. Are you clear that that language does that?

Mr. PARKER. I think it is stated in a practical way.

Senator BYRD. Would you mind checking this no. 7, and if there is any change, just dictate it. This has the excess profits. I want to get it down in exact language so that there cannot be any question.

Senator CONNALLY. Let him just state it in plain English.

Mr. PARKER. The rule is simply this. You take your net income as defined in the law. You take off your interest from Government bonds. That gives you what was defined in the House bill as the adjusted net income. Upon that income you are going to levy 18 percent flat tax.

Mr. SELTZER. How about the incorporate dividends under the present law?

Mr. PARKER. I thought I would take that up separately, but I can put that in. You put into your net income, of course, in computing net income, all of the dividends received. They go into net income, and then you deduct from that net income 90 percent of those dividends received. That comes into the computation of your net taxable income. You apply your 18-percent tax, you subtract that from the adjusted net income, and then from that you take the dividends paid, and you apply your 7 percent or whatever rate, upon that.

Senator BYRD. What about the excess-profits tax?

Mr. PARKER. That is in. You have to make an addition to your undistributed net income which is subject to this tax, of the amount of intercompany dividends received, because if you retained those, you are going to pay 7 percent on them. They have to be put in 100 percent into your income that is subject to the undistributed profits tax.

The CHAIRMAN. Does everybody understand that?

Senator BYRD. Does that conform with this proposal no. 7?

Mr. PARKER. That conforms with that.

Senator COUZENS. I want to offer as a substitute, 4 percent instead of 7 percent.

The CHAIRMAN. All in favor of making it 4 percent will say aye; those opposed no.

The noes have it.

Senator BYRD. I would like to vote for 4 percent, but if the agreement which we reached yesterday, which I think is for the best interests of all propositions is to be carried out, I will vote for the 7.

The CHAIRMAN. All in favor now of making it 7 percent on the basis we have discussed as explained by Mr. Parker and by others, will say aye.

(Discussion off the record.)

The CHAIRMAN. It is carried. Now, all in favor of putting a $1,000 exemption on corporations earning $20,000 or less will say aye. The motion is carried.

Mr. BEAMAN. That is strictly understood for the purpose of both the 18-percent tax and the 7-percent tax.

Mr. SELTZER. In these other cases where we have exempted a $1,000 for the small corporations, we have changed the law only in connection with the undistributed income. Here you would allow this income from statutory net income as well? I have to know that.

The CHAIRMAN. As I understand, that was the object, of relieving these small corporations and giving them some benefit.

Mr. SELTZER. You will obviously get a larger loss there than you should under the other proposals.

Senator WALSH. Why not give us the figures both ways?

Senator COUZENS. I am opposed to exempting the $1,000 for the 18 percent.

Senator BARKLEY. I did not understand that the $1,000 applied to the 18 percent; it only applied to the tax on undistributed profits. I may be wrong about that.

(Discussion off the record.)

Mr. SELTZER. You can get substantially the same revenue from the corporation tax from a graduated corporate tax of 12.5 to 19 percent as you get from a flat 18 percent, in which case you might not need this $1,000 exemption for the statutory net.

Senator COUZENS. May I ask if in passing that motion, the committee intended to waive all cushions?

The CHAIRMAN. That was one thing we wanted to get away from, the cushions.

Senator COUZENS. I just wanted to know what you did. I do not disagree with it.

Senator BYRD. My motion yesterday was to exempt from 18 percent normal tax and the 7-percent-retention tax.

The CHAIRMAN. That is on corporations of $20,000 or less?

Senator BYRD. Yes. We certainly cannot increase the little man 5.5 percent and the big corporations 3 percent.

Senator COUZENS. Will you give me an example of that?

Senator BYRD. The present rate starts at 12.5 percent at $32,000. Now we are making it a flat 18 percent. Therefore we increase the little corporation 5.5 percent, and yet the large corporation, which has most of its income above the $40,000 bracket, pays 15 percent, and they only get an increase of 3 percent.

Senator HASTINGS. Suppose they make $10,000. What is the first thing they do?

Senator BYRD. Take off $1,000 up to $20,000 net. I agree with Senator Couzens that it is not a very good practice, and I hate to see an arbitrary line drawn because a corporation with $21,000 might be as much entitled to it as one with $19,000.

The CHAIRMAN. Why can we not agree on $1,000 on corporations of $15,000 or less? It has been pointed out to us that 90 percent of the corporations are $15,000 or less.

Senator COUZENS. You are framing all kinds of laws to make cheats out of taxpayers.

The CHAIRMAN. Those in favor of giving them $1,000, both on corporation tax and supertax, on corporations of $15,000 or less earnings, will say "aye."

(The motion is carried.)

The CHAIRMAN. How much can I safely say now that we will get in revenue?

Mr. SELTZER. You cannot say a thing, safely.

(Discussion off the record.)

Mr. SELTZER. If corporations under this proposal paid the same dollar amount of dividends after the taxes to their stockholders as we had anticipated, that they would do under the budget, the proportion of those cash dividends to their net income after taxes would be some 3 or 4 percent greater than they were estimated under existing law, so that you do get a greater percentage of distribution of earnings to stockholders. We did not feel that we could count upon a greater dollar volume of dividend distribution both because corporations would be paying a larger sum in direct taxes, and because you have a relatively small differential tax on retention of earnings. You tax them 7 percent, but if the earnings are paid out, you collect 4 percent from the stockholders anyhow, so you really have a 3-percent penalty on the retention of earnings, and we did not feel that that penalty could be counted upon to do very much in the way of distribution.

The CHAIRMAN. Is it your idea if we just put no penalty at all, that we would have gotten just as much money out of it, less than $240,000,000 that you say we will get by virtue of it?

Mr. SELTZER. No. We include for this penalty tax $225,000,000. If you did not have that penalty tax, you would not get that $225,000,000.

Senator CONNALLY. You get the money under it, but it does not operate much as a penalty for distribution.

Senator BYRD. Do you not think if you penalize them to the extent of $225,000,000, it certainly ought to have some effect in trying to get rid of that penalty?

The CHAIRMAN. Do you figure we would get as much as if it was 4 percent instead of 7 percent?

Mr. SELTZER. Oh, no.

The CHAIRMAN. It is not influencing forcing it.

Senator LAFOLLETTE. But you get it in the tax. The inducement has not been changed very much as far as the distribution is concerned, but you get the distribution, because if the corporation retains it, you have a higher rate.

Senator GEORGE. What you mean is that the figure of 7 percent on the undistributed earnings will not force out more in dividends actually paid than 4 percent would. I mean, in your figures.

Mr. SELTZER. It is our judgement that it is not safe to count on additional dollar distribution.

Senator GEORGE. You have considered that the distribution would be the same?

Mr. SELTZER. Correct.

(Discussion off the record.)

Mr. SELTZER. What your 7-percent tax does is to give a partial compensation to the Treasury for the revenues that it sacrifices by reason of the retention of earnings, but you do not in the first place of course get a full compensation, and you do not necessarily and in our judgment you cannot count on getting any further distribution of earnings, but from the corporation you collect a partial compensation.

Senator BAILEY. I think that is a matter for our judgment. It is my opinion that 7 percent will stimulate the distribution.

Senator COUZENS. It does not make much difference whether it does or not. We will never know until after the event.

Senator GEORGE: Mr. Chairman, I submitted yesterday a certain suggested amendment—at least the thought was there—to 113 (a) (6). Mr. Alvord has prepared a series of amendments applicable to 112 (b) and 113 which I wish to submit for the experts and have them studied. That is intended to affect this question of liquidation, whether by merger or consolidation or outright liquidation. I would like to hand this to the Treasury experts and have it carefully studied by the time we next meet, or as soon as you can.

The CHAIRMAN. I wish you would have a copy of this also, Mr. Parker.

Mr. PARKER. I have a copy.

(And the same is as follows:)

AMENDMENTS—SIMPLIFICATION OF CORPORATE STRUCTURES

AMENDMENTS TO SECTION 112 (B) (6)

(1) Amend the first sentence of section 112 (b) (6) to read as follows:

"No gain or loss shall be recognized by a corporation upon a statutory merger or consolidation with another corporation, if the corporation is the owner of voting stock (in such other corporation) possessing at least 80 percent of the total combined voting power of all classes of stock entitled to vote (whether or not such merger has the effect of a liquidation of such other corporation), or upon a complete liquidation of such other corporation."

(2) Amend the last sentence of section 112 (b) (6) to read as follows:

"This paragraph shall not apply to any liquidation if any distribution in pursuance thereof has been made before the date of the enactment of this Act; but section 112 (b) (6) of the Revenue Act of 9934 (added by section 110 of the Revenue Act of 1935) shall continue to apply with respect to liquidations initiated under such section, whether or not such liquidations have been completed prior to the enactment of this Act."

AMENDMENTS TO SECTION 113

(1) Amend the first sentence of section 113 (a) (6) by inserting after the word "inclusive" a comma and the following: "other than a transaction described in section 112 (b) (6)."

(2) Amend the first sentence of section 113 (a) (7) by inserting after the words "the same persons or any of them" a comma and the following: "or upon a transaction described in section 112 (b) (6)."

(3) Amend section 113 (a) by adding the following new paragraph:

"(15) *Basis established by Revenue Act of 1934.*—If property is acquired under section 112 (b) (6) of the Revenue Act of 1934 (added by section 110 of the Revenue Act of 1935), then the basis shall be the same as that provided by section 113 of that act."

AMENDMENT TO SECTION 112 (H)

Amend section 112 (h) to read as follows:

"*Definition of control.*—As used in this section the term "control" means the ownership of at least 80 per centum of the total combined voting power of all classes of stock entitled to vote and at least 80 per centum of the total number of shares of all other classes of stock of the corporation."

Senator HASTINGS. Mr. Chairman, I have had submitted to me an amendment on the question of tax-free covenant bond amendment of section 143 of H. R. 12395. I would like to submit this to the Treasury Department and find out their attitude.

The CHAIRMAN. It is all right to submit it to them, but this gentleman appeared before the committee on that matter and has appeared before on the proposition also, and it has not met the approval of any so far, but the experts will take the matter up and give us a response on it.

Senator BYRD. I have one on the same subject.

(The proposed amendments are as follows:)

PROPOSED AMENDMENT TO PENDING REVENUE BILL

(H. R. 12395) Finance Committee Print No. 1)

SIMPLIFICATION OF CORPORATE STRUCTURES—FOREIGN CORPORATIONS

Page 88, after line 4, add the following new paragraph to section 112 (b) of the bill:

(7) No gain or loss shall be recognized if stock or securities in a foreign corporation which, prior to the date of the enactment of this Act, is in control of a domestic corporation, are exchanged by one or more persons solely for stock or securities of such domestic corporation, if immediately after the exchange such person or persons are in control of such domestic corporation.

(H. R. 12395, Committee Print, Comparative Print No. 1)

Beginning on page 143, line 16, strike out subsection (a) (1), (2), and (3), and beginning on page 147, line 13, strike out subsections (d), (e), and (f).

On page 146, lines 13 and 14, strike out the words reading: "in the cases provided for in subsection (a) of this section and except".

On page 149, line 3, strike out the proviso reading: "*Provided*, That in the case of interest described in subsection (a) of that section (relating to tax-free covenant bonds), the deduction and withholding shall be at the rate specified in such subsection."

TAX-FREE COVENANT BOND AMENDMENT TO SECTION 143, H. R. 12395

History: Change recommended by House subcommittee report December 4, 1933.

Existing law requires no withholding of tax on bonds issued after January 1, 1934.

1934 tax bill, as passed by the Senate, eliminated section 143 (a) (1), (2), and (3) and subsections (d), (e), and (f).

Senate amendment not agreed to in conference. Only $10,000,000 in taxes involved.

Effect of amendment: No loss in revenue would result from amendment.

Bondholder would pay tax on interest instead of corporate obligor.

Immense saving of time and expense to banks, corporations, and Bureau of Internal Revenue in administering present provisions.

Would result ultimately increasing Government revenues.

Would dispense with 6,000,000 tax forms and monthly and annual returns by corporations.

Would avoid paying large number of small refunds.

Would reduce enormous detail work of sorting section, Internal Revenue Bureau, and release approximately 100 present employees for more useful tasks.

Would eliminate two items and give more space on face of income-tax return.

House subcommittee found withholding at source is an administrative nuisance.

Reasons supporting amendment: Simplification and reduction in Government administrative expense will result.

Does not affect nonresident alien individuals, foreign partnerships, or foreign corporations.

Treasury Department does not seriously object to proposed change.

SECTION 143. WITHHOLDING OF TAX AT SOURCE

1. In 1934, when the tax bill passed the Senate, section 143 (a) (1), (2), and (3), and subsections (d), (e), and (f) were stricken from the bill. In conference the Senate amendment was not agreed to.

2. The present proposal to eliminate these provisions is covered by the attached amendment, and excerpt showing the bill (H. R. 12395) after amendment.

3. Section 143 requires withholding of 2-percent tax at the source on interest on so-called tax-free covenant bonds of domestic corporations when the interest is payable to a citizen or resident of the United States or a domestic partnership; at 10 percent in the case of a nonresident alien individual or a nonresident partnership composed in whole or in part of nonresident aliens; at 15 percent in the case of a nonresident foreign corporation; and at 10 percent in case the payee is unknown.

4. There seems to be some duplication because section 211 of the bill taxes all nonresident alien individuals at 10 percent of the same items of income specified in subsection (b) of section 143. Section 211 is entirely new. Likewise, there is apparent duplication, so far as the item of interest is concerned, between subsection (a) of section 143 and section 231 (b) in the case of nonresident foreign corporations, the tax being the same, 15 percent, in each section.

5. There would be no loss of revenue if section 143 (a) were eliminated from the bill.

6. Existing law applies the withholding provisions only to bonds issued before January 1, 1934. The 1934 act amended the prior law in this respect. This is the only remant of taxation at the source which remained unrepealed since 1916.

7. The House subcommittee report of December 4, 1933, recommended "that this system of withholding a tax on tax-free covenant bonds be entirely discontinued. * * * It is an administrative nuisance and requires a payment of many small refunds. Simplification and reduction in administrative expense can be secured by the elimination of this section. No loss in revenue will result from the change."

8. The provision requires the filing of over 6,000,000 tax forms and a tremendous amount of detail work by corporations and the sorting section of the Bureau of Internal Revenue. The corporate obligor is required to "deduct and withhold" the tax, and the individual bondholder must report the interest in his taxable income and then take credit for the 2-percent tax withheld at the source, if he is liable for tax at all. If the corporate obligor has paid the tax, and the bondholder files no return, or does not take credit for the tax paid at the source, a refund of the tax must be made to the corporation.

9. Total taxes colected is about $10,000,000 per annum. If it were not for the provisions of section 143, corporate obligors, especially in the cases of railroad bonds issued prior to 1913, would fulfill the bond obligation by paying the full amount of interest without deduction, which is done in any event, and only where there is an express covenant to pay 2 or 4 percent of the Federal normal tax is there an enforceable contract right on the part of the bondholder against the corporation.

10. In the Senate Finance Committee report on the 1934 bill it was stated that "from the Government viewpoint there seems no more reason for withholding in the case of bond interest than in the cases of salaries, dividends, and other items." The amendment proposed does not affect withholding as to nonresident alien individuals, nonresident partnerships, or foreign corporations. It is believed advisable that withholding at the source should be retained in respect to foreigners.

11. Section 147 of the bill enables the Bureau to obtain full information as to the payment of interest to citizens or residents of the United States, whether the interest payment is for $1,000 or less, and section 148 (a) could be amended to cover interest as well as dividend payments.

12. Under the pending bill, if stockholders are to pay normal and surtaxes on dividends, then bondholders should be required to pay the tax on interest received. There is no normal or legal obligation or public policy for intervention of the Government in the enforcement of a private contract right.

13. Undoubtedly simplification in administration would result by eliminating this anomalous provision of withholding tax at the source on bond interest.

Mr. BEAMAN. While you are on this question of rates, can we not settle a few more questions before you take up the miscellaneous things?

The CHAIRMAN. Yes.

Mr. BEAMAN. The committee voted yesterday afternoon to apply the 18-percent flat rate to all of the corporations which under the House bill were exempted from the undistributed profits tax and subjected by the House bill to a 15-percent flat tax—banks, insurance companies, corporations in receivership, and a few others.

Assuming that you are going to adhere to that decision, what was not covered yesterday and what we want to be certain on is: Do all of those people for the purpose of that 18-percent tax get a $1,000 exemption, or do they not?

Senator COUZENS. Oh, yes; there are no exceptions on that.

Senator BARKLEY. Does that $1,000 apply to those that get the 15-percent rate?

Mr. BEAMAN. We are going to get an 18-percent rate now.

Senator BARKLEY. Did we not make an exception as to banks?

Senator GEORGE. We did not impose any surtax on them. But the $1,000 exemption would apply to any corporate earnings of $15,000 or less.

The CHAIRMAN. Is it the view of the committee that that shall apply to all institutions such as named, corporations in receivership, banks, insurance companies and so forth, where they earn $15,000 or less, that they should have a $1,000 exemption? That is the view of the committee without objection.

Senator CLARK. Do I understand you are putting the flat tax at 15 instead of 18?

The CHAIRMAN. It is 18 percent.

Mr. BEAMAN. I wanted to be absolutely sure of that. The banks and insurance companies and all of these people that are taxed 18 percent flat, that, like the ordinary corporation, include in their income subject to the 18-percent tax, the 10 percent of the dividends received from other corporations.

The CHAIRMAN. The same principle. Is there anything else, Mr. Parker?

Mr. PARKER. No.

The CHAIRMAN. Mr. Beaman, do you want to ask any other question?

Mr. BEAMAN. No.

The CHAIRMAN. Will you please get just as soon as you can, Mr. Seltzer, an estimate of just what revenue would come in from that source?

Senator BYRD. I would like to ask Mr. Parker—it has been called to my attention that in the consolidated returns that railroads have some privileges that motor-vehicle carriers do not have. The motor vehicle people think that they ought to be in the same class with the railroads. I am not very familiar with it, but is that the situation?

Mr. PARKER. There has been that argument advanced.

Senator BYRD. Do you think that the motor carriers ought to be?

Mr. PARKER. In 1934, when we took the consolidated-return privilege away from our corporations except railroads, we allowed railroads to file consolidated returns. I think it was through a misunderstanding, but I think this committee meant to include street railroads. The department ruled that street railroads were not entitled to file consolidated returns. The House bill has amended that section and they have included with steam railroads, electric railroads.

Senator BYRD. Do you think motor carriers should be put in? They are in direct competition.

Mr. PARKER. That is a question of policy.

The CHAIRMAN. Do you mean interstate buses?

Senator BYRD. They are doing exactly the same business as the railroads and the street cars.

Senator CLARK. There is a difference between them in that railroads are regulated and the busses are not.

The CHAIRMAN. They will be under the law.

Senator GEORGE. We might let them go along another year and see how they come out.

Senator HASTINGS. The reason for the railroad provision, as I recollect it, was that the corporate form was such that they could not very well separate them. I do not know whether that is true with the bus companies.

Senator COUZENS. That was one reason, but the primary reason was that under different State charters they were compelled to take out separate incorporations. That is not true of the bus companies, and I do not think they should be included, at least at this time.

The CHAIRMAN. Let us get the expression of the committee. All in favor will say "aye"; those contrary "no."

The "noes" appear to have it. The suggestion is rejected.

Senator LA FOLLETTE. Mr. O'Brien called my attention to the fact that we did not take any action yesterday afternoon in the matter that was brought up by the secretary of the Federal Reserve Board. Do you want to take that up now?

Senator GEORGE. That might affect the rates. Let us see what that is.

Senator LA FOLLETTE. Mr. O'Brien has the section of the 1933 Banking Act which is really the crux of the whole thing. You need not read the definition, Mr. O'Brien, but read what the law requires them to do.

Mr. O'BRIEN. The banking act of 1933 provides that after 5 years after the enactment of that act, every holding company affiliate which is defined in section 1 of the act shall possess and shall continue

to possess during the life of such permit—that is, the permit issued to it by the Federal Reserve Board—free and clear of any lien, et cetera, readily marketable assets other than bank stock in an amount not less than 12 percent of the aggregate par value of all bank stocks controlled by such holding company affiliate, which amount shall be increased by not less than 2 percent per annum of such aggregate par value until such assets shall amount to 25 per centum of the aggregate par value of such bank stocks; and (2) shall reinvest in readily marketable assets other than bank stock all net earnings over and above 6 per centum per annum of the book value of its own shares outstanding until such assets shall amount to said 25 per centum of the aggregate par value of all bank stocks controlled by it.

Senator GEORGE. What is the suggested amendment?

Mr. O'BRIEN. The amendment suggested by the Federal Reserve Board proposes to exempt from both the corporation tax and the undistributed tax the amounts required to make up this requirement—to purchase the assets other than bank stock.

Senator LA FOLLETTE. Are they not paying the flat corporation tax now?

Mr. O'BRIEN. Under this bill they are not included within the definition of a bank, and therefore would be subject to the flat corporation tax just as they are under the present law, and under this bill, not being defined as banks, they would be subject to the undistributed profits tax.

Senator LA FOLLETTE. As I understand it—and this need not go on the record.

(Discussion off the record.)

The CHAIRMAN. Do you understand just what was the result of this discussion?

Mr. O'BRIEN. Yes.

The CHAIRMAN. Will you draw it up then in proper form and submit it?

Senator GUFFEY. In my State we have some institutions which do not accept deposits, but they do only a trust business.

Senator WALSH. We have the same thing in my State. Banks which now do a general deposit account business are exempted. Those same banks do a large trust business, but they come under the classification of a general account business. What we want to do is to put the banks that do more of a trust business than an account business in the same category, because they are in competition with each other.

The CHAIRMAN. Mr. O'Brien is going to submit something on this.

Now, what else is there that we have not taken up?

Mr. BEAMAN. The method of treating foreign corporations is the most important.

Mr. PARKER. I have been waiting to get in touch with Mr. Kent. I was hoping that we could bring in a plan that would be clear and would not provoke a great deal of discussion.

(Discussion off the record.)

Senator BAILEY. Mr. Chairman, I have copies of an amendment here.

(The amendment referred to is as follows:)

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

AMENDMENT Intended to be proposed by Mr. Bailey to the bill (H. R. 12395) to provide revenue equalize taxation, and for other purposes, viz: At the end of title IV insert the following:

TITLE V—AMENDMENTS TO PRIOR ACTS

SEC. 701. TAX ON CERTAIN OILS.

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

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

SEC. 702. PROCESSING TAX ON CERTAIN OILS.

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

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

SEC. 703. CONSTRUING PROVISION.

The amendments made by sections 701 and 702 shall not be construed as repealing section 402 of the Revenue Act of 1935, and such section shall be construed as applying to products of section 601 (c) (8) of the Revenue Act of 1932, as amended by this Act, and section 602½ (a) of the Revenue Act of 1934, as amended by this Act.

Change title V to title VI and change sections 701, 702, and 703 to 801, 802, and 803.

Senator BAILEY. The amendment purposes to perfect what we undertook to do in the 1934 act respecting the importation of fats, oils, and oil producing seeds competitive with our products. Fats and oils of certain types are interchangeable now one with the other.

The object of the amendment is to place all of these oils on the same basis that the oils were placed upon in the 1934 act. This is not a new matter; it simply stops the holes that were driven in the 1934 act. That is to say, it places certain taxes, processing taxes and also tariff taxes on the importation of these oils, but we did not place them on all of the oils and the interchangeable oils.

For instance, we did not get tallow. They are shipping tallow into this country at this rate. Prior to the passage of the 1934 act it was 264,000 pounds, but since then it is 265,000,000 pounds, so the act is ineffectual wholly by way of substitution of other facts and oils for those fats and oils upon which we placed the taxes.

To make the statement complete, I must say that we went beyond that, and as the act was drawn, we included fish scrap and fish meal. They are not oils. To that extent, the bill is not precisely in line with the 1934 act.

Senator COUZENS. Are the rates the same?

Senator BAILEY. Yes, the rates are the same. I have a statement here on linseed oil, which is the principal oil used for the drying of paints. Under the Smoot-Hawley tariff, that carries a duty of 4.5 cents a pound. My amendment makes uniform the import tax on all other imported drying oils that are interchangeable with and substituted for linseed oil.

That is the whole principle of the bill, simply to expand the 1934 act so as to take in these substitutes for those oils upon which we placed the tax.

Here is the effect of it. Unless we do that, cottonseed will go down in price. Cottonseed went up at first under the influence of the 1934 act, but as these substitutes came in from abroad, cottonseed started down, and it is selling now for about 50 percent of what it was selling for.

You take the same thing in other oils. Take the soybean. We are developing the soybean at a tremendous rate. The soil conservation act is planting soybeans all over this country. That is the vegetable or plant they are using for soil conservation, and it produces the very finext oil and of world-wide use. But what use will those soybeans be to us if the oriental and other countries ship it in at a price at which it would not pay for us to press them? That is the principle of the bill.

You can read the bill and see what they are, whale oil, fish oil, marine-animal oil, tallow, inedible animal grease, and fatty acids of any of the foregoing oils or fats, et cetera.

I have the statistics here on the whole subject, and shall be glad to place them in the record to show the imports, and also to show an estimate here which I did not make, but made from data gathered by the Department of Commerce——

Senator CLARK (interposing). Who made it?

Senator BAILEY. It is made by the advocates of this bill, which is the Farm Bureau. I will come to that. These estimates show that we will get additional revenue of about $25,000,000. That would be lifting the price here but not preventing the importation of these articles; they will continue to come in, but simply enable our people to get a better price for them.

I would not have introduced this measure at this time but for the fact that I had petition which I did not think could well be resisted by the Congress or anybody else. Here is the National Cooperative Milk Producers Federation, in a letter to myself, and in behalf of the dairy farmers of America.

I also have a letter from the Federal Farm Bureau which I want to go into the record.

Here is a letter addressed to Senator Harrison from E. H. Cooley, of the Massachusetts Fisheries Association.

Senator WALSH. The fishing interests are very much in favor of it.

Senator BAILEY. We have fishing interests in North Carolina. They are telling me that they will have to go out of business, they will cease to operate their plants, they will let the fish that are off our coast go wherever they may.

Senator BYRD. Virginia fishermen say the same thing.

Senator BAILEY. Rather than get them and crush them for the simple reason that the Japanese and the Scandinavian people are catching fish, and under their low-wage scale and standard of living,

are shipping the oil over here or the fish scrap, at a price that will not permit our people to operate. By way of illustration of that, I have seen 100,000 pounds of mullets brought into Moorhead City and carried back to the sea and fed to the sharks simply because you could not get a cent a pound for them. That is the situation.

I do not think I would bring forward a tariff measure at this time. I think my position on those matters is perfectly plain. I have never hesitated to vote for the protective measures for the farmers. I think they are entitled to it. I read what Mr. Chester Davis said yesterday in the paper after his trip through France. He said that we have lost our market abroad and we will never get it, the farmers will never get it.

If that is the case, we have to preserve their market at home. There is no use for us to sit down here and let the other people sell farm products all over this country. But I am bringing the amendment forward solely by way of saying that it is not a new matter but it is a correction and the fulfillment of what we undertook in the 1934 act, and I think it will be a revenue-producing measure.

Senator COUZENS. Do you know why it was not considered in the House, Senator?

Senator BAILEY. Yes; it was not considered, and these gentlemen tell me that they brought it before the chairman of the committee. He hesitated to bring it up on the ground that he was afraid it would introduce other tariff matters; that there would be riders put on for all sorts of things.

Senator LA FOLLETTE. It is my understanding that the Ways and Means Committee early in their deliberations felt that they would not consider any subject matter that was not mentioned in the President's message, and therefore this, along with other things, was excluded from their deliberations.

Senator WALSH. As I understand, Senator Bailey, you are not changing rates, but you are including substitutes that were not defined in the original law?

Senator BAILEY. That is right; we are just putting the rates that we put in the 1934 act on these substitutes. I think it is a very timely and beneficial measure, and I really believe it will add a great deal to our revenue. I would not offer it except I believe it is a necessity, and I have all of the farmer organizations and, in addition to that, the fisheries, and I am going to ask the committee to adopt the amendment.

Senator COUZENS. May I ask Senator Bailey why he repeats the rates; why he does not just put in these articles and put them under the old act without repeating the rates in the bill?

Senator BAILEY. I did not draw it. It was presented to me by the Farm Bureau. But I do not care about the mechanics of it. All I say is that we should put these substitutes under the same rates as we put the original articles. I think you will find that that is what was done.

Senator LA FOLLETTE. I suppose there is some relationship probably that has to be expressed in this amendment—I am just assuming there is some relationship to these rates—that has to be expressed in this amendment, between the articles or the products that were taxed in the 1934 act and these substitutes. In other words, I do not know, but you probably could not put the same rate on inedible animal

grease as you put on the article for which it is a substitute, but you would have to take into account the conversion costs and all of that.

Senator BAILEY. That is right.

Senator CONNALLY. Mr. Chairman, I am in sympathy with the Senator, but I have an amendment to his amendment that covers certain other aspects of this oil situation that I would like to present to the committee and have a vote on it along with this amendment.

It will be remembered that when we first put on this vegetable-oil or coconut-oil tax, the processing tax with regard to the Philippines, that we provided that the revenues arising therefrom should be paid to the Philippine government. They have attacked that in the courts on the ground that it was not authorized and that we have not the power to levy a tax for the benefit of the Philippines.

So I propose here now an amendment that so much of that section relating to payment of the tax that is derived to the Philippines be repealed, and we just leave it straight out. Then if we want to appropriate in the appropriation bill, that same money to the Philippines, we can do it so as to obviate that attack. That attack goes to all of the foreign vegetable oils that are now in the law.

The CHAIRMAN. Is it a fact that some court did hold that?

Senator CONNALLY. I understand some subordinate trial court held adversely to the act.

Senator GEORGE. It has not reached the Supreme Court. The amendment to which Senator Connally refers was inserted by Senator Norris. He made the amendment on the floor of the Senate and it was not carefully considered—the legal effect of the thing—on the body of the amendment that we were trying to put in.

The CHAIRMAN. What you ought to do, it seems to me, Senator Connally, is to keep these two propositions separate. I understand what you are trying to do is to cover a loophole because of the court's ruling.

Senator CONNALLY. That is one aspect of it, but there is somewhat more. I have in mind giving both of these amendments to the experts and the drafting people, and let them work out something in harmony, because there is one of mine that sort of overlaps Senator Bailey's in that I do include some flower oil and tallow, and you have them both in the bill.

Senator BAILEY. I have them both in mine.

Senator CONNALLY. I do not want any conflict.

Let me call attention to one other matter in respect to this amendment, section 2. As I remember, there was an exemption of these oils for the manufacture of tin plate. I do not see any reason why any particular industry should be exempted from the use of these oils when everybody else has to pay.

Section 3 also refers to section 402 of the revenue act relating to compensatory tax on the products of certain oils.

My thought was that since these were related, they ought to be turned over to the drafting men, and if we adopt them both, let them modify the language so as not to have any conflict. That is why I bring it up now.

Senator BAILEY. All I want is the objective, and if the committee approves, I am perfectly willing to turn my amendment and Senator Connally's and this data, which I wish to go into the record, to the experts and have them report to us on Monday.

Senator GUFFEY. I have more protests against Senator Bailey's amendments in my office, which I would like to present to the committee before it is voted on, than all the other protests about the whole tax bill. I do not have them available this morning, but I would like to have the opportunity of presenting those protests. I should like to suggest to Senator Connally that he consider this removing the tax on inedible coconut oil——

Senator CONNALLY (interposing). No; that is the whole thing. That goes into the making of soaps, and that is where the big tax is.

The CHAIRMAN. The State Department thinks that to enlarge this greatly may affect some of these agreements. Senator Copeland has a bill in to repeal that part of the present law pertaining to whale oil, except sperm oil, and he has been very insistent on that.

There is one part of Senator Bailey's amendment that I hope that he will eliminate, and that is tung oil. Down in my country they have recently been exploiting the tung oil trees and they are really making quite a success of it. They have called me up and they are fearful now to put any tax on the proposition or a tariff, because it might be prejudicial to them. Tung oil goes into varnishes and paints.

Senator BAILEY. Tung oil is classified as a very fine carrier for the soybean oil.

The CHAIRMAN. I did not know that it came into competition with it at all. Tung oil goes into varnishes; that is its great use.

Senator WALSH. Why are the domestic producers against the tariff on tung oil?

The CHAIRMAN. They are just afraid that it will cause them to start to use something else instead of tung oil. They are trying to build up the tung-oil industry now.

Senator BAILEY. You misapprehend me, Mr. Chairman. I am willing to strike out tung oil on the ground that the use of tung oil aids the use of the soybean oil.

Senator GEORGE. Mr. Chairman, it has really resulted in producing revenue, and with this amendment it will produce very much more.

Senator CONNALLY. Importations have fallen very little, but there has been a good deal of revenue.

The CHAIRMAN. In view of what Senator Guffey said, can we take this up Monday morning?

Senator BAILEY. Just allow me to present the amendment and then present the data, without reading it. There are certain briefs and letters which I wish to go into the record. I will be back here Monday and we can settle the question on Monday.

Senator HASTINGS. Senator Guffey does not insist on your holding up the vote. He wants to put his protests in the record.

Senator CLARK. I do not desire to delay the vote on the matter in view of the fact that Senator Bailey wants to get away. I merely say that I wanted to be recorded against the amendment. This is an effort, as I see it, to turn the revenue bill into a tariff bill by picking out certain specified items for increasing the tariff. That is all it amounts to. It has always been my view, and until last year it was supposed to be the settled view that the deplorable situation of agriculture in the United States was caused by high protective prohibitive tariffs, and it has been maintained by occasionally throwing a little sop through these so-called farm organizations to agriculture to delude them into going along with the generally high protective theory.

As far as I am concerned, I would much rather take the view of Mr. Davis as to the abandonment of our foreign markets for farm products and accept the view of Secretary Hull and the announced view of the administration, who I think know a great deal more about it than Mr. Davis; therefore I am not willing to hand out a little sop of this sort to contribute to the fastening further on the people of the United States of the high protective tariff system, and resulting as I believe, in a great detriment to agriculture. I have no desire to go into it fully at this time. I voted against the excise tax in the 1934 act and I do not desire to say anything more, but I do desire my vote recorded against it.

The CHAIRMAN. I have brought to the attention of the committee the Copeland amendment with reference to whale oil.

Senator HASTINGS. Is there to be a vote on this today?

Senator CONNALLY. Why not dispose of it and let the experts frame the amendment?

Senator COUZENS. I would like to see the protests. It is very illegitimate to try to pass these tariff acts without any hearings, to pass it without being heard. I am perfectly willing to have this bill reported, and then between the time it is reported and the time it is taken up on the floor, let us have some hearings. Senator Capper has a proposal which does something else to some other commodity. Senator Guffey has stated that he has all kinds of protests, and I am getting protests. And I do not know the merits of the thing.

Senator BARKLEY. I have put off and denied all of my constituents the right to come here, by telling them that we were not going to take up anything except this bill, that we were not going to open it up to tariff legislation or for considering present excise taxes that are being collected. I have a lot of friends in Kentucky who want to come here to reduce the taxes on some of the things which are now taxed, and I told them that we were not going to consider any of those things. If you are going to open up this bill for tariff legislation, there are just as equally meritorious reductions on some of the present excise taxes. I think it is very unwise to open this thing up for the benefit of anybody who wants the tariff changed or the excise changed.

Senator COUZENS. I think we will make better progress if we do not try to vote on it today.

The CHAIRMAN. I think you had better put this over until Monday, and in the meantime let the draftsmen get up a combination amendment.

Senator LONERGAN. Can you tell us to what extent the Philippines are competitive, Senator Bailey?

Senator BAILEY. No; I could not tell you to what extent. I have here the data showing the increase in the volume of the imports generally of these substitutes against which we laid the tariff in the 1934 act.

I wish to repeat just one thing. We are not trying to write here a tariff act; we are simply trying to perfect one that we wrote in 1934. I am not bringing any new matter in, but I am simply stopping up the holes that we drew in the best of faith, which worked for a time and which was rendered useless by substitutes, and to such an extent that there has been a tremendous increase in the revenue. If we

put the taxes on, we will save the bill that we passed in 1934. That is all it does. It does the work which we originally intended to do.

Senator CONNALLY. It is just really filling up the gaps.

Senator BAILEY. I should like all of this data placed in the record, Mr. Chairman.

The CHAIRMAN. Very well.

(The matter referred to is as follows:)

Imports of tallow, certain oils, oil-bearing seed and oil cake, 1931–35

Material	Duty	1931	1932	1933	1934	1935
Tallow	½ cent per pound	1,671,973	501,585	238,562	42,813,299	245,725,434
Perilla oil	Free	13,285,492	16,525,139	22,776,858	25,164,203	72,327,854
Perilla seed	do					
Tung oil	do	79,311,155	75,922,209	118,759,963	109,787,088	120,058,817
Tung nuts	do					
Olive oil (sulphured)	do	36,925,256	45,909,339	40,468,388	86,165,879	83,797,218
Olive oil (inedible)	do	12,045,441	11,759,045	12,909,541	9,670,342	19,743,452
Hempseed oil	1½ cents per pound					
Hempseed	Free	8,596,689	6,374,852	4,538,464	12,981,949	12,443,131
Rape seed	do	8,027,037	10,747,605	13,629,936	9,323,796	29,515,220
Rape seed oil	do	947,933	609,437	1,464,841	1,975,841	3,348,295
Kapok seed	Free, pound				14,617,641	12,655,000
Kapok oil	Free					
Sesame oil (inedible)	do	832	424	4,312	600	11,088
Sesame oil (edible)	3 cents per pound	62,586	71,330	58,468	72,798	
Sesame seed	Free	139,596,870	19,182,095	42,630,809	22,326,588	147,470,944
Caster bean	½ cent per pound	103,214,816	83,166,166	118,100,250	92,839,588	77,048,901
Flaxseed	35 cents per bushel, 56 pound.	[1] 14,480,474	8,038,867	13,825,163	14,170,002	17,559,662
Cottonseed oil	3 cents per pound				9,157,392	166,678,414
Soybean cake	1/10 cent per pound	39,620,454	36,558,700	67,241,318	60,207,438	107,463,044
Linseed cake	0.003 cent per pound	18,808,000	22,388,384	24,950,459	16,151,278	20,979,647
Fish meat and scrap	Free	38,447	21,805	26,526	35,672	27,851
Copra cake, Philippine Islands.	do		7,494,756	20,335,431	72,008,617	102,399,208
Copra cake, other	0.003 cent per pound		3,263,605	859,700	1,551,848	1,388,187
Cottonseed cake	0.003 cent per pound	1,532,800	979,241	7,004,025	44,891,090	59,743,572
Tankage (tons)	Free	22,746	21,130	25,007	13,499	30,851
Palm nuts and kernels	do	34,815,619	28,699,751	14,918,052	8,509,404	50,072,548

[1] Bushels.

In testimony favoring the excise taxes contained in sections 602 and 602½ of the 1934 revenue bill witnesses estimated the annual revenue from these taxes at $30,000,000. It is generally believed that this figure will be exceeded by a most substantial amount for the fiscal year ending June 30, 1936. Most conservative estimates by these same witnesses show an estimated annual revenue from the proposed Bailey amendment of well over $30,000,000, making a total revenue from tax on foreign fats and oils of approximately $65,000,000, with the tax being widely distributed and a hardship on none.

The purposes of this bill are in the main corrective. Due to the various improvements, experiments and developments, it has been definitely determined that fats and oils of certain types are interchangeable one with the other. For example, among others, whale oil, fish oils, cottonseed oil and soybean oil by hydrogenation can be hardened to any consistency desired and utilized in the manufacture of soaps or other commodities where a hard fat such as tallow is required.

Under sections 602 and 602½ certain of these oils are taxed at 3 cents per pound. It is one of the purposes of the proposed legislation to place on the same tax basis all imported oils and fats which are interchangeable and substitute one for the other so that none will be shown preference.

Linseed which is the principal drying oil consumed in paints carries a duty under the Smoot-Hawley bill of 4½ cents per pound. It is the purpose of the Bailey amendment to make uniform the import tax on all other imported drying oils that are interchangeable with and substituted for linseed oil.

Fish meal is used principally in the manufacture of poultry feed about 10 percent to the ton. Domestic meals, due to improved methods in the taking, the preserving and the reduction process, are much lower in oil content than imported meals. Hence, the tendency to rancidity is reduced to a minimum. Unprincipled feed mixers naturally use the cheaper material, usually resulting in a heavy loss in chicks to the farmer consumer.

It is for this reason that this tax has the active support of the various farm organizations.

Prior to the passage of the Smoot-Hawley bill fish scrap and fish meal were protected under the tariff acts.

This tax, as was the case in the 1934 revenue bill, will not curtail imports but will raise the price level of domestic competing products, increase wages and employment, as well as aid most materially the American farmer.

Unless sections 602 and 602½ of the 1934 revenue act are made effective by the passage of the Bailey amendment it will no doubt follow that importation of these tax-free oils and fats will increase and thereby render the provisions of the 1934 Revenue Act ineffective and the revenue from this law will decrease most materially.

(The tabulation referred to is as follows:)

Imports of tallow, certain oils, oil-bearing seed and oil cake, 1931–35

Material	Duty	1931	1932	1933	1934	1935
Tallow	½ cent pound.	1,671,973	501,583	238,562	42,813,299	245,725,434
Perilla oil	Free	13,285,492	16,525,139	22,775,858	25,164,203	72,327,854
Tung oil	do	79,311,155	75,922,299	118,759,963	109,787,088	120,058,817
Olive oil (sulphured)	do	36,923,256	45,909,339	40,463,888	36,165,879	33,797,218
Olive oil (inedible)	do	12,045,441	11,759,045	12,909,541	9,670,342	19,743,452
Hempseed oil	1½ cents pound.					
Rape seed oil	Free	947,933	609,437	1,464,841	1,975,841	3,348,295
Kapok oil	do					
Sesame oil (inedible)	do	832	424	2,317	600	11,083
Perilla seed	do					
Hempseed	do	3,595,689	0,374,852	,838,464	12,981,949	12,443,131
Rape seed	do	8,027,037	10,747,605	13,629,930	9,323,706	20,515,220
Kapok seed	Free, pounds				14,617,641	12,655,000
Sesame seed	Free	139,596,870	19,182,095	42,630,809	22,326,588	147,470,044
Tung nuts	do					
Fish meal and scrap	do	38,447	21,805	26,526	35,672	27,851

THE NATIONAL GRANGE,
Washington, D. C., May 9, 1936.

Hon. JOSIAH W. BAILEY,
Senate Office Building, Washington, D. C.

DEAR SENATOR: It has come to my attention that you intend to offer an amendment to the pending revenue bill imposing excise taxes on certain imported oils and oil-bearing seeds for the benefit of domestic producers of oils and fats. Such a step is needed to make more fully effective sections 602 and 602½ of the Revenue Act of 1934. Your proposed amendment could not fail to benefit producers of cottonseed, peanuts, soya beans, beef, sheep, hogs, and dairy products.

The excise taxes imposed by the act of 1934 have not only brought considerable revenue into the Treasury, but they have greatly benefited the American producers of oils and fats.

We, therefore, approve your proposed amendment and trust that it may be adopted.

Very sincerely yours,

FRED BRENCKMAN,
Washington Representative.

AMERICAN FARM BUREAU FEDERATION,
Washington, D. C., May 8, 1936.

Senator JOSIAH W. BAILEY,
Senate Office Building, Washington, D. C.

MY DEAR SENATOR BAILEY: You may be assured that the American Farm Bureau Federation is 100 percent in favor of the amendment which you intend to present to the pending revenue bill, to place certain excise taxes on a list of oils and fats.

The American Farm Bureau Federation for 10 years has stood firmly on the principle that an imported and competitive product, such as the oils and fats listed in your amendment undoubtedly are, should, before they enter the commerce of our nation, pay an excise or an import duty, so that when they are sold in our markets they must move at prices which will permit American producers of our own oils and fats to survive.

In fact, your amendment, in a brief way of considering it, is nothing more or less than stopping some leaks and plugging up some holes in the excise taxes which were secured in 1934 on a too limited list of oils and fats.

Anything which I can do to help you in this effort will be gladly done, if you will let me know when I can be most effective.

Very respectfully,

AMERICAN FARM BUREAU FEDERATION,
CHESTER H. GRAY, *Washington Representative.*

THE NATIONAL COOPERATIVE MILK PRODUCERS' FEDERATION,
Washington, D. C., May 15, 1936.

Hon. JOSIAH W. BAILEY,
Senate Office Building, Washington, D. C.

DEAR SENATOR BAILEY: Our attention has been called to your amendment to the pending tax bill in which you levy import and processing taxes upon certain designated oils and fats which come into this country in competition with oils and fats produced by American farmers.

It has been an historic principle of the National Cooperative Milk Producers' Federation, which represents more than 52 dairy cooperative associations with a farmer membership of more than 360,000 dairy farmers, to protect the home market for the American farmer.

Insofar as oils and fats are concerned, the first step in this program of protection to the American producer was taken in the Revenue Act of 1934 when taxes were placed on a fairly comprehensive list of foreign fats and oils.

These taxes have been of immense value to the American farmer in maintaining a price level for domestic fats and oils under which reasonable returns could be obtained for domestic fats and oils. The taxes have not acted as an embargo as indicated by the imports of these fats and oils since the taxes were levied.

Your bill will be a further and valuable step in the program of American agriculture to obtain a well-rounded tax structure on all foreign fats and oils. Your amendment will substantially improve the price level of domestic fats and oils while at the same time the rates are so reasonable that they will not act in any way as an embargo on imports.

Your amendment will produce substantial revenue and will at the same time stimulate the production of fats and oils in the United States to the end that we may gradually approach that time when American farmers will be in a position to supply all of the fats and oils needed in the American market.

Your amendment will be of great value to all American producers of oils and fats and will also be of substantial value to the dairy farmers of this country by protecting them against the influx of cheap substitutes from abroad.

We are enclosing herewith study made by our statistical department showing the present rate of tax or duty on these oils, the suggested rates in your amendment, and the amount of revenue which might be expected from imports of these fats and oils, provided your amendment is adopted.

Yours very truly,

THE NATIONAL COOPERATIVE MILK PRODUCERS' FEDERATION,
CHARLES W. HOLMAN, *Secretary*.

Comparison of revenue returns from the present and proposed new rates based on 1935 imports

Article	Excise tax effective as in amended sec. 601(c)(8) in Revenue Act of 1932 (1)	Excise tax as proposed by Mr. Bailey (2)	Additional tax as proposed by Mr. Bailey (col. 2 less col. 1) (3)	Imports for final year of 1935 in Monthly Summary of Foreign Commerce (4)	Revenue received by tax now in effect (estimate) (5)	Revenue proposed amendment by Mr. Bailey would yield (estimate) (6)
	Cents per pound	*Cents per pound*	*Cents per pound*	*Pounds*		
Whale oil (except sperm oil)	3	3	0	3,076,422	$92,293	$92,293
Fish oil (except doc, cod-liver, and halibut-liver oils)	3	3	0	1,245,483	37,346	37,364
Marine animal oil	3	3	0	(1)		
Tallow	0.5	3	2.5	245,850,922	1,244,255	7,465,528
Inedible animal grease	0	3	3	(1)	Free	
Fatty acids, etc., from any of the foregoing oils (see proposed amendment)	0	3	3	(1)	Free	
Inedible:						
Olive oil (as classified under par. 1732 of Tariff Act of 1930)	0	4.5	4.5	53,540,670	Free	2,409,330
Sesame oil (as classified under par. 1732 of Tariff Act of 1930)	0	4.5	4.5	11,088	Free	499
Perilla oil	0	4.5	4.5	72,327,864	Free	3,254,754
Sunflower oil	3	4.5	1.5	37,051,732	1,111,552	1,667,328
Tung oil	0	4.5	4.5	120,058,817	Free	5,402,647
Rapeseed oil	0	4.5	4.5	25,447,042	Free	1,145,117
Kapok oil	0	4.5	4.5	(2)		
Hempseed oil	1.5	4.5	3	(2)		
Fatty acids, etc., of any of the foregoing oils (see proposed amendment)	0	4.5	4.5			
Fish scrap and fish meal	0	.625	.625	62,386,240	Free	389,914
Other marine animal scrap and meal	0	.625	.625	(1)		
Perilla seed	0	2	2	(2)		
Hempseed	0	2	2	116,681,757	Free	2,333,635
Rapeseed	0	2	2	29,515,220	Free	590,304
Sesameseed	0	2	2	147,470,944	Free	2,949,419
Kapok seed	0	2	2	12,656,625	Free	253,133
Tung nuts	0	2	2	(2)		
Total					2,485,464	27,991,265
						2,485,801
Potential additional revenue from proposed increased rates						25,505,801

[1] Not available.
[2] No imports.

Compilations based on Monthly Summary of Foreign Commerce and Division of Foreign Trade Statistics.

WASHINGTON, D. C., *May 15, 1936*.

Senator PAT HARRISON,
Senate Office Building, Washington, D. C.

DEAR SENATOR: As requested in our conversation this morning, I submit herewith:

The domestic producers of oils and fats found themselves unable to operate under conditions existing immediately prior to 1934, when Congress placed an excise tax of 3 cents per pound on competing interchangeable imported oils.

To summarize the results of this tax:

1. Contrary to claims of opponents, there has been no decrease in importation of oils and fats; in fact, Government statistics prove a general increase.

2. Foreign producers, instead of being injured, have been definitely benefited also by increased unit prices.

3. Domestic producers of oils and fats have been materially benefited, and enabled to open idle plants and give employment to thousands of workers.

4. Despite the claims that products made from these oils and fats would reach prohibitive prices, there has been little or no increase in the price of these products and markets have been broadened.

5. Scientific study and invention have made oils and fats interchangeable, hence untaxed oils and fats have been imported and substituted for those included in the Revenue Act of 1934, thus defeating the purpose of the legislation and resulting in destructive competition, which has again lowered the prices of domestic oils and fats until bankruptcy again threatens a widely diversified industry.

6. The logical solution is to tax the remaining oils and fats of the interchangeable group as provided in the amendment introduced by Senator Bailey.

7. Revenues to the Government amounting to more than $60,000,000 annually will accrue from this source, yet not possess the usual characteristic of a tax since there is definite benefit to practically all producing areas of the whole Nation, yet a detriment to no one since interchangeable oils and fats are produced by dairymen, fishermen, livestock growers, soya-bean growers, flax-seed growers, the growing tung-oil industry, and the growers of cottonseed, as well as every butcher and retailer who benefits from the sale of the waste trimmings from his meat counter, a byproduct usually yielding enough to pay the rent of the independent grocer.

8. Soil conservation is furthered since there is a potential industry for the farmer in raising soya beans.

9. Poultry raisers using fish meals are seriously harmed by inclusion of cheap, rancid imported meals now used in commercial feeds. Hence, the farm groups endorsing this excise tax on fish meal as proposed in Senator Bailey's amendment.

10. *Reason for proposed rate.*—Linseed oil now carries a tax of 4½ cents per pound. All competing drying oils should carry the same rate.

Coconut, palm, and other soap oils carry a tax of 3 cents per pound. Logically competing oils as provided in Senator Bailey's amendment should bear the same rate. The soybean and cottonseed oils are cared for in the Tariff Act of 1930 at similar rates.

11. *Summary.*—The Bailey amendment but corrects the omissions that time and experience have demonstrated to have been made in the Revenue Act of 1934. It should be remembered that any one of these interchangeable competing imported oils, if left out of the revenue bill of 1936, will destroy this necessary protection to domestic industry and lose a revenue more than $60,000,000 annually to the Government.

I have made this brief—very brief—as you suggested but shall be glad to get further data for you if desired.

Thanking you for all that you have done for my industry and for your great interest, I am as always,

Very truly yours,

E. H. COOLEY,
Massachusetts Fisheries Association,
Fish Pier, Boston, Mass.

THE NATIONAL DAIRY UNION,
Washington, D. C., May 8, 1936.

Hon. JOSIAH W. BAILEY,
Senate Office Building, Washington, D. C.

MY DEAR SENATOR: I am taking this occasion to let you know the deep interest which is felt by the members of our organization in the amendments which have been prepared and placed in your hands for introduction concerning the internal-revenue taxes and import taxes on various tropical and other fats and oils.

I have been familiar with the preparation of this amendment and as you know have given much attention to this particular proposition ever since it came to public attention by the most effective action taken by Congress in 1934.

The amendment passed in 1934 placing the 3-cent tax on these various oils was one of the most beneficial pieces of legislation for American agriculture which was passed by that session of Congress, benefits running into the hundreds of millions of dollars by direct increases in the values of all domestic fats and oils.

Experience has shown, however, that certain interests in the United States have been able to secure substitutes and in other ways avoid and escape these taxes, so the present amendment has been prepared with extreme care to prevent these evasions, place equal taxes on the substitutes, and thereby to carry out the intent of Congress as expressed in the 1934 enactment.

In particular we are interested in the dairy industry in having an adequate tax placed upon sunflower oil and sesame oil in refined form which can be used in the manufacture of oleomargarine as a substitute for butter and in place of coconut oil which is already subject to the tax.

I am authorized as a representative of the dairy industry to say to you that your efforts in behalf of this proposed amendment to the oils and fats tax enactment will be of great value to the entire dairy industry of the United States and we are supporting you to the best of our ability in your effort to have this amendment enacted into law as a part of the tax bill which is now under consideration.

Yours sincerely,

THE NATIONAL DAIRY UNION,
A. M. LOOMIS, *Secretary*.

BRIEF EXPLANATION OF SENATOR BAILEY'S AMENDMENT

These two brief amendments will correct minor defects which experience has shown to exist in the provisions for the fats and oils excise taxes enacted by Congress as a part of the Revenue Act of 1934.

Experience has disclosed that numerous evasions of these taxes were found to be possible and that substitutes for the taxed oils have been developed by foreign producers, imported in considerable quantity, and their use free from tax has made these amendments necessary.

EVASIONS CORRECTED

Certain of the taxable oils have been imported in fully processed form, thus escaping the processing (excise) tax. This is corrected by transferring these oils from the excise tax paragraph to the import tax paragraph. This includes sunflower oil and sesame oil.

FATTY ACIDS INCLUDED

Certain users in the United States evade the processing tax on certain oils by doing the processing abroad and importing the resultant fatty acids for use in this country, such fatty acids being held by the Internal Revenue Bureau not subject to tax. This is corrected by specifying in the amendment that the fatty acids, salts, etc., derived from the fats and oils shall be equally subject to tax.

CERTAIN NEW OILS INCLUDED

Experience has also disclosed that certain fats and oils were imported last year in large quantity which were not included in the taxable list in the 1934 act and that this volume of new importations has seriously affected domestic producers also reducing the importation of the taxable oils and thus reducing the expected revenues. The more important of these oils have been added by these amendments to the taxable list, notably, tallow and animal greases, inedible olive oil and kapoc oil.

DRYING OILS INCLUDED

Rapeseed oil, perilla oil, hempseed oil, and tung oil have been added to the taxable list. This will materially increase the revenue and assist domestic producers of drying and semi-drying oils, particularly soybean oil, fish oil, linseed oil, and domestic tung oil.

The oil seeds, the raw materials from which the taxable oils subject to the import taxes are produced have also been included at the reduced rate of 2 cents per pound. This includes perilla seed, hempseed, rapeseed, tung nuts, sesame seed, kapok seed and sunflower seed.

PROTEIN FEEDS PROTECTED

Fish and marine animal meals and cake (the byproducts of the fish and marine animal-oil industry) are added to the taxable list with a nominal tax of five-eighths cent per pound. This will insure the continuance of the domestic production of these important plant and animal protein feeding materials. It would be

most unfortunate to lose these industries and become dependent upon foreign sources.

PREVAILING LOW PRICES OF DOMESTIC FATS AND OILS MAKE THESE CHANGES IN THE LAW NECESSARY

A survey of the important domestic fats and oils industries shows that, due to the increasing imports of untaxed oils during the past 14 months, prices have again dropped to a point in most cases below cost of production. Prices are still declining. This is the urgent and controlling reason for favorable action on these amendments and their inclusion in the present revenue bill.

The present prices of important domestic fats and oils compared with the prices of the same oils 1 year ago are as follows:

	May 1, 1935	May 1, 1936		May 1, 1935	May 1, 1936
Coconut oil	5¾	4⅛	Corn oil	8⅞	8⅛
Palm kernel oil	6⅛		Peanut oil	9⅜	8¼
Palm oil	4 1/10	4⅛	Soybean oil	9	6½
Tallow	7¼	5¾	Cottonseed oil	9¼	8
Hydrogenated fish oil	6½	5¼			

AMERICAN FISHERIES ASSOCIATION, COOPERATIVE,
Suite 1004, Raleigh Hotel, Washington, D. C.

RE TAX ON CERTAIN IMPORTED OILS BY MODIFICATION OF SECTION 602 OF REVENUE ACT OF 1934WHICH WILL INCREASE PRESENT ANNUAL REVENUE OF $30,000,000 TO APPROXIMATELY $60,000,000 AND MAKE FULLY EFFECTIVE WITHOUT DISTURBING IMPORTS AND GREATLY BENEFITING DOMESTIC PRODUCERS OF FATS AND OILS. THESE FACTS ARE FULLY SUBSTANTIATED HEREIN

Prices of domestic-produced fats and oils, including dairy products, during the period 1930 and early 1934 declined to their lowest level in history. During that period rendered lard was sold as low as 2 cents per pound; cottonseed oil at 3 cents per pound; rendered tallow at 2 cents per pound; fish oils at 10 to 12 cents per gallon; and others in like proportion. These prices were the direct result of immense imports of duty-free foreign-produced interchangeable oils and fats.

The Revenue Act of 1934 provided taxing certain of these foreign-produced oils for Revenue. Opponents of this claimed—

1. That the imposition of the tax would not in any way tend to advance the price of domestic fats, oils, and dairy products.
2. That the tax would not produce revenue.
3. The imposition of this tax would prohibit the importation of the oils taxed.

The first contention is answered by the immediate response in the advance of prices of domestic fats, oils, and dairy products. Lard advanced to 12 cents per pound; cottonseed oil advanced to 10 to 11 cents per pound; tallow to 7½ cents per pound; fish oils to 36 cents per gallon with all other domestic fats, oils, and dairy products advancing in proportion.

2. As to the revenue feature, we submit that the first year the tax was operative, July 1, 1934, to June 30, 1935, the revenue amounting to $24,817,948.24 (see p. 1 attached hereto), while for the 8-month period from July 1, 1935, to February 29, 1936, a revenue of $19,884,622.29 has resulted. At this rate for balance of year the revenue should approximate $30,000,000. (See. p. 2 attached hereto.)

3. That the tax has not curtailed the imports but has tended to advance the price of domestic fats and oils.

We submit the importation figures on coconut and palm oil for the past 5 years. (See p. 4 attached hereto.) These oils were and still are imported in far greater quantities than any of the oils covered under the act of 1934. For example: The imports of palm oil duty-free in 1933 were 287,516,000 pounds, and these imports increased with the tax of 3 cents per pound to 296,502,000 pounds in 1935. Coconut oil imports free of duty were 612,428,000 pounds in 1933, against 639,500,548 pounds in 1935, with tax of 3 cents per pound.

The tax as enacted in 1934 while most beneficial, nevertheless, left certain leaks which should be remedied immediately. For example: A processing tax of 3 cents per pound was applied to sunflower oil. The results were that sunflower

oil was processed and packed ready for sale when imported and thus the tax was evaded. From July 1, 1934, to June 30, 1935, there were 33,625,463 pounds of sunflower oil imported but approximately 23,890,798 pounds were processed abroad and thus evaded the processing tax. The loss in revenue to the United States Treasury in this one instance amounted to approximately $716,723, and has had a most depressing effect on domestic cottonseed oil with which it comes in direct competition recently. (See p. 3 attached hereto.)

Another feature of the act of 1934 that calls for immediate correction is the item of tallow. During 1933 there were but approximately 238,000 pounds imported, but by reason of taxing imported oils and greases interchangeable with tallow and not providing for imported tallow the imports of this product by 1935 increased to 245,000,000 pounds—over 1,000 percent increase.

From the attached page 5 it is apparent that imported drying oils, such as perilla, hempseed, tung, etc., are increasing in imports to the extent that they are displacing domestic drying oils such as soy bean (see p. 6), fish oils, linseed, etc. These oils should be placed on a parity with linseed oil which now bears a duty of 4½ cents per pound.

In order to make the tax fully effective, we would recommend that the taxes as listed on page 5 (attached hereto) be provided and that the processing tax on Sunflower oil be changed to an excise tax.

This we believe would at least double the revenue now accruing from the tax and maintain a price level at which domestic fats, oils and dairy products can be manufactured at a fair margin of profit.

Respectfully submitted,

AMERICAN FISHERIES ASSOCIATION, COOPERATIVE,
By THOMAS H. HAYES, *Chairman of the Board.*

P. S.—See page 7 for the story of the American fisherman.

PAGE I. *Tax receipts from sec. 602 and 602½ of Revenue Act of 1934 (period July 1 1934–June 30, 1935)*

[Compiled from figures furnished by Mr. Asmuth, Department of Commerce]

Sec. 602: Whale and fish oils	$460, 857. 12

[Figures given by Mr. M. E. Hoyt, Internal Revenue Department]

Sec. 602½:		
Sesame oil	$583, 100. 84	
Palm oil	4, 406, 400. 00	
Palm kernel oil	851, 098. 75	
Sunflower oil [1]	292, 130. 03	
Mixtures	186, 906. 79	
Coconut oil:		
Other than Philippine Islands	22, 503. 22	
Combination mixtures	262, 023. 37	
Philippine Islands	17,142, 472. 20	
Other United States possessions	138, 103. 52	
Floor tax	472, 352. 40	
		24, 357, 091. 12
Total		24, 817, 948. 24

[1] Figures on this page from United States Chamber of Commerce and the Department of Commerce, Division of Foreign Trade Statistics.

PAGE II. *Tax receipts from section 602 and 602½ of Revenue Act of 1934 (period July 1, 1935 to Feb. 29, 1936)*

[Compiled from figures furnished by Mr. Asmuth, Department of Commerce]

Sec. 602: Whale and fish oils	$631, 485. 99

[Figures furnished by Mr. M. E. Hoyt, Department Internal Revenue]

Sec. 602½: Total revenue derived for period July 1, 1935 to Feb. 29, 1936, from imports under above section (sesame oil, palm oil, palm kernel oil, sunflower oil, mixtures, cocoanut oil; all classes)	19, 203, 136. 30

PAGE III. *Sunflower oil* [1]

	Pounds
Imports from July 1, 1934, to June 30, 1935	33, 625, 463
Tax paid as per figures of Internal Revenue Bureau	9, 737, 665
Processed abroad and tax under sec. 602½ evaded	23, 890, 798

This tax evasion amounted to $716,723.94 in fiscal year July 1, 1934, to June 30, 1935.

PAGE IV

[Figures from U. S. Department of Commerce, Division of Foreign Trade Statistics]

	Pounds
Palm oil imports:	
1929	261, 816, 000
1930	287, 494, 000
1931	258, 144, 000
1932	216, 166, 000
1933	287, 516, 000
1934	155, 530, 000
1935	296, 502, 000
Coconut oil imported for United States consumption (copra imports figured at 63 percent oil):	
1930	692, 982, 000
1931	614, 310, 000
1932	534, 788, 000
1933	612, 428, 000
1934	566, 319, 790
1935	639, 500, 548

PAGE V. *Recommendations to make fully effective secs. 602 and 602½ of Revenue Act of 1934*

Material	Present duty	1935 imports	Proposed duty	Revenue
		Pounds		
Perilla oil	Free	72, 327, 864	4½ cents per pound	$3, 254, 753. 88
Tung oil	do	120, 058, 817	do	5, 402, 646. 77
Olive oil:				
Sulphured	do	33, 797, 218	do	1, 520, 874. 81
Inedible	do	19, 743, 452	do	888, 455. 34
Rape-seed oil	do	3, 348, 295	do	150, 673. 27
Kapok oil	do	(4)	do	(?)
Hempseed oil	1½ cents per pound	(4)	do	(?)
Sesame oil (inedible)	Free	(4)	do	(?)
Tallow	½ cent per pound	245, 850, 922	3 cents per pound	7, 375, 527. 66
Fish meal and scrap	Free	[3] 27, 851	½ cents per pound	348, 137. 50
Perilla seed	do	(5)	2 cents per pound	(?)
Tung nuts	do	(5)	do	(?)
Palm nuts and kernels	do	50, 072, 548	do	1, 001, 450. 96
Hempseed	do	12, 443, 131	do	248, 862. 62
Rape seed	do	29, 515, 222	do	590, 304. 40
Sesame seed	do	147, 470, 944	do	2, 949, 418. 88
Kapok seed	do	12, 656, 000	do	253, 100. 00
Potential additional revenue estimated from proposed increased rates as above				23, 984, 206. 09

Figures from U. S. Department of Commerce, Division of Foreign Trade Statistics.

[1] No imports, seed free.
[2] Nominal imports, seed free.
[3] Tons.
[4] No imports, no tax on oil.
[5] No imports, oil free.

PAGE VI. SOYBEAN

In respect to soil conservation, our Government is encouraging the growing of legumes.

Perhaps the most profitable, if properly protected from the competition of foreign produced competing and interchangeable oils will be the soybean from which soybean oil is extracted.

Thirty years ago soybean was not grown in the United States. Today there are over 5,000,000 acres under cultivation and it is the fourth cash crop in the United States.

"It may be grown on any land that is normally considered good for corn and the nodules in the root of the bean enrich the nitrogen content of the soil in much the same manner as does alfalfa," according to Dr. Donald M. Marvin, economist of the Royal Bank of Canada.

The same authority further states: "Until a few years ago soybean oil was considered unsatisfactory for use in high-grade paint, but recent experiments at the University of Illinois overcame the chemical difficulties in this connection and in 1934, 10,000,000 pounds of soybean oil were used by the paint industry in the United States. In varnish and lacquers soybean oil is the principal base. The Ford car is finished with soybean lacquer, and the Ford Co. is erecting a $5,000,000 plant in Detroit to make soybean products. In soaps, glues, linoleums, and rubber substitutes the ingredients of the soybean have come to be of predominant importance." And still further he adds: "The soybean brings a return to the farmer roughly equivalent in value per acre to that which is obtained from wheat."

At the present time numerous soybean crushing mills are in operation in various sections where the bean is cultivated to take care of the oil extraction.

If this very desirable industry is to flourish in the United States, it is obvious that it must be protected from the low-priced cheaply foreign produced interchangeable oils and fats.

PAGE VII. THE AMERICAN FISHERMAN

On the Atlantic coast and in the Gulf of Mexico, a species of fish, known as "menhaden", are found in great quantities during certain seasons of the year. On the Pacific coast a type of fish used for many similar purposes, known as the sardine or pilchard, are very plentiful.

The taking of these types of fish for reduction purposes is a most important industry of very long standing on the Atlantic, Pacific, and Gulf coasts. The principal volume productions are fish oil, fish meal, and fish scrap.

Vessels are of course employed in taking the fish and transporting them to the shore plants for reduction; these shore plants being located at strategic points along the coast and labor is by far the greatest expense item, both in the actual taking as well as in the reduction process.

The principal commercial value of these types of fish oil is in connection with the manufacture of oil cloth, linoleum, soap making, paint and varnish, tanning, and allied industries. Fish scrap is of major utility for poultry feeding and the fish scrap contributes exceedingly valuable nitrogen elements to the fertilizer trade.

During the period 1921 to 1930 average price of crude fish oil varied approximately between 45 to 50 cents per gallon; but due to the generally disturbed and depressed conditions from 1930 on, which, resulting in a flood of competing products of foreign origin of interchangeable and substitute oils and fats, the price of domestic fish oils in 1933 had declined to a price level approximately 10 to 12 cents per gallon.

After the passage of section 602 of the Revenue Act of 1934, crude fish oil prices advanced to 36 cents per gallon, which is distinct evidence of the beneficial effect of this act as a measure of partial relief. When making this law more effective as proposed herein, there would appear to be no question but that this commodity will regain its proper price level. Results of section 602 in this industry would immediately increase the wages, the building of new vessels and plants, and restoring to operation vessels and plants which have hitherto been idle.

Prior to the enactment of the Smoot-Hawley bill, fish meal was protected by tariff but for some unknown reason it was omitted from that bill and the price started to decline rapidly from that time because foreign fisheries, in most cases, subsidized by their governments, overwhelmed our markets with cheaply produced meals in competition. (Fish meal is dried ground fish scrap.) From 1921 to 1930 this material sold for $60 to $80 per ton but ruinous foreign competition forced this price to $30 per ton in 1933 and this price was far below the cost of domestic production for a fine protein feeding meal of this class.

It is absolutely essential that the tax herein proposed be applied to fish scrap, fish meal, and marine-animal meals if this branch of American fisheries is to survive and such a measure will again permit the reemployment of the American fishermen at a full fair wage through the operation of all vessels and shore plants many of which still are idle and closed.

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

(Whereupon, at 12:30 p. m., a recess was taken until Saturday, May 23, 1934, at 10 a. m.)

REVENUE ACT, 1936

SATURDAY, MAY 23, 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, Clark, Lonergan, Black, Gerry, Guffey, Couzens, LaFollette, Hastings, and Capper.

Also present: L. H. Parker, chief of staff, Joint Committee on Internal Revenue Taxation and members of his staff; C. F. Stam, counsel, Joint Committee on Internal Revenue Taxation; 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; Prew Savoy, special attorney, Department of Agriculture; L. H. Seltzer, assistant director of research and statistics, Treasury Department.

The CHAIRMAN. The committee will be in order. The Secretary of Agriculture called me up this morning about the title of the bill. There is one change to be made that they think is very important. Explain that, Mr. Savoy. It was a change of date, I think.

Mr. SAVOY. That matter was touched on the other day.

Senator KING. Let me have it explained de novo, because I do not think I heard about that.

Senator LA FOLLETTE. Is that the one about making it 30 days after the passage of the act?

Mr. SAVOY. The Secretary suggested if you made it 30 days after the passage of the act the secondary processors will compel the processors to pass the tax on to them, and instead of having 2,000 wheat millers, for example, you will have several hundred thousand bakers, cake makers, and so forth.

Senator LA FOLLETTE. Have you considered the fact that it is very much easier to collect it from those people than it is from the processors, beause you have got a very much less difficult computation and administration problem to tackle? Now we talked that all out with the Treasury experts and it is their idea, and I think you ought to have this in mind in commenting on it, as I understanl it, it is their idea that while it will increase numerically the number of people that they have to deal with, that because of the simpler problem with regard to these other people it may not entail any greater amount of work in the Treasury Department in collecting the tax. Have I stated that right, Mr. Turney?

Mr. TURNEY. Yes. We think, as to the administrative problem, that it works both ways. It will unquestionably increase the number of taxes, but some of those taxpayers, especially in the cotton textile industry, will present a much less difficult problem than you have in the original processors. Of course where the reimbursement goes to a secondary processor your problem is just about the same.

Senator LA FOLLETTE. As I understand it, it is your feeling that the greatest part of the increase will not be from the secondary processors.

Mr. TURNEY. That is probably our guess; yes.

Mr. SAVOY. That, of course, is anybody's guess. In looking at it from the standpoint of the molasses and sugar industry as contrasted with cotton, it is obvious you would have thousands of processors and it would be quite an accounting problem to determine it.

Senator LA FOLLETTE. What do you suggest to meet this situation?

Mr. SAVOY. We have two things to suggest. One is going back to March 3, which is the date on which the President announced this windfall tax.

Senator LA FOLLETTE. You know there are a lot of cases where it is going to be very unfair to them. Take the case that Senator George mentioned, this concern somewhere that he is familiar with; they had all their accountants work on it and they just could not get their tax out by the 3d of March.

The CHAIRMAN. Senator George, you understand what we are getting at, do you not?

Senator GEORGE. No, sir.

The CHAIRMAN. The Secretary of Agriculture called me up this morning and he said the secretary of the Millers' Association had come in and he said he thought this was going to raise a good deal of trouble.

Senator LA FOLLETTE. This changing the date, Senator, from March 3, as it was in the House bill, to 30 days after the act becomes effective.

The CHAIRMAN. Mr. Savoy, you may discuss the matter with Mr. Turney, and let us see if we cannot agree on some statement about it. We have already passed on it, but if it is a glaring mistake I am willing to consider it.

Mr. TURNEY. Senator, it is purely a question of policy, where, on the one hand, you have the undoubted unfairness in a large group of cases by sticking to this March 3 date, and on the other hand you have the possibility that to some extent the administrative burden of this thing will be greater by putting in the amendment, and possibly—nobody knows—a greater loss of revenue.

The CHAIRMAN. How much loss of revenue?

Mr. TURNEY. We did not anticipate that there would be any great loss of revenue.

The CHAIRMAN. You do not think that there would be?

Mr. TURNEY. No.

Mr. SAVOY. The second suggestion was with respect to this administrative problem. About 95 percent of the tax was paid by 1,400 taxpayers and about 4,700 taxpayers paid over $1,000. Now, if you allowed a credit of, say, $500 against the tax you would eliminate

of the 73,000 taxpayers as much as perhaps somewhere between 60,000 and 65,000.

Senator GEORGE. What do you propose to do, Mr. Savoy? Why don't you talk plain?

Mr. SAVOY. The proposal was to go back to March 3.

Senator GEORGE. I know, but here are the facts: Here is a processor who, immediately after the court's decision, hired all the available auditors he could get and went to work, and before they could work out the exact amount that was due to all of its customers with whom it had contracts, and those with whom it did not have contracts, because it wanted to be fair and treat them all alike, it had to do it from a commercial point of view, then on March 3, when it spent all its money, and before it could get out the checks, why, you propose to come in here now and say it shall not be allowed any refund. You are putting an 80 percent windfall tax on a legitimate, honest concern. You are going to say, "You pass it on, every bit of it, to the customers by March 3 or you will not get a dime's credit on your taxes."

I will not defend it. I do not care what any department thinks about the matter of policy, because after all the tax that the people of his country must pay is imposed by me and the other members of this committee, and the Senate and Congress, and not by the Secretary of Agriculture.

The CHAIRMAN. I merely wanted to bring that to your attention because the Secretary was very much exercised about it.

Mr. SAVOY. Yes, there would probably be a few cases of hardship in cotton.

Senator GEORGE. There will be innumerable cases of hardship, where they were trying to act perfectly honest. If we would meet that in a perfectly frank and open way we could write a very much simpler tax bill, one that a citizen would know what it was about, would know what he was doing. The man who is going to pay the money in this country certainly ought to have a tax bill which he could read himself and understand it.

The CHAIRMAN. Now, Senator Murray has a matter that he wants to bring to the attention of the committee.

Senator MURRAY. I received a letter from Mr. McLeod of the Missoula Mercantile Co., which I ask you to consider in your deliberations.

The CHAIRMAN. The letter may be inserted in the record and given consideration.

(The letter referred to is as follows:)

MISSOULA MERCANTILE CO.,
Missoula, Mont., May 18, 1936.

Hon. JAMES E. MURRAY,
Senate Office Building,
Washington, D. C.

Re Revenue bill of 1936; item: Floor stock taxes.

MY DEAR SENATOR MURRAY: I understand that the present revenue bill as passed by the House provides for a refund of floor stock taxes based on taxable merchandise on hand January 6, 1936, the date the Agricultural Adjustment Act became invalid. There is a proposed amendment to the effect that this refund should be based on the floor tax paid by the merchant as of August 1933 when the processing tax went into effect.

I am opposed to the bill as now written and am in favor of the proposed amendment for several reasons.

First. It would be difficult for all retailers to attempt to establish the taxable content of merchandise on hand as of January 6, 1936. The larger concerns could probably do this because their records are more complete, but the smaller merchants, in particular, would have innumerable difficulties in trying to prove to the Government the exact amount of their taxable merchandise on hand as of January 6, 1936.

Second. By adopting the amendment there would be no uncertainty about the processing tax paid as of August 1933 because that was a sum actually paid to the Government and figured on a stock on hand and the whole matter was a matter of record filed with the Government. By using the August 1933 return there would be less chance for fraud.

Third. I believe failure to adopt the amendment will cause a financial loss to the smaller retailers who have not been able to keep proper records and would cause a greater amount of confusion and uncertainty among the merchants and would cause the Government to incur an exorbitant clerical and printing expense which would not need to be incurred because it already has possession of the August 1933 returns.

I am calling this matter to your attention because I understand the proposed amendment to this bill is now before the Finance Committee of the Senate and will soon be acted upon.

If you thing I am right will you do what you can to see that this amendment is adopted?

Sincerely yours,

C. H. McLEOD.

SENATOR KING. Mr. Chairman, before leaving that, I just passed to Mr. Kent the letter to which I called your attention, complaining about the floor stock taxes, and so on. Have you any light to throw on this, Mr. Kent?

Mr. KENT. All I want to say is this letter is right in light with communications we have been receiving from other groups recently protesting to any proposal to go back to 1933 and indicating that many groups are very much satisfied with the way in which the thing was worked out in the present bill. They favor a clear-cut provision for refunding taxes on January 6, 1936, stock.

Senator KING. January 4.

Mr. KENT. Or January 4; yes.

Senator KING. This writer states that the industry is now in a state of turmoil and uncertainty bordering on chaos with reference to the question of processing tax refunds from millions of customers, and from these customers to their respective customers, and so forth. There is no end of trouble, and so forth.

Senator BARKLEY. It is exactly what we have done except we made it January 5.

Mr. KENT. It really does not make any difference, because the 4th is Saturday and the 5th is Sunday.

Senator COUZENS. May I bring up another matter? I brought it up when there were very few present the other day. It is with respect to page 241, where no claim shall be allowed in an amount of less than $10. I think there is perfectly silly legislation. If a man has a claim of $11 he can get it back, but if he has a claim of $9 he cannot get it back. My view is there will be hundreds of thousands of little claims for $3, $4, $5 that will never be made.

I would like to eliminate that clause from the bill. It seems a silly legislative policy in the first place, and then it precludes a man who may have a $9 claim from getting it back, and the man who has a $11 claim would get it back.

Senator BARKLEY. It may be silly, but it is along the line of all the jurisdiction legislation that limits the rights of people according

to the amount involved. I think the Department ought to spend as much time on a 30-cent claim as on a $300 claim.

Senator COUZENS. As a practical matter do you think they will file such silly claims?

Senator BARKLEY. I do not know. I have come to the view that a lot of people will do almost anything to get something back from the Government. They will spend three times as much as is involved to get it back. I do not care what you do with it. It just means a lot of work over a lot of little chicken feed.

The CHAIRMAN. That was the reason for this provision.

Senator COUZENS. I understand the reason for it, but I think it is silly to say that if a man has a claim for $11 he can get it, and if he has a claim for $9 he cannot get it. I am convinced, from the practical application of this thing, that there will be hundreds of thousands of these claims to which the Treasury seems to object, that will never be made because of the cumbersome method of making the refunds.

Senator LA FOLLETTE. I do not think the objection came originally from the Treasury. It was in the law.

Mr. KENT. That is right. In drafting the bill, Senator Couzens, we tried to following as closely as we could the question of what rights there would have been had the processing taxes been terminated by administrative proclamation rather than by adverse judicial decision, and, of course, we regarded it as primarily a question of policy. The mere cost of handling a small claim, even though no attempt is made to have any sort of an investigation, is considerable.

Senator COUZENS. I will make the motion anyway.

The CHAIRMAN. I had a communication from the secretary of the Retail Dry Goods Association, advocating just what you wish to do.

Senator COUZENS. I did not get any letters about it, but it does seem so unfair and unreasonable to adopt such a legislative procedure.

Senator BLACK. Mr. Chairman, before the motion is put, as a member of the subcommittee I would like to add to what Senator Barkley said, that we asked for the reason for that provision, because I do not think it impressed either one of us in the beginning, and my recollection is we were told that under the tobacco law that a limitation of $20 was put on it, if I am not mistaken. That is what we were told. I know we were told there is a limitation, and someone said it is $20.

I will say now that there would be thousands who would be denied their claims and there would be a discrimination, and I think it is unfair.

At the same time, if we are going to open it up to all, it would seem to me that it should be made uniform in connection with the other refunds, and if I had anything to do with the original passage of it, I would have favored giving a man the right to the refund whatever it is.

Senator KING. May I ask you a question, Senator Black?

Senator BLACK. Yes.

Senator KING. Don't you think that by mentioning $10 you are calling the attention of a large number of persons who might have small claims to the fact that they can get a claim if it is above that

amount and they will present their claims, whereas if there is no mention made in the law at all the effect would be that people would say, "It is a small amount; I am not going to bother with it." By mentioning $10, you are going to invite everybody who has got a claim for $10.01 to file a claim.

Senator BLACK. I think they will practically all file them, Senator, because my observation has been that some lawyer will get busy and get an agreement out of all of them, practically, as they do in other things, and it might be wise to consider that in connection with the amendment.

I want to say, personally, that I believe a man ought to get what is coming to him, whether it is $2, $10, or $1,000, but the committee did not take any decided view, except when we found it had been the uniform custom to limit, we did not feel justified in asking for a discrimination in this case. That is the way I understood it.

The CHAIRMAN. Without objection the vote by which that part of the amendment was agreed to is reconsidered.

Now we will just vote a just vote on it. Those in favor of the suggestion of Senator Couzens say "Aye." Those opposed "No." The "Ayes" seem to have it, and the "Ayes" have it, so the draftsmen will write it up accordingly.

Senator GERRY. Mr. Chairman, I have an amendment here that I would like to bring up for the attention of the committee. It refers to when an employer and employee have a stock bonus profit-sharing plan. I talked with Mr. Parker about it.

Under the present law, as I understand it, the employee, if he receives his stock, is taxed on the year that he receives it, when it is paid in to him. After the employer and employee have paid up the full amount of the stock and the stock is turned over to him he is taxed on the year he receives it, on the market value, the amount that the face value of the stock is over the market value, and as I understand it, that was in the 1926 law and then it was amended in the 1928 act.

The amendment that has been suggested to me is that the stock should not be taxed on the supposed increase in value until it is sold, because an employee who has been paying into the corporation to get stock, as a part of a profit-sharing plan, is taxed on it apparently when he receives the stock, although he has not really had any increase until he sells it. Now that comes into section 165.

Senator CONNALLY. Let me ask you, Senator, suppose he does not sell it? He has, as I understand it, received a portion of the value of this stock as a part of his profit-sharing plan in the corporation. If he does not sell it how is he going to be taxed on the profit?

Senator GERRY. Apparently he is taxed when he receives the stock although he has gotten nothing from it.

Senator CONNALLY. If he gets it as a part of the profits why does he not get the profits when he gets the stock?

The CHAIRMAN. What is your reaction to this, Mr. Parker?

Mr. PARKER. Let me give you an example of the two rules. In the first place, these plans are generally provided in order to allow the employees of the company to get a stock ownership and to have an actual participation in the business. That has been good for the employee in many cases, and good for the corporation, because the

employee, of course, takes more interest in the corporation if he owns some of its stock.

Now under the existing law, suppose the employer has contributed $1,000 toward the purchase of this stock of the company for which the man is working, and the employee has put in $1,000, that is $2,000 worth of stock. Now suppose at the time that the employee gets his stock it has not been paid up, and at the time he gets it the stock is worth $3,000, there has been an appreciation in value.

Now of course the real purpose of the plan was not to have the employee sell his stock, but to keep it, to participate in the business. Under the present law he is taxed in such a case on $2,000 profit, he is taxed on everything that he has not put in, including appreciation.

The old rule that we had at one time was this: He was taxed on $1,000, but he was not taxed on the capital gain, the appreciation, under the law, until he sold it, because he might never realize it. In other words, under the old rule, which has a good deal of consistency, you might say, in view of the general policy of this thing, he is taxed on everything that the employer has put into it, and he is taxed on every dollar that the employer has put in, he is taxed on all dividends, and so forth, that have all accrued on the stock while it has been held, but he is not taxed on the appreciation until he sells the stock.

As I understand it, that is the rule that Senator Gerry is advancing.

Senator COUZENS. It seems to me a perfectly equitable rule.

Senator LA FOLLETTE. It depends on the way the market is going.

Mr. PARKER. It does not make any difference which way the market is going.

Senator COUZENS. I am objecting to charging him for the appreciation which he has not realized.

Mr. PARKER. That is what we are doing now.

Senator GERRY. That is the point that I am raising.

Senator BLACK. You mean the employees are the only ones who pay on the appreciated value?

Mr. PARKER. The employee pays it when he gets the stock.

Senator CONNALLY. Mr. Parker, suppose I buy stock and it goes up in value, I do not pay until I sell the stock?

Mr. PARKER. Oh, no.

Senator CLARK. Why does the employee pay it, if nobody else pays it?

Mr. PARKER. I will tell you how we got that rule. We got that rule when the market value was declining. For instance, suppose the employee has paid in $1,000 and the employer has paid in $1,000, that is $2,000; at the time he gets the stock it is only worth $1,500; under the rule proposed here he would still pay on the $1,000 because that is what the employer has put in for him, and of course, under this proposition, really the purpose of it, to my mind, is that the employee should not sell the stock; the whole purpose of this thing was to allow the employee to get an interest in the company. I think it is a matter of which is the right policy.

Senator GERRY. I would like to read right here what the Ways and Means Committee said about it. It is short, it will not take very

long. This was the report of the Ways and Means Committee on the 1928 act explaining the change:

Section 219 (f) of the 1926 act provides that where a trust is created by an employer as a part of a stock bonus or profit-sharing plan for the benefit of the employees, and contributions are made to the trust by the employer and the employees, the amount actually distributed to the employees by the trust, in excess of their contributions, is taxable when distributed. Upon the termination of the plan there is distributed to the employee his proportionate share of the stock or securities purchased under the plan. Under section 219 of the 1926 act, in such a case the appreciation in the value of the stock, from the date of purchase by the trustee to the time of the distribution, is treated as income. As a result the employee is taxed not only upon the amount contributed to the trust by the employer and the dividends or interest distributed to the employees, but also upon the appreciation in the value of the stock, which has not been realized. The amendment provides that upon such a distribution to an employee there should be taxed to him as compensation the amount contributed by the employer toward the purchase of the stock, all cash dividends on the stock, any interest paid to the employee, and any other income received by him but that any appreciation in the value of the stock over the cost to the trustee should not be taxed unless and until the gain is realized.

In other words, the reasons set out in the report are entirely sound and warrant a change in the present act to conform with the provisions of the 1928 act. The only amendment to the present bill necessary to carry out this change is one restoring it to the language of the 1928 act.

Senator LA FOLLETTE. You should not consider this entirely from the point of view of the small, low-wage-earning groups in the corporations. These big executives class themselves as employee for this purpose too. Otherwise we would not have so much interest in what the Congress is doing in connection with it.

Senator COUZENS. Mr. Stam is throwing a different light on it than I understood here. Mr. Stam, you pointed out to me section 165 of the employees' trust, which you have a different construction of than some of the members of the committee seem to have.

Mr. STAM. I say under the present law the employee is taxed when the trust is terminated on the difference between what he put into the trust and what he got out of it, and in order to arrive at that difference, if there is distributed to him stock in the corporation they have to file that stock and see what it is worth at the time of distribution, and the value of that stock over what he put in is regarded as income to him at the time of the termination of the trust. That is the present law.

Senator GERRY. Therefore, if he is a small employee he will sell the stock, if he wants to raise money he will sell it.

Mr. STAM. He has income when the trust is terminated.

Senator GERRY. You kill the profit-sharing plan. That is the thing I am thinking about.

Senator BLACK. Mr. Chairman, I think that they all ought to be taxed alike, both the employees and the others. It seems to me the statement in the trust-fund provisions is quite a different thing.

I want to state that I do not agree with the views of policy as expressed by Mr. Parker. My observation is that it is not such a good thing for all these employees frequently to be coerced into buying stock. We happened to have some evidence where employees were practically coerced all over the United States to buy stock, and at the very time they were paid their price for it the man who had control of

it sold $19,000,000 worth of that stock on the market. It is my judgment that, to a large extent, a lot of this so-called profit-sharing plan of employees is a plain racket and it is intended not for the benefit of the employees and does not redound to their benefit or advantage.

I am not willing myself to vote for any amendment on the basis that I want to further encourage any such schemes that have been perpetrated in this country by numerous countries. I do not mean that all of them do that at all; I think some of them are honest and bona fide in their efforts to get their stockholders interested, but with reference to a large number of companies we have had evidence that they hire agents, they hire promotors to go over the country and sell this stock to their stockholders. My observation has been that the stockholders have actually lost a great deal of money, that is the employees, and it has been brought about by the control of the people who were tryng to get them to buy this stock and succeeded in doing so.

Now, I fully agree with the principle expressed by Senator Gerry that stockholders who happen to be employees should not be assessed higher or lower than anybody else, and to that extent I favor any amendment that would bring that about, but I do not want us to pass amendment on the theory that we want to do it to encourage a continuation of this widespread practice over the country.

Senator LA FOLLETTE. They got the advantage of it when the market was going down and now they want the advantage twisted around because the market is going up. That is what it amounts to.

The CHAIRMAN. Have you got an amendment, Senator Gerry?

Senator GERRY. I do not believe it is in the form of an amendment. It goes back to Mr. Parker to draft that. I was going to suggest that Mr. Parker draft the proper amendment.

Mr. PARKER. It is just like the old law, that is all. It is just a matter of policy whether you want to tax appreciation of the stock in the hands of the employee who gets it.

Senator GERRY. This would help the profit-sharing plan of the employees. I thought it was a good thing. Of course there may be bad cases, but I thought this was a good thing.

The CHAIRMAN. Suppose you get the amendment up, Mr. Parker, and present it Monday morning, Senator Gerry.

Mr. PARKER. There is nothing to the drafting of it. It is all drafted practically in the 1928 act.

Senator BARKLEY. Mr. Chairman, I have a letter from Judge Covington suggesting an amendment to section 112 (B) (6) covering liquidations. He wants it broadened so as to cover voluntary consolidations and purchases.

(The letter referred to is as follows:)

COVINGTON, BURLING, RUBLEE, ACHESON & SHORB,
Washington, D. C., May 21, 1936.

Hon. ALBEN W. BARKLEY,
Washington, D. C.

DEAR SENATOR BARKLEY: I am transmitting herewith a memorandum dealing with certain proposed amendments to the pending revenue bill designed to effectuate the purpose of the amendment in the Revenue Act of 1935, to make possible the elimination of subsidiary corporations and thus simplify corporate structures.

Your technical experts will say, I am sure, that the 1935 amendment does not afford a full opportunity to accomplish the desired purpose, and it is hoped that the now proposed amendments will be included in the pending bill. They

are simply intended to make it possible for corporations to take over the property of their subsidiaries, whether by statutory merger, consolidation, or liquidation as may be necessary under the laws of the various States and in consonance with the existing corporate structures, without capital gain or loss and with a preservation to the parent of the basis of value of the property of the subsidiary.

It is earnestly hoped the Senate Committee on Finance will see its way clear to adopt the proposed amendments.

Sincerely yours,

J. HARRY COVINGTON.

MAY 21, 1936.

MEMORANDUM ON H. R. 12395

SUGGESTED AMENDMENTS TO SIMPLIFY EXISTING CORPORATE STRUCTURES

The elimination of subsidiary corporations wherever possible has been urged by the President and others for some time. It is conceived to be in the interest of the public, and it also conduces to a more expeditious and efficient administration of the revenue laws. In pursuance of that purpose the Revenue Act of 1935 provided in section 110 (which added subdivision (6) to sec. 112 (b) of the Revenue Act of 1934) for "exchanges in liquidation" without gain or loss where property (other than money) was distributed to a corporation in complete liquidation of another corporation when the corporation receiving the property was in control of the liquidated corporation.

It developed, however, that in many instances corporations, by reason of the restrictions of State laws or the peculiar nature of the corporate organization, could not effectually, under the 1935 amendment, eliminate their subsidiaries. The amendment had been proposed and adopted in the closing days of Congress without adequate opportunity to study fully the legal situations involved and thus completely to achieve the avowed purpose of the amendment.

The proposals for further amendments are simply intended to assure the full accomplishment by corporations of the previously determined intent of the Congress to promote the liquidation of subsidiaries with the consequent simplification of corporate structures.

(1) Amendment to section 112 (b) (6)

Amend the caption thereof to read "Exchange by statutory merger, consolidation, or liquidation", instead of "Exchange in liquidation."

Amend the first sentence of section 112 (b) (6) to read as follows:

"No gain or loss shall be recognized upon the receipt of property (other than money) by a corporation in a statutory merger or consolidation with another corporation (whether or not such merger or consolidation has the effect of a liquidation of such other corporation), or in complete liquidation of another corporation, if the corporation receiving such property is the owner of voting stock possessing at least 80 per cent of the total combined voting power of all classes of stock of such other corporation.

Amend the last sentence of section 112 (b) (6) to read as follows:

"This paragraph shall not apply to any liquidation if any distribution in pursuance thereof has been made before the date of the enactment of this act; but section 112 (b) (6) of the Revenue Act of 1924 (added by section 110 of the Revenue Act of 1935) shall continue to apply with respect to liquidations initiated under such section, whether or not such liquidations have been completed prior to the enactment of this act."

so that the section as amended will read as follows:

"(6) *Exchange by Statutory Merger, Consolidation, or Liquidation.*—No gain or loss shall be recognized upon the receipt of property (other than money) by a corporation in a statutory merger or consolidation with another corporation (whether or not such merger or consolidation has the effect of a liquidation of such other corporation), or in complete liquidation of another corporation, if the corporation receiving such property is the owner of voting stock possessing at least 80 per centum of the total combined voting power of all classes of stock of such other corporation. As used in this paragraph 'complete liquidation' includes any one of a series

of distributions by a corporation in complete cancellation or redemption of all its stock in accordance with a plan of liquidation under which the transfer of the property under the liquidation is to be completed within a time specified in the plan, not exceeding 5 years from the close of the taxable year during which is made the first of the series of distributions under the plan. If such transfer of property is not completed within the taxable year the Commissioner may require of the taxpayer, as a condition to the nonrecognition of gain under this paragraph, such bond, or waiver of the statute of limitations on assessment and collection, or both, as he may deem necessary to insure the assessment and collection of the tax if the transfer of the property is not completed in accordance with the plan. This paragraph shall not apply to any liquidation if any distribution in pursuance thereof has been made before the date of the enactment of this act; but section 112 (b) (6) of the Revenue Act of 1934 (added by section 110 of the Revenue Act of 1935) shall continue to apply with respect to liquidations initiated under such section, whether or not such liquidations have been completed prior to the enactment of this act."

(2) *Amendments to section 113*

Amend the first sentence of section 113 (a) (6) by inserting after the word "inclusive" a comma and the following: "other than a transaction described in section 112 (b) (6)".

Amend the first sentence of section 113 (a) (7) by inserting after the words "the same persons or any of them" a comma and the following: "or upon a transaction described in section 112 (b) (6)".

Amend section 113 (a) by adding the following new paragraph:

"(15) *Basis established by revenue act of 1934.*—If property is acquired under section 112 (b) (6) of the Revenue Act of 1934 (added by section 110 of the Revenue Act of 1935), then the basis shall be the same as that provided by section 113 of that Act."

(3) *Amendment to section 112 (h)*

Amend section 112 (h) to read as follows:

"*Definition of Control.*—As used in this section the term 'control' means the ownership of at least 80 percentum of the total combined voting power of all classes of stock entitled to vote and at least 80 per centum of the total number of shares of all other classes of stock of the corporation."

The CHAIRMAN. Have you brought in an amendment here?

Mr. PARKER. We had to work on the foreign-tax situation. We have not gotten down to that.

Senator BARKLEY. I wanted Mr. Parker to look it over and see what there is to it.

Senator WALSH. Mr. Chairman, the question has been asked me: "Is the amount of tax at 18 percent to be deducted from the earnings upon which the 7 percent is to be paid?"

Another question was: "Is the windfall tax to be deducted first?"

Mr. BEAMAN. You are asking a question of policy, Senator. The present law provides that you do not get a deduction from gross income in computing net income in the amount of income taxes paid. The windfall tax is an income tax, therefore, as far as I know, it would not be deductible.

Senator WALSH. Neither would it be deductible from the 7-percent tax?

Mr. BEAMAN. No.

Senator WALSH. I would like to have the experts' opinion as to whether that is sound policy. Why should not this tax be deducted before the 18-percent levy is made?

The CHAIRMAN. Is it not because this tax has already been collected? The Supreme Court held it was collected improperly and now they are trying to get it back.

Senator COUZENS. Therefore it is not a tax.

Mr. TURNEY. As far as the 18-percent tax is concerned, the income on which this windfall tax is imposed is, in effect, though the mechanics is not exactly that, but it is, in effect, excluded from the computation of the 18-percent tax, because there is given as a credit against the windfall tax the amount of the 18-percent tax or of the 7-percent tax which is imposed on that same income. Now it may conceivably be that as to the 7-percent tax you would want to adopt a different rule, on the theory that they could not distribute the income which was necessary to pay the windfall tax.

Senator WALSH. They certainly cannot distribute income that has already gone to the Government by way of a tax, can they? I would like to submit that to the committee members for consideration.

Senator LA FOLLETTE. They cannot distribute it and get it back, that is sure.

Mr. TURNEY. The way the bill is set up it seems to me you get substantially the same result, because if there is a 7 percent tax on the amount of the income which is subject to this windfall tax the 7 percent tax is credited against the windfall tax. It is just the same, in net effect, as if this windfall were excluded from the computation of the other income tax.

Senator WALSH. If I understand you, it is not credited against the 18 percent tax but is credited against the 7 percent tax.

Mr. TURNEY. To state it exactly the way it works under the bill, there is a credit against the windfall tax to the amount of any other tax, 18 percent or 7 percent, which is imposed on that amount of the income, and as far as any double taxation is concerned it is completely eliminated.

Senator BLACK. Is it double taxation when an individual pays the surtax over and above the normal tax? Is that considered double taxation?

Mr. TURNEY. I would not say it was.

Senator BLACK. Do you consider it double taxation then when it is paid by a corporation? Does the same rule apply to it?

Mr. TURNEY. No.

Senator CONNALLY. No; it is not the same rule.

Senator BLACK. We have departed from the individual rule, though.

Mr. TURNEY. Of course you can make a distinction, I think, here, because the individual surtaxes depend on what he does with his income.

Senator BLACK. It depends on how much he made. In other words, however, both of them constitute, in effect, a surtax, do they not?

Mr. TURNEY. That is true; yes, sir.

Senator BLACK. In the corporation plan, where you permit them to first take out the taxes they paid the Government, we apply quite a different rule than we do to an individual.

Mr. TURNEY. I think it is a different situation. One is taxed on distributed earnings and the other is taxed on income. The credit

provision in the windfall tax gives the taxpayer more relief than a deduction of the windfall tax in computing the 18 percent and 7 percent.

The CHAIRMAN. Mr. Seltzer, let us get at the estimates again. This is your final estimate on this same proposal?

Mr. SELTZER. This is what we call C–4 of the proposal made yesterday.

The CHAIRMAN. All right, go ahead and explain that, Mr. Seltzer.

Mr. SELTZER. We get a total net estimated increase in revenue of $522,000,000. Of this amount $215,000,000 would come from the increase in the ordinary corporation income tax to 18 percent.

Senator CONNALLY. How much?

Mr. SELTZER. $215,000.

The CHAIRMAN. Then you estimated about $19,000,000 on that $1,000 exemption. I think you had $244,000,000 yesterday on that item.

Mr. SELTZER. We were comparing that with plan no. 7 or C–3.

The CHAIRMAN. I thought yesterday you said that the increase on the 18 percent, the present rate, was $244,000,000.

Mr. SELTZER. That is right.

The CHAIRMAN. Now with the $1,000 exemption on $15,000 corporations, there would be a difference between this $215,000,000 and $244,000,000, which would be $29,000,000.

Mr. SELTZER. That is right, $29,000,000. Then we get $217,000,000 from the undistributed earnings tax. That is $8,000,000 less than we had gotten under no. 7. And we get $90,000,000 from the normal tax on dividends, making an aggregate of $522,000,000.

I might say that no account has been taken in this estimate of the exemption of banks and insurance companies from the surtax on undistributed earnings. I do not believe that that exemption will reduce the revenues very appreciably. I do not believe that that exemption would reduce the revenues by more than $5,000,000 or $6,000,000. For one thing the banks in the past have usually paid out in dividends a greater amount than they reported in taxable net income. That is the tax-exempt interest.

The CHAIRMAN. You did not put that in the House bill. You put a 15 percent flat rate on banks.

Mr. SELTZER. That is right.

The CHAIRMAN. Here we put an 18 percent flat rate on.

Mr. SELTZER. That is right.

The CHAIRMAN. Why would not you get more revenue?

Mr. SELTZER. I am referring here only to the undistributed earnings tax, that 7 percent on undistributed earnings. I am saying I do not anticipate that a correction of this estimate for the exemption of banks and insurance companies from the 7 percent supertax would make an appreciable difference in the estimate.

Senator COUZENS. It would be so small it would hardly be worth taking into account?

Mr. SELTZER. Yes, because a large part of the income is tax-exempt.

Senator WALSH. Does the exemption include mutual savings banks?

Mr. PARKER. It is mainly those that are exempt under the present law. That will not cost you any money. Usually pay a rather small tax. If they are taxable they would pay the flat rate, 18 percent.

The CHAIRMAN. Here is a matter that gives me some concern. You said that under this House bill, under this theory, you would raise $623,000,000 more, I believe, in taxes; is that right?

Mr. SELTZER. Yes.

The CHAIRMAN. And that, in order to transform the complete distribution and put it in the form of a flat rate, it would take about 25 or 25.5 percent?

Mr. PARKER. 25.5 percent.

The CHAIRMAN. In other words, 25.5 percent would give you what you would expect to get the other way, this $623,000,000?

Mr. SELTZER. No.

The CHAIRMAN. That was as I understood it. I understood that to be Mr. McLeod's testimony. Am I wrong or right about it?

Mr. PARKER. That was repeatedly testified to. The 25.5 percent flat increase on corporations, without the $1,000 retention of income, would produce the necessary additional revenue, both in the House and, I think, here.

The CHAIRMAN. That is way I understood it. Now, if you take the 18 percent flat rate and put 7 percent on top of that, on the amount retained, that is 25 percent, is it not?

Mr. SELTZER. Yes.

Senator CONNALLY. Now, Mr. Chairman, it is 7 percent on only that part that is retained.

The CHAIRMAN. That is what I mean, on that part retained. Of course, it is not 7 percent on the 18-percent tax.

Mr. SELTZER. I was not here when Mr. McLeod gave his testimony.

Senator BARKLEY. What was said, Mr. Chairman, was that, in order to raise the amount of money provided for in the House bill, the way the House bill provided to raise it, it would take a flat rate of 25.5 percent on all net earnings of corporations, without regard to any retention or distribution. Of course, this proposal that we have adopted is different from that in that it does not tax the undistributed income more than 18 percent. That would make a difference.

The CHAIRMAN. Well, if it is distributed it does not change the situation. They pay the increased tax.

Mr. SELTZER. Well, that is excluded, you see, in the present budget picture. You are seeking a net increase of $620,000,000, or thereabouts, I take it, over what we anticipate in the budget picture. The dividends that we anticipate corporations would pay during the calendar year 1936, in the absence of any change in the law, are already included in our budget picture, so far as their effect on individual incomes and the surtaxes that we collect on those incomes are concerned.

Senator BARKLEY. The question was asked during the hearing: "What sort of a flat rate would be required with no supertax on the part retained, in order to produce the amount of revenue the House bill provided for?"

The CHAIRMAN. He said 25.5 percent.

Senator BARKLEY. Yes.

The CHAIRMAN. Did you take into consideration that the 7 percent that we put in here applies to intercorporate dividends and under the House bill it did not apply to them?

Mr. SELTZER. As I understand the House bill, it would apply to incorporate dividends there. That is, the withheld earnings subject to tax under the House bill do include dividends received by corporations.

The CHAIRMAN. Well, you are getting 7 percent and 18 percent and you are applying it on intercorporate dividends too in this proposal that we have got now?

Mr. SELTZER. Oh, yes.

The CHAIRMAN. Did you take that into consideration at all?

Mr. SELTZER. We did.

The CHAIRMAN. Well, it does look to me like the figures are awfully low. Here you get $522,000,000 and you get $623,000,000 in the other case.

Mr. SELTZER. You get $591,000,000 in the other, from the comparable provisions.

The CHAIRMAN. That is by exempting the $1,000?

Mr. SELTZER. No; that is from the taxes on corporations and the effect on distribution, that would give you $591,000,000. It brings it up to $623,000,000 by a number of miscellaneous provisions which I mentioned yesterday.

Senator BARKLEY. You mean under the House bill you would get $591,000,000.

Mr. SELTZER. I beg pardon?

Senator BARKLEY. The House bill, as I understand it, provides $591,000,000 on the corporation tax, but your figures yesterday, before we exempted so many people, produced $596,000,000?

Mr. SELTZER. That is correct.

The CHAIRMAN. It did not go to $596,000,000, it went to $544,000,000, did it not?

Mr. SELTZER. It went to $596,000,000 before you made the deductions for small corporations.

The CHAIRMAN. Oh, yes, when you put a tax on a tax.

Mr. SELTZER. That is true.

Senator COUZENS. May I say, Mr. Chairman, I think we are getting more confused every minute when we try to add the 18 percent and 7 percent. They have no relation to each other and you just cannot add those together and say it is 23 percent. That is not true. The more we discuss the 18 percent and 7 percent together the more confused we get, because they are two different things entirely. They cannot be added together.

Mr. SELTZER. We had estimated that for 1936 the dividends to be paid by corporations would increase over the dividends that we estimated were paid in 1935 by, I think, $370,000,000. Under this bill the corporations would be paying in taxes to the Federal Government $215,000,000 plus $217,000,000, or a total of $432,000,000 more than we had anticipated in making up the Budget estimate. Nevertheless, in making the estimate for this proposal we said that corporations would not reduce their dividend disbursements at all, despite the fact that they will pay in Federal taxes $432,000,000 additional. We said that that could be counted upon approximately to counteract the additional stimulus to distribution provided by a net 3-percent tax differential on retained earnings.

Our estimates under this proposal assume a greater proportion of earnings paid out by corporations after taxes than they did under

the Budget estimate. They do not assume a greater dollar volume of dividend payments, because we believe, as I have just said, that the additional taxes paid by corporations, $432,000,000, would act as a partial or total counteractive.

Senator COUZENS. That means substantially that the corporations will obviously have to curtail the dividends in many cases because of the increased corporate tax, is that what you are trying to get at?

Mr. SELTZER. No. What, in effect, I was trying to say was that the tendency to increase their dividend distributions by reason of a net 3-percent penalty on retained earnings might be counterbalanced by this $432,000,000 of additional taxes that they had to pay.

Senator COUZENS. That is exactly what I said. They cannot distribute as much when we take it away from them in the form of taxation than they would distribute if we did not take it away from them by taxation.

Mr. SELTZER. What I am trying to say, Senator, is that they would distribute just as much in dollars despite the fact that you are taking $432,000,000 additional away from them, I said that they might distribute just as much because you do impose a penalty on not distributing, but I also say that they will not distribute as much additional as you might at first think because of this penalty, because of the fact that the absolute volume of their taxes will be increased.

The CHAIRMAN. Well now, you estimate we have got to get some additional taxes if we carry out the President's message. Now let us see just how much we need. You have got $522,000,000 and we want $623,000,000.

Mr. SELTZER. The President's message said $620,000,000.

The CHAIRMAN. $620,000,000. So we have got about $98,000,000 more to get; is that right?

Mr. SELTZER. That is correct.

Senator LA FOLLETTE. That is not quite accurate, either; is it?

The CHAIRMAN. No; that is not quite accurate.

Mr. O'BRIEN. Senator, do you not have to get the difference between $522,000,000 and $591,000,000 instead of the difference between $522,000,000 and $620,000,000?

Senator CONNALLY. Mr. Chairman, I do not subscribe to the principle that we have got to get $621,000,000 exactly. We ought to levy what we believe to be a fair and just act. I do not subscribe to the theory that we have got so much cloth here, and we have got to fit it on a person, whether it does or not.

Senator COUZENS. I said the same thing yesterday. We are all experimenting.

Senator CONNALLY. Suppose we miss it by $100,000,000; what difference does it make?

The CHAIRMAN. Of course, it is a rather difficult proposition. I am frank to state, without any element of criticism, that I think the estimate is too low on this proposition.

Senator LA FOLLETTE. Senator, it is a disagreement between you and the Treasury on what you figure this 3-percent penalty on retentions will bring, as to what effect it is going to have on distribution of dividends. That is what it comes down to.

Mr. SELTZER. As I understand the House bill—I may be mistaken, I have been working on the Senate proposals for several weeks—as I recollect the provisions of the House bill intercorporate divi-

dends were included in the earnings subject to tax, retained earnings subject to tax. If I am mistaken I should like to be corrected.

The CHAIRMAN. Is that right?

Mr. BEAMAN. Sure.

The CHAIRMAN. Is that your information, Mr. Stam?

Mr. STAM. In figuring out your 25.5 percent flat, the testimony was given if you had a flat rate of 25.5 percent, that that would produce the needed amount of revenue. Now, that was based on existing law, as I understand, that 25.5-percent flat rate, and, of course, the existing law did not take into account the intercorporate dividends. In the proposal you said you could raise this much revenue by 25.5 percent flat. Now, the 7 percent flat is imposed on the intercorporate dividends, so that you would probably get more by that 7 percent rate than you would through your 25 percent flat. I mean that is the thought we had in mind.

Senator CONNALLY. That is impossible.

Mr. STAM. Why?

Senator CONNALLY. Because the 7 percent is only on one-half of it.

Mr. STAM. You see the part that is distributed is taxable in the hands of the shareholders, and we picked up from them. The part that is not distributed is taxable in the hands of the corporation and we get the 7 percent of the intercorporate dividends that are not distributed. So I think you would pick up something from that source.

Mr. SELTZER. You are not, however, talking about the House bill provisions?

Mr. STAM. No, no.

The CHAIRMAN. What is your reaction to that, Mr. Parker?

Senator CONNALLY. Mr. Parker, let me ask you right there, before you start, you already figured the 4 percent that you are going to pay on the dividends in the hands of the individual shareholder, you figure that in a separate bracket, so you have got to disregard that in computing any increase?

Mr. STAM. Pardon me just a minute, Senator. We have not figured there would be any increase in distributions due to the 7 percent additional tax.

Senator LA FOLLETTE. It is only 3-percent net, as far as that inducement is concerned. Furthermore, I think we are talking at cross-purposes, because what I understood Senator Harrison was asking about was whether or not, in proposing the House bill, they took into account the intercorporate dividends, whether they had that in this estimate, trying to squeeze a little more money out of Mr. Seltzer on the ground he did not figure it in the House bill and did figure it in the Senate proposal. That is not true. They did figure it in the House, and it is figured in this, so you can not get any more money from it on that basis.

Mr. PARKER. I think there is an item here on this liquidation proposition that ought to add $33,000,000.

Senator LA FOLLETTE. He said $591,000,000 in the House bill compared to $522,000,000 in this one. You have not eliminated those provisions, therefore you are not in a position to add that. Now you can go ahead and add these other things and see what you get.

The CHAIRMAN. Mr. Parker, how about this and section 102?

Senator LA FOLLETTE. I do not think, Mr. Chairman, it is fair to ask the Treasury experts and actuaries to estimate on how much 102 is going to do until they know what you are going to do to 102.

The CHAIRMAN. I am asking Mr. Parker now; I am not asking Mr. Seltzer.

Mr. PARKER. I think the possibilities are, there will be a very considerable amount of additional revenue from the psychological effect of changing section 102, if we can do it in a practical manner.

Senator BARKLEY. I think as far as section 102 is concerned, for all practical purposes it is just like a turnip, it has got no blood in it yet.

The CHAIRMAN. We have got $69,000,000 difference between the $591,000,000 and $522,000,000. How much have we lost, Mr. Turney, by this windfall tax business and the refunding proposition from what we started out with? We expected to get there $100,000,000, did we not?

Mr. TURNEY. Under the provisions of the House bill—I think Mr. Seltzer can answer the question—it was reduced from $100,000,000 to—do you know what the figure is?

Mr. SELTZER. Yes. Under the original House bill provision it was $100,000,000.

The CHAIRMAN. Now, as to these changes that were made, what effect have they upon the revenue?

Mr. SELTZER. We have not seen the changes yet. When we get those changes we will be glad to submit a revised estimate.

The CHAIRMAN. Well, Mr. Turney, have you any idea what it will be? We have got to get more revenue. We would like to know what it would be.

Senator GEORGE. That is temporary anyhow, Mr. Chairman.

Senator LA FOLLETTE. Mr. Chairman, if you want to figure out on the basis of the Treasury estimate what your bill would raise under the proposal the committee adopted yesterday, as I understand Mr. Seltzer's testimony, you are now in a position to add to the $522,000,000 those other things which were estimated and included in the $623,000,000 and which are still retained in this bill, such as the liquidation provisions and other things of that kind. I think it would be helpful if, in an orderly way, we could proceed to do that.

The CHAIRMAN. Now, what are those things, Mr. Parker?

Mr. PARKER. The principal provision is the Treasury estimate of $33,000,000 on the liquidation proposition.

Senator LA FOLLETTE. That is for 1 year.

Mr. PARKER. Well, that is what they estimate for 1 year. I think myself it is going to last for 2 years, because I have got a list of corporations that will liquidate, that will run up to $42,000,000, a list of actual cases.

Senator LA FOLLETTE. That is just temporary.

The CHAIRMAN. What other provisions are there now?

Senator LA FOLLETTE. How much did you say that was?

Mr. PARKER. $33,000,000 was the Treasury estimate. Is that right, Mr. Seltzer?

Mr. SELTZER. I believe it is, but I would like to look at the sheet to make sure.

Mr. PARKER. I am pretty sure that is it. I estimated $40,000,000 and the Treasury said $33,000,000.

Senator GEORGE. What about the foreign stockholders and nonresident aliens?

Mr. PARKER. If we keep section 351—I do not think the Treasury ever made an estimate of what that would be, but we get considerable money under section 351 now.

Senator LA FOLLETTE. You mean you want to include that?

Mr. PARKER. I think we lost a certain amount under the House bill. I do not know whether they figured any loss under section 351 or not, but if they figure a loss, then we ought to add it in.

Senator LA FOLLETTE. Did you figure any loss, Mr. Seltzer, do you, know, under the House bill by the repeal of section 351?

Mr. SELTZER. I would have to refresh my memory there. I have gotten away from the figures in the House bill during the last several weeks.

The CHAIRMAN. What other item is there, Mr. Parker?

Mr. PARKER. On this bank situation the House bill had 15 percent flat and we have 18 percent; I do not know just the nature of their figures, whether that is taken into account. I should think it would eliminate any loss there, any loss from taking the banks out of the 7 percent, because we have done it under the House bill, when we only had 15 percent on the banks.

The CHAIRMAN. Have you taken that into consideration, the increase in the rate on banks, in your estimates here?

Mr. SELTZER. Yes. We do know this, Mr. Chairman, that the House bill yields $591,000,000 from the comparable provisions that you have in your bill, and they get a total of $623,000,000. There is a difference there of $32,000,000, to which you might add $5,000,000, because of a loss accounted for in the House bill by reason of certain buffer provisions which are absent in the present bill. So that you get an addition of $37,000,000, which will be reduced by any changes that may possibly be made, or any changes which you have made in other respects.

The CHAIRMAN. I have got it up to $560,000,000 now.

Mr. PARKER. We have the elimination of the cushion. That would add $5,000,000. Then there is the matter of the exemption of the banks, that were exempted from the 42.5-percent provision on the House bill. I think that is inconsequential.

Mr. SELTZER. The banks do not make much difference.

Senator CONNALLY. Why is it? Because so many of their holdings are tax-exempt bonds, and things of that kind?

Mr. SELTZER. That is right.

The CHAIRMAN. Let me ask you, Mr. Parker, in reference to the estate tax—on the estate tax we exempt the first $40,000?

Mr. PARKER. That is correct.

The CHAIRMAN. How much could we raise if we would permit the first $40,000 to be exempt, and put a $20,000 exemption on the fellow who has an $80,000 estate, and a $10,000 exemption on the fellow who has a $100,000 estate, and after you get up here over $120,000, to wipe out the exemption; how much would you get in that case?

Mr. PARKER. Well, I think one of those proposals ran around $40,000,000. I think that one proposal was to take the exemption away entirely at $80,000.

Senator BARKLEY. Take what away?

The CHAIRMAN. The $40,000 exemption.

Mr. PARKER. If you had a $40,000 estate it would be all exempt, if you had a $60,000 estate there would be $20,000 exempted, something like that, and then if you had an $800,000 estate it would be all exempted.

Senator CONNALLY. He would be worse off than the man with a $40,000 estate.

Senator GERRY. As a matter of fact, Mr. Chairman, it is going to hit the fellow with a small estate.

Mr. PARKER. It hits the estates between $50,000 and $500,000.

The CHAIRMAN. Cannot you pare that off so it will not hit them?

Mr. PARKER. We could reduce it probably and work out some schedule that would return you $20,000,000.

Senator CONNALLY. Don't you get the best results by graduation, to put a higher rate above $80,000?

Senator GERRY. Mr. Chairman, I have an amendment that I want to bring up now or sometime today, I do not want to bring it up at just this minute, as to an estate which is in trust. I spoke of it the other day. One of the heirs, when she gets her estate, will owe the Government money. I can bring this thing right now. It gives you an example of your estate taxes.

Here is an estate where a man died in 1900, when there was no estate or inheritance tax on it, and he created a trust and one of the heirs has now inherited the estate and has to pay the estate tax on it.

The estate cannot be distributed because it is held in trust until certain other beneficiaries are dead, and the trust is not making as much interest as the Government is taking the beneficiary of the estate. Possibly that will run on for twenty years and the heir will not be able to get any estate, and when she does, the interest will probably eat up everything that the heir is receiving. I would like to have that referred to Mr. Parker and the experts here, to see if something cannot be worked out on that.

Mr. KENT. If I might say a word regarding that. I made some inquiry as to these cases. The remainders are handled up in the estate tax unit, and I was informed that it was very seldom that actual advantage was taken of that provision of the statute that provides for a postponement of payment, that what they usually did was to talk to people and discuss the matter with them, and they would make an arrangement for them to pay the tax immediately upon a discounted basis. They have various mortality tables, and so forth, that they use in that connection. If the probable period before the remainder would come into possession was 15 years, for instance, they would pay a tax, discounted upon the 4 percent basis for that period, and clean the thing up right away.

Senator GERRY. In this particular case they cannot do that.

Mr. KENT. I know that.

Senator GERRY. In this particular case it is absolutely impossible to do that.

Mr. KENT. That is a peculiar case. The only point I was making is that the 4 percent interest which is charged under the statute is really just making up the difference between the discounted value which would be taken if they wanted to pay their tax immediately and what the Government gets if the tax is postponed until the remainder comes into possession. I think Senator Gerry has a very

difficult case, on the facts. It is just one of those occasional cases of severe hardship that will arise.

Senator GERRY. Mr. Chairman, I think you are going to get a great many more of them. You have got your estate tax so high that it is confiscatory in a great many cases, and you are going to have a great many more bad cases.

Senator LA FOLLETTE. Mr. Seltzer, how much did you figure in the estimate of the House bill for the change in the treatment of nonresident aliens and foreign corporations, and so on?

Mr. SELTZER. $4,000,000, if I remember correctly.

Senator LA FOLLETTE. There is $4,000,000 more for you.

Mr. SELTZER. That, of course, was included in the $37,000,000.

Senator GEORGE. Mr. Seltzer, did you figure anything at all on the capital stock that would be in addition to what was estimated in the House, did you figure anything additional in this estimate?

Mr. SELTZER. No. In computing this estimate we went on the assumption there would be only those three changes in the law, the increase in the corporation income tax, the surtax, and the application of the normal tax to dividends. We assumed that the capital stock and the excess profits tax would remain unchanged, hence you get no increase on that account.

Senator GEORGE. That is under the present law?

Mr. SELTZER. We made no computation of an increase in the rate of capital stock and the excess profits taxes.

The CHAIRMAN. Mr. Savoy is here from the Department of Agriculture with reference to this sugar proposal, and I think we should take that up. The committee is familiar with the fact that we passed the sugar equalization law. It expires when, Mr. Savoy?

Mr. SAVOY. December 31, 1937.

The CHAIRMAN. In 1937. You are not collecting any processing tax now?

Mr. SAVOY. No, sir; we have not since January 6.

Senator KING. What law is to be continued until next year?

Mr. SAVOY. The Jones-Costigan Sugar Act, under which quotations have been established, and which deals with allotments.

Senator KING. That is still in effect?

Mr. SAVOY. It is still in effect; yes, sir.

Senator CONNALLY. Are any benefits paid out to the Government under that act?

Mr. SAVOY. No, sir.

Senator CONNALLY. It is purely a quota matter?

Mr. SAVOY. It is purely a quota matter. Secretary Wallace presented a letter to the committee at the request of the committee, on May 7, with respect to sugar, and we have drafted a proposal to have the tax continued, the old tax in the Jones-Costigan Sugar Act. The first section imposes the tax in exactly the same manner and at the same rate as is in existence in the Jones-Costigan Act.

Senator GEORGE. Is that in existence until 1937?

Mr. SAVOY. No, sir; it is not. That is, no taxes have been collected since the decision in the *Hoosac Mills case*, no processing tax.

The CHAIRMAN. You did collect it before that?

Mr. SAVOY. Yes.

Senator CONNALLY. It is still on the statute books, even though it was nullified by the Supreme Court decision?

Mr. SAVOY. The Treasury Department has apparently so concluded, since it suspended the collections.

Senator KING. You suspended collection on all commodities?

Mr. SAVOY. We suspended collection on all commodities.

Senator KING. What is your theory then as to the continuation of the taxes upon sugar?

Mr. SAVOY. This is not a continuation, this is the imposition of a new processing tax, our theory being that there is nothing in the decision which says you cannot impose a processing tax.

Senator CONNALLY. You do not earmark it?

Mr. SAVOY. That is correct.

Senator KING. The other day we decided, as I recall, adversely, to the imposition of processing taxes upon all other commodities but reserved it on sugar. Why should we differentiate?

Senator COUZENS. He is coming to that, Senator.

Mr. SAVOY. In the Secretary's letter he pointed out that up until the Jones-Costigan Act we used to collect in import duty $96,000,000. We now collect $36,000,000. With a tax of one-half cent per pound on sugar the total revenue from import duties and sugar taxes would amount to about $102,000,000. That would restore, then, $66,000,000, and it would be possibly in excess of that which we calculated for, without there being any additional cost to the consumer, because it would be reflected in the price of raw sugars rather than in any additional charge to the consumers.

The table which accompanied the Secretary's letter shows that when a tax went on on sugar in 1938 the raws, duty-paid, were $3 a hundred, and the average over the period 1935, while there was a temporary rise, it levelled out, and the average for 1935, with the one-half cent tax on, was 333, which was practically the same as that for 1933.

Senator CONNALLY. When there was no tax?

Mr. SAVOY. In 1933 it was 321, and in 1935 it was 333.

Senator CLARK. How much did you raise?

Mr. SAVOY. We raised $65,000,000 at that time. The consumption requirements have increased, and we now estimate the consumption requirements will be 6,600,000 tons. That will give us $66,000,000.

Senator GERRY. Did the domestic price of sugar go up?

Senator COUZENS. It went up considerably above border prices.

Mr. SAVOY. Yes.

The CHAIRMAN. This Jones-Costigan bill has been a very great help to the sugar-beet people?

Mr. SAVOY. Yes.

The CHAIRMAN. They put it in this Canadian agreement, that is where you want to recoup.

Mr. SAVOY. There is a bill now pending in Congress to cure such legal defects as are considered to exist, such as the delegation of power and nonfixation of definite quotas in the bill. I believe the Jones-Costigan and other acts with relation to this subject were referred to this committee.

Senator KING. Suppose it will not pass, how will it affect your proposition here?

Mr. SAVOY. We will administer the law with reference to quotas. The Secretary points out that with a quota system in effect and no

processing tax the returns to processors would amount to something between 14 and 16 percent on their invested capital and surplus.

Senator GERRY. What do you figure is due to the rising cost of sugar to the original individual?

Mr. SAVOY. To the ordinary individual we estimated there would be no material additional cost.

Senator GERRY. You figure that the retail price of sugar will not go up?

Mr. SAVOY. Not materially.

Senator GERRY. What do you mean by "not materially?"

Mr. SAVOY. There will be an immediate reaction, but over the period of a year it would level out, just as it did during the operation of the processing tax.

Senator CONNALLY. If you lower the tariff, if you do not put the tax on, we will just hold that back?

Mr. SAVOY. In answer to your question, sir, the chart which was made of retail prices shows there was an immediate reaction here, when the tax went on it was leveled out, then there was a slight rise, and then it was leveled out again.

The CHAIRMAN. What is the amount of the processing tax?

Mr. SAVOY. One-half cent a pound. That is the tax rate which was put into effect under the Jones-Costigan Act.

Senator KING. I am not quite clear as to the deduction to be drawn from your answer that this would not increase materially over a leveling-out period, whatever that may mean, the cost to the consumer. It would seem to me that if you establish a policy under the terms of which you are going to impose a processing tax, that means that the processor is going to pay less to the producer of the sugar, or he is going to charge more to those to whom he sells, and the person to whom he sells, the wholesaler and retailer, is going to charge more to the consumer.

Mr. SAVOY. Experience shows that during the operation of the last tax the price of raws was affected somewhat and the processor's margins narrowed somewhat. Of course, in your beet area, where the tax comes partly out of the processor and partly out of the producer, that would necessarily have to be taken care of in some other way, and is being taken care of under the Soil Conservation Act and under the new act which is being proposed. There is nothing to prevent similar additional payment under the Soil Conservation Act to take care of that situation in a separate legislation.

Senator KING. Then you anticipate that the administration under the Soil Conservation Act is going to pay the beet-sugar producers and cane-sugar producers for not plowing some of their land and planting it?

Mr. SAVOY. No; but for marketing within the interstate marketing quotas for the particular area.

Senator COUZENS. May I ask if this proposal of yours does not, in part, at least, tend to compensate the producer for the loss of the protective tariff?

Mr. SAVOY. Well, I would not say that this was for the purpose of doing anything for the producers at all. The tax itself will not be of benefit to the producers. We propose to benefit them under our conditional payment act and the Soil Conservation Act.

Senator KING. What do you mean by "conditional payment?"

Senator CONNALLY. The proposition of the limitation of the amount that could be imported could be a benefit to the domestic producer, he gets some benefit there.

Senator COUZENS. Yes; but you are running a hazard there of it being declared unconstitutional. We ought to make adequate provision at this time so that in the interim there is no action taken to declare it unconstitutional and leave the producer high and dry without a tariff and without this allocation of quotas.

Senator CONNALLY. You certainly have a right to levy a processing tax without earmarking.

The CHAIRMAN. Now you have got an agreement that does not conflict with the Jones-Costigan Act?

Mr. SAVOY. The Philippine Islands have reduced their production very materially. Hawaii has reduced its production very materially, and it cannot, within 2 or 3 years, increase it.

The CHAIRMAN. Do you think that by putting this processing tax on sugar it would be an encouragement to change the law in these respects, according to the recommendation of the Agricultural Department?

Mr. SAVOY. Yes; I think very materially. I think if a tax on sugar is imposed that there will be a very strong movement to clear up the legal defect in the Jones-Costigan Act.

The CHAIRMAN. Is the trade generally pretty much for these amendments and for sustaining the Jones-Costigan Act?

Mr. SAVOY. Yes, sir; very much so.

Senator GUFFEY. Senator Harrison, this morning I was called over the telephone by a man representing three large sugar refineries in Pennsylvania, in Philadelphia, and he said that they are for this processing tax of one-half cent a point, and they hope also that we will extend the Jones-Costigan Act, because it saved the sugar industry in this country. They tell me they were in very bad shape.

The CHAIRMAN. My observation is there has been no opposition to it and they are all satisfied with it, with the exception of the sugarcane producer in Louisiana who does not think he has a large enough quota. Is that about right?

Mr. SAVOY. Yes, sir. Our recollection is that there is to be no change now that the Jones-Costigan Act be really enacted with the difficult or bad parts out, that the question of quota is not to be reopened at this time.

Senator CLARK. Take the sugar producers in Puerto Rico, Hawaii, and the Philippines, would there not be a discrimination against them if you had a quota?

Mr. SAVOY. They have been very satisfied, at least so far as we have been able to determine, with this Jones-Costigan Act; there may be some individuals who oppose it, but by and large every member of the industry has been very pleased with its operation, except Louisiana.

The CHAIRMAN. Well, Louisiana is producing so much more sugar than the other States. I would like to see Louisiana helped in some way in their quota, if it is possible, because it seems like they have a cure for that mosaic disease that has gotten into the sugarcane.

Senator KING. What is the view of the beet-sugar people in Michigan, Nebraska, and Colorado, not to say Utah, with respect to your proposition?

Mr. SAVOY. So far as I have been able to determine, from discussing the matter with Senators from some of the States that you mentioned, they seem very well pleased with the pending bill.

Senator KING. You have talked with Mr. Kearney, haven't you?

Mr. SAVOY. Yes, sir.

Senator KING. What is his attitude?

Mr. SAVOY. Entirely for it, and he is out today trying to ascertain whether everyone is all ready to support the bill.

The CHAIRMAN. There was a group in my office, the Secretary of Agriculture came up, and Chairman Jones, of the House Agriculture Committee, was over, and my observation to him was that unless the sugar-beet people and the sugarcane people can get together there would be no use to try to amend the law.

Senator KING. Senator, not as expressing any opposition to this proposal, but if you begin with one industry by introducing the processing tax and so on, are you not going to be pestered with demands for processing taxes with respect to other commodities? We turned it down the other day.

The CHAIRMAN. Give us your idea. What is the distinction now?

Mr. SAVOY. The important distinction is that this is really replacing the import revenue due to the lowering of the tariff, and the second distinction is it is the only industry which is operating under a quota system, the other industries are not, and that quota system has been of tremendous advantage to the whole industry.

Senator CONNALLY. As a matter of fact the Government helped it to operate the quota system.

Mr. SAVOY. Yes; but that was not very expensive.

The CHAIRMAN. Mr. Savoy, what is the amendment that you want to write? We do not want to change this whole law and write it into this bill. Do you want us to just put the processing tax on it and let the proper committees make the other changes? It has got to come in from the House first. Of course, we could put it in this bill here.

Mr. SAVOY. We are not suggesting, in this proposal, any changes in the act. This deals with sugar only.

The CHAIRMAN. It makes no change in the present law?

Mr. SAVOY. It makes no change in the present law.

Senator COUZENS. While we are on that point may I ask, when you come to amend the Jones-Costigan Act, do you propose to specify the quotas in the act itself?

Mr. SAVOY. Yes.

Senator COUZENS. That will obviate the constitutional objection.

Mr. SAVOY. The objection to delegation of power; yes, sir.

Senator COUZENS. In amending the Jones-Costigan Act you propose to put in the quotas in substantially the same amount as they now exist?

Mr. SAVOY. Yes, sir.

Senator KING. Let me ask one question there, in view of the Senator's question.

Senator COUZENS. Yes.

Senator KING. The Virgin Islands, as you all know, is a liability to the Federal Government. We are spending considerable money, two or three hundred thousand dollars annually, to help them maintain that government, and the Federal Government has gone into

activities there, it is making rum, it is making sugar, it bought a sugar mill there, and so on. About the only product that may be obtained from the Islands are sugar and rum. Now complaints have come to me from representatives of the Islands, have come to members of the Committee on Territories and Insular Affairs, that they are restricted, as my recollection goes, to 5,000 tons. Now with the acquisition of lands by the Federal Government for the purpose of helping those poor people, who are rather helpful in a way economically, they must have a larger quota, because that is about the only thing they can produce, and if they can produce more sugar then the subsidies from the Federal Treasury for the maintenance of their insular government will gradually diminish and they think they can be self-sustaining in a few years. Have you contemplated the effect of increasing the quota there?

Mr. SAVOY. Not at this time, Mr. Senator, because in order to give any area more sugar you have got to take it from another area, and when you do that you precipitate a quota fight, and when you precipitate a quota fight it will take too many months to handle it.

Senator COUZENS. Senator Bulkley handed me this letter here which refers to some corporation organized to take care of the Mather estate. I think Mr. Parker knows something about it. I told Senator Bulkley that I would bring the matter to the attention of the committee, and I ask now to have the letter put in the record.

The CHAIRMAN. It may be inserted in the record.

(The letter referred to is as follows:)

PICKANDS MATHER & CO.,
January 3, 1936.

HON. ROBERT J. BULKLEY,
Senate Office Building,
Washington, D. C.

DEAR ROY: You will recall that at the time the special provisions for surtax on personal holding companies were put into the 1934 Revenue Act you arranged to have subparagraph (b) (2) (B) inserted omitting deductions from the special tax of "amounts used or set aside to retire indebtedness incurred prior to January 1, 1934, if such amounts are reasonable with reference to the size and terms of such indebtedness."

It was thought that this might protect the unfortunate situation of Mr. Samuel Mather's estate which had large indebtednesses to Western Reserve and other charitable organizations as well as to the banks so that it was practically insolvent and which was able to get additional time from its creditors only by incorporating and pledging all of its assets to a trustee for the creditors, subject to provisions requiring all income and realizations from sales that were made to be applied on the debts.

Unfortunately, however, the incorporation was delayed by a threat of the Government to impose large inheritance taxes without allowing deductions for the recognized valid obligations to the charities, etc. This so disturbed the creditors that we were unable to close the arrangement until the inheritance-tax matter was finally adjusted in 1935. In the meantime, under the Treasury Department's interpretation of the quoted section, it is now apparently clear that although the debts involved were incurred prior to January 1, 1934, they were not so incurred by the corporation and therefore the corporation will find itself in the unfortunate position of having been compelled to pledge all of its assets to pay these debts which were incurred prior to January 1, 1934, but unable to deduct such payments, leaving it subject to the penalty tax on moneys it may be forced to realize by its creditors and pay over to them.

I believe you know about the situation generally and the large public interests involved, both on account of the university and its difficult financial picture, the other charities, and the substantial amounts involved for the closed banks. Just to refresh your recollection, the university holds about $2,200,000 of the notes and the closed banks about $1,600,000.

You have been kind enough to say that you would be glad to take this matter up to try to have it straightened out by an amendment of the law at the first opportunity which I very much hope will occur at the coming session of Congress. The estate company has been able so far to get along because its income has been materially less than its interest charges but if we are compelled to sell a substantial block of securities next year to pay down on the debt, as we may well be, it will be a most unfortunate situation for all involved.

As to a definite suggestion for the amendment, the paragraph involved is subparagraph (b) (2) (B) of section 351 and if it were made to read as follows it would, I believe, properly take care of our situation:

"Amounts used or set aside to retire indebtedness incurred prior to January 1, 1934, (including such indebtedness of an estate assumed by a corporation organized to take over its assets and liabilities prior to January 1, 1936, and the indebtedness of such corporation substituted for any such estate indebtedness) if such amounts are reasonable with reference to the size and terms of such indebtedness."

You will notice in this language I have confined it as much as possible so that it will not be broadened in any general way to affect other unsimilar situations.

You may conclude that it may be better to have this taken care of by adding a separate paragraph, in which event I would think it would be accomplished say, by inserting as paragraph (b) (2) (D), the following:

"In the case of a corporation organized prior to January 1, 1936, to take over the assets and liabilities of an estate, amounts used or set aside to retire indebtedness of such estate which existed prior to January 1, 1934 (or any substituted indebtedness of such corporation), if such amounts are reasonable with reference to the size and terms of such indebtedness."

With best wishes for your health, happiness, and success throughout the New Year, I am,

Sincerely yours,

Senator BLACK. Mr. Savoy, you made the statement that a tax of one-half cent a pound would not increase the price retail. As I understand it, you based it on the statement that it would be absorbed by the processor. What economic force is there, or what is there in your judgment, that would cause the processor to absorb that and not pass it on to the public?

Mr. SAVOY. During the operation of the act in the past the processor's margin was narrower than it is now. On the removal of the tax, since January 6, the consumer has had no benefit, and the consumer did not pay materially more during the operation of the tax over the period of a year.

Senator BLACK. Did not that tax immediately follow the taking off of the tariff?

Mr. SAVOY. Yes; it did.

Senator BLACK. So, as a matter of fact, there was no reason why the price should have gone up, economically speaking, if you simply substituted one method of paying the tax for another, was there? I do not quite get how we can anticipate that these particular men would fail to pass this tax on to the consumer.

Senator CONNALLY. The purpose was to take off the tariff and get it through the processing tax, and if you do not get it through the processing tax you are going to lose that amount of revenue.

Senator BLACK. Personally I favor raising taxes by other means than taxing any kind of food and letting it go on to the whole public.

Mr. SAVOY. Since January 6 the price of raws to the refiners has been reduced by virtually the amount of the tax, but the price to

the consumer has not materially changed. It means the margin of the processor has widened.

Senator BLACK. The spread has increased?

Mr. SAVOY. Yes, and our belief is that they will be narrowed materially.

Senator LONERGAN. Mr. Savoy, does refined sugar come into this country in competition with the refiners in this country?

Mr. SAVOY. The act provides that only a given percentage of the total quota may come in a refined state. That is limited to 22 percent from Cuba, and from Hawaii, the Philippines and Puerto Rico.

Senator LONERGAN. I met a man 2 or 3 weeks ago here who was employed in business in Massachusetts, who employed seven or eight hundred people, and he said that they are in competition with these refineries in Cuba.

Mr. SAVOY. They cannot be materially in competition with them, because the major portion of the sugar is imported by Hershey's and the Coca-Cola people.

Senator GUFFEY. Hershey gets the bigger percentage.

Mr. SAVOY. Yes.

Senator LONERGAN. Is there anything in your proposal that would be injurious to the planters in the territories?

Mr. SAVOY. No; we have not changed the situation as it exists in the Jones-Costigan Act.

Senator BLACK. Do the refineries sell sugar at the same price or is there any active competition between them?

Mr. SAVOY. It is virtually the same price. It is determined by the world price, plus tariff, plus tax..

The CHAIRMAN. As a matter of fact, Mr. Savoy, this Jones-Costigan bill gives to the local people their own market, it gives them a corner on the market in the United States?

Mr. SAVOY. Yes.

The CHAIRMAN. And it has worked very satisfactorily?

Mr. SAVOY. It has worked very satisfactorily.

The CHAIRMAN. It was the Jones-Costigan Act and the way it operated that influenced largely this country in making the trade agreement with Cuba to reduce the tariff on Cuban sugars in this country?

Mr. SAVOY. That is right.

The CHAIRMAN. It is the difference between what the tariff was and what it is now that you seek to put this processing tax on?

Mr. SAVOY. On the tariff generally.

The CHAIRMAN. If you did not do that the refinery would increase the price and make it up in other ways, and the producers would not get the benefit of it?

Mr. SAVOY. That is right.

The CHAIRMAN. Suppose we go to the amendments now.

(The proposed amendment is as follows:)

(1) On page 264 strike out lines 1 and 2 and insert in lieu thereof the following:

"TITLE V.—TAX ON SUGAR

"SEC. 701. *Imposition of processing tax.*—There is hereby imposed upon the first domestic processing of sugar beets, sugarcane, or raw sugar, whether of domestic production or imported, a tax, to be paid by the processor, measured by the direct-consumption sugar produced therefrom at the following rates:

"'(1) Direct-consumption sugar, except sirup of cane juice, edible molasses, and sugar mixtures, 0.5 cent per pound of sugar raw value;

"'(2) Sirup of cane juice and edible molasses, 0.125 cent per pound of the total sugar content thereof, translated into terms of pounds of raw value;

"'(3) Sugar mixtures, the sum of the tax computed with respect to the sugar ingredients used in any such mixture at the rates specified in subdivisions (1) and (2) of this section applicable thereto.'

"SEC. 702. *Determination of raw value.*—For all purposes under this title the following methods shall be used to determine the raw value of any sugar or article containing sugar:

"'For all sugar derived from sugar beets by multiplying the number of pounds of the sugar's weight by 1.07;

"'(2) For all sugar derived from sugarcane (except sirup of cane juice, edible molasses and sugar mixtures) testing 92° by the polariscope, by multiplying the number of pounds of sugar's weight by 0.93;

"'(3) For all sugar derived from sugarcane (except sirup of cane juice, edible molasses and subar mixtures) testing more than 92° by the polariscope, by multiplying the number of pounds of the sugar's weight by the figure obtained in adding to 0.93 the product obtained by multiplying 0.0175 by the number of degrees and fractions of a degree of polarization thereof above 92°;

"'(4) For all sugar derived from sugarcane (except sirup of cane juice, edible molasses and sugar mixtures) testing less than 92° by the paloriscope, by dividing the number of pounds of the total sugar content thereof by 0.972;

"'(5) For all sirup of cane juice, by multiplying the number of gallons thereof by 7.56;

"'(6) For all edible molasses, by multiplying the number of gallons thereof by 7.36;

"'(7) For all sugar mixtures, by adding the pounds raw value of the respective ingredients used in the production of such mixture, computed in the manner prescribed in subdivisions (1), (2), (3), (4), (5), and (6) of this section;

"'(8) In the case of any article derived in chief value or partly from sugar beets, sugarcane, or sugar, the amount of sugar established to have been used in the manufacture of the article shall be translated into raw value in the manner prescribed in subdivisions (1), (2), (3), (4), (5), (6), and (7) of this section, in accordance with the respective sugar ingredients used in the manufacture of such articles.'

"SEC. 703. *Definitions of certain terms.*—'For the purposes of this title (*a*) the term "processing" means the last processing of sugar beets, sugarcane, or raw sugar which directly results in direct-consumption sugar.

"(*b*) The term 'sugar' means any grade or type of sugar derived from sugar beets or sugarcane, whether raw sugar or direct-consumption sugar, including but not limited to dry sugar, liquid sugar, invert sugar, invert sirup, sugar mush, molasses, sirups, and sugar mixtures.

"(*c*) The term 'raw sugar' means any sugar as defined above, manufactured or marketed in or brought into the United States in any form whatsoever for the purpose of being or which shall be further refined or improved in quality or further prepared for distribution or use.

"(*d*) The term 'direct-consumption sugar' means any sugar as defined above, manufactured or marketed in or brought into the United States in any form whatsoever, which is to be used or which shall be used for any purpose other than to be further refined or improved in quality or further pepared for distribution or use.

"(*e*) The term 'sirup of cane juice' means sirup made by evaporation of the juice of the sugarcane or by the solution of sugarcane concrete.

"(*f*) The term 'edible molasses' means any molasses when obtained as a byproduct in the manufacture of sugar, except that any molasses when obtained as a byproduct in the process of refining raw sugar shall not be considered as edible molasses within the meaning of this definition if it contains more than 90 percent of the total solids therein in the form of total sugars.

"(*g*) The term 'sugar mixtures' means the mixture of any two or more products or byproducts of sugar beets or sugarcane.

"(*h*) The term 'raw value' means a standard unit of sugar testing 96 sugar degrees by the polariscope. For the purposes of all tax or refund measurements under the provisions of this title, all sugar shall be translated into terms of raw value as provided in section 702 of this title.

"(*i*) The term 'total sugars' or 'total sugar content' means the sum of sucrose (Clerget) and reducing or invert sugars contained in any grade or type of sugar.

"SEC. 704. *Imposition of floor stocks tax.*—There is hereby imposed upon any direct-consumption sugar, whether of domestic manufacture or imported, that on the effective date of this title is held by any person for sale or for manufacture into other articles for sale (including direct-consumption sugar in transit), a tax, to be paid by such person, equivalent to the amount of the processing tax which would be payable with respect to the processing of sugar beets, sugarcane, or raw sugar into such direct-consumption sugar if the processing had occurred on such date. Such tax shall become due and payable on the last day of the month immediately following the effective date of this title: *Provided, however,* That the taxes imposed by this section shall not apply to the retail stocks of persons engaged in retail trade, but the exemption granted herein shall not be deemed to include stocks held in a warehouse on the effective date of this title. In determining the amount of tax due and payable under the provisions of this section, all such direct-consumption sugar shall be translated into raw value according to the provisions of section 702 of this title.

"SEC. 705. *Imposition of import compensating tax.*—There is hereby imposed upon any article processed or manufactured wholly or in chief value from sugar beets, sugarcane, or raw sugar imported into the United States or any possession thereof to which this title applies, from any foreign country, or from any possession of the United States to which this title does not apply, whether imported as merchandise or otherwise, a compensating tax equal to the amount of the processing tax in effect with respect to the domestic processing of sugar beets, sugarcane, or raw sugar into such article. Such tax shall be paid by the importer prior to the release of the article from customs custody or control. In determining the amount of tax due and payable under the provisions of this section, the sugar content shall be translated into raw value, according to the provisions of section 702 of this title.

"SEC. 706. *Exemptions.*—(*a*) No tax under this title shall be required to be paid upon the processing of sugar beets or sugarcane, by or for the producer thereof for consumption by his own family, employees, or household.

"(*b*) No tax under this title shall be required to be paid with respect to 200 gallons or less, in the aggregate, of sirup of cane juice processed during any calendar year when the processing is done by or for the producer of the sugar cane from which such sirup of cane juice was processed, and when the producer, or his family, employees or household, finally prepares the sirup of cane juice for ultimate sale to, or exchange with, consumers: *Provided, however,* That the provisions of this subsection shall not apply when the producer processes, or has processed for him, during any calendar year, for sale or exchange, more than 500 gallons, in the aggregate, of sirup of cane juice.

"(*c*) No tax under this title shall be required to be paid with respect to the processing of sugar beets, sugarcane, or raw sugar for use and which shall be used for animal feed or for distillation purposes.

"SEC. 707. *Refunds and credits generally.*—(*a*) When any product processed wholly or in chief value from sugar beets, sugarcane, or raw sugar, with respect to which a tax imposed under sections 701, 704, or 705 of this title has been paid or is payable, is subsequently disposed of for the exclusive use of the United States, any State, Territory of the United States, or any political subdivision of the foregoing, or the District of Columbia, or is subsequently distributed or used for charitable purposes by any organization, and such disposition, distribution, or use is established to the satisfaction of the Commissioner of Internal Revenue, under rules and regulations prescribed by the Commissioner of Internal Revenue with the approval of the Secretary of the Treasury, an amount equivalent to such tax shall be paid to the United States, the State, the Territory of the United States, or the political subdivision of the foregoing, or the District of Columbia, as the case may be, or to such organization, none of which shall be required to establish that the tax has been paid.

"(*b*) Upon the exportation of any foreign country (or to the Commonwealth of Philippine Islands, the Virgin Islands, American Samoa, the Canal Zone, or the Island of Guam) of any product processed wholly or in chief value from sugar beets, sugarcane, or raw sugar, with respect to which product a tax has been paid or is payable under this title, the tax due and payable or due and paid shall be credited or refunded, and in the case of a person not the taxpayer, an amount equivalent to such tax shall be paid to such person,

who shall not be required to establish that the tax has been paid. Under regulations prescribed by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, the credit, refund, or payment shall be allowed or made to the consignor named in the bill of lading under which the product is exported, or to the shipper or to the person liable for the tax, provided the consignor waives any claim thereto in favor of such shipper or person liable for the tax.

"(c) When any product of sugar beets, sugarcane, or raw sugar, with respect to which a tax imposed under sections 701, 704, or 705 of this title has been paid, is subsequently used as animal feed, or in the production of animal feed, or for distillation purposes, and such use is established to the satisfaction of the Commissioner of Internal Revenue, under rules and regulations prescribed by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, the amount of such tax shall be credited or refunded to the person who uses such product as animal feed, or in the production of animal feed, or for distillation purposes.

"(d) In determining the amount of refunds, credits, or payments to be made under the provisions of this section, the sugar or the sugar content of the article shall be translated into raw value, according to the provisions of section 702 of this title.

"SEC. 708. *Refunds, credits, and abatements relating to processed articles.*—(a) When the processing tax imposed by section 701 is wholly terminated:

"'(1) There shall be refunded or credited to any person holding for sale any direct-consumption sugar upon the processing of which the tax is terminated with respect to the processing of which direct-consumption sugar the tax under this title has been paid; and

"'(2) There shall be credited or abated to any person holding for sale any direct-consumption sugar with respect to the processing of which a tax under this title is payable, where such person is the processor liable for the payment of the tax; and

"'(3) There shall be refunded or credited (but not before the tax has been paid) to any person holding for sale any direct-consumption sugar with respect to the processing of which a tax under this title is payable, where such person is not the processor liable for the payment of such tax.'

a sum equivalent to the amount of the processing tax which would have been payable with respect to the processing of the sugar beets, sugarcane, or raw sugar into such direct-consumption sugar if such processing had taken place immediately prior to the termination of the tax: *Provided, however*, That the credit, refund, or abatement referred to in this subsection shall not apply to the retail stocks of persons engaged in retail trade that are held on the date the tax is wholly terminated.

"(b) In determining the credit, refund, or abatement to be made under the provisions of subsection (a), all such direct-consumption sugar shall be translated into raw value, according to the provisions of section 702 of this title.

"SEC. 709. *Collection of taxes.*—(a) All provisions of law, including penalties, applicable with respect to the taxes imposed by section 600 of the Revenue Act of 1926, and the provisions of section 626 of the Revenue Act of 1932, shall, insofar as applicable and not inconsistent with the provisions of this title, be applicable in respect to taxes imposed by this title: *Provided*, That the Commissioner of Internal Revenue is authorized to permit postponement, for a period not exceeding 180 days, of the payment of not exceeding three-fourths of the amount of the taxes covered by any return under this title. The Commissioner of Internal Revenue may permit the taxes in the case of sugar to be paid each month on the amount marketed during the next preceding month and in such case may postpone payment of the entire tax for a period not exceeding 180 days.

"(b) In order that the payment of taxes under this title may not impose any immediate undue financial burden upon processors or distributors, any person subject to such taxes shall be eligible for loans from the Reconstruction Finance Corporation under section 5 of the Reconstruction Finance Corporation Act.

"(c) Under regulations made by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, any person required pursuant to the provisions of this title to file a return may be required to file such return and pay the tax shown to be due thereon to the collector for the district in which the processing was done or the liability incurred. Whenever the

Commissioner of Internal Revenue deems it necessary, he may require any person or class of persons handling or dealing in any commodity or product thereof with respect to which a tax is imposed under the provisions of this title to make a return, render under oath such statements, or keep such records, as the Commissioner of Internal Revenue deems sufficient to show whether or not such person, or any other person, is liable for the tax.

"SEC. 710. *Penalties for false statements concerning tax.*—(*a*) Whenever in connection with the purchase of, or offer to purchase, any commodity subject to any tax under this title, makes any statement, written or oral, (1) intended or calculated to lead any person to believe that any amount deducted from the market price or the agreed price of the commodity consists of a tax under this title, or (2) ascribing a particular part of the deduction from the market price or the agreed price of the commodity to a tax under this title, knowing that such statement is false or that the tax is not so great as the amount deducted from the market price or the agreed price of the commodity and ascribed to such tax, shall be guilty of a misdemeanor, and upon conviction thereof, shall be punished by a fine of not more than $1,000 or by imprisonment for not exceeding 6 months, or both.

"(*b*) Whoever in connection with the processing of any commodity subject to any tax under this title, whether commercially, for toll, upon an exchange, or otherwise, makes any statement, written or oral, (1) intended or calculated to lead any person to believe that any part of the charge for said processing, whether commercially, for toll, upon an exchange, or otherwise, consists of a tax imposed under this title, or (2) ascribing a particular part of the charge for processing, whether commercially, for toll, upon an exchange, or otherwise, to a tax imposed under this title, knowing that such statement is false or that the tax is not so great as the amount charged for said processing and ascribed to such tax, shall be guilty of a misdemeanor and, upon conviction thereof, shall be punished by a fine of not more than $1,000 or by imprisonment for not exceeding 6 months, or both.

"(c) Whoever in connection with any settlement under a contract to buy or sell any commodity, or any product or byproduct thereof, subject to any tax under this title makes any statement, written or oral, (1) intended or calculated to lead any person to believe that any amount deducted from the gross sales price in arriving at the basis of settlement under the contract consists of a tax under this title, or (2) ascribing a particular amount deducted from the gross sales price in arriving at the basis of settlement under the contract to a tax imposed under this title, knowing that such statement is false or that the tax is not so great as the amount so deducted and ascribed to such tax, shall be guilty of a misdemeanor and, upon conviction thereof, shall be punished by a fine of not more than $1,000 or by imprisonment for not exceeding six months, or both.

"SEC. 711. *Limitations on refunds and credits.*—(*a*) No refund or credit shall be made or allowed under section 707 unless, within 1 year after the right to such refund or credit accrues, a claim for such refund or credit (conforming to such regulations as the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, may prescribe) is filed by the person entitled to such refund or credit.

"(b) No refund, credit, or abatement of any amount of any tax shall be made or allowed under section 708 of this title unless, within 120 days after the right to such refund, credit, or abatement accrues, a claim for such refund, credit, or abatement (conforming to such regulations as the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, may prescribe) is filed by the person entitled to such refund, credit or abatement. No such claim shall be allowed for an amount less than $10.

"(*c*) The provisions of section 3226, Revised Statutes, as amended, are hereby extended to apply to any suit for the recovery of any amount of any tax, penalty, or interest which accrues under this title (whether an overpayment or otherwise), and to any suit for the recovery of any amount of tax which results from an error in the computation of the tax or from duplicate payments of any tax, and to any suit for the recovery of any refund, credit, or abatement authorized by section 707 or 708.

"SEC. 712. *Applicability of this title.*—The provisions of this title shall be applicable to the United States and its possessions, except the Commonwealth of the Philippine Islands, American Samoa, the Canal Zone, and the Island of Guam.

"TITLE VI—GENERAL PROVISIONS

"SEC. 801. *Definitions.*—

"(2) Page 236, line 3, strike out the figures '702' and insert in lieu thereof the figures '802.'

"(3) Page 236, line 8, strike out the figures '703' and insert in lieu thereof the figures '803.'"

Senator KING. Can you tell me why it needs 12 pages?

Mr. SAVOY. Yes, sir.

Senator GEORGE. You provide for methods for refund, and everything in there?

Mr. SAVOY. Yes, sir, we put back all of the provisions that are necessary to administer the act. If we have to have a processing tax on a given event we define what that event is, and we must define those terms. In addition, since it is based on raw value you must define what raw value it.

Senator WALSH. How much tax will be realized?

Mr. SAVOY. $66,000,000.

Senator GEORGE. You have definitions for sugar, sirup, and so forth?

Mr. SAVOY. Yes, sir; we felt that it was essential not to leave anything having to do with the imposition of the tax to regulation.

The CHAIRMAN. That is in the present law?

Mr. SAVOY. That is in the present law.

Senator GEORGE. Is there any change from the present law at all?

Mr. SAVOY. The only change is as respects floor stocks. Since we are not reducing the tariff and since we do not have the two types of sugar that we had at that time, those which had paid the higher duty and those which were coming in under the lower duty——

Senator GEORGE. From Cuba?

Mr. SAVOY. From Cuba—we have not put in the exemption provisions which we were required to do at that time in order to equalize the situation.

Senator GEORGE. In other words, when this goes in you are going to have a processing tax on sugar?

Mr. SAVOY. Since they will move in channels of trade in competition with the newly processed sugar.

Senator GEORGE. And you are going to have them absorb that and you are not going to pass the processing tax on to the consumer, you are not going to raise prices?

Mr. SAVOY. Yes.

Senator WALSH. Is this presented for the purpose of increasing the revenues to the Government?

Mr. SAVOY. Yes, sir.

Senator WALSH. And for that purpose only?

Mr. SAVOY. Yes.

The CHAIRMAN. We lost it when we reduced the tariff.

Senator KING. You stated a few moments ago that you expected the soil conservation administration was going to go out and spend millions of dollars to aid the farmers.

Mr. SAVOY. Yes.

Senator CONNALLY. That was whether they levied this tax or not.

The CHAIRMAN. Suppose I appoint a subcommittee to look over this until Monday? I will appoint Senator King, Senator George,

and Senator Couzens. You go ahead and give us your report on it on Monday.

Senator GEORGE. Does the industry generally know about this? Did they have any hearings?

Mr. SAVOY. There have been no hearings on it. The matter has not been presented before.

Senator GEORGE. I mean both the producers and refiners; do they know what it is?

Mr. SAVOY. The producers know what it is, because that has been discussed with all the producer organization and they have favored it. Now, the refiners have seen it also, and, as Senator Guffey said, he received word from his refiners today saying they were in favor of the processing tax.

Senator GEORGE. I am curious to know whether the refiners who make and produce sugar in Cuba object to it.

Mr. SAVOY. The refiners generally, and their representatives, have both come in to discuss the matter and have not raised any objection.

The CHAIRMAN. Senator George, you and Senator King and Senator Couzens will take up this matter and we will discuss it on Monday.

Senator Walsh, you had something to present.

Senator WALSH. This is changing the definition of "bank or trust company" in section 104 of the proposed Revenue Act of 1936.

(a) *Definition.*—As used in this section the term "bank" means a bank or trust company incorporated and doing business under the laws of the United States (including laws relating to the District of Columbia), of any State, or of any territory, a substantial part of the business of which consists of receiving deposits and making loans and discounts, or of exercising fiduciary powers similar to those permitted to national banks under section 11 (k) of the Federal Reserve Act, as amended, and which is subject by law to supervision and examination by State or Federal authority having supervision over banks.

I am informed that this will not make any material difference in the revenue produced.

The CHAIRMAN. That is to take care of the trust situation?

Senator WALSH. Yes.

Mr. KENT. May I state, Senator Harrison, that this is not a Treasury proposal. Several of us helped yesterday in polishing it up, but the Treasury feels that the amendment is properly drawn and it has no objections to it, if the committee feels that it is a desirable policy to do so.

I might say in some States they have laws which really classify institutions in two groups, more or less: Those that are engaged primarily in the banking aspect and those that are engaged in the business of administering and receiving trust deposits, and under those laws similar restrictions are applied to trust complaints with respect to the distribution of earnings before proper reserves have been built up as are applied to banks, and to that extent their situation is substantially similar.

Senator KING. Mr. Parker, I sent a gentleman to talk with you, a Mr. Bennett, who said he wanted to say something about banks. Was his proposition involved in this? Would that be involved in this?

Mr. PARKER. No. He was not particularly interested in that. He was worried about the House bill which, in regard to the bank-holding company, might impose a tax of 15 percent and then another

15 percent when the dividends went to the holding company on account of the intercompany dividends proposition, but, as I understand the action of the commitee now with relation to these bank-holding companies, it seems to me it ought to be reasonably satisfactory.

The CHAIRMAN. I think the committee thought something ought to be done with reference to that situation, and if this amendment is in order, in proper form, I do not see why there should be any objection.

Mr. KENT. Mr. Chairman, I was asked to report on a matter that came up in the meeting of the committee day before yesterday during the afternoon. It was suggested that the amendment to section 115 (c), that is the liquidation provision, should be given a limited retroactivity.

Senator KING. State that again, please.

Mr. KENT. Should be given a limited retroactivity. One case was called to the attention of the committee where a little manufacturing corporation down in Louisiana which had been operating for a great many years had received some unfortunately erroneous advice from someone connected with the revenue service and it found itself caught in a trap under this liquidation provision as it stands, because it had to take up 100 percent of the gain realized in income, and, if they had been properly advised, there were other ways in which they could have achieved the same result without being caught in that manner.

The committee was unwilling to act upon the amendment at that time without having further information as to whether there were any other cases which had developed under this section where similar circumstances were not present and where a retroactive amendment would entitle them to a refund.

I made inquiry down in the Income Tax Unit yesterday morning and I find they have a record of only two cases. One is this Louisiana case and the other case is a somewhat different case from another district, but is equally bad. So that there would be no appreciable revenue effect if that suggestion were adopted.

Senator KING. You think it was not the fault of the taxpayer but the culpability of the representative of the Government?

Mr. KENT. That is right. He was acting honestly; it was just a new amendment.

Senator CONNALLY. Mr. Chairman, as I recall it, the only case was instead of being applicable on the date of the enactment of the act in 1935 they made it 1934. I will ask that the committee authorize it. I will see that somebody draws it up properly.

The CHAIRMAN. The amendment is not drawn yet?

Senator CONNALLY. It is drawn, but I have not got it here.

Mr. PARKER. That is a simple matter. We would know how to make it effective.

The CHAIRMAN. All right.

Senator KING. Did you make such an investigation down there that would give us assurance there was not a large number that would fall in that category?

Mr. KENT. I think so. I consulted with one of the veteran men there who searched the income-tax records. They have a very careful classification of all these cases down there, and there were only

the two cases of which they had any record. Of course we had suspected, and this confirms our conviction, that the 1934 amendment to section 115 had really operated as simply to block liquidations in such a manner that the section would not be applicable.

Senator GERRY. Are we going to take up the question of liquidation?

The CHAIRMAN. Yes. I understand you have an amendment ready?

Mr. PARKER. We are not ready to report on general liquidation, that is what they call simplification of corporate structures; we are not ready to report on that. We are going into that this afternoon.

Senator CONNALLY. Was this amendment adopted?

The CHAIRMAN. That applies to 1934? Is that the year?

Senator CONNALLY. That is right.

The CHAIRMAN. Without objection, that will be adopted.

We want to take up the foreign corporations proposition.

Mr. PARKER. Yes; so we can progress to draft a bill.

The CHAIRMAN. What page is this one?

Mr. PARKER. The main portion of it is on page 25. You will remember that we have already disposed of the taxation of nonresident aliens. This simply now is a taxation of foreign corporations, and since of course the principal changes in the bill are in connection with the taxation of domestic corporations it is a matter of trying to be as consistent as we can and still be practical in a taxation of these foreign companies.

Senator GERRY. Mr. Parker, do the Philippine corporations come under this section?

Mr. PARKER. No, Senator. The trouble with the Philippine proposition was the matter of the individual stockholders. That is a separate proposition.

Senator GERRY. That is a separate proposition?

Mr. PARKER. Yes.

Senator CONNALLY. Mr. Chairman, let me ask the committee a question. Is there any sound reason of government policy which we should not tax foreign corporations more than we do our own corporations?

The CHAIRMAN. That is what they have done in this House bill.

Senator CONNALLY. I do not see why we should not. We levy tariffs to protect our people, we do this and do the other, and then we invite the foreign corporations to come in here and compete with our own people and levy the same tax on them as we levy on our own people.

Mr. PARKER. Senator, we also have our own foreign corporations operating in other countries.

The CHAIRMAN. I think you are absolutely right, in principle. We have got to give it consideration because of the system that is built up. Section 231, page 185, what does that mean?

Mr. PARKER. That is the first class of corporations. Those are the corporations that are resident here, that are doing business here, that have an office or place of business here.

Senator KING. Like some of the Canadian corporations?

Mr. PARKER. They might be Canadian or they might be any other country.

The CHAIRMAN. You put 22.5 percent on those corporations.

Mr. PARKER. That was what was done in the House bill. Our recommendations are slightly different from that.

The second class of corporations are those that are not engaged in business here. Under the House bill, you will recall, the maximum tax was 42.5 percent on our own corporations, so the 22.5 percent was a considerable cut. It is true our own corporations might have paid no tax, but it was about half way between.

The CHAIRMAN. Why did they arrive at 22.5? We have tried to give them favored treatment.

Mr. PARKER. No. When you come to the foreign corporation doing different percentages of its business here, and doing business in other places in the world, it seemed to us it was just impractical to try to levy the tax on them in respect to the amount of the dividends they paid. In other words, the distribution of dividends by an English company over in London, with checks made out to London stockholders, English stockholders, it did not seem that we could properly apply the undistributed profits tax plan to the foreign corporations. It leads into a lot of difficulty, the difficulty of finding out their entire income and allocating the portion that comes from the United States, and what is the dividend paid out, or was paid out of American profits or foreign profits. It just does not fit in.

Senator WALSH. We levy the same tax on the foreign corporations that we levy on domestic corporations, but we add the contractual obligation not to pay dividends?

Mr. PARKER. That is what the House bill did. We have a little different theory now.

Mr. KENT. May I interrupt there? Another thing that influenced the selection of the 22.5-percent rate was this, that under the House bill it was proposed to raise the additional revenue by increasing the burden upon corporate enterprise, looking at it as a totality, by about $600,000,000, which compared with about $1,100,000,000 derived from corporations under the existing corporate-tax laws. Now that was an increase in the neighborhood of 50 percent, and it was felt entirely equitable that foreign corporations doing business in this country should contribute to the revenue needs of the Government in a substantially similar proportion, and for that reason the tax on them was raised from 15 to 22.5 percent.

The CHAIRMAN. About 50 percent?

Mr. KENT. About 50 percent.

The CHAIRMAN. Now, if we place this other matter at a flat 18 and 7 percent, do you think it would carry out the same theory?

Mr. PARKER. We came to an agreement on that after a long time and we were prepared to recommend that the foreign corporation pay 22 percent. We arrived at it in this way: If they pay 18-percent normal tax on individuals and we add to it 4 percent that would be paid by the individual stockholders, that would give us 22 percent. Under this bill the highest rate of tax that any domestic corporation can pay is 23.7 percent.

Senator WALSH. That is where they distribute nothing?

Mr. PARKER. That is where they distribute nothing. The highest tax they will pay is 23.7 percent. We have got the foreign corporation paying 22 percent.

The CHAIRMAN. Of course you would apply the 7 percent then on the retained earnings?

Mr. PARKER. No. We did not want to go into the distribution of the foreign corporations.

Senator GEORGE. It is more or less impractical.

Mr. PARKER. But if we did apply the 7 percent the most we could get out of it in that case would be 23.7 percent.

The CHAIRMAN. What is the viewpoint of the committee?

Senator CONNALLY. Why not make it 23 percent instead of 22 percent? That would approximate the House rate.

Mr. PARKER. We suggested 22 percent, the highest rate is 23.7 percent and the House rate is 22.5 percent. I am just telling you how we arrived at it. We took the 18 percent and added the 4 percent normal, making it 22 percent.

Senator KING. Would there be any repercussions elsewhere, any reprisals, any retaliations whereby we would lose more than we would gain?

Mr. PARKER. We have a sound reason for it.

Senator CONNALLY. I do not see where it would raise repercussions. We raised the tax on our own corporations.

The CHAIRMAN. I do not see how they can kick on that. Without objection we will fix the rate then at 22 percent on these foreign corporations.

Mr. PARKER. I will point out now that these foreign residence corporations file a return just like an American corporation, though we do penalize them in one further respect, we recommend that we do not give them the $1,000 exemption that we give to domestic corporations. They have their income from elsewhere and we do not give them a $1,000 exemption.

The CHAIRMAN. Without objection, the $1,000 exemption will not apply to them.

Mr. BEAMAN. That includes foreign insurance companies?

Senator GEORGE. Yes; all of them.

Mr. PARKER. Now, we come to the other class of corporations.

The CHAIRMAN. Nonresident corporations.

Mr. PARKER. Those that are engaged in business here and do not have any office or place of business here. At the present time the payments to such corporations are withheld at the source at the rate of 15 percent, in the case of interest, royalties, and similar annual income, and on dividends they have deducted at the source only this 1.5-percent tax, on account of the intercompany dividend proposition.

The CHAIRMAN. Let us take up the foreign corporations that have no business here, that do not live here, that have their headquarters in some foreign country but they do business here.

Mr. PARKER. They do not do business here. Suppose you had an English investment trust and they have got some railroad bonds, or what not, they are not over here, they just clip the coupons and send them over here to the bank for collection, that is all they do. When the bank sends them the money they withhold 15 percent of the interest.

The CHAIRMAN. That is the present law?

Mr. PARKER. That is the present law. But if they get dividends from the United States Steel stock there will be deducted at the source only what amounts to 1.5 percent.

The CHAIRMAN. What do you propose to do now?

Mr. PARKER. Under the present law they have a right to file a return in spite of the fact that they are not residents, and in spite of the fact that they do no do any business here, they can file the return and get the advanage of certain deductions. We propose not to have these people file returns, except in exceptional cases, and we propose to withhold 18 percent on these payments, gross. There is no deduction. The 18-percent tax is really on gross income, you might say, instead of net. But, of course, not being engaged in trade or business here their deductions should not be very large. That is on interest, royalties, and all other income except dividends.

On dividends, inasmuch as our own corporation has only withheld, or has already paid at least 18 percent, we propose to withhold 10 percent in the case of all countries except Canada, where we propose to withhold 5 percent.

Senator CONNALLY. How about Mexico?

Mr. PARKER. Yes; Mexico.

The CHAIRMAN. Why do you not say "contiguous countries?"

Mr. PARKER. Yes; contiguous countries. In respect to dividends we expect to treat the foreign corporation just like the foreign individual. That is a practical way to do also, because the foreign corporations can readily defeat a higher withholding rate by holding their stock in the names of nominees.

The CHAIRMAN. Are we getting any revenue from that source now?

Mr. PARKER. We are getting very little revenue from the dividends, because we practically withhold a very insignificant amount of the dividends.

The CHAIRMAN. You think we will get some revenue under this law?

Mr. PARKER. Yes. What is proposed is that the tax on foreign corporations would be 18 percent on all income except from dividends.

The CHAIRMAN. To be withheld at the source?

Mr. PARKER. Yes; and on dividends it will be 10 percent.

Senator KING. You mean foreign corporations that are not functioning in the United States?

Mr. PARKER. That is right.

Senator COUZENS. I move that be approved.

The CHAIRMAN. Without objection that will be agreed to.

Mr. PARKER. I should have mentioned that it is less in the border countries.

The CHAIRMAN. That is, in contiguous countries it is 5 percent?

Mr. PARKER. That is right. That is what they do with us.

Senator BLACK. Mr. Parker, you mentioned royalties and dividends. What about the insurance company in London, for instance, that does not have an office in America? There are a great many that do not. They write marine insurance and they do a very large business.

Senator KING. Some of the States, I think my State, forbids any insurance company doing business in the State without having a residence in the State.

Senator BLACK. That is correct. A great many people engaged in the shipping business go to London, American shippers that are subsidized by the Government, buy their insurance in London. Does that apply to them?

Mr. PARKER. Well, the law enumerates, along with interest and other things, just what is being withheld. It enumerates premiums.

Senator BLACK. It does?

Mr. PARKER. Yes. Most of the companies that are likely to do a substantial amount of business here it seems to me would be engaged in trade or business of the United States.

Senator CLARK. The American shippers can go to London and negotiate an insurance contract, they receive a subsidy from the United States Government for carrying merchandise on American ships, but the insurance is carried in a London company, is that right?

Senator BLACK. That has been a very serious complaint from American insurance companies. I know that the insurance companies are bitterly complaining about the fact that American shippers go to London and buy their insurance there.

Mr. PARKER. The way I interpret the law, it would be too severe on them. As I interpret the law, if I pay a premium to a British insurance company that is not doing business here I would have to take 18 percent off the premium and send it to the Government.

Mr. BEAMAN. They are not taxable under this bill.

Senator BLACK. I simply wanted to call the attention of the committee to it.

Mr. PARKER. That is right. Insurance companies are taxed separately. This would not apply to transactions of that kind. I think we ought to go over to the insurance section and do it over there.

Senator BLACK. I simply wanted to call the attention of the committee to it, because, as I thought, there is no provision in here that would require any payments by those companies who sell insurance in London to our people here. It may not be wise to do it.

The CHAIRMAN. I thought they were included in this proposition.

Mr. PARKER. Oh, yes; they have to pay their 18 percent, they have to pay that on their business. They are not free from tax.

Senator BLACK. They are not engaged in business in this country, they go to London and buy it.

Senator GERRY. How would you get at them?

Senator BLACK. Well, with reference to the transactions of the American company, they are required to withhold a part of the payment. It may not be a wise policy to require that in that connection.

The CHAIRMAN. You mean an insurance company here would take out an insurance policy in London?

Senator BLACK. No.

Senator CLARK. It is the shipowner who wants maritime insurance; he goes over to London and negotiates a maritime insurance contract with some insurance company or set of underwriters like Lloyds, and the premium is paid frequently from funds furnished by the United States Government in the way of subsidy, that is paid to some British concern.

The CHAIRMAN. How do you get at it, Mr. Parker?

Mr. PARKER. That is a special case. The transaction is made abroad. We would like to make a special investigation into that.

Mr. KENT. You would have a substantially similar situation if the American shipowner that wanted insurance sent a cable to London, to an insurance company over there, and made an offer to place insurance with them and they accepted by cable, because under the accepted legal principles of the common law that contract is completed in London when the cablegram is sent accepting the agreement.

Senator KING. Would not this case be analogous: Suppose I am in London. I have a good deal of faith in one of the life-insurance companies there and I get life insurance for $25,000, and I remit my premium to them every year. How can you tax that?

Mr. Parker. I do not know.

Senator CLARK. You can remedy it by an amendment of the ship subsidy bill.

The CHAIRMAN. I do not see how you can get at them. Is there any other phase of this thing now that we have not touched?

Mr. PARKER. Just a few minor points.

Senator KING. We got through the major points?

Mr. PARKER. Yes; in dealing with the resident corporation, which is taxed practically the same as our corporation, when they get dividends from a domestic corporation they are going to include 10 percent of that dividend, which has already been taxed, of course, in their income just like a domestic corporation.

Now, as I pointed out, the $1,000 exemption is not allowed to any of these foreign corporations doing business here, but we do propose to give them the Liberty bonds and excess profits tax credit, just like our own corporations, because they are subject to the capital stock and excess profits tax.

The CHAIRMAN. I do not understand what you mean by that.

Mr. PARKER. It was agreed the other day that for the purpose of the corporate taxes we would give them a credit against net income of the excess profits tax paid, that is for our own domestic corporations. We suggest you do the same thing with the foreign corporations doing business here.

The CHAIRMAN. All right, without objection that will be understood.

Senator COUZENS. And also on the tax-exempt income.

Mr. PARKER. The tax-exempt income?

Senator COUZENS. Yes.

Mr. PARKER. The Liberty Bond Act requires that.

The CHAIRMAN. Without objection you can write it that way.

How about the foreign banks?

Mr. PARKER. Now, foreign banks, there has been an investigation made of foreign banks and we find that there were a couple of foreign banks in New York, and one in California, and the laws of those States now require that they can take the deposits only from nonresidents. They cannot deal with our own residents. Therefore, it seems to us that foreign banks ought to be taxed 22 percent, the same as any foreign corporation.

The CHAIRMAN. You mean these foreign banks are located in the United States?

Mr. PARKER. That is correct.

The CHAIRMAN. They cannot take deposits from anybody except a foreigner?

Mr. PARKER. That is right. They do an exclusively foreign business. We think they ought to be taxed 22 percent.

The CHAIRMAN. Is there any objection to that? That seems to me to be all right. All right, without objection, we will make that 22 percent. I did not know that we had any such banks.

Mr. PARKER. We also propose that you take away the $1,000 exemption from foreign insurance companies, China trade corporations, and so-called section 251 corporations. Eighty percent of their business comes from the possessions of the United States.

Senator KING. I move we accept that.

The CHAIRMAN. Without objection that will be done.

Mr. PARKER. The next thing is in section 119, page 125. The House bill provided for a change here on page 125, paragraph (B), and we propose that we eliminate that change and return to the present law, except for lines 5, 6, 7, 8, and 9.

The CHAIRMAN. Now explain exactly what that section (B) is.

Mr. PARKER. I think I will ask Mr. Beaman to explain that.

Mr. BEAMAN. Here is the situation, gentlemen, that led to the change in the House bill: The House bill provides, and the present law provides, and your own bill provides, that certain people, under certain circumstances at least, are taxed on their net income from sources in the United States and not on any income that is not from sources in the United States. Therefore, it is important to determine what is net income from sources in the United States. In section 119 there is laid down a whole lot of rules. One of the rules is that dividends from domestic corporations was income from sources within the United States.

Now, the question that has got to be settled arises, obviously: What about dividends from foreign corporations?

Senator KING. To American citizens?

Mr. BEAMAN. No; not to American citizens. They are taxable on all their income from anywhere. It is unimportant to know in their case whether it is income from sources within the United States or not. In the case of the foreigners it is important, because they are only taxed on income from sources in the United States.

So we get down to the question: Is the dividend from foreign corporations income from sources within the United States?

The present law says that if the foreign corporation during the period of 3 years back has got 50 percent or more of its gross income from sources within the United States, then all the dividends paid by it constituted income from sources within the United States.

Senator KING. That is a rather hit-and-miss proposition.

Mr. BEAMAN. It is. It seemed perfectly unfair to the House, and I think it will to you, gentlemen, to say that if a corporation gets 51 percent of its income from sources within the United States and pays out $100 in dividends, that the whole $100 is income from sources within the United States. Obviously only $51 of that $100 is income from sources within the United States. That is one change the House bill made. As Mr. Parker said, we recommended that it be rewritten, confining it to the pro rata amount.

Now, the House bill went further and provided that it should not be income from sources within the United States unless 85 percent

of the gross income of the corporation was realized or was derived from sources within the United States, and, furthermore, that if the foreign corporation was not engaged in trade or business in the United States, then no dividend, under any circumstances, should ever be considered as income from sources within the United States.

Now that opens up a very large loophole which I will describe to you. Senator King, I suppose you and I have got $1,000,000 apiece which we want to invest and accumulate an income on; we organize a foreign corporation, we organize two of them, we organize a parent foreign corporation which owns all the stock of a foreign subsidiary; we take our $2,000,000 and give it to the foreign sub, which buys United States bonds, investments, and so forth, and all we get out of it from that foreign sub is the tax we withhold at the source—which was just agreed upon as 18 percent, or in the case of dividends 10 percent—the foreign sub then declares out all its income in dividends to the foreign parent, and assume that under the House bill 10 percent of the foreign investment would not be income from sources within the United States, then the foreign parent would not only pay no tax to us because it had no income from sources within the United States, but it would not be subject to section 102, no matter how many terrible teeth you put in section 102, because you have got no income. You can make it 100 percent or zero.

So in order to get away from that terrible loophole we propose that you go back to the present law and say that if a foreign corporation has more than 50 percent of its gross income from sources within the United States, the dividends are paid to the extent of that percentage, whatever it is, and that shall be income from sources within the United States. Now, we are faced with the proposition that the House was faced with, as to what cases there are that you shall require a withholding in.

Now that, of course, is entirely a matter of policy. So far as we are concerned, we do not change the House bill, unless you gentlemen want to change it. We will carry out the House bill, unless you gentlemen want to change it. We propose that you write into the withholding section a provision that foreign corporations shall not withhold anything on dividends unless that corporation is engaged in trade or business within the United States, and even if it is engaged in trade or business within the United States it shall not be required to withhold on is dividends unless more than 85 percent of its income for the 3-year period preceding was derived from sources within the United States, and if it has derived more than 85 percent of its income, say it has derived 90 percent of its income from sources within the United States, every time it pays out $100 in dividends it will be required to retain $90. The tax is on $90, it is 10 percent on the $90.

That, of course, leaves a little gap for the fellow that receives it under the preceding section, it constitutes income from sources within the United States, but there is no withholding unless the percentage is over 85. But the important thing is it closes up the gap, or loophole of reorganizing a couple of foreign corporations and getting them out of absolutely any possibility of reaching them under section 102.

Mr. KENT. If I may make a remark about the withholding question, we were influenced in the suggestion on that proposition, to a very considerable extent, and I think the House committee was also, by the fact that other countries do not normally require foreign corporations doing business in their territories to withhold tax on dividends paid by such foreign corporations to their shareholders. There are some difficulties that are present there. The revenue involved is not very important, and I think there is something to be said from the practical point of view.

Senator KING. The administrative features ought to be considered.

Mr. KENT. Yes.

Senator GERRY. I would like to ask Mr. Beaman something, Mr. Chairman. I do not know that I have this clear. Do I understand that the foreign corporation gets the dividends received from this country without paying a tax?

Mr. BEAMAN. That is not the question at all. That question you disposed of awhile ago. On the dividends received by a foreign corporation from this country you taxed the company 10 percent, or 5 percent if it was a contiguous country.

Senator GERRY. If they invest in securities of foreign countries?

Mr. BEAMAN. No; it is a broader thing than that. What we are dealing with here is the question of a foreign corporation that pays dividends to a foreign individual, or another foreign corporation. Shall that be considered as income from sources within the United States? Because if it is not considered as income from sources within the United States it is not taxable to that recipient.

For instance, if foreign corporation X pays a dividend to me, in Paris, and also pays a dividend to the Kent Corporation in London, then the question is: Do I, as an individual, a Frenchman, and Kent, and English corporation—are we taxable as one corporation X, are we taxable on what corporation X paid us as a dividend?

Senator GERRY. If the profit was made in this country?

Mr. BEAMAN. No; if I, as the Frenchman, lived in Paris, and the British corporation was in London, corporation X, which is a foreign corporation, pays a dividend to me and also pays a dividend to Kent Corporation, the question is: Is that dividend in my hands and in Kent's hands income from sources within the United States? Because, if it is not, it is not taxable. If it is, it is taxable. This rule that I have been describing attempts to settle that question.

The CHAIRMAN. Have you got your amendment drafted carrying out the ideas that you have expressed here?

Mr. BEAMAN. Partially.

The CHAIRMAN. All right.

Senator KING. I move they complete it and that they dispense it to us as soon as possible.

Mr. KENT. In order to avoid the necessity of bringing this matter up again, Senator Harrison, I would like to say that we have one or two suggestions.

The CHAIRMAN. You mean on this last question?

Mr. KENT. Yes; this general problem. I would like to say that there are one or two suggestions other than a few clerical changes, that is the clarification of the text that we would want to make to the experts. The principal one is a provision which would make it

clear that the penalties applicable in respect to the tax as imposed by title I of the act shall be applicable in respect to the liability imposed by section 143 and section 144; that is, if a withholding company was under a duty, under the law, to withhold the tax and fails to do so, it shall be subject to the proper penalties under the statute. And, moreover, that if there is a question as to the amount of tax which he is liable to withhold, if that question arises, he should be given the same records of the Board of Tax Appeals that any other taxpayer would pay under the same circumstances.

The CHAIRMAN. All right.

Mr. KENT. There is one other thing. I have been making some progress, I believe, on including in section 211 a legislative definition as to what is meant by "engaged in trade or business in the United States", which it is anticipated is the one thing in this set-up that would be likely to be the most fertile source of controvery.

Senator KING. That is on page 211?

Mr. KENT. Yes.

Senator GERRY. What page is that?

Mr. KENT. That is page 180. What we should endeavor to do is to define "trade or business" in such a way as to give us a legislative rule in respect to the border-line situations where we are likely to have the most trouble. We have a good many precedents on what constitutes doing a trade or business, and I should like to have the approval of the committee in attempting to draft language that would cover it.

The CHAIRMAN. You and the experts try to get together on the rule.

Mr. PARKER. There is one thing in connection with the draft that is not definte about the 90-day proposition.

Mr. KENT. Yes. I may say that there have been several references in the committee's discussion to these complaints regarding our taxing and collecting the tax from these people who come over here on commercial business for just 3 or 4 weeks, perhaps, and find themselves confronted with an income-tax demand when they are at the point of leaving the country.

Senator KING. Some have been here only 10 days, when they have made a pretty good sale here.

Mr. KENT. Yes. I think it is possible to eliminate most of that difficulty. It seems to me it is rather undignified and absurd for this Government to hold the employee of a foreign corporation, or foreign individual, who has come over here to negotiate some contracts, or some business, and he being held in order to collect a few dollars of tax from him. It leads to international ill will out of all proportion to the amount of revenue involved.

Senator KING. Especially when we are sending our representatives abroad. We had Mr. Peak and others trying to find markets for our wheat and cotton.

Mr. KENT. Yes.

The CHAIRMAN. What else is there?

Mr. KENT. There was one other matter that I am informed I was asked to report upon at the request of one of the Senators, I believe it was Senator Hastings. He is not here. Do you wish me to bring that matter up?

The CHAIRMAN. No; we will wait until he gets back.

There is a brief here from Mr. Haussermann, this gentleman who is from the Philippines.

Mr. PARKER. It has not been discussed with the experts. I am not ready to make any suggestion. His proposition was something else. As a practical matter, if a man goes to the Philippines and conducts a grocery store——

Senator KING (interrupting). Assuming he is an American citizen?

Mr. PARKER. Assuming that he is an American citizen, the income he gets is not subject to the income tax of the United States, but it is subject, of course, to taxes there, he is subject to the Philippine taxes.

Now, if a man is over in the Philippines and he incorporates a grocery store, for instance, and he gets dividends from that corporation, he is taxable on that under the income taxes of the United States. Mr. Haussermann claims that puts that kind of person at a serious disadvantage with competitive concerns.

The CHAIRMAN. The letter of Mr. Haussermann may be incorporated in the record.

(The letter referred to is as follows:)

MAYFLOWER HOTEL,
Washington, D. C., May 14, 1936.

To the Honorable The Committee on Finance, United States Senate:

MY DEAR SENATORS: I should like to call to your attention a matter which at one and the same time results in changing, by inadvertence, the policy of the United States with reference to the Philippine Islands, and in a discrimination against the American citizens actually and in good faith engaged in business in the Philippine Islands; in the hope that you may see fit to recommend to Congress at this time a clarifying amendment to section 251, of the revenue act now before you.

By virtue of a construction of section 262 of the 1921 act (now section 251 of the pending act) by the Revenue Bureau and the court contrary to what Congress meant it to have, the American citizen actually, and in good faith, engaged in business in the Philippines is subjected to discriminatory taxation, and the Philippine Government, as a result of such taxation, will lose the income taxes which might otherwise come into its treasury.

Undoubtedly the policy of this Government with reference to the Philippines is well known to you; but since our occupation of the Philippines it has always been the fixed purpose of this Government not to derive any revenue by way of taxation, either directly or indirectly, from business conducted in the Philippines by Filipinos, Americans, Germans, Spaniards, British, Japanese, or other nations. The reason for the policy has been that this Government has always sought to maintain the position of guardian and ward.

The best evidence of this is the first income-tax law passed by the Congress of the United States (act of 1913), which was put into force and effect in the Philippine Islands, save and except that by special provision of that act it was to be administered in the Philippines by the officials of the Philippine Government, and all revenue derived therefrom by way of income tax was to incur intact to the treasury of the Philippine Islands. This policy was again reiterated by the Congress of the United States in the enactment of the 1916 income-tax law, which contained the same provisions, and by the revenue acts up to this date.

Another concrete evidence of the fixed policy of the United States in this regard is the provision of the act of Congress, or administrative order, requiring that cigars and tobacco imported into the United States from the Philippine Islands should bear the revenue stamps as set forth in the internal-revenue law of the United States, but declaring at the same time that all the revenue collected in the United States under the tax must revert intact to the treasury of the Philippine Islands. During all those years, all persons residing in the Philippine Islands, regardless of their nationality, filed income-tax returns in the Philippine Islands and the tax thereon was collected by Philippine officials and the proceeds turned over to the treasury of the Philippine Islands. No

one doing business in the Philippine Islands was required to file any income tax returns in the United States covering income derived from sources within the Philippine Islands.

The World War brought on conditions which made it necessary for the Congress of the United States to materially increase income-tax rates here in the United States; but, because our legislators were not familiar with conditions in the Philippine Islands, they did not consider themselves competent to fix the rates to be enforced in the Philippine Islands. Thus the War Revenue Act of 1917 did not alter the rates insofar as the Philippine Islands were concerned, but continued rates and procedure as fixed by the act of 1916 in full force and effect therein. Furthermore, in the same act authority was delegated to the legislature in the Philippine Islands to change, modify, or repeal the income-tax law insofar as the Philippine Islands were concerned, and, acting thereunder, the legislature did fix rates in 1917, which said law was legalized and ratified by Congress.

After the United States entered the World War, and in order to prevent draft dodgers and tax dodgers, citizens of the United States, from leaving the United States to avoid their obligations, a rule was enforced requiring every person who sailed from the United States to obtain and file with the steamship company a paper known as the "tax clearance." American citizens, who were engaged in business in the Philippine Islands, and made periodical trips to the United States, either on vacation or business, were confronted by the steamship agent with a demand for Federal tax clearance, and were told that no ticket could be sold to an American citizen without such clearance. The American citizen, on his side, being engaged in business, and convinced that he was not liable for any Federal income tax, because of his payment of such Federal tax to the Philippine Government, usually appealed to the War Department Bureau of Insular Affairs, which intervened with the result that every American honestly and in good faith in business in the islands, was enabled to sail without the necessity of such a tax clearance. In due course these cases of intervention of the Bureau of Insular Affairs became so numerous and burdensome that the administration in Washington was asked to undertake the clearing up of this matter.

The unfairness and injustice of the situation was apparent in the Philippine Islands and the Philippine Legislature passed a resolution in February 1920 instructing its Commissioners to the United States, as follows:

"Be it resolved by the Senate, the House of Representatives of the Philippines concurring, That the Resident Commissioners be, and they hereby are, instructed to ask Congress for the amendment of the United States Internal Revenue Act of nineteen hundred and nineteen, in the sense that American citizens who are bona-fide residents of the Philippine Islands shall not be subject to any income tax greater than that required of other residents of said islands."

On September 5, 1921, the United States Philippine Commission, commonly known as the "Woods-Forbes Commission", cabled the Secretary of War, as follows:

"All Nationals in the Philippines, except Americans, exempt from liability for the United States income tax. No foreigners here required to pay income tax to his home government. Americans here also pay income tax Philippine Government. Financial situation very critical and heavy losses have already been sustained. Attempt collect back taxed under Revenue Act 1918 would be futile the majority of cases and would only result in bankrupting many of such Americans as still remain in business, leaving commercial field entirely in the hands of British and other foreigners. We, therefore, urgently recommend that Americans be placed on the same tax basis here as other Nationals; otherwise, they are penalized for being Americans unable to successfully compete with those who are exempt, and that the relief granted be made retroactive to include exemption from tax liability under Internal Revenue Act of 1918."

Congress then endeavored to remedy and clarify the situation; and in November 1921 it enacted into law as part of the Revenue Act of 1921, the following provisions, known as section 262, which have been continued down to this date, it now being known as section 251 in the pending revenue act:

"SEC. 262 (a). *General rule.*—The case of citizens of the United States or domestic corporations, satisfying the following conditions, gross income means only gross income from sources within the United States—

"'(1) If 80 per centum or more of the gross income of such citizens or domestic corporation (computed without the benefit of this section), for the 3-year period immediately preceding the close of the taxable year (or for

such part of such period immediately preceding the close of such taxable year as may be applicable) was derived from sources within a possession of the United States; and

"'(2) If, in the case of such corporation 50 per centum or more of its gross income (computed without the benefit of this section) for such period or such part thereof was derived from the active conduct of a trade or business within a possession of the United States; or

"'(3) If, in case of such citizen, 50 per centum or more of its gross income (computed without the benefit of this section) for such period or such part thereof was derived from the active conduct of a trade or business within a possession of the United States either on his own account or as an employee or agent of another.'

"(b) *Amounts received in United States.*—Notwithstanding the provisions of subsection (a) there shall be included in gross income all amounts received by such citizens or corporations within the United States, whether derived from sources within or without the United States."

All of us in the Philippine Islands, as well as the responsible officials in the United States, thought that that section cleared up the situation, and for a number of years we went on paying our taxes to the Philippine Government as usual.

In 1926, the Revenue Bureau audit of my Federal income tax return filed here in the United States disclosed the revenue that I was receiving from the Philippines which had been omitted in the calculation of the tax because of the above-named provisions; whereupon the Bureau held that that part of the income which I had received from sources within the Philippine Islands and, which was represented by dividends, should be excluded in calculating the 50 percent, prescribed in section 262. The effect of this was that, notwithstanding I was actively engaged in the conduct of a business, the segregation from such business of that part of my income which was derived from dividends, placed me below the 50 percent, and, under the ruling, subjected my income from the Philippine Islands to the Federal income tax law. The question involved was finally submitted to the Board of Tax Appeals, which, in the case of *Haussermann* v. *Commissioner*, docket no. 29101, sustained the interpretation of the Revenue Bureau. The decisions of the Board of Tax Appeals was subsequently affirmed by the Court of Appeals of the District of Columbia (no. 5547) and, on certiorari from that court to the United States Supreme Court, the writ was denied. This we believe to be, in effect, an erroneous interpretation of the act of Congress which results in onerous discrimination against American citizens actually and in good faith engaged in business in the Philippine Islands under corporate form.

No question has been raised as to the exemption of an American individual doing business in the Philippine Islands, or an American engaged in the profession of law, or of medicine, or a partnership, from Federal income tax, provided 80 percent of his gross income is derived from sources within the Philippine Islands and 50 percent thereof from the active conduct of such business or profession. Needless to say, the great bulk of American business that is done in the Philippine Islands, by citizens of the United States residing therein, is done in corporate capacity.

The unfairness and injustice of this interpretation by the Bureau, having become apparent, in 1928 administration officials concerned in the matter, including the President of the United States, the Secretary of War, the Secretary of the Treasury, and the Governor General of the Philippine Islands, joined in requesting Congress, then engaged in writing a new internal-revenue act, to clarify section 262 so as to permit that part of the income which a business man in the Philippine Islands derived by way of dividends from a company conducted by him to be included in that 50 percent.

This effort on the part of the administration failed and I feel that the matter is of sufficient importance to again call to the administration's attention the gross injustice and discrimination imposed upon American citizens and to urge that clarification be made of section 251 (formerly 262) in the income-tax law now before the Senate.

I was personally present when this effort was being made, here in Washington, in 1928, and I have no hesitation in saying it failed simply because Senator Smoot, then chairman of the Finance Committee, was opposed to it for personal reasons, the nature of which need not be dwelt on at this point.

Clarifying Amendment to Section 251 (Philippine-United States Residents)

The matter has been discussed informally with Mr. Parker, the legislative counsel, now aiding the Finance Committee, at the suggestion of Senator Harrison.

The amendment proposed by us for such clarification follows:

Amend section 251 of the proposed Revenue Act of 1936 to include a new subsection thereto to be known as (a) (4), and to read as follows:

"Provided, however, that for the purpose of subsection 5 of this section, dividends received from a corporation, sociedad anonima, partnership, trade, or business, shall be deemed to be gross income derived from the active conduct of a trade or business, when such citizen is actively engaged in the conduct of such corporation, sociedad anonima, partnership, trade, or business."

The effect of such clarification will be to lift the discrimination which now exists against the American citizen who is bona fide and actually engaged in the conduct of a business in the Philippines, and put such American businessman on an equality for taxes with the Filipino, German, French, British, Japanese, Chinese, and any other nationals engaged in business in the Philippines. It will not in any way result in depriving the United States Government from receiving income taxes on the dividends received by any American citizen who has merely invested his money in the Philippine Islands.

Another important effect of this clarification will be to enable the Philippine Government to have the full benefit for taxing purposes of the income which an American citizen engaged in business in the Philippine Islands earns in the Philippine Islands, which the Philippine Government would not now receive because of the credit allowed to such American citizen for any tax paid to the United States Government.

Realizing that the undersigned is not known to the members of this committee, I perhaps should mention that I went to the Philippine Islands in 1898 as an officer of the Twentieth Kansas Infantry Volunteers; and was subsequently commissioned as a first lieutenant in the Thirty-fourth United States Volunteer Infantry. Thereafter, I served under the United States Military Government then in existence in the Islands as chief of the municipal law department under the provost brigade of the city of Manila. I then served as city attorney of the city of Manila, and later as Assistant Attorney General of the Philippine Islands, in which capacity I remained until 1903. I then engaged in the practice of law until 1915, and since then I have been actively engaged in the mining business in the Philippine Islands.

Personally I will not profit by this clarification because I am about to retire from active business in the Philippine Islands, and have paid my taxes under the existing erroneous interpretation. The clarification will not enable me to receive a return of the taxes paid.

Respectfully submitted.

JOHN W. HAUSSERMANN.

The CHAIRMAN. Mr. Parker, will not you discuss this matter with Mr. Kent and Mr. Beaman, and the others, so we go into this matter further?

Senator KING. Would not that fall somewhat in the category of the China Trade Act, the benefits and losses that are experienced there, in handling that question?

Mr. PARKER. It would be a good deal like the China Trade Act, in a way.

Senator KING. I think you better consider the two together.

The CHAIRMAN. Is there anything else?

Mr. PARKER. There is one more question that I forgot to mention. We agreed on the $1,000 exemption for domestic corporations.

The CHAIRMAN. Yes.

Mr. PARKER. For the purpose of the 18-percent tax and the purposes of the 7-percent tax. We did not say anything about giving the $1,000 exemption from the excess-profits tax. Now we changed the credit on the excess-profits tax.

The CHAIRMAN. I would not pay a $1,000 exemption on the excess-profits tax. That is a different proposition altogether.

Mr. PARKER. We have changed the credit, Senator. Under existing law, in figuring the excess profits taxes, you deduct the income tax. Now we have changed that around, we do not allow them that credit for the income tax that we allow for the excess profits tax. We feel that it would be rather peculiar for some corporation to pay no normal income tax and still have to pay the excess profits tax.

The CHAIRMAN. In other words, we charge them, on the one hand, the excess profits tax for doing something they should not have done, but we are going to allow them a credit on other tax for having done that. I do not think that is right.

Mr. PARKER. No, not exactly. We have a $1,000 corporation, for instance, and they are exempt under the 18-percent and 7-percent tax. Now do you want to put an excess profits tax on them, on that $1,000?

The CHAIRMAN. We have here a corporation that makes just $1,000, is that right?

Mr. PARKER. That is right.

The CHAIRMAN. I think that is absolutely exempt, under the rules we passed, that all corporations making $15,000 and less have a $1,000 exemption.

Mr. PARKER. That is just what we have to do. We have to give them $1,000 credit for excess profits tax. We do not feel we should make them pay an excess profits tax if they only make $1,000.

The CHAIRMAN. Where does the excess profits tax come in?

Mr. PARKER. Supposing they have declared the capital stock value of $1,000, and they make $1,000, that is 100 percent; they will have to pay practically 12 percent tax.

The CHAIRMAN. Would not the capital stock and the excess profits tax be taken as a credit against that exemption?

Mr. PARKER. That is not the question, Senator. The question is on the $1,000. The other part has been agreed to. You want to give then $1,000 exemption, the domestic corporations, for the purpose of the excess profits tax.

The CHAIRMAN. The excess profits tax does not come in here except on the capital stock, does it?

Mr. PARKER. It is measured by that.

Mr. BEAMAN. The excess profits tax is a tax on net income.

The CHAIRMAN. That is quite true. I do not know where we have got any excess profits tax in this thing, except on the capital stock levy for the year where the fellow fails to come in, or underestimates his capital stock and he makes more net than we charge him under the excess profits tax. Now where we have got the excess profits tax otherwise than that?

Mr. PARKER. That is the only one.

Senator KING. I move we pass it out and proceed with the next proposition.

The CHAIRMAN. Take the case of a man who puts his capital stock at $20,000 and he makes $30,000, and so on.

Mr. PARKER. That is not the case. That would not be affected.

The CHAIRMAN. I would be inclined to disallow the excess-profits tax. That is what I would do in figuring your $1,000 exemption.

Mr. PARKER. The whole thing comes down to this: Here is a man that makes $1,000, he is exempt from the 18-percent tax, he is exempt from the 7-percent tax, he only makes $1,000; if you do not give him the $1,000 exemption he may have to pay the excess-profits tax. Do you want him to pay the excess-profits tax because he made the $1,000? That is all there is to it. It seemed to us very peculiar that a man would have to pay an excess-profits tax when he did not have to pay these other normal taxes.

The CHAIRMAN. I would let him do it. If he did not put in his capital stock tax right I would let him pay it.

Senator BLACK. Is it simply an excess-profits tax where they make a mistake in putting in the capital stock?

The CHAIRMAN. We penalize them if they do not put in the capital stock at its true value.

Senator BLACK. I think you ought to penalize them in that case.

The CHAIRMAN. In that case we put on the excess-profits tax. I do not think they should be permitted to take a deduction from that.

Mr. PARKER. All right.

Senator KING. Mr. Chairman, I move we adjourn until Monday at 10 o'clock.

(Whereupon, at the hour of 1:10 o'clock p. m. the committee adjourned until Monday, May 25, 1936, at 10 o'clock a. m.)

REVENUE ACT, 1936

MONDAY, MAY 25, 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 Fayette, Metcalf, Hastings, and Capper.

Also present: L. H. Parker, chief of staff, Joint Committee on Internal Revenue Taxation; 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; L. H. Seltzer, assistant director of research and statistics, Treasury Department.

The CHAIRMAN. The committee will come to order.

Mr. Parker, will you let us have what you have on this matter of liquidation? First, what is the present law on that?

Mr. PARKER. It is at page 87 of the bill. This was section 110 of the 1935 act, which has now been incorporated in the print of the bill under section 112 (b) (6).

Last year it was pointed out, in order to give the corporations an opportunity to simplify their corporate structure, that it would be advisable to provide a method by which corporations could be liquidated and the capital-gains tax postponed. That was done, and the principal point involved is the question of what basis the property would take in the hands of the corporation that took over their assets.

For instance, if we have a parent company that wishes to dissolve a subsidiary, assume that the parent company has paid $100 for the stock of the subsidiary. The basis of the assets in the hands of the subsidiary may be $50. The effect of this section is that on a liquidation of that subsidiary——

Senator LA FOLLETTE (interposing). You are speaking of the present law now?

Mr. PARKER. Yes, sir; of this section.

Senator KING. You are speaking of this section in this bill?

Senator GEORGE. That is existing law.

Mr. PARKER. When that subsidiary is liquidated, the basis of the property in the hands of the parent is $100, and that $100 has to spread over the assets of the subsidiary, because on the books of the subsidiary, they only show as being worth $50.

In that particular case that is an advantage to the corporation, and the most serious point is that they can write up by that method, the value of their depreciable assets, such as plant and property, and get depreciation over again. Of course, then we have the reverse case where the cost of the stock of the parent was $100 and the book value of the assets $150. In that case, there is a write-down.

But it is true that under the existing law there is very great uncertainty, because there is no method set forth as to how this sum, this cost of stock, shall be distributed over the assets of the subsidiary.

The main purpose, as I understand it, of this liquidation proposal is to have the parent take over the assets of the subsidiary and carry in their accounts that basis of the subsidiary, the basis that the subsidiary had for those assets. That is exactly the rule that is followed in the case of a merger or consolidation as distinguished from a liquidation.

This deals with liquidations and reorganizations, which is generally accepted to be one of the most difficult sections of the law. The experts do not know what the existing law means, and that is what makes it a very difficult proposition to make a change in something that the courts do not agree on, and the interpretations do not agree on.

I think that Mr. Beaman ought to make some statement as to the difficulties of that, because he has been involved in that thing for a long while.

The CHAIRMAN. All right, Mr. Beaman.

Mr. BEAMAN. You are picking on the wrong man, Senator. I heartily agree with what Mr. Parker says, that it is complicated; but I do not know enough about it to form an intelligent judgment except the intelligent judgment that it is complicated and very difficult. I have heard people discussing it, and apparently everybody agrees that neither rule is right. One rule is right in some cases and the other rule is right in the other cases. If you are going to pick out of two evils the one that is the least evil, and pick that one, which one you pick, I just don't know enough about these business transactions to know, but the only thing I do know is the point that Mr. Parker touched on, that where you deal, as you are dealing here, with a situation where the present law is based on inferences or an absence of a specific provision in the law, and as to which apparently no one is quite in agreement as to what the proper inference is, particularly in view of a very recent decision of the Supreme Court last Monday, which has nothing to do with problem, but as showing the way the court is heading up, it is extremely difficult to write an amendment dealing with the matter properly; in other words, it is the kind of a thing that as far as I am concerned, if they knew what the situation was so that they could describe to you the exact situation, so that you could adopt a policy, and secondly to write it up to carry out your intention, that is a matter that will take some time.

Senator KING. Were there any witnesses either in the House or in the Senate hearings, that went into this question and pointed out the perplexities and suggested some rectification of the evils or the mistakes?

Mr. BEAMAN. Plenty of people suggested remedies. Mr. Alvord suggested a remedy, but just what it does, I am not prepared to say. I do not know enough about the business situation and the way the present law is being administered.

The CHAIRMAN. What do you think, Mr. Kent?

Mr. KENT. I had studied, as much as the time permited, some of the proposals that had been made, and I am not prepared to say that here is not merit in some of the suggestions. On the other hand, I am equally unready to say that the hastily considered amendment, in order to correct one situation, may not open up a veritable Pandora's box of evils and uncertainties in other situations arising under the statute. I think that these sections of the statute, as I said the other day, are probably the most sensitive and difficult sections in the statute, and that quick action may lead us into difficulties and troubles that we cannot now foresee.

I feel, almost, that it is pretty dangerous to tamper at this time with the liquidation provisions of the statute. The safest thing, I think the least radical thing that could be done, would be to make it clear that the term "reorganization", which is defined to mean a statutory merger or consolidation, includes a statutory merger of a subsidiary into a parent corporation.

On the other hand, if that particular change were made, it would fail to accomplish its purpose completely as long as the 50-percent clause which has been in the statute for a great many years—it was formerly 80 percent—remains in section 113 (a) (7)—I think that there is probably some need of some changes in these sections of the statute, but some of the suggestions that are being seriously urged are so radical in character that if they were adopted at this time, they might throw out or cease to make applicable at least some decisions of the Supreme Court and the lower Federal courts under the existing statute which has at least given us an approach to certainty on some points, and I cannot help but feel that it is the sort of thing that ought to be very carefully studied for a period of weeks or months before any very radical changes are considered.

Senator GEORGE. Let me call your attention to the fact that there is this language on page 87; that is, where the difficulty came, because it was thrown in here without any really serious consideration.

Mr. KENT. I think that is true.

Senator GEORGE. I know it is. We were going to let these 80 or 100 percent subsidiaries get out; we undertook to do that. It was a hastily drawn section, and we did not give it the consideration that it ought to have had. It seems to me if you carry out your first suggestion that the liquidation should be included in the term "merger" and "consolidation"——

Mr. KENT (interposing). I do not mean that, Senator. I mean that in form, a merger under the State statute of a subsidiary into a parent, should be treated as a merger, even though in some respects it has the effect of a liquidation, but of course the changes that are being suggested in the liquidation provisions here go much further than that. They would include other cases of liquidation.

Let me point one thing that can happen. If you write into the law at this time a provision allowing the basis to go over liquidation under 112 (b), it is perfectly possible for a corporation which intends

to liquidate under that section to first declare out in dividends all of its liquid surplus, for instance, and to get a stepped-up basis with respect to the declaration so made; in other words, the corporation has it within its own control to determine what property shall go over under the liquidation, with the basis of going over along with it, and that fact alone makes me pause before giving approval to any specific proposal which there has not been adequate time to think through.

Senator GEORGE. If they did declare out all of their liquid assets, they would become taxable, would they not?

Mr. KENT. Yes; that is true.

Senator GEORGE. You can reach them. That is what we were trying to do, or at least one of the things we were trying to do.

Mr. BEAMAN. Only 10 percent would go into the income of the parent.

Mr. KENT. Yes; you see, in the case of the subsidiary and the parent corporation, it is an intercorporate dividend We only get the tax of 1½ or 1.8 percent under the rates in the present bill from the corporation receiving the dividend, and it is at that point that the decision of the Supreme Court last Monday to which Mr. Beaman calls attention has led to a great deal of doubt and confusion.

Senator GEORGE. I have not studied that decision, but our difficulty, Mr. Kent, is that we get on to these complicated provisions that really do have a very serious effect upon business, at the end of a long and hard struggle over rates and over what kind of scheme we are going to adopt, and everybody is worn out when we reach it, and we continue passing it over from year to year.

The CHAIRMAN. I had understood that you gentlemen would talk among yourselves and had agreed upon something to recommend to the committee.

Mr. PARKER. As far as I am concerned, as I said, I think the most practical basis is to carry over the basis the same as we do in mergers.

Senator GEORGE. I think it would do a great deal of good if the next time we get on a tax bill, that we write harmoniously some of these features. I realize that even then, as Mr. Kent says, it runs into other provisions. But something really ought to be done if we can do it.

Mr. PARKER. I think, Senator George, that it is something to which some very hard study ought to be given, and, as I say, I am not prepared to disagree with some of the suggestions that have been made. I think they probably contain a great deal of merit, but experience has shown that it is quite possible in making what seems in itself to be a meritorious change in these reorganization provisions and liquidation provisions, that you may be exposing yourself or the revenue to dangers that were not anticipated at the time that the change was made.

Senator KING. Do you concur in the suggestion just made by Mr. Parker?

Mr. KENT. I think I might concur in that if the problem is limited to a statutory merger of a subsidiary into a parent.

Senator KING. I assume you are not contemplating interfering in any way with the laws of the States with respect to mergers and corporations and the formation, and so on.

Mr. KENT. Not at all. As a matter of fact, I think myself that under the law as it is now drawn, a merger of a subsidiary into a parent is included in the reorganization provision of the statute, but there is some feeling of uncertainty with regard to that because of a decision of the Board of Tax Appeals 2 or 3 years ago. That decision was handed down, however, before the word "statutory" was interpolated before "merger" in section 112 (g) of the statute on page 90. But I think so far as the present law is concerned, if that were made perfectly clear in the statute, it would simply clarify what the law probably already is.

Mr. PARKER. It is true when you depend upon a statutory merger, you go back to State law. Some States do not provide for any statutory merger, and so the same transaction which would be postponed in one State will not be postponed in another State, because we do go back to State laws, and it does seem to affect their uniformity.

The CHAIRMAN. Mr. Parker, let us take the amendment you have suggested and analyze it and get through with this proposition. You have it all prepared there, have you?

Mr. PARKER. No; this is simply the amendment that was suggested to us, and we have been studying it.

Senator LA FOLLETTE. Do you mean the Alvord amendments?

Mr. PARKER. Yes.

Senator HASTINGS. The Alvord amendments are not satisfactory?

Senator LA FOLLETTE. As I understand, their position would be that they have not had sufficient time to make a study to see whether they could recommend them or not. The matter has so many ramifications that you cannot give a horseback opinion about them.

The CHAIRMAN. Mr. Parker, do I understand you to say that it is your opinion that this ought to be incorporated?

Senator LA FOLLETTE. When you say "this" what do you mean, Mr. Chairman? All of the amendments?

The CHAIRMAN. The Alvord amendment that you have been considering about which they have had conferences. Do you approve or disapprove of the proposition or what do you advise the committee to do with reference to it? To do nothing about it, or proceed and try to change this liquidation provision?

Mr. PARKER. I believe it would be better, as a matter of policy, to take the basis of the assets that are in the hands of the subsidiary so that you get rid of valuation and allocation and that kind of problem.

As to the legal task of making this right, of course Mr. Beaman knows more about that than I do. I would always hesitate to go against his judgment when he says it is a hard legal proposition to draft; because I know it is. The only thing I might suggest is that if we get a little more time—we have all spent several hours on it—we might come to an agreement on a draft.

The CHAIRMAN. What would you think about a little more time? If we are going to do anything with this bill, we have got to get it out pretty soon. This one of the matters that I thought you had been conferring on a good deal about.

Mr. PARKER. Of course, there is this much to be said. The present law is imperfect. Maybe we can put something in that won't be any worse than it is now.

Senator BARKLEY. If the law at the present time does not include the whole picture of mergers and consolidations as well as liquidations, you mean to simply add that to the section and let it go at that? As far as I am concerned, I do not think we ought to delay this bill a day on account of either putting anything in or leaving anything out on this subject. Would it not be easy to do that?

Mr. PARKER. Of course, you can put it in and take a chance on fixing it up in conference.

The CHAIRMAN. Won't you all get together on some draft to recommend to the committee and then let us pass on the proposition?

Senator GEORGE. Let me make this suggestion, Mr. Chairman. If the suggestion which Mr. Parker makes can be carried out in an amendment, that the committee will then consider it on the floor as a committee amendment. You can then offer it on the floor as a committee amendment and not delay the other features of the bill. I a very much interested in it, because I do know how it cuts, and I know we should do something with these various sections. As Mr. Kent says, they are complicated. Mr. Alvord worked out what he thought was a complete scheme. I do not know; I have not studied his proposal, and I do not know whether it is or not, but if it is possible, as Mr. Parker suggests, to go a little further at the present time, to put it into the act and ask the experts to work it out and let it be handed to you and offered on the floor as a committee amendment.

The CHAIRMAN. All right, Mr. Parker. You all confer about this proposition and see what you can get together on that you will recommend to us. If you need further time, we will follow Senator George's suggestion.

Senator BLACK. Anything on that will be resubmitted to the committee?

The CHAIRMAN. Oh, yes.

Mr. KENT. There is one clarifying change upon which we are entirely agreed, and that is 112 (h) on page 91. That is simply a clarifying change in the definition of "control." As amended, the section would read:

> As used in this section, the term "control" means the ownership of at least 80 per centum of the total combined voting power of all classes of stock entitled to vote, and at least 80 per centum of the total number of shares of all of the classes of stock of the corporation.

Senator GEORGE. Confusion has existed there as to whether it meant 80 percent of the voting or 80 percent of the other stock?

Mr. KENT. No. As a matter of fact, the change suggested does not, I think, change the meaning.

Mr. BEAMAN. Mr. Kent, I want to know right off, if the Treasury will tell me that that change is absolutely certain, that that is the present law, then all you have to do is to write that in. If you are not going to make that statement, then if there is any possibility of doubt on that score, it is for the committee to tell me what to do. I do not care what they tell me. But you have to spend a couple of hours at least to go through it to see what you have to write under section 113 (a) (12). If it makes no change in the present law.

Senator KING. Does it make any change in the law?

Mr. BEAMAN. If 112 as it now stands read 80 percent of each class of the voting stock, then I should say that the change suggested would change the meaning of the section.

Senator CONNALLY. The ownership of the voting stock is what really controls in the corporation, is it not?

Mr. KENT. That is true.

Senator CONNALLY. These big companies issue a very small portion of the stock that has voting privileges, and many of them issue the bulk of the stock with no voting privilege. The fellow that has not the voting privilege is just out.

Mr. KENT. Of course, the amendment does not change that at all; it does not change at all the last portion of 112 (h) as it now stands. It includes at least 80 percent of the total number of shares of all other classes of stock of the corporation. The present section requires 80 percent of the voting stock and 80 percent of the nonvoting stock of the corporation. That is left unchanged under this amendment. The only change that is made is that instead of saying 80 percent of the voting stock, we say 80 percent of the total combined voting power of all classes of stock entitled to vote.

The CHAIRMAN. Is there any change in the law?

Mr. KENT. I do not think that it is.

The CHAIRMAN. What do you say, Mr. Beaman?

Mr. BEAMAN. The problem presented is very simple. Fixing it right is the difficult part.

The CHAIRMAN. Just a moment. Senator Steiwer is here and wishes to present a matter to the committee.

Senator STEIWER. I want to ask whether the committee would consider a supplemental definition of lumber. Under the excise tax law, the language as used is interpreted by the Department to be so narrow as to include only sawn lumber and not sawn timbers, like 4 by 8's, or 8 by 10's, and things of that kind. The result is that there is no excise tax upon sawn timbers but only upon sawn lumber.

I have here a proposal for an amendment that was prepared by the legislative counsel. I am not going to take the time of the committee to read it. I just want to know whether this committee will consider an amendment of that kind.

The CHAIRMAN. Did you take it up with the Tariff Commission to find out what their construction is?

Senator STEIWER. No; the matter is being construed in the customs courts. It is in litigation in two or three courts, Los Angeles, Seattle, and elsewhere.

My attention was called to it by Colonel Greeley, who, you know, is now the manager of the West Coast Lumber Manufacturers' Association.

The CHAIRMAN. Did the State Department give any expression as to the Canada agreement in regard to it?

Senator STEIWER. No; it was not touched in any reciprocal agreement that I know of. The matter is still in litigation, and it is anticipated and feared that the court may hold finally that a piece of dimension timber, we will say 6 by 6 or 6 by 10, is not lumber.

Senator KING. Is it lumber?

Senator STEIWER. That is quite a question.

Senator KING. Is a tie lumber?

Senator STEIWER. It is quite a question, as I say.

Senator CLARK. The N. R. A. held that a tie was lumber.

Senator STEIWER. Some of our courts in the past have held that this dimension material is lumber, and I think they all intended it so. Otherwise, our definition in the excise law is inadequate and insufficient.

If the committee does not want to consider it, I do not want to impose upon the good nature of my friends. I probably will offer it on the floor.

The CHAIRMAN. If you desire to have your amendment incorporated in the record in connection with your remarks, you may do so.

Senator STEIWER. I appreciate that. Would the committee go at least so far as to consider it, or indicate whether they will consider it at this time?

The CHAIRMAN. We have not determined anything with reference to that. We have several amendments here with reference to the tariff in various different ways, which we are going to take up.

Senator STEIWER. This is a very important matter if we are going to make the excise tax mean what we thought it meant upon the various occasions we considered it.

Senator KING. Why is the tariff now on lumber?

Senator STEIWER. There is a tariff in the old tariff bill of $1 per thousand, but the description in that act is sufficiently broad to cover both lumber and timbers. The excise tax, as you know, was adopted at a later time, and the language employed in the excise tax was a little different, sufficiently different, that some of the customs courts held that it should be interpreted to mean a different thing.

The CHAIRMAN. Thank you, Senator Steiwer.

Now, on the suggested amendment that you made, Mr. Kent, where would that come?

Mr. KENT. That would come in section 112 (a). Since, however, the other problem is being left for further consideration, I do not see why this one could not be included at the same time and looked into and make absolutely certain.

The CHAIRMAN. All right, we will leave it for further consideration.

Now, what other propositions are left open in this bill?

Mr. KENT. May I take just another moment? I understand, Mr. Chairman, that the other day when I was not present, it was suggested that I report the Treasury's attitude with respect to the suggested removal of the withholding requirement on tax-free covenant bonds. I think Senator Hastings was interested in that. I think there is possibly a joker in that proposal, for this reason——

The CHAIRMAN (interposing). What proposal?

Mr. KENT. In the proposal to abolish the withholding requirement on tax-free covenant bonds. I might say that from a purely administrative point of view, the point of view of the Bureau, there are many of them down there that would like to see it done.

But here is the difficulty. A large number of bonds have been issued containing some such language as the following, that the obligor of the bond agrees not to deduct from the interest payments on the bonds any tax—many of them contain a limitation of

2 percent—any tax not to exceed 2 percent, which the obligor is permitted or required by law to withhold. When they withhold this 2 percent and pay it into the Treasury, the holder of that bond gets the benefit of it. He returns the 6 or 7 percent or 5 percent interest which he receives as income, but he is allowed a credit for the amount of the tax which the obligor of the bond has paid into the Treasury.

Now, if you take away the withholding requirement in such a case, it means that the holders of all of these bonds lose the benefit of that 2 percent which the corporation has already paid, and it means——

Senator CONNALLY (interposing). Why can they not take that deduction in their return?

Mr. KENT. They could not take a deduction unless the Treasury has received the money, and it does not receive the money unless the corporation under the section has paid the 2 percent into the Treasury.

My feeling about the thing is that all of these corporations that issued these bonds made that contract, and if this provision of section 143 is taken out of the act, they are thereby relieved from a measurable financial burden at the expense of the holders of the bonds. I cannot see any other answer to it.

Senator CONNALLY. Why should the Government assume the obligation of adjusting their equities? Why can they not pay the tax and reclaim it from the bonds?

Mr. KENT. For the reason that when section 143 was amended, the withholding was limited to bonds before January 1, 1934; in other words, the problem will gradually eliminate itself as these outstanding bonds are refunded or retired.

Senator CONNALLY. I do not see that it is any of our business.

Mr. KENT. Of course, many of these bonds were issued when Section 143 was in the statute. That has been the established policy of the Government since, I believe, 1916.

Senator CONNALLY. That may be, but I do not see any obligation on the part of the Government in it. Here is a man that takes a bond and the corporation says that it will pay the tax——

Mr. BEAMAN (interposing). No, Senator; that is not what the bond says. Most of the bonds say that the corporation will pay any tax up to 2 percent, which they are required to withhold. If they are not required to withhold it, which they would not be if you repealed this thing, they would not be under any obligation to the bondholders. They do not have to pay them a cent.

Senator CONNALLY. I do not see that it is the Government's duty to have to hunt up these squabbles between these people and adjust them. Let them file a claim with the corporation.

Mr. BEAMAN. They cannot do it.

Senator CONNALLY. That is their business. They made the contract, and I do not see that it is the duty of the Government to go around and spend a lot of money protecting these people.

The CHAIRMAN. What do you recommend for us to do?

Mr. KENT. I have already indicated that our own position is unfavorable, but it is all a question of policy.

The CHAIRMAN. All in favor of putting this section in as suggested by Mr. Gerrity will say "aye"; contrary "no."

(The chairman announces that the suggestion is rejected.)

The CHAIRMAN. Are there any other amendments?

Mr. PARKER. Yes; we have some more things that have to be considered by the committee.

The CHAIRMAN. Then we will first take up some more of these amendments.

Senator KING. Before you do that, I should like to ask this:

I understand that the Treasury actuaries have advised us that the effective rate of tax on corporations under existing law, with the graduated schedule, is between 13.3 and 13.4 percent. Mr. McLeod stated in the hearings before this committee (executive hearings no. 2, p. 95) that on the basis of the estimated corporate income for the calendar year 1936 the Government would get $964,000,000 from corporation incomes for 1936; during the hearings before the Committee on Ways and Means he stated that the statutory net income of the corporations for 1936 amounted to $7,200,000,000. In arriving at the amount of $964,000,000 to be obtained from corporations for the calendar year 1936, was not the base of $7,200,000,000 used? It appears that in applying an effective rate between 13.3 and 13.4 to that base approximately $964,000,000 is obtained. Is that correct?

Mr. SELTZER. Yes, sir.

Senator KING. If the base of $7,200,000,000 was used in computing the estimated revenues from corporate incomes for 1936 under existing law, why was not such a base used for computing the revenue from the 18-percent flat tax imposed under the plan of the Committee on Finance? Applying an 18-percent flat rate to a base of $7,200,000,000 we get $1,296,000,000. Subtracting from this the $964,000,000 to be obtained under existing law, we arrive at an additional revenue of $332,000,000. Allowing $30,000,000 for the exemption of $1,000 to corporations with net incomes of $15,000 or less, I find we have left additional revenue of $302,000,000, to be compared with your estimate of only $215,000,000.

My recollection is that Mr. Helvering stated in the House hearings and Mr. Oliphant also, that the existing corporate rates, if raised to 25.5 percent, will produce the 620 million additional revenue required from corporations under the President's proposal. It was also stated by some of the Treasury experts—and I think confirmed by Mr. Kent—that for every 1-percent increase in rates over existing law $60,000,000 in revenue would be added. In other words, a 10.5 percent increase in revenue would produce $630,000,000 additional revenue.

If an increase of 10.5 percent in the case of graduated rates would produce additional revenue in the amount of $630,000,000 it appears that a flat rate of 25.5 percent would produce even a greater amount.

If an increase in the corporate rate about 25.5 percent will produce as much as $630,000,000 it is not clear why the committee plan of a flat 18-percent rate plus a 7-percent rate on undistributed profits will not produce a greater sum than that indicated. It should be remembered that a 7-percent tax on undistributed profits adds to the tax base. According to Mr. McLeod's figures on page 36 of the hearings of the House, about one billion was in intercorporate dividends which are not taxed under existing law and which are not included

in computing the revenue from the flat 25.5-percent rate. The amount of revenue to be derived from including such dividends in the tax base will certainly more than offset any loss in revenue due to the allowance of the 18-percent tax as a deduction in computing net income subject to a 7-percent undistributed-profits tax. In your estimate without this deduction for the 18-percent tax you estimated the 7-percent tax would yield $292,000,000. With the deduction for the 18-percent corporate tax it was estimated that this tax would yield $217,000,000, or a loss in revenue of $75,000,000, due to the allowance of this deduction. However, with the enormous increase in the tax base due to the inclusion of these intercorporate dividends it would appear that this loss would be more than made up.

Are not these deductions which I have indicated here accurate?

Mr. SELTZER. Do you want a one-line answer to a number of questions?

Senator KING. No; that would not be fair.

Mr. SELTZER. The mathematics are all right in here. We, too, arrive at your gross revenue of $1,200,000,000 from an 18-percent tax, but you neglected to correct that gross revenue figure for the regular difference between tax liability and tax collections.

I pointed out one day that over a period of years we find that we can regularly expect that tax revenues from the corporation income tax will average about 6.8 percent less than the computed tax liability, and in making our revenue estimates, both for Budget purposes and in connection with new bills taxing corporations, we regularly have to make that allowance. Otherwise our figure would be all haywire. You will find, I think, Mr. Senator, that if you apply that correction our arithmetic is all right.

Senator KING. I will go through it and apply it. I am not sure that you are right and I am not sure that I am right. It did seem to me the other day there was a great difference there.

Mr. SELTZER. As regards this 25.5 percent rate, I was not here when Mr. McLeod or Mr. Helvering made the statement, but I am sure that what was meant was this, that if you raise the flat tax on corporation incomes to 25 percent or 25.5 percent, and you have got no decrease in dividend distributions in consequence, then the Federal revenues would be increased by more than enough to make your $620,000,000. It should be something in the neighborhood of $700,000,000. That is quite right, but if you were going to make a revenue estimate based upon a 25 or 25.5 percent flat corporation income tax, you would have to take into account the probable effect of such a heavy flat tax upon dividend policies. Corporations would have less to distribute than they have at this time.

Moreover, as I tried to say on Saturday, you cannot add up the 18 percent flat corporation tax that you had in your (c) (4), I believe, and the 7 percent supertax on undistributed earnings, and come to a 25 percent tax, because the bases are different. The 18 percent applies to statutory net income; the 7 percent applies only to undistributed adjusted net income. So you cannot get a simple addition there. You have your 18 percent and your 7 percent applied to two different bases, the 7 percent being applied to a much smaller base than the 18 percent. So you have not the equivalent in an 18 percent plus 7 percent supertax of a 25 percent tax on all statutory net income. Have I answered your questions, Mr. Senator?

Senator KING. I will examine your statement. I think you have answered it from your point of view. I am not quite sure that you are right and I am not quite sure that I am right.

The CHAIRMAN. I am very uncertain about these estimates, Mr. Seltzer. Here is no. 7 that you furnished an estimate on, and you get $642,000,000, is that right?

Mr. SELTZER. Correct.

The CHAIRMAN. There you retain the present capital-stock and excess-profits taxes?

Mr. SELTZER. Correct.

The CHAIRMAN. But on this other, you repeal the present capital-stock tax and you impose 18 percent tax on corporations, and you repeal the present exemption on dividends from normal tax and impose 7 percent tax on undistributed earnings, and you only get $522,000,000.

Senator CONNALLY. You eliminated the increase on individual incomes of 1 percent.

The CHAIRMAN. Yes; that makes a difference of $60,000,000—or is it $90,000,000?

Senator BYRD. $88,000,000 is what they testified to the other day.

Mr. SELTZER. In this no. 7 here you had no exemption for small corporations.

Senator GEORGE. That is $30,000,000.

The CHAIRMAN. That would be $30,000,000. That reduces it to $612,000,000.

Mr. SELTZER. And you have this increase as you pointed out in the normal tax on dividends.

The CHAIRMAN. But you have your capital-stock tax there. I do not understand by what we have done already and since, under this House bill, the capital-stock tax is repealed, and we lifted it and put it back again at $1.40—that is a permanent law and is going on in the future—I do not understand why we do not get credit for that when you compare what we have done with the House bill.

Mr. SELTZER. Of course, that is something that I have never done. This committee is framing revenue legislation. I make these estimates without reference to estimates in connection with the House bill, this being an independent matter here.

I recall, however, that under the House bill the minimum rate on retained earnings is something like 28⅔ percent. That is the minimum rate. That is bound to make a very considerable difference.

You have also this factor. When corporate earnings are distributed to stockholders and you impose a normal tax on dividends, and the regular surtax, you get a very substantial rise in individual tax collections for two reasons.

In the first place, you have a larger volume of dividends subject to these individual rates, and in the second place the average effective surtax rate rises on the whole base. For example, for the budget we estimated that we would get about $518,000,000 in surtaxes from dividend distributions; gross dividend distributions to individuals of, if I recall correctly, $2,700,000,000. That is an average rate without any normal tax on dividends of a little better than 19 percent. That is when corporate earnings go out to individuals, even on the budget basis, without any additional distribution and without any

normal tax on dividends, we get back through individual income-tax collections, better than 19 percent.

Senator CONNALLY. As an average?

Mr. SELTZER. Yes; on the over-all. If you add a normal tax on dividends and make an allowance for tax-exempt institutions and tax-exempt individuals, you could add approximately 3.58 or 3.6 percent to that surtax. Immediately you get a rise to better than 22 percent of earnings paid out in dividends that you collect through your income tax.

For this reason: Any proposal that encourages a greater distribution of the corporate earnings is bound to be very productive from a revenue standpoint. The productivity may be out of proportion to what looks like the immediate incentive because there is no mechanical relationship there. If earnings go out, they go to people who hold stocks now. These people are distributed in certain income-tax brackets. Such a large proportion of them happen to be the higher income-tax brackets that our over-all average surtax increases over what it is at the present time.

Senator BYRD. What percentage of the stockholders do you regard as in the nontaxable brackets today under the present income tax?

Mr. SELTZER. I have no figures on that.

Senator BYRD. I do not see how you can make up accurate estimates until you get some figures on that, because there are many of these stockholders that won't pay any tax on their dividends because they are not in a taxable class.

Mr. SELTZER. We can make our estimates, nevertheless, for this reason, that we do not have to know the number of stockholders that are not taxable.

Senator BYRD. The percentage.

Mr. SELTZER. If we know how much dividends they get, that is, if we know what corporations have paid out in dividends, and how much have been reported for income-tax purposes, the difference obviously has gone to institutions and individuals not subject to income tax.

Senator BYRD. Then would you not have to investigate all of the comparative rates, starting at 4 percent and going right up?

Mr. SELTZER. There is not any very great investigation needed, because that is automatically done over at the Bureau of Internal Revenue every year, and a good deal of the information is published in this volume, Statistics of Income.

Senator BYRD. So far as a speculative estimate is concerned, this will more surely, much more surely, bring in the revenue than the House bill, because this is based upon an established principle, and it does not relieve anybody of their taxes, while the House bill did relieve certain corporations of taxes. You would say that this would be a more certain estimate?

Mr. SELTZER. I do not think that I would, Mr. Senator.

Senator BYRD. The other is entirely new in the field of taxation. It has never been tried before, and there is necessarily so much speculation in it, while these estimates, I imagine, are just about as accurate as any estimate can be, because you have the basis to make them as accurate as is possible to make them, because you have the present taxation to go by.

Senator KING. I may not understand your statement, but for my own information, did you take in account in estimating your distribution for dividends which would be subject to taxation the fact as illustrated by the testimony, for instance, of Miss Curtis, the head of some women's organization, to the effect that there were more women receiving dividends—that is, more women stockholders in corporations—than there were men; and my recollection is some 14 or 16 million, and the holdings were very small, and the interference that I deduced from her testimony was that the majority of them were not in any of the brackets for surtaxes. I do not know whether that fact would militate against the testimony you are giving or the estimates which you have given or not.

Mr. SELTZER. As I said to Senator Byrd, we have not any data on the number of individual stockholders. You can easily see how difficult it would be to get accurate data. One man would own 10 shares each in, say, 20 corporations. Should you count him 20 times or once? But we do have, I think, fully adequate information on the volume of dividends that goes to individuals subject to income tax, and we find that, of course, the largest proportion of dividends goes to such individuals.

The CHAIRMAN. Mr. Seltzer, the thing that has given me concern, and which is giving me concern, is that capital-stock tax. It may be that because I do not understand it, but I am all up in the air. I thought when we made that permanent after the House had repealed it, and that from your figures here, that we had raised some $560,000,000, that by the imposition of this $168,000,000 being raised from the capital-stock tax that we were going to get pretty much the President's demands, with probably $60,000,000 more to raise, but I find that you are including in this $520,000,000 or more the capital-stock tax. Let me get that clear in my mind, because it is very material. If we have to go to some other plan here, we might just as well know it.

We adopted (c) (4) the other day with 18 percent. You said we would get $220,000,000 additional from that, did you not?

Mr. SELTZER. (c) (4) was different.

The CHAIRMAN. My figures were that you gave $220,000,000 increase from the flat rate of the present loss to 18 percent.

Senator GUFFEY. That was $215,000,000, was it not?

Mr. SELTZER. On (c) (4) it was $215,000,000.

The CHAIRMAN. That was after the $1,000 exemption came off?

Mr. SELTZER. Yes.

The CHAIRMAN. Then you impose your 7 percent on the undistributed adjusted net income. You put that at $217,000,000.

Mr. SELTZER. Correct.

The CHAIRMAN. Then you put $90,000,000 on the repeal of the 4-percent exemption?

Mr. SELTZER. Correct.

The CHAIRMAN. That gives you about $522,000,000?

Mr. SELTZER. Yes.

The CHAIRMAN. Then there was some new provision with reference to this liquidation, where we were to get about $33,000,000; and also, you said, that $5,000,000 should be added on the cushions that we eliminated.

Mr. SELTZER. I figured that you could add about $37,000,000 if you adopted some of the provisions of the House bill relating to liquidation and the like.

The CHAIRMAN. That gave us about $560,000,000; in fact, $559,000,000. Now, where is the capital-stock tax involved in that? You do not put it in at all there.

Mr. SELTZER. That is right.

The CHAIRMAN. Where have we lost it?

Senator CONNALLY. That is in the present law.

The CHAIRMAN. I understand it is in the present law; but the House bill has repealed it and we are putting it back.

Senator CONNALLY. He is making these estimates on the basis of the present law and not of the House bill.

Senator BARKLEY. The reason why it has confused you is that the House eliminated it and tried to raise that amount of money from some other source. We leave it like it is and that also eliminates the other source. You have that. This is a net increase over the present law, so that you do not have to be worried about that capital-stock tax.

Senator CONNALLY. It is there and we are going to leave it there.

Senator KING. The Secretary of the Treasury gave me an estimate of $218,000,000 or $209,000,000—I do not have his report here but it is in my office—upon an 18 percent graduated from the present law. Twelve percent on up. Take that graduation and his estimate then was $208,000,000 or $209,000,000. Certainly it would be more when those graduations are eliminated and it is a flat rate of 18 percent.

Mr. SELTZER. It is a little more, is it not? $215,000,000 with your $1,000 exemption as against your $208,000,000 or $209,000,000.

Senator KING. You eliminate those graduations, and doesn't that make a difference?

Mr. SELTZER. The graduations do not really lose you very much revenue. In the present law the steps are so small. For example, the 12.5-percent rate applies to the first $2,000. The next step applies to the next $13,000. You get a new step at $15,000. Then you go to $40,000. Then you stop your graduation at $40,000. You can easily see that the bulk of your corporate income is subject to the 15-percent rate.

Senator BYRD. As I understood you to say Friday, you made no allowance for the stimulation that would occur in the payment of dividends by the imposition of the 7-percent tax.

Mr. SELTZER. As I pointed out on Saturday—I do not believe you were here, Senator Byrd—we did make allowance in this respect. We said that corporations are going to pay out in taxes some $432,000,000 more than they are paying out right now. Nevertheless, they are going to maintain the same dollar volume of dividends, which would mean of course an increase in the proportion of earnings that they pay out after taxes. We do not feel that we could safely allow for more than that special incentive in view of the fact that you had a 4-percent normal tax rate operating as a partial counter incentive.

Senator GERRY. Did you not take into account the fact that the corporations' directors were not thinking so much about the tax that the stockholders would have to pay, but of the good showing that

corporations would make. Naturally, if they do not have to pay that 7 percent tax, it seems to me that that is going to affect the directors seriously in their decision. I do not think the directors in a corporation are only thinking of how much tax their stockholders are going to have to pay.

Mr. SELTZER. Of course, the directors also are charged with responsibility for maintaining the corporation's position in its field, maintaining the corporate finances. They are faced with the fact that they pay out $432,000,000 extra in taxes, taking corporations as a whole.

Senator GERRY. Yes; but the director is going to look at the fact that if this tax is paid out in dividends, they are going to save 7 percent. There is not any question in my mind that any board of directors is going to look at it in this way. This theory that they are only going to pay dividends on what the increased taxes are going to be is a wrong basis, in my judgment.

The CHAIRMAN. Let me ask you, Mr. Seltzer: The House bill was estimated to produce $803,000,000 for the first full year of operation. That is right, is it not?

Mr. SELTZER. I would have to look at it.

The CHAIRMAN. Well, it is right. Assuming we enact the proposed corporate tax plan of the committee, you would get $560,000,000, and the windfall tax, I think, is about $100,000,000, is it not?

Mr. SELTZER. Yes; except, Mr. Chairman, that you recall that on Saturday you asked us to estimate the effect of the changes that you have made. We have a preliminary estimate on that, and it would reduce that $100,000,000 by $18,000,000.

The CHAIRMAN. So it would be around $82,000,000?

Mr. SELTZER. That is our preliminary estimate.

The CHAIRMAN. Well, you add those two together—I am not counting the sugar proposition and the other.

Mr. SELTZER. You did ask me also to get an estimate on an estate-tax change.

The CHAIRMAN. How much was that?

Mr. SELTZER. We have it on three different bases. If you were to maintain the present $40,000 exemption for estates of $40,000 and less, but would remove that exemption for estates in excess of $80,000, and graduate the exemption in between estates of $40,000 and $80,000 so everybody would always have a $40,000 estate at the minimum, and as the estate got larger he would have a larger estate after paying his taxes none the less, you could get $53,000,000. If now you raised the point at which the exemption vanishes, if you said instead of graduating the exemption between $40,000 and $80,000, making it disappear at $80,000, you graduate between $40,000 and $100,000, making the exemption disappear at $100,000, you would get $41,000,000.

If now you took $120,000 as the net estate size at which the exemption should disappear, you would reduce the yield to about $30,000,000.

In order to make every one of these three yields effective for the next year, you would have to make the change in exemptions applicable to estates that came into being since January 1, 1936, on which your returns are not due until January 1, 1937.

Senator GERRY. Would you have to make it retroactive?

Mr. SELTZER. As you would, for example, in the revenue bill you are now discussing the other parts, you would make it applicable to the calendar year 1936 which started January 1. So in this case if you wanted to have your revenues come in in 1937, you would have to make the change applicable to estates that came into being since January 1.

Senator GERRY. Do you mean by that if the people died before January 1, 1936——

Mr. SELTZER (interposing). No; I mean people who died in 1936.

Senator GERRY. The people who died in 1936?

Mr. SELTZER. I have just given you the information. I am not arguing.

Senator GERRY. That is what I am trying to get; I am trying to understand this. You will say you will make the tax applicable to 1936. Do you mean by that that you make the tax apply to anybody who died since January 1936, although at the time of his death the tax did not apply, but you now put the tax? The title has already passed to this estate, and now you are making it retroactive, because the theory always has been on these past estate taxes that the tax did not go on until the title passed, and I should think there is a question about that, about putting a tax on after the title has passed. I do not know. It is a novel idea in estate taxes, and I think a very unsound one.

Senator BARKLEY. Of course, there is already an estate tax on.

Senator GERRY. Yes; but this increase is not, and this is increasing the tax. The theory always has been that they did not put the tax on until after the title has passed. I think this is extremely dangerous procedure and unsound.

The CHAIRMAN. Let us get to this other proposition of seeing how much we have to raise. As I get the figures now that you have given us, the 215, 217, and 90 make 522, and 37 million increase by virtue of other changes, which is $560,000,000 increase in this bill.

Mr. SELTZER. $559,000,000, exactly.

The CHAIRMAN. All right. $82,000,000 on the windfall, which gives $642,000,000.

Senator BLACK. May I call attention that that is one year, and we did adopt a provision which will probably be taken advantage of, on extensions of the time of payment. I simply want to call your attention to that as applying to what we can get this year.

Senator GERRY. If business picks up.

Senator BLACK. This year you will probably pick it up on your other taxes.

The CHAIRMAN. That is $642,000,000 total. We were trying to get $803,000,000 for the first full year. We are short the first full year by $106,000,000.

Senator BARKLEY. In arriving at that $803,000,000 you had to absorb the loss of $168,000,000 by the repeal of the capital stock and excess profits taxes, so that when you do not repeal them, you do not have to absorb that.

The CHAIRMAN. I did not think so either, but I get right back to that same proposition. I have not got it clear yet.

Senator BARKLEY. You had to wipe out your loss due to the repeal of the capital-stock and excess-profits tax before you started to get any new revenue in the House bill. Isn't that true?

Mr. SELTZER. The House bill makes the effective revenues from individuals so great that without the capital-stock and excess-profits taxes they reach their permanent revenue figures.

Senator BARKLEY. But they had to start out by absorbing that loss somewhere before they could start again.

Mr. SELTZER. Correct.

Senator BARKLEY. So they absorbed $168,000,000 that they were repealing, and after absorbing that by a new tax on corporations and individuals they started out and got $620,000,000. We do not have to absorb that loss. Those $168,000,000, they are there, and they are going to be there.

Senator HASTINGS. The Treasury said that we had to raise $803,000,000 this year. You do not take into consideration the capital-stock tax in these figures.

The CHAIRMAN. Yes; you do. That is what gets me confused. Here is Mr. Morgenthau's statement. He says the yield from corporate earnings under the House bill is $623,000,000. That is one item. Then $100,000,000 from the windfall. Then $80,000,000 from the capital-stock tax. That was because they had cut it down to 70 instead of $1.40. So he adds $80,000,000 there to get the $803,000,000. You are now figuring the same way. We get $560,000,000 out of what we have done, and I do not see why we do not add to that, the windfall of $82,000,000, and then add to that instead of the $80,000,000 capital, because we retain it at $1.40, add to it $168,000,000. I cannot get it out of head the other way.

Senator CONNALLY. If you increase the capital-stock tax you might get it that way, but if you do not increase it, it is static.

Senator LA FOLLETTE. It all depends upon whether you are asked to compare this bill with the House bill, or whether you are trying to find from the Treasury how much this bill will raise over existing law, and you cannot do both things at the same time and get any kind of arithmetically sound estimates.

Senator CONNALLY. These estimates are not based on the House bill at all; they are based on the present law; so I do not see why we should have to consider the House basis.

Senator BARKLEY. The President asked for $620,000,000 permanent revenue over the present law. He suggested that it be gotten from corporations, but he said he wanted it. Now, we have that $620,000,000 here, and in addition, your present revenue. It is true that $82,000,000 of it may be temporary, and will be only for once.

Senator HASTINGS. That leaves you $183,000,000 short.

The CHAIRMAN. Can you help us out on this, Mr. Seltzer?

Mr. SELTZER. I will be glad to try.

The CHAIRMAN. It is quite true that here was a case of comparing this bill with your estimate and not with reference to our bill. But here is Mr. Morgenthau's statement of the yield under the House bill, and he adds $80,000,000 from the capital-stock tax.

Senator GERRY. Did you not only add part of the capital tax in that money that he asked for?

The CHAIRMAN. In the House bill they reduced it one-half to 70 cents, and they got $80,000,000. If they had not repealed it but had left it as at present, they would get $168,000,000 out of that proposition. Why was it that in that estimate that he first took it all out, but then put it back in?

Mr. SELTZER. For this reason. The House committee wanted to raise the permanent revenues in a way separate and different from the way in which they would raise the temporary revenues, so in computing what they would get from their changes in corporation and individual taxes, principally corporation taxes, they said, "Let us assume that the capital-stock and excess-profits taxes are repealed, because they are repealed in their view for permanent revenues." Then they set up taxes which it is estimated would yield $623,000,000 or $620,000,000 rgular revenues without including the capital-stock or excess-profits tax.

The CHAIRMAN. That was from corporate earnings?

Mr. SELTZER. That is right.

The CHAIRMAN. All right.

Mr. SELTZER. Then they say, "But we are short on the temporary revenues, so let us impose a temporary capital-stock and excess-profits taxes combination to raise some of these temporary revenues."

There is no real conflict, therefore. Here you are raising without repeal of the capital-stock and excess-profits tax these sums which you added up to $599,000,000, so you cannot use those for temporary revenues, since you are counting on them right here for permanent revenues.

Senator BYRD. Would it not simplify it a great deal if we would consider that we were short on permanent revenues, then consider what we are short on temporary revenues. There is a vast difference between the two. Roughly, what do you think that we are short of now on permanent revenue?

Mr. SELTZER. Well, on permanent revenues you are short the difference between $620,000,000 and $559,000,000, or about $60,000,000.

The CHAIRMAN. What are we short on temporary revenues?

Mr. SELTZER. Any way that you would like to handle that. The President had suggested making up the sum of $517,000,000 in 2 or 3 years. He was not very specific whether it should be 2 or 3 years.

Senator CLARK. Mr. Chairman, I do not see that the question whether they are permanent revenues or temporary revenues could really be of any predominant importance in this thing. It is still contemplated that the Congress will meet next year, and it seems to me the thing that this committee ought to do and that Congress ought to do is to provide for the revenue for next year. If it is necessary to put on something else next year to supply some of the temporary items of taxation which pass out of existence, we will have plenty of time to do it next year.

Senator GERRY. You are going to have a tax bill next year any way.

Senator BARKLEY. You do not have to raise but $793,000,000 to carry out the President's suggestion. If you spread this $517,000,000 out over 3 years, you get $173,000,000 a year, which with your $620,000,000 permanent revenue makes the total $793,000,000.

The CHAIRMAN. I want to ask Mr. Parker to explain this proposal (c) (1) which struck me as a very forcible proposition. In this proposal, you provide for the repeal of the present capital-stock and excess-profits taxes, and, in addition to that, even though you are repealing it, you are getting $641,000,000, or if we do not repeal it, we ought to get $168,000,000 a year on top of it.

Mr. PARKER. Nearly that; not quite.

The CHAIRMAN. Explain that and let us see about it.

Mr. PARKER. In spite of the fact that it throws the whole plan more or less before the committee again, it does seem to me that it ought to be considered on account of the very little difference in the taxes that occur under the two plans, and I could make that plainer by comparing the total tax that would be secured under the two plans.

Let us take a corporation with a net income of $100,000. If no dividends are declared, under the committee plan as adopted a few days ago, the tax would be $23,740. Under this plan (c) (1), which contemplates 25-percent tax with a 40-percent deduction for dividends paid, it would pay $25,000.

Senator LA FOLLETTE. If no dividends were paid?

Mr. PARKER. No dividends at all. The plan (c) (1) would only increase the tax by $1,260; that is in the maximum case. That is, with absolutely no dividends declared. That is the unusual case, and it is not the average case.

Suppose this corporation declares about one-tenth of its net income, or $10,000, in dividends. Under the committee plan, as adopted, it would pay $23,040. Under plan (c) (1) it would pay $24,000, a difference of only $960. These differences will get less and less as more reasonable distribution is declared.

Supposing $20,000 is distributed in dividends. On the committee plan the tax would be $23,660. Under plan (c) (1) $23,000, a difference of only $660.

Senator CONNALLY. Does your plan take into account the exemption of $1,000?

Mr. PARKER. No. Of course, you can put that in or not. The $100,000 here is not affected by that $1,000 at all.

Senator CONNALLY. It would, though, on the other corporations?

Mr. PARKER. That is $30,000,000 altogether.

With $30,000 distributed—that is, under the community plan—the tax would be $21,640; and under the plan (c) (1), $22,000, a difference of only $360.

With a dividend distribution of $40,000, or 40 percent net income, the committee plan would be $20,940; and (c) (1) $21,000, a difference of only $60.

The CHAIRMAN. Does that contemplate an increase in the normal taxes?

Mr. PARKER. No; except that we are repealing the exemption. The dividends will be subject to normal tax, but there is no proposition from 4 to 5.

The CHAIRMAN. What is the lowest flat rate that you will reach under that plan under the corporation tax?

Senator COUZENS. Let him finish the schedule.

Mr. PARKER. I will skip through it a little faster. I would like to give you the $50,000 distribution, or 50 percent. Under the committee plan the tax is $20,240; and under the plan C1, it is $20,000; in other words, now we are going the other way. The plan C1 is going to give you the advantage whenever you distribute 50 percent or more of your net income in dividends. This now is going to the advantage of the corporation.

Senator BYRD. The same thing applied to the House bill. They gave down to zero tax if they distributed everything.

Mr. PARKER. Yes; I still think the differences are very small.

Senator BYRD. Have you provided for any cushions?

Mr. PARKER. I think cushions are unnecessary except the contract cushion, which I think is necessary under this plan, and which I suggested to the committee the other day, which I suggested was necessary under the proposal the committee made.

Senator BYRD. A corporation that has no debts to pay would only have to pay 15 percent, where one that had debts would have to pay 25 percent.

Mr. PARKER. Under the committee proposal, you are going to have to pay 23.74 percent.

Senator BYRD. I understand that. It is a difference of 10 percent instead of 7 percent.

Senator HASTINGS. If they pay out the whole 100, they pay a tax of $15,000.

Mr. PARKER. That is true, but that would mean, of course, that they would have to distribute some of their surplus to do that. I am taking the limiting case where they declare out $82,000, which is all subject to the 18 percent. Under the committee plan, they would pay $18,000. Under plan C1, they pay $16,800, or $1,200 less. In other words, you have a tax here of $1,200 less, which is a very small amount in comparison to $18,000, and in the top bracket where they do not distribute anything, they pay $1,200 more. It just about balances up.

Senator BYRD. To a modified extent it carries out the same principle of penalizing the small company that applies its earnings either in the building of a plant or to pay a debt, and benefits the big company, except to a modified degree.

Mr. PARKER. That is true, Senator, but that is an argument against the undistributed-profits tax. You have in your Senate proposal an undistributed-profits tax. Some people like it and some people do not.

Senator BYRD. One vital difference between the two is that under your plan, the rich corporation that can distribute all of its earnings will only pay 15 percent. Under the plan that we adopted the other day, they will have to pay 18 percent.

Mr. PARKER. They will have to pay more than 15 percent unless they distribute some of the surplus. The only way they are going to get down to 15-percent tax, and we can take that away and stop it at $16,800, if you want to.

Senator BAILEY. I thought the chairman asked you to state the difference between the two plans. Now we are discussing this plan. I think that is past. I am not ready to consider the whole thing. Let us go ahead and see where we are. I want to know what we are doing under the present. If it does not raise enough money, let us find other ways to do it. If we are going to change the plan every morning, we will be here until doomsday.

Senator COUZENS. That is what Mr. Parker is trying to do, to explain it.

Senator GERRY. You are going back to something we voted down in principle.

Mr. PARKER. I want to show you the difference in the estimates.

The CHAIRMAN. There is no desire to change the plan unless it meets with the approval of the committee and everyone thinks that we have to get more money, and this is the way to do it.

Senator LA FOLLETTE. I think it does bring out one thing that I have been impressed with from the beginning, and that is that the amount of tax the corporation pays under any plan is the thing that is vital to the corporation. It is not the rates. And I think that this shows conclusively that there is not any very great variation between these two plans so far as the actual application of them is concerned, even though you may say that there is a very substantial difference so far as the rate is concerned.

Senator BYRD. I differ with Senator La Follette there greatly on that, because there is a vast difference in the application to different companies. The rich corporation will benefit much more by Mr. Parker's plan than by the plan this committee has adopted, and no one can deny that.

Senator BLACK. I do not care to deny it myself, but I have a very vigorous protest from a small corporation insisting that the Senate plan would be most injurious to them and favoring the other idea of the undistributed-profits plan. I am just calling your attention to it. It was the first letter that I had on the subject.

Senator BYRD. The corporation that is in a position to pay all of its earnings out in dividends is in a favorable position. The minimum rate under the plan the committee adopted is 18 percent.

Mr. PARKER. The small corporations can take advantage of it just the same.

Senator BYRD. They may not be in a position to do it.

Mr. PARKER. There is a difference, Senator, but the difference is very small. That is what I want to bring out.

Senator BYRD. It carries out the same principle that the committee voted against.

Mr. PARKER. What I was particularly interested in was the estimates on these two plans, and the fact that the second plan gives $150,000 000 more and puts you in a position where your revenue proposition is practically concluded, whereas under the plan as adopted by the committee, you have got to go on and get $200,000,000 of revenue.

Senator BYRD. Wait a minute, Mr. Parker. Let me correct you on that. They have testified here that the House bill with respect to corporate taxation would bring in $591,000,000. We are only short with respect to those particular taxes, something like $60,000,000. The other shortage comes from other things. Your plan would not correct that shortage. Am I correct about that? The House bill, it has been testified here, brought in $591,000,000 from the corporate income. This bill brings in how much?

Mr. SELTZER. A good deal of the revenue of this bill, $641,000,000, is obtained from individuals.

Senator BYRD. I understand; but I am speaking about this schedule no. 7 compared with the House bill. The House bill brought in how much?

Mr. SELTZER. $591,000,000 from corporations.

Senator BYRD. $591,000,000 from corporations, and as a substitute to this the committee's bill brings in how much?

Mr. SELTZER. 522.

Senator BYRD. A difference of about 50 millions between the two.

Mr. PARKER. Senator, I cannot agree with that, because we get right back to the other proposition that the House bill was estimated on the proposition of the capital stock and excess-profits tax being repealed, and that additional revenue was not only additional over existing law, but this is additional to the extent of making up for the repeal of the capital-stock and excess-profits tax. The $560,000,000 contemplates retention of this capital-stock tax.

Senator BYRD. It is not included in the figures, Mr. Parker. I have the figures right here. The $168,000,000 is not included in the $560,000,000 at all.

Mr. PARKER. To get the $560,000,000 additional revenue under that estimate, Senator, as I understand it, and I am sure that I am right, you have got to retain the capital-stock and excess-profits tax, which brings in one hundred and sixty million-and-odd dollars a year. Is that your understanding?

Senator BYRD. It is to be retained, but the $168,000,000 is not included in the $560,000,000. The $168,000,000 is completely new revenue.

Mr. PARKER. No, Senator.

The CHAIRMAN. They argue that it is contained in it.

Senator BYRD. Let us go over it, because that is very important.

Senator BARKLEY. Under this Senate bill, the $168,000,000 is not included in the figures that make up the figures of $559,000,000. That is absolutely certain. Because you have $215,000,000 to $217,000,000, $90,000,00 and $37,000,000.

Mr. PARKER. And what are those figures, Senator? Those figures represent additional revenue over existing law, contemplating the retention of existing law, which contemplates the retention of the capital-stock tax.

Senator BARKLEY. Of course. But your House bill raised $803,000,000 revenue, which, of course, included enough to obsorb the loss of the capital-stock and excess-profits tax, but that does not mean $803,000,000 net revenue over and above existing law. You have to subtract in the House bill your capital-stock and excess-profits tax from $803,000,000 in order to get your net over the present law.

Mr. PARKER. No, Senator.

Senator BARKLEY. Take your $641,000,000, then, from your corporate taxes under the House bill. Where do they get enough to make up $803,000,000?

Mr. PARKER. Under the House bill, the estimate of $591,000,000 was additional revenue over existing law after subtracting out the capital-stock tax, which they contemplate being repealed.

Senator BARKLEY. That is true.

Mr. PARKER. In other words, if they estimated in the House bill this corporate plan on the basis of retaining the capital-stock and excess-profits tax, their estimate of revenue instead of being $591,000,000, would be $168,000,000 additional.

Senator BARKLEY. That is true; $591,000,000, which absorbs $168,00,000, and then makes up that much difference, in the corporate tax, and $559,000,000, and that leaves about $40,000,000 difference between the corporate-tax provisions of the House bill and the Sen-

ate, because you are leaving your excess-profits tax in there, and therefore you do not have to absorb it.

Mr. PARKER. I do not think that is right, that it is only $40,000,000; $591,000,000 is contemplating repeal of the capital-stock tax.

Senator BARKLEY. I understand that; it contemplated it.

Mr. PARKER. And $560,000,000 not contemplating it.

Senator BARKLEY. What is the difference between adding enough money in the House bill to get $168,000,000 and leaving it in the law as it is now? You get it just the same. You might wipe the capital-stock tax and the excess-profits tax out of your mind. Just forget it.

Mr. PARKER. No, Senator. I have two estimates in my hands here.

Proposal no. 7 gives you a certain estimated increase in revenue. What does it say for the assumption? Right up in the first paragraph it says that the assumption on which this additional revenue is estimated is, (1) retain the present capital-stock and excess-profits tax.

Senator BYRD. But that is not added in the total.

Mr. PARKER. Proposal C–1 says that this additional estimate is estimated on a repeal of the present capital-stock and excess-profits tax. There must be a difference.

Senator BYRD. If we repeal the capital-stock tax, you would be right. But we do not propose to repeal it. We put it back to the extent of $168,000,000.

Senator BARKLEY. The House repeals it but makes it up. The Senate does not repeal it, so those two things cancel each other out.

Mr. PARKER. This proportion of the House estimate must have been estimated on the basis of the repeal, because after putting in the $591,000,000, one of the items which they used in order to get the temporary revenue is $80,000,000 due to the retention of the capital-stock for 1 year, which they add on at half the rate. So in the House bill itself, the capital-stock tax is added, $80,000,000.

Senator BYRD. Does it make any difference to you whether we put the capital-stock tax back or not? That is a matter for the committee to decide. If they get $168,000,000 that way, you cannot say then that the bill is short because it is put back.

Senator LA FOLLETTE. It depends on what you are comparing it with.

Mr. PARKER. That is the whole thing that I am interested in. I am assuming the committee wants to get $793,000,000.

Senator BYRD. What I want to make clear is that this retained capital-stock and excess-profits tax in proposal no. 7, $168,000,000 is not carried out in the total of that, but you can add it up.

Senator LA FOLLETTE. They wanted to give you an estimate over the existing law, and the capital-stock and the excess-profits tax are in the existing law. This estimate furnished you by the Treasury is not a comparison with the House bill; it is a comparison with existing law and states what the additional revenue will be.

Senator BYRD. All I want to make clear is that the item that says "Retain the capital-stock and excess-profits tax, $168,000,000" is not carried in the totals of that particular proposal. You can add them up and see that it is not.

Senator LA FOLLETTE. For the simple reason that they are trying to tell you how much it will raise over existing law.

Mr. PARKER. That point absolutely has to be clear, because that is the whole crux of the matter. I still think, and I think if we have Mr. Seltzer's attention that he will agree on it. The committee must get that straight.

The CHAIRMAN. We have to understand this proposition.

Senator BARKLEY. Let us forget the House bill for a moment. We have to raise $620,000 of permanent revenue?

Mr. PARKER. That is correct.

Senator BARKLEY. Our bill up to date raises $559,000,000 permanently. That does not include the windfall taxes?

Mr. PARKER. That is correct.

Senator BARKLEY. Which leaves us $61,000,000 short for permanent revenue?

Mr. PARKER. That is true.

Senator GEORGE. Let us not do more than one thing at a time. I am willing to base my guess that we will get it under the administration of this bill.

Senator BARKLEY. As I figure it, you are $150,000,000 short.

Mr. PARKER. Yes; and you cannot make up that shortage by putting on the capital-stock tax. That is what I want to make clear to Senator Byrd.

Senator BARKLEY. With the windfall tax added, and what this bill raises here now, whether you consider it permanent or temporary, because the windfall can only be temporary, you are $150,000,000 short.

Mr. PARKER. That will show that we both interpreted it the same way, if Mr. Seltzer confirms that. If we annex the Senate proposal to return $560,000,000 approximately, and enact the windfall tax, which is $82,000,00.

Senator BARKLEY. That is $642,000,000.

Mr. PARKER. Yes. The President asks for $793,000,000. According to my figuring, that leaves $151,000,000 short for the first year. Is that right, Mr. Seltzer? Do you figure that we are about $151,000,000 short, assuming that we need $793,000,000 the first year?

Mr. SELTZER. Yes.

Mr. PARKER. And we cannot make up that shortage by retaining the capital-stock tax, because that has already been figured in.

Mr. SELTZER. That is correct.

Senator BARKLEY. That is the shortage you get after figuring the capital-stock tax in?

Mr. SELTZER. Yes.

Senator BYRD. If I am incorrect, I want to be corrected. This proposal relating to the permanent revenue is $60,000,000 short now as compared with the House bill.

Mr. PARKER. That is right.

Senator BYRD. That is the basis we can go on. The permanent revenue we are only short $60,000,000 as compared to the House bill. There must have been some changes made in the windfall tax and other things to have created this shortage independent of what we did in proposal no. 7.

Mr. PARKER. I did want to point out, and that was the purpose of comparing this other plan, that under this $641,000,000 that contemplated the repeal of the excess-profits tax, so if you kept it you

could have added on $150,000,000 more and you would have your total.

Senator BARKLEY. I do not understand how, if the House bill produced $591,000,000 from corporations and $100,000,000 from windfall, which makes $691,000,000, I do not know where the House bill gets that $110,000,000 to make up the $803,000,000 that you say their bill raised.

Mr. PARKER. They kept the capital-stock tax of $80,000,000 right in the estimate, at half the rate.

Senator BARKLEY. Of course, our bill here on the corporation tax is only about $32,000,000 short of the House bill.

Mr. PARKER. The House bill had an estimate, as I recall, of $623,000,000 of permanent revenue above existing law, after having repealed the capital-stock tax.

Senator BARKLEY. I understand.

Mr. PARKER. And then they added $100,000,000 more for the windfall tax, which is $723,000,000, and then they had $80,000,000 for the retention of the capital-stock tax at one-half the rate for one year, and that is the $803,000,000.

Senator BYRD. Do you not think that we should just assume that what the comittee did the other day is the action of the committee, and if we have to get some more revenue, to try to get it? I voted for that on the idea that it was a compromise. I do not approve of it and I feel that having compromised it as we did, that we should stand by it.

The CHAIRMAN. We all stood by that the other day as a compromise proposition. I thought we were going to get the money. If this other proposition should appeal to the committee and the committee should feel that it would get rid of the shortage by adopting it, all right; but we won't have any dissension in the committee about that. This informal discussion need not go on the record.

(Discussion off the record.)

The CHAIRMAN. We will resume at 3 o'clock this afternoon in the District of Columbia Committee room at the Capitol.

(Whereupon, at 12 noon, a recess was taken until 3 p. m. of the same day.)

AFTERNOON SESSION

The committee reconvened at 3 p. m., at the expiration of the recess, in the committee room of the Committee on the District of Columbia, Capitol Building.

The CHAIRMAN. Is there anything further from Mr. Savoy?

Mr. SAVOY. I have nothing further.

The CHAIRMAN. Is the Subcommittee on Sugar ready to report?

Senator KING. The committee has not met. If we were not going to have a session this afternoon, I thought that we would get together. But at the present time we are not ready to report.

The CHAIRMAN. I think now we have finished with the administrative features except the liquidation proposition. What other administrative changes are there, Mr. Parker?

Senator BAILEY. You have this matter of common trust funds. I would like to submit a statement about that. A common trust fund is a fund in a trust company or a bank with a trust department, in which by reason of the number of small deposits in trust, they make

a common fund. Say that I put in $1,000,000, you put in $1,000, Senator Gerry $1,000. You cannot invest the $1,000 well, but when you get $100,000, you can make a good investment, and they participate in the profits pro tanto. The law has held that that sort of a trust is an association under the existing law.

Of course, it is not an association. It is a necessity if the bank is going to get trust business. It can associate my $1,000 with several other $1,000, and lend it out, but alone it cannot make a fair investment of $1,000. The proposition is that the funds invested, the profits, shall be taxed to the individual just as if it were a person and not a corporation. As the law stands it is proposed to constitute that association of trusts as an association and tax it as if it were a corporation, which is clearly not intended by the law, and it is clearly unjust. The corporation is the trust company. You tax its profits as a corporation.

Mr. KENT. That situation has resulted from a decision of the Circuit Court of Appeals for the Second Circuit, which has held that that is the effect, under the present law.

The CHAIRMAN. To be taxed as a corporation?

Mr. KENT. Yes.

Senator BAILEY. This amendment reads as follows [reading]:

A common trust fund shall not be subject to taxation under this title, but each trust participating therein shall include in computing its net income its share of each item of the income, deductions, and credits of such fund, computed, classified, and subject to the same provisions as in the case of an individual.

That is what it is—it is not a corporation.

Senator KING. Any profit that goes to the trustee——

Senator BAILEY (interposing). That goes to the bank. But whatever I got as an individual, would be as an individual. The amendment goes on further [reading]:

Subject to the approval of the Commissioner, the share of each trust in each such item shall be determined in accordance with the principles of accounting adopted in connection with the operations of such fund. The computation of the gain or loss realized, if any, and the basis of assets received, by a withdrawing trust, upon the withdrawal of a trust from such fund, shall be governed by the rules applicable in the case of the withdrawal of a partner from a partnership.

That is to say, if he withdraws, he pays his tax from his profits. You simply throw him into the individual bracket.

Continuing:

No gain or loss shall be realized by a common trust fund by reason of admission of new participants. The term "common trust fund" means any fund maintained by a bank or trust company, incorporated under the laws of the United States or any State or Territory or of the District of Columbia and subject to the supervision of Federal or State banking authority or both, solely for the purpose of managing, investing, and reinvesting, as a unit, funds contributed thereto from trusts, estates, or other funds as to which such bank or trust company is a fiduciary (referred to in this section as trusts), provided that such fund is one which is maintained pursuant to rules and regulations of the Board of Governors of the Federal Reserve System prevailing from time to time (or could be so maintained if the bank or trust company maintaining the same were a member of the Federal Reserve System).

It strikes me that that is thoroughly reasonable and just, and I hope the committee will adopt it.

The CHAIRMAN. I recall that the other day when we had this matter up, that this question arose. Senator Black brought it up,

I believe, and the experts said that it was impossible for them to get it fixed immediately. That is my recollection.

Senator BAILEY. There is no complication about that, and in practically every trust company of the United States there are common trusts. They make their reports to the fiduciaries, and the report is, "Your profits from this institution in the past year at 4 percent amounted to $4 or $400", or whatever it may be.

I happen to get one of those reports; I happen to be a guardian. There is no trouble on earth about it; they tell me what to report on the income tax. It is a simple thing, and it is a great injustice to prevent somebody with $5,000 or $10,000 from getting his money invested in a trust company or by means of a trust company without being taxed as a corporation.

Senator GUFFEY. I quite agree with the Senator.

Senator LA FOLLETTE. Mr. Beaman made a statement about it, as I remember. He said there might very well be something in this, but if the committee wanted it in language carefully worked out, that it would take some time to do it.

Senator KING. That is my recollection of his statement.

Senator BAILEY. They have not worked anything out, and this language is perfectly simple and it is not susceptible to misconstruction. It simply provides that where a common trust is made up of several funds, the profits to each beneficiary shall be taxed as if he were an individual—precisely what he is—and that the sum of it should not be taxed as if it were a corporation.

Senator KING. The existing law has attempted to segregate from the aggregate profits, if any, the amount which would be due to A, B, and C.

Senator BAILEY. Yes; and you do not propose to tax aggregate profits as if they were a corporation. You propose to divide the profits according to their pro-tanto interest.

Senator KING. I was wondering whether the Treasury Department, where these common trusts exist, have attempted to separate from the aggregate the amount which would be due to A, B, C, and D.

Senator BAILEY. Here is the statement of Mr. Gilbert Stevenson, who, by the way, is the trust officer of an institution in Delaware and was formerly the trust officer of an institution in North Carolina [reading]:

> A common trust fund makes it possible to invest a fund of $1,000 as economically and satisfactorily as a fund of $100,000. In other words, a common trust fund is merely a means of grouping the funds of many small trusts for investment purposes.
>
> At the present time there is no general rule as to the taxation of common trusts and the general uncertainty has been heightened by the recent Brooklyn Trust Co. decision (80 Fed. (2d) 865), where the composite fund of the Brooklyn Trust Co. was held to be taxable.
>
> Since all of the ordinary income of the common trust fund must, under the rules, be distributed, it follows that if the common trust fund be taxed as an association, small trusts—the very ones that are least able to bear the burden of taxation—are subject to an extra tax burden, the income being first taxed at the full corporate rate upon the common fund as an association, and then taxed again to the estate or trust itself as though the income were corporate distribution.

This amendment is for the purpose of clearing up that situation. It does not deprive the Government of any of its taxes justly due,

and it may throw taxes into the hands of the Government if somebody gets a high income in the individual brackets.

Senator KING. Has the Treasury been treating them as a corporation, or been attempting to collect from the individuals, and have the individuals who have interests reported their dividends as part of their income?

Mr. KENT. The problem did not come to my attention at all until the matter was presented in the committee hearings, and I assume that since this case got into court in the second circuit up there, that the Bureau is proceeding on the theory that they are in associations.

Senator KING. How have you been proceeding anterior to this time?

Mr. KENT. There has been a number of important decisions recently which have put a rather broader interpretation upon the association provisions of the statute that have formerly been the case, over the considerable number and variety of what were regarded as strict trusts and have been swept into the ambit of the association provision of the statute.

Senator BAILEY. You are here representing the Treasury. Does it appear to you that this is unjust in any particular, that if I put $1,000 in a common trust and they put it in with $100,000, and in there they make 6 percent on my $1,000, where they could not have made 3 percent without it, does that constitute me a member of an association? Should we not have a law that would enable me to get my income from a trust fund and pay my income as an individual? What is wrong with it?

Mr. KENT. I have not at the present time any quarrel with their objective. As far as I can see, there is a great deal of merit in it. But we have been so busy with so many different things we were not prepared to say for any particular form of amendment that it would accomplish what they had in view.

Senator WALSH. Are there many taxpayers in this classification?

Senator GUFFEY. A great many.

Mr. BEAMAN. It is not right to say that the individual trust shall be taxed as an individual, because under the law now it may be taxed as a trust.

Senator BAILEY. I don't see how you would have any trouble. I had dealt with these things for a long time; and I never had any trouble with it. I can invest $100,000 for everybody in this room and do it. The Treasury says that they are not ready because they have not passed on it. They do not have to pass on these simple things. It is hard enough for them to pass on the addition and the subtraction, but when it comes to such a simple matter as this, I think the committee is perfectly competent to pass on it.

Senator KING. Do you see any chance for evasion or investment being made ostensibly as a common trust to escape the corporate taxes?

Senator BAILEY. I do not see how there could be any such difficulty. Just take a practical instance. I get a report from the Norfolk Bank of Commerce and Trust once a year for certain wards that I have. The investment this year comes to so much, and so much of it is tax which is withheld at the source, and on so much they tell me, "You

are liable to pay taxes to the State of Virginia and to the United States." That happens to be a Virginia trust company. I go out and I make my report. There is not any trouble in it, but if they were converted into what you call an association, then it will make my ward pay taxes on the individual income and also a pro-rata share of a corporation income. That is not fair and it was never so intended by the law.

Senator BLACK. I would like to see this amendment pass and go to conference, and I want to say that it is on exactly that basis that I favor the original objective of this bill. I do not think it is fair to put a tax on an individual simply because he has his money in a trust, and it is a common trust, when you let an individual who invests it on a different basis. I believe exactly the same way about the original objective of this bill; and feeling as I do about the original objective, I am bound to be for this, and I hope we can pass it.

Senator GEORGE. I think it ought to go to conference. I think that we ought certainly try to work out something on the dissolution of the corporations and something that would bring the issue in conference, and it ought to go to the conference.

Senator KING. Something like the liquidation we were talking about this morning?

Senator GEORGE. Certainly. To bring the issue to the conference to see if we can do something.

Senator KING. If there is no objection, the amendment offered by Senator Bailey——

Senator BAILEY. I have the amendment here, page 767 of the Revenue Act of 1936, hearing, part 8, dated May 8, 1936. The amendment is marked, and I will give it to the stenographer.

(The proposed amendment is as follows:)

A common trust fund shall not be subject to taxation under this title, but each trust participating therein shall include in computing its net income its share of each item of the income, deductions, and credits of such fund, computed, classified, and subject to the same provisions as in the case of an individual. Subject to the approval of the Commissioner, the share of each trust in each such item shall be determined in accordance with the principles of accounting adopted in connection with the operations of such fund. The computation of the gain or loss realized, if any, and the basis of assets received, by a withdrawing trust, upon the withdrawal of a trust from such fund, shall be governed by the rules applicable in the case of the withdrawal of a partner from a partnership. No gain or loss shall be realized by a common trust fund by reason of admission of new participants. The term "common trust fund" means any fund maintained by a bank or trust company incorporated under the laws of the United States or any State or Territory or of the District of Columbia, and subject to the supervision of Federal or State banking authority, or both, solely for the purpose of managing, investing, and reinvesting, as a unit, funds contributed thereto from trusts, estates, or other funds as to which such bank or trust company is a fiduciary [referred to in this section as trusts]: *Provided*, That such fund is one which is maintained pursuant to rules and regulations of the Board of Governors of the Federal Reserve System prevailing from time to time [or could be so maintained if the bank or trust company maintaining the same were a member of the Federal Reserve System].

Senator KING. I hope our experts will examine it very carefully.

Mr. BEAMAN. Senator, if the committee so votes, we will put it in the bill, but if you want the experts to examine it, it will take us a long time. Unless you want us to hold up the bill.

Senator KING. There is no objection to your examining it anyway.

Mr. BEAMAN. We will put it in just the way it is.

Senator HASTINGS. This has been the suggestion, Mr. Beaman—that you examine it after it goes in the bill, so that when it comes to the conference, if you find anything particularly wrong with it, or any suggested language that would improve it, you may suggest it to the conferees.

Senator KING. That matter is disposed of.

Senator GERRY. I would like to bring up an amendment that I brought up yesterday in regard to the profit-sharing plan and distributing stock to employees. I brought this question up with the experts, and I brought it up yesterday, and what it is, then, is that where a corporation distributes stock to its employees, and the employees contribute and the corporation contributes, when the stock is distributed the employee is taxed on the yield of the distribution of his stock, not when the stock is sold.

I think I can give an example which will explain this. For example, the employee puts in $1, and the employer puts in $1, and then the stock goes up in value say 50 cents, so that the value of the stock is $2.50. When that stock is distributed, the contribution of the balance that the employer puts in is taxed, plus the proposed 50 cents appreciation in value. What should be taxed is only the $1 that the employer puts in.

What I have in mind is that it is not fair to tax the employee. The whole idea of this amendment is that this is a profit-sharing scheme, and the employee gets the benefit of it by holding the stock, and when he sells that stock, he has to pay whatever has been made on the capital gains, and capital losses. It is not fair to tax him on it before it is distributed, because it means that probably he has not got the money and he has to sell these shares instead of realizing on them, and it seems to me that this plan is a beneficial plan.

Senator Black called attention to the fact that some of these people forced the employees to buy stock, but I do not think this has anything to do with this profit-sharing plan. But to the employees, the mere fact that they have to pay this tax when the stock is distributed to them, does not have anything to do with it, and I think it is a very unfair thing to make these men working in the factories pay this tax when they have not realized on it. What they do is that they assess the amount of the profit on the stock on the market value, and the amount they receive, and if the market value is higher, they tax him for it. If he wants to hold his stock, which is the whole idea of the plan, it is a saving plan, and if the market goes down, he already pays the tax and he has lost.

Senator KING. That has been changed several times, that provision.

Senator GERRY. The Ways and Means Committee came out in 1928 and had a long statement on it, which I read to the committee the other day, and it seems that the plan has merit.

Senator HASTINGS. If he puts in $1 and the employee puts in $1, and the stock at the time it is distributed is worth $2.50, does he count it at $1.50 or just 50 cents?

Senator GERRY. Just the 50 cents.

Mr. PARKER. He pays on what the employer puts in. He does not pay on the capital gains until he sells the stock.

Senator HASTINGS. What does he pay on?

Mr. PARKER. Whatever contribution the employer paid, plus the dividends or interest that has accrued to his share during the time

the stock was being purchased. It would be something like buying stock on a purchase plan, only the employer and the employee both contribute.

Senator BAILEY. Suppose I buy stock on the installment plan, and I pay tax on my income. I do not pay any tax on the stock until I sell it. Why should we make somebody else pay a tax on a stock before he sells it?

Senator LA FOLLETTE. We had it the other way once, and then we changed it because they got an advantage out of it by changing it. When the market was going down it was an advantage to them to take the loss.

Senator BAILEY. I am in favor of treating them like anybody else is treated.

Senator LA FOLLETTE. I personally think that as long as they have had the benefit of it when it was going down, that the Government ought to get the benefit of it when it is going up. Take it off sometime when it is a sound thing to do. But I think that where we switch around and try to take into consideration the position of the taxpayer and try to give him an advantage, the Government always takes a licking because they always switch it around at a time when it is going to be to the advantage of the taxpayer and to the disadvantage of the Government.

Senator BAILEY. We should fix the principle and keep it.

Senator LA FOLLETTE. You cannot fix it because they come around here and want it changed all the time. I feel a good deal about this, in a smaller way, as I do about the capital gains and loss proposition. The Government, it seems to me, ought to have some consideration in the picture.

Then, as I said the other day, these are not only these small stockholders, but all of the executives that participate in this thing. I think that is why you hear so much about it.

Senator GERRY. I do not see where the executive gets anything out of it.

Senator LA FOLLETTE. They regard themselves as employees.

Senator GERRY. If they go into an outside corporation and have stock, they are not taxed on it unless they sell. I do not see that it makes the slightest difference.

Senator LA FOLLETTE. It makes a great deal of difference if they can take off the taxes when the market is going down and not have it added when the market is going up.

Senator GERRY. At the present time, if you adopt this, they cannot take it off, because, as a matter of fact, they can only take that loss on it or the profit, when they sell. That is what you do on every other stock.

Senator BLACK. I would like to ask a question of Mr. Kent about it. Do you know to what extent these plans are used by the companies over the country?

Mr. KENT. There are a great many of them. I have not any exact statistics with me on it, Senator. There are a great many of these plans, set up following the war. A large number of concerns over the country set up plans in which their employees participated.

Senator BLACK. Is it possible to use them in such a manner that those who wanted to escape taxes could put large blocks of stock in these funds?

Mr. KENT. Of course, it is hard to generalize, because each plan differs in some respects from any other plan. Some of these contain limitations upon the amount of stock which an employee can purchase. Those limitations are usually in terms of percentage or income.

Senator BLACK. I ran up on some funds of that kind where it seemed that very large stockholders were in the plan.

Mr. KENT. Yes.

Senator BLACK. What I am getting at is, Could that be used as a device for preventing the payment of taxes?

Senator KING. Or dumping it on the employees?

Senator GERRY. As soon as you sell the stock, you have to pay the tax. I do not see how it could be.

Senator BLACK. I am trying to find out, because I have heard that those plans are used for that purpose. Frankly, I do not see how, but I would like to get the information.

Mr. KENT. If a company is contributing a portion of the purchase price, under the present rule when the stock is distributed, the employee pays a tax not only upon the amount which the company has contributed toward its acquisition, but also upon any appreciation in the market value of the stock. You value the stock at the time of distribution, and the difference between its then value and what the employee has actually put into it in the earlier years is treated as taxable income at that time.

Senator BLACK. You do not know of any method by which this plan could be used or is used for the purpose of evading taxes?

Mr. KENT. No; other than the method which any taxpayer can use in selecting the year in which he is going to dispose of his securities, and of course the 1934 limitation on the deduction of capital losses was aimed, in part at least, to meet that situation.

Senator KING. Mr. Parker, you are familiar with this proposition that has just been presented. What is your view in regard to it?

Mr. PARKER. I testified the other day on it. I pointed out that it was a matter of getting a consistent policy and a question what was the right policy. I am inclined to the view that the policy suggested is correct, but, on the other hand, I recognize considerable merit to Senator Black's contention that these pension plans are not all of one variety. There have been some good ones and some bad ones. Whether there could be any improvement made in that section to keep out the bad ones, I do not know, and I do not know how many of the bad ones are left. I think Senator Black knows more about that than I do, because he has investigated some of those.

Senator LA FOLLETTE. Won't you get into this question, too, if you go back to the old rule, and you will have a controversy as to why ownership in this thing was effectuated, whether it was when the thing was established or whether it was when it was terminated?

Mr. PARKER. I was informed today of something I did not know yesterday, and that is that the old rule, that there has been a court decision on it which has held to this effect, that if the value of the

stock when a man gets it is less than what he himself contributed to the stock, that you cannot tax him. That mitigates the severity of the former rule, which I had presumed to mean that even if a man had contributed $100 to the stock and he only got back something that was worth $50, that you could still tax him on what the employer put in. You cannot do that, it appears, under existing law.

Senator BAILEY. On the other hand, you never know what the value of the stock is until you sell it. We are not dealing with stocks that are listed on the exchange.

The CHAIRMAN. All in favor of the amendment will say "aye"; all contrary "no". The amendment is agreed to.

Gentlemen, I am going to leave, and Senator King will preside. When you recess, will you recess until 11 o'clock in the morning, because there is a subcommittee on the sugar matter that wants to meet, and we will go on this afternoon and finish up as much as we can.

Senator KING (presiding). Are there any other matters to be brought before the committee?

Senator BAILEY. My amendment on oils.

Senator KING. The chairman suggested that that come up tomorrow morning.

Senator CAPPER. I have an amendment on starch that I have offered.

Senator KING (reading):

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

AMENDMENT Intended to be proposed by Mr. CAPPER to the bill (H. R. 12395) to provide revenue, equalize taxation, and for other purposes, viz: At the end of title IV insert the following:

TITLE V—EXCISE TAXES

SEC. 701. TAX ON HAPIOCA, SAGO, AND CASAVA.—The Revenue Act of 1924, as amended, is amended by adding after section 611 the following new section:

"SEC. 611½. TAX ON TAPIOCA, SAGO, AND CASAVA.—There is hereby imposed upon the first domestic processing or use of sago, sago crude, and sago flour, tapioca, tapioca flour, and casava, whether or not such products or any of them have been refined, modified, or otherwise processed, and in whatever combination or mixtures containing a substantial quantity of any one or more of such products, a tax of 2½ cents per pound, to be paid by the processor or user thereof in manufacturing or processing. For the purposes of this section the term 'first domestic processing' shall mean the first use in the United States, in the manufacture or production of an article intended for sale, of the article with respect to which the tax is imposed. The tax on the article described in this paragraph shall apply only with respect to such articles imported after the date of the enactment of this paragraph and shall not be subject to the provisions of subsection (b) (4) of section 601 of the Revenue Act of 1932, as amended (prohibiting drawback), or section 629 of such Act (relating to expiration of taxes)."

Senator CAPPER. I have a little statement here, Mr. Chairman, which will tell why I think we ought to have this.

The amendment proposes an excise tax of 2.5 cents per pound on tapioca, sago, and cassava, now on the free list.

Expected revenue should be from three to six million dollars annually. On imports equal to 1935 revenue would be $5,672,750. If imports decline, revenue from starches now subject to tariff should increase.

Farm benefit from the measure is an issue at least as important as revenue—more so in the mind of the farmer, because he expects it to increase his income by stimulating the sale of his wheat, rice, corn, potatoes, and sweetpotatoes for the manufacture of domestic starch.

Tapioca, sago, and cassava starches, not grown here but which have the same chemical formula as all other starches. They are used in competition with all other starches in the making of textiles, adhesives, paper, chemicals, and other industrial goods. They are the only imported starches on which the lower cost of production abroad is not equalized by tariff duties. They sell at a price more than 40 percent below the cheapest domestic starches.

Imports by 1-year periods: 1905–14, 62,000,000 pounds; 1915–24, 90,836,000 pounds; 1925–34, 150,304,000 pounds.

In 1935 the imports were 226,910,000 pounds.

First 3 months of 1926, 77,711,000 pounds, or at the rate of 310,000,000 pounds per year.

In relation to United States consumption, of all starches, domestic and imported, tapioca, sago, and cassava constituted 12 percent in 1924, 23 percent in 1934, 26 percent in 1935. In price relationship compared to domestic starches, tapioca, sago, and cassava were 22 percent higher than cornstarch in 1924 and 45 to 46 percent lower in 1934 and 1935.

The principal foreign source, Java, exported to all countries in 1924 about 157,000,000 pounds, of which the United States took 49 percent. In 1935 Java reported over 224,000,000 pounds and the United States took 84 percent of this larger amount. These figures apply to tapioca flour alone and do not include additional quantities of sago and crude tapioca. Among industrial nations Germany uses no tapioca flour; France uses less than 200,000 pounds; Great Britain, with her huge starch-using textile industries, uses less than 8,500,000 pounds; the United States is using more than 188,000,000 pounds, plus about 38,000,000 pounds of sago and crude tapioca. With consumption by foreign nations decreasing or actually vanishing, the United States is taking practically the entire output. Other tropical countries, attracted by Java's success, are cultivating larger amounts of tapioca for the American market. Brazilian exports to the United States grew from 2,204 pounds in 1934 to 6,471,480 pounds in 1935, and have totaled more than 3,300,000 pounds in the first 3 months of 1936.

Competition of these duty-free foreign starches deprives domestic starches of their own market. It has taken over a great part of the previously developed business and is constantly absorbing a large part of the new business developed by the research departments of the domestic starch industry. Many potato-starch mills have been closed, and a surplus of more than 20,000,000 pounds of domestic potato starch now remains unsold.

Enactment of this legislation, in addition to providing new revenue, will block an existing avenue of escape from payment of the present tariff duties on other imported starches (purchase and use of duty-free tapioca and sago in place of dutiable potato, wheat, and rice starches), will give domestic agriculture its rightful opportunity to market its own wheat, rice, corn, potatoes, and sweetpotatoes for domestic starch manufacture at a fair American price, and will stimulate business in the starch industries and in the fuel,

equipment, transportation, and labor activities connected with their operations.

Relief from the present situation has been requested by national farm groups, potato growers, rice producers, and at least one corn State legislature. The National Agricultural Council, the National Grange, the National Farm Bureau Federation, the Rice Millers Association, the Potato Program Development Committee of the United States, and the Illinois State Legislature are among those on record in favor of this legislation.

Senator KING. Are you ready for the question?

Senator CLARK. I would like to say this, that if we going to turn this bill into a tariff bill, there are a multitude of rates that I think are altogether too high in the tariff bill, and we ought to start in and hold hearings on a real tariff measure and bring in a measure designed as far as possible by independent action of the United States, outside of the reciprocal-trade agreements, working out a competitive tariff situation.

I object to the amendment proposed by the Senator from Kansas for the same reasons that I assigned the other day, and to the amendment proposed by the Senator from North Carolina, for this additional reason, that this matter urged in favor of the amendment of the Senator from North Carolina, that there was an excise tax included on oils in the revenue bill 2 years ago, and it may be fairly urged, as Senator Bailey did the other day, that his proposed amendment is to close loopholes in that measure which the Senate and the Congress adopted 2 years ago. The measure of the Senator from Kansas simply is to open up the gate to a whole tariff revision, and certainly if we are going to reduce the tariff, if that is what that amounts to, I think that this bill ought to be stopped as a revenue measure and we ought to hold comprehensive hearings on a complete revision of the whole tariff schedule. Therefore, I am very much opposed to the amendment of the Senator from Kansas.

Senator KING. Those favoring the amendment will say "aye"; contrary, "no."

The amendment is rejected.

Are there any other amendments?

Senator GERRY. I would like to present a matter just to be referred to the staff of the Joint Committee, and that is in regard ot the estate matter that I brought out, and I would like the committee to study it and see what they can recommend.

Senator KING. It will be referred to the committee. It may be well to have it put in concrete form.

Senator CLARK. I would like to bring up a question for the purpose of getting some information from Mr. Parker; a matter in which I have no great personal interest, except that it was presented to me and it seemed to me to show a condition of hardship which may be widespread throughout the United States.

I had a case presented to me the other day of a man who had been divorced from his first wife for a great many years and had been paying to her an alimony of some $30,000 a year, which was not burdensome to him before this very heavy tax system came along but which, with the imposition of tremendous taxes on personal income, have gotten to be very burdensome. It seems that under the present law, although this wife—and, as I say, the case is not impor-

tant unless it should happen to be more or less widespread—under the present law this wife is getting an alimony of $30,000 a year, and she does not pay anything at all.

Senator KING. Why?

Senator WALSH. Because it is paid at the source.

Senator CLARK. I would like to ask Mr. Parker if he has any information on the subject of how much difference in revenue it would amount to to allow a credit of any set amount—say 8 or 10 or 12 or 15 percent—on the man that pays the alimony, and impose the normal tax on the person who receives it.

Mr. PARKER. Do you mean the whole tax?

Senator CLARK. Yes; I mean the whole tax.

Mr. PARKER. With that limitation, say 15 percent, I do not think it would cost very much money. It might in one or two cases cost you something, but I could not think it would be excessive with that limitation.

Senator CLARK. I have no particular interest in the matter, but it does seem to me that that is a case where a taxpayer would have a just complaint.

Senator WALSH. You would want this $30,000 deducted from the man's net income as a legitimate deduction?

Senator CLARK. Up to a certain amount. I do not wish to open up a matter of agreement between a man and his wife if divorced. But, on the other hand, that does seem to me to be a legitimate complaint on the part of a taxpayer.

Mr. PARKER. In some instances, under this rule, we might even get more money than we do now, as I understand it. For instance, suppose a man has $200,000 income and he has to pay $100,000 alimony. At present he pays a tax on the whole $200,000. Under the rule contemplated he would be permitted, even with the highest limit you suggest of 15 percent, he would be entitled to deduct 15 percent of the $200,000, or $30,000. So he would pay a tax on $170,000. That would probably cost us in tax about $15,000 less from the man.

Now, if we tax the wife on the $100,000, as I understand it, the full amount, and she would pay a tax of $30,000, roughly, so that in that particular case we would pick up $15,000 tax. Of course, in other taxes we would lose a little, but I cannot see that the result would be very great in revenue.

Senator CLARK. I know you have a lot of estimate to make, and that sort of thing, but could you by tomorrow make up some sort of a little study on what that provision might mean?

Mr. PARKER. I do not believe the records are going to be sufficient.

Senator CLARK. I understand you have no definite data on which to figure it, but I would like to have some typical cases on which you might figure.

Mr. PARKER. I will make a guess on it by assuming various amounts of income, and see what we would lose and what we would gain on the average, for the Government.

Senator CLARK. That is all that I would like to have. I am not at all committed to the proposition, but it may be very suggestive to me as being a fair case in which the Government could increase its revenue.

Mr. PARKER. I have always thought that a woman getting alimony should pay a tax. Is there any constitutional question on that, Mr. Beamon?

Mr. BEAMAN. I think there is. It may be doubtful what the answer to it is, but I think the question is there.

Senator KING. Is there anything else?

Mr. PARKER. We have a few points that we have some suggestions to make on.

Senator KING. Are there any other amendments by members?

Senator LA FOLLETTE. Yes, certainly; but I did not assume that the committee was going to go into the matter of additional revenue this afternoon. I am ready to go ahead at any time.

Senator KING. We will omit that. Senator Guffey, have you any amendment?

Senator GUFFEY. I have some when Senator Bailey's comes up.

Senator CLARK. I was called out of the committee this morning before final adjournment. Was anything done about the amendment to the Lonergan amendment that was put on by Senator Couzens the other day? If there was not, I do not desire to take up the matter in the absence of Senator Lonergan and Senator Couzens, but I simply desire to reserve the right to do so.

Senator BARKLEY. There was nothing done about it this morning.

Mr. PARKER. There are several minor points here on questions of policy that we need a decision on before the draft of the act will be completed.

You will remember that the other day the committee decided that a company in receivership or bankruptcy should pay the 18-percent flat tax but should be relieved from the 7-percent undistributed profits tax. In discussing that matter it has been pointed out that receiverships may be brought about in some States in the case of solvent corporations through some dispute between stockholders or holders of minority interests when the corporation is perfectly solvent and able to pay taxes and with a large surplus.

Senator KING. Still doing business and making profits?

Mr. PARKER. Yes.

Senator CLARK. I was in a case which is pending out in Missouri now where two partnership interests, each owning 50 percent of the stock, and they cannot agree on the policy. And the only thing to do is to throw them into receivership. It is a very profitable business.

Mr. PARKER. May I ask the Senator, in that case, because it has troubled me somewhat—could the receiver declare dividends?

Senator CLARK. I do not see how they could. Any distribution would have to be under the order of the court.

Mr. PARKER. This was a suggestion, but the suggestion we make would not take care of that particular case. We were going to suggest that as to the tax, as to receiverships, which, if they had taken place before the enactment of this act, be given 18 percent, but in the case of receiverships or bankruptcies after the date of the enactment of this act, we will apply the 7-percent tax.

Senator KING. Whether they are solvent or not?

Mr. PARKER. Unless those receiverships or bankruptcy come under the Bankruptcy Act. When they come under the Bankruptcy Act, they are insolvent.

Mr. KENT. The Bankruptcy Act, of course, includes 77(b), which is applicable in cases where there is no insolvency in the strict sense, but merely a shortage of liquid working capital, where they have to reorganize in order to get the ready money that they need.

Senator KING. Is it your suggestion that the 7-percent tax be imposed upon solvent corporations that come under the Bankruptcy Act?

Senator CLARK. What would be the situation in which a concern was in bankruptcy under section 77(b) of the Bankruptcy Act, in which the distribution of dividends would not be a fraud upon creditors. That is the only way they are in court as being bankrupt, and for a bankrupt concern to distribute dividends to stockholders seems to me to be a fraud on its face, on creditors.

Senator BAILEY. Is there a tax on bankrupt estates?

Senator CLARK. I do not see how they can distribute dividends to stockholders.

Mr. BEAMAN. Mr. Parker's proposition takes care of that. He said any corporation now in receivership from the date of the enactment of this act gets the 18-percent rate. But in the future, any corporation going into receivership should be exempt from the 7-percent tax only if it has gone in through the Bankruptcy Act, including 77(b), when it is in there under 77(b), then it does not have to pay its dividends. It is not subject to the 7-percent tax.

If, however, in the future it goes into receivership in the State court, then it has to pay 7-percent tax if it does not distribute.

The effect of that is that a corporation that wishes to get out of the 7 percent, has to go through 77(b) or bankruptcy rather than go through receivership in a State court.

It is a quick and rough method to get us out of the trouble we are in. If the committee does not wish to do that, tell us something else to do.

Senator BAILEY. Do I take it that if an estate in receivership makes profits and does not distribute them, notwithstanding it is insolvent, it will have to pay 18 percent plus 7 percent?

Mr. BEAMAN. If it goes in in that.

Senator BAILEY. That is monstrous.

Senator WALSH. Do I understand if two corporations equally insolvent, one of which chooses to apply for receivership in the State court and liquidate, and the other chooses to go into the bankruptcy court under the bankruptcy law, in that case they will not have to pay the 7 percent?

Senator BAILEY. It is not in contemplation that a corporation in receivership is paying dividends to stockholders. It is doing very well to pay the liquidating dividends to creditors.

Senator WALSH. Why should there be any distinction made in the tax between the company that chooses to liquidate through insolvency proceedings in the United States court, and a company that chooses, which is the less expensive for all parties concerned, to go into the State court and liquidate? Why should there be a distinction in taxation?

Senator BAILEY. I do not know.

Senator WALSH. That is what this proposition proposes to do.

Senator CLARK. We do not want to put the premium on concerns running into receivership to evade taxes.

Mr. KENT. You have a very definite safeguard under the bankruptcy act, because there are in general only two situations in which a corporation can be placed in receivership under that act. One is where it is a bankruptcy, an actual bankruptcy in the strict sense; its liabilities are more than its assets, and the purpose of the bankruptcy is to liquidate and distribute the assets to the creditors.

The other is where the purpose of the receivership proceedings is to reorganize the corporation under the 77 (b) amendment. Those amendments are being used by a lot of corporations that are not insolvent in the bankruptcy sense.

Senator BAILEY. Why not draw this distinction between the corporations in receivership or bankruptcy making profits for the stockholders, and a corporation in receivership or bankruptcy simply making profits for the benefit of creditors? Why should you tax profits that are just for the benefit of creditors? That is not what this bill is for. Why not try it that way, and then you will have a principle to follow?

Senator CLARK. I think a judge that would permit dividends to be paid to stockholders, or as they might then be, the holders of a beneficial interest, ought to be impeached, and I do not think we should have a right to come along and levy a tax on a basis of trying to have receivers do something which is immoral for them to do.

Senator BAILEY. We should not tax profits available to creditors.

Senator WALSH. What they had in mind was receiverships in the State courts, where it was found a corporation was not bankrupt. There are cases where the petition is filed where the corporation is not bankrupt, and that is the case where you want to tax?

Senator KING. Take the case that Senator Clark mentioned, of the company making money and the creditors get the benefit of any declarations of dividends, then the dividends should be taxed.

Senator CLARK. It is all right to levy a tax like that, but I was just afraid Mr. Parker had made the situation too broad; in other words, we were trying to apply the taxing power to a situation where the payment of dividends to stockholders would be a fraud on the creditors.

Senator WALSH. Why can you not reconstruct your amendment along the lines proposed by Senator Bailey?

Senator BAILEY. Put the 7-percent penalty tax on any profits made by the corporation in bankruptcy or receivership that are available as dividends to stockholders, but any othe profits that are simply by way of increasing the estate for the benefit of creditors, there is no penalty tax and there should not be. You are trying to press out into the hands of stockholders money that was never intended to be put into their hands. It was intended to be put into the hands of creditors.

Senator KING. If it was put into the hands of creditors, they would have to pay the taxes. I think that that is the proper solution of this. What do you think of that?

Mr. PARKER. I think if that is to be the policy, I do not know whether we can state that——

Senator KING. Can you, Mr. Beaman?

Mr. BEAMAN. I do not see how we can do it offhand; we will try.

Senator BAILEY. If these gentlemen cannot draw that amendment, I will be glad to draw it.

Senator CLARK. I do not think anybody on this committee or anybody else can take the position that we should have the right to try to make receivers pay money to stockholders that belongs to creditors.

Senator KING. That matter is disposed of. Is there anything else?

Mr. PARKER. One other thing in connection with receiverships. Receivership may commence in the middle of the year and may terminate in the middle of the year, and it is a very difficult proposition to require a short period of return they are in receivership and then when they are not in receivership. So we are recommending that any year in which the receivership starts, they are not subject to the 7 percent for any portion of the year, and in the year in which it terminates they are not under the 7-percent tax for any portion of the year. Of course, that gives them a break, but it seems to me reasonable that in respect to the period just before they go into bankruptcy they certainly must have been going downhill, and there is no special reason for imposing the 7-percent tax on that portion of the year when they get out of receivership, we will say, in August, and I think we can apply it and give them the 4 or 5 months before they try to put the 7-percent tax on them. It is a very difficult proposition to try to have these portions of one year, one taxed on the one plan and one taxed on the other plan.

Senator KING. What do you say to this suggestion of Mr. Parker's? All in favor will say aye, contrary no.

The suggestion is adopted.

Mr. PARKER. We gave a $1,000 exemption in the case of corporations whose net income is $15,000 or less. We have in certain cases a return for a period of less than 12 months; for instance, a corporation may change from the calendar-year basis to the fiscal-year basis, and some cases like that, where we have a return for less than an annual period.

We suggest, in order to get rid of the difficulty of proration, et cetera, that in these short periods, we do not allow the $100,000 exemption.

In that connection, though, I would point out that that does not penalize the corporation that starts in business. If you start in business in August and you are on a calendar-year basis and file a return, really have been in business from August 1 to December 31, the courts have held that that is a return for the full year, so those new corporations that get the $1,000 exemption; but if they want to shift over from one basis to the other, I do not think they should get the $1,000 exemption.

Senator KING. Is there any objection to that suggestion? Hearing none, it is approved.

Senator BAILEY. I have drafted a proposed amendment as follows [reading]:

The 7-percent tax provided for herein shall not apply to nor be imposed upon corporations who are in receivership or bankruptcy, with respect to the profits available only to creditors, but shall apply to any profits available to stockholders after payment of the same in full to creditors.

I will offer that as a base to work on.

Senator KING. It will be accepted and referred to our experts as a guide in their peregrinations.

Mr. PARKER. The bill provides for consolidated returns in the case of railroad and railway companies. Where we have a number of corporations in a group filing one return, the question arises, if you have got five corporations, whether they should get the $5,000 exemption in case the total income is less than $20,000, or whether they should get less than $1,000. We recommend in the case of a consolidated return, where the net income, of course, is less than $15,000, then they only get one $1,000 exemption.

Senator KING. Is that approved? All in favor will signify by saying aye; contrary nay.

The suggestion is approved.

Mr. PARKER. You will recall that we levied certain taxes here on foreign corporations and nonresident aliens, and that we collect that tax in many cases by withholding at the source. This bill is retroactive to the 1st of January 1936. Of course, withholding under this bill cannot be retroactive. The first date we could get would be to withhold at the date of the enactment of the act.

It is suggested, however, that there should be at least some few days for people to inform themselves of their duties as withholding agents so they can familiarize themselves with the law.

Senator KING. Do you want 30 days?

Mr. PARKER. I would suggest not less than 10 days. You can go a little more or less.

Senator GERRY. We should give them 30 days in a case like that.

Mr. BEAMAN. The only thing in making it as long as 30 days is that this bill makes certain changes in the law, and they can shoot those dividends out during those 30 days.

Senator CLARK. It is getting close to the normal dividend times, too.

Mr. PARKER. I suggest 10 days.

Senator KING. If there is no objection, 10 days will be approved. Hearing none, it is approved.

Mr. PARKER. There is a provision that we were going to suggest on dividends out of current earnings. Under existing law, if a corporation has current earnings in a taxable year but has a deficit at the beginning of that year more than sufficient to absorb those earnings, all the profits, that if a dividend is declared, it is not a dividend within the contemplation of the act. It is a distribution of capital, and if we do not do something about it, the corporation won't get its dividend-paid credit, and the stockholder will pick that up tax-free from income tax, and reduce the basis of his stock.

We think on account of the construction of this act, that, being a corporation and finding itself in shape so that it can declare this dividend out of its annual earnings, it ought to get credit for it and ought not to be subjected to a 7-percent tax when it has actually distributed the current earnings.

Vice versa, we think the stockholder should pick that up in his income. And I pointed out in that connection that a deficit may appear under the income-tax rules which may be entirely different from a deficit as shown on the books. It is perfectly possible to have a deficit under our income-tax computations and have a surplus

as far as the State laws would be concerned, which might restrict the company from declaring out a dividend. That is, many companies actually can declare a dividend in spite of the fact that they have an income-tax deficit, and to penalize them and say that they have got to pay this 7 percent, whether you declare a dividend or not, seems to us very hard. On the other hand, we would lose no money by that. We want to say that where current annual earnings are distributed to the stockholders, that should be considered a dividend which will give the corporation the deduction for that dividend in respect to the 7-percent tax, and the stockholder will pick that dividend up and be taxed at the normal rate of 4 percent on it. I think it is an equitable proposition.

Senator KING. What shall be done with it? Without objection, the suggestion made by Mr. Parker is approved, and he is instructed to draft the necessary amendment.

Senator BAILEY. I want to move, for the purpose of having it thought over, that instead of undertaking to raise any taxes in addition to those in contemplation upon the plans we have here, assuming that to be $642,000,000, that we authorize the President to reduce the expenditures for the tax period to which this applies by a sufficient sum to equal the $803,000,000 that we expect to raise.

Senator WALSH. Is that to be incorporated in the bill that we report?

Senator BAILEY. Put it in the bill.

Senator GEORGE. You mean from any appropriation?

Senator BAILEY. Let him pick out any that he pleases.

Senator BARKLEY. I did not hear the motion, but I have heard enough to gather its import. We have already appropriated money for the fiscal year 1937. It has been done in all of the appropriation bills. The only thing left is the deficiency bill, which is now in the committee and will soon be out here. To authorize the President, after having appropriated this money and just finished appropriating it, to delegate to him the power to cut wherever he wants to cut or wherever he feels like cutting, simply because we cannot find that much revenue in the United States, it seems to me unthinkable.

Senator GEORGE. I think we should think the matter over.

Senator KING. If there is no objection, we will postpone consideration of Senator Bailey's suggestion.

Senator BAILEY. I made it as a suggestion, but I made it in good faith after a good deal of worry as to what we should do. I think it is the best thing to do. And it will notify the American people, instead of appropriating and taxing, that we are beginning to reduce appropriations and are not going on with the taxing business; but it will just give them the greatest heart that you ever saw at the time they need it.

Senator BARKLEY. As far as I am concerned, if there is any way of reducing it enough to obviate the necessity of passing this bill at all, I would be glad to do it.

Senator BAILEY. Let him reduce $160,000,000 from the money we appropriated. The President himself wished $500,000,000 cut off on March 8, 1938. We were going to do it, and I will give him credit for saying that he had not been in office 4 days before he sent the message down here. I remember all about that and why it was not done. That is where we lost the battle for economy in this country. I would

like to start back. We are appropriating millions and billions, and it is a simple proposition to save $160,000,000, but it is a very hard one to collect that amount.

Senator KING. I regard it as very unfortunate to have a deficit of $6,000,000,000 with all of these lavish expenditures we are making.

Senator BARKLEY. This motion, if it is carried, means that you reduce the amount which would be available for relief by whatever amount you authorize him to reduce from the expenses. That is what it amounts to. It may be that that is all right and ought to be done, but we certainly ought to know what we are doing.

Senator KING. What is the next matter?

Mr. PARKER. The chairman has requested several times the consideration of section 102, which deals with the avoidance of surtaxes by corporations, to see whether or not we could strengthen that section.

The general plan suggested was to do away with the necessity for proving a purpose to evade surtaxes and to make section 102 depend merely on the reasonableness of the accumulation. We talked over that a long while, and we are unable to get any definition of "reasonableness"; and if we leave "reasonableness" alone in there, we are very much afraid that the Commissioner will find it is his duty to make an exhaustive investigation of every corporation's business and find out what the needs of that business are.

It is very obvious, perfectly obvious, that the general run of internal-revenue agents will not be able to tell the reasonable needs of the various and complex industries in this country. So what we have suggested, I think it is fair to state, is not a very severe proposition, but one which will, we think—which may have a very good psychological effect, because it is reliably reported that many corporations fear the imposition of section 102 under existing law, and the changes which are made in it will make them more apprehensive.

In the bill, section 102 begins on page 78, and the matter in italics is the House bill, which, of course, will be entirely stricken out, because the structure of the House bill was supposed to do away, in a great majority of cases, with section 102.

So on page 80—in fact, we go back to the existing law as shown there in roman type. The first change would be under section (c) on page 81. The definition of "adjusted net income" will be stricken out, and we are proposing a definition as follows: We have changed the term "adjusted net income", because we used that in other parts of the bill, and we call it "special adjusted net income"; and the term "special adjusted net income" means the net income minus the sum of first taxes, Federal income and war-profits and excess-profits taxes paid or accrued during the taxable year, to the extent not allowed as a deduction in section 23, but not including the tax imposed by this section or the corresponding section of prior income-tax law.

Then there is a minor deduction here for bank affiliates; credit that we gave for these bank holding companies that are unable to declare out their dividends.

We propose a deduction for contribution of gifts not otherwise allowed as a deduction to or for the use of donees described in section 23 (o). Those are strictly charitable gifts, educational organizations, et cetera.

Senator WALSH. Religious?

Mr. PARKER. Religious also. Not gifts to individuals.

Finally, a fourth deduction, losses from the sales or exchanges of capital assets which are disallowed as a deduction by section 117 (d).

Of course, we have to keep in mind all the time that here we have a 25- and 55-percent tax graduated, which is going to be imposed on top of your 18-percent tax and your 7-percent tax.

Having gotten at the special adjusted net income, which, you will see, excludes from the net income all other taxes, and these losses realized on the sale of capital assets which have been disallowed, and these contributions to charitable organizations, we have got a net income there which really represents what the corporation has left, except for one thing.

Then we have a definition of the term "retained net income" which we believe is a fairer definition, and we want to make it fair.

This definition has not strengthened the law so much, but it has made a much fairer definition. Our present definition that we propose is fair.

What we have now in the law is not fair, and that makes the courts all the more stringent in interpreting it.

Now, here is a thing which we think will have a considerable phychological effect on the taxpayers. This subsection will be headed "Statement of the reasons for accumulation." It provides that every corporation subject to taxation under this title other than personal holding companies as defined in section 351—we take care of that separately—of the retained net income of which is more than 30 percent on the special adjusted net income, or more than $15,000, whichever is the greater, shall include in its return a statement setting forth the reasons for accumulating gains and profits.

We think if we make it mandatory in certain cases for the corporations to set forth the reasons for the accumulation that it will have a great deal of psychological effect on them.

Senator BAILEY. Are you going to get corporations to state reasons now?

Mr. PARKER. In the first place, we exempt all corporations from this requirement that make less than $15,000. We only exempt from the necessity of making any statement all corporations who declare 70 percent of their income out in dividends. It is only those corporations that keep more than 30 percent or have a net income of more than $15,000 who will have to make these statements.

Senator BAILEY. You want them to give reasons why they hold that?

Mr. PARKER. There would not be 5 percent of the corporations in this country that will have to make these statements.

Senator BAILEY. Do you want them to give a reason why they are withholding it?

Mr. PARKER. Yes.

Senator BAILEY. I think that is their business.

Senator GEORGE. If they withhold an unreasonable amount, we already have in the law that they can be taxed 50 percent.

Senator WALSH. That only applies to that section where the Commissioner can order a tax of 50 percent on all of the net income in case he finds that they have not made a satisfactory distribution?

Senator GEORGE. Yes.

Mr. PARKER. It puts a corporation on notice that they ought to have some reason for this. It may be helpful to them; it may build up a record.

On the other hand, if they keep on year after year and say, "We are putting this in stocks and bonds so that we can build a plant next year", and if they keep on doing that, we will have something on which to go to court and say that it is unreasonable.

Senator BYRD. Do you not think that 30 percent is too low? Are you not assuming that a corporation accumulating 30 percent is doing something wrong? I am not a lawyer, but I would assume that the Government thinks that they should not retain more than 30 percent because they have to explain why they do, in the event that they do retain more than 30 percent.

Senator LA FOLLETTE. It is only that the purpose of section 102 is to prevent the accumulation of these huge amounts for the purpose of avoiding taxes. I do not think it would be subject to that construction, Senator. It would simply be that if the corporation retained more than 30 percent, that it should have a sound reason for doing so.

Senator KING. It may be regarded as a sort of a presumption that if they retained more than 30 percent, that they had to make an explanation and a reason. Whether it is satisfactory or not is a matter for the Commissioner to determine. If he determines that it is unsatisfactory and attempts to collect, he runs the risk of being defeated if the court holds that it is satisfactory.

Senator BYRD. Does it not put all of the corporations under suspicion if they retain more than 30 percent?

Senator METCALF. Many corporations put that aside for the purpose of building an addition to a mill.

Mr. PARKER. Then all they have to say is that they want to build an addition to the mill. But if they go on year after year saying that they want to build it and they do not build it, that is another matter.

Senator BYRD. If they are convicted under section 102, there is a double penalty over and above the other penalty?

Mr. KENT. If I may say so, I do not believe that this will necessarily work against the interests of the taxpayer. It may save the taxpayer in a great many cases from having preliminary deficiency letters sent out against him. An agent goes out and examines their books, and he thinks they are accumulating a little too much of their corporate earnings, and he sends in a report recommending that the deficiency be assessed. Whenever a deficiency letter is sent out, then it does become necessary for the taxpayer to come in and show his reasons for accumulating these earnings, otherwise the deficiency will be sustained.

Senator LA FOLLETTE. Under existing law if the deficiency letter goes out, the corporation must furnish reasons and indicate why it is not liable for the deficiency, and here you are simply asking him to make that statement under certain circumstances before they have been served with the deficiency letter.

Senator BYRD. Will the Commissioner then say that the reasons are approved or disapproved? What I am getting at is that it does not seem to me that this should be hanging over the corpora-

tions indefinitely, that they may be proceeding against them to collect a lot of back taxes.

Senator LA FOLLETTE. There won't be any difference under those circumstances on this suggested amendment than there are under section 102 now.

Mr. KENT. The statute of limitations runs, anyhow.

Senator BYRD. But the Commissioner, under this section, has never sent letters where the retained amount was as low as 30 percent, has he?

Mr. PARKER. Oh, yes, they have.

Senator BYRD. A corporation may feel that these additional taxes may be assessed against them in future years. If it could be settled, it would be all right.

Mr. PARKER. Well, there has been a very large past accumulation of surplus, and letters have been sent out with 10 percent or 15 percent.

Senator KING. Are you ready for voting on this suggestion, gentlemen?

Senator BAILEY. I do not understand what it is. You are going to require the corporation to give us reasons?

Senator KING. If he retains more than 30 percent after all of these generous deductions.

Senator BAILEY. And pays the tax?

Senator KING. And pays its tax.

Senator BAILEY. I think when the Government collects the money and that man pays the tax, he might be spared the necessity of anything further.

Senator LA FOLLETTE. Under existing law, under section 102, if the Commissioner thinks, or it is recommended to the Commissioner by an agent that he send out a deficiency letter, then it is up to the corporation to come in and fully justify. They are told to come in. Here, all that you are asking them to do is to make the statement under certain circumstances prior to the issuance of a deficiency letter.

Senator BARKLEY. Is it not likely to be true that a statement filed with the return is more calculated to allay any suspicion on the part of the Commissioner, than to cause any trouble to the corporation?

Senator BAILEY. Is it compelling him to give his reasons, or is it up to him?

Senator BARKLEY. He must accompany his return with the statement. A large corporation with large earnings that retained more than 30 percent, the mere retention of it might create a suspicion on the part of the Commissioner that something was wrong, but if he has a reason there which he has filed, that might clear it up in itself. I think it is very likely that this will in many cases render improbable the sending of these deficiency letters.

Senator KING. Mr. Parker will make a brief explanation, because two Senators have just come into the conference.

Mr. PARKER. We have been talking about strengthening section 102 which deals with accumulations by corporations, which result in our getting no taxes from the stockholders' surtaxes. The part that is important begins on page 80, because the italics are all stricken out of the House bill.

The main suggestion is this, that we think it will have a good psychological effect and bring it to the attention of all of these corporations which are accumulating a large amount, if we require a certain statement to be made with the return, and it is proposed only to require a statement which I will describe later, in the case of corporations whose special adjusted net income, which is defined, exceeds $15,000, which the retained net income exceeds 30 percent of the net income; in other words, all of the corporations, and that will be about 95 percent of them—won't have to make any statement, because those that make less than $15,000, there is no statement required, and those that distribute 70 percent or more in dividends, won't have to make any statement. The only statement we are asking them to make is to set forth reasons, with their return, for the accumulation of their gains and profits.

Senator BYRD. How much would the penalty be? You have already taxed them 7 percent.

Mr. PARKER. The penalty is the same as the existing law.

Senator BYRD. What is it?

Mr. PARKER. The penalty is 20 percent of the retained net income below $100,000, and 35 percent of the amount of the retained net income in excess of $100,000.

Senator BYRD. That is in addition to the 7 percent?

Mr. PARKER. That is right, but the retained net income has got pretty nearly everything off of it. We have taken the net income and reduced it by all of the taxes paid, the income taxes, and undistributed-profits taxes, all of the taxes come off. We have taken off the losses on the sales of securities, which is disallowed in the ordinary income tax. We allow the contributions and gifts to charitable organizations which exceed 5 percent, which is the present limitation. Then, finally, to get the retained net income, we deduct all the dividends paid, so that we have reduced that amount to which the penalty tax can apply to a very fair minimum.

Senator COUZENS. What do you do with the statement that you get from them?

Mr. PARKER. That builds up our record in the Bureau so that we have some record. If a corporation goes on year after year and makes fictitious reasons, we will have some kind of a reason to try to apply this matter in the court.

Senator BYRD. How far back can the Commissioner go in giving them notice?

Mr. PARKER. This is not retroactive.

Senator BYRD. I understand. Suppose in the time allowed——

Senator COUZENS. I think the statute of limitations—how long is it now?

Mr. PARKER. Three years.

Senator COUZENS. I believe the statute of limitations should be 5 years. If they repeat for several years these promises of development or some other purposes which are not carried out, and that probably will be many of the promises that these people will make, the Commissioner should have a right to go back 5 years to determine whether or not they have substantially carried out the promises which they have made in that connection, and I think in those cases the statute of limitations should be increased to 5 years. They will jockey along 2 or 3 years and then the statute will have run.

Senator BAILEY. Does not the language as written predicate that the taxpayer will have to state his reasons in the event that the Commissioner should find there was some ground for suspicion under the reasonable needs as called for here? That means that it is a case which he must rebut by evidence on his part. Why not let him state his reasons?

Senator KING. This supplements existing law by requiring that he shall file this statement with his return. The present law simply means that if the Commissioner is dissatisfied with the return, after he has made it, he may give him a deficiency notice, and then he will have to come in and make the showing.

Senator BAILEY. That predicates that he shall state his reasons upon a prima-facie case being stated by the Commissioner.

Mr. PARKER. The thought that I had in the matter was the fact that the corporation having to set forth briefly the reason for the accumulation of these profits, will put him on notice that the Commissioner intended to impose this section vigorously or to put him on notice that Congress wanted him to enforce this section, and it will have a considerable moral effect, because when the corporation made up its return, he would say, "Why do they want the reason?" And he will say, "Because he is going to enforce them if we do not have an adequate reason."

Senator LA FOLLETTE. As I said before, I do not have much faith in your ability to make section 102 work, but certainly you are up against this dilemma, you are either going to have to make section 102 work or you are going to have eventually to come to the President's recommendation so far as attempting to establish equity under the tax system, and it seems to me if you require them—I think the point that Senator Couzens made if you require them to build up their own record for several consecutive years as to why these accumulations are being made, and then they do not build the factory they say they have been setting it aside for, or they do not improve their plant, or do whatever they have said, you will have some record upon which to go into court, and the position of the Commissioner will be to that extent strengthened.

Mr. PARKER. On the other hand, if they are an honest taxpayer and have set forth adequate reasons, it will help them.

Senator LA FOLLETTE. Because he establishes a record of performance.

Mr. PARKER. Otherwise, he may have no record when the Commissioner tries to assess a tax 3 years afterward.

Senator BYRD. I have not seen it as you have proposed it. I would like to read it.

Mr. PARKER. Here it is [handing paper to Senator Byrd].

Senator BYRD. Is this new from the House bill?

Mr. PARKER. Yes.

Senator KING. Is there any objection to taking a vote on this?

Mr. PARKER. May I——

Senator BYRD. I have no objection. I think it is one of the most important parts of the bill, and I think we should wait on it to vote until the morning. I have not read that section carefully.

Senator KING. If there is no objection, we will take a vote on that the first thing in the morning.

Senator BYRD. And I think each member of the committee should be furnished with a copy of it.

Senator KING. Please see that they get it, Mr. Parker. Is there anything else?

Mr. PARKER. I think that is all.

Senator KING. Mr. Beaman, have you anything further to suggest?

Mr. BEAMAN. No.

Senator KING. Mr. Kent?

Mr. KENT. No.

Senator KING. The secretary has the individual amendments offered by various Senators.

Senator Steiwer came before the committee and offered an amendment, which is as follows. For your information L will read it [reading]:

For the purposes of this paragraph, lumber is defined as the product of the saw and planning mill not further manufactured than by sawing, resawing, and passing lengthwise through a standard planing machine, crosscut to length and matched. The board measurement of dressed lumber shall be based upon the corresponding nominal dimensions of rough green lumber. Lumber less than one inch in thickness shall be measured as one inch.

Senator KING. Those in favor of the amendment of the Senator from Oregon will signify by saying "aye"; those opposed will say "no"; the "noes" have it. The amendment is rejected.

Mr. PARKER. This next amendment has been explained before. It is pointed out that our law permits a man to go to the Philippines and conduct a grocery store, we will say, as an individual, and he is exempted from our income tax. He pays a Philippine tax insofar as the income derived from that store is concerned, even though he is a citizen of the United States. If he incorporates that store——

Senator KING. Under the Philippine law or under our law?

Mr. PARKER. If he incorporates under their law he is subject to be taxed on the dividends he derives, although he still remains in active conduct of the business. Mr. Haussermann's brief points out that that situation puts an American citizen conducting business in a corporate form in the Philippines at a disadvantage with the English, German, and French, which countries do not attempt to collect their income taxes in such a case.

Senator KING. Is that not analogous to the China Trading Act and its benefits?

Mr. PARKER. The China Trade Act is entirely different. We gave them a very considerable benefit, it is true.

Senator LA FOLLETTE. As I understand it, that was one of the matters that we asked to have looked into, and they have been so busy that they have not looked into it.

Senator KING. Have you looked into it?

Mr. PARKER. No.

Senator KING. It will be passed on tomorrow morning.

The CLERK. Senator Bone offered an amendment and also appeared before the committee in respect to red-cedar shingles under the trade agreement between this country and Canada. Senator Harrison suggested that he offer it on the floor and have it referred to the committee, and he would ask the State Department for a report on it. The State Department wrote Senator Harrison that the matter had been discussed with Senator Bone, and as a result of the

discussion they were inquiring into the prospects of an agreement between the interests in this country and in Canada in the hope that it would make unnecessary any legislation.

(Senator Bone's amendment is as follows:)

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

AMENDMENT Intended to be proposed by Mr. Bone to the bill (H. R. 12395) to provide revenue, equalize taxation, and for other purposes, viz: At the proper place insert the following:

Whenever any organization or association representing the producers of more than 75 per centum of the red cedar shingles produced in the United States during the previous half-year period shall request the President to limit the importation of red cedar shingles from Canada under paragraph 1760 of the reciprocal trade agreement entered into with the Dominion of Canada under date of November 15, 1935, and the President finds from available statistics that the total quantity of red cedar shingles produced in the Dominion of Canada which is entered, or withdrawn from warehouse, for consumption in the United States, during any given half of any calendar year exceeds or will exceed 25 per centum of the combined total of the shipments of red cedar shingles by producers in the United States and the imports during the preceding half year, the President shall issue an order limiting for the six months immediately following the half of the calendar year in which said excess occurred, the quantity of red cedar shingles to be imported from Canada to 25 per centum of the combined total of the shipments and imports of red cedar shingles for such preceding half calendar year. The President shall issue a new order for each half of the calendar year thereafter during the continuation of the operation of the reciprocal trade agreement entered into with the Dominion of Canada, under date of November 15, 1935, with the same limitations as hereinbefore set forth.

Senator CLARK. I move it be indefinitely postponed.

Senator LA FOLLETTE. I do not think that should be done. The fact of the matter is, if I recollect the testimony, Senator Bone stated that it was pretty generally conceded that these Canadian manufacturers have been very unreasonable in their attitude on this question, and I do not think it should be foreclosed by action on the part of this committee in case the State Department finds it is in agreement with their contention.

Senator CLARK. The State Department has not any authority at the present time to modify a trade agreement, as I understand it. As I understand it, this proposition puts into a revenue bill a provision for changing an agreement heretofore entered into. If you open up that field, you will have everybody coming in to change provisions in the agreements.

Senator KING. Suppose we let it go over until tomorrow.

Senator CLARK. I am agreeable, but if you open up the subject of modifying these trade agreements, we will have very, very little revenue bill and we will be here all summer.

Senator KING. If there is no objection, the committee stands at recess until 11 o'clock tomorrow morning.

(Whereupon, at 5 p. m., the committee took a recess until tomorrow, Tuesday, May 26, 1936, at 11 a. m.)