SURVEY OF EXPERIENCES IN PROFIT SHARING AND POSSIBILITIES OF INCENTIVE TAXATION

HEARINGS

BEFORE A

SUBCOMMITTEE OF THE COMMITTEE ON FINANCE UNITED STATES SENATE

SEVENTY-FIFTH CONGRESS

THIRD SESSION

PURSUANT TO

S. Res. 215

PROVIDING FOR AN INVESTIGATION OF EXISTING PROFIT-SHARING SYSTEMS BETWEEN EMPLOYERS AND EMPLOYEES IN THE UNITED STATES

NOVEMBER 21 TO DECEMBER 14, 1938

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SURVEY OF EXPERIENCES IN PROFIT SHARING AND POSSIBILITIES OF INCENTIVE TAXATION

MONDAY, NOVEMBER 21, 1938

UNITED STATES SENATE,
SUBCOMMITEEE OF THE COMMITTEE ON FINANCE,
Washington, D. C.

The subcommittee met, pursuant to call, at 10 a. m. in room 312, Senate Office Building, Senator Clyde L. Herring (chairman) presiding.

Present: Senators Clyde L. Herring and Arthur H. Vandenberg.

Also present: Senator William H. King.

Senator HERRING. The committee will be in order. I think perhaps, first of all, we should introduce into the record the original resolution, and that will be followed by the statement which Mr. Despain will make.

(The resolution referred to is as follows:)

[S. Res. 215, 75th Cong., 3d sess.]

RESOLUTION

Whereas the maintenance of the profit system is essential to the preservation of the competitive capitalistic system under which the United States has attained the largest measure of general economic welfare enjoyed by any people in the world; and

Whereas the exploration of all available means for extending the direct benefits of the profit system to the largest possible number of citizens is highly desirable and important: Therefore be it

Resolved, That the Senate Finance Committee, or any subcommittee thereof, is authorized and directed to make a complete study of and report to the Senate upon all existing profit sharing systems, between employers and employees, now operative in the United States with a special view (a) to the preparation of an authentic record of experience which may be consulted by employers who are interested in voluntarily establishing profit-sharing plans; (b) to the consideration of what advisable contribution, if any, may be made to the encouragement of profit sharing by the Federal Government, including the grant of compensatory tax exemptions and tax rewards when profit sharing is voluntarily established; (c) to the consideration of any other recommendations which may prove desirable in pursuit of these objectives; and be it further

Resolved, That for the purposes of this resolution the committee, or any duly authorized subcommittee thereof, is authorized to hold hearings; to sit and act at such times and places during the sessions, recesses, and adjourned periods of the Senate during the Seventy-fifth and succeeding Congresses; to employ such experts and clerical, stenographic, and other assistants; to require by subpena or otherwise the attendance of such witnesses and the production of such books, papers, and documents; to administer such oaths; and to take such testimony and to make such expenditures as it deems advisable. The cost of stenographic services to report such hearings shall not be in excess of 25 cents per one hundred words. The expense of the committee, or any duly authorized subcommittee, which shall not exceed $30,000, shall be paid from the contingent fund of the Senate upon vouchers approved by the chairman of the committee, or any duly authorized subcommittee thereof.

Senator HERRING. We will hear from Mr. Despain, the Director of Survey. He will make an opening statement as to an interpretation of profit sharing, a historical review of its growth in industry, and an outline of the objectives of this survey.

STATEMENT OF DONALD DESPAIN, DIRECTOR OF SURVEY, SUBCOMMITTEE OF THE COMMITTEE ON FINANCE OF THE UNITED STATES SENATE

Mr. DESPAIN. Gentlemen of the committee: In behalf of the staff which has conducted the survey of the principle of profit sharing in its application to employee-relations policies throughout American industry and business, I ask your indulgence to present the following brief review of our research in that field for the purpose of presenting a basis of understanding of the subject which is to be discussed in these hearings.

The Senate resolution which authorized this study of experiences in profit sharing was presented to the Senate with the following preamble:

> Whereas the maintenance of the profit system is essential to the preservation of the competitive capitalistic system under which the United States has attained the largest measure of general economic welfare enjoyed by any people in the world; and
>
> Whereas the exploration of all available means for extending the direct benefits of the profit system to the largest possible number of citizens is highly desirable and important.

The context of the resolution directs the committee to make—

> a complete study of all existing profit-sharing systems, between employers and employees, now operative in the United States.

Profit sharing is not a new subject. "The worker's fair share" has been a real problem ever since the world began, and has stood forth as a paramount issue since the birth of the modern industrial era.

The subcommittee, in considering the term "profit sharing" for the purpose of the present survey, was faced with a problem arising out of the fact that prior to this time the term "profit sharing" had been given varied and extremely limited definition. In fact, no two writers or students of the subject seem to agree upon the subject matter to be included in a definition of profit sharing. This conflict and lack of agreement is accentuated by different conceptions of objective and purpose.

Practically all the literature on the subject is limited by the definition set forth by the International Cooperative Congress at a meeting in Paris, France, in 1889. Their definition is as follows:

> An agreement freely entered into, by which the employees receive a share, fixed in advance, of the profits.

In the discussion of this cooperative congress, profits were further defined as being the actual net balance or gain realized by the final operations of the undertaking in relation to which the scheme exists, and the sums paid to the employees out of the profits were to be directly dependent upon the profits.

For purposes of classification of plans this definition may be practical. However, for purposes of this survey, such limitations are not desirable since our objective is not the analysis of certain plans which might fall within a definition set forth 50 years ago, but rather an analysis of the existing employer-employee relationship.

A BROADER DEFINITION OF PROFIT SHARING

The committee was, therefore, initially faced with the problem of what shall or shall not be recognized as profit sharing in this survey.

In an attempt to be logical and realistic, the problem was considered from three different approaches. A brief summary of each of these approaches is given as follows:

Approach 1: Beginning with the International Congress definition of 1889, we find from the results of our survey such plans as the one existing in Sears, Roebuck & Co. Technically, it complies with the Paris definition in that it is an agreement freely entered into by which employees receive a share, fixed in advance, of the profits. This plan specifically provides for setting aside 5 percent of the net profits of the company before taxes, in a fund to be accumulated for the purpose of providing retirement benefits upon separation from the service of the company. The 5 percent of profits as calculated is charged as an operating expense before income taxes are calculated. This plan, therefore, while technically a profit-sharing plan, is also a retirement or pension plan, and, except for the fact that the cost to the company for any given year is determined by profits rather than by the cost of specific benefits, the plan is identical with a fixed retirement plan, the costs being charged as operating expenses.

It, therefore, follows that insofar as the effects are concerned, a fixed retirement plan is as much a form of profit sharing as the Sears, Roebuck profit-sharing plan; such plans must therefore be included in our consideration of profit-sharing systems, if a satisfactory analysis is to be obtained.

Following this trend of thought, these retirement plans (whether costs are computed on profits or otherwise) also generally provide for death, disability, and other benefits. Therefore, to be consistent, any plan which provides death, disability, or separation benefits must also be included.

In analyzing the conditions of various companies, it became apparent that some, for example, provide hospital, nursing, and other medical services directly to employees in lieu of specific benefits under a formal plan. Other companies contributed sums to employee-benefit associations for the purposes indicated above. These are simply other forms of providing benefits similar to those provided under profit-sharing plans, and as such must also be considered profit-sharing.

As a result of this approach, it became apparent that any satisfactory and complete analysis of profit-sharing systems must include all employee-benefit plans to which the employer contributes any sums, or because of which the employer incurs any expenses which in the final analysis must of necessity be paid from profits.

Approach 2: From a purely accounting point of view, profits represent the income remaining after all expenses are paid. For income-tax purposes generally the costs of profit-sharing plans to employers, while determined by profits, are included as operating expenses, just as are the payments to retirement and other benefit funds. Accounting records can be used as a basis for a technical distinction between a profit-sharing plan and a fixed retirement plan, but such records cannot be used as a basis for segregating actual profit sharing from operating expenses because the existing accounting practices are inadequate.

From the point of view of fundamental economic principles, profits represent the excess of income over the market costs of land, labor, and capital. Theoretically, therefore, all payments to labor in excess of those required by the market would constitute a sharing in profits. From an accounting point of view, these excess payments are not distinguished from the market wages; and in certain instances these excess payments may be included as expenditures and in others they may appear as profits. The profit system and the individual capitalistic system are economic concepts. Analyses affecting them, therefore, must be fundamentally economic; they cannot satisfactorily be based on accounting procedures which do not recognize the economic differences.

Fundamentally, therefore, the profits which must be considered as being available for sharing with employees are not limited to those which appear as a result of accounting procedures. All payments to employees, regardless of the form in which they are allocated or distributed, which are in "addition" to the market or basic wage rate, must, therefore, be included in the concept of profit sharing and must also be included in the considerations of this committee.

Section (b) of the resolution further provides that your committee give consideration to—

what advisable contribution, if any, may be made to the encouragement of profit sharing by the Federal Government, including the grant of compensatory tax exemptions and tax rewards when profit sharing is voluntarily established.

Approach 3: In accordance with this objective, let us take the hypothetical situation wherein government was today empowered to reward, by some form of tax exemption or otherwise, those employers who, through a sharing of income or profits, improved the financial status of their employees, insured their old-age security, or otherwise contributed to employee welfare, thereby contributing to the common good. Here we find a company which, in the judgment of its management, decided it could best aid its employees by establishing a pension fund, thus insuring the old-age security of its employees. From its profits it pays an annual substantial premium for the maintenance of that pension system during the working years of the employee. On what grounds, gentlemen, could you deny to that institution the reward authorized by the Government for the voluntary creation of profit-sharing plans?

Over here we find a company which, in its desire to share its profits with its employees, decided that the best method was to distribute a cash bonus annually, the amount being dependent upon the percentage of earnings. Who, may I ask, can say that that institution is not entitled to the reward offered by government?

And so we might proceed through the varying types of employee-relations policies which have been adopted in good faith and by the desire to give employees a larger share in the fruits of their toil. In each case we face the judgment of the employer, who, by the decision of management or a joint arrangement with employees, sought to distribute, through sharing of additional compensation in any one of many forms. Unless adequate and equal consideration is given to each of the varying forms of profit sharing, discrimination will result.

In all these cases it is quite apparent that the governmental body, having the power to grant the rewards, would find it extremely difficult, if not impossible, to draw fine and technical lines of distinction between the various policies of the many institutions.

In many instances we would find a situation where employees were accepting and interpreting a certain policy of extra compensation resulting from earnings, as profit sharing, while certain writers, clinging to a narrow interpretation, would deny that such a policy involved the principle of profit sharing. Likewise certain employers insist that they are sharing profits under a form of distribution which would not be defined as profit sharing by those who insist upon narrow and technical definitions.

Who, we may ask, is to be the judge; the theoretical observer, or those actually engaged in practical operation?

Summary: In brief, the attempt to draw fine distinctions between types of employee policies and especially to segregate profit sharing within strict and narrow limits is quite similar to attempting to analyze the advantages of a medicine on the basis of whether it was administered in capsules, tablets, or liquid form. It is as difficult, and finds its parallel in the attempts which have been made to define labor. One encyclopedia refers to labor as "the term so dependent for its meaning on the circumstances in which it is used, that any scientific definition of it would lead to misunderstanding." It would appear that this phraseology would apply with equal force to any attempt at a specific or scientific definition of "profit sharing."

As practically demonstrated in hundreds of institutions throughout America, profit sharing is a modification of the wages system which removes the laborer from his status as a simple earner of fixed wages, who has no further interest in the business beyond securing the maximum regular wages, and converts him into the relationship of a partner, to a specified extent, in the profits realized by the company, thereby completely changing his attitude and position toward his employer.

We have approached this subject from the higher and broader purpose of seeking a formula for a wider application of the capitalistic economy by extending the direct benefits of the profit system to the largest possible number of citizens.

If the profit motive—that is, the lure of gain, the hope of reward—is the heart of the American plan and the base of the capitalistic system—by what logic can we insist that its rewards be restricted to some and not to all—or that its incentive power will not induce greater effort from all men as well as a few?

Both employers and employees have too often lost sight of the necessity for a unity of interest, a bond of cohesiveness, between employer and employee which is the concrete base upon which a sound, enduring, individual capitalistic economy must be built. If a profit system is to be used as a spur to production, and a regulator of distribution, the profit incentive must be made applicable to the greatest possible number of individuals within the system. The profit system must increase its membership.

Throughout the years certain individual instances have stood forth as being examples of a satisfactory solution to this problem. These cases generally were those in which some form of employee interest and responsibility has been created through a system of profit sharing in one form or other.

HISTORICAL SUMMARY OF PROFIT SHARING

The principle of profit sharing is as old as man. The principle of participation in profits was recognized in a published pronouncement in America as early as 1775.

So far as is known, the first systematic plan of profit sharing was inaugurated in 1794 by Albert Gallatin in his glass works in the State of Pennsylvania. Gallatin, who served as Secretary of the Treasury under Presidents Jefferson and Madison for 12 years, advocated profit sharing on the ground that "the democratic principle upon which this Nation was founded should not be restricted to the political processes, but should be applied to industry."

Although Gallatin's plan preceded that of Maison Leclaire, of Paris, announced in 1842, the wide publicity given the "Leclaire" plan and the long-time operation of his program has brought to Leclaire the credit of being the "Father of profit sharing." Leclaire was a Parisian house painter and decorator. Beginning to admit his workmen to participation in the profits of his business in 1842, he continued the system with improvements and modifications until his death in 1872. His financial success was spectacular and he became one of the noted "captains" of French industry. However, it was not due to his personal rise to wealth which publicized his plan, but rather the fact that his employees shared his good fortune with him, many retiring with substantial fortunes as a result of his distribution of profits. The plan of Maison Leclaire has stood as an example of a practical method of reconciling and uniting the interests of employer and employee for nearly a century.

It is recorded that the success of the "Leclaire" plan was due to the fact that Leclaire knew his craft and the men who practiced it; he knew their temptations and their difficulties; he knew their weaknesses and their impulses and he constructed his plan in such a way as to govern, control, and protect men against themselves.

Throughout France and England, many business institutions copied and installed plans wholly or in part following the pattern of Leclaire. Some failed, others succeeded and have endured through the years. Throughout the balance of Europe the record is similar. Search, trial, and experimentation to find the successful and effective formula for the establishment of the partnership relation—the unity of interest and the spirit of cooperation—has been, and is now being, carried on.

DEVELOPMENT OF INDUSTRIAL RELATIONS IN AMERICA

In America, labor relations in industry have developed with economic and social evolution, but not in equal pace. First efforts toward improving industrial relations were frankly and openly paternalistic. Nineteenth century management emerging from the period of master-and-servant labor relations conceived a paternalistic program as the remedy for former harshness of rule.

At the turn of the twentieth century the promise of a "full dinner pail" seemed to satisfy labor's demands. The concept seemed to be that labor looked no further than the job and that it worked and traveled like Napoleon's army—"on its stomach." We have come a long way from those concepts of labor relations in the past half century. Later, industrial management took up "systems and costs," "piece work" rates, and "production bonus" policies in an effort to solve labor's growing demand for a larger share in the fruits of labor's production.

Gradually there developed the philosophy that the worker cannot live financially in the present only—that consideration must be given to his future. Pension plans, annuities, wage dividends, and other varied forms of profit sharing began to appear in many institutions. Measured by the test of years of successful operation, by the record of labor satisfaction and tranquillity and by the results of morale and cooperation, of all the plans and systems attempted, "profit sharing" when properly applied so as to make the employee cognizant of his relationship, has unquestionably established itself as the most effective of all labor-relations policies for establishing labor stability and amicable relationships between employer and employee.

HISTORY OF PENSION PLANS

Historical records of employers providing pensions for employees are available since the beginning of industry. These cases, however, are generally isolated and were not the result of any definite plan.

At the beginning of the twentieth century there were probably less than a dozen formal plans in existence in the United States. The first plans were generally developed by railroads and public utilities. The first formal plan of which there is a definite record available was originated in 1874 on the Grand Trunk Railroad. By 1900 there were six plans existing in the railroad industry. The first formal public-utility pension plan was probably that of the Consolidated Gas Co. in New York which was established in 1892. The first plan established in the banking industry was in Chicago in 1899. In the manufacturing industry there are indications of two plans prior to 1900 both of which were discontinued prior to the turn of the century.

In the first 10 years of this century some 54 plans were established; during the next 10 years (1911–20) 221 plans were established; and from 1921 to 1930 some 130 plans were established. Of the approximately 420 formal plans created prior to 1930 about 400 of them were still in existence at that time, although many have been revised in structure. At the present time there are probably some six or seven hundred plans in existence, many of which, however, are plans which cover only a limited number of the employees and are not, therefore, strictly comparable to the earlier plans.

More accurate figures on the present situation will be available at the close of this survey when all of the information has been accumulated, classified, and analyzed.

PROFIT SHARING IN AMERICA

As previously stated, Albert Gallatin was the pioneer sponsor of profit sharing in America in 1794.

Horace Greeley had a profit-sharing plan in the New York Tribune and was a strong advocate of its mutual benefits. In 1869 Brewster & Co., New York, carriage builders, started a plan of sharing profits which, however, was abandoned in 1871. Pillsbury Flour Mills, of Minneapolis, Minn., established a plan in 1882. In 1886 the N. O. Nelson Co., of St. Louis, initiated direct profit sharing in the company, which continued without interruption for 49 years until the recent great depression caused temporary suspension.

In 1884 the Baltimore & Ohio Railway Co. inaugurated a "pension relief-savings" plan which has operated as a model in the railroad field for 54 years. In 1886 the Procter & Gamble Co. of Cincinnati introduced into the industrial field a profit-sharing and general employee relations program which in its 52 years of operation has probably attracted more attention and study than any other plan in American industry. Col. William Procter was the recipient of widespread criticism from his fellow industrialists for proposing and adopting the advanced and progressive philosophy involved in his new employee-relations policy. Colonel Procter again astounded the industrial world, when in August 1923 his company announced the "annual wage" system guaranteeing 48 weeks of work and 48 pay checks annually. These policies have withstood all tests as the company has grown to its present proportions with over 5,000 employees.

Gradually other companies adopted profit sharing, prominent among them being the Simplex Wire & Cable Co., of Cambridge, Mass., in 1901; Hibbard, Spencer, Bartlett & Co., of Chicago, in 1902; the R. J. Reynolds Tobacco Co., Winston-Salem, N. C., with 15,000 employees; and the Eastman Kodak Co., with some 24,000 employees, in 1912; the Edison Electric Illuminating Co., of Boston, in 1913; the California & Hawaiian Sugar Co., Crockett, Calif., in 1914; the Cleveland Twist Drill Co., Cleveland, in 1915.

Of the more significant plans inaugurated in later years, we find in 1916, the Sears, Roebuck & Co., of Chicago, having a normal employee group of over 30,000, initiated a plan under which the company pays 5 percent of its net profits which has prevailed against war periods and depressions. Even in 1931 this company paid $1,000,000 into its profit-sharing fund.

In 1918, after experimenting with nearly a dozen different forms and types of employee relations over a period of 18 years, the Joslyn Manufacturing & Supply Co. of Chicago, adopted a "profit-sharing-saving-retirement fund" plan, which, although operating with the highest degree of success for 20 years, has only recently become known to industry.

In 1919 the Endicott-Johnson Shoe Co. of Endicott, N. Y., inaugurated a broad employee relations plan of profit-sharing including a most generous medical and hospitalization program. Since its adoption this company has distributed more than $12,000,000 in profits, has never suffered from labor trouble, but on the contrary had the pleasant experience in 1937, of having 19,000 employees voluntarily sign and address a pledge of loyalty to Mr. Johnson during the wave of labor unrest in the spring of that year.

Since 1920, the General Electric Co. of Schenectady, N. Y., with 58,000 employees, has operated a plan of profit-sharing coupled with savings which recommends itself highly as an instrumentality for industrial peace and stability.

The more recent addition to the family of profit-sharing companies is the Westinghouse Electric & Manufacturing Co. of Pittsburgh, with more than 40,000 employees, which inaugurated a most distinctive and comprehensive plan in 1936.

Fairbanks Morse & Co. of Chicago, in spite of having the enviable and remarkable record of 100 years of industrial peace, adopted profit sharing in 1937.

As an illustration of the experience of one company having a satisfactory profit-sharing plan, the president and founder of that company states:

> For 20 years we had always been striving for some practical form to progressively advance the standing of employees in the corporate structure, without at the same time so weakening that structure as to endanger its progress as a whole. We tried

all kinds of temporary plans. There was much confusing talk at the time about the partnership between labor and capital but little real attempt to move in that direction. Any real partnership can only be based on the laborer first becoming a capitalist himself. We believed the common laborer, working year after year for a normal wage, with nothing but Saturday pay day to look forward to, with no consciousness of steadily bettering himself, with no consciousness of his recognized and participating relationship in the company, lost hope and energy and delivered to his employment only part of the value he was capable of delivering under happy conditions.

Senator VANDENBERG. Who is it you were just quoting?

Mr. DESPAIN. I did not give the name. That was Mr. Joslyn's analysis of the philosophy that caused him to adopt their plan.

A review of the progress made in industrial profit sharing brings forth certain significant facts. First, profit sharing for wage earners prevails about equally throughout the country between small establishments and large organizations. Second, profit sharing has been adopted and is in operation in all different types and fields of industry and business; in highly competitive as well as noncompetitive operations; in institutions with high labor cost ratios as well as low labor costs; in widely disintegrated organizations as well as closely integrated operations. The progress and experimental approach to profit sharing has been gradual and widely diversified.

When we include the many varied public relations plans which share profits directly or indirectly through various forms of plans and policies, it is estimated that between 2,000 and 3,000 companies throughout the United States are substantially sharing profits with employees in one manner or another. Coincident with the steady increase of profit-sharing plans is the dissimilarity or lack of standardized form of program or policy. This in itself, is a strong reason and powerful argument in support of a comprehensive survey and analysis of the entire field for the purpose of discovering the weaknesses which have caused failure or abandonment of plans, as well as definitely distinguishing the corrective and strengthening features of brilliantly successful plans from which the sound basic principle underlying the subject may be found.

CONFUSED IDEAS ABOUT PROFIT SHARING

Profit sharing has been the victim of both prejudice and misunderstanding. We are inclined to believe that the term "profit sharing" is in itself a great stumbling block; that if "product sharing" were used today as it was in the early experiments in this direction over a century ago, or if we used the term "income sharing," much of the prejudice might vanish. But we must not lose sight of the fact that it is the profit system of the American plan which is today the center of attack of all those who would undermine capitalism and the American plan. Therefore, the psychology of establishing profit sharing as a means of establishing mass consciousness of participation in the profit system, is imperative as a fortification of the profit system.

Equal to the confusion existing among employers as to ways and means toward the insurance of industrial peace is the misunderstanding and divergent views on the operation of profit sharing—what it means—what it will do--and how it applies to different types of employers.

Some declare, "You cannot share profits without sharing management"; still others are fearful that "profit sharing" transfers ownership. These fears are utterly unfounded. Signally successful plans which have operated for as long as a half a century refute such contentions.

Others assert "Profit sharing will necessarily raise wages" and in the same breath another argues that "its operation will reduce wages." As to the effect upon wages, the result of profit sharing has been to stabilize wages in the long run.

There are those who claim that "the sharing cannot be differentiated from wages," hence it all adds to the wage scale and continues the strife caused by demands for more and more wages. The testimony of the most successful and effective profit-sharing plans disprove this statement. We are familiar with plans under which the employee attaches no relationship whatsoever between wages and "share funds." And in practically all sound profit-sharing plans, benefits are in excess of market wages.

Then there is the quite prevalent idea that employees will support and approve a profit-sharing plan while profits are made and shared, but who will become resentful and rebellious when losses occur and profits are not available for sharing. Such an attitude and reaction depends entirely upon the form of the plan. A number of companies can testify that no such condition prevails in the operation of their plans.

Too prevalent is the concept of employers that profit sharing involves a division of profits on the 50-50 basis with employees. Such a concept has had no place in the minds of those conducting this survey. In fact, from a poll of thousands of individual employees throughout the Nation, an insignificant percentage of employees have expressed their idea of a division of profits on any such basis. On the contrary, the overwhelming majority of employees show their extremely reasonable attitude toward a safe and practical distribution of a small percentage.

EXPERIMENTS ARE NOT FAILURES

Most writers who have assumed the position of experts, and authorities who have written on the subject of profit sharing, have conveyed the conclusion and opinion that because more profit-sharing plans have been discontinued or abandoned than have survived therefore the principle of profit sharing is unsatisfactory and impractical.

It might be stated that the same fact is true of corporations, with even a greater percentage of failures, yet we do not conclude from that record that corporations per se are unsatisfactory or impractical. No progress in social, industrial, or political development was ever brought to successful practice or conclusion except from the lessons gained from experience with earlier failures.

Permit me to submit the philosophy expressed by Mr. Harry S. Dennison, president of the Dennison Manufacturing Co., one of the early pioneers in the study of profit sharing and employee relations, and a man who has personally spent half a century in studying our industrial problem. Mr. Dennison says:

"In tackling any complex problems, I think it extremely wise for us to recognize that betterment is a process—that betterment cannot be simply installed. We should recognize that it has got to start slowly, that it has got to grow.

"Experiments have been going on for thousands of years, but we cannot call them experiments—we have usually called them failures; and yet there are no experiments that are failures.

"If you will study, you will learn something about them. We have tried to learn more from the failure of an experiment than it cost us in money."

The analysis applied thus far by your staff to the study of discontinued and abandoned profit-sharing plans in the United States indicates that the causes of discontinuance were generally due to the provisions and vulnerable form of the plans themselves, and the conditions existing in the industry at the time or to the objective set forth to be accomplished, rather than the fundamental difficulty with the principle or concept of profit sharing. On the basis of present accumulated data, it could have been foretold at the time of inception that practically all of the discontinued plans would, of necessity, have failed.

It also has been claimed that profit sharing offers little incentive for direct production. This is possibly true in many instances where only immediate direct production was considered or where the installation of a plan was for that purpose only. In such instances the obvious intent of the plan would almost insure its failure. On the other hand, our data indicate that certain types of plans when properly applied do definitely provide incentive in a far more significant and broader sense. The testimony of those executives and employers who have found the formula of success in applying the principle of profit sharing is well-nigh unanimous that profit sharing when properly applied to the existing conditions, whether the concern is profitable or not, creates improved employee attitude, increased personal interest, individual and group cooperation, self-imposed supervision, and a definite reduction of labor difficulties.

The record of profit-sharing experiences shows both complete failures and brilliant successes. The application of profit sharing to a concern requires intelligence and study. Too many overlook and ignore psychological features which are as important if not more so than the dollars or percentages involved. In principle profit sharing is grounded in the traditions creating the American system. To widen its base, increase the membership of its participants, and instill personal consciousness of the individual's place and responsibility in the profit system, is to mobilize an unbeatable defense of the American capitalistic system.

AN UNPREJUDICED SEARCH FOR A PRACTICAL FORMULA

In conclusion, gentlemen of the committee, I would again repeat that we have conducted this survey and study without regard to prejudice and with an open mind toward the hope of discovering positive and constructive facts for the development of an authoritative and accurate record of experiences for the guidance of American employers. We have been actuated by the thought that experience, not theories, is the source from which we must draw practical results. We have sought—effects—results—values—rather than definitions or technicalities. It has been our belief that the working man is not interested in a definition or the technical structure of a program, but that he is vitally interested in recognition, participation, and security. We have sought to be practical rather than technical; realistic rather than theoristic, although our study has not overlooked any of the theoretical aspects involved in the subject matter. We have approached the study of the principle of profit sharing not with the thought that it is a substitute for the wage system, but rather with the idea that it should be recognized as having its rightful place within the present economic system as a fortifying supplement to the wage system. Profit sharing appears to be one effective key to a real partnership between labor and capital and we must therefore attempt to solve its perplexities, if possible. Likewise, we have not shared the belief of the more enthusiastic advocates of profit sharing that it would solve all the problems arising between employer and employee. We do not believe that it can in any way be a substitute for good management, nor that it can make up for the lack of personality in management; its introduction cannot transform an unsuccessful and poorly managed business into a highly successful and prosperous one.

We have been controlled and actuated by the thought that we may make a contribution toward the achievement of the greatest goal in America—that of making democracy work, socially and industrially, as well as politically.

Senator HERRING. Thank you, Mr. Despain. In following the spirit of the resolution, the committee has not found it necessary or advisable to resort to subpenas. We have invited a number of the leading employers and employees to confer with us. We have had splendid cooperation from everyone approached.

As the first witness we have invited Mr. Deupree, the president of Procter & Gamble Co. He has very kindly come today and I should like Mr. Deupree to please step forward.

Mr. Richard R. Deupree, president, Procter & Gamble Co., Cincinnati, Ohio. Mr. Deupree is thoroughly familiar with the work of the committee. He and his firm have been very helpful. This is not an inquisition, Mr. Deupree. We are glad to have you come to help us. We want your advice and your experience. We want you to feel perfectly free to tell us anything that you think would be helpful to us and to the committee.

STATEMENT OF RICHARD R. DEUPREE, PRESIDENT, PROCTER & GAMBLE CO., CINCINNATI, OHIO

Mr. DEUPREE. I was away from the office since I knew I was to be here, so I have not prepared a statement, Senator, and if I can talk within the scope of the previous speaker, that is in the broad sense of profit sharing, I would like to do so. If I get astray you can tell me. I made some memoranda coming down.

I think the statement of Mr. Despain was terribly good. The statement made by the gentleman preceding me, that profit sharing is not the whole story, it is tied up with a great many other things.

I would like to go back and talk about Mr. Procter's viewpoint when he established profit sharing in our company.

Mr. Procter had a view something like this, which is fundamental to me, and that is, that back in 1886, he had these thoughts, and they have been on record, so to speak, he felt that a man should have an opportunity of work, that a man who was willing and capable to work should have work, if one could give it to him. He believed in a steady job and an opportunity of the man getting the best out of himself. He felt that a workman should be a good citizen, and that anything that could contribute towards that would be a helpful thing in our whole economy. So he set about trying to find a way to help a man to create an estate, a protection against old age, and a decent place in which to work. He felt that he should have pleasant surroundings, an opportunity of schooling his children, of owning his home, and taking part in his community work.

Now, that was the philosophy back of our start in profit sharing, and merely to show you that, in our pamphlet which we give to our employees on profit sharing, here is an original statement that has practically never been altered:

"In originating and continuing this plan it was and is the desire of the company to encourage thrift among all its employees and to favor those who remain continuously in its employ. It has always been the declared policy of the company to recognize that its interest and those of its employees are inseparable."

Now, I make that point because to me anything which is helpful in this scheme of things is the result of an attitude of mind, a desire to do something, and from that standpoint we believe that a man had to make a good citizen out of himself if he was going to make a good employee, and that we had a certain part in helping him to do that. So that in anything that we have done over the 50 years—and when I say "we," it was pretty much the brain of Mr. Procter. Mr. Procter started this thing just out of college, and he kept it up until his death 5 years ago, and we tried to follow him.

Now, profit sharing was first started with a cash payment.

Senator King. Was it a corporation or partnership?

Mr. Deupree. It was a partnership until 1890. When they started the profit sharing it was a partnership, just the two families. Of course, they had the benefit of Mr. Procter's grandfather and his father coming through the business, and even when Mr. Procter came into the business there were not over 300 employees, so he grew up in the plant with the men, and he had an understanding of some of the things which men think about, which they want and desire.

Now, we started out by paying a profit-sharing dividend in cash twice a year, but we always did it at a kind of a, what we call, dividend-day meeting. In the summertime they would have a picnic and the families would bring their baskets, and the management or the owners, if possible, would mingle with the people, and they made a picnic day out of the profit-sharing day. They were paid in cash. That was not very satisfactory. In other words, the men took their money, and I suppose, human nature prevailing, it was spent, and at the end of the next year there was nothing left. You will find it all through this. For 50 years the plan has been changed, at times through experience. Nobody apparently could foresee.

It went on about 5 years that way, and then Mr. Procter felt that the scheme was not reaping its full benefit, so he made a radical change in it, and instead of paying profit-sharing dividends in cash, he worked out a plan whereby the profit-sharing dividend was credited to the employees' accounts for a period of 6 years, and at the same time he felt that the thrift idea had not penetrated, it had been just the reverse, so he asked the employee to put up 5 percent of his wages in cash, the company put up anywhere from 10 to 20 percent. It varied a great deal over the years, but at that time it was 12 percent. Then he told the employee that we would buy shares of stock in our company equal to 1 year's wage, and it took about 6 years of 5 percent from the employee and 12 percent from the company when the stock was paid in full, and after that the profit-sharing dividend would be given to him semiannually in cash.

Well, now, basically, that plan has never changed, that is, in those fundamentals. We still ask the employee to put up 5 percent of his money during those 6 years out of his wage, and we add a profit-sharing credit to what he has put up, and usually we put up two for one, or something in that ratio.

Senator VANDENBERG. Excuse me. Do you mean the amount you put up is regulated in proportion to the employee's contribution, or is it related to your profits?

Mr. DEUPREE. It is not distinctly related to our profits. It has a fixed basis to it. It has been, through some of the period of the company, but today it is a fixed basis of profit sharing, running from 5 to 15 percent, depending upon the length of service of the man. In other words, it is 5 percent the first 2 years, then it runs up to 15 percent after 15 years' service, and is 15 percent from there on. The limit is 15 percent of his wage.

Senator VANDENBERG. And that is your contribution regardless of the profits of your corporation?

Mr. DEUPREE. That is correct, sir.

Senator KING. Have you found any objections by your employees to the plan in the various forms in which it has been submitted?

Mr. DEUPREE. I think we could say that there has been no great objection. There have been, of course, men who would like to receive the profit sharing in cash right from the start, but our experience has told us that that is not good; it does not accomplish the thing that we think is fundamental for him, that is, the sense of saving and thrift, and helping to create his own estate. You see, through this plan, over the years, over half of our employees have a stock ownership or just a cash bank balance, if you want to call it that, of approximately $2,000 or more. A great many of them own their homes. It is conducive to home owning. The rest of the employees are working toward that end, and we think it has been exceedingly helpful to the employee, and naturally we think it is good for us.

Senator HERRING. After you reach the 15 percent, the dividend then is in cash; there is no further stock?

Mr. DEUPREE. It does not require the 15 percent, Senator; it requires 6 years—6 years of the profit-sharing plan—and then he gets his profit-sharing dividend in cash.

Senator HERRING. Semiannually?

Mr. DEUPREE. Semiannually. That occurs when he is getting about 7 percent of his wage in cash and that runs on up to 15 percent.

Senator VANDENBERG. I do not wish to anticipate your statement, but I am interested in knowing how many employees you have and how many of them have voluntarily joined your system.

Mr. DEUPREE. Our profit sharing is limited. We have about 10,000 employees, roughly speaking. Now, of those eligible, which are in a wage scale up to $3,000 for factory and office employees, practically 99 percent are in the plan. In other words almost all of them. In that sense I think it would answer Senator King a bit, I would say it is fairly reasonably satisfactory to the group.

Senator VANDENBERG. Are you going to tell us what it means in dollars and cents in a typical employee case?

Mr. DEUPREE. I can do it at anytime, because I have some memoranda I can go on. It is something like this: To the average employee the wage today is something around $1,500 to $1,600 a year. I am talking of factory workers now.

Senator VANDENBERG. Yes.

Mr. DEUPREE. Theoretically, and practically, in 6 years he has a paid-up account of $1,600. If he has bought company stock he gets, of course, the stock dividend, whatever it may be, like any other stockholder. It is regular stock.

Senator HERRING. Does he get it during the 6 years?

Mr. DEUPREE. It is credited to him. I think I ought to make this clear. In order for a man to remain in our profit-sharing plan, he must hold that original stock issue; I mean, that is a part of the plan. At the end of 6 years he cannot take his stock and go and sell it and still remain in the profit-sharing plan, but if there is any really good reason—if he has sickness in the family, if we know he is going to make a down payment on a home, or any other very, very good reason, we are willing that he should sell half of his stock and continue in the profit-sharing plan; but he cannot take his stock and sell it out for any old reason and continue with us in the profit-sharing plan. We do not have many requests to do that; it is very limited.

Now, the man creates, we will say, an estate in 6 years of $1,600.

Senator HERRING. That is including the 5 percent that he puts in?

Mr. DEUPREE. That is right. Part of that is his money. By the way, it was a very fine statement that the gentleman made who preceded me. A successful profit-sharing plan must be based, I think, upon paying the ruling wage of the community, and your profit sharing, or whatever you do, must be plus. I think it is an awful mistake to try to cut the wage below the prevailing unit and then give profit sharing to make up for it. So our plan is based upon a prevailing wage, a very fair prevailing wage, and anything else is plus.

Now, you take the man, at the end of 6 years, that has a $1,600 estate, instead of paying 5 percent into the plan of his own wages, he has that in addition to what he has been living on, and then instead of having the, say, 7 or 8 percent at that stage credited, he has that coming to him in cash. So at the end of 6 years he has 12 or 13 percent more cash available than he has had during the previous 6 years.

Now, the man that has been living on what he had left out of his wage, less 5 percent, and then suddenly receives the 12 or 13 percent, well, he has practiced thrift long enough to take that money and do something with it. He has had 6 years of practicing the art of thrift, and he becomes an accumulator, he commences thinking about his home.

We have had a pension plan for 40 years. He has been reasonably sure of protection in his old age. We have had a sick-benefit plan for 40 years. That helps him. Now, the man is becoming—I hate to say it in this way, but it is nothing else but that—a capitalist. He has accumulated something. He has stuck to his community and he becomes a pretty good citizen. When he gets through working, say at 65, he has a reasonable estate waiting for him, he has his old-age pension, the chances are he has his home, and he is in pretty good shape to go on.

Senator HERRING. Your sick benefits and your old-age pension are in addition to the profit sharing?

Mr. DEUPREE. Oh, yes; yes, sir. That all is in addition.

He has his guaranteed employment, which is probably fundamental to me, even more than profit sharing, in any business which can do it, and not all businesses can do it. There are businesses that are in luck and there are businesses that are out of luck, just the same as there is land with good topsoil and land with almost no topsoil. You cannot apply anything to general business, until you know the individual business. The steady job, if a man can do it, to me is more fundamental than profit sharing.

Senator VANDENBERG. We start on this inquiry, then, with the proposition that it would be absurd to attempt ever to dictate a standard formula to American industry; is that your view of it?

Mr. DEUPREE. Senator, I would say literally it is impossible.

Senator VANDENBERG. Of course it is.

Mr. DEUPREE. I am in the Roper Council, the Advisory Council of Secretary Roper. I have just been asked to make a study of what I term steadier employment. I spent 6 months on it, and they came out with just that statement. I cannot believe there is any set plan, procedure, panacea, or cure-all. It is more a question of what an individual man does who gets a desire to do something and works it out as it fits his own particular business, and there are loads of plans in this country. I was surprised in the study of giving steady employment, or much steadier employment, than formerly and I have not found any two of them alike. There are different phases of different businesses, there are different problems in each industry. I do not think any human being can pass a law that would get anywhere in forcing or attempting to force any such thing as steady employment, or even profit sharing. The problem is too individual.

Senator VANDENBERG. In other words, a socially minded employer is more important than a socially minded statute?

Mr. DEUPREE. I do not believe there is any other answer to it.

Senator HERRING. Your annual pay roll is not dependent on the profit sharing, it is entirely separate from your profit sharing?

Mr. DEUPREE. Absolutely, sir. We have to pay the prevailing wage in the different communities.

Senator HERRING. You have an annual wage plan, do you not, where they get 48 checks per year?

Mr. DEUPREE. Yes. We have guaranteed since 1923, and we have been fortunate enough to be able to go through with it even in the depression. We have guaranteed to the employees, after they have been with us—a man has to be with us 2 years before he enters that plan, but all employees over 2 years are guaranteed at least 48 weeks' work per year, and we have done that.

Senator HERRING. And that is the plan that cannot be applied to all businesses?

Mr. DEUPREE. It is literally impossible. It cannot even be applied to some phases of our business. We crush cottonseed in the South. If there is a big crop we have a year's crush, or maybe 10 months, and if we have a light crush, 4 months or 5 months, and there is no way in the world that we can control it. It just cannot be done.

Senator VANDENBERG. Did you ever have any strikes during those 50 years?

Mr. DEUPREE. The answer really is "no," but we really asked our people during the war, that is in 1917, to go out in Kansas City. It got so difficult there, and the men went out. I mean at one time in Kansas City it was pretty bad, but our men did go out. So, in a sense, you can call it a strike, I guess, but we urged them to. The real answer is "no." We have not had a strike in 50 years.

Senator VANDENBERG. You have had no labor trouble at all, I mean, of a major nature?

Mr. DEUPREE. No major labor trouble. Our people have their own set-up, they have their own representatives, they have selected probably 1 in 50 that represents them on a conference committee, and then they go on down to an executive committee of their conference committee, and they fuss at us, and we encourage their fusses, because it is only through that sort of thing that we arrive at the right thing to do. Our statement to them has been for years that we are seeking the right thing to do, if we can find out what is the right thing. When you say trouble, not literally trouble, but they are constantly asking us, "Don't you think we can do this" or "Should do that." It is talked over and worked out, and where we can do something we do it, but there has not been any major trouble.

Senator VANDENBERG. You attribute that peace, at least in part, to the fact that you have this profit sharing?

Mr. DEUPREE. I think profit sharing, plus the steady job, is fundamental to a nice relationship with our people. I mean the men own stock in the company, they are part of the company, and the success of the company is helpful to them, and I think it has contributed largely to it.

Senator KING. Do any considerable numbers of them, after they acquire stock ownership, attempt to dispose of it, or do they prefer to hold it and enjoy the dividends that result?

Mr. DEUPREE. I do not believe, Senator, 1 percent disposes of it. He would have to be a rather foolish man. You see by that time he is probably getting 10 percent cash dividend, that is 10 percent over his wage in cash. It would be rather foolish. I cannot imagine any reason for him doing it, except, well, I will just say it would be plain foolishness.

Senator VANDENBERG. What is the total stock ownership now by the employees?

Mr. DEUPREE. Well, those employees under $2,000 own about $6,000,000 worth of stock.

Senator VANDENBERG. Out of what total?

Mr. DEUPREE. I would have to multiply 55 by 6,000,000, that is about $330,000,000. However, that does not tell the story. For instance, I started in profit sharing 33 years ago, when I went with the company, and other men like me, and we have all come through this profit-sharing plan. You see, when we make over $3,000 a year—it used to be $2,000—we go out of the profit-sharing plan. I would think the employees would own a good deal more than that, including the men who have been in profit sharing and have gone out of the plan.

Senator KING. Are most of the higher salaried employees of the company those who have come up from the lower ranks, using the ordinary expression?

Mr. DEUPREE. I think it is 100 percent, Senator. Our administrative committee of six men average in length of service about 35 or 38 years, somewhere in there.

Senator KING. So that those starting in at the bottom of the ladder, so to speak, may have the expectation of some time reaching the higher rungs of the ladder?

Mr. DEUPREE. Yes. We do not employ an executive. Maybe that will give you the answer.

Senator HERRING. How much did your profit-sharing plan have to do with the gradual advancement of those on the lower rungs?

Mr. DEUPREE. I do not believe I can answer that, Senator. It is all so tied in with a company, its policies, its plans, and its procedures. I was trying to think of myself. I do not know that profit sharing was the means of my going through the company. I like the company, I like the work, and I have rather a notion that most men would be with the company, but unless profit sharing, or something similar to it, was an expression of management, I do not think probably that the men would stay with the company as long as they do.

Senator HERRING. Of course, it encourages continued employment?

Mr. DEUPREE. That is true.

Senator HERRING. And through continued employment they get advancement?

Mr. DEUPREE. Even in our factories the average length of service is something like 8½ years, and that is a fairly long average for a factory employee, when you have very large numbers of employees.

Senator KING. What arrangements are made for sick benefits and for old-age insurance, and who meets the bill?

Mr. DEUPREE. The employees meet the bill on sick benefits. They contribute 1 percent of their salary. The company has always put up all the money toward old-age pensions.

Now, I will just skim through this thing. I feel very much that this whole subject is tied up with the attitude of mind of management, and in our profit-sharing plan, which started way back in 1886, we soon put in the old-age pension, and the sick and accident benefits were tied in with the plan.

An interesting thing to note is, I think, that Mr. Procter established the first half Saturday holiday west of the Alleghanies way back in the late eighties. I mean that is just part of the thinking. The conference committee of employee representatives has been in our business since I have known it. We had plans for the purchase of stock other than profit sharers. We had a building association, in which the company simply participated and was helpful at times when the association might be in a little trouble. There was an elimination of danger spots in the plant constantly going on, better air, better light; a development from the common labor and unskilled labor of our own selection into semiskilled and skilled labor. Most of our work is unskilled and semiskilled, but we try to bring our laborers through to fill those other jobs. We encourage the sons and daughters of our workmen. It is all a part of the plan. I do not know whether your committee is particularly interested in it, but we eliminated the right of the foremen to hire and fire. A foreman can refuse to take a man, he can say, "I do not want him in my department," but he cannot discharge him from the company. That used to be a source of a great deal of trouble.

We have the hospital, we have the doctors and nurses, and first aid, and this is surprisingly effective with the men. The men come to our doctor there for practically everything they have, outside of a serious illness, and they are helped. They are taught cleanliness and medicinal values and things like that. We have injected cold serums and reduced the number of men with colds something like 60 percent; that is my recollection, and all of this, of course, is free to the men.

We put in a 1-week vacation with pay, which is a very acceptable thing, of course, to the men who used to come down to the shut-down period and have trouble, and today they come up to the shut-down period with their week paid for.

The 48 weeks' guaranteed employment you brought out.

Now, as to this tax relief, I have mixed feelings on that, gentlemen. I do not know. It is going to be the most difficult law to write and administer, for the reasons that were brought out. It is very nice to have a tax relief, of course, if you do something like this, but I am not sure of it as something that is going to mean something to a great many people who will handle plans of this sort. It may be an incentive, that is my own thinking on it, and maybe it is not good thinking. I mean, I do not have all the data that you men may have, but if you can do something to get an employer to think, to concentrate on this problem, probably offering some inducement to get him started, then let it peter out after 5 years or so, let him get started, I think that would be a tremendous thing.

Senator VANDENBERG. What, for instance, would you suggest? That is a pretty difficult question to answer, is it not?

Mr. DEUPREE. It certainly is, Senator. It may be that you might give him some exemption in his corporate tax. He has that, of course, on any of these plans, as an expense of doing business, but particularly I had the view that if a man had a plan that gives his men steady work some reasonable number of weeks per year, that the cost of that plan might be shared about one-third by the Government and two-thirds by himself, or one-half by the Government and one-half by himself, or, if it cannot be fixed in that ratio, say you have a flat corporate rate, which you do not have today, give him 2 percent of the profit reduction, something that would force him to strive for that objective. I would not know how to write it, but I am only saying if you put an incentive in front of a man to do a job, I think it would stimulate his thinking tremendously, but that alone will not do it. It is an educational job, and in the report that we made for the council, we are recommending that it is a State educational job; that it starts right in a State and goes down to the manufacturers. With that kind of a job done, coupled with some incentive, it would be a good start.

Under the Social Security Act several States have the merit rating, and several of them do not. Most of them do not, but they have the theory in their heads that they will have it by 1942. Certainly each and every State, in my judgment, should have a merit rating clause for good employment, so that instead of paying 3 percent into the unemployment fund, if a man has a performance that shows it is not costing anything like that, he should get the benefit of that saving. If that is not done, I think it would be too bad. I think it will be done.

Senator VANDENBERG. That is one form of incentive taxation, is it not?

Mr. DEUPREE. That is right.

Senator HERRING. Would not the application of the compensatory tax exemption to the employer aid greatly in the extension of the profit-sharing plan by the employer?

Mr. DEUPREE. What was your question?

Senator HERRING. I say, if you apply the compensatory tax exemption to the employer, would that not, in reality, be extending the profit sharing as an incentive to the employer, just as your profit sharing provides the incentive to the employee?

Mr. DEUPREE. Yes; only in a little different way. It would give him something to strive for, because, as I say, we are all human, we are all trying to lower our costs, and a man will struggle like the "dickens" to lower his cost of production, and that lowers his cost of production if he can eliminate the 2 percent.

Senator VANDENBERG. Do you find any clash between the Social Security Act and your profit-sharing plan?

Mr. DEUPREE. No, sir; not that I know of.

Senator VANDENBERG. There is no collision?

Mr. DEUPREE. No. All men do not like the deduction, because, for instance, our men have to pay 5 percent of their wage in their profit-sharing plan, and this is just another "duck" as they say down South; it is another deduction in that sense. That is a question, naturally. Men do not like deductions from their salary, but it is all done for their future security, and I think they are digesting it.

Senator KING. May I ask a question? Now, please do not answer it if you experience any hesitation in the propriety of doing so. Have you found, on the part of labor, of labor organizations, any objections to this partnership plan under which the employees ultimately become co-owners in the business?

Mr. DEUPREE. I will say we have not found it.

Senator KING. The labor organizations have not objected to the plan, as far as you know?

Mr. DEUPREE. No.

Senator KING. The outside organizations?

Mr. DEUPREE. No; we have had no objections. I know a great many of the labor men. I think they feel we are all right in the plan; it is helpful to the employee; it is fundamentally helpful.

Senator VANDENBERG. Is this the latest book carrying your plan [indicating]?

Mr. DEUPREE. Yes, sir.

Senator VANDENBERG. Let us have that marked as a committee exhibit.

(The book referred to was marked "Exhibit 1" and is filed with the committee.)

Senator KING. Have you any extra copies of that?

Mr. DEUPREE. You may have this one that I have, Senator. Let me keep it until I get through, in case someone cares to ask me some questions about it.

Senator KING. You may leave it with the clerk when you have finished.

Senator HERRING. Just go right ahead, Mr. Deupree.

Mr. DEUPREE. Now, I have finished my story, Senator. I did not want to go into too much detail on any of these things.

Senator VANDENBERG. You have a very low turn-over in labor, do you not, Mr. Deupree?

Mr. DEUPREE. Yes, sir; it is almost nothing, probably one-half of 1 percent a month to 1 percent, depending on the way you think.

Senator VANDENBERG. As compared to other industries in that area, that is amazingly low, is it not?

Mr. DEUPREE. I think it is low, Senator.

Senator VANDENBERG. Is that the result of your profit-sharing plan and your other social attitudes?

Mr. DEUPREE. Unquestionably.

Senator VANDENBERG. What effect does it have on the elimination of waste and the encouragement of production efficiency?

Mr. DEUPREE. No one can measure that and make a positive statement about it, but we are just as positive as though we could measure it, in our own mind, that the employee, knowing that he has a job and that he is a part of us and we are a part of him, he is friendly and interested in accepting suggestions for improvement, the result of which is that even with all of these plans and the cost to us is somewhere between 15 and 20 percent of his wage, we have been able to keep our costs of production units reasonably steady. I think we are up 50 percent in hourly wages since 1929, 50 percent greater wage per hour, and if you go back to 1920, or before the war, 1915, we are up 150 percent and yet through the interest and effort of employee and company working together, our unit cost is pretty steady. I am sure it has contributed, but I cannot put my finger on it.

Senator VANDENBERG. In other words, speaking generally, you not only have had the happy satisfaction of a better social relationship with your employees, but it is also profitable for an employer to be socially minded?

Mr. DEUPREE. I would say that it is, yes; definitely; but I do wish you gentlemen would appreciate that a business must first make money. Now, that is the first object. I cannot ask you to loan me money to go in business unless I can make money on it, because I have got to give you a return. Now, business has got to be successful before it can start doing these things.

Senator HERRING. Is not one of the requisites of such success the loyal, efficient employee?

Mr. DEUPREE. I think it is. That is all right, yes; but you must have a capable management.

Senator KING. Certainly.

Mr. DEUPREE. And you probably would have to be in one of these businesses that have at least some topsoil.

Senator KING. The men on the ship must be loyal to those in their occupation, but you must have a captain on the ship.

Mr. DEUPREE. Yes; you must have management.

Senator HERRING. Is there anything further?

Senator KING. I want to ask just one question. You have referred to the families. To what extent have children of your employees found employment with you? Do they seek it?

Mr. DEUPREE. Yes, sir.

Senator KING. Are they eager to follow the footsteps of their father to find employment with your company?

Mr. DEUPREE. Now, I cannot answer that categorically, Senator, I can only say we encourage it. An employee's child certainly has first consideration, and we have a great number in all phases of the business.

Senator KING. So that you have not only the loyalty of the man who is working for you, but you have the loyalty of his family?

Mr. DEUPREE. We talk to our employees once a year, every one of them, through the dividend meetings, and we see that the wives get there, if they can. We like to talk to the family.

Senator HERRING. Thank you, Mr. Deupree. It has been mighty fine of you to come here. We appreciate your work.

Mr. DEUPREE. Thank you, Senator.

Senator HERRING. We will adjourn until 2 o'clock, at which time we will hear Mr. Folsom, treasurer of the Eastman Kodak Co., and General Wood.

(Whereupon, at 11.30 a. m., a recess was taken until 2 p. m. of the same day.)

AFTERNOON SESSION

(The hearing was resumed at 2 p. m., pursuant to recess.)

Senator HERRING. Mr. M. B. Folsom, treasurer, Eastman Kodak Co., Rochester, N. Y.

Mr. FOLSOM. Yes, sir.

Senator HERRING. You are familiar, Mr. Folsom, of course, with the purpose of the resolution in the committee? I don't need to go over that with you?

Mr. FOLSOM. That is true.

Senator HERRING. We appreciate your cooperation. Your company has been mighty fine and we appreciate your coming here today, and we want you to go right ahead and tell us, in your own way, your experiences so they will be helpful to the committee.

STATEMENT OF M. B. FOLSOM, TREASURER, EASTMAN KODAK CO., ROCHESTER, N. Y.

Mr. FOLSOM. I am very glad to be here at the invitation of the subcommittee and describe the industrial-relations program of our company, particularly the profit sharing plan.

I have a statement which is prepared, which I will file, but I would like to describe our plans in general, and would be glad to answer any questions which you might have.

We adopted in 1912, a profit sharing plan, and have paid a wage dividend to our employees every year since that time with the exception of the depression year, 1934. This plan has changed very little in principle since it was devised by Mr. Eastman, in 1912, and we consider it a very important part of our industrial-relations program.

For many years the company has recognized that satisfactory relations between employees and management is a very important essential in the successful conduct of the business. There are certain fundamentals which we think necessary.

There must be payment of fair rates of wages, provision for suitable and safe working conditions, reasonable hours of work, and another factor which is very important is stability of employment, a steady job; and also, an intention on the part of management that there must be a square deal for all employees.

Our industrial-relations program consists of these essentials and also a provision for the economic security of the worker, and giving him a fair share in the financial success of the business.

Now this involves not only a profit-sharing plan but life insurance, retirement annuities, benefits for total and permanent disability, a sick-benefit plan, a medical service, and also personal loans to employees in emergency, and also vacations with pay. That is our complete program.

One of the first steps we took in this program was the adoption of the wage-dividend plan in 1912. The purpose of that plan was to enable the employees to participate in the earnings of the business after a reasonable return had been paid to the stockholders on their investment, and after all expenses had been met.

We look upon the wage dividend as an extra return to the employees in the form of a dividend on their wages, just as the return to stockholders is a dividend on their investment. This is a recognition of the contribution which loyal workers make to the success of the company. Its purpose is to give the employees a share in the financial success of the business, and afford a source of income over and above the regular wages in order to help the employees provide for their future. It also has, for its purpose, the encouragement of continuity of service.

This wage dividend is dependent each year upon the earnings of the company and also the action of the board of directors each year, but we have actually paid the wage dividend to employees every year, with the exception of 1934.

Senator HERRING. Does it fluctuate or is it a percentage, a fixed percentage?

Mr. FOLSOM. It fluctuates with the payment on common stock dividends.

We make this payment each year in cash, usually in March. We make no restrictions whatsoever as to how the employee can use that money, and the amount is increased or decreased as the dividends to the common-stock holders increase and decrease. This formula is well established and well known to the employee.

We have never considered this wage dividend as a substitute for wages, and it is not taken into account by the company in establishing our wage rates. We base this wage dividend rate on the dividends which we declare on common stock of the company in the preceding year, and the employees participate in this in accordance with their earnings for the last 5 years. All employees are eligible if they have been with us for 6 months, except for those who are regular part-time workers.

The formula is this: For each dollar declared on common stock of the company the preceding year, over and above $3.50 per share, the wage dividend rate is one-half of 1 percent of the salaries or wages received by the worker during the last 5 years.

To give you an example of how it actually works out: In 1937 the company declared dividends on common stock of $8 per share. That was $4.50 above the minimum which we set. And the rate paid in 1938, was 2¼ percent. That was one-half of 1 percent multiplied by $4.50, which is the excess of $8 over $3.50.

So the rate was 2¼ percent, and we applied that to the wages the workers has received in the last 5 years

If an employee had been with us for 5 years he got an average of approximately 5 weeks' wages. He got a check on the 1st of March, figured for his individual case; and if a man had been with the company for 5 years it amounted to about 5 weeks' pay, and if he had less than 5 years' service, it was proportionately less.

During this year our business declined because of the business recession, and the profits declined, and the dividends we have declared this year are $6 instead of $8. Now, the wage dividend which we have just declared payable next March will be 1¼ percent of the 5 years' wages, instead of 2¼ percent, which it was this year.

Senator VANDENBERG. Do the employees understand this formula thoroughly?

Mr. FOLSOM. Yes; it has been in effect so long, and it is printed in all our company booklets, and so forth, and when the year's dividends are declared on the common stock, the employee can figure it out.

Two years ago, for instance, when we declared an extra dividend at the end of the year, because of the undistributed-profits tax, the employee knew right away it was going to affect his wage dividend. So the employee knows that his dividends go up and down with the dividends on the common stock.

Senator VANDENBERG. How many employees are sharing in these dividends?

Mr. FOLSOM. This year this dividend was paid to 22,500 employees in this country, and that represents 90 percent of our employees. The employees who don't participate are those who have been with us for less than 6 months' time. The dividend amounted, in this country, to $2,900,000, and our employees throughout the world received $3,400,000.

But our wage dividend next year, in March 1939, will go down to $2,200,000.

We have actually paid out in dividends under this plan, including the payment we are making next March, $43,000,000.

Senator VANDENBERG. In how many years?

Mr. FOLSOM. Since 1912. And $36,000,000 has been paid to employees in this country.

The rate has fluctuated quite widely during the past few years, particularly during the depression.

Our rate in 1930, was 2¼ percent; that is, 2¼ percent of the wages for the last 5 years. It stayed at that level during 1931 and 1932. Then, during 1932, our dividends on common stock declined quite considerably, so that in 1933, our rate was down to only one-fourth of 1 percent. Then the dividend on common stock was further reduced in 1933, so we had no wage dividend at all in 1934, because the dividend on common stock was below the $3.50 figure, which is set as the minimum.

Now, the next year there was a business recovery, and our dividends increased, and in 1935 we had a wage dividend of one-half of 1 percent, and in 1936 it was 1 percent, and the next year, 1937, 1⅝ percent, and last year 2¼ percent, which reached the peak rate that we had before the depression.

Senator VANDENBERG. Tell me again, a wage dividend of 2¼ percent would represent a stock dividend of what?

Mr. FOLSOM. Of $8.

We feel that this plan has been successful throughout the years, and the objectives of the plan have been realized.

The employees understand that their share in the profits is dependent upon the company's operations.

For instance, in 1934, the one year we had no wage dividend, the employees realized why it was so, because the earnings of the company declined to such a point that we simply didn't pay it.

Now, after that, the next year, however, our operations did improve, and we were able to pay a wage dividend. We think that, because of that suspension and low payments during two or three years, the employees really appreciate and understand the plan more than they did before.

There might have been some tendency before that to take it for granted, because we had gone on for a number of years at the same rate, but when we came down to a low point, and then went up again, I think they realized and appreciated more fully than before how the plan works.

Senator VANDENBERG. Was there any general discontent aimed at the company?

Mr. FOLSOM. We didn't get any. There might have been some, but we didn't hear of any. The employees fully realized why it was so. They knew the profits were down considerably, and the business wasn't there, and we just hadn't earned it.

Senator VANDENBERG. Well, we constantly hear that a profit-sharing plan is very popular as long as there are profits to share, but the moment there are no profits, that there is a compensatory restlessness which wipes out all the previous advantages.

Mr. FOLSOM. We didn't have that experience at all. We had this plan in operation from 1912, up to 1934, and the employees knew how it worked, and received their wage dividends every year. They knew the formula, and they had seen the common stock dividends come down and down, and they knew that when they got down below $3.50 there wouldn't be any wage dividend, but we didn't hear any grumbling at all because they had been sold on the principle of it.

The next year, when we paid that one-half of 1 percent, I think they appreciated that more, probably, than they did some of the larger dividends we had previously paid because they knew we were going to continue the plan. But we can foresee all sorts of practical difficulties in trying to work out a definite plan of tax exemption.

This incentive taxation should not be confused with merit rating in unemployment insurance. In many of the State unemployment compensation laws there is a provision for merit rating, or experience rating, under which the tax rate varies within certain limits in accordance with an employer's experience in causing unemployment. Under this plan, however, the taxes are levied for the definite purpose of providing benefits to workers who become unemployed and the money presumably will all be used for that purpose or for the administration of the plan.

Under these merit-rating provisions the taxes are levied under the principle, long established in insurance, of basing the rate upon experience, and here we simply say that the employer should pay for the benefits of those workers he lays off. This theory has long been followed in connection with workmen's compensation laws. Under many of these laws the employer may self-insure and pay for his accidents, or if he covers the risk through an insurance company, his rate will vary with his accident record. The indirect result of this has been that the employer makes a strong effort to reduce accidents as he thereby reduces his cost.

Likewise, under the merit rating or the individual-reserves type of unemployment compensation, by varying the tax rate according to the amount of unemployment which the employer causes, there will be a strong urge on the part of the employer to reduce unemployment. This, however, is an indirect result and all taxes are levied with the definite purpose of collecting money to pay benefits.

The question in point here is that if additional credit or exemption were given to a company for money paid out under a profit-sharing plan, it would not be the purpose to collect taxes but rather it would decrease the amount of taxes collected and the taxing power is thus used for an entirely different purpose than to collect revenue. However desirable this end might be, we do not consider it sound policy to use the taxing power for this purpose.

There is an increasing interest on the part of employers in employee plans of this type and if individual companies show good results, more and more profit-sharing plans will be adopted.

Senator HERRING. Do you think that the definite relationship between the common-stock dividend and the profit-sharing percentage which you have satisfies them and allays any suspicion that they may not be getting a square deal? That convinces them that they are being honestly treated, does it?

Mr. FOLSOM. Yes; they do go up and down together, the stock dividend and the wage dividend.

Senator HERRING. Because there is always suspicion that they are not being fairly treated?

Mr. FOLSOM. Yes; I will go into that later. I think there are quite a few other parts of the program that are important there, too.

One of the purposes that Mr. Eastman had in mind, when he devised this plan in 1912, was to enable the employee to provide for his own old age, and he stated so very definitely in announcing the plan.

As the years went by, however, we found that the plan was not taking care of the pension problem, and it was necessary to adopt some sort of a retirement annuity plan.

The reason probably was that the people, in spite of the purpose of the plan, enabling them to provide for the future, just didn't put it aside, and we were having workers reaching old age and not being able to carry on efficiently, and yet, in many cases, not being able to retire.

So we became convinced that it was necessary to have retirement annuities, a retirement annuity plan, and we actually adopted such a plan in 1929. It was underwritten by the Metropolitan Life Insurance Co., and it provides, in addition to retirement annuities, group life insurance and benefits for total and permanent disability.

When we adopted that plan we had a big accrued liability. That is, because of the service that the workers had rendered up to that time, there was this accrued liability, we had to have enough money to turn over to the insurance company to take care of the pension for the people that were going to retire within the next few years, and also for the service of all the workers up to that time. We actually turned over to the insurance company $7,500,000 to take care of the greater part of that accrued liability. Half of it was put in by the company and half was taken over from a fund which had previously been donated by Mr. Eastman and the company for the welfare of the employees. So that sum was used to take care of the accrued liability.

Now we financed the current cost by making a reduction in the wage-dividend rate, the cash wage-dividend rate. We said, "From now on, instead of putting all of this wage dividend in a cash payment each year, we will put two-thirds of it in cash and the other third will go to finance the cost of this insurance and annuity plan."

At that time our rate was 3½ percent, and we took 1¼ percent to pay these pension costs, life-insurance costs, and the other 2¼ percent was paid in cash.

So we changed our formula at that time. Before that we had said that common dividends declared in excess of $1 per share would be used in figuring the wage dividend, but from that time on we changed it to $3.50 a share, and the difference was paid over to the insurance company.

Senator VANDENBERG. I don't want to detour you, but I am curious to know whether the Social Security Act collided with this plan.

Mr. FOLSOM. We had this plan, of course, before the Social Security Act went into effect. We had it since 1928, and we changed the plan so that in the future the employee will get practically the same as he got before, but he will get part from the Social Security and part from the insurance company, and the cost to the company is going to be practically the same as it was before.

In other words, instead of paying all these premiums to the insurance company, we are deducting from the amount we pay the insurance company the amount of our tax under the Social Security Act.

Senator VANDENBERG. Your plan was much more liberal than the Social Security Act?

Mr. FOLSOM: Yes; especially for the people retiring during the first few years of the Government plan. The employee is just as well off as he was before as far as the company's contributions are concerned, and in addition he will get benefits from the Social Security Act because of his own contribution, which he didn't make before.

Now we find that our retirement-annuity plan has worked out quite well, and accomplishes its purpose. We have had a number of people retire under it, and it is a good business investment because we can retire a worker after he has passed his period of usefulness. If we didn't have such a plan there probably would be a tendency to keep him on and cut down the efficiency of the organization.

So we think a good pension plan is a sound investment.

Now besides this pension plan, which covers group life insurance and disability benefits, as well as retirement annuities, we also have a sick-benefit plan under which workers are paid when they are out sick, up to a maximum of 26 weeks in 1 year. We also have vacations with pay for our factory workers, as well as the office workers. We have a medical department which looks after the general health of the employees. We also have a savings and loan association which encourages the employees to save and invest their money, and pays them a return greater than they could get in the ordinary savings and loan association. And we also use these funds to help finance employees' homes, by mortgages. Loans are also made to employees in emergencies, on easy terms.

Another very important part of our program is a systematic plan of foreman training, in order to get across to the workers the policies of the management. We find it is very essential to have the foremen understand the policies of the management so that they can in turn get them across to the workers.

Another very important part of our plan is the question of providing steady work. I don't think I can stress that too much. If the worker is steadily employed and has a good annual income, he is much more efficient and his attitude is much better than if he is subject to seasonal lay-off. We have developed, over a period of 35 years, a plan of stabilizing our employment, although our sales fluctuate quite widely. In our amateur photographic goods, our roll film, and so forth, the sales during the summer months are much greater than during the winter months, because the people take more pictures during the summer months.

By the careful forecasting of sales, and scheduling of production, we have been able to stabilize the production during the year and stabilize employment, and as a result we have few lay-offs except during a period of deep depression.

I have a chart here which you might be interested in [indicating], which shows the method which we use. I think that business now generally is becoming much more interested in this question of stabilizing employment. I am convinced that very much more can be done in that direction than has been done. I am hoping that the unemployment insurance laws, which have merit rating, under which the rate will depend on the actual experience of the company in the amount of unemployment it has, will serve as an indirect incentive to the employers to do a better job in stabilizing employment.

This is the system which we use [indicating]. This happens to be our roll film, one of the most important parts of our business. This is our sales curve in here. It starts in at the very low point in January, and reaches a peak up here in the middle of the summer. There is about 15 percent of the year's business there in that 1 month, and down here there is about 3 percent. This is the way the sales go. Of course, if we produced at that rate, we would have a very highly fluctuating producing organization.

At the first of September, that being the end of our season, we make our estimates of the sales for the next year, and start producing at that rate, which is in here. That is our schedule of production. We allow for a drop in the summer months to take care of the vacation period of our employees, and during the fall here we are producing quite a lot more than we are selling. This is the sales curve here [indicating] and as a result this line here [indicating], which is stock inventory, goes up, and it keeps going up until it reaches the peak along in March. All during this period our sales are below production, and we are putting it in inventory. And from that time on, starting in March or April, the sales curve goes above the production curve and the stock comes down and reaches the low point at the end of the season. That is our ideal which we try to work for each year.

This forecast we make in September is based on a great deal of work in our statistical and planning department, going back for a number of years and taking into account business conditions and various other conditions, and we have been able to forecast our sales quite accurately.

This chart [indicating] shows what we have actually averaged for the last 2 or 3 years. This is our sales curve and this is our production. The dotted line is the production curve, with some slight fluctuations. This is the employment curve, practically steady, no fluctuation, or very little fluctuation. As a matter of fact, during the 2-year period, 1936 and 1937, out of 16,000 workers in Rochester, our lay-offs amounted to only 300. This year the record was not quite so good because we had a decline in business the first part of the year. This plan is intended to eliminate seasonal employment, and when you get into a depression you can't avoid some reductions.

We find that steady employment is a very important consideration from the point of view of the workers, and also the company. If the worker has 52 weeks' work in the year, he is naturally better off than if he were subject to seasonal lay-offs, and we are able to attract a better type worker, and keep him better satisfied.

Also, it results in a lower cost to the company because workers steadily employed are better workers, and you can get better production from them. We also can utilize a higher percentage of our plant. If we had a plant, for instance, that would turn out goods at the rate which we are selling them in the summertime, we would have it idle during a large part of the year.

We believe that this whole program has been very well worth while, that is, our whole industrial-relations program. We can't measure it in dollars and cents, and we don't know how much of the success that we may have had in this plan has been due to any one part of it, but we do know that we have been able to maintain an effective and highly skilled working force, and kept them steadily employed except during the period of severe depression.

Senator HERRING. Have you had any labor troubles?

Mr. FOLSOM. No, sir.

Senator HERRING. None whatever?

Mr. FOLSOM. No, sir. Our labor turn-over has averaged less than 10 percent for a number of years. That is considerably less than the average for the country as a whole.

Senator VANDENBERG. Have you any idea what the average would be in the country as a whole?

Mr. FOLSOM. I have a chart here, based on a study that the Bureau of Labor made, and it is the best information I have as to that. By "labor turn-over" I mean the percentage of employees who leave, in proportion to the average number.

Senator VANDENBERG. Yes.

Mr. FOLSOM. Now in 1936, which I think should be considered a typical year because it was more of a normal business year than we have had in a number of years—it was before the recession started in the fall of 1937—the number of separations per hundred employees as reported by the United States Bureau of Labor for the manufacturing industry as a whole, was 40 percent. In that year the turn-over in our Rochester plant—I haven't got many figures for other places—was 8 percent. That is 8 percent against 40 percent for the country as a whole.

When it comes to lay-offs, which includes all separations, lay-offs in 1936 for the country as a whole was about 25 percent, and we were down to less than 1 percent.

That, it seems to me, is where the business people generally should spend an awful lot of time and thought to see if they can't cut down the fluctuations in their force and try to bring about more stable employment.

I think a great deal can be done in that direction.

Another indication that our plan has helped is that we have been able to attract and hold a highly desirable type of worker. About half of our men, for instance, have service of over 5 years, and one-third of the men have had service of over 10 years, which gives us a very stable force.

Now, here I would like to summarize our whole program—I have an Employees' Guide Book, which I thought you could keep, if you would care to. On the last page is a chart which summarizes our whole plan. I thought you might be interested in going down that chart briefly.

The first is normal employment and normal health. At the top is wages at the rates prevailing in the community for similar work—a standard 40-hour week, and 8 hours a day. The next, as I have indicated, is the production scheduled to minimize irregularities in employment due to seasonal fluctuations in demand.

Then the wage dividend, which is paid in cash depending on the dividends paid on common stock.

The supervision of health, and vacations with pay.

Then we have a savings and loan association, which helps the worker own his own home, and in some cases we actually build houses.

That is all during the normal employment.

Now in case of illness we have a sick-benefit plan under which benefits are paid, varying with the length of service, with a maximum of 26 weeks in 1 year, and in case of total and permanent disability, not due to occupational causes, we have a benefit-disability plan which varies with the length of service.

In the case of occupational accidents, we have workmen's compensation, of course.

Upon retirement we have retirement annuities payable for life at age 65 for men and at age 60 for women, the amount depending upon the length of service and the wages. These benefits are in addition to the Social Security Act.

In case of death, we have life insurance which amounts to 1½ years' salary for workers with more than 5 years' service, and 1 year's salary for workers with less than 5 years' service.

In case of unemployment, we had our own voluntary unemployment plan, or had it before the Social Security Act was passed, but we abandoned that when the unemployment law in New York State went into effect, because it was a duplication.

And in financial trouble or legal problems, we have emergency loans and legal advice through our employees' association.

All of these benefits are given to the employee without cost to the worker, with the exception of part of the life insurance.

Last year we offered the employees an additional life insurance if they participated in the cost of it, they to pay part and the company to pay part. But with the exception of that plan, all the rest of these plans are paid for by the company, except, of course, the employee's Social Security tax.

Senator VANDENBERG. Of course it is impossible to say to what extent the wage dividend contributes in proportion to the balance of your factors?

Mr. FOLSOM. We know it is a very important part of the program, but we can't say that it is more important than the others, or how much of the credit should be due to that and how much to the others.

But we have tried to work out a well-balanced program, and profit sharing is one important part of it. But there are some things which would probably come ahead of profit sharing.

Senator VANDENBERG. I think your schedule that you filed with us, says that you consider the wage dividend as probably the most important single factor.

Mr. FOLSOM. Yes. Well, it would be hard to say, if you put it in terms of what a company should do. First, for instance, there are certain things that probably should come ahead of it, such as fair wages and fair treatment and good working conditions, reasonable hours, and steady employment. You would put those ahead, but after you have those fundamentals, then it is a question as to whether you should go into a retirement-annuity plan, sick-benefit plan, or profit sharing plan.

But in most companies the two work together very closely, if you have a well-balanced company.

Senator VANDENBERG. How long have you had all of these various plans?

Mr. FOLSOM. We started the wage-dividend plan first in 1912; then we adopted the sick-benefit plan next. Then the next plan was the retirement annuity, and the disability and life insurance.

Senator VANDENBERG. When, for instance?

Mr. FOLSOM. The sick-benefit plan came in 1920, and the retirement annuities and insurance plans came in 1928, and then the unemployment-benefit plan in 1931, and the vacation-with-pay plan came last year.

Senator VANDENBERG. But the wage dividend seems to have been at the base?

Mr. FOLSOM. That was at the very beginning and we used, as I have indicated, part of the wage dividend, to finance the retirement annuities and insurance. The cost to the company is the same, but instead of paying it all in cash we pay part in cash and part in the form of these benefits.

I noticed one of the subjects you are going to take up is whether there should be any encouragement of profit sharing by the Federal Government, by incentive taxation. We are not inclined to favor any special tax exemption or the granting of tax awards in order to encourage profit sharing. We do not like the idea of using taxes to influence action of this type, but they should be for revenue purposes only.

We, of course, take wage dividends into account in figuring our income. We don't consider wage dividends as a substitute for wages in any way. We don't take it into account in fixing wages, but for tax purposes we treat it as an income to the individual, and treat it as a deductible expense of the company. So in that way we do get the normal benefit from our wage dividends. We get the credit for that just the same as wages.

Senator HERRING. You wouldn't want that taken away?

Mr. FOLSOM. Of course not, because it is an expense to us just the same as wages are an expense to us, and we count it as a business expense. But we don't—if you go further than that and give an additional benefit—we can't see how you could work out a practical exemption because it would be very difficult to avoid some tendency to have it come out of wages. If you started in with an incentive plan right now, say, if a company were inclined to increase wages—instead of increasing wages they might put it in the form of profit sharing, and it would be very difficult to draw the line, and say what was wages and what was profit sharing.

That is just one point. Whether there might be some way of overcoming that, I don't know. But, by and large, we don't think that a scheme using the taxing bonus in this way is sound.

Now, it is an entirely different story in the merit rating in unemployment insurance. In unemployment insurance most of the State laws have a merit rating or experience rating under which a company that provides steady employment and has few lay-offs will pay a lower tax than a company with considerable unemployment, but that is based on the theory that the company is going to pay for the amount of unemployment which it causes, and the money is actually collected, but instead of assessing all of the people the same way, you vary the tax according to the experience.

This incentive tax would be levied here not for the purpose, primarily, of producing revenue but to encourage employers to adopt this plan, which is a very good plan, but it is a question of whether the principle is right of using the taxing power to bring that about. There are many other things that we think the employers are generally going to find out which will convince them that it is a good scheme, and as more companies adopt it, a greater interest is created in it.

Senator VANDENBERG. Would you also say, Mr. Folsom, that there might be no validity in incentive taxation used to encourage plant expansion?

Mr. FOLSOM. Yes; I am inclined to be not in favor of that, too, because on the general principle that we shouldn't use a taxing power to bring about results like that.

Senator HERRING. We are glad to have your expressions. You understand we are not committed to that; it is something we are looking into.

Mr. FOLSOM. As far as profit sharing is concerned, we are convinced it is very desirable, and it is a very effective method of bringing about better cooperation between the workers, the management, and the stockholders.

Since as in our case, the wage dividend to employees goes up and down with the dividends to stockholders, the employee can more readily appreciate that his and the company's interests are to a large extent, mutual.

We feel that this spirit of cooperation is reflected in the attitude and efficiency and also the longer service of the worker, and naturally in the corresponding benefit to the company.

Senator VANDENBERG. Well, in other words, your social-mindedness is a good investment?

Mr. FOLSOM. Yes; and we don't think that you should adopt any employee-benefit plan unless it is a matter of good business, and we feel that our pension plan, our sick-benefits plan, our wage-dividend plan, is a good business investment, and we have had enough experience, over the years, so that we are pretty well convinced of that.

Senator HERRING. That is in addition to your prevailing wages—that has never been questioned?

Mr. FOLSOM. Oh, yes; we shouldn't consider any of these as a substitute for wages.

This book I have here will give you the details of all these various plans, and I particularly call your attention to the first two pages, which contain a letter written by Mr. Lovejoy, president of the company, which sums up our policy of industrial relations. The first few pages of the book give what we call a code of industrial relations, which explains to the employees the general policies of the management, in connection with this whole program.

Senator VANDENBERG. Let's have one of these books marked as an exhibit for the committee.

(The book referred to was marked "Exhibit 2" and is filed with the committee.)

Senator HERRING. Do you have any other suggestions?

Mr. FOLSOM. None, unless you have more questions.

I would like to have this prepared statement incorporated in the record.

Senator HERRING. It may be incorporated.

(The statement referred to, of Mr. Folsom, is as follows:)

Statement by M. B. Folsom, treasurer, Eastman Kodak Co., November 21, 1938

WAGE DIVIDEND PLAN AND INDUSTRIAL RELATIONS PROGRAM OF EASTMAN KODAK CO.

I am very glad to appear before the subcommittee of the Committee on Finance and to describe the industrial relations program of the Eastman Kodak Co., particularly the profit-sharing plan.

In 1912 the Eastman Kodak Co. adopted a profit-sharing plan and has paid a wage dividend to employees each year since then, with the exception of the depression year, 1934. The plan, which has changed little in principle since it was devised by Mr. Eastman, founder of the business, is a very important part of the industrial relations program of the company.

For many years the company has recognized the importance, in the successful conduct of a business, of a satisfactory relationship between employees and management. Fundamental in such a relationship, it believes, is the payment of a fair rate of wages; the provision of suitable and safe working conditions; reasonable hours of work; stability of employment, as far as possible; and a definite intention on the part of management to see that all employees receive a "square deal."

This industrial-relations program includes the essential features just mentioned, and in addition methods for assisting employees in making provision for their economic security and giving them a share in the financial success of the business. It involves group life insurance, retirement annuities, and benefits for total and permanent disability all provided through a definite plan underwritten by a responsible life-insurance company; payments to employees temporarily incapacitated by illness; a medical service designed to conserve health; personal loans in case of emergency and vacations with pay.

One of the first steps in this program was the adoption of the wage dividend plan under which employees would, in addition to their regular wages, participate in the earnings of the business, after business expenses had been met and a reasonable return had been paid to stockholders of the company on their investment.

The wage dividend is paid by the company as an extra return to employees in the form of a dividend on their wages just as a return to stockholders is a dividend on their investment. It is a recognition of the contribution which loyal, steady, and efficient workers make to the success of the company. Its purpose is to give employees a share in the financial success of the business and afford a source of income over and above regular wages to help employees provide for their future. It also has the purpose of encouraging continuity of service.

Although the wage dividend is dependent upon the company's earnings being sufficient to warrant payment and is subject to annual authorization by the board of directors, payment has been made each year since 1912 except 1934, when the dividends declared on the common stock in the preceding year had fallen below the minimum requirement of the formula for the wage dividend. Improvement in the results of the company's operations led, however, to the resumption of wage dividend payments the following year.

Payment of the wage dividend is made in cash in a lump sum, usually in March. There are no restrictions to the use to which an employee may put the dividend. The amounts increase or decrease as the dividends on common stock increase and decrease, according to an established formula well known to the employees. The wage dividend has never been considered a substitute for wages, and it is not taken into account by the company in establishing wage rates.

The wage dividend rate each year is based on the dividends declared on the common stock of the company in the year preceding. Employees participate in proportion to their earnings for the previous 5 calendar years. All employees except those specifically employed for only part-time work are eligible to participate, provided they worked at least 26 weeks in the preceding year and provided they are in the employ of the company on the date of payment.

The formula according to which the wage dividend is paid is briefly this: For each dollar by which dividends on the common stock during the preceding calendar year exceeded $3.50 per share, the wage dividend rate is one-half of 1 percent of the salaries or wages received by qualified employees within the 5 calendar years immediately preceding the date of payment.

For example, the common stock dividends declared in 1937 were $8 per share, or $4.50 above the minimum required before the wage dividend may be authorized. The rate for the wage dividend payable in 1938 therefore was 2¼ percent (one-half of 1 percent multiplied by $4.50) of the 5 years' wages. For employees of 5 years' service or more, this was equivalent to over 5 weeks' average wages. Employees of less than 5 years' service participated proportionately.

Because of the business recession, the common-stock dividends declared in 1938 declined to $6 per share, and the wage dividend recently declared for payment in March 1939 will be at the rate of 1¼ percent of the 5 years' wages. This will be equivalent, for employees of 5 years' service or more, to about 3¼ weeks' average wages.

The wage dividend paid in 1938 to employees throughout the world amounted to $3,400,000, of which $2,900,000 was paid to 22,500 employees in this country. Over 90 percent of the employees participated in this dividend. The wage dividend to be paid in March 1939 will amount to about $2,200,000.

Up to the present time the company has disbursed in wage dividends, including the estimated amount authorized for payment in March 1939, over $43,000,000, of which $36,000,000 has been paid to employees in this country. The rate and amount of the dividends paid in recent years are as follows:

	Wage dividend—United States only			Wage dividend—United States only	
	Rate [1]	Amount		Rate [1]	Amount
	Percent			Percent	
1930	2¼	$1,980,000	1935	½	$500,000
1931	2¼	2,170,000	1936	1	910,000
1932	2¼	2,170,000	1937	1¾	1,760,000
1933	¼	260,000	1938	2¼	2,900,000
1934	....	....	1939	1¼	1,900,000

[1] Applied to wages paid during the preceding 5 years.

Throughout the years the plan has operated successfully and in the main its objectives have been realized. Employees understand that their share in the profits are dependent upon company operations. In 1934, the one year when no wage dividend was paid the employees fully appreciated the reasons and, if anything, the net result of the one year suspension was a more complete understanding of the plan. There might formerly have been some disposition to take it for granted. Now employees realize more fully how the plan actually works.

While the wage dividend has been an important factor in the development of the general program of the company, it must be remembered that it is only a part of a comprehensive policy of industrial relations.

While one of the purposes of the wage dividend was to enable the employee to provide for his old age, it came to be felt that a definite retirement annuity plan was necessary. Such a plan was adopted on January 1, 1929. It is underwritten by a large life-insurance company and provides in addition to retirement annuities, group life insurance, and benefits for total and permanent disability. The accrued liability for retirement annuities amounting to over $7,500,000 was financed in part by the company and in part by a fund which had been previously set aside by Mr. Eastman, personally, and by the company to be used for the general benefit of employees. The current costs of the plan were met by a reduction in the cash wage dividend formula.

Prior to 1929 the wage dividend had been based on common dividends declared in excess of $1 per share, which seemed a reasonable point at which employee participation should begin. Beginning in 1929 the cash distribution was reduced so that it now is based on declarations above $3.50 per share, and the difference is paid to the insurance company for the current costs of the annuity plan.

This plan has been continued in effect since the enactment of the Federal Social Security Act but has been modified as to the amount of retirement annuity benefits only in such a manner that employees in the future will receive a combined annuity under the company plan and from the Federal Government of approximately what they would have received under the original company plan.

Provision is made for systematic saving and home financing through the Eastman Savings & Loan Association and for personal loans on easy terms to employees in case of emergency. The company's medical department functions for health conservation of employees through care of emergency cases and advice on matters of health. Benefits are provided for temporary disability caused by illness or accident not covered by workmen's compensation payable up to 26 weeks in any one year. Vacations with pay are provided for both office and factory employees. A systematic plan of foremen training helps in the development and carrying out of the general policies of the management.

The sale of many of the company's products, especially amateur photographic goods, is highly seasonal, a large percentage of the entire year's output being sold in the summer months. The management has given close attention to this problem for many years. By careful forecasting and scheduling of production it has been able to arrange its manufacturing program at a fairly level rate throughout the year, producing beyond current requirements in the fall and winter in order to meet the peak summer demand. In consequence marked stability of employment has been achieved with comparatively few seasonal lay-offs. This policy has been worth while, not only from the point of view of relieving employees from the difficulties attendant upon seasonal lay-offs but has been profitable to the company by reason of being able to maintain a stable work force and a high percentage of plant utilization.

We believe this whole program has been worth while. It is not possible to measure the results in dollars nor can we say how much of the success we may have had has been due to any one part of the program. An effective and highly skilled working force has been maintained, and except in periods of severe depression, steadily employed. Labor turn-over has averaged under 10 percent for a number of years. We have been able to attract and hold a highly desirable type of worker. About half of our male employees have service of 5 years and over, and more than one-third of the men have service of over 10 years.

We notice one of the subjects to be covered by the subcommittee is the encouragement of profit sharing by the Federal Government by incentive taxation. We do not favor the establishment of tax exemptions or the granting of tax rewards in order to encourage profit-sharing plans. We believe it is unsound to impose or withhold taxes as a means to influence or direct action of this type, but that taxes should be levied for revenue purposes only.

While our wage dividend is not taken into consideration in fixing wages, for tax purposes it is regarded as income to the individual and as a deductible expense of the company. That affords the company the only normal benefit to which we believe it is entitled.

We doubt if a compensatory tax exemption to promote profit-sharing plans would be practical. It would be difficult, if not impossible, to apply a method of determination that would avoid in all cases a possible tendency to lower wage rates to offset profit sharing.

We are convinced from our 26 years' experience that profit sharing is a very desirable and effective method of bringing about better cooperation between the workers, the management, and the stockholders. Since, as in our case, the wage dividends to employees go up and down with the dividends to the stockholders, the employee can more readily appreciate that his and the company's interests are to a large extent mutual. This spirit of cooperation is reflected in the attitude, efficiency, and longer service of the worker and in corresponding benefit to the company.

M. B. Folsom.

Senator HERRING. General Wood?

Gen. Robert E. Wood, president of Sears, Roebuck & Co., Chicago, Ill.

General, I want to say to you that we want to express our appreciation for your cooperation, and the cooperation your company has given us at Chicago. You have been more than willing, sending your men and records to our office to help us, and we appreciate your coming here today, and we want you to help us in your own way.

STATEMENT OF GEN. ROBERT E. WOOD, PRESIDENT, SEARS, ROEBUCK & CO., CHICAGO, ILL.

Mr. WOOD. We have furnished the committee with all our figures of the profit sharing fund at Sears. It started in 1916, and it has been in existence for 22 years. The plan is very simple—the employees contribute 5 percent of their wages or salaries up to $5,000 per annum. That, of course, is entirely voluntary. The company contributes 5 to 7½ percent of its profits before taxes.

The proceeds are invested in the stock of the company and held in a trustee fund. The employees can withdraw their full profit sharing at the end of 10 years. They can withdraw before 10 years in the case of death, discharge from reduction of force, marriage in the case of female employees. Employees discharged for cause before 10 years get their savings back, plus 5 percent, compounded semiannually, and the difference goes back to the fund, goes to the other employees—it doesn't go to the company.

Senator VANDENBERG. General, in the first instance this formula whereby the employee pays 5 percent and you pay from 5 to 7½ percent, that is unrelated to any question of whether the company currently is making large or small profits?

Mr. WOOD. If they make any profits at all they get this 5 to 7½ percent.

Senator VANDENBERG. Of the profits that have been made?

Mr. WOOD. Of the profits that have been made. Now you have the figures, but I can summarize the results.

Since the beginning of the fund, 22 years ago, 70,087 employees have left the fund, either through death, discharge, or marriage. Those employees contributed to the fund out of their savings, $10,929,067. They received cash, or stock, when they left the company, to the value of $49,422,489. So they got almost 5 to 1 on their savings. That takes care of those that have left.

Today there are 38,440 employees in the fund who put in $10,678,328. The market value of their holdings is $42,662,000. So, for the employees in the fund, they have about 4 to 1. Of course it varies, the contributions of the company are divided, so to speak, one, two, and three. Those under 5 years get one; five to 10 years, get two; and those over 10 years get three. So the older employees have about 8 to 1 and the younger employees anywhere between 1½ to 1 to 2 to 1.

In the case of our company we believe the plan has been very successful. However, it is not one that can be widely adopted. It has been successful primarily because the company has been a great money maker and the employee has received the participation in the earnings and also the appreciation of values.

Based on some questions Mr. Despain gave me, I give you my own conclusions, based on a study of our own plan and some of the other plans that have come under my observation.

Profit sharing can't be a substitute for good wages. It must be a supplement to good wages rather than any substitute. In our own company we pay the going wages of the industry; in fact, we try to pay as well or better than that. Our contributions to the profit sharing are additional.

The plan was originally intended primarily as a pension plan to help the employee to accumulate something against old age or disability.

In the period 1930 to 1932, inclusive, it worked out practically as an unemployment-compensation plan, because we had to drop several thousand employees during that period. They got their profit sharing and it worked out that there wasn't any person who left the company with over 10 years' service that didn't get at least 2 years' annual salary. In other words, they didn't go on the bread line.

Senator HERRING. Was that paid at one time or monthly?

Mr. WOOD. The employee the day he leaves can either get his stock or he can get cash, based on the value of his stock at the close of the market that day. He has the right to demand the cash or the stock—either one.

To make the plan successful, sustained and good earnings are necessarily essential. You can't divide profits when there aren't any, and to make it really successful it has got to have sustained profits.

The relation of the capital invested to the size of the pay roll also has an important bearing on the type of profit sharing. For instance, you take a railroad—they have to invest $5 for every dollar of annual sales. We have about $1 of fixed investment to $5 of annual sales. So the ratio is about 25 to 1 between the type of business that has a great big fixed investment and a type of business like ours.

We believe that a successful profit-sharing plan does increase the employees' responsibility, it helps to avoid labor unrest and strikes, and gives the employee a feeling of greater security and unity of interest with the employer.

We believe, if adopted generally, that profit sharing would lead to a more flexible wage scale. Of course, as every economist knows, there is a very serious danger existing in the rigidity of wage scales in this country, in some industries.

We question the effectiveness of cash distributions to the rank and file of the workers. Usually they are considered as part of their wages. Usually they are spent, and not saved. We give cash bonuses dependent on profits, to plant managers, store managers, buyers, and key men, with the exception of our officers. But we do not give cash distribution to the rank and file. That goes to this fund.

We believe firmly in the joint contribution of employees and employer. It creates a feeling of mutual responsibility and trust.

From our observations we think that the greatest fear of the worker today is his insecurity in the midst of a very complex industrial civilization. Anything that tends to relieve that insecurity and that gives the worker a chance to accumulate a modest estate, will make him a more useful and contented citizen.

Every employer can't do it, but those that can, we believe, should do it, and share their prosperity. We think, in the long run, it is not only good ethics but good business, and while this plan was adopted 22 years ago, because the people in charge of the company felt that it was right, and we will go ahead with it, regardless of what happens, we think it would be a fair thing, and we believe it would promote it possibly with other employers, if some incentive were given.

Now how that incentive should be given I don't know, but we think it should be given. And if the company has a prosperous year or a series of prosperous years, we believe in the policy of sharing them.

Senator HERRING. With the employer as well as the employee?

Mr. WOOD. With the employee as well as the stockholder. And it has turned out very well, at least in our case. We have managed to go along and we have contributed altogether about, I think, between $28,000,000 and $30,000,000. There were only 2 years that there was no contribution, in 1932, and I think it was 1921. Those were the only 2 years we didn't make some money.

And I see it from what it means to the families of these workers when something happens. I mean, when there is a death for instance. I gave a widow, the other day, a check for $40,000. One of our men had been there 28 years and was not a man with a large salary, but I see what it is doing for them all the time, and we never ask anybody to belong to the fund. The older employees tell the younger employees to get in the moment they can.

Senator VANDENBERG. Is there any disappointment or uneasiness caused by the fluctuation in your stock values?

Mr. WOOD. I don't think so, Senator, largely because of these old employees. They have seen it vary, they have seen it go up and down. They know by the law of averages that it will come back. The older employees, you see, have the cushion of the company's contribution, they have got the dividends that have accumulated for them, they have got the part that the employees that fall out of the fund have left, and they have got the law of averages.

Since this stock was begun to be purchased in 1916, there has been a great appreciation of value, so of course the real test came in 1932, when stock values were at their lowest, and even then, with the exception of the 2-year employees, there wasn't anyone in the fund that didn't have considerably more than the amount they put in; and those younger employees, any that had to leave the service, we made up and gave them their 5 percent—I mean their savings, plus 5 percent. So there is no one who has ever left the fund that didn't go out with more than he put in. There never has been a disappointed employee in the sense that he has lost any money.

Senator VANDENBERG. What would be the advantage in providing a preferred stock rather than a common, or would there be a disadvantage?

Mr. WOOD. We have been considering it. Of course, during the depression when the stock was low, we felt very safe in buying it. Now we are getting to the point where we feel perhaps we ought to possibly invest in bonds of other companies, or Government bonds. After all, I feel, as president of the company, that it is the heaviest responsibility I have—I mean the investment of this fund—because it is, I think, now the third largest investment trust in the country, $45,000,000—and $10,000,000 of that represents employees' savings.

Senator VANDENBERG. Does the employee have anything to say in the voice of the management of the trust?

Mr. WOOD. He has a good deal to say about the rules of the profit sharing, and who shall get it, and who shall not get it. He has had very little to say about the investment of it.

Senator HERRING. General, in letting these immense amounts accumulate and then paying them over in large sums as you have in many instances, at retirement, you have had the experience of some of these people losing that money?

Mr. WOOD. Yes; and that is another mooted question. We have people who went out of the fund in 1929 with as much as $60,000 and have come back in 1932, looking for a job, without a dollar, and it has been a very much discussed point among the officers of the company as to whether we shouldn't try to protect them further. But of course we feel it is their money, not ours; and all we can do—and we are trying to do that now for those employees over 50 years of age—is that we are advising them to withdraw some of their savings and put it in annuities or insurance. But we never force it because, after all, it is their money.

Senator HERRING. That is true, but do you think that if they were distributed annually they might become accustomed to handling these funds and protect themselves?

Mr. WOOD. No; in fact, after 10 years they can withdraw a portion annually, and we had a meeting last Wednesday, and the greatest thing is to protect the employee against himself, the members of his family who want to get it. They want to buy an automobile, for instance. There are a lot of things. The one thing we always let them do, if they want to do it, is to withdraw some of it to build a home; but we try—they have the right, you see, to withdraw it all after 10 years—but if they once withdraw, they can't come in again. What we are trying to do is to build an estate for them, and as I say, it has worked out because of the prosperity of the company. There have been a great many estates that have been built, of anywhere from $10,000 to $50,000.

Originally they permitted anyone to go in up to the extent of 5 percent of their salary, but we felt that was giving too much to the higher-salaried employees, so we set an arbitrary line of $5,000, a $5,000 salary, which means a $250 contribution. I have 190 shares in the fund, and my file clerk, who has been with the company 19 years, has 160.

Senator VANDENBERG. General, I understood you to say that you would favor the general idea of incentive taxation if it could be practically developed?

Mr. WOOD. If it could be developed.

Senator VANDENBERG. I notice in your very excellent letter of a few days ago, that while you had no suggestions to make in respect to incentive taxation as regards direct profit sharing, you did have some suggestions regarding what might be called the equivalent of an incentive taxation in respect to pension plans. Would you care to discuss that at all? We would be greatly interested.

Mr. WOOD. Not being a tax expert, I haven't developed those.

Senator VANDENBERG. That is the reason why we might stand a little show of getting somewhere.

Mr. Wood. The only thing I see is that if there were some incentive, it might have to be only a mild incentive, and I can say this for Sears, that we are going right ahead whether there is any incentive or not—so I can be disinterested in a sense—but I believe more employers might do it with an incentive. What appeals to me in your general idea, Senator, is this: You take a great many industries, new industries, and, generally speaking, industries follow a pattern—something new is developed, we will say, like the harvester and the reaper. A new industry, it takes it, and is efficiently managed—there is a great deal of money made in the beginning, in the first few years. Then the competition enters in, and then there is usually a struggle for survival, and then a good many pass out of the picture.

Now, in the early days of any industry, when a great deal of money is made, the worker gets his wages, but he doesn't get any of the velvet. I have often thought that perhaps, just as you start a business, you issue preferred stock and bonds and then you issue some promoters' stock or common stock without much value—and you might set aside 10 percent of that stock for a fund like this. You might set aside that right in the beginning. Now, if the firm were unsuccessful, they wouldn't get anything; but on the other hand, if it made a killing or became very prosperous, that might constitute a very large interest for the employee.

Senator Herring. If we were sure they would have the success of Sears, Roebuck, the stock plan would certainly be all right, but many of them wind up with a piece of paper that isn't worth much.

Mr. Wood. I mean, set aside—without the employee contributing anything—set aside 10 percent of the common stock for a profit-sharing fund. If the concern didn't do anything, they wouldn't be out anything. They would have a worthless piece of paper but they wouldn't have paid anything for it. Just like in the case of the entrepreneur or the initiator of an enterprise—he sets aside 10 or 20 percent of the stock for himself. If he wins, it is worth something; and if he loses, he is not out any money.

Senator Vandenberg. Have you found that your system collided in any way with the Social Security Act; is there any conflict?

Mr. Wood. No; except it means an additional burden. When the social-security plan went into effect, Senator, we reserved to ourselves—we notified the employees that a certain amount of what we paid as social-security tax would be deducted from our profit-sharing contribution. So far, we haven't done it, though. We reserved the right, but we kept on contributing both. Last year we contributed, I think it was $2,500,000 to the profit-sharing fund and $2,600,000 to the social security; so we put aside, altogether, about $5,000,000 between our own fund and the profit-sharing fund; I mean, between our fund and the social-security taxes.

Senator Herring. Well, you are convinced that this policy lessens the labor turn-over?

Mr. Wood. Yes; we have always had—of course, the employer fools himself sometimes—but we have always had a very good relation between the employees and ourselves, and the older ones who are in this profit sharing, they are as much interested in the success of the company as I am.

Senator Herring. You have not had labor troubles, have you, to amount to anything?

Mr. Wood. Practically none. Until 2 years ago, in 40 years I think we have never had a strike. We had one in Minneapolis 2 years ago that lasted about 8 days.

Senator Herring. There have been quite a lot of them in Minneapolis?

Mr. Wood. Yes.

Senator Herring. What has been the labor turn-over, do you know, General, about on an average?

Mr. Wood. I couldn't tell you. Of course, we have one source of turn-over all the time. Of our 53,000 employees, 50 percent are women, and they are always getting married.

Senator Herring. You have no plan to prevent that?

Mr. Wood. No; and we encourage them. A girl who gets married, even if she hasn't been with us 10 years, gets her share of the profits.

Senator Vandenberg. Well, if you are in competition with a concern which, let us say, has none of these profit-sharing plans or objectives, aren't you at a mathematical disadvantage with them except as the Government equalizes your situation through a tax compensation of some sort?

Mr. Wood. Well, exactly, Senator. To make it very direct and personal, every year in our business we have one direct competitor. That is Montgomery Ward & Co. We deduct 2½ million dollars from our profits and they deduct nothing, and we have paid over $28,000,000 into this fund, and they have never contributed a dollar. From the standpoint of equity, it doesn't seem entirely fair. I mean, it doesn't seem entirely fair for one firm trying to do the right thing and the other not following along.

Senator Herring. There is no great difference between the wages paid?

Mr. Wood. No; if anything our wages are a little higher.

Senator Vandenberg. Well, there is a point—that is what I am getting at—there is a point in this relationship where there ought to be a leveling compensation.

Mr. Wood. Exactly. We have been able to do it because the company has been unusually prosperous, but in certain industries that leveling compensation you speak of may be just the point that would turn the scale and turn more employers into profit sharing.

Senator Vandenberg. Have you thought at all how that could be done?

Mr. Wood. No; as I say, I haven't arrived in my own mind of how it could be done. I thought the committee would be more competent to do that than I would.

Senator Herring. That is a real compliment.

Senator Vandenberg. I am much obliged.

Mr. Wood. You have got the standpoint I mean of self-interest too. Of course we do count this contribution as an expense to the business. We don't pay a tax on that contribution. But it is an expense that the other fellow doesn't have at all.

Senator Herring. You treat it as an expense, of course?

Mr. Wood. Yes; say of $2,500,000, we get credit for say 15 percent, or $375,000, but that still leaves us $2,125,000 more than the other fellow.

You ask, Senator, about the feeling. Now as I say, it is very easy for an employer to fool himself. He may think he may have a beautiful, happy situation, and his employees may think quite otherwise. But I do think that there has always been a very unusual feeling between the employer and the employees in our company, and I lay a good part of the credit to this fact. The employees know we don't have to do it. I go up every year at the close of the year when we publish our annual report; I have a forum with about 1,500 employees—anybody can come there—and I explain the balance sheet.

Senator HERRING. There is never any question about it, they are satisfied and content?

Mr. WOOD. Yes; they can ask any questions they want, and after all, today that profit-sharing fund is the largest owner of the business, it is the largest block of stock in the business. It runs about 11 percent.

I might also say, Senator, that for a widely scattered company, and so many of these national companies are, I think the only way you can run them successfully is to have the employees with you. If they don't believe in a company, and in the fairness and justice of the company, you certainly don't get the best results, and you can't be watching a fellow in Chehalis, Wash., and Harlingen, Tex., from Chicago. He is more or less on his own. These employees, even in these little places, are interested. They feel they have a stake in the company.

Senator HERRING. And that gives you increased efficiency and lowers your costs?

Mr. WOOD. Yes; that is what I mean by saying that I think it is not only good ethics, but it is good business for the long pull.

Senator HERRING. Well, if you have anything else you would like to suggest, we would be glad to hear you, General.

Mr. WOOD. I have nothing to suggest specifically except I think you are performing a great service in bringing this out, and I believe if American industry can or will adopt it more generally, it will be a very good thing for the industrial situation.

Senator VANDENBERG. There isn't any standard formula that could possibly be created?

Mr. WOOD. No, Senator; the condition of companies varies so greatly, the condition of industries varies so greatly. Take for instance, the lumber industry, an industry where there aren't any profits. Some industries would have great difficulty in adopting this. Also, the industries with a tremendous investment in comparison with a very small pay roll. But there are a great many industries that can do it and should do it.

Senator HERRING. And might not satisfied employees aid in the profits, by increased efficiency and a lessening of sabotage and losses of different kinds?

Mr. WOOD. I think that is so.

Senator HERRING. Doing away with strikes and the loss of some $42,000,000, I think, in the last few years?

Mr. WOOD. I think it would help greatly. Of course, a lot depends on the good faith of the management. If you go into it you have got to go into it for keeps, and not tell them one year that you are going to give 10 percent, and the next year 1 percent. You have got to stick with it.

Senator VANDENBERG. Might you not get some approach to the incentive-taxation idea through the Social Security Act taxes, pay-roll taxes?

Mr. WOOD. You might give a credit on your Social Security taxes, a part, perhaps, of what you contribute to your profit-sharing fund.

Senator VANDENBERG. Exactly.

Mr. WOOD. That would seem the easiest and most feasible way of doing it.

Senator VANDENBERG. That is not so difficult, is it?

Mr. WOOD. I don't see any difficulty in it.

Senator VANDENBERG. Well, it gets a little simpler as we go along.

Mr. WOOD. You take our particular case: We pay $2,600,000 in social security to the Government; we pay $2,500,000 to our own fund, of which we get credit for $375,000. That leaves us $2,125,000. You might make a credit of $200,000, $300,000, $500,000—depending on what you are doing or what you think fair.

Senator VANDENBERG. And the moment that was done the employer who was not eligible for the benefit would be far more inclined to try to apply some such system to his own operations, wouldn't he?

Mr. WOOD. Yes, sir.

Senator VANDENBERG. He certainly would.

Senator HERRING. And if it promotes increased efficiency and lowers the cost of business, it might increase taxes, which the Government would collect from the ultimate business made more prosperous?

Mr. WOOD. It might.

Senator HERRING. Well, I think that is everything, General.

We want to again tell you how much we appreciate your cooperation.

Mr. WOOD. Any way we can help, we would be very glad to do so.

Senator, would you care to see the statement given to the employees at the end of the year?

Senator VANDENBERG. I certainly would.

Mr. WOOD. I just picked these at random.

For instance, this girl is an employee in the Trenton, N. J., store. She put in $55 last year. That meant her pay was $1,100. She earned a little over $20 a week, and the company put in $67. The dividends from the other employees were $62. For her $55 she got 2¾ shares of stock last year, so she got 2¾ of about $200, against her $55. Altogether she has paid $335 and has 13 shares of stock, which are worth about $950, and she isn't in the 10-year class either, so she has received 3 to 1.

Now, here is the manager of that store. He is a higher-paid man. He put in $195 last year. He had $3,900; his salary is $3,900. He received for that $195, 10¼ shares of stock. That made it about $730. He got nearly 4 to 1. He has put in $1,433, and he has received 57 shares, which is about $4,000, and he isn't in the 10-year class.

I wish I had brought along some of the fabulous ones with 20 or 25 years' service. It goes up to two or three or four hundred shares of stock for people that don't get over $2,000.

Senator VANDENBERG. Each employee has one of these separate cards?

Mr. WOOD. That is their statement, given them at the end of the year. I mean, nothing is kept secret from them. They have a right to see this and do receive it.

Senator HERRING. We will adjourn until 10 o'clock tomorrow morning.

(Whereupon, at 3:15 p. m., an adjournment was taken until 10 a. m., Tuesday, November 22, 1938.)

SURVEY OF EXPERIENCES IN PROFIT SHARING AND POSSIBILITIES OF INCENTIVE TAXATION

TUESDAY, NOVEMBER 22, 1938

UNITED STATES SENATE,
SUBCOMMITTEE OF THE COMMITTEE ON FINANCE,
Washington, D. C.

The subcommittee met, pursuant to adjournment, at 10 a. m. in room 312, Senate Office Building, Senator Clyde L. Herring presiding.

Present: Senators Clyde L. Herring (chairman) and Arthur H. Vandenberg.

Senator HERRING. Is Mr. Fuller present? Mr. Fuller, I am certain you are familiar with the purposes of the resolution and the work of this committee. We appreciate your coming here to help us this morning. We are going to permit you to make your own statement in your own way, and we will try to think of some questions to ask afterward.

STATEMENT OF WALTER D. FULLER, PRESIDENT, CURTIS PUBLISHING CO., PHILADELPHIA, PA.

Mr. FULLER. If it is agreeable to you, I will go ahead with the prepared statement I have, and then I shall be delighted to answer any questions that are germane to the subject.

I should like to begin my statement with a bit of simple philosophy. It seems to me to be far more practical to approach our problems, whether they be personal, corporate, or political, along channels of natural human impulse rather than counter to such channels.

For countless thousands of years people have been persuading other people. Compulsion has always been the minority impulse. Compulsion receives much more publicity and attention than persuasion, but it is not the natural way of human life. "You can catch more flies with molasses than with vinegar" is a simple expression typifying this concept.

If we accept this philosophy, and I do not see how we very well can do otherwise, then we should approach the problems of your committee from that angle.

I prefer to discuss the "incentive taxation" subject first. I realize that you are probably already facing a contention that the acceptance of the premise that taxation may be used for any purpose other than revenue is wrong. Advocates of this principle will contend that the use of taxes for any form of persuasion is merely a sugar coating and that if we accept that theory we must also accept the use of taxation as a means of coercion. I do not agree with this contention.

An automobile is capable of great good and also of much damage, but I do not refrain from using it because it might do damage. Food sometimes gives us indigestion, but we do not stop eating for that reason. There are medicines which in an overdose are a deadly poison and yet under proper safeguards and with competent handling their usage is invaluable.

I reserve my right to disagree with the methods of incentive taxation that may be proposed if I do not agree with them, but I certainly favor strongly the survey which your committee is making and I can see the possibility of great good in properly worked out and safeguarded plans for incentive taxation.

I believe that an extremely productive field for you to investigate would be the building and heavy machinery industries. Certainly there is no branch of our economic life that has suffered more during the years of the depression. What are the reasons? There are probably many, but I suggest that the rates of depreciation allowed under our tax laws have been a major factor in the delayed recovery of these capital-goods activities.

What is the first question that the board of directors of a corporation or of a bank will ask when a replacement building or replacement machine is suggested? It is, "How far is the old one written off?" If the depreciation reserves approach a complete charge off, then there is little difficulty in securing approval for the replacing building or replacing machine, provided there is no other objection to the project. But if only a relatively small portion of the original cost has been set up in the reserves, then it will take a very strong reason backed by convincing economy figures to secure consent for the expenditure.

Progressive businessmen everywhere advocate reasonable and regular charges for depreciation—they also generally prefer to charge off their physical assets at a more rapid rate if their profits will warrant such action. The insistence of the present tax laws on minimum tax allowances has defeated this procedure which would be highly desirable from the point of view of social economies.

For example, I can quote the experience of one company which 25 years ago built a large and elaborate building. It cost about $8,000,-

000 and still stands in that company's list of assets at about $4,000,000. The bricks and mortar are the same, but the building and machinery industries have traveled a long way in 25 years, and this company would be glad if it could now construct a new plant. But to do so would require the taking of approximately a $4,000,000 loss in the current year because the building in question would have little or no value except for its present use.

It is unthinkable that the stockholders or directors would authorize such a loss in this time of thin earnings and small profits, for the building is not inefficient—it merely lacks some of the advantages, working conditions for employees, and space of a newer structure.

Thus a 5 or 6 million dollar plant is not built at a time when work and employment is badly needed.

But during the 1920's this particular company would have gladly reserved the full value of its plant—as a matter of fact, I happen to know that they asked permission years ago to charge building depreciation at a 5-percent rate and were refused by the tax examiner.

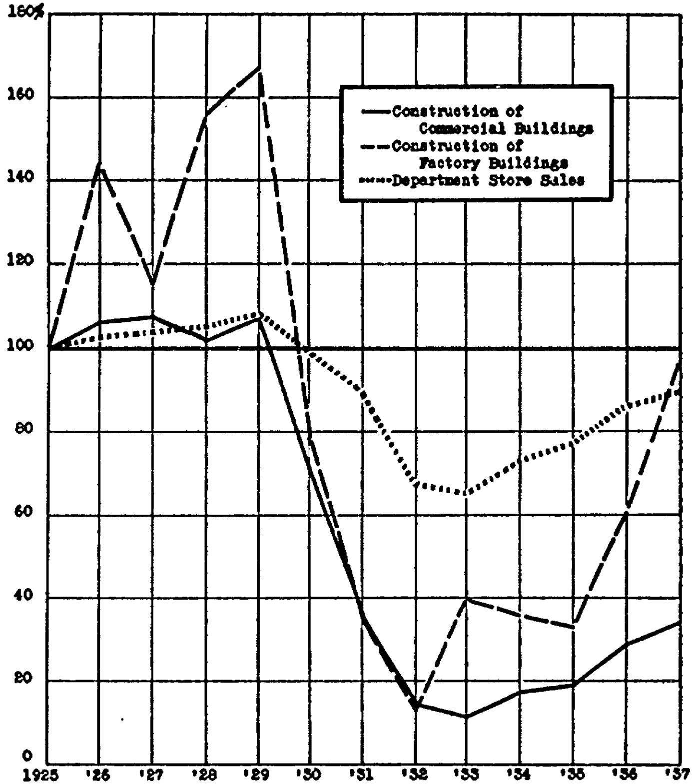
If they had been allowed to follow their inclination, the full amount needed would now be available for use. This one company is quoted merely as an illustration—as an individual it has no significance, but when you multiply this illustration by the tens or hundreds of thousands of other concerns similarly situated in this country, it is possible to see what a very powerful stimulus to building and heavy industry the free right to charge off assets might mean. The fact that a taxpayer may charge off what he pleases in his own books, although he may only include in his tax return that stipulated percentage as ruled by the taxing officials, is of no value because most concerns will not set up in their reserves more than the amount of the tax allowance.

There is a further advantage to such a process. The reserve would be largely accumulated in the profitable years when the withholding of such money would cause no trouble either to workers or to stockholders—in many cases it would be spent in depression years since costs would then be lower and the work would be badly needed. The accumulation of these reserve funds in advance of need might also at times ease a concern's expense situation during a depression and thus help them to weather the storm, or possibly continue dividend payments, where under the present system such payments must be eliminated.

Gentlemen, I have here a chart showing Industrial construction and consumer purchases.

These are the figures which back up the chart, and they will be filed with the other information.

(The chart and figures referred to are as follows:)



Industrial construction and consumer purchases (37 Eastern States)

	Value of commercial buildings [1]	Percent	Value of factory buildings [1]	Percent	Total	Percent	Department-store sales [2]
1925	872.4	100.0	326.6	100.0	1,199.0	100.0	100.0
1926	920.9	105.6	471.2	144.3	1,392.1	116.1	102.9
1927	932.9	106.9	375.9	115.1	1,308.8	109.2	103.9
1928	884.6	101.4	508.8	155.8	1,393.4	116.2	104.9
1929	929.2	106.5	545.9	167.1	1,475.1	123.0	107.8
1930	616.3	70.6	256.6	78.6	872.9	72.8	99.0
1931	311.1	35.7	116.2	35.6	427.3	35.6	89.3
1932	122.7	14.1	43.5	13.3	166.2	13.9	67.0
1933	99.4	11.4	127.5	39.0	226.9	18.9	65.0
1934	150.6	17.3	116.1	35.5	266.7	22.2	72.8
1935	164.5	18.9	108.9	33.3	273.4	22.8	76.7
1936	249.1	28.6	198.0	60.6	447.1	37.3	85.4
1937	297.0	34.0	313.7	96.0	610.7	50.9	89.3

[1] Computed from F. W. Dodge figures, in millions of dollars.
[2] Computed from Federal Reserve Board figures.

Mr. FULLER. There are other applications of the idea of incentive in taxation along somewhat similar lines. The extension, for example, of merit rating in unemployment insurance under the Social Security Act as a requirement upon all State acts would establish naturally a strong incentive to maintain steady employment and to eliminate peaks and valleys.

I urge your committee to ask certain of the large national associations such as the American Institute of Accountants, the Controllers Institute of America, and possibly others, to appoint working committees to carefully review the possibilities along these general lines of incentive taxation and to give you the benefit of their experience and study. I am very sure that you would receive ready and willing cooperation and doubtless many practical suggestions.

Obviously there are possibilities for the use of tax incentives as direct aids in the relief of unemployment. I believe such methods should be attempted only after the most careful study and consideration. Action along the line of subsidies to employers for employment, whether the subsidies are direct or concealed through tax credits, in my opinion offers both promise and danger. Witness the controversy which has continued for years over the protective tariff which is frankly defended as a subsidy for employment. On the other hand, the opportunity for a most valuable contribution to our system of taxation and to our whole business structure is very great. Of even greater importance is the emergency need for a solution of the national unemployment problem. I suggest that some means be devised by which promising plans can be subjects of experiment in a limited manner before any general legislation is attempted.

So far as the subject of profit sharing is concerned, all I have to suggest is that you could secure genuine and valuable assistance by asking certain of our large national business associations such as the National Association of Manufacturers, the Chamber of Commerce of the United States of America, and perhaps others, to appoint special committees to study this subject and to report to your committee.

Senator HERRING. Do you have a pension-insurance plan?

Mr. FULLER. Yes.

Senator HERRING. And also profit sharing?

Mr. FULLER. Our own company plans are about like this, sir: We pay regular salaries and wages that slightly exceed, I believe, the customary wage for the same type of employment in our vicinity, and in addition we have in effect plans which we call economy sharing, whereby we take measurable production, measurable savings in waste, measurable improvements in quality, and various other factors of that kind—this is a matter that has taken many years of experience in building up—and we determine, so far as possible, the economy that increase of better production along that line, less errors, more production, and various other things, creates for the company. We then share that saving with our employees, usually on a pretty liberal basis. The great advantage of such plans is that the material is definitely measurable and both know exactly what they are getting, the employee and the company.

In addition, our company pays a 2 weeks' vacation salary to every employee of the plant. There are many other varieties of employee consideration such as illness allowances, and so forth, as is customary in most progressive companies.

Our pension plan is perhaps a little different from those generally in effect. The company maintains a pension reserve; that is, we keep an adequate reserve built up and we pay a pension entirely payable by the company, and at the company's option; the employee makes no contribution to this fund at all. This pension amounts to about $10 a week to employees who pass the age of 65, when they retire, and, of course, they do not get it until they retire, and some of our employees are well past that age who have not retired and they are very valuable to us. Women past 60 are eligible to this same pension of $10 a week.

In addition we maintain, with a large insurance company, a plan which we call the thrift-unit plan, by which the employee pays part of the cost and the company pays part of the cost, which sets up an amount of approximately $10 per week by the time the individual reaches the age of 65. So the employee may receive a pension the rest of his or her life of $10 from the company and $10 from insurance. Of course, if he leaves our employ and objects to the insurance company, he can take take it away, that is his property, he can take that along and do it himself, that is no deal of the company, except that he will have to do it, and the insurance company probably would not write it if it were not a mass policy, but he or she will have an income of $20 a week. Both of these plans will unquestionably be affected by the social-security payments when they start in 1942 and we have already restricted the extensions of the thrift plan.

As you and as Senator Vandenberg know, I am on the Social Security Advisory Committee, and I am fairly familiar with the operation of that particular group and what probably can be recommended. I think it is only fair to say that any company plan is bound to be modified by the Government plan, because it is a very large expense and it is going to be a very much larger item of expense in the future than it has been in the past. Does that answer your question?

Senator HERRING. Yes, sir. Is not the distinction between your economy plan and profit-sharing plan largely in name, inasmuch as when you have increased economies you get increased profits and you pay your economy plan benefits out of profits, of course?

Mr. FULLER. I should not compare them at all, sir, for this reason: The profit-sharing plan, as I interpret it—perhaps that is not your interpretation of it, but as I interpret it, it is a plan by which profits of the company, no matter from what source they come, are used. The economy-sharing plan is a definite sharing of the economy which the employee makes between the company and himself. I have often expressed that this way, sir: If is a grubstake proposition. You are familiar with the old western grubstake, whereby the man was given food, clothes, so forth and so on, and he went off into the hills. If he made a strike, if he came back and had hit something, why, then both the fellow who grubstaked him and he would share. If he did not hit anything, well, the money was just gone and there was no debt. In much the same way we set the men up with machinery and with the tools to work, with the opportunity, we sell their goods for them, we pay them an adequate wage, which is better than the average wage for that particular type of work in the community. They have that as their grubstake. In addition, if they do better than the average, or whatever we call the standard, we then divide what they save with them.

Senator HERRING. As a sort of speed-up incentive?

Mr. FULLER. I would not call it a speed-up incentive, because it is not a speed-up. I do not like the word "speed-up," because that implies a change of quality. We do not want that to go into the picture.

Senator HERRING. You established your pension plan in 1928, wasn't it?

Mr. FULLER. I have forgotten the exact year. I think it was about that time.

Senator HERRING. Did you have any definite purpose in it?

Mr. FULLER. Simply the desirability of a pension scheme. At that time—I have forgotten the exact number—we had 35 or 40 old employees whom we had pensioned. They were pensioned on a more or less hit-or-miss basis.

Senator HERRING. Do you think it accomplished the object you had in mind at that time?

Mr. FULLER. Yes.

Senator HERRING. You are satisfied with it, then?

Mr. FULLER. Reasonably so. I do not think any plan of that kind ever is as liberal as the recipient would like it to be.

Senator HERRING. All of this is supported out of profit in the end?

Mr. FULLER. Oh, yes. Of course, on the question of profit sharing, sir, it depends entirely on what you mean by the words "profit sharing." You cannot share profit if you do not have the profit.

Senator HERRING. No.

Mr. FULLER. Very frequently the companies where there are no profits are the ones where the employer and employee have to work the hardest.

Senator HERRING. Don't you think profit sharing will help to increase profits?

Mr. FULLER. I think it would help in some particular situations, but I personally think profit sharing must be looked at very carefully to be sure there are no injustices, because I think very frequently those that would be most liberal in their profit sharing arrangements might be the ones where the need for stimulation is the least.

Senator HERRING. We agree with you on that, and that is why we are glad to have your opinion on it.

Senator VANDENBERG. I wanted to ask Mr. Fuller particularly about incentive taxation. Before doing so I would like to linger for a moment on profit sharing to this extent: You referred to the merit rating.

Mr. FULLER. Yes, sir.

Senator VANDENBERG. In connection with the compensation laws. Do you think the present unemployment-insurance laws provide adequate benefit?

Mr. FULLER. I would not feel competent to answer that, Senator.

Senator VANDENBERG. Would it not be advisable to provide a surplus reserve through setting aside profits for employees in good years to augment the unemployment-insurance laws?

Mr. FULLER. It would be very desirable. Whether it is economically practical or not, I do not know.

Senator VANDENBERG. In other words, you are not at war with the objectives?

Mr. FULLER. Not at all.

Senator VANDENBERG. You simply question the practicability?

Mr. FULLER. I haven't any quarrel with any of your objectives in this thing, but I think we have got to keep ourselves on the basis of practicability, if we can do it.

Senator VANDENBERG. Senator Herring and I agree on this a thousand percent. I would like to repeat again what the Senator said yesterday—that the purpose of this inquiry is to discover the facts and not to propagate a cause. Let me chat with you a moment about incentive taxation. I do not want to go too far afield from the jurisdiction of our resolution, but I am impressed by some of the things you have said, because I so heartily sympathize with them. You are making an address this evening in Baltimore on this general subject?

Mr. FULLER. That is right.

Senator VANDENBERG. I do not want to anticipate your evening address; but if you will permit me to read one sentence from it, I think it is so strong that I would like to have it in the record. May I quote a sentence from your manuscript?

Mr. FULLER. Yes, sir.

Senator VANDENBERG (reading):

> Is it not logical to assume that if "the power to tax is the power to destroy", that likewise, if properly applied, the power to tax might be the power to construct?

I take it that you believe in that thoroughly?

Mr. FULLER. Very definitely.

Senator VANDENBERG. Then in your statement this morning you carried the possibilities of the application of that theory even to the extent of meeting the direct unemployment problem through incentive taxation.

Mr. FULLER. Yes.

Senator VANDENBERG. In other words, you are thinking, are you, of the possibility of absorbing unemployment through regular channels of industry, encouraged to do so by favorable and compensating Government taxation rather than through a supplemented dole system?

Mr. FULLER. That is very definitely what I have in mind, Senator. You notice that I have very carefully surrounded that with cautions against the reefs and bars and sand spits that we would likely run into. I think there is a channel we can go through, but I think it is a channel through which we must navigate very cautiously so we do not wreck our somewhat fragile new ideas on the way. Do I make myself clear in that regard?

Senator VANDENBERG. Yes; and again I completely agree with you. Have you given any thought to the fashion in which this thing might be done?

Mr. FULLER. I have given a lot of thought to it, sir, but it has been pure surmise. I think it is a matter of study, and again I would strongly urge—I do not know whether it is proper for the Senate to consider it or not—I would very strongly urge that certain of our larger associations, made up of the most prominent businessmen of the country, be asked to appoint special committees to study this very subject. Not regular committees but special committees. I think that would be highly desirable. Then you would receive information and assistance that would be most helpful, and I think the education of the gentlemen that are on those committees would be very worthwhile.

Senator VANDENBERG. You are a practical businessman of long experience, you are no casual theorist. Would you be hopeful that it might be possible——

Mr. FULLER (interposing). I would go beyond that.

Senator VANDENBERG. That it would even be probable?

Mr. FULLER. Yes.

Senator VANDENBERG. That through incentive taxation adequately and properly framed to absorb a major portion of unemployment through regular industrial channels rather than through direct Government expenditures?

Mr. FULLER. I agree with you in every one of the words you used. I would not agree if you said all unemployment, because I think that is too far, but if you said a major portion, or a very large portion—I do not know what the word "major" exactly means—if you say a very large portion I agree with you entirely.

Senator HERRING. You believe that money poured in at the top must trickle down through to where they will get their share, rather than getting it in any other form?

Mr. FULLER. I believe, sir, so far as we have a social-security plan in this country, which I personally believe in—I do not mean I believe necessarily in the present plan, but I mean I believe in a plan of some kind—that the most important thing that we can do for the workers of this country is, first, to get them back to work. That is fundamentally vital to get them back on some kind of a basis, or at least a substantial portion of them. Second, that we put as much into the pay envelope as our economic system will allow us to do; my own personal experience has been that the pay envelope is much the best place to put it. You will find most industrialists will agree on that score.

Senator VANDENBERG. The most specific immediate incentive tax that you appear to have in mind relates to the encouragement of the replacement of a plant that has become obsolete?

Mr. FULLER. Yes, sir. I think that is very definite. I think that the American Institute of Accountants, and the Comptrollers' Institute, these would be of great help to you in that regard. It is their suggestion along that line. Those men are working in fields all the time; they are thoroughly familiar with it and I think would be glad to be helpful. I should mention, as an aside, that one very major form of incentive taxation, that has been one of the bedrocks of the economic policy of this country for a great many years, is the protective tariff. If that is not incentive taxation to create the safety and prosperity of the American workingman, I do not know what it is. It has always been so defended.

Senator VANDENBERG. Of course; I completely agree with you.

Senator HERRING. A member of the staff makes this suggestion. You made the statement that we cannot share profits unless we have them, and that is true. Let me ask you if it is not possible, unless we continue a profit-sharing economy there might be no profit and even no returns on capital, considering the present labor problem? That is the first question.

Mr. FULLER. Anything I would say on that would be purely surmise. I personally think that the thing needs very careful and thoughtful study, gentlemen. I do not think these are things to which you can simply sit down this morning and say "yes" or "no." I would not want to make statements that really ought to be very carefully and thoroughly studied.

Senator VANDENBERG. You have been pretty firm and pretty definite in your unbelief that incentive taxation will meet, in full, the unemployment proposition.

Mr. FULLER. That is right.

Senator VANDENBERG. I assume you would expect that whatever revenue the Government temporarily lost in taxes through the payment of these compensations would be far more than offset by the revenue from the enhanced general productivity of the American system?

Mr. FULLER. Well, the Government of the United States is in business just as we individually are in our companies. The Government of the United States has got to build up the United States, just as we have got to build up our individual companies. It is the duty of the Government of the United States to treat the United States in the same way as you would any other going concern. Now, that means they have got to build up the country, have got to build up as well as take out. It seems to me at times we have got to plow back. We have got to plow back in business. That is why during a depression unquestionably there would be some temporary slight falling off of revenues, which would have to be made up probably from some other source. That is very minor, compared to the long-range view. I think possibly one of our difficulties has been our view at times has been a little too short. We ought to look further into the future.

Senator VANDENBERG. That is like paying a commission to a man to get subscriptions to the Saturday Evening Post, so the Post could increase its advertising rate.

Mr. FULLER. We have got so much circulation now it is almost embarrassing.

Senator VANDENBERG. That is all.

Senator HERRING. Thank you, Mr. Fuller.

Senator VANDENBERG. Mr. Fuller, would you object if I put your evening speech into the record?

Mr. FULLER. Not at all, as long as you do not release it now.

(The address referred to is as follows:)

INCENTIVE TAXATION AND ITS STIMULUS TO BUSINESS

An address by Walter D. Fuller, president, the Curtis Publishing Co., before joint banquet of Maryland Association of Certified Public Accountants, Baltimore Chapter of the National Association of Cost Accountants and Credit Men's Association of Baltimore City, Emerson Hotel, Baltimore, Md., November 22, 1938

On May 18, 1938, the United States Senate passed a resolution authorizing a subcommittee to make a complete study and report to the Senate upon existing profit-sharing systems and upon what advisable contribution can be made by the Federal Government to encourage employers toward desirable social objectives through compensatory tax exemptions and tax rewards.

The subcommittee was promptly appointed. It consists of Senator Clyde L. Herring, of Iowa, chairman, with Senators Edwin C. Johnson of Colorado, and

Arthur H. Vandenberg, of Michigan, as the other members. The director of the survey is Donald Despain and the offices are in Chicago.

The study was begun early last summer and has been proceeding apace. Thousands of letters have been exchanged and there have been hundreds of personal discussions between the representatives of the committee and the businessmen all over the country.

Let me quote from a letter recently received from Mr. Despain, the director:

"We have had a very interesting experience in developing this survey, especially with reference to the study of incentive taxation. The first inquiries dispatched to industrial executives and tax experts brought an almost unanimously negative reaction. We had simply projected the inquiry as to whether taxation might be used from an incentive angle as a departure from the punitive manner in which we have heretofore operated. We simply asked for original thought. We fully appreciated that we were nevertheless entering a virgin forest without blazed trails and, of course, when you do that it is not to be wondered at that a small crop of thought is brought forth. However, the thing which has pleased us, and I might say at times amused us, is that after replying to these original negative reactions with letters presenting premises of thought and advancing some structural form for the foundation of future thought, we have witnessed the development of a virtual prairie fire which has swept the minds of these executives, economists, and tax authorities from coast to coast.

"Within the past 10 days we have had daily visits from individuals and committees from the foremost business groups and industrial organizations in the country. These men have come to seek further lifting of the curtain on this fascinating subject. In the vernacular, their general expression is, 'You've got something there.' There is no question about it—we have started something on this subject that is daily arousing more and more thought and active cooperation."

Let me quote further from Mr. Despain's statement last month in the Illinois Journal of Commerce:

"In authorizing a study of 'incentive taxation' or 'compensatory tax rewards' as a medium for promoting increased employment and establishing better relationship between employers and employees, the committee approaches this survey without preconceived convictions.

"'Incentive taxation' as the antithesis of 'punitive taxation' by which government now harasses business on all sides, offers, if sound in principle, a new philosophy for the constructive application of tax power in many fields of industrial activity.

"In theory it proposes tax rewards to those taxpayers who voluntarily contribute to the material welfare of the Nation.

"Existing programs of taxation penalize success and offer no hope of relief from an ever-increasing burden.

"In brief, compensatory tax rewards envisages a formula for giving practical businessmen an opportunity to solve the unemployment problem—and to be rewarded if they succeed.

"Incentive taxation is a fascinating subject for original thought, and the committee cordially invites constructive criticism and comment upon this interesting theme, since it fully realizes that new horizons are discovered only by intensive explorations.

"To get at the source of the thought which inspired this resolution and the survey now under way, let us remember what has happened in America in recent years. It is safe to say that few men in America would have dared to predict in the year 1928 that within 10 years industrial and business operations would be under the domination of Washington as it is today. So complete has been the transition from freedom of private enterprise to bureaucratic control, accompanied by successive punitive taxes, that today industry knows not what tomorrow may bring forth.

"Simultaneously, a social problem has arisen which has been fomented and fanned by a campaign which for the first time in our history has created class distinction and class consciousness in America. The cleavage is growing. As a result of this arraying of class against class, let us consider some of the outstanding paradoxes to be found in America today.

"In the greatest Nation of individual capitalists on earth—a Nation made superlatively great by capitalism—we find prevailing a condemnation of capitalism and a submissive approval of its attempted destruction.

"We behold a country profoundly conservative at heart accepting radical and revolutionary theories that would have been scorned with contempt and rejected with popular rage only a few years ago.

"We witness a Nation made great upon the principle that 'production is wealth' being lured into believing that we can 'have more by producing less' and even get 'something for nothing.'

"We see the greatest property-owning people on earth believing they can 'protect their own property by destroying their neighbor's.'

"During the strike epidemic of 1937 we witnessed thousands upon thousands of workers whose very bread and butter depended upon the operation and success of the institutions they were attempting to destroy.

"In short, we witness the most successful and really benevolent governmental system ever devised by the mind of man—which in 150 years of its free operation has produced and distributed more wealth than was produced by all the world in all history prior to its birth in 1776, being denounced as unsuccessful, a failure and necessary of complete change.

"In just 10 words, H. G. Wells has recapitulated our national condition—'The situation in America is a race between understanding and catastrophe.'

"Capitalism, private enterprise, individual initiative—the vitals of the American system—hang in the balance. Make no mistake about it, these are on the way out, unless we create understanding among those who control in a political democracy."

I am not here tonight to merely read Mr. Despain's letter and speech, but they set up the picture, and are authoritative and are at least semiofficial. In other words, the subject of incentive taxation that I am talking about is not a mere personal idea—it is a thought that is definitely going places. Gentlemen of your professions and connections will be deeply interested, I am sure.

Let us look at the situation which all of us in business are facing.

Most of our troubles would disappear if we were busy. Increase the turnover of American goods by from 25 to 100 percent and watch the troubles evaporate. Just apply it to your own business—think what a greater volume of sales of your present products would do. What we need are concrete ideas for such an accomplishment.

Relief, W. P. A., social security, and so forth, are all defensive tactics and who ever won a battle by defense? I hesitate to quote the trite old statement that "the best defense is a strong offensive," but it is true. Let's reserve the discussion of economic theory to its proper place; let's regard necessary defensive tactics like relief and W. P. A. as the palliatives they are, not as cures; and let's work together in a real offensive to lick this depression once and for all. We can do it, we American businessmen, if we set our hands to it.

We can do it individually if we must, but we can do it better, more quickly and more thoroughly, if we work together toward our common end.

After all, gentlemen, we face a practical situation. Are you familiar with the recent study of consumer purchases, supposedly of nonrelief families, made this year by the Departments of Labor and Agriculture at a cost to the taxpayers of about $7,000,000? Here are some of their findings. From this study we find the surprising situation that evidently the families of urban America with incomes up to slightly less than $1,500 a year actually spend more than they receive. The large group with the smallest income—those with incomes up to $750 a year—showed an average income of $626 against expenses of $830, or an excess of spending over income of about 33 percent. It is not possible to tell exactly the number of urban families in this country whose incomes are less than $1,500 a year, but it is a big group—certainly well over 50 percent and probably about 60 percent of the national population.

How this great mass of people spend consistently more than they receive is a puzzle, but it seems to be the case. Money from relatives, deferred payments on credit purchases, relief money from various private agencies, borrowed money, previous savings, unpaid grocers' and doctors' bills, etc., all probably have a part.

The Social Security Board in their initial studies several years ago estimated that the income of the average full-time American industrial worker, and that included everyone from the corporation president to the office boy, was about $1,100 yearly. At present over 30,000,000 individuals are registered in Washington under the Social Security Act, and it is now evident that the $1,100 figure is too high—it looks as though the average income is nearer $900. These are facts, not theories or opinions. Thus facts show that well over half of the urban population of this country spends more each year than they receive. How can you expect much popular concern over the balancing of the National Budget when all these millions of personal budgets are not balanced?

In one city, my company, using this consumer survey, was able to set up a market pattern of consumption. Thus we found that half way up the scale of income for the 822,000 families in the city studied, the annual income figure of $1,446 a year seemed to be the balance point between income and outgo. Below that point there generally was debt—above it, generally surplus. Here we found that half of the families which received incomes greater than $1,446 bought 70.3 percent of all consumer goods and those of smaller incomes bought but 29.7 percent. The percentage of sales accounted for by the half of the families with larger incomes varies considerably with the type of expenditure, dropping as low as 63 percent for housing and running over 90 percent for auto expense. The half with lower incomes spend most of their income for sheer necessities such as food and housing. The startling fact is disclosed that an enormous segment of our population at the bottom of the income scale spend for food and housing alone over 100 percent of their income.

The significance of these figures cannot be denied. They show that well over one-half of the urban families of the United States have incomes below the amount they regard as necessary for existence. Such families obviously can save little or nothing. It is equally obvious that they cannot have the things they need and want.

Someway, somehow, my friends, the incomes of a sizable portion of that part of our population during the next decade or two have got to be lifted, or else the needs and wants of that whole group are going to be satisfied in some other way. Remember that today they constitute more than 50 percent of the people—they have more than half the votes. Somehow we—you and I—have got to so contrive that in the future well over 50 percent are on the side of the adequate incomes. How is it going to be done? I hope by businessmen like you and me, both directly and through our great associations. We have a double purpose in doing the job. Not only is self-preservation and the future happiness of our businesses, our families, and ourselves involved, but if we do this job we shall open up new markets greater than any of which we have ever dreamed. The successful accomplishment of this objective might easily mean a 100-percent increase in your business volume within a few short years—and a sound increase at that. Increased production, greatly increased production, and broader distribution, with the lower prices which such production and distribution bring in their train, are in part the answer to our problems.

We all hope for a real solution, I am sure, but we had better be about our business in this connection, because if we don't do it, then these millions of people I have been describing, through the Government of this country, are going to raise their incomes or accomplish the equivalent result in some other way, and in spite of us—they have the votes with which to do it.

The danger is that people, incited by unscrupulous and irresponsible politicians, may try to rush the boat. But I have little fear of this. By and large, the American citizen is a solid and constructive individual and thinks much the same way as do those of us in this room; and if he sees progress, he will be content to wait. But if we do not show steady progress, and if Government finally does the job, then look out, for we may easily end up with an entirely different kind of economic and political system in this country—a system in which liberty will be dead and the rights and happiness of your children and mine may be completely obliterated.

We have our chance; let us make the most of it.

How can we obtain the advantages of private initiative, of individual incentive, and reasonable rewards to those who accomplish desirable results without at the same time reducing all of us to a standardized mediocrity?

Why has America made progress far beyond that of any other nation in the world? Why is the national wealth of every man, woman, or child in America today about $500, as against an average wealth of all other nations of the world of but $30 a person? Why does America lead in the creation and manufacture of automobiles, airplanes, radios, plumbing supplies, and most of the other devices that add to the comfort and happiness of mankind? Why do the 30,000,000 families of the United States of America have as large a total income as all 450,000,000 families in all the rest of the world combined?

Following are some figures quoted from a speech by Arthur Kudner:

"Let us look at some income figures, based on 1936 statistics: In the United States 70 percent of the people have incomes of over $1,000; 30 percent have incomes of under $1,000. In Great Britain, the situation is just reversed; 26.8 percent have incomes over $1,000, 73.2 percent under that figure. In France the ratio is 23.3 percent over to 76.7 percent under; in Germany it is 18.1 percent over to 81.9 percent under; in Norway it is 15.4 percent over to 84.6 percent under; and in Denmark it is 6.9 percent over to 93.1 percent under."

Kudner went on to say:

"We have frequently heard the machine age blamed for the ills of the world. That is a convenient conclusion. But the fact is, the country with the highest income per family has the most horsepower per worker. United States ranks first, with 4.86 horsepower per worker, Great Britain has 2.56, and France has 1.78. Despite all that has been said or is being said against the America we have known, you are still doing business in the best country as well as the best market in the world. The measure of that can be seen, for example, in the typical wage a carpenter earns here and abroad. In Warsaw, Poland, a carpenter gets $1.21 for a day of 8 hours. In Paris, France, he gets $2.20. In London, England, he gets $3.20. In New York, United States of America, he gets $11.20."

These figures are handsome, and they listen well. They are entirely true and accurate, but so is the fact that more than half of the people of the urban areas of this country are still below the income needed for modest comfort. We have done a wonderful job, we American businessmen, we and our fathers before us, but we have our biggest job just ahead. Does the man with a little property, or with his family warmly clad and comfortably fed, incline toward radicalism? You know he doesn't. Does the man who knows that his security and that of his loved ones is moderately and modestly provided for, turn to communism or fascism? He shuns them as a plague. The problem is one of business and economics—the solution is not political, although the helpful cooperation of an understanding and friendly government would probably bring quicker results.

How are the businessmen of America with their associations, and I hope with the cooperation of their Government, to work out their problems. There are too many possibilities available for them to be discussed this evening, but let us look at the possibilities of incentive taxation in this connection.

There is no denying that the present view of taxation, at least by some people, is that aside from its purpose of raising revenue, it can also be used as a means to discourage and penalize different types of economic development, the difficulty being, of course, the fact that persons differ in their judgment of what is or is not desirable. A good many people seem to think that if there is overproduction at any point, the cure is to cut production. It does not seem to occur to them that the cure may be to increase distribution so that all may have more rather than all have less. The change in tax philosophy indicated by the appointment of the Senate subcommittee may mean much to all of us, for we certainly need to change our thinking about the whole question of taxes. Too long have we let an archaic system wreak havoc in our whole economy. Too long has our tax system been despotic and by its injustices brought to naught the endeavors of one businessman after another.

Is it not logical to assume that if "the power to tax is the power to destroy," that likewise, if properly applied, the power to tax might be the power to construct? May it not be possible to make taxation work for us instead of against us, to make it a servant instead of a master? Perhaps through such "incentive taxation" it may be possible for businessmen to so cooperate with a friendly and helpful government that adequate incentives will be given manufacturers to use up and discard their heavy machinery and their old buildings.

We are all familiar with the policy of the Government in restricting depreciation for tax purposes on modern buildings to 1 or 2 percent annually and holding down depreciation on machinery and equipment to a strict wear-and-tear basis. A condition encouraging manufacturers to charge off their physical assets at a much higher rate might give enormous stimulation to the building trades and heavier industries, with consequent great increases in the number of men employed.

It is easy to let one's imagination roam with this idea. Suppose, for example, that with this new philosophy we told the businessman that he would be credited on his tax bill for many of the things he did that were constructive to the general economy. Under such a plan the employer who used foresight and money to expand his plant and provide the most modern equipment might have a lighter burden of taxation than the one who made no such progress. Under such a program the employer who through foresight and planning provided his workers with steady employment, and eliminated the vicious peaks and valleys which cause consternation among employees, might be rewarded for contributing to a better economy, whereas today such an employer is treated just the same as the one who produces at high speed for a short time and then cuts his workers adrift to be cared for by public assistance, to which we all contribute.

Let us presume, too, that the incentive taxation philosophy might be applied as an inducement to steadily increased employment so that the plants which showed more persons at work and a higher pay roll this year than the previous year would be rewarded.

Is this not better than a policy of taxing business unfairly and unwisely to keep workers at a subsistence level on relief rolls—a policy which at the same time fosters additional employment?

Under a system of incentive taxation we might have such an expansion of business and reemployment as we have worked and prayed for during the last 8 years. Men would go marching gaily back to their jobs, with the sort of social security that comes from steady employment. Vacant store rooms might fill up with prosperous businesses, new plants might dot the landscape, and expansion of facilities might no longer be delayed by debate as to whether the additional taxes would eat up the capital as well as the profits.

I leave to your judgment the need for the revision of our taxing system, and I have no doubt of your decision. For today, as you know, the tax collector takes about 33 percent out of the average of every person's dollar of income either directly in taxes or indirectly through higher prices or in deferred payments through increases in national debt.

I leave to your imagination the many ramifications of this promising thought of incentive taxation. What we need to make its benefits effective are willing businessmen and strong business associations, together with friendly and cooperative government.

Taxation may be designed to afford an incentive and will be most valuable and welcome for such assistance, but we must do more than that to get out of this depression of 1938.

The only way we are going to get out of this depression is to trade and work our way out. There is no soft way out; and it needs all the ingenuity and cooperation of all of us to find even the difficult way.

The rising volume of money which has been withdrawn from active enterprise during recent years and which is seeking security rather than profit, is one of the danger signals of today. Other danger signals are the development on the part of many citizens of a hopeless "what's the use?" complex, a belief in high places that unemployment will always be with us and a falling off in the American spirit of ingenuity and adventure typified by a marked decrease in patent applications since the 1920's.

Suppose that the American people more definitely came to realize that all desirable things, whether personal or political, come from production and that only as we all produce more can we all have more. Suppose that people more clearly recognized that the quickest and surest way to beat the depression is by a marked and radical increase in the turn-over of consumer goods.

It is true that such a situation would require a change on the part of Government to recognition that our economy is an incentive economy in more than taxes, that ours is a free people who respond more readily to the pull of an attractive goal than to the spur of compulsion or the ambition-deadening frustrations of restraint. It must be realized that economic activity can only be kept at an efficient maximum by providing incentives for both production and consumption. We must get away from the assumption that the desire to consume is a fixed quantity which does not require stimulation and that the desire to profit through production is so ingrained that it needs to be curbed and regulated rather than encouraged.

What we need is a frank realization of the basic and time-tested fundamental idea which has motivated America through its 150 years of growth and which has built this country. What I am talking about is the need for turning to the fundamental American selling method to accomplish results; the necessity for stimulating the desires, the wants, and the needs of our 130,000,000 population.

American businessmen should never forget the magic of increased turn-over; $100 turned over yearly at a 10-percent profit gives us a gain of $10. The same hundred dollars turned over twice yearly and with the same percentage of profit means more than a $20 gain. Thus, through the process of increased turn-over may come work for more people, lower costs, and better things for everyone. Better selling makes higher turn-over possible.

The fundamental thing is a tremendously intensified desire, a desire so acute that it will simply drive individuals to some way, somehow, find the way

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to satisfy their need. I realize that there are many difficulties in the way of such an accomplishment. As the young lady said, "Everything I want is either illegal, immoral, or fattening." In similar fashion, everyone is looking for an easy way out of the present situation and is unhappy because it cannot be found.

Well, my friends, that is my piece for tonight. I have tried briefly to review the beginnings of what I believe may well be a history-making movement in taxation, I have tried to show the facts and figures which indicate a fundamental but curable fault in our economy, and I have tried to paint a picture of the possibilities of production and of incentive taxation which it is well for us all to ponder long and carefully.

Senator HERRING. Is Mr. Marshall present?

Senator VANDENBERG. While we are waiting, Mr. Chairman, I would like to put into the record a letter from George Doubleday, chairman of Ingersoll-Rand Co. Mr. Doubleday will not be a witness, but he has submitted some very concrete ideas on the subject of incentive taxation, and I think it would be very much worth while to have the letter in the record.

Senator HERRING. It will be included in the record.

(The letter referred to is as follows:)

INGERSOLL-RAND CO.,
New York, October 11, 1938.

(Executive office.)

Mr. THOMAS I. WALSH,
Technical Adviser, Subcommittee of Committee on Finance of the United States Senate, Federal Building, Chicago, Ill.

DEAR MR. WALSH: I acknowledge receipt of your letter of October 4, and thank you for your expression of appreciation of my communication of September 29.

In offering for your consideration the scheme of tax rewards in connection with plant expansion and replacements, I have in mind two things to be accomplished:

1. The setting aside of an imprest fund for such purposes in a prosperous year when the tax reward would effect a worth-while saving to the industry without seriously affecting tax revenues.

2. The expenditure of an imprest fund in a year of slack business, thereby creating more employment, bringing up the business level, with a possible tax advantage to the Government.

Usually in a year of good business, industry feels the need of additions and replacements, but is too busy to make them. When this is followed by a period of depression the incentive is lost and the expenditures are not made, although that is the time when industry might plan and execute such extensions and improvements under a well-considered plan in preparation for the returning tide of prosperity. I would, therefore, suggest the following:

Plant expansion.—That industry be permitted to set aside in a prosperous year an imprest fund for expansion in the plant and purchase of major items of equipment, to be expended over the following 2 years, and that as a tax reward such appropriations be subject to a tax credit of, say, 5 percent, either as a direct reduction or divided as a relief from the undistributed-profits tax, now 2½ percent, and an additional direct credit of 2½ percent, and that this tax reward have a carry-over provision of 2 years.

If expenditures in the following tax year for such expansion exceed the appropriation for the preceding year, an itemized sworn statement filed with that year's tax return would validate the tax allowance of the previous year. Otherwise the statement would show the appropriation, with a list of expenditures made therefrom and the balance unexpended.

With the tax return for the second year following an itemized sworn statement to be filed if there was an unexpended balance, such statement to show the original appropriation, the amount expended during the first year thereafter and also the expenditures for the second year. If, during the 2 years the appropriation had been expended, the original tax allowance in the appropriation year would be validated and if there remained any unexpended balance at the end of the second year it would be restored to the general cash fund and a tax of 5 percent paid on this balance, but without penalty for the over-deduction in the appropriation year.

Replacements.—The same course might be pursued in the case of replacements, with a further proviso that where there is a detailed property record kept any undepreciated value of the asset replaced, less the proceeds of a sale thereof as scrap or otherwise or of a trade allowance toward the purchase of the replacing asset be allowed as a loss, which is now denied where a composite depreciation rate is used.

Home construction or rehabilitation.—Where industry builds houses for sale or rent to employees, a tax reward might be set up on a scheme similar to that proposed above.

Special maintenance.—An appropriation might be made during a prosperous year of funds to be expended during the next 2 years for special maintenance, such as through overhauling of equipment, replacement of defective parts and rearrangement, with a tax reward in the year of appropriation without reference to a deduction of such expenditures from taxable income as an expense in the years of expenditure, during which there might be no tax saving because of a lack of taxable income due to poor business. Tax on any unexpended balance to be paid in tax return of second year.

We do not believe that such expenditures should be out of a depreciation fund.

Very sincerely yours,

INGERSOLL-RAND CO.,
GEORGE DOUBLEDAY, *Chairman.*

Senator VANDENBERG. While we are further waiting, here are some additional letters, Mr. Chairman, that are very excellent, from prominent executives who will not be able to appear as witnesses, and I suggest that we carry in the record a letter from Mr. L. A. Warren, president of Safeway Stores, Inc., of Oakland, Calif.; a letter from Mr. V. E. Bird, president of the Hartford Electric Light Co., Hartford, Conn.; a letter of Tanner H. Freeman, executive vice president of the Associated Employers, Inc., San Antonio, Tex.; and a letter from G. F. Brewer, resident partner of Ernst & Ernst, accountants, of Chicago.

Senator HERRING. Without objection, they will be included in the record.

(The letters referred to are as follows:)

SAFEWAY STORES, INC.,
Oakland, Calif., November 2, 1938.

Mr. T. I. WALSH,
Technical Adviser, Subcommittee of Committee on Finance of the United States Senate, Federal Building, Chicago, Ill.

DEAR MR. WALSH: In accordance with your letter of October 25, we are pleased to give you the following answers to the questions raised in your letter:

1. Suitable tax rewards would encourage us to expand productive facilities.
2. Tax rewards could be equitably granted to those companies who spend abnormal amounts for capital expenditures as follows:

(*a*) Credit to be based on a certain percent of the excess of net capital asset expenditures made during the taxable year over the depreciation charges allowable for the year.

(*b*) Definition of capital assets would be "land and property used in trade or business of a character which is subject to allowance for depreciation as provided in section 23 (1) of the Revenue Act of 1938."

The only other measure, we believe, that would be essential for the encouragement of capital in the resumption of normal activity of progress would be special credits for sharing profits with employees, which was commented upon in a recent schedule of information by employers sent to Mr. Donald Despain, director of survey, at your Chicago office.

Very truly yours,

SAFEWAY STORES, INC.,
L. A. WARREN, *President.*

THE HARTFORD ELECTRIC LIGHT CO.,
Hartford, Conn., November 8, 1938.

MR. DONALD DESPAIN,
Director of Survey, United States Senate,
Committee on Finance, Federal Building, Chicago, Ill.

DEAR MR. DESPAIN: Many thanks for your letter of October 20. It is very apparent that I completely misunderstood your question regarding incentive taxation.

Of course, I wholeheartedly believe that a profit-sharing plan contributes greatly in the establishment of satisfactory industrial relations. Hence it would be a decidedly constructive move for the Government to encourage profit-sharing plans in some way. Incentive taxation would seem a very good way.

It might be said that a graduated tax rate under the 1938 act is a step in that direction, inasmuch as any disbursements in the direction of employee welfare or profit sharing would be deductible for income-tax purposes and would therefore automatically tend to lower the applicable tax rate. The "incentive" is not very pronounced. On the other hand, a provision in the tax law might become very effective in this direction if it were possible to apply a multiple to the amount disbursed for "profit-sharing" purposes in any one year and this product became deductible from net taxable earnings.

On such a basis as I have here suggested, a factor of (2) would seem necessary in order to have the plan become really "incentive."

In the hope that this thought is responsive to your question and that it may be of some slight value, I am,

Sincerely yours,

V. E. BIRD, *President.*

ASSOCIATED EMPLOYERS, INC.,
San Antonio, Tex., October 24, 1938.

MR. T. I. WALSH,
Technical Adviser, Subcommittee of Committee on Finance,
Federal Building, Chicago, Ill.

DEAR MR. WALSH: This will acknowledge yours of the 22d, in which you remind me that hearings are scheduled for the middle of November.

The only tangible and possibly interesting comment which I have thus far been able to stir up comes from our business counselor, Mr. William Aikman. I do know that Mr. Aikman has given this question a great deal of thought. He is a competent analyst and student of taxation problems as they apply to productive industry, and for this reason I believe his ideas on the subject worthy of careful consideration. They are very briefly outlined herewith:

"The plan which I have in mind as an aid in relieving unemployment is comprised in the very simple expedient of giving an added credit to employers of labor in computing net income for the purpose of arriving at the tax liability of employers. I have not worked out the satisfactory answer to the exact credit that should be allowed; but, for purposes of this suggestion, let us say that an added credit is to be given of 15 to 25 percent of the amount of the ordinary pay roll. In addition to the inducement to an employer to increase wages and increase the number of employees, I believe the income-tax revenues would be increased rather than decreased by virtue of the additional credits allowed on the theory that the incentive to obtain this credit would tend to induce added business activity and finally result in more profits in the end upon which taxes would be paid.

"It is true that this is rather an arbitrary proposition to be incorporated in the income-tax laws, but it is well recognized that the income-tax laws are not written upon the equitable theory. For instance, the law arbitrarily provides that capital losses sustained shall be allowable only as to certain percentages of these losses, and then after arriving at these percentages deduction may not be made to exceed $2,000. The law is full of arbitrary provisions with respect to curtailing credits or deductions. There is, therefore, no reason why arbitrary provisions may not be made for additional credits.

"Such a provision in the law would not be unconstitutional merely because it had for its effect a purpose other than the result upon taxation. In a case arising under the Harrison Narcotic Drug Act, having for its purpose certain prohibitions or restrictions, rather than revenue, the Supreme Court in the case of *United States* v. *Doremus* (249 U. S. 86), said: 'An act may not be declared unconstitutional because its effect may be to accomplish another purpose as well as the raising of revenue. If the legislation is within the taxing authority of a Congress, that is sufficient to sustain it.' Another illustration is in connection with the decision with reference to taxes levied upon oleomargarine where a low tax was placed on white oleomargarine and a much higher tax on yellow. It was not in dispute that the purpose of the tax was to drive yellow oleomargarine off the market on account of the fact that it could be sold as butter. The Court, in the case of *McCray* v. *United States* (195 U. S. 27), upheld this tax.

"The only argument I can conceive of that could be urged against this proposal is that there are disparities between different businesses on the proportion or factor of labor in relation to the gross income. Still this could be worked out on the basis of a reverse ratio."

Very truly yours,

TANNER H. FREEMAN.

ERNST & ERNST,
Chicago, Ill., September 6, 1938.

SUBCOMMITTEE OF COMMITTEE ON FINANCE OF
THE UNITED STATES SENATE,
Federal Building, Chicago, Ill.

GENTLEMEN: Your inquiry of August 30, 1938, for an expression of our views in the matter of profit-sharing plans and compensatory tax exemptions has received consideration.

A number of our clients have also consulted with us following receipt of questionnaires from your committee concerning operations of their profit-sharing plans. In the return of such questionnaires you will obtain details of many plans formulated with our assistance, these varying according to circumstances present in each case.

Undoubtedly the extension of the profit-sharing system to a greater number of industries can be brought about with offers of special inducements to employers. The payments made to employees under profit-sharing plans now constitute deductible expenses in computing Federal income taxes of the employer. Under the circumstances any relief from taxation as an inducement to extend the adoption of the profit-sharing principle would have to give recognition to increased allowances; for instance, the Government might consider matching the profit-sharing payments by allowances of a special income-tax deduction equal to the payments made by the employer. The effect of this would be to permit an expense deduction of $2 for each dollar expended by the employer. The cost to the Government of such a special allowance would be the income tax which would otherwise be collected in the absence of the special credit.

The advantage of such a reward or incentive, irrespective of the amount of the allowance, is that it would have a direct relation to the profit-sharing payments made by the employer. It is simple of computation and could be readily verified in the usual examination of income-tax returns. Employers would be quick to observe the benefits of such a plan and this would facilitate the results which your committee desires.

Undoubtedly there are many other ways in which the desired result may be accomplished, and we will be glad to cooperate with your committee in the further consideration of this subject.

Very truly yours,

O. F. BREWER, *Resident Partner.*

Senator HERRING. Come right up, Mr. Marshall. This is W. G. Marshall, vice president, Westinghouse Electric & Manufacturing Co., Pittsburgh, Pa.

STATEMENT OF W. G. MARSHALL, VICE PRESIDENT, WESTINGHOUSE ELECTRIC & MANUFACTURING CO., PITTSBURGH, PA.

Senator HERRING. You are familiar, of course, with the purposes of the resolution and the committee, Mr. Marshall?

Mr. MARSHALL. Yes.

Senator HERRING. Mr. Marshall has been very fine and kind to our representatives, and we appreciate that. We further appreciate your coming here today, and we will let you proceed in your own way to tell us what you want to.

Mr. MARSHALL. Right from this point?

Senator HERRING. Yes, sir.

Mr. MARSHALL. I assume that you are interested in the so-called profit-sharing plan.

Senator HERRING. That is correct.

Mr. MARSHALL. We do not think of it in the Westinghouse Co. as a profit-sharing plan, strictly speaking, but more in the manner of a wage-adjustment plan. That plan itself is founded on an increment monthly which is charged back into the operating expenses at the end of each month. In that feature we think that it is, strictly speaking, not a profit-sharing plan. We first set aside $600,000, which practically takes care of dividends. As the average earnings for any 3-month period rise above $600,000, for each $60,000, 1 percent is added to the total take-out of the employees. This affects employees from the sweeper in the plant up through the chairman of the board.

Senator VANDENBERG. I do not quite understand this $600,000. Is that per month or per 3 months?

Mr. MARSHALL. That is an average over 3 months. That is, we make that an average of 3 months in order to eliminate sudden rises or falls.

Senator VANDENBERG. Yes. All right; go ahead.

Mr. MARSHALL. If the earnings drop below $600,000, then, in the same degree, the total take-out of the employees is lessened by 1 percent for each $60,000, except those under $125 per month. They are not affected.

Senator HERRING. They are not?

Mr. MARSHALL. No. We are taking care, we think, of the lower-paid employee. The drop in these percentages, furthermore, does not affect in any way the fixed rate of the hourly paid man in the plant. His lessening of earning power comes from loss of hours, dependent on the amount of business which we take in.

Senator VANDENBERG. Does not that affect his income?

Mr. MARSHALL. It affects his take-out, but if he is a 90-cent an hour man, that in no way is disturbed. If he is working 40 hours a week, or 30 hours a week, his lessening of take-out is based on the lessening of time.

Senator VANDENBERG. Yes.

Mr. MARSHALL. I think you will be interested in the effect of the plan and how it has operated since May of 1936, because it has passed through now a period of rise and fall in business.

From May 1936, the average monthly increment over and above all take-out of all employees has been 10⅝ percent above the going rate in the community for similar kinds of work. In 1937, it was 13.3 percent, and in 1938, we had the test, when business dropped and we dropped to zero earnings for the month of October, but the increment has risen to 3 percent for November of this year.

The amount of money paid out in 1936, for 8 months, was $4,927,126 over and above their normal take-out. For 1937, $12,100,907.

Senator VANDENBERG. How many employees, for instance, did that last figure affect that you just read?

Mr. MARSHALL. Fifty thousand employees. Of course, in 1938, we dropped to about 43,000.

For the year 1938, to date, $1,783,902.

I should explain what we mean by over and above full take-out; A salaried employee may be making $200 a month; he may have 10 percent under this plan, and that $200 a month is a going rate for that particular job or work in the community; after a very careful analysis of the community work, and his job analysis, 10 percent will be $220, which would be his take-out. Under the plan, if the man is making 90 cents per hour and has the usual standard bonus, which is an incentive plan which we have in our plant, that may bring it to 96 cents. This 10 percent is based on the 96 cents, instead of his negotiated rate of 90 cents.

Senator VANDENBERG. Is that a negotiated rate?

Mr. MARSHALL. The negotiated rate is the 90-cent rate.

Senator VANDENBERG. Negotiated between whom?

Mr. MARSHALL. Between the employees' committee and management. Furthermore, we have a committee composed of the men and management which meets every 6 months to review all rates in the plant. If at that time there are any individual complaints they are taken up and ironed out in the committee.

Senator VANDENBERG. How are the employee representatives chosen?

Mr. MARSHALL. By the employees through their own election, in no way supported by the company, under the Wagner Act. We have had employee representation since 1919, and now we have some organized labor in some plants and no organization whatever in some plants. They are independent, and we take them as they come, with an open policy of meeting them at all times when they choose to call a meeting.

Senator VANDENBERG. Does this plan apply both to organized and unorganized labor?

Mr. MARSHALL. Absolutely. It would fail if it did not.

Senator VANDENBERG. Is it included in the contract with the union?

Mr. MARSHALL. We have no contracts.

Senator VANDENBERG. Go ahead with your statement.

Mr. MARSHALL. That is the statement on the plan. I am subject to any questions, unless you want a brief statement of our industrial relations program.

Senator HERRING. Were the employees consulted in the determination of your wage-dividend policy?

Mr. MARSHALL. The principle of this plan developed through our chairman some years ago, and just through general discussion back and forth among the employees and management; the principle was first adopted in 1932. It was not until 1936 this became a plan in itself. There was no immediate discussion of the plan, but if you go back far enough, it came out of the thinking of the employees and management in their discussions.

Senator HERRING. Did the management lose any control of the plan as the result of that, or do you think it really gained some by this cooperation with the employees?

Mr. MARSHALL. Well, we all gained, the employees and management both. We know that the men gather around the bulletin boards on the 15th of each month to see what the increment is going to be, and we can tell by the buzzing that goes around that there is an interest in the plan. Furthermore, we have a suggestion system, and we know through the increase in the number of those suggestions, in the desire upon the part of the employees for savings in the company, that they like the plan, and they know that through their savings they increase their take-out each month.

Senator HERRING. Is their confidence and their loyalty and confidence sufficient to withstand a period of depression when the profits are reduced?

Mr. MARSHALL. We have passed through that, and we are now satisfied that it is, because the psychology of the employee is tuned to low earnings at the period of depression.

Senator VANDENBERG. Well, you say it is not a profit-sharing plan. I should say it was more than a profit-sharing plan; it is a profit-sharing and loss-sharing plan, in effect.

Mr. MARSHALL. Yes, sir.

Senator VANDENBERG. It is unique, is it not, in that aspect? Is there anything else like it in the country?

Mr. MARSHALL. We know of no plan like it. It was not planned in advance; we just rode into it naturally.

Senator HERRING. Is not their confidence as the result of your taking notice of them, in your consultation on this plan with representatives of the employees, so they know what the conditions are and that they are being fairly treated?

Mr. MARSHALL. Yes; I am satisfied of that, in talking with the men. Then they make certain that the employees have full information as to the financial status of the company. Our managers are meeting in Pittsburgh today, in their monthly meeting, and the finances of the company will be discussed. The plan is they shall go back tomorrow and call together their representatives and give them the information that they received in Pittsburgh.

Then each month there is placed on the bulletin board a complete statement describing the plan. They know just how much they will get and how it will be arrived at.

Senator HERRING. They know it through their own representatives?

Mr. MARSHALL. They do.

Senator HERRING. You do not call that a sharing of management any more?

Mr. MARSHALL. No, sir.

Senator VANDENBERG. Is there any floor below which the net income to the worker cannot sink, or do they take the full risk?

Mr. MARSHALL. We have said when we reach 90 percent of their base rate that the plan will again be reviewed. When I mention that, that is borne out of the experience in 1933, that when you come down to those depths very drastic measures have to be taken if you want to save jobs for some of your employees.

Senator VANDENBERG. Your plan, in effect, makes wages a variable factor in cost rather than a fixed cost?

Mr. MARSHALL. That is right. The cost of this plan is charged back into production at the end of each month before earnings are determined for that month. It is just as if you took each employee and arranged a new rate of pay for him at that time.

Senator VANDENBERG. Have you had any rebellion against this thing? Have you had any labor difficulties during the period that you have been operating under this system?

Mr. MARSHALL. No, sir. As a matter of fact, we felt that anybody who would take from the employees as high as 16 percent, which it was last July, would have to answer for having disturbed that amount of increment per month, and when you are down to zero earnings you are not having labor troubles, because there is no business.

Senator VANDENBERG. What did you do prior to 1936, in this field? Did you do anything?

Mr. MARSHALL. In the way of profit sharing?

Senator VANDENBERG. Yes; or your paraphrase of profit sharing?

Mr. MARSHALL. Yes. Prior to 1936, that goes back a good piece with us, or with my experience in this work. We had a very complicated plan which did not work out, but it was put in with our intention to develop something along these lines. We have now something that we think works with our company. It may not work with other industries or in other parts of the country, but we have 17 plants scattered throughout the East, and it has worked with uniform satisfaction among the 52,000 employees to date.

Senator VANDENBERG. Speaking generally, what were the difficulties you ran into prior to 1936, in connection with the development of these plans? We are particularly interested in discovering the obstacles.

Mr. MARSHALL. I would not say that we had any difficulties, because we had what we call a rate and occupation committee that met each 6 months with the hourly paid men, in an endeavor to iron out any inequalities in their salaries, but this has just grown out of that rate and occupation committee, in a desire to eliminate those controversies before they become evident.

Senator HERRING. Well, you have demonstrated that your plan works satisfactorily even when you have no profits to share.

Mr. MARSHALL. We believe so; we are satisfied it has.

Senator VANDENBERG. You think it increases efficiency and eliminates waste, in addition to making for pacific relations?

Mr. MARSHALL. We are sure of that; we feel certain of it.

Senator VANDENBERG. In other words, it has been profitable for you to be socially minded to this extent?

Mr. MARSHALL. Yes, sir.

Senator HERRING. From your experience, dealing with the 52,000 employees, you think the basis of wage dividend should be discussed and negotiated with the employees?

Mr. MARSHALL. This plan has nothing whatever to do with the fixing of the basic rates in the plant, or the basic salary of the salaried employees.

Senator HERRING. Merely the wage dividend?

Mr. MARSHALL. That is correct.

Senator HERRING. But as to wage dividends, you think that that is proper to be negotiated?

Mr. MARSHALL. I would not like to say that just that way. It is dependent entirely upon business. Where the employee has his part in this is in the savings which he can make and his effort toward more efficient work. That is his part in it, not that we worked this out by any discussion with the employees among management. It is entirely dependent upon the amount of business which we receive and the efficient manner in which it is handled.

Senator VANDENBERG. What about your stockholders? Are they satisfied with it?

Mr. MARSHALL. Yes, sir. We have letters from our stockholders. We have verbal expressions from our stockholders, because the more money that we can make and pay the employee, the more money the stockholders are getting.

Senator HERRING. You confirm the proposition that there is no interference with management by handling it that way?

Mr. MARSHALL. Yes, sir.

Senator HERRING. It is suggested by a member of the staff that you stated that your plants showed losses and yet your employees were satisfied. Does this not, in effect, tend to assure at least a minimum return on capital even during years that might otherwise result in losses?

Mr. MARSHALL. Yes; I think so.

Senator VANDENBERG. In other words, this is mutually advantageous?

Mr. MARSHALL. Mutually advantageous.

Senator VANDENBERG. What have you to say about the other phases of our work, Mr. Marshall? Have you any suggestions with respect to incentive taxation?

Mr. MARSHALL. I am not prepared to say that that would have any effect—I am speaking now of our own company—I am not prepared to say that that would have any effect on our attitude toward the cooperative work of our company with our employees.

Senator VANDENBERG. Speaking generally, have you any ideas on the subject of incentive taxation?

Mr. MARSHALL. There are so many different conditions that enter into it that I would hesitate to make an answer on that.

Senator VANDENBERG. I notice a sentence in a letter from your committee, reading as follows:

> We believe that if a sound method of compensatory tax exemption were worked out in an act, it would contribute greatly to the general public welfare.

Mr. MARSHALL. If it were worked out; yes; but I do not anticipate whether or not it can be. I say if it were, no doubt there would be some saving.

Senator VANDENBERG. The problem is to find it.

Mr. MARSHALL. It is problematic, of course.

Senator VANDENBERG. Is it compulsory—and I suppose it is—that every employee has got to operate under this system?

Mr. MARSHALL. That question was raised by others. We have not had anyone express himself as not desiring to be under the plan. I cannot imagine employees who would prefer not to be under a plan where they might get as high as 16 percent added to their total take-out per month.

Senator VANDENBERG. It is compulsory in its persuasiveness?

Mr. MARSHALL. It is to me.

Senator VANDENBERG. I think that is a tremendously interesting contribution you made, Mr. Marshall.

Mr. MARSHALL. I have a copy of our wage and salary payment plan, and some data that I would like to leave for your record.

Senator HERRING. It may be included in the record.

(The matter referred to is as follows:)

WAGE AND SALARY PAYMENT PLAN

There are two features of the wage and salary payment plan that tend to equalize and level out the effect of the plan both to stockholders and employees:

1. The total payment to employees, including the additional amount under the plan, is charged to cost of operations in the month in which earned and before determining the net income for the month, which is used as the basis for calculating future months' participations. It is this feature which in our opinion takes the wage and salary payment plan out of the category of bonus or profit-sharing plans.

2. The divisor of the equation for any month's calculations is determined as a function of the basic pay roll (gross pay roll minus adjusted compensation) of the previous 3 months. The principle back of this feature is that as total dollars pay roll increases it should require a larger increment of earnings to finance 1 percent adjusted compensation; and, vice versa, as total pay roll decreases it requires less increment of earnings to provide 1 percent of adjusted compensation.

The simplicity of the plan is, in our opinion, the key to its ready acceptance by the employees; the rules are simple and the monthly application of these to earnings can be clearly shown and bulletinized.

The net income used as the basis of the calculations is after all additions and deductions from operating income, such as normal reserve requirements, provisions for Federal taxes, provisions for depreciation, obsolescence, etc.

WESTINGHOUSE ELECTRIC & MANUFACTURING CO. WAGE AND SALARY PAYMENT PLAN

The wage and salary plan applying to hourly paid and salary employees of Westinghouse Electric & Manufacturing Co. is as follows:

The basis of the plan is that the company's net income for any consecutive 3 months determines the pay that each employee receives for the next succeeding month. The wages and salaries thus determined are regularly included in the cost of operation.

When the average of the monthly net income of the company (net income is shown on line 27 of the monthly consolidated earning statement No. 2–A) for a 3-month period is $600,000, the employees receive, for the next succeeding month, their base rate of pay.

When this 3 months' average net income of the company is greater than $600,000, then each $60,000 of the increase (about $600,000) results in 1 percent increase on the base wage or salary of each employee for the next succeeding month—so long as the average base pay roll of the company for the same 3 months is not over $5,000,000.

When the average base pay roll of the company for the said 3 months is greater than $5,000,000, then the amount of the average net income (above $600,000) which will result in a 1 percent increase of base wage or salary for the next succeeding month is the figure which bears the same relation to $60,000 which the average base pay roll of the company for the preceding 3 months bears to $5,000,000.

When the 3 months' average net income is less than $600,000, that portion of each salaried employee's base rate salary over $125 per month is subjected to a 1-percent reduction for each unit of $60,000 that the net income is below the $600,000 average.

The plan will not automatically vary the rate of pay for hourly rated employees when the 3 months' average net income of the company falls below

$600,000 per month—nor will it automatically vary the rate of pay for salary rated employees when said net income of the company falls below zero.

With all wages and salaries depending upon the net income of the company and varying each month in relation thereto, an incentive is provided for harmonious, efficient, and profitable operation beneficial to all interests concerned in the welfare of the company.

INDUSTRIAL RELATIONS,
Pittsburgh, Pa., August 1, 1938.

THE STORY OF 9 YEARS AND A BILLION AND A QUARTER DOLLARS

How This Amount Has Been Dispersed to Suppliers, Employees, Stockholders, and Others

1929–37

WESTINGHOUSE ELECTRIC & MANUFACTURING CO., AND SUBSIDIARY COMPANIES

Statement of operations, 1929–37

	Dollars	Percent
Income:		
1. During this 9-year period we received from our customers for Westinghouse products which they purchased from us	$1,234,461,000	....
2. And from our investments (dividends, interest, etc.)	26,852,000	....
3. Which gave us a total income of	1,261,313,000	100.0
Disbursements:		
4. We paid out for materials, supplies, fuel, transportation, and other expenses	491,112,000	38.9
5. We set aside to replace plants and equipment as they wear out	58,036,000	4.6
6. And paid in interest on borrowed money	383,000	....
7. While Government tax collectors (Federal, State, local and foreign) required	42,292,000	3.4
8. These disbursements (items 4 to 7 inclusive) amounted to	591,823,000	46.9
9. Which left for our employees, for our stockholders, and for future needs	669,490,000	53.1
10. Of the amount shown in item 9 our employees received in wages and salaries	589,091,000	46.7
11. And group insurance premiums and payments to the employee annuity fund amounted to	15,253,000	1.2
12. Which left net earnings, available for stockholders and for future needs, amounting to	65,146,000	5.2

WESTINGHOUSE—1929 TO 1937

The financial history of these 9 years is of interest to many—particularly to those who, having been Westinghouse men or women throughout the period, have had a continuous part in making that history.

The 9-year period was selected for this summary because late in 1928 the financial year of the company was changed to coincide with the calendar year.

The period 1929 to 1937 also has included both good and bad business conditions.

Of further interest are the following figures published by the United States Treasury Department for all manufacturing companies in the United States for the period 1929 to 1935 (the figures for 1936 and 1937 have not yet been completed):

All manufacturing companies in the United States

Total income (corresponding to line 3)	$330,709,960,000
Employees' salaries and wages (corresponding to line 10)	62,743,726,000
Net earnings (corresponding to line 12)	7,348,668,000

Published by industrial relations with the cooperation of the accounting department.

AUGUST 1, 1938.

Adjusted compensation, wage and salary payment plan

	1936		1937		1938	
	Percent	Amount	Percent	Amount	Percent	Amount
January	------	----------	13	$790,602	9	$555,145
February	------	----------	13	804,185	4	219,408
March	------	----------	14	937,838	3	170,671
April	------	----------	15	1,184,609	1	58,337
May	9	$511,849	15	1,095,971	3	100,979
June	11	599,116	15	1,129,154	5	251,537
July	13	755,300	15	1,199,427	3	156,318
August	14	762,442	16	1,244,067	1	51,503
September	9	492,230	15	1,121,625	------	----------
October	8	489,834	13	1,031,690	3	160,000
November	10	562,033	12	833,319	------	----------
December	12	754,321	10	728,475	------	----------
	10¾	4,927,128	13⅚	12,100,907	3.7	1,623,902
						[1] 160,000
						1,783,902

[1] 1938 to date.

NOTE.—$600,000 or bust.

Senator HERRING. We thank you for coming, Mr. Marshall. We will adjourn until 1:30, at which time Mr. Verity will appear.

(Whereupon, at 11:05 o'clock, a recess was taken until 1:30 p. m. of the same day.)

AFTERNOON SESSION

(The hearing was resumed at 2 p. m., pursuant to the recess.)

Senator HERRING. Without objection, we will place in the record a statement by Mr. W. G. Marshall, vice president of the Westinghouse Electric & Manufacturing Co., in addition to that which he stated this morning.

(The statement of Mr. W. G. Marshall, vice president, Westinghouse Electric & Manufacturing Co., is as follows:)

The Westinghouse industrial-relations program is built around its employees and the public through the employees. The purpose is to keep all employees fully informed in detail as to the activity and operations of the company. Each month the managers from 17 operating plants are called for conference in order that policy might be discussed and established.

Concurrent with this the industrial-relations managers of the 17 plants are called in for discussion of industrial-relations problems. Upon the return of these two groups to their respective plants, the policy which has been developed is put into effect.

Information is thus advanced through the managers with the employees' committees through collective bargaining. Information is further presented to the employees through posters, letters, company magazines, and leaflets.

The company provides an educational program whereby employees may advance in education up to the degree of doctor of philosophy, the latter being in cooperation with the University of Pittsburgh and Carnegie Institute of Technology.

Classes in foremanship training are continued throughout the company at all times.

A savings program is established whereby both principal and interest is guaranteed to the employee by a company interest rate, being 4 percent upon the amounts up to $500 and 2½ percent on amounts above $500.

A group-insurance program is carried on in a cooperative way with approximately a hundred million dollars insurance coverage. The labor policy is well defined, in that collective bargaining has been and is now carried on with representatives of the employees' own choosing.

Senator HERRING. We have here Mr. George M. Verity, chairman of the board, American Rolling Mills Co., Middletown, Ohio, and Mr. Charles H. Murray, director of public relations, of the same firm.

Mr. Verity, we appreciate your cooperation, and we will permit you to proceed in your own way with any information you wish to give us.

STATEMENT OF GEORGE M. VERITY, CHAIRMAN OF THE BOARD, AMERICAN ROLLING MILLS CO., MIDDLETOWN, OHIO

Mr. VERITY. Mr. Chairman and Mr. Vandenberg, we are very glad indeed to have an opportunity to tell you of our experience in human relations, because, after all, they are the foundation of all human progress.

I would like first to give you a rather condensed statement of what we call profit sharing in all its phases, and that condensed statement will give us a basis for any discussion in as much detail as you like.

So, if you will indulge me to that extent, I will be very glad to present this statement.

Senator HERRING. Yes.

Mr. VERITY. All personal-relations work performed in the interest of employees, all incentive plans, all special compensation over and above standard wages and salaries comes under the broad heading of profit sharing, as we see it.

In the days of hire and fire of 40 years ago a fair day's work for a fair day's pay was considered the standard of excellence on the part of both employer and employee.

Men worked for their pay, and that alone; and management had not as yet envisioned the possibilities of cooperative effort.

Those old yardsticks are gone, never to return, as cooperative effort is now essential to modern industry.

The cost and quality of present-day manufactured articles which are placed within the reach of such a large majority of our people can only be attained through coordinated cooperative effort, where men and women, the great army of workers from top to bottom, are putting the best they have in interest and effort into their work.

Cooperation is the product of understanding, confidence, and good-will, supported by policies, plans, and programs that give men every sound incentive to work with rather than for their company, and to put their best effort into their work, whatever it happens to be. There is no place where the old adage, "United we stand, divided we fall," is more effective than in modern industry.

Human life will do and dare, work and serve, in proportion to the necessities, urges, and incentives that surround it. That applies to all of us. Without special incentive, few men will do more than they must.

Incentive plans must be numerous and varied to fit into the many different kinds of difficult work a part of modern industry. There is no panacea in human relations at all.

In our experience we have always felt that actual profit sharing as such, as is generally understood—that is, a sharing in net earnings at the end of a considerable period—should only be applied to those responsible for management, whose work can only be measured by final results.

All incentive plans or programs that permit men to earn more than a mere fair day's wage for a fair day's work can and should be considered profit sharing, as they represent the only practical way to provide a fair distribution of the fruits of industrial progress.

Men engaged in manufacturing operations are acquainted with production problems; they understand the cost of the various operations they perform; they know what waste, loss, and defective production means, and they fully understand the value of quality. They are not familiar with the problems of management or with all of the factors that go to make up profit and loss as shown on the trial balance sheet. They can understand a production bonus or any other incentive plan which rewards meritorious service as and when performed. They prefer to work under some plan that gives them their fair share of results secured as they go along, rather than to wait for a distribution of "profits" which they do not understand at the end of some definite period. They prefer a direct reward and continuity in the payment of their compensation, whatever it may be.

Practical and effective incentive plans applied to those in productive effort makes a reward to management based on profits possible. Management profit-sharing plans are not operable until a reasonable return to stockholders has been created and reserved.

Modern industry provides additional profit sharing for all of its employees, both management and men, through programs carried out for the benefit of them all, irrespective of the individual things that are done.

Where parks, playgrounds, and recreational facilities of many kinds are maintained and sound community conditions and community institutions are supported, they affect the social, educational, religious, cultural, and recreational lives of them all. Such surroundings and conditions as make life more worth the living outside of their working hours could not be created and supported by individual workers on their own initiative.

All of these profit-sharing plans, taken as a whole, not only give men better direct and indirect returns for their contribution to the constructive work of industry, they give them a greater interest in their work and in the success of the joint effort of their associates, which provides that sort of expression for which every normal human being craves, and insures a more stable economic and social order.

Now, by all this I mean that we, in our development have endeavored to impress our men with the fact that we are going to be fair in all our dealings with them, that we are going to let them understand the problems of the industry. What do we have to do to hold our jobs? If we hold our jobs, the business succeeds. What are the policies under which they are going to work? Where do they come in? What are the opportunities for promotion? What effect is it all going to have on them?

We have followed this policy from the very beginning. Definite incentive plans and what we call profit-sharing plans were not inaugurated until 1917, and it was not until 1921 that we had reached a place where we could begin to capitalize our experiences and to do still more effective things.

All work in human relations, like everything else, is progressive, and its effectiveness depends upon the soundness of the policies under which you are trying to work, all of which will be very clearly divined by the men.

There is no use to think that you can fool a group of men by glossed-over statements. You must state what you are going to do, and then you have got to do it. Whatever policies or programs you have, must be carried out, they have got to work, and you have got to be consistent in all the things you claim you are trying to do.

Now, we know, as we have studied human nature, that being consistent is one or the most difficult problems we all have to meet. It is all right for us to want to do things and to have certain policies which govern our lives and work; but to always be consistent in those policies, that is another matter; and nobody in the world is a better judge of that than the practical man who is doing the work of the world.

So you have got to make those policies and programs clear. You have got to live up to them consistently. You have got to show them that they will work, and the worker has got to be shown where he comes in.

Our early conception of human relations was that of getting the confidence and the goodwill and the cooperation of the men; that first, they had to have a much better understanding of their jobs and of industry itself. What are the problems of industry and what are the particular problems of their particular industry? What are the competitive problems? What are the production problems? What are the sales problems? What are the financial problems?

When men understand those problems and understand them clearly, our experience has been that they are always glad to leave the job of management to somebody else.

But when they understand them it gives them a better idea of what they must do, what they must do on their part to make the whole thing work. It is a question of having a workable program.

Now there is no workable program that doesn't take into consideration a fair return to everybody involved—employees, your clients, the public at large, and your stockholders. They must all have the same fair consideration. If you are going to favor any one group as against the other, be lopsided in your application of fair policies, that will disclose itself very quickly. You must be consistently fair to all of the different elements that make industry possible. Each of them is necessary.

But the first thing that is necessary, which sometimes the stockholder doesn't understand—the first thing that is necessary is to have the goodwill and the cooperation of the worker. You may have all the machinery and equipment in the world—the best you can get from time to time—but if you don't have the cooperation and goodwill of the worker that machinery is going to be very ineffective.

So that must be done first, not after the stockholders' return; but it must be done before you get any return to the stockholders.

So we started out in our early experience, which was backed by much of necessity—our company started very small 38 years ago—in fact, it was about the smallest it could be and perform the operations that it did; it started out at a time when its competition was the largest company in the country, who controlled maybe 65 percent of the production of the country, who had all the capital in the world and a lot of experience; and we didn't have either capital or experience. Our only hope was to put such an effort into our job to capitalize the experience of the individual, to get his goodwill and cooperation, so that we could in our humble way serve our customers and compete in the markets of the world.

So that our whole effort from the beginning was how to get the goodwill and the legitimate cooperation of our workers. Now, we had to apply those same policies to the other groups, but that was the first thing. And we followed that policy from the beginning. Our early experience taught us much. We found that while the men that we first employed were a part of the older day—the older "hire and fire" day—their fathers had lived in those older days; and they themselves had lived in the day of "hire and fire," where it was just a job and where some one man owned a mill; and you either did what he liked or out you went; so we were fortunate in getting a small group of men who were responsive to that sort of a program, who had the ability to understand, while it seemed a little strange to them; and for a long time, of course, they were looking for the "nigger in the woodpile"; it sounded too good to be true.

But they were responsive and were willing to go along and feel their way and give us a chance to prove that what we said would work would work. We got that chance from that first group of men. That was the beginning of our industry through that effort. If we hadn't had the goodwill of that first group of men, hadn't made them believe in our honesty of intention, I don't think our company would have ever been heard of.

That was the beginning of things. Now with that beginning we have gone along through the years and, as our business has grown through cooperative effort, we have been able to broaden our ideas on human relations, to build up plans for a special compensation, which have been changed constantly. You can't have any one set plan or plans. Times and conditions change, and you must adjust your plans to meet the changes. But from time to time we have created such plans as would give men—first it would convince them that they were going to be treated fairly, that they were going to have an understanding of things, that there was going to be no mystery about the business.

Next, that there was going to be every fair chance for promotion, and no favorites played; and that they would be rewarded in proportion as our joint efforts made possible.

They realized very early that profits had to be earned before they could be distributed, that unless we did a good job we couldn't pay good wages, that we could have plans for special and regular compensation that were good only in proportion as they worked, and in no other way.

And so I say, as time has gone on we have broadened those plans so as to apply them to the different groups, and of course during

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all of that time you would be amazed if I had the time to describe to you what a marvelous change has taken place in the processes involved, in the kind of machinery used, in the kind of work that is done.

We are not in the same business today as we were 35 years ago at all. It is an entirely different business. Tools are different, the problems are different, the products are different. We are making products that nobody could conceive could be made in those days.

So as time went on and those more difficult things had to be done, we had to treat the subject differently, we had to encourage men in all lines of inventive and productive effort, to solve those difficult problems.

Management does not solve the intricate problems of production. Management, in cooperation with men, solves them, but it is the practical man on the job who can see things and tell you things, that the man in the office can never see, whether he is an engineer or an inventor or what; that is really the man that counts. The man that is dealing with the operation every day can see things and if you are willing to let him tell you, and he will tell you, and you can get an awful lot from the experience of the men all up and down the line—there isn't any man employed in a company that can't tell you something worth while at some time or other if you encourage him to tell you.

So I say our plans have broadened as our work has increased and has become more difficult and complex and has changed. We have gotten away from the old back-breaking, common labor entirely. We don't have that any more. That is done by machinery. But our difficult work, our processing work, has multiplied time and time again. Where our products used to be a finished product, today it is only begun. Things we have to do to that product to make it serve our customers, makes necessary a long line of processing to change the structure of those machines to make them do the things, the difficult things, that have to be done, and that we have had to learn how to do.

It has taken a different type of men, and today we are employing three times as many men in work that did not exist 25 years ago, as we employed in the jobs that have been displaced in the common labor jobs.

So I say we have had to adapt our human-relations plans to all those changes; our mutual relations plans, our incentive and profit sharing plans to all of these changes.

And we have not only done that, but through our inauguration of what we call "mutual interest"—we call our plans mutual-interest plans—through the inauguration of those plans and getting the interest of the individual where it wasn't just a job any more, he had an interest, he was a part of something, he is having a chance to express himself—through that, and as the demands of the industry broadened, we were able, through the interest and cooperation of these men, to develop new methods, new equipment, new and ingenious ways of handling operations. And not only as to methods, but as to products.

Now, out of it all—to make a long story short—after over 25 years of cooperation in meeting the changing conditions in an industry, changing equipment and changing products, that group of men—and you have to give them all credit for it, because they all contributed—that group of men worked out an entirely new method for the manufacture of sheet metal, called the "continuous mill."

For a hundred years certain mechanical operations were necessary for the reduction of a steel ingot into a light sheet. The rolling of rails, of wire, and of bars was always continuous. That has just developed and been refined. But sheets—there was a lot of hand labor, hand manipulation, to rather coax a big heavy piece of metal down into a thin piece, get the right gage, and to get the right surface on it. There was a lot of skilled hand labor involved in that thing. That method was prevalent for some seventy-five to a hundred years.

Some of our men felt that it could be done in a more mechanical way, more like a paper mill is operated; that a big ingot could be taken and run continuously down a long line of machinery and come out a finished product, rather than have so much intermediate work. So after a good deal of time and effort, and, of course, expenditure, a mill was devised and built which enabled us to take a large steel ingot and gradually process it down to a sheet, through continuous operations. We were able to produce three or four times as much tonnage, change all the jobs, and revamp the thing entirely.

Now that method which has cut the cost of our product in two in 15 years, and which has multiplied the number of men by two or three times, had so many economic possibilities in it that it has been adopted by the entire industry.

I only tell you to show you that it was a product of cooperation, the whole scheme was not possible because of the work or brains or experience of an engineer or two; it wasn't possible. They had the idea, but it was worked out in conjunction with practical men of long experience, who were so close to us that we could talk to them about this and that problem. It was a myriad of intermediate, detailed problems that had to be solved before that could be worked out, and it is because they were all interested in it, even though a lot of them knew their jobs were going to be greatly changed, that it was possible to work it out at all.

That is one of the outstanding large accomplishments of a definite practical scheme of mutual interest and cooperation among a group of men of all types which it takes to make up a business like ours.

Now, I say we have changed our plans, we have broadened them, so that today we try to—you can't have any plan that applies to a lot of different types of work at all—we have production bonuses and we have incentive plans of all kinds applying to different men. We have a sales bonus, we have a production bonus here and another production bonus there, and we have an incentive plan for foremen, and we have a profit sharing plan for the managers, and we have tried to have something practical to affect every single group of men that has anything to do with the conduct of that business.

Senator HERRING. Do you define those as profit sharing, all of those?

Mr. VERITY. We claim that in its broadest aspects—not as profit sharing is understood today—but in its broadest aspects all those things would have never come into being if we were simply paying men a given wage for certain work; they would never have been possible. So that is profit sharing that has come out of our mutual cooperation and they have helped themselves, as I will show you, immeasurably. It has all been proved to them that it was practicable.

Now I say that these plans have all changed, but today we have something which is subject to change any minute, that applies to every group, so that they don't have to wait for a distribution of earnings, but they feel they are being compensated as they serve, for the kind of service they perform.

As I will explain to you, our hourly wage rate and our yearly compensation is higher than our competitors'. That isn't just something philanthropic on our part. Our men do more, they produce more, and they get more results, and we pay them for those results. So they are paid directly as a part of the cost of production, not waiting until we can figure out the profit and loss on the balance sheet. They are paid in proportion to what they do. We feel that if anything will incite ultimate profit, that will, because when men exert their extreme efforts, where men are interested in their jobs, and their hearts and hands are working together, in waste loss, in tonnage, all the things that go to make up a finished product that you can sell for primes, has a tremendous bearing—and when they found that through careful effort and through mutual interest they could perform their work in a way that they would get larger returns for themselves, and their company would be more successful, there is no trouble to sell a man a plan like that.

Now we have done that as best we could, continually from year to year, right up to the present day, and it has brought returns to the men that speak for themselves.

So, of course, the proof of the pudding is always in the eating. It is all right to say that our men have been happy and they have worked together and they have done efficient work. All right, what has it all amounted to? Have they made any more than other men that worked differently, and have we got better results than other companies, and how has it worked?

Well now, I could give you one little illustration that I think will be helpful, to show you that these things can't be done by management alone, they must be done in a cooperative spirit.

We were the first to inaugurate the 8-hour day in the steel industry. We had it going some 3 years before it was generally adopted. It was considered impossible. Tradition was so strong for the 12-hour day and a lot of the employees were so used to it, that a lot of the men themselves didn't want it changed. Some did. Our men had indicated, at different times, that they thought it would be fine if we were to have a 3-shift mill, working 8 hours instead of 12. We said, "All right, boys, we will see what we can do." Nobody in management sat down and mapped out a plan for an 8-hour day. No—the managers sat down with the men, department by department, not the mill as a whole, because each department has its own problems. We sat down department by department with the men themselves and said, "Now, boys, if we are going to add another crew here, if we don't get any better results we are sunk, there won't any of us have any jobs if we just arbitrarily add another crew and add that much to the cost of our product; so let's sit down and see what we can do to offset this extra cost. Can we get more tonnage, can we get as good quality by adding another shift, adding another crew of men?"

And they said, "All right; we will be glad to help." So the members of management and the men themselves sat down with the managers, as I have said, and they figured out what they could do. They had an objective, a worth-while objective. We couldn't have done it alone at all. But through the help of the men in that first department, which happened to be in the first operation, the big blooming mill, where you reduce an ingot to a slab, in a very short time we figured out how the tonnages could be so increased that we could take care of another crew of men without any additional cost to our product—total cost.

That was put into effect. Then, department by department, we went through that same story. Now, there were some departments where we had a distinct loss, but, taken as a whole, in the operation of all of our departments all over the mill when we got through we just about broke even. In the actual final cost of the product we were just about at the same place we were when we had the two-shift mill. But we had a happier lot of men; they were working less hours; they were able to do more work in 8 hours than in 12; they worked more efficiently and more happily, and in some cases we got considerably better results because of it.

Now, I tell you that to show you how all things must be cooperative in an industry to get you anywhere at all. Management can't just arbitrarily plan, like a set of engineers and architects, how things are going to be done. If you work with the men that are practical in all the different phases of your work whatever can be done will be done sooner or later.

Now, to get right down to facts, the steel industry as a whole in 1937 had an average hourly rate of 82 cents. Now, gentlemen, that 82 cents compares with 15 cents an hour for common labor and 25 cents an hour for skilled labor when I first went into the business 38 years ago. Common labor was 15 cents and mechanics were receiving 25 cents.

Today all hourly wages in the whole industry, all jobs, boiled down to an average of 82.4 cents per hour.

Armco's average at the same time was 96.1 cents per hour. Taking all lines of manufacture, it was 69 cents.

You have heard a different gentleman here tell what income their men have. All industry was 69 cents, our industry as a whole was 82, and our own company was 96 cents an hour.

Now, to boil that down in hourly wages is one thing, but the question is, Does a man get enough hours to do him any good? That is the vital question. If he doesn't get work enough, the rate per hour don't mean much.

So that in 1937 the average income to industrial workers was $1,415; the average earnings in the steel industry was $1,581 per year; the average in Armco was $1,774.

Senator VANDENBERG. When you speak of "Armco" you mean the American Rolling Mills Co.?

Mr. VERITY. Yes, sir.

There are times when that has hit as high as $2,000. This is the average for the whole year. In 1937 you must remember we had a very active operation for 7 months and then a very inactive operation for the rest of the year. So that didn't represent a year of full operation, where the men would have made much larger annual earnings if the whole year had been worked out on a favorable basis. So that, in dollars and cents, shows what happened there.

Now, according to our psychology, and based on our own experience, that phase of industrial life is not the concluding factor at all. That is the fact, that our men have earned a little more than other men, the amount they actually earn in dollars, but that is not the largest contributing factor in their happy relations with our company by any means.

We might be paying as much as that, arbitrarily, in the way of wages or anything; we might be paying more than that to our men, and we might have a very unhappy and a very unsatisfactory relation.

So after all it isn't profit-sharing per se, or the result of incentive plans, the dollar result from those plans, it is the sum of all the things that a management can do to make life in a job in the mill more worth-while, and to make life in the community for the men and their families more worth-while.

We have come to feel that community life is one of the largest contributing factors to the efficiency of men. If men's families are happy in their community life, the community gives them the things they want, they are happy in their social relations, the man comes to work in an entirely different frame of mind, and is a different kind of a man than if his family was unhappy or the community conditions were bad.

So that anything and everything that has to do with community life has a great bearing on it. But in the first place, gentlemen, it is the having men believe that they are going to be treated fairly. Our men not only believe it but they know it through long years of experience. They know that there are certain definite company policies that are going to be followed, and while they can't tell just how they are going to be applied to this, that, and the other situation, they know that those definite policies of fair treatment are going to be applicable to everything the company does. They are not concerned about the fairness of it at all, but how it is going to work out, and how much help it is to them.

So it is the sum of all the things that an industrial family can do, the little and the big, conditions in the mill and outside, their chance for promotion, their chance for expression—if a man has a chance to suggest something from time to time, nothing gives him a greater uplift. The fact that he has suggested something that they put into effect, that has worked, is a tremendous stimulus; whereas if he had never had a chance to suggest anything, and he is working in a humdrum way, he won't be the same sort of a man at all.

So, according to our psychology, the problem of management today is to get out of men the good that is in them, to encourage them and develop them.

Now, you can't do that by treating them unfairly; you can't do it by putting them in refrigerators and freezing them; you have to thaw them out and let them work under favorable and pleasant conditions, and give them those incentives that make human life struggle for better things, feeling that in proportion as they work, they will serve, and in proportion as they serve, the whole thing will go ahead and they will be better off.

So after all, it is the sum of all these things that make for a satisfactory or unsatisfactory and efficient condition in industry. The money side is important, of course. If they know they are as well off as everybody else, or a little better off, in money, that is one factor, but in our opinion it is not the concluding factor. It is the sum of all things, the money return and the things that make their life worthwhile, that govern men in determining whether they are going to put the best that is in them into these things.

Now, there are millions of people in this world that never had a chance to do their best at anything, and if they did, it wasn't appreciated; so when men have a chance to do their best and a chance to have that best appreciated, then men will work and strive as they will not do under any other conditions. We have proven that, not over a few months but over a period of 38 years.

Now, in the results of that, not only the wages that I tell you have been possible but during that time, during those 38 years, from the very beginning, when we and our men were strangers to each other, and where they had come from the hire-and-fire days, they listened, and were willing to give us a chance. They put us on trial, while we put them on trial, but because of that feeling of friendliness that was established from the beginning, our company has never lost a pound of product because our men weren't willing and ready to work when we had the orders.

And a man has never lost a day's work because there was any conflict or dissension or disagreement among them jointly, any labor disagreement of any kind that made it impossible for us to carry on our business.

We have had a chance to work together and meet the problems that existed, whatever they were, and we have enjoyed our work.

Now that, of course, I think to our mind, and to most anybody else, is one of the most conclusive arguments that can be made for a plan of operation, but now I want to say that we don't claim that our plan or the different things we do can be done just as we do them by anybody else. Somebody else may have the same objective, but their conditions are a little different, maybe their men are a little different, and they have to do it some other way. So after all it is the objective that counts, the policies that underlie things that count, and whether in your own way you do an intelligent job or not.

But in our opinion there is no yardstick by which you can gage profit sharing and incentive, things that affect human life. There is no yardstick. Every group of men has got to get acquainted with each other and work out, in their own way, meeting their particular problems at their particular location. The problems in one mill will be different from another mill; we can't do it the same way in another mill. The set-up is different; it won't work the same way. You have got to be very adaptable.

But we have been able to do that, and with that result.

So that we feel that it has been a great demonstration of the value of real, honest-to-God cooperation, and while we don't claim perfection for it, we claim our men have responded to it and we have had, from period to period, year to year, the best that our men could give us, and it has taken that best for us to meet the problems that we have had from year to year as our company has developed from a small business to a large one; it has taken that best because there was never a time that even with the best we could do we had any very large margin. If we hadn't had that best—now I feel safe in saying that as far as our company is concerned, starting so small as it did with only 350 men, and a half million dollars invested, and 900 tons a month product, and having grown to a concern that has 15,000 men now and can produce 140,000 tons a month of product against 900—I think that demonstrates the fact that the things we have done have paid, and I believe that if we had gone along in a stereotyped way, just figuring that to pay men fairly for what they did was sufficient, as was the custom for so many years, if we had followed that in our little beginning, nobody would ever have heard of our company. We would have never gotten anywhere except for the fact that our men as a whole were willing to contribute more than had formerly been contributed, and they contributed the best they had to the conduct of that business, whatever their jobs might be.

That, to me, has been the whole strength and crux of the whole situation.

Now, with that statement, if there is anything in the way of detail or any questions you would like to ask, I would be happy to try to answer them.

Senator HERRING. You are convinced, Mr. Verity, that this plan, this policy, has really increased efficiency, the efficiency of your plant, and in return has paid its way?

Mr. VERITY. The efficiency has increased constantly. You can't believe how changed an industry could be in so few years; but all the operations that we had, and the work that we did 35 years ago, as we see it today, was tremendously crude, and step by step, through cooperative methods, we met the demand for greater efficiency and better products and lower costs, and all of that. There is no question about that.

Senator HERRING. And you have not had any serious labor troubles?

Mr. VERITY. We never had any labor troubles. We have a happy family.

Senator HERRING. You have a salary-adjustment plan?

Mr. VERITY. We have an incentive compensation plan that affects those engaged in management only. They are the ones that have to wait until there is some profit, and a certain reserve made for stockholders, before they have any compensation.

That is what people would ordinarily call profit sharing, but to us it is only a little part.

Senator HERRING. Do you have any special way of assuring your employees that they will get their profits? Do they fit in and know the actual operations of the business, in any way, as to the adjustment?

Mr. VERITY. Yes; all these schemes, all these plans, that we call incentive plans, as I explained to you about the three shifts, are all worked out in conjunction with the men themselves. That is, they contribute to the plan, and it is their contribution that makes it workable. So, when it is put into effect they are satisfied with it, naturally, because it was largely their own creation. Human beings want expression. They don't want to be stereotyped people, and that is what we are all struggling for, whether we are artists or artisans, or what not; we are trying to have a form of expression, and when men can find that in their work as well as in their homes then they are happy men, indeed.

Senator VANDENBERG. Are you going to indicate the various specific incentive plans that you have, Mr. Verity?

Mr. VERITY. Well, we have a plan, and if you want to have the number of plans, I would like to have our director of personnel, Mr. Murray, give you that, because I don't follow the details. I know what the schemes are, but if you want the number of plans and how they are applied to each group, he would be glad to give you that.

Senator VANDENBERG. Suppose we have Mr. Murray tell us that.

STATEMENT OF CHARLES H. MURRAY, DIRECTOR OF PUBLIC RELATIONS, AMERICAN ROLLING MILLS CO., MIDDLETOWN, OHIO

Mr. MURRAY. This will be somewhat repetitious here, quite naturally.

I have prepared a brief statement here in the interest of continuity, and I would like to present it in the way that it has been prepared.

Any discussion of profit sharing in industry naturally leads to the discussion of the relative merits of all the methods of wage payment, as a profit-sharing plan is one of the numerous methods of paying wages.

From our standpoint, we have always considered that all of the incentive plans in effect within our company are definitely profit-sharing plans. We recognize that any remuneration paid to employees above the prevailing level for any particular job is, in effect, a sharing of profits with the individual members of the organization. It has always been our contention that best results from the standpoint of loyal, effective working organization can best be secured by the payment of direct incentives wherever possible, based on the actual performance or contribution of the individual. In fact, it is necessary to provide sound incentives before the attainment of profits is possible.

To illustrate the type of incentives to which I refer, I wish to briefly outline our own company's wage-payment plans which apply to approximately 14,000 employees.

THE INCENTIVE FOR PRODUCTION EMPLOYEES

Under our incentive plan for production employees and direct production supervisors, a basic rate of pay is established for each job which compensates for the experience, skill, responsibility, and other qualifications demanded of the incumbent. These rates compensate the individual for what is considered a normal day's work established by scientific time-study methods. Premiums are paid for any productive effort above the normal. Under this plan, it is possible for a workman to earn, by developing proficiency, a premium of from 25 to 30 percent above the basic rate of pay in direct relationship to his individual contribution to efficient operation. Such incentives not only fairly reward the employee for his individual part in maintaining the company's operation on a profitable basis, but also provide the means through which the efficiency and effectiveness of operations may be improved to permit and sustain constantly increasing basic rates of pay.

To illustrate how the production worker has benefited by this incentive plan, it is only necessary to look at the amount of premium earned.

In 1935 our production workers, in addition to their basic rates of pay, averaged 18.4 percent premium, amounting to $1,601,704.

In 1936 premiums were earned at the rate of 20 percent, amounting to $2,018,945.

In 1937 the premium earned was 21 percent and gave the production workers extra compensation of $2,354,386.

During the current year, in which the company has operated at a loss, premium is being earned at the rate of $1,250,000 for the year, with drastically reduced operations.

And I might repeat here the figures that Mr. Verity gave you with respect to average hourly earnings: At Armco it is 96 cents; for the iron and steel industry it is 82 cents; for all manufacturing it is 69 cents. That includes these premiums that I speak of, approximately 20 percent in 1937.

Their weekly earnings for 1937 were: At the American Rolling Mills, $34.02; for the iron and steel industry, $30.32; for all manufacturing industries it was $27.

The annual earnings, as Mr. Verity has stated, are $1,774 for Armco in 1937, $1,581 for the iron and steel industry, and $1,415 for all manufacturing.

The benefits derived by the Armco worker, both in the form of increased basic rates of pay and additional reward for his contribution to efficient operation, are self-evident. We are firmly convinced that such results could only have been attained through the use of direct incentives which measure and compensate the worker in direct relationship to his individual efforts and achievements and his influence over those elements of profit over which he has control.

THE INCENTIVE FOR PRODUCTION SUPERVISORS—ANOTHER TYPE OF INCENTIVE

Closely allied with the incentive plan for hourly production workers is our incentive plan for principal supervisors of production departments. These are superintendents of departments. This group is rewarded for effective management of their departments as reflected by their administration of the items of manufacturing costs over which they have control. This plan has resulted in a premium of from 20 to 30 percent, in addition to basic salaries.

INCENTIVE FOR SALES EMPLOYEES

Sales employees receive incentive compensation, above base salaries, for maintaining the volume and character of products sold, and control of selling expense. This type of incentive fairly compensates the sales employees for maintaining production at the highest possible level and securing desirable business. The maximum premium earned under this plan is 28 percent.

INCENTIVES FOR MANAGERIAL EMPLOYEES

Managerial employees, the effectiveness of whose work is directly reflected by the final results attained by the company, as represented by the annual profit and loss statement, participate in a plan of special compensation.

This group includes all those individuals who are primarily a part of the general management, and whose decisions and administration of their functions have an important bearing on profits and losses and the welfare of the entire organization.

However, this group only participates when the company earns a profit, after deducting all charges, including depreciation, interest, and reserves for all taxes, including Federal income and excess-profit taxes, and after an allowance for the payment of common-stock dividends.

Due to the fact that this incentive is only paid in years when the company's balance sheet shows a profit, it has resulted in an average payment, as a percentage of the salaries of those receiving it, less than that received by employees participating under other plans of our company.

Senator VANDENBERG. This is the only point at which the incentive is related to the earnings of the company?

Mr. MURRAY. Yes; definitely; yes; directly.

THE QUARTERLY SALARY ADJUSTMENT PLAN

This is not an incentive, and not anticipated as, or considered as, an incentive plan or profit sharing in any respect. However, it is based on the profits of the company, but is merely a means of reducing salaries and restoring salaries above and below a base.

For a number of years we have had in effect a sliding-scale adjustment plan, applicable to all salaried employees, which at the present time provides for the quarterly adjustment of current salary payments anywhere from 9 percent below base rates to 7 percent above base rates, depending upon company earnings. It will be recognized that salary payments represent a fixed overhead charge which ordinarily does not vary with the fluctuations in volume of business. This plan operates to minimize lay-offs in the salary group, and thus regularizing employment and automatically assuring the salary worker of the highest current rates of remuneration within the company's ability to pay.

Production incentives to hourly employees are paid as a part of current earnings, as I have pointed out, while all other incentives are paid on a quarterly, semiannual, or annual basis.

In establishing our incentive compensation system we have recognized that a separate plan is necessary for each distinctive major group, the nature of the work performed by the individual determining the type of incentive best suited to properly compensate him for his effective effort in the mutual interest of himself and the company.

In addition to these direct incentives, many other forms of indirect incentives are provided, such as vacations with pay, Christmas gifts, group insurance, disability, dismissal, and retirement allowances.

Throughout its entire history our company has enjoyed an extremely friendly relationship with its employees. In the more than 38 years of operations, as Mr. Verity has pointed out, no employee has ever lost an hour's time, and the company has never lost a pound of production on account of a labor dispute. Naturally, our compensation policies alone have not been responsible for bringing about this condition of mutual confidence and respect. However, it is our sincere belief that the incentive program in its entirety has been one of the most important contributing factors.

From the description of these plans I believe you will agree that we have attempted to distribute the fruits of production as equitably as possible among the employees in proportion to their individual or group contribution.

That an equitable distribution has been effected is evidenced by the earnings record of the company.

During the past 10 years, 1928 to 1937, inclusive, we have earned a net average return on invested capital of 2.6 percent per year. During the years of 1935, 1936, and 1937, a period of high-capacity operation, the net annual earnings on invested capital were, respectively, 4.1 percent, 5.9 percent, and 6.8 percent, or an average for the 3-year period of 5.6 percent.

It must be evident from these facts that our company has long recognized and practiced the principle of profit sharing with employees.

Modern corporate life is extremely complex, and there are many factors, both within and without any industrial organization, affecting profits and over which no individual or one group of employees has direct control. In view of this, we believe that our plan of compensating the individual or group for favorably influencing that element of profits over which he or they exercise control achieves more effective results and is more desirable to the employee than profit sharing as it is ordinarily conceived.

In exploring the possibilities for encouraging profit sharing in industry we know that there will be presented to you descriptions of many different types of plans. It is only natural that these plans will differ widely as each company and each industry has its individual characteristics and problems. It is our opinion that the primary purpose of the majority of these plans is the sharing of profits, whether or not the methods employed in the distribution are based on corporate net income.

We believe that it is in the mutual interest of all, and that the most effective distribution of the profits can be attained through the retention of this individuality of methods.

Now we are confident that you gentlemen will recognize that unless these plans are given consideration in drafting any legislation on this subject, these companies which have of their own accord developed plans which fairly and adequately compensate their employees, and result in an equitable distribution of their income, will be penalized and placed at a distinct disadvantage as compared with those companies not carrying out this responsibility to the same extent.

Thank you.

Senator VANDENBERG. I will say to you, Mr. Murray, on that final point, that we are not contemplating the dictation of any formula to American industry. We happen to believe that this country is too big and complex to be run from Washington. Perhaps I had better say that for myself. [Laughter.]

Mr. MURRAY. I am very happy to know that.

Senator HERRING. I think you have covered the subject so thoroughly that I have no questions to ask.

Mr. VERITY. I might add this one point, that, of course, we figure the human side of things is the controlling interest. Capital and machinery and all that are essential, but without the human association they are of very little value. So that in the development of working organization, what we are talking about, men, you must at the same time develop a management. That isn't something you can go out and buy or something we started out with and carried along. The men running the Armco, like this man here [indicating Mr. Murray], are the men that are the products of these 30 years. They started in, most of them, as high-school or college boys, and they have developed executive ability and have drifted into executive jobs or managerial jobs, just as the other men have drifted into more practical jobs.

So we must all the time develop management, men who can be foremen and superintendents and salesmen, sales managers, and that sort of thing.

And that, to our mind, is the only way to do it. We have never followed a policy of going out and buying expert experience that somebody else has raised. In fact, we don't want them; they would be raised in a school that would not teach them what it is all about in our industry. We wouldn't harmonize at all, and the few men that we have brought in, occasionally, have never worked out at all. It is the men who are raised within the company who make their way among their fellow men, and show certain abilities, that finally gravitate into the managerial jobs, that can do that side of things and make the contact with the workers. It is management and men working together that do the job.

Now, as an example of that, and something you may know or may not, at the end of the second year of our early struggle—and believe me, the first 5 years was some struggle—at the end of our second year I employed a young man 23 years old, as night superintendent.

Senator VANDENBERG. The first 5 or the last 5?

Mr. VERITY. The first 5. If an industry can live through its first 5 years, it has a chance the second 5; if it can live through the second 5, it has some chance. But the first 5 is the real test.

This man came along in the first period, the first 2 years, 23 years old, and he was employed as night superintendent in the sheet mill, along with a lot of older men who were supposed to have more experience. This young man who started in, in 25 years he was president of the company. That is the answer.

Senator VANDENBERG. Mr. Verity, have you any ideas on the general subject of incentive taxation?

Mr. VERITY. Mr. Vandenberg, I really believe, from our psychology, I feel that legislation that would reward this sort of thing, or legislation that would penalize not doing it, would be almost equally harmful. In other words, if we had to do any of these things by compulsion because it was the law to do them, we would get no credit for it, and we would get no benefit from something that we were doing because we were living within the law.

Senator HERRING. There was no sort of compulsion contemplated, involuntary incentive merely.

Mr. VERITY. As to what you could do to leave us in a voluntary condition, I really don't know what could be done. I think it is a problem that we have got to work out for ourselves.

Senator VANDENBERG. Your whole theory in your whole plant apparently is based on the proposition that incentives produce results?

Mr. VERITY. Sure.

Senator VANDENBERG. Why does that philosophy stop short when we reach the tax law?

Mr. VERITY. Well, now, I know more about incentives than I do about tax laws. [Laughter.] And just where you gentlemen might find some way to help things, to support it, to make it more effective, that is really beyond me, just so we don't have to arbitrarily do the things that we want to do, and get credit for doing them.

Senator VANDENBERG. I don't want to be arbitrary about the thing.

Mr. VERITY. Now, if our men felt that these things which we do, we had no choice about doing, about half the joy and effect would be lost. It is the fact that we do them out of a spirit of mutual interest, and we do them because we want to do them, that gives them their value. The things that a man does, to live within the law, or to live within the customs of his community, he has to do that to be decent at all. He gets no credit for that. But you show me the things that a man or a group or a company does that they don't have to do—and you get the measure.

Senator HERRING. Wouldn't a compensatory tax benefit or an incentive of that kind be merely extending the profit sharing or incentive to the employer which has worked so successfully with the employee?

Mr. VERITY. Well, from my limited knowledge of law and taxation, my feeling would be that you could help us in a lot of other fields more than that, that is something we have very nearly got to work out for ourselves, "root hog or die." And there are lots of things that can be helped by the Government.

Senator VANDENBERG. I don't think we had better go into that. [Laughter.]

Mr. VERITY. You had better let us work that out.

Senator HERRING. If there is nothing further, we appreciate your coming and you have contributed a great deal to this survey.

Mr. VERITY. Thank you. It has been a great pleasure to do it. Thank you very much for your courtesy.

Senator HERRING. Mr. Charles P. McCormick, the president of McCormick & Co., importers, packers, and manufacturers—of Baltimore, Md.

Mr. McCormick is also the author of Multiple Management, the book which is creating so much interest, and is one of the big sellers.

Just proceed, Mr. McCormick.

STATEMENT OF CHARLES P. McCORMICK, PRESIDENT, McCORMICK & CO., BALTIMORE, MD.

Mr. McCORMICK. I am somewhat at a loss to start off today because of the fact that I question, Mr. Chairman, whether the particular subject that is assigned to me, the philosophy of business, may be just exactly what you want. I am over here, though, to serve you in any capacity; and I have studied, during the last 6 years particularly, a plan of trying to bring labor and capital together.

I feel that I must be a little personal, if you will allow me.

Senator HERRING. Certainly.

Mr. McCORMICK. My first 17 years were spent in Spanish-American countries, in countries where, since that time—for instance, Mexico, Spain, and France—a good deal of communism has encroached. I am not going to get into the subject of why, but I came to an early conclusion that the question of the masses was very much of an answer, and whether we had a democratic form of government, whether we had a king or what not, if the masses weren't satisfied, that eventually there would be an overthrow.

Naturally, getting back into the business at a later time, I saw somewhat of the same situation that I had observed in some of these Spanish-American countries earlier; namely, that the classes in the mills, the youth, and the salesmen were not particularly interested in their work; they didn't have a motive and a reason.

They were being hired, and when talking to, for instance, the youth in our business—and I will make this a personal study of this particular business of mine, and I am not making a cover-all of industry, please understand that—in our business the youth came in and was paid a salary. He was told that some day he might be president of that corporation. All right. That was fine, but that is about as far as it went. The people that had the money and influence and what not ran the business. Somehow or another there was a classification and to clear it we might say it was a one-man type of business. The result of it was that that youth came in for 1 year, 2 years, 3 years, 4 years, or 5 years, and then automatically 50 percent were lost to our business. Fifty percent went out because they weren't interested.

Now, when it came to the factory worker, the type that we have been talking about here, there was another drop even further; and because of lack of education, because of lack of influence or pull or financial ability or what not, they were practically cut out for either a daily laborer or finally to become a factory foreman.

The sales department was somewhat the same thing.

So in 1932, when the genius, you might say, of our business, who built it up to the largest in our field, died suddenly in the middle of the depression, I had to do some deep-sea thinking. So I tried to set up some plans, certain rules and regulations that were simple and democratic, that would help and assist in making what I call a "pride of ownership" in business.

And may I say while you are discussing taxes, tax incentives, and so forth, I still would like to go back to the philosophy of business. Unless a businessman has the proper spirit in the front office, and by that I mean the president's office, and will look at labor and capital, and Government, incidentally, as a third party sitting off seeing that the regulations are applied properly, unless there is a pride of ownership there from the bottom to the top, there is something wrong with that particular business and it is eventually doomed to trouble, whether financial or labor.

There must be some incentive whereby a person entering the business has a peak to shoot for as far as merit is concerned.

So I would like to use this blackboard, if you don't mind. I may bore you a little bit, but it is a system that has been adopted by many. In England it has been adopted by 22 of the largest firms and in this country by over 200 firms from large to small. So, therefore, it is not an experimental proposition or a wild-eyed dream. It is a plan, a definite, democratic plan, by which an entered apprentice, whether he be a youth, a factory man, or a salesman, has his opportunity to start and see ahead of him opportunity step by step.

I would like to start on this philosophy, so to speak. Let's call the old board of governors, senior. Prior to 1932, they were called by us the board of directors. By that I mean the stockholders elect their senior governing board. That, I think, is stable, that is right, and in this system please bear in mind I have tried to preserve all of the good things and add to and build up on a planned basis.

Mr. McCormick was a genius, but often geniuses are autocrats, and that is off the record, please, for the present. He happened to be a very fine man—but for a basis of discussion I want to draw the comparison that I think a great many American businessmen, and I say a good many of them, are dictatorial in method; by that I mean a one-man type of business manager, who insists on knowing all the answers in the front office.

I do not think that is democratic in the first place. In the second place, I don't think it is good for the business. Thirdly, I don't think the employees profit and go up high enough sufficiently to help make that business go ahead.

So, therefore, I found the senior board in this particular case looking to the average type of business in that particular field, for the president of that firm to answer all questions. For instance, the board of directors would meet. The question would be asked, "Are we in favor of this particular package?" There would be possibly 11 "yeses" and 2 "noes." The gentleman in the room with me and myself would say "no" if we thought not. We were always in trouble.

Now, the point I make is this: This system totally explodes that theory that one man can run a business, so therefore we call it multiple management, which is management by many, and at the same time I think you have some safeguards. By the same token these senior board members had gotten to the point where they were not thinking. They were relying on one man to do the thinking for the business. That is wrong, and I still say that in the depression of 1932 that was one trouble with our business, the fact that one man was doing the thinking for it instead of every single person in the business.

So, therefore, we started off on the first step—junior. May I say that this system takes the question of age out of the picture. I still say that we have men in our business, and in every line of business, that at 65 years of age—and I am not saying this flatteringly, sir—are younger mentally than men of 25. That refers to men of 60, 65, or 55. The point that I am making is this: That too many of us, I think, are looking upon the men that have gone through the mill, and have arrived at the stage where they can be conservative—pardon that as a tactical break, but I will make more of them later on, sir—the idea is that these men should be brought in and used as bulwarks of conservatism, and also of thoughtful planning, while younger men in the business come along and step up the tempo of the thinking.

By the same token, I have seen youngsters in our business at 25 that are really more valuable than men at 55 and 60, by virtue of the fact that they have a quick mind; they were not "yes" men and thought the thing out. So when I use the words "junior" and "senior," I do not mean in years. On this junior board we have older men than we have on the senior board that are youngsters. This senior board ran roughly from 45—I was 36 at that time, the youngest member—and the average was 55 years of age. The junior board normally will run around 40 years of age, but you have plant superintendents that have been there 35 years. So, therefore, get out of your mind the fact that this is a junior board in junior executives. It means that these juniors will eventually be on the senior board, running the business as the future policy makers.

So they selected, the factory people down there, and the people in these plants, selected and named 17 persons, the most potential, best, coming young men, not on the senior board, young men of middle age and older. Those 17 men were brought into a room. They were set around a table and they were given this charge, "You may do anything that you desire; you may see our cost books and you may see anything; nothing is secret to you men. You are potentially the future supervisors of this business. These men [indicating senior board] will die some day and you men will step up, so by virtue of that we want you to know the business 5, 10, or 15 years earlier, so that when you go on the senior board you will know the story. Now, we are going to penalize you, however: every recommendation must have your unanimous approval."

By that I meant to convey the impression that if there were 16 radicals and 1 conservative, no radical measures could go through, and by the same token, if there were 16 conservatives and 1 radical, no too-conservative measures could go through.

There had to be a meeting of minds, and a unanimous approval of all those 17.

There is a reason for that philosophy in business. It is because of the fact that if those younger men, who do not know the business as much as the older, do not make unanimous decisions, they may be serious.

Secondly, the second penalty was that after they made this unanimous recommendation it had to go to the senior board or the president for approval.

That gives the juniors the freedom that the senior board has, with two exceptions. It has to be unanimous or the recommendation stops right there, and that is as far as it goes.

I want to call your attention, though, for people who think that younger men are radical and that their ideas are not good, that out of 1,207 suggestions, 6 have been turned down. I just pause to pay my tribute to the younger men.

Now, the idea is because it is unanimous. That is the main purpose of it.

I was particularly interested to see that these men got parliamentary practice, so therefore they elected a chairman and a secretary. I hope I am not making this too slow, but I think I will unveil it, and you will get the philosophy in a minute.

The chairman automatically serves for 3 months and the secretary becomes the chairman thereafter. There is a reason for that. We are interested in seeing that labor sees the capital's side of the picture, if I may use those terms. I don't like either one of them. It gives the man a chance way down the line to step into office, regulate and run the business, so to speak, and still pass on it while he is chairman—and, Mr. Chairman, if you want to find the biggest capitalists in our business, they are these past secretaries and chairmen from down in the factory that have served in that position. They lean backward instead of the other way.

We found that the senior board was really—and I talk very frankly here, because I understand this is a frank meeting—they were rather selfish. These senior men of yesterday were particularly interested in how much income they had, whether their particular friends had so much stock, and so forth. They were interested more in a clique affair. I was interested in these junior board members as they came on the senior board—and there have been five in the last 5 years—I wanted to see that they were unselfish, and the only way to do that was to assign them a job, and that is to sponsor other men coming into the business.

Each one of these 17 junior board members has one man to sponsor. Those boys may be the sons of any one of you people here. I will give you a typical illustration. A youngster applies for a job. He is put through four different people. After those four people pass on him the two personnel men, a salesman, and I pass on him as the fourth one; after he has gotten into the business he is turned over to the junior board for checking up. The junior board gets with these new employees socially and otherwise. They finally pass on them and turn one of these men over to each one of the juniors for 2 months, after which he is assigned to another junior.

Now, the purpose of this, again, is—I am off the subject of taxes today—the purpose is not to teach them how to run the department; it is to give them the spirit, the spirit of the organization, the philosophy of running the business, the pride of ownership, and that type of material, so that they may look at the business as a possible potential possibility for advancement and for happiness in a business way. You may term it "idealistic"; I don't think so.

So, therefore, these 17 men have 17 sponsored individuals. Now at the end of every 6 months, in order to keep this from being a political organization—and again I may be sticking my head out, I don't mean that in the way it sounds—to keep it from being a group that wants to continually stay in office and to perpetuate themselves, we make three of them go off the board. Then there is an opportunity for three of these new sponsored men to come on the board. So in that way, during the course of roughly 5 years, instead of having 17 men we have had, roughly, 76 men go through this course.

Now the next question is—there have been five vacancies here—these have stepped up, these men have stepped up here, and don't forget there is the early entered apprentice, an employee.

That is a very interesting factor, but the more interesting factor that might be interesting to you in this day and age is the factory angle. It is fine for young executives, and there again I caution the

Government to give some consideration to both sides, the factory man over here has just as much merit as the junior men.

So, therefore, we establish the same identical type of board, with the same function of a sponsorship course for the factory. It might interest some of these gentlemen in here who are sitting back there and thinking in terms of dollars and cents, that it was this factory board that, during 1932, ran the business overhead down 12 percent. Now mind you, I didn't say the president of the business did it. I said that these fellows over here, when given an opportunity to run their own business, ran the cost of business 12 percent downward. It is just the difference between profit and loss, incidentally.

Now, the interesting factor again is that these two boards are interchangeable, and you will find often a man coming into the factory with a high-school training eventually making the factory board jump over, through merit again, to the junior board, and eventually to the senior board, and whether he makes an officer or not, that is beside the point.

I would like to make another comment on the factory board. It is this factory board that worked out the 10-minute rest period in the morning and afternoon. For instance, we shut down the plant for 10 minutes. Why? Because it is efficiency, if you want to know the truth of it. It is selfish efficiency. But they worked out that plan, they worked out the 40-hour week long before the N. R. A. They worked out the steady income of so many dollars per week, long before any State legislation. They worked out the vacation period whereby the factory and the junior and the senior all equally worked this proposition out.

Incidentally, just beside the picture, they were the ones that worked out also the 48-weeks guaranteed employment. That is rather unusual, but it is a very necessary thing because I believe business management should try to establish as much as possible a steady earning capacity for workers.

I am fearful of stating this, but it is a frank open meeting. I still believe this, that if labor gets the price of labor up too high, that business cannot stabilize employment. At the same time there are many businesses that can find ways and means of changing, instead of guaranteeing 25 weeks, let them guarantee 30 weeks the next year, and work it up. Our business is no different from the average. Our sales volume runs in peaks, from the top to the bottom, of 58 percent. So, therefore, you can see we have three depressions a year. When those three depressions hit us, in the old days of 1932, we used to let people go, and when the peaks of high business came in, we, of course, rehired.

I would like to leave these figures for what they are worth. Under this new system the factory board handles that, and there is less than 5-percent labor turn-over. I think that is a low figure. It used to be considerably in excess of 15 percent in 1929.

Now, to skip over to the other side, which I won't dwell on as this is a matter you are not interested in, is the sales board, which, of course, identifies and gives us an outlet for all of our business.

So, therefore, the philosophy of this business is to allow every department to be broken up into particles so that each different type of man that comes into that business has a board to appeal to.

Secondly, he has a board that he can make if he has merit. Incidentally, he may be dropped off of those boards, but I can say this: The funny part is that when they are dropped they try harder to get back on.

I have a couple of notes that I wrote on a card. I was on a call last night, sir, so I haven't given an awful lot of thought to this.

On the question of life insurance and sick benefits and social things of that sort, we are up to date on that, I think, and I won't take your time to even discuss those phases. If there are any questions, I will be glad to answer them. I do say this: That this type of business here has culminated in a point where every other Saturday morning we have a general meeting, and this meeting might interest you, and then I am through with the discussion of this plan.

This general meeting is still democratic. On every other Saturday morning the factory executive chairman takes charge of that meeting. There are, roughly, 40 men in the room discussing the business. If you will follow this through, this is what I call cooperation. The factory chairman gets up and asks each one of his factory men two questions—"What did you do in the last 2 weeks?" and "What is your stewardship in the next 2 weeks?"

While this factory man is telling his story to the chairman, the juniors and the sales and the seniors are listening to that story. It is an open policy, in other words, a democratic appeal, and after he finishes, the junior chairman takes charge and goes through with his men, and likewise over in the sales, and finally the seniors.

The reason I mention this is that there is no more, in our particular type of business, a 1-man business, and I defy a President, dictatorial or otherwise, to come in and try to change our business. After all, there is a bonus participation proposition when profits are made, and when they are not made they are just as happy, and in this particular thing you have a "pride of ownership."

The reason I call it a democratic method of approach is, first, that there is free speech. I defy you to find over 10 percent of industry where a man at the bottom of the ranks can come into the front office and state his mind. I think that is harmful. In some cases it can't be done. But I think it should be encouraged.

In the next place, there is a definite apprenticeship from the time that the man enters that plant. And may I give you an interesting factor. It is harder to fire a man in our business than to hire him, because these same four men sit on that board, not on a board but on a committee, and they pass judgment on whether a man should be fired.

The result of that is that during the last 6 years we haven't had any labor troubles; I don't see why we should. We have never had a man leave disgruntled, and there is no reason why he should, because we have had seven cases where they came up before the boards and were reinstated. And at any time any man or woman can appeal to any one of these three boards and get a hearing as good as any court in the land.

I also call your attention to the fact that this is a merit system. I really don't know what the different people own in the corporation. It matters not at all to me. That has no bearing on it, and I don't think it should in the ordinary business. The question of profits—

I will leave that out of the picture. They have been minimum, but I still say that the philosophy of this Nation—and I stand here ready to prove it—is changing, and the question of making profits for stockholders only is a serious one that should be given consideration.

I think personally that the people working in a business have a priority right over a man outside that owns financial stock in it. I think he should be paid. But I think if there are any bonuses or things of that sort that the employees should be taken into consideration. Therefore, take, for instance, 1937, as a typical instance. I haven't the figures with me, but I know about what they are; we took, roughly, 28 percent of the net profits of the business and we distributed them back to the employees.

We distributed 54 percent of the total bonus to these four boards. Now I would like to pause just long enough to answer the question, before you ask me, why 54 percent. We consider that labor has a right to a proper payment, and also has a right to advancement. And a person that is the thinking type of man—and, by the way, I don't believe there is over 1 out of 10 in a factory that really is a thinking type of man; I don't think he has vision—therefore, if he is doing the thinking of the business, I think he is entitled again to a priority right in the question of profits, because he has helped considerably more than just filling that package or producing goods. Therefore, 54 percent was devoted to these four boards, and the rest went to the plant people as a whole, the whole mass through the plant.

The mass in the plant, I think, have been overlooked in a great many cases. How does a person feel who comes into a business, hears they have a profitable year, and reaps no personal benefit? It is rather inconsiderate.

The last point I would like to leave—and I am through. If there are any questions, I would be glad to answer them.

It might be interesting that we publish, in order to clarify that, a book entitled "Personnel Policies." If industry as a whole would just take the time to get the personnel managers of its companies to sit down and write out its policies, they would find that there are very few pages that would be written in a great many cases, and also they would find that if they wrote these policies out, that the pride of ownership of that business possibly would bring them to realize the fact that they are overlooking a great many things.

So, therefore, every person before they are hired, or even discussed, is given a set of rules. They know what they are working for, the policies, and the theories, and the result is that I don't think a person is taken into the plant without knowing the ideals of that plant.

Senator VANDENBERG. How many employees are involved in that operation?

Mr. McCORMICK. About 42.

Senator VANDENBERG. The whole operation?

Mr. McCORMICK. In these boards it is about 42. The total is, roughly, 600.

Senator HERRING. You have had no labor trouble?

Mr. McCORMICK. I don't see why we should, sir.

Senator HERRING. Do you have any opinion as to the principal cause of most labor troubles?

Mr. McCormick. Well, that is a rather drastic statement, but for want of a better one I would say that somewhere in the background, way back, there is some mismanagement, possibly—possibly. In other words, I don't like to commit industry because there are certain cases where I am sure they have been perfectly just and honorable with the employees, and through reasons beyond their control they have had labor difficulties, but I do not think that is true in the majority of cases.

Senator Herring. Well, thank you very much, and we appreciate your coming over, Mr. McCormick.

We will adjourn until 10 o'clock tomorrow morning.

(Whereupon, at 3:25 p. m., a recess was taken until 10 a. m., Wednesday morning, November 23, 1938.)

SURVEY OF EXPERIENCES IN PROFIT SHARING AND POSSIBILITIES OF INCENTIVE TAXATION

WEDNESDAY, NOVEMBER 23, 1938

UNITED STATES SENATE,
SUBCOMMITTEE OF THE COMMITTEE ON FINANCE,
Washington, D. C.

The committee met, pursuant to adjournment, at 10 a. m. in room 312, Senate Office Building, Senator Clyde L. Herring presiding.

Present: Senators Clyde L. Herring (chairman) and Arthur H. Vandenberg.

Senator HERRING. This is Mr. H. Boardman Spalding, chairman of the government finance committee, National Association of Manufacturers.

STATEMENT OF H. BOARDMAN SPALDING, CHAIRMAN, GOVERNMENT FINANCE COMMITTEE, NATIONAL ASSOCIATION OF MANUFACTURERS

Senator HERRING. Mr. Spalding, I understand you will speak extemporaneously?

Mr. SPALDING. Yes, Senator. I was called down here on rather short notice. I do not have any prepared statement, and I would rather talk in a conversational way with you.

Senator HERRING. I understand you wish to deal with incentive taxation.

Mr. SPALDING. Not particularly with profit sharing, because that is being considered by another committee of the national association, and they have taken no position with respect to it. The subject of incentive taxation requires, first, more or less a definition of what we mean by those words. They are very appealing words and they have certain connotations probably differing among different people.

I will approach the problem by stating, in general, that you can make incentive taxation directly with respect to anything you want to accomplish or you can make incentive taxation in an indirect manner. All taxation, of course, in that respect is going to be an incentive to do something or not to do something in greater or less degree. You probably recall that when in, I think it was the 1918 law, you imposed a tax of 80 percent on excess profits that you created a very strong incentive on the part of business to indulge in expenditures which they could charge to expense, such as increased advertising, increased promotion, various things of that kind, which they probably would not have done if there had not been that heavy a tax, because they could say, "Well, the Government pays 80 percent of that cost."

Now, the National Association of Manufacturers have taken no definite position as yet on the subject of direct taxation, except that, so far as they have expressed themselves, they are opposed to it, but they are still open for further consideration even of that direct form of incentive taxation.

The executive committee, at its meeting yesterday, passed this resolution:

> We are opposed to the proposal that any special tax relief or incentive be granted to companies having regularized employment, except as they may exist under State unemployment compensation laws. Any such tax treatment in the general tax laws would tend to subsidize employers who find it economically feasible to regularize production and employment at the expense of those who are unable to do so.

When, however, you enter the broader field of what we may call incentive taxation by trying to make such changes in the tax laws as will remove, to some extent, the deterrent that the present tax laws have to the taking of business risks, I think you have a field there that can be very profitably explored. We have a subcommittee now exploring three rather technical phases of that question. Those questions relate to amendments of the law to provide greater liberalization for charges to depreciation. They are to examine the statutory definition of net income, to see where changes may be made there. There is another point that escapes my mind for the moment. I may come back to that in a moment, Senator.

Another thing I would like to call your attention to, which I called to the attention of the Senate Finance Committee in the hearings which they held last spring on the 1938 law. If you examine the taxes, Federal and State, which are based upon business profits, first, the taxes that are paid by the business itself, if it is a corporation; second, the tax which the individual in turn pays on those business profits when they are distributed to him, you find that you have a very high rate of taxation applying to business profits. In the memorandum I gave to the Senate committee last spring I worked out very roughly the rates of that taxation applying to business income which ultimately reached individuals of certain classes of income. I took a \$10,000-a-year man, a \$25,000-a-year man, and a \$50,000-a-year man, and I assumed him to be a resident of the State of New York. Now, I only took into consideration Federal income taxes on the corporations and individuals, and the New York State income tax on individuals only, and I found that a man in the \$10,000-a-year class who had an investment in a corporation, and which corporation distributed all of its net profit, after payment of its taxes, was subjected to a rate over 30 percent on that part of his income which came from those net profits. When you reach the \$50,000-a-year man, you pass the 50-percent rate, and of course if you get up into the higher brackets you have reached almost astronomical figures. That study was a very incomplete one, and I think that it would pay your committee if you have the experts that you have in your employ, or else ask the Treasury Department if they would explore that further, taking into consideration some of the State franchise and capital-stock taxes of the larger industrial States, and of course you should include among your Federal taxes not only those I have mentioned but also the capital-stock and excess-profits taxes, which are, indirectly at least, based on the net incomes of corporations. I think then you will find that, not only the investor of enormous fortunes but the investor that lies in the class of income between $25,000 and $100,000 a year, you have a rate of taxation applying on the business profits which is so high that it necessarily discourages the taking of business risks. You find that if that investment is made in a company that is likely to have a very wide fluctuation of income between taxable periods, you can readily reach a situation where the total of those taxes over a period of less than 5 years will pass 100 percent of the net profit of those 5 years.

I am not coming here to tell you dogmatically that there is a certain rate of taxation beyond which if you go you are going to stop investment in business. I do not know what that point actually is. We all have to guess at it. I should say when you get above 40 percent or 50 percent of the business profit you have a very strong discouragement to the taking of business risks. It becomes too much a case of heads you win and tails I lose. To my view, it is necessary, if we want to achieve the ultimate purpose of this committee, which is to have business expand and through expansion take up this slack in employment, to attack that problem not by dealing so much with incentives to encourage this particular employer to employ 10, 15, or 20 more men but to attack it indirectly through removing the tax deterrent to the taking of business risks.

Now, how are you going to do that? Well, of course, there are a number of different courses that you can pursue. You here cannot do much about the State taxation problem, that is outside the congressional field. Your Federal taxes that apply directly or indirectly, on business profits are first: your personal income and surtaxes, your corporate income taxes, your tax on capital gains, and finally the capital-stock and excess-profits tax follow.

I can only suggest to you the following possibilities of correcting that condition: You could, first, materially reduce the rates of taxation on personal surtaxes; you could reduce the rate on the corporate income tax; you could eliminate what is left of the undistributed-profits tax. On that, I think the elimination of that tax in and of itself would objectively have very little effect, but subjectively it would have an enormous effect upon businessmen, because, rightly or wrongly, they have almost universally condemned the principle of the undistributed-profits tax. I have been personally somewhat amazed at that universal condemnation of the principle. I was as critical as anybody of the particular tax that was imposed by the 1936 law, but I have observed a certain lack of consistency in opposing the principle entirely and at the same time requesting that you go back to the procedure prior to the 1936 law and allow exemption from individual and corporate income taxes on the dividends that are paid.

Senator HERRING. Mr. Spalding, that is most interesting, this vast field of revenue that the Finance Committee as a whole considers, but the purpose of this resolution, as I understand it, was to attempt to find something that might prevent the continuation of the trouble with labor and employment. For example, I understand the Government reports some 42,000,000 hours of labor lost in the last 2 years as the result of strikes. Now, the National Association of Manufacturers, of course, employ hundreds of thousands of men; they must have lost a great deal during that time as the result of strikes and labor troubles.

I think one of the things we are primarily interested in—and I should like to have Senator Vandenberg confirm this—we are attempting to find something that will give us industrial peace and in that way benefit the employer and employee alike, and for that reason we are investigating the possibilities of profit sharing and possibilities of incentive taxation to encourage a profit-sharing plan of some kind that will promote industrial peace, rather than going into the intricacy of all the revenue acts which this Finance Committee, as you know, considers, and you have been before it for that purpose.

Mr. SPALDING. Yes.

Senator HERRING. I just thought I might make that observation so you would understand we are not going into that whole field of taxation through this subcommittee.

Senator VANDENBERG. That is perfectly correct.

Mr. SPALDING. I am here, Senator, largely by your invitation, and I do not want to extend my remarks into a field that you do not think you should consider, so there is no need of my going on over the various things that might tend to relieve business profits of the excessively high rate that they pay through the cumulative total of all the taxes that are measured by business profits, but I do want to emphasize very strongly my view that that would be the most effective means of indirect incentive taxation; that by the removal of what I think is today a very strong deterrent to business investment, you would get the business investment and ultimately you would get the absorption of the unemployed.

As far as profit sharing is concerned, unfortunately the National Association of Manufacturers referred that to another committee. They have not brought in a report as yet, so I do not know what their position is going to be on the subject of profit sharing, and if I said anything it would be my personal views, and I would not want to have it understood that I was in any way committing the association.

Senator VANDENBERG. May I see the resolution that was adopted yesterday that you referred to?

Mr. SPALDING. Yes.

(The resolution was handed to Senator Vandenberg.)

Senator VANDENBERG. Now, that is adopted by the executive committee of the national association, is it?

Mr. SPALDING. By the executive committee, and they intimated that they would like to have the subject again referred back to the full board for further consideration.

Senator VANDENBERG. I think that was a wise intimation.

Mr. SPALDING. I do, too.

Senator VANDENBERG. Who is on the executive committee that met yesterday and passed this?

Mr. SPALDING. I am sorry, Senator, but I do not know. Undoubtedly the officers of the association. Mr. Hook is the president; Mr. Warner is the chairman of the board. I think they are probably both on the executive committee. Who the other members are I do not know.

Senator VANDENBERG. When they exempt from their condemnation such incentives as exist under State unemployment compensation laws, are they referring to merit rating?

Mr. SPALDING. I assume they are.

Senator VANDENBERG. In other words, they are in favor of merit rating?

Mr. SPALDING. I think that is the position of the association on that.

Senator VANDENBERG. If they are in favor of the merit rating incentive, why would they not be in favor of comparable incentives in the Federal treatment of business? I do not understand the consistency. They applaud the only single concrete exhibit of incentive taxation that is available today and then condemn the principle.

Mr. SPALDING. Their feeling is twofold. First, they think that the general revenue laws should be used to raise revenue rather than to accomplish some ulterior purposes. Secondly, they believe that if they concede the principle of incentive taxation, they are at the same time conceding the other side of the thing, punitive taxation.

Senator VANDENBERG. They get that whether they concede it or not. It does not do much good to quarrel with the principle of punitive taxation, inasmuch as they cannot escape it, anyway. Frankly, I am amazed at this action of the executive committee, and I am wondering who would be prepared to testify as to the reasons for this action. Whom would you suggest?

Mr. SPALDING. Well, I attended a meeting of the board in which this matter was discussed, and I know that the reasons set forth there were the two that I have given to you. Another reason was that if you give a tax reward to a company that increases the number of people it employs from some base period from which you obviously have got to start, or if you give a tax reward to a company which constructs a new and modern plant and scraps what it now has, they feel that you are giving a competitive advantage which is unfair to those people whose economic and business situation does not permit them to increase their employment, or whose business and financial situation does not permit them to build a new and modern plant.

Senator VANDENBERG. I think that is a fair criticism.

Mr. SPALDING. And that, I think, is the major criticism. I do not think any witness you would get from the National Association would state it very much differently. They might elaborate on it to a very considerable extent.

Senator VANDENBERG. I do not want to be misunderstood in what I am saying. We are not committed by any manner of means to any theory of incentive taxation at all, but the action of the executive committee in announcing this general condemnation is so contrary to the testimony of thousands of employers across the country, whose opinions will be later presented through the Tax Research Institute, that I am wondering how we can arrive at what is the voice of the employer of this country on the subject. In other words, does the executive committee speak for the American employers accurately when it, in this rather cavalier fashion, just announces that it is all wrong?

Mr. SPALDING. There is, without any doubt, a difference of opinion, not only among the businessmen on this particular subject, but there is a difference of opinion, I am sure, in the board of directors of the National Association itself. That was one of the reasons why, when Mr. Walsh communicated with me I was rather reluctant to come down before you at the opening of the hearings. I was hopeful that between now and the time your hearings are closed that their position on these questions would have more clearly crystallized than they have at the present time. I have been hopeful that I could urge upon them that this was not a subject on which it was desirable to take too theoretical a position, that taxes are an extremely practical question, that we should examine the merit of any tax pragmatically, and that we need not be deeply concerned if it violates some preconceived theories that we may have, but I can at the present time only state to you how far the association has actually gone.

Senator VANDENBERG. Well, we are entirely receptive to criticism of the idea; in fact, we have searched for criticism as actively as we have searched for anything else, because the essential thing is to find the attacks on a thing of this sort, and I am not complaining at all about the critical attitude, I am simply finding myself wondering what we are entitled to consider to be the views of the employers in this country when the executive committee of the National Association dismisses the matter so completely in the presence of cumulative evidence from thousands of other employers across the country that they are tremendously interested in it, that if they could have some sort of incentive taxation, probably it is the precise thing that would be the determining factor in releasing the industrial activity in this country, I was wondering why we would confront two totally opposite views.

Mr. SPALDING. Senator, I do not think there is as much difference as that resolution of the executive committee has led you to imply. Unfortunately, we tend to get confused over the use of words. We have at the present time a subcommittee of experts considering the questions to which I referred awhile back, and if they bring in any valuable, concrete suggestions on the subject of depreciation, I should be very glad to submit those to your committee before your hearings are closed. Now, broadly, suggestions of that kind will fall within the scope of what you are seeking, incentive taxation, and I am quite certain that the National Association will not oppose changes in the tax law along those lines. What they have objected to is the direct subsidizing, if you please, of an employer through a reduction in the amount of his tax bill if he happens to be in the fortunate enough position to be able to employ more people next year than he was able to employ in whatever your base period may be, and I think they have the feeling that that direct incentive, unless it is of an extremely large amount, will not have very much effect, in and of itself, in increasing employment, that the more people are employed because that business is a success and is able to employ them rather than the fact that you have given it an incentive in the form of special tax relief.

Senator VANDENBERG. I think you can make a very formidable argument on that point.

Mr. SPALDING. They think it is unfair to leave the heavy tax burden on those businesses which are so unfortunate that they simply cannot employ more people, or may actually be employing less people than they did in the past year.

Senator VANDENBERG. Would not this general statement be a perfectly good argument against all tariffs?

Mr. SPALDING. Well, if you are asking my personal view—I am not on the tariff committee, fortunately.

Senator VANDENBERG. I am wondering how the National Association of Manufacturers keeps in harmony with itself on all the various applications of the theory of incentive taxation.

Mr. SPALDING. Senator, I have wondered that myself.

Senator VANDENBERG. Then, we can agree on something.

Senator HERRING. Well, it is of interest to explore the incentive taxation as to plant equipment and the effect it will have on reemployment. It is a fact that our resolution is directed to using any possible means to encourage profit sharing, for the purposes which I mentioned a little while ago. The resolution definitely states, "including the grant of compensatory tax exemption, tax awards, when profit-sharing is voluntarily established." The method of approach, we think, to incentive taxation through this resolution is for the purpose of encouraging profit sharing in industry, hoping that through the encouragement of profit sharing we will obtain industrial peace and increased employment, and, through increased employment and industrial peace, perhaps efficiency, increased economies, and an increase in loyalty, we will reach a condition that will be of inestimable value to the employer. We are not attempting to go into all the fields of incentive taxation as to plant equipment and reemployment directly.

Senator VANDENBERG. Without disagreeing with Senator Herring in any way, because he has read the resolution, I want to add, however, there is a basket clause which permits us to consider other things.

Senator HERRING. Which permits us to consider any other recommendations which may be deemed desirable. The Senator wrote the resolution.

Senator VANDENBERG. It is pretty broad, when you get through it.

Mr. SPALDING. Senator, I said at the outset that another committee of the national association has been considering the subject of profit sharing, and I do not know now what position they have taken on it. I cannot speak for the association. If you want my personal views, I can go ahead, but I cannot speak for the association on that.

Senator HERRING. Go right ahead, then.

Mr. SPALDING. Then, with the clear understanding that what I am saying now is purely my personal view and in no way the view of the National Association of Manufacturers, or business generally, I have this suggestion to make to you regarding profit sharing: In the first place, if you examine the records of business as a whole, you will find that the existing amount of net profit for business as a whole is so inadequate that there is nothing to share.

Senator VANDENBERG. At the present time?

Mr. SPALDING. At the present time. Well, on a broad average, I think you will find that true over a period of years.

Senator VANDENBERG. Five years?

Mr. SPALDING. If you take individual companies there may be situations where they can use profit sharing, and use it quite effectively. How far down they can carry that in a way that is satisfactory and understandable to their labor, I do not know. I have a great deal of doubt and a great deal of reservation in regard to carrying it much below the executive and junior executive positions in any company.

Senator HERRING. Are you familiar with the testimony here in the last 2 or 3 days, of these five or six men who employ up to 50,000 people?

Mr. SPALDING. I have not read that. I say this with the reservation that there are unquestionably situations of individual companies that not only can but have used profit sharing right down through the whole plant with a great deal of success. I think most enlightened companies try to have, if not a direct share in the net profit of the business as a whole, at least try to give certain wage bonuses for accomplishments within a certain department or division of a business. Now, it depends on the organization of the business whether they can use the results of the business as a whole or whether they have got to use the results of the individual department. I will call your attention in the first place to the fact that there is already a fairly strong tax inducement from the fact that any payments in the form of profit sharing to employees become, for tax purposes, an expense of the business, so you get a complete deduction from your gross income of the amount you distributed in profit sharing, under the existing laws. So that if you went beyond that it would mean that you were going to reduce the rate of taxation applying to what was left, or going to give some specific credit in the taxation applying to what was left of the net profits after profit sharing. I do not have any dogmatic views as to whether something along that line might be helpful. I am very skeptical of anything that would be within the practical limitations of what you may allow, as to whether it would accomplish very much, even to promote a profit-sharing plan.

Senator HERRING. We are just as glad to receive criticisms and objections to this proposal as we are to have it approved.

Mr. SPALDING. As I said, I did not have time to prepare a statement for you. I have come down here and have tried to deal with this thing in a conversational tone.

Senator HERRING. You have done very well, and we appreciate it.

Mr. SPALDING. I would welcome any questions. I will try to answer them to the best of my ability.

Senator HERRING. We appreciate your coming, Mr. Spalding. If you do not have anything else to suggest, we will call the next witness.

Mr. SPALDING. Senator, if there is anything further that we develop between now and the close of the hearing, may I have permission to submit a written statement on it?

Senator HERRING. Certainly. We will be glad to have you do that.

STATEMENT OF WILLIAM GREEN, PRESIDENT, AMERICAN FEDERATION OF LABOR

Senator HERRING. Mr. Green, we appreciate your coming over. We know you are thoroughly familiar with the purposes of this committee and the resolution. We will permit you to just go ahead in your own way and be of such assistance as I know you can be.

Mr. GREEN. Thank you.

Mr. Chairman, I am happy to respond to your invitation to meet with the committee this morning, and I have a short statement prepared that I will submit, and then I will be glad to answer any questions that you may desire to ask.

Labor is not opposed to principles involved in profit sharing, but it is opposed to the way in which it has developed and operated. So-called profit-sharing plans were mainly developed by corporations that attempted to substitute for real collective bargaining an arrangement termed "employee representation" which for the most part was the form without the substance. The companies sought to oppose trade unionism by "refined" methods of the "employee-representation" plan or company union, including the substitution of the term "industrial relations" for "labor relations," employee representation for union and collective bargaining, industrial-relations problems for labor problems, et cetera. The purpose of these substitute terms was to obscure the real labor problems and to direct attention from the union's concentration on establishing workers' equities in their jobs and fair compensation for their participation in joint work. This background militated against developing of profit sharing on a sound basis.

Labor believes all plans affecting labor must rest on collective bargaining. Beginning with the basic fact of our social organization that people must have incomes to buy the necessities and comforts for living, labor asserts the right of every person to opportunity to earn that income which includes the right to payment for work done. The right of labor to the fruits of its toil has been obscured by the complexities flowing from the corporation form of financing, and mass production with its standardization of designs and machines and subdivision of work for repetitive processes. Corporation financing has altered and obscured the responsibility of investors in a business enterprise; mass production or large-scale production has obscured the relation between the worker and his productiveness. What is needed in this situation is genuine organizations of workers in unions so that they may have an agency for collecting and collating the facts of the work relationships and of the results of joint and individual work, for the purpose of joint discussion with management to define the principles and standards of compensation for work.

This union function is indispensable to justice to workers, to balanced progress of the industry within the business structure, and to social justice and peace in the community. Denial of this fundamental justice to those who carry on the production processes of industry or maintain our service institutions, or attempts to frustrate collective bargaining are what cause labor disputes and social discontent. Substitutes for justice may for a time prevent the outbreak of disputes, but they increase and foster a spirit of unrest which sooner or later takes its toll. In recognition of these facts our Nation has undertaken to assure to wage earners the right to organize in unions and to bargain collectively through representatives of their own choosing. This priceless foundation of economic liberty we intend to maintain against all invasions whether by employers or governmental administrators. It follows that we are equally unwilling to see the scope of collective bargaining narrowed so that profit sharing or any other new provision affecting work relationships must mean an extension of collective bargaining to the new field. All of the terms and conditions of payment for work should be determined through joint conferences of representatives of management and workers concerned and carried to mutual agreement upon issues discussed. Should union and management consider—I want to emphasize this point—should union and management consider a form of profit sharing these would be elements in the consideration. Labor cannot be asked to accept blindly management's decision on what constitutes profits. All of the facts must be available.

(1) Production and costs records must be equally available to union and management.

(2) Sales policies must be considered by both parties and be mutually acceptable. All records must be equally available to both sides.

(3) Salaries of executives and officers and returns to investors must be subject to the same conditions.

(4) Financial policies and proposals must be subjected to the same review and decision.

(5) The standard wages of producing workers, which are production charges, should be fixed by collective bargaining at the highest level industry could reasonably be expected to pay and should provide for customary standards of living proportionate to productivity as human labor power is increased by mechanical power and machine tools, and reflecting lower unit-production costs. The standard wage is the cost item which is the first charge on industry and which is necessary to the sustained consuming power upon which all business depends.

(6) Profit sharing or a partnership wage is the share which labor would have in the net income of the enterprise. In reality labor is a partner in production, not from the investment of capital but from the investment of experience and work ability. As a partner labor would have a voice in determining rates of profit sharing.

Recognition of real partnership and frank acceptance of the privileges and rights derived therefrom would be the greatest incentive to sustained efficiency in work that industry could devise. Nothing involved in the acceptance of this real partnership alters the functions of management and workers. Management would still write the work orders and the production staff would execute them.

Investors have always claimed that profits belonged exclusively to them because they alone bore the risk of industry. But we all know the risk of business is borne by every person dependent upon it for jobs and income. The risk of wage earners is no less frightening and hazardous than that of investors; food, clothing, and shelter are at stake.

The profit motive is a strong force. It gives an individual opportunity to benefit from resourcefulness and efficiency. It has been a most powerful force in developing present-day civilization, and we do not wish to limit the scope of its operation. We, therefore, propose that collective bargaining be extended to the field of profit sharing as rapidly as possible.

Profit sharing in the strict sense means a plan to share net profits with employees. Some have used the term in a broad sense, making profit sharing include types of bonus payments, insurance or savings plans, stock ownership, and production bonus, such as gift or merit bonus, percent-on-wages bonus, cost-of-living bonus, and service bonus. The difficulty of including these plans in profit sharing is that they are a part of the wage structure and therefore are production charges and therefore must be charged off before profits can be determined and divided.

A study by the British Ministry of Labor (1936) showed that out of 532 bona fide profit-sharing plans in that country 330, or 62 percent, had been discontinued. The National Industrial Conference Board reviewed experience in this country in its 1937 study and found that 96 out of 161, or 60 percent, had been abandoned. Dissatisfaction of employers or employees was found to be the cause for discontinuance of 26 percent of the British plans and 29 percent of the American. Substitution of higher wages, shorter hours, or other benefits replaced profit sharing in 11 percent of the British companies and in 14 percent of the American.

The American Federation of Labor is unalterably opposed to using the tax power of the Government to promote profit-sharing plans. We are squarely opposed to amending the Social Security Act to provide tax credits for funds allotted to profit sharing or any similar purpose, however worthy they may be in themselves.

The Social Security Act is to provide some degree of security for the victims of industrial unemployment. It cannot be used to remedy the defects of industry without interfering with its prime function.

The costs of administering social security are already too high—between $40,000,000 and $60,000,000. These high costs are due in part to our inexperience in the field and in part to the very complicated provisions in our laws. Merit rating provisions in the laws not yet in effect will definitely increase these costs. The Federation believes these provisions should be removed. Credit for profit sharing would multiply the difficulties and the costs.

Now, I have submitted this brief statement as my own personal and official opinion regarding the subject matter being considered by this committee, but it occurred to me I might not have made plain, in this brief statement, one particular point, so with your permission I will be glad to supplement what I have said with this explanation: We believe that the first obligation of industry and industrial management is to provide for the payment of a wage, and to establish wage and working standards through collective bargaining, and that the wage established and the standards agreed upon should provide for the payment of an income to the worker that would insure him and his family a living in decency and comfort. Now, that is the first charge on industry. There should be no profit sharing until first, that definite standard wage has been established and paid.

After that is established, then if the earnings of the industry will justify an equitable distribution of the profits of industry between investors, management, and employees, let it be done, with a full understanding and in full cooperation with the representatives of the workers. The one trouble about profit sharing, as practiced by a number of corporations, is that it has created suspicion, distrust, because the workers know nothing about the basis upon which the profits were distributed. If it is to be put into effect in a practical and satisfactory way, there is great need of frankness and open dealing between the management of the corporation and the workers themselves. Let the workers know the truth. "These were the profits. This is the net income; here are the figures, and we proposed to make an equitable division of these profits."

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Senator VANDENBERG. I think you are making a very splendid contribution to the discussion, Mr. Green. Of course, there is no substitute for justice, using your phrase.

Mr. GREEN. No.

Senator VANDENBERG. And, of course, profit sharing, to be successful, has got to be mutually understood, mutually agreeable, and mutually contracted. Now, as I understand your position, with collective bargaining as the basis—which again I agree with, speaking for myself——

Mr. GREEN (interposing). Thank you.

Senator VANDENBERG. If profit sharing is part of the bargaining it is entirely agreeable to you?

Mr. GREEN. Yes; arrived at through collective bargaining.

Senator HERRING. I think we had four or five witnesses here in the last 3 or 4 days, Mr. Green, that have profit sharing in their industries.

Mr. GREEN. Yes.

Senator HERRING. As I recall, they all testified that the amount of profits are arrived at through negotiation with employees.

Mr. GREEN. Well, I am not sure. I know that some of the corporations whose representatives appeared here have been pioneering in that experiment, if I may put it that way, and I have always regarded the representatives of these corporations as very high-minded men. I do not know; I do not know whether anybody really knows and understands the basis upon which they made this distribution of profit. Perhaps they did deal with their representatives. I say I do not know, but I am speaking on it from the trade-union point of view, and that is through the development of collective bargaining, participated in by the representatives of free, independent, democratic trade unions and the management, and through such a process I am sure it could be made a success.

Senator HERRING. I am thoroughly in accord with the statements you made, and I think that applies to Senator Vandenberg also, but I am wondering if, in your opinion, profit sharing arrived at in that way would in any way be sharing the management?

Mr. GREEN. Probably would, to some extent, and we have never been opposed to the development of a fine standard of union-management cooperation. We have pioneered in that experiment, in making that experiment in many fields.

Senator HERRING. The objections from some employers have been that they could not share profits without sharing management.

Mr. GREEN. Well, I think there is a line that could be drawn in that. Management, of course, is susceptible of a broad interpretation. When you come to the formation of corporation policies, which involve sales and administration, and all that sort of thing, that is one form of management; performance of work in the factory, or in the shop where you come in contact with the workers' representatives, is another form of management, and I think that through the development of collective bargaining and the right kind of a human relationship, that there can be a form of union management, insofar as the management of the factory is concerned. I do not mean to broaden that out so as to cover the other field of investment policies, and all that sort of thing.

Senator VANDENBERG. You used another very significant phrase when you spoke of the workers' equity in his job.

Mr. GREEN. Yes.

Senator VANDENBERG. Might not the worker better establish his equity in his job through profit sharing than through any other medium, if it be through collective bargaining?

Mr. GREEN. Yes.

Senator VANDENBERG. Does not that spell "equity?"

Mr. GREEN. That might be the result of it; yes. It could be, I can see that.

Senator VANDENBERG. You spoke casually, in your final statement, about merit ratings and State unemployment laws. Do I understand the Federation is opposed to the merit rating system?

Mr. GREEN. We have never looked with favor on it, because it offers an opportunity for the introduction of, oh, unjust methods and discrimination, and all that sort of thing, so we have not looked upon that with favor and approval. We are going into it, however, to study it more carefully. They have pioneered with that to some extent in the State of Wisconsin, as you know.

Senator VANDENBERG. Yes.

Mr. GREEN. The element of favoritism can enter into that too, and, after all, we have got to follow a social and political policy that will bring to the most helpless worker that degree of protection to which he is entitled. We do not think it is a good thing to establish one class up here and another class down here, and that is what merit rating would probably do. We are afraid of it.

Senator HERRING. Mr. Green, do you know of a company that is practicing profit sharing and whose ideas and plans coincide with yours? Do you know of any company that is sharing profits?

Mr. GREEN. No; I do not know of any at the present time, that is, sharing profits in accordance with the plan I have outlined.

Senator HERRING. Would you be in a position to outline what you would call a proper profit-sharing plan?

Mr. GREEN. I would be very glad to, in a simple way, and send it over to you.

Senator HERRING. We would be very glad to have it. Thank you very much.

Senator VANDENBERG. You made a fine contribution.

Mr. GREEN. Thank you.

Senator HERRING. We will adjourn until 1:30.

(Whereupon, at 11:30 a. m. a recess was taken until 1:30 p. m. of the same day.)

AFTERNOON SESSION

(The hearing was resumed at 1:30 p. m., pursuant to the taking of the recess.)

Senator HERRING. We will come to order, please.

Senator VANDENBERG. I would like, before we start, to put into the record the following letters:

One from Mr. C. D. Haskell, president, Beatrice Creamery Co., Chicago, Ill.; and one from Mr. A. Holmes, president, Mallow Suburban Motors, East Orange, N. J.; and I would also like to put into the record the preamble to the resolution under which the committee is operating. Only the resolution itself has been introduced heretofore, and I think the preamble, which, as usual, was stricken out by the Senate, is more descriptive of the real purpose which we have in mind.

Senator HERRING. They will be included in the record.

(The documents referred to are as follows:)

BEATRICE CREAMERY CO.,
Chicago, November 19, 1938.

Mr. T. I. WALSH,
Technical Adviser, Subcommittee of United States Committee on Finance, United States Senate, Federal Building, Chicago, Ill.

DEAR SIR: Attached is "Schedule of information by employers" as requested by the Subcommittee of Committee on Finance.

We were unable to fill out page 2 because through error you mailed us two copies of page 2. If you will send us page 2 we will be glad to fill it out.

We are unable to fill out completely questions 6 and 7 as those records are not available.

In response to questions for comments on incentive taxation and the advantages and disadvantages of tax rewards, we will endeavor to answer these in the order given in your letter.

1. Would suitable tax rewards encourage us to increase our plant and equipment-maintenance expenditures?

Yes; the dairy business is such that it operates every day in the year and no substantial increase in plants and facilities could take place until consumption increases in the United States. However, additional money could and undoubtedly would be spent by the industry for modernization and improved equipment if some tax incentive was given. The net loss limitation now in the tax law prevents junking or selling of old equipment and replacing with new.

2. As regards tax rewards for profit sharing, we have not studied this far enough to make any constructive suggestions, but it is our opinion tax rewards could be made to encourage employee profit-sharing plans.

3. The question as to what other measures are essential for the encouragement of capital in the resumption of normal activity and progress should include, we believe, the following:

(1) The principle of carrying forward losses; reporting taxable earnings on the basis of a 5-year average or by some other method, equalizing the tax burden over a cycle of years.

(2) Corporations should be allowed the dividend paid credit on dividends paid subsequent to the close of the taxable year and prior to the due date of the tax return or to some other reasonable subsequent date.

(3) The inequitable corporation capital net loss limitation of $2,000 should be removed.

(4) Land used in trade or business should be excluded from the definition of capital assets. Land and the building attached thereto generally are considered to be one asset and almost any transaction which could result in capital gain or loss would involve the sale or exchange of the land and building together.

(5) Consolidated returns covering the operations of parent and subsidiary companies should be made mandatory and the taxation of intercorporate dividends between affiliated corporations should be repealed.

(6) The capital-stock and excess-profits tax provision should be repealed. The declared value of the capital stock is arbitrary and has no relation to the actual worth. The amount of the excess-profits tax is based upon an estimated figure instead of sound principles.

(7) A standard Federal income-tax act should be adopted eliminating the uncertainties due to repeated changes in the law. The tax should be adjusted to the needed annual revenue by the revision of rates.

We trust that the suggestions contained herein will be helpful to your committee.

Yours very truly,

BEATRICE CREAMERY CO.
C. D. HASKELL, *President*

MALLOW SUBURBAN MOTORS,
EAST ORANGE, *November 18, 1938.*

Mr. T. I. WALSH,
Technical Adviser, Federal Building, Chicago, Ill.

DEAR SIR: The Manufacturers Association of New Jersey states you are interested in suggestions on incentive taxation. Here's today's problem for us—and it can be helped by proper taxation methods.

We employ about 160 people in three stores and one large central used-car reconditioning plant. The last 12 months (up to October 1, 1938) were the worst months we ever experienced. We did not lay off any men, although we allowed the number employed to go down by about 5 to 10 percent through not replacing an employee when any left.

As a result of this procedure we lost a good deal of money and, of course, will have no tax on profits this year. It looks as though 1939 will be different, and we should show a profit with resultant tax.

After due study of the past months, we have decided that never again will we try and maintain employment, but will work on the opposite basis and endeavor to operate with little if any loss during any subsequent slow business period.

Now, if these losses of the past were deductible from the gains of a taxable year, we would have an incentive to maintain our organization, as by so doing we could more quickly get under way when business picks up.

The tax set-up now encourages the employer to increase or decrease his force with change in business volume, and that is wrong.

Yours very truly,

MALLOW SUBURBAN MOTORS,
A. HOLMES, *President.*

PREAMBLE

Whereas the maintenance of the profit system is essential to the preservation of the competitive capitalistic system under which the United States has attained the largest measure of general economic welfare enjoyed by any people in the world; and

Whereas the exploration of all available means for extending the direct benefits of the profit system to the largest possible number of citizens is highly desirable and important: Therefore be it * * *.

Senator HERRING. Mr. Funk?

Mr. FUNK. Here.

Senator HERRING. Donald S. Funk, vice president, Sangamo Electric Co., Springfield, Ill.?

Mr. FUNK. Quite right.

Senator HERRING. We appreciate the cooperation you have given us. We appreciate your coming here, and we ask you to proceed in your own way to be of any assistance you can to the committee.

Mr. FUNK. Thank you very much.

STATEMENT OF DONALD S. FUNK, VICE PRESIDENT, SANGAMO ELECTRIC CO., SPRINGFIELD, ILL.

Mr. FUNK. I am not going to make a long talk or a formal talk. I haven't prepared anything. I am assuming that you would like to know just a little something about our company and our practices in the way of this general subject of profit sharing.

I work for the Sangamo Electric Co., in Springfield, Ill. We manufacture electric watt-hour meters. They are the devices that the power companies buy and put in your homes, by which they charge you the bill for the electric current you consume. They are sold all over the United States.

The manufacture of these meters requires high-class labor; that is, they are more or less intricate, delicate devices, and consequently I can only speak from the standpoint of an employer of a high-grade type of men and women. We don't have any very rough labor, or heavy labor.

Senator HERRING. How many people do you employ?

Mr. FUNK. About 1,300 normally. It has been up and down, I am sorry to say, at various times during the last few years, but I should say that would be about normal employment. We have now probably some 1,175. That is about normal.

I am only sorry that our president, Mr. Lanphier, himself can't be here. He is the man that has really been at the helm for 40 years that the company has been in existence, and in what I have to say here I want to make perfectly clear that it is his guidance and his wisdom and his general policy that has made these things possible. Unfortunately, he is ill.

The company grew from a very small company to its present status. We have a branch factory, a complete factory, in Toronto, and another one in England. I won't say anything about those two factories now, although if, later, you would like to hear something about what we are doing along these lines there, very briefly, I would be glad to mention that. I have just come back from England, where I spent the entire month of October at our British plant.

But coming now to the subject in hand—that is, as to what our company has done in the past, what we are doing now, and possibly a little something about what we would like to be able to do—I won't give a great many facts or figures or dates.

To my recollection, the first thing I can really remember—no; I won't start that way—first I want to say this: That fundamentally I don't think any of these schemes amount to a row of pins unless a good wage scale is kept up. Now, I am not going to say what that should be for any particular industry, nor for our own. We pay high wages and I have no use for the employer that pays low wages and then does some fancy things and has them written up in a book or a newspaper or something of that sort and pats himself on the back. The people aren't fooled by that at all. Fundamentally the first thing you have got to do is to pay a good, fair wage scale.

Senator VANDENBERG. Social service is no substitute for a fair wage scale?

Mr. FUNK. Absolutely not at all. I have seen some evidences of substituting social service that make me mad. I have no patience with that at all; it is no good.

Mr. Lanphier himself is more interested in the people in our factory than he is in making money. I want to make that as a point because perhaps our experience has not been typical of what other people may have had. He believes, of course, that business should pay something to the stockholders and that a fair profit should be realized. But beyond that, he is interested in seeing that the wage earner gets, in some form or other, the fruits of his labor, and he sincerely believes in that.

Moreover, he is always accessible and people can come to him. We are perhaps fortunate in that respect in being in a small town, a town of some 75,000 people, where the plant has grown slowly. The families live there. Many of them have their children, relatives, cousins, working there. I think that has been something of a factor, I know it has, in building up the feeling that there is in our organization.

But, of course, unless they are treated properly it doesn't amount to anything at all. But we don't have a labor turnover, we don't have floating labor to amount to anything.

Probably the first thing that was initiated was some 20 years ago, at about the time I started with the company when I got out of school, and that was the group life insurance. It is very interesting to remember that it was received at that time with a good deal of suspicion, that people didn't know quite what was behind it. Now, of course, group life insurance is taken by everyone. I don't think there is an employee in our plant who does not have group life, and as a matter of fact we pay it all, or did for a number of years. Now the employees pay 50 cents a month and the company pays the balance.

It is our feeling that they can well afford to do that and previously I don't think that some of them knew they had it, as a matter of fact, when we paid the whole thing. It gives them a little more appreciation of it.

Then, as the years went on, you could see this grow as a sort of a family proposition in many respects. Next the formation of our mutual benefit association. I won't go into that in any great detail. It is very similar to mutual benefit associations in other plants, many companies have them. The people contribute so much a week and the company puts in a certain amount of money. We have ours pretty well built up, not only for the matter of accidents, but of sickness. It is in a shape where the association will pay for 4 months about 70 percent of full wage for participation, which is good because we have found that the fear of accident and sickness is strong in the employees' mind in general.

You can talk about a lot of other things, but they will say, "What happens to me if I am hurt and am laid up and have to go to the hospital for 2 or 3 months?"

Everyone belongs to the relief association and they have been able to see the results and the fruits and benefits of that.

Then the other things, I don't think need any particular stressing. We run our own cafeteria where we sell food at cost. The things just about break even. We don't charge up anything in the way of rent or heat, I don't suppose they even charge for the gas. It is just a matter of food, the food that is bought. We serve some two or three hundred people there a day.

Medical service; yes. We employ a reputable firm of doctors who have their men out there every morning for an hour and a half or 2 hours, or longer if it is necessary, for people to see them. They come in for free consultations, go to anybody that they please—of course, their own physician if they want to. The same thing with the dental service.

Just how much that is appreciated is a little difficult to say, but I think it is. The best proof of that is the fact that the people in the plant, if they feel a little bit upset or something out of the way, they run right straight up to find out what is the matter with them. I don't know that they always trouble to say "Thank you"; but there is no reason why they should. It is a good thing for the company as well as the employees.

These physical examinations have detected cases of what might well be contagious diseases, and all that.

Then the Credit Union was started by the employees entirely on their own. The company has nothing to do with that at all, and it is being run very successfully. I have often wondered how they have done as well as they do, but the people that are on the loan committee must be a pretty good bunch, because it is a tough job. None of the officers of the company stick their noses into that at all. We keep entirely out of it. That is none of our affair. They have made a go of it. They might turn John Jones down and tell him "No," that he can't borrow any money. We didn't start that, but it is a great help to the company. I am not bringing that up as anything that we need to be patted on the back about at all. It relieves us of the people constantly coming in for a loan, "Can I get $50, my wife is sick"; or something of that sort. They can get their money there.

Perhaps, however, more important from the standpoint of dollars and cents, is this scheme that we initiated some 4 years ago, which we call our "service warrant" plan. It has now been abandoned. I want to tie that in with the pension work we are doing. It was not original with us. It was started, I think, by the Package Machinery Co. of Springfield, Mass. We just adopted it.

Very briefly, it simply means this, that to each of our employees who had been with us more than 1 year, we issued a certificate, made up a nice looking certificate, of course nontransferable. It had no value or anything of that sort, but it was equivalent to two shares of the common stock of the company. Then, for each succeeding year of service they got another two shares, either an additional certificate or a new certificate with the proper number of shares of stock on it.

Anytime that the company paid a common dividend on its stock, these holders of these certificates were paid in essence a dividend, the cash equivalent of a dividend for the number of shares that they held.

Well, naturally that was accepted very gladly, and worked very well indeed, because it wasn't quite the idea of the Christmas bonus proposition which, if you start, it is pretty hard to stop. That is, it gets to be just a regular thing and about November people begin to say, "I wonder if they are going to pay a bonus this year, or if they aren't." And if you don't, for perfectly good reasons, somebody will say, "They could have done it if they wanted to. They sat around in the directors' room and just decided they weren't going to."

This other way we could and did pay dividends to employees when we paid the shareholders. But it did have, in my opinion, this one fundamental drawback. I won't take much time with this. But it had this drawback as presented to me by many of our employees, namely that the dividends were only paid in good times. "When employment is at a peak, and they are working on a 40-hour schedule, which is our standard work week, we don't need it so much then." They were glad to have it, but that doesn't help them any when the week drops down to 28 hours or 20 hours. When the company doesn't make any money they don't pay any dividend, and the employees get both peaks and valleys. That was the drawback. Of course that is the fundamental thing that I think employers in industry have to worry about. It is a big subject. But they didn't like it.

So I asked a great many of our people around the plant, and a great many came to me, about the pension plan idea. It is becoming an acute problem in our company now, after 40 years of existence, namely, that we have—I have forgotten the exact figures—but perhaps 50 or 60 men and women over 60 years old. Most of them haven't saved anything up. I think that is no criticism of the individual. I frankly do not see how the average laboring man that raises a family and carries on on a decent scale is going to be able to save money. Some few of them do; they are lucky; but if they have a lot of sickness and a lot of other things come up, they are not going to hit 65 with a lot of money in the bank, in most cases, and I don't think they should be criticized for it.

They had their own ideas about starting a pension scheme. Well, of course, that wouldn't work. You know you can't start a pension scheme that is going to last and pay out on a shoestring. So during this last summer we worked up with one of the biggest insurance companies, the Travelers' Insurance Co., which handles that sort of business, the present Sangamo pension scheme, which was like many others. They are all pretty nearly the same, with a few different features.

In other words, at age 65 they are simply paid for life a certain amount per month. I won't go into the details; I know you are familiar obviously with the general idea of pensions for workers.

It happened that I had the most to do myself with handling that thing, and I made some rather serious mistakes in the way I went about it. I had the feeling that all of our employees would accept a pension plan very gladly. Well, I was very much mistaken about it; fooled. The young people, I am sorry to say—and I can understand it, I can see their point of view—a young man 25 years old is not a bit concerned about what is going to happen to him, or he is exceptional if he is, what is going to happen to him 40 years hence. He says, "I want as much money as I can make; I am going on up in the world; I will be independent and wealthy, possibly, at the time I am 65; I am not going to bother a hoot about this pension."

The girls all expect to get married, and most of them do.

The appeal comes to the group of thinking people in their forties and fifties, who are willing to lay aside something and plan and save for a retirement fund. Although again some of our older people—I hope I am not digressing; I will make my remarks brief—I mean the people of 62 and 63 and 64, weren't going to have anything to do with it, and they got a pretty fairly decent income. We set this thing up so that they would normally, the employee would normally get, no matter what his age was, not less than about 40 percent of what would be his regular income.

The younger ones, if they keep in it, are eventually going to come out with a good deal more than that. But some of the older fellows, the older employees, said: "No; we are not ready to retire; if the company, when I am 65, is going to put me on the shelf, that is very nice; but I do not want to retire then."

We explained to them that we didn't want people that were perfectly able to work to quit; we wanted them to keep on. But from the company's standpoint we have a factor there that will enable us to carry on, with the proper retirement of our older people, which is fundamentally important, because you have got to do something about it. Industry just can't take the attitude that they won't do anything—at least I don't think so—and say that the Government will or should do it. I don't believe that. I think it is up to the industry to see what they can do about it to help out on the thing.

Now, all of these things—that is a rather haphazard, sketchy talk on the thing, and I know you will have a lot of questions, that I will be glad to answer to the best of my ability—all of these things have had a very decided effect, in my opinion, on the feeling of our employees. It is good. I know pretty well what is going on there. We haven't more than 12 or 13 people there in that plant that haven't an intense feeling of loyalty primarily to Mr. Lanphier, which they should have, because he is the man that has really done the thinking and the planning and carrying through on this, and also loyalty to the company, using the broad term, and the other officers in general.

The few people that are not satisfied are chronic kickers; they are not "reds," they are not bad, they feel rather important. They never will be quite pleased with any situation and they don't do a great deal of harm. They kicked against this pension plan and influenced some people, but I find out that while we only have about 84 percent of our employees that actually signed up at the time, I am convinced that most of them as time goes on are going to come in and get into the thing.

There was a little heat right at the start—"No; we are not going to go into anything like that"—but that has really died down now and it is reflected in their work. There are no loafers; they are not deliberately trying to stall, and there is no sabotage; we are not the least bit concerned about that, about them being careless or destroying machinery; and from the standpoint of the management of the company I think that the money that we have spent along these various lines, which—let's see, last year I believe we expended some $172,000 in what you might call, very broadly, profit sharing, which is these various things that I have been talking about; that on a total business or a total net income of $1,000,000, not quite, but almost. In other words, that is pretty close to one-fifth, you might say, of what we are making in the way of profits that is going back into that line of endeavor.

Senator VANDENBERG. How did it compare with the amount of dividends paid?

Mr. FUNK. Let's see. We paid last year more than that; we had a big year last year. We paid roughly between four and five hundred thousand dollars in dividends. But, of course, this year we will spend almost as much as that, or practically the same amount, on that line of endeavor, whereas the dividends will be way down.

Now that is a very broad statement and I don't know whether that is the type of thing that you wanted to hear, or were interested in or not, but that is the story, and I will be very glad to amplify it or answer any questions.

Senator HERRING. You are paying the prevailing wage scale?

Mr. FUNK. We are; yes. As a matter of fact our wage scale, when compared with our competitors, I might say, the General Electric and the Westinghouse Co.—we know pretty well what they pay—also the electrical industry in Chicago, and there are about 18 or 19 firms up there that compile figures—so much for a machinist, so much for operators of punch presses, and the various types—yes, we are above the local scale, and well up with any of the trade organizations, a little bit ahead of Chicago.

Senator HERRING. Are your employees organized?

Mr. FUNK. They are; yes, sir. They formed their own organization, and I really mean it when I say that we had absolutely, the officers of the company had absolutely nothing, to do with it at all. There were many of our older people that felt that—well, let's call them some of the outside organizations which were pretty active in that part of the country—might come in there and temporarily, at any rate, attract some following.

So these people—I say I didn't know, and I know nobody else knew anything else about it—went downtown and hired a lawyer and had a formal contract drawn. They call themselves, and practically everybody in the plant belongs, the Selco, Sangamo Electric Co. They met us with their contract. A committee called on Mr. Lanphier and me, and the contract contained the provisions, usual provisions, a little something about wages, working hours, and so forth, and so forth, all of which was our standard practice at the time. That is, we for a long time have only worked 8 hours a day and a 40-hour week. They have no idea of going beyond that. We don't work at all on Saturdays, that is, the factory doesn't; the offices do. And we pay time and a half for any overtime, which seems to be the standard practice as far as I can see in the electrical industry.

So there really was nothing that they asked for or wanted to ask for in the way of fundamentals, that is, in regard to wage scales, which we were not already providing.

They do come after us all the time—I have had a lot of experience in that with the committee, on the subject of seniority, which is bothering them terribly, and it is a pretty tough thing to tackle. They have just gotten their teeth into that thoroughly now, and anybody who has 1 day's seniority over anybody else, they are mighty proud of it and they are going to be sure that they get the breaks, which is all right. It does present some problems, but the committee comes up and we sit down and talk them over, we don't always agree, but I try to be as fair as I can.

Senator HERRING. They are not affiliated with any national organization?

Mr. FUNK. They are not.

Senator HERRING. And all these various social items that you have given to them, were they arrived at through negotiations with the employees or was that determined by the employer?

Mr. FUNK. That was determined entirely by the employer.

Senator HERRING. They were not even consulted about them?

Mr. FUNK. They were not—Selco has only been in existence for a year and a half, but previous to that the older group of men and people in this and that department, were consulted about various things. I don't think we consulted them enough on this pension plan, but that is a mistake that was made.

Senator VANDENBERG. When you discontinued your wage dividend or your service warrant plan, and went to the contributory retirement plan, was it your conception that there was a greater incentive in the new plan than there was in the old one?

Mr. FUNK. It was mine. I am not sure that I wasn't somewhat mistaken. Of course, that wage dividend, service-warrant scheme, as we called it, had a good deal of bearing on the acceptance of the pension plan. We knew it would have. We could not do both. The thing was growing to a point where—a pension plan for a group of old people is expensive, it costs a lot of money—we should have done it years ago, but of course you don't wake up to those things until the average age of your group of employees is where it costs a lot of money. I could readily see a lot of people did not want to give up the service-warrant plan. I don't particularly blame them, I can sympathize with them. The younger people that had built up a certain number of service warrants would say, "That is no good, you are getting me to contribute and you are taking something away from me, and I don't get this pension for 40 years—what is it all about?"

Senator VANDENBERG. You canceled the warrants?

Mr. FUNK. Had to, yes, sir.

Senator HERRING. This $172,000 is put in as the cost of the business before you got to dividends at all?

Mr. FUNK. Surely.

Senator HERRING. It isn't a profit sharing, to that degree, is it?

Mr. FUNK. No.

Senator VANDENBERG. What is your final conclusion as to which plan is preferable, the compulsory pension or the wage-dividend warrants?

Mr. FUNK. The pension plan.

Senator VANDENBERG. You prefer the pension plan?

Mr. FUNK. Yes, sir; I think that this flurry was occasioned by improper handling of the thing, mostly on my part, or rather my convictions that almost anybody would be glad to accept that. They are beginning to think about it more now, the idea of having a fairly decent retirement income is beginning to appeal to people to whom it didn't appeal before.

Senator VANDENBERG. Your pension plan produces far greater benefit payments than the Social Security Act does, I apprehend?

Mr. FUNK. Yes, sir.

Senator VANDENBERG. Could you have kept your wage dividend going and just operated under the Social Security Act, so far as retirement pensions are concerned?

Mr. FUNK. Well, for the younger people, possibly, but you see the people that are in their sixties now, they are not going to get very much out of thhe Social Security Act, or at least not what we wanted them to have. Of course, they could live on it. I am not criticizing it; it is all right.

Senator HERRING. Have you had any labor troubles?

Mr. FUNK. No, sir; we have never had any labor troubles at all, and I am sincerely hopeful that we won't.

Senator HERRING. Thank you.

Mr. Sheaffer. Mr. W. A. Sheaffer, president of the Sheaffer Pen Co., of Fort Madison, Iowa.

STATEMENT OF W. A. SHEAFFER, PRESIDENT, SHEAFFER PEN CO., FORT MADISON, IOWA

Mr. SHEAFFER. Senator Herring and Senator Vandenberg.

Senator HERRING. Just proceed in your own way, Mr. Sheaffer.

Mr. SHEAFFER. Well, it is really encouraging to industry to see a hearing conducted by two outstanding men of each political party, men—I have not known Senator Vandenberg except by reputation, but his fairness to industry is known and it is much easier to say what little I have to say in the presence of people that are helpful, that are in a receptive mood.

And I can't help but go back a few years to a thing that makes me more at home with Senator Herring. He was in business and we were struggling in the fountain-pen business, and it makes me feel at home knowing that he was paying his scrub women $5 a day when we couldn't afford to.

Profit sharing is probably the greatest subject that has come before any hearing in the last few years. It is the most far reaching in a democracy of any one thing, I believe. It could contribute more to increasing wages, expanding employment, making a better democracy than any one thing.

The profit sharing or the merit system are about one and the same thing. I have seen by the papers that some of our businessmen think that profit sharing should only extend to the management of the business. That may be true in a great many businesses; I am not prepared to say; but in our application we have had profit sharing extend to the most humble employee, because we believe that the most humble employee that is working with us is entitled to his just share for his contribution to the success of that industry.

The woman that scrubs the floor, the night watchman, can either contribute a great deal to a successful industry or they can do the little things and neglect the good things that will help to wreck an industry. So for that reason the widest possible application of the profit sharing or merit system to industry, to every part of our national life, and it even could be extended to the Government with great profit and benefit, should follow.

If a farmer who produces and owns his farm could allow every employee on that farm to share in the success of that farm it would be beneficial both to the farmer and to the employee.

We all expect reward for every act of our life in some form. If a man sets a good example before his children, he expects to be rewarded by having better children. So if in employing labor and if in working in an industry of any kind we take into consideration the great help that harmony and the best endeavor plays in that industry, then we will be working in the right direction.

Of course, there is no place for profit sharing in an autocracy, because there is neither private profit nor sharing thereof, is contemplated.

Profit sharing, if generally applied to all branches of an industry, will greatly expand employment. In employing our sales people, whom we depend on for the expansion of our industry, we find that where they are not rewarded for results produced we do not get the best results; no matter how altruistic or how fine they are, and even though they will still do a good day's work. But if they are rewarded according to what they do, they will go on and do a little more than a day's work and keep the people at home employed.

The profit-sharing plan, properly applied, will definitely raise wages, because it is applied to the selling behind the counter. I mean fairly applied. If the person behind the counter receives additional pay, an additional pay check at the end of the week for having done a better job, the volume of that department has increased, a better grade of goods has been sold. Therefore the dollar volume of business has been increased. We realize today that we must have a dollar volume of nearly $90,000,000,000 in industry to employ all the employables. But there comes into the picture the duty of the consumer. We speak about the farmer and his duty, and the producer. We speak about the laboring man and his duty. We speak about the manufacturer and his duty and the retailer and his duty.

But those each have their group. The middlemen have their group. But we are all consumers and without the cooperation of the consumer of the United States we cannot employ all people. We can employ most of them by the profit-sharing plan. Suppose a man is able to buy a $50 watch and goes into a store and purchases a dollar watch. He has only a dollar that he has started in circulation. If he purchases a $50 watch, and is amply able to do so—I am not speaking of those that are only able to purchase the dollar watch because they should be given the best value possible for their dollar, they are the most needy and the ones that should be looked after first—but I am speaking of the duty of the consumer, who can afford a $50 watch. Such a man has his choice between purchasing the $50 watch and the dollar watch. He gives good mechanics work to do, making them better American citizens, if he purchases the $50 watch. If he only purchases the dollar watch, there must be a large share of that $49 taken away from him to employ people on Government jobs or on relief.

In the one case, you are giving men good wages which they spend. The things that they spend that money for, gives other people employment. This results in an expansion of employment. But when you spend the dollar and the other portion, greater portion—a large part of the $49—is employed by the Government to keep people on low wages, doing things that they are not happy doing, it is a definite injury.

No matter what people think, anyone in industry knows that you cannot expand employment by making cheap merchandise. Cheap merchandise must be made, because people are not able to buy the best merchandise at all times.

Money that is spent in profit sharing, in the profit-sharing plan, and is taken out of the profits, should receive favorable treatment. Reserves built up for the purpose of employing people in times of depression, should be favorably treated. But there should be a clause in there to keep the men receiving this favorable treatment from abusing this privilege. If industries ask for favorable treatment for building up a reserve to employ people in times of depression, and they fail to do so when that depression comes, then they have failed to do their duty, and that money should be taxed what it would have been taxed in the first place.

The idea of coming before this committee with a plea for favorable treatment, without a saving clause that if the treatment, the favorable treatment, that industry asks for isn't performed then there should be some way to take away that favor on the part that they didn't live up to their contract.

Industry can't employ people in times of depression if they are not allowed to build a reserve for it, but they should not be allowed to abuse that reserve.

In seasonal businesses, such as ours, it is quite difficult to employ people 12 months in the year. It can be done, but it is done at quite an additional expense. We sell probably more goods in 4 months of the year than we do in the other 8. Therefore we have to provide the capital in January to carry us through most of the year for the sole purpose of keeping our people employed 12 months in the year. We believe it is a beneficial thing to do. We believe it makes better employees. We believe it is fair, but I am only speaking of this feature because if they were to look at our statement on the 1st of March, they would want to take some of our money away from us. But if they were to look at it 4 months later they would wonder where we were going to get it from.

Employees should be paid a good wage before profit sharing is taken into consideration. That they are entitled to. In America every family ought to be able to own their automobile, their home, have plenty of time for recreation and to educate their family in the right way.

If the volume of business is to climb to the point where everybody is to be employed, then there must be no impediments put in the way of honest endeavor to employ everyone possible. There must be nothing done to decrease jobs. The prices of merchandise must naturally be lowered insofar as it is possible to do so until it reaches the masses, but after the price of an article of industry comes within the reach of the masses the driving of the price below that point decreases wages, decreases employment, and is definitely an injury to the country as a whole.

If a home was brought within the reach of all and everybody built the cheapest house that could be built, the plumbers would not have much to do, the electricians also, but if everyone—after that house was brought within the reach of the masses—if every man was induced to build as good a house as he could afford to build, that would result in an expansion of employment.

So in industry and in the profit-sharing plan I probably can relate it; I don't want to refer to our industry, but it is the only industry that I know anything about.

We have pens—so do our competitors—retailing from, we will say, $1 to $10. Now, let's follow what happens. After the devaluation of gold we found that we couldn't make a dollar pen and make any money, but we did feel that the consumer was entitled to the best that we could give for a dollar. We realized if we made a dollar pen and a solid-gold point that our workmen would have to work for a lower wage, that our dealers would have to make a less profit, that our traveling salesmen would have to work for less, and the people behind the counter in the retail stores would have to work for less. Therefore we felt that it was our duty to meet our share, and even if we couldn't meet cost it was our duty to supply that dollar pen, for which there was a great demand and which was the only pen a great many people could afford.

But we trained, as far as we could, our people to sell every man that could afford it a $10 pen, but to be sure that they gave the man that could only afford the dollar pen the best in the world for that money.

This should be true of all companies.

Now, what happened when we sold the dollar pen? The wages of every employee working on that pen were decreased. We started the dollar—but only one dollar in circulation. Our salesmen's salaries were decreased; the dealer that sold it only had one-tenth the volume: the clerk behind the counter, if he was on a profit-sharing basis, had his wages reduced. The customer got the full value of his money, which he should.

But when we sold and persuaded the customer to buy a $10 pen, we put $10 into circulation; we immediately raised the salary of every employee that touched that pen. Therefore they had more money to spend, which was an expansion of employment. The salaries of our salesmen were automatically increased; the dealer's volume was increased 10 times; the salesman behind the counter, his salary was automatically increased.

But was this fair to the consumer who paid for it all?

We found that the consumer that bought that $10 pen had a pen that would last more than 10 times as long as the dollar pen, and would always have a better writing instrument for his $10. As a consumer he had benefited 8 people by that transaction—that is, besides 1,000 people in the factory. He had helped, as a consumer, to expand employment.

So, if the consumers of the United States, along with the profit-sharing plan of industry, would realize what their actual duty is, and that duty is to buy as good merchandise as they can afford to buy, that this is the best way that we can raise wages, expand employment, and bring our volume of business up to $90,0000,000 a year.

I don't know as I have very much more to say. If there are any questions or if there are some points that I haven't brought out that I should, I would be glad to answer them. This work is unfamiliar to me.

Senator VANDENBERG. You haven't specifically described your own profit-sharing plans?

Mr. SHEAFFER. I thank you, Senator.

Our present profit-sharing plan is based on how much we earn. We pay what we believe is a good wage. As far as I know, my son, C. R. Sheaffer, tends to the labor relations and the wages, and those things, but he tells me that our wages are not affected by any laws, that we are ahead of any law that requires us to do anything.

Our profit-sharing plan, Senator, is based on the amount of the dividends we pay. Last year we paid a $2-a-share dividend and we paid 10 percent of each workers' wages every 6 months for every dollar we paid in dividends to our stockholders. We had to guess that at periods, but we try to pay this in addition to a good wage, about 2 weeks before Christmas and just at their vacation time in July.

In other words, last year we paid $2 a share in dividends, and we paid every employee in January and July 10 percent of the wages they had earned for that 6-month period.

This year we saw that our profits were running smaller and we guessed that maybe we could pay 75 cents a share twice this year, or $1.50. Therefore, we paid our employees this June, just before their vacations, 7½ percent of their 6 months' earnings. That was true with respect to every employee in our organization, traveling salesmen, and everyone. We paid a semi-annual dividend in October of 75 cents per share instead of $1.

Now, if we find that we are mistaken and that we can pay $1.25 next March, we expect to add 2½ percent to what we would otherwise pay in July.

So that on the basis of every dollar that we pay to our stockholders, we have been paying and hope to continue paying 5 percent of the wages that the employee earns.

Senator VANDENBERG. So that when the stockholder gets a 1-percent dividend on his money, the employee gets a 5-percent dividend on his wage?

Mr. SHEAFFER. Well, it depends on what that stockholder, Senator, paid for that stock. Our present stock cost many stockholders about $60 a share. It is only selling for about $27 now. A stockholder today who would buy our stock at $27 a share, if we were to pay $2 a share in dividends, would receive a much greater return than those that paid $60.

Senator VANDENBERG. Oh, yes.

Mr. SHEAFFER. But the majority of our stockholders, I believe, have paid about $60 a share for their stock.

When we pay those $2 a year in dividends, we pay our employees a 10-percent dividend.

Senator VANDENBERG. Let's put it this way. For every dollar that a stockholder gets on his stock, an employee gets $5 on his wages?

Mr. SHEAFFER. He gets 5 percent on his wages.

Senator VANDENBERG. Five percent, I mean.

Mr. SHEAFFER. And if we pay $2, he gets 10 percent. If we get up to $3, we will give him 15 percent provided there is no material change in the business outlook between the time we pay our dividend and the next bonus paying date. Please bear in mind that our dividend paying dates and our bonus paying dates are a month apart.

But we do believe that before you start the profit-sharing plan that you should give an adequate wage, so they won't be deprived of that even if you earn nothing.

Senator VANDENBERG. How many employees do you have?

Mr. SHEAFFER. The last time that I asked for an accurate count was a year ago, and we had 1,288 at that time. I would have to guess a little at this time, but I would say almost 1,100. We have more employees today than we had in 1929, and our business in 1929 was considerably greater than it is today. So it shows that we are making progress in giving a greater percentage of our income to the employees than ever before.

Senator HERRING. You have had no labor troubles, have you?

Mr. SHEAFFER. No; we have had a very healthy labor situation. We have done as we thought our employees wanted us to do. We have never interfered in any way. We have never told them that they shouldn't do this or that. They can come to us with their grievances any day. They elect their own shop people in the 20 or 30 departments to deal with the foreman. If they can't agree with the foreman, they are privileged to come to Mr. C. R. Sheaffer any time, because he is there most of the time.

And it is very interesting—awhile back they came to us and we thought we had very good walks, but they suggested to us that the cinders, the cinder walk on the west of our factory, was wearing out the soles of their shoes and the heels on the ladies' shoes, and we were asked to put in a new walk, which we did. And the request was very reasonable. You are liable to forget many of the things that need to be done. We find that we are derelict a little bit in our duties and we can't always see the employees' side of it—that is, I mean, not until it is called to our attention.

And therefore we find it very helpful in letting our employees know that anything that they think they ought to have they can bring it to us and we will grant it if we can.

Senator VANDENBERG. Well, I noticed, for instance, from your reply to our questionnaire, that already in 1938 you have distributed $147,000 in dividends to your employees.

Mr. SHEAFFER. 1938?

Senator VANDENBERG. Yes.

Mr. SHEAFFER. We have only distributed about half of that, Senator. The other half will be distributed next month. That will be in 1938 still. That figure is correct, but only half of it has been paid up to date. The other half will be paid about 2 weeks before Christmas, and we have only declared so far this year a 75-cent dividend.

Senator VANDENBERG. What is that in dollars and cents, that dividend to stockholders? For the year will it be in the neighborhood of $318,000, as indicated on the schedule?

Mr. SHEAFFER. How many stockholders have we there?

Senator VANDENBERG. It doesn't show.

Mr. SHEAFFER. We have a little less than 160,000 shares of stock outstanding, so it will be approximately $158,000 at the rate of a dollar dividend.

Senator VANDENBERG. So that your dividend to your employees almost equals your dividend to your stockholders?

Mr. SHEAFFER. Yes, sir; it is about half. But all the stockholder receives is his dividend and the employee bonus is over and above a good wage.

Senator VANDENBERG. No wonder you don't have any labor trouble. I congratulate you.

Mr. SHEAFFER. Well, we couldn't manufacture today at a profit if we didn't have the whole-hearted cooperation of our employees. So they are getting nothing more than they actually deserve. A little letting down, a little loafing, a little carelessness, would turn our profit today into an actual loss.

Senator HERRING. You have no pension plan, retirement plan, or anything like that, do you?

Mr. SHEAFFER. No; we have been working on one and we have been taking care of them in a great many ways. We have one of our officers today who has been sick a year on full wages. We had one of them pass away just recently and we arranged for a life income for his widow at about $200 a month, and we have a fund for the employees that we never allow a man to lose his home in the depression, or if he is in the hands of loan sharks we take him out, and if sickness comes on there is a fund available for him. We have a clubhouse for them for their convenience.

Senator VANDENBERG. How long has this plan been in operation?

Mr. SHEAFFER. Well, Senator, I can't tell you exactly. Part of it has been in operation for several years. The profit-sharing plan I can't give you the exact date on, because I didn't write the record down and I don't know.

Senator VANDENBERG. Is it some time?

Mr. SHEAFFER. Yes.

Senator VANDENBERG. And no labor troubles during this entire period?

Mr. SHEAFFER. No; no labor troubles.

Senator VANDENBERG. In other words, your pen is mightier than the sword?

Mr. SHEAFFER. Yes; I hope so. [Laughter.]

Senator HERRING. Thank you, Mr. Sheaffer. That is mighty fine of you.

Mr. SHEAFFER. You are entirely welcome, and I thank you for your consideration.

Senator HERRING. We will adjourn now until 10 o'clock Monday morning.

(Whereupon, at 2:35 p. m., an adjournment was taken until 10 o'clock Monday morning, November 28, 1938.)

SURVEY OF EXPERIENCES IN PROFIT SHARING AND POSSIBILITIES OF INCENTIVE TAXATION

MONDAY, NOVEMBER 28, 1938

UNITED STATES SENATE,
SUBCOMMITTEE OF THE COMMITTEE ON FINANCE,
Washington, D. C.

The committee met, pursuant to adjournment, at 10 a. m. in room 312, Senate Office Building, Senator Clyde L. Herring, presiding.

Present: Senators Clyde L. Herring (chairman), and Arthur H. Vandenberg.

Senator HERRING. We will next hear from Col. Hanford MacNider of Mason City, Iowa, president, Northwestern States Portland Cement Co.

STATEMENT OF COL. HANFORD MacNIDER, PRESIDENT, NORTHWESTERN STATES PORTLAND CEMENT CO., MASON CITY, IOWA

Senator HERRING. You have discussed this with Mr. Despain, Colonel, and you know the purposes of the committee. We are glad to have you here. You just go right ahead in your own way and tell us what you are doing out there in the way of a dividend plan.

Colonel MACNIDER. Yes, sir. We have a small company with a very simple fiscal structure. Our employees only number four hundred odd. For years, in fact up until 1931, we gave them a month's extra pay as a Christmas present every year, when the year's result allowed it. We dropped that in 1931 and picked up our present wage-dividend plan in 1935. The month's extra pay was not geared into the company's profits, and the decision as to whether they should get it or not was arbitrary with the management and did not make the employees conscious of our prosperity for the year. When we had to drop it they naturally felt they were losing something to which they were entitled, because they had been getting it for so many years. So when we were able to pick up this new plan we tried to gear it into the company's profits for the year, and also to recognize another point which we thought was important, their length of service with the company.

Our plan is very simple. We take the wage per hour and we get that in the case of the salaried employees by dividing the number of hours that they work in the month into their monthly pay check, and the rest of them have their pay per hour for the work they do; we multiply that by the number of years they have been with the company, we multiply that by the return paid on every $100 of invested capital. Everytime the stockholder receives a dividend every employee in the plant receives a dividend. If the stockholders get no dividends, the employees get no dividends.

We had three things we were trying to prove by this——

Senator VANDENBERG (interposing). Before you go on with that, what is the rate of dividend the employee gets? Is it the same as the stockholder gets?

Colonel MACNIDER. The same as the stockholder.

Senator VANDENBERG. Go ahead.

Colonel MACNIDER. In the first place, we try to take his value to the company, and that is represented by the wage per hour. Being a small company, we can get them all together. We have two or three meetings a year and explain this to them. We tell the employee we want him to receive just as much per hour as he can show us he is worth, that the higher he is paid the happier we will be. We wanted to recognize the long and loyal service to the company. We thought the man who had been with us for 25 years ought to be taken care of in a much better way than a man who had been with us just a year. There are a number of reasons for that, which I think are apparent. Breaking in a new man costs us money. Every year an employee, if he is doing his job correctly, should be of a lot more value to us.

Then we wanted the company to make money, and we wanted him to want the company to make money. We explained to him that every time a piece of machinery goes wrong or there is any waste in the plant, or if there are any accidents which put up our insurance rate, that the man who was responsible not only hurt himself, but he hurt every one of us that were in that company.

Now, we have never run up against the situation where we have been without these wage dividends, but it has been extremely helpful to us in the morale of our whole organization. We have made it perfectly clear to them that we are not giving them anything, that if we did not think we were making money by it we would not do it. We told them also when we found it was not making us money we intended to drop it, that there was nothing philanthropic about it, there was no gift in it, and that we expected to make a lot more money by the operation of this plan than it cost us.

Senator VANDENBERG. Do you think you do?

Colonel MACNIDER. I think so, Senator.

Senator HERRING. You have about 425 employees?

Colonel MACNIDER. About 416, I think, the present pay roll.

Senator HERRING. And they all participate?

Colonel MACNIDER. Everyone participates if he has been with us 1 year or longer, Senator.

Senator VANDENBERG. To make that just a little plainer for the record, Colonel, let us take a typical employee and see how this plan works, what he gets, and so forth.

Colonel MACNIDER. All right, sir. We will say a man gets 80 cents an hour; he has been with us 20 years; 0.80 times 20 is 16. We call those participation units, although it is not important what we call them. Say we pay 10 percent to the stockholders during that year, he gets $160.

Senator VANDENBERG. That is very simple.

Colonel MacNider. Now, if he worked 160 hours a month at $0.80, that is $128. He receives more than a month's extra pay during the year for his share.

Senator Vandenberg. Yes.

Colonel MacNider. The majority of our men have been with us over 10 years, I think about one-half of them 15 years continuous service.

Senator Vandenberg. This is after he has received, in the first instance, the full prevailing wage?

Colonel MacNider. Yes, sir.

Senator Vandenberg. Your wage dividend is not a substitute for adequate wages in the first instance?

Colonel MacNider. Not at all, sir.

Senator Vandenberg. You used one phrase which appealed to me greatly. You said that you found it desirable that these wage dividends should be geared to the profits. It has been my conception of the problem that you could not hope for any adequate labor consciousness except as these extra payments which they receive from time to time reflect, by rule of thumb, the actual condition of the company for which they are working. I think your phrase is an excellent one. I understand you to believe that except as these incentive payments are geared as to profit, they fail to achieve their essential purposes; is that right?

Colonel MacNider. Yes, sir. We have had that experience, Senator.

Senator Vandenberg. That is one of the reasons you dropped the extra month's pay formula that you previously operated on?

Colonel MacNider. Because that became a part of the regular wage to those men. Whether the company made any money or not, they expected it, and sometimes we were unable to pay it.

Senator Vandenberg. Have you had any labor troubles?

Colonel MacNider. No, sir.

Senator Herring. Your employees are not organized, are they?

Colonel MacNider. No, sir.

Senator Vandenberg. Do you consider that your wage-dividend plan has anything to do with your success in maintaining industrial peace?

Colonel MacNider. Yes, sir.

Senator Herring. Do other plants up there have any similar plans, do you know?

Colonel MacNider. No, sir; they do not. The plant just right across the street from us gives a bonus in years when they feel their profits entitle them to.

Senator Herring. Is the hourly wage they pay about the same as yours?

Colonel MacNider. It is the same.

Senator Herring. Yours is at least equal to that which they pay?

Colonel MacNider. Yes. The bonus which they pay amounts to as much or more than our wage dividend, but I do not think they have the same effect at all.

Senator Vandenberg. I would like to ask you one other question, Colonel, going into the larger field of incentive taxation which we are exploring somewhat. Would you think that the government could substantially facilitate plant replacements and plant expansions if there were tax credits allowed in some measure for such portions of corporate income as are put to these uses? Have you given any thought to that subject?

Colonel MacNider. Well, you do not mean the profit sharing?

Senator Vandenberg. No, no; I am talking now about the use of incentive taxation in respect to equipment replacement and plant expansion, for the purpose of stimulating employment.

Colonel MacNider. Now, Senator, to be frank with you, I do not believe in either incentive or punitive taxation.

Senator Vandenberg. You get the punitive whether you believe in it or not.

Colonel MacNider. I realize that.

Senator Vandenberg. Would not you like a little incentive to offset it?

Colonel MacNider. I think if the undistributed-profits tax were removed, it would have practically the same effect.

Senator Herring. Thank you, Colonel.

Senator Vandenberg. We were glad to hear you, Colonel.

Colonel MacNider. Thank you.

Senator Herring. Mr. Gerard Swope.

STATEMENT OF GERARD SWOPE, PRESIDENT, GENERAL ELECTRIC CO., NEW YORK, N. Y.

Senator Herring. Mr. Swope, we thank you for coming here. We would be glad to have you tell us anything you think would be helpful to this survey which we are making. We will leave it entirely with you to go ahead in your own way.

Mr. Swope. I do not know that I can add much to my letter to Mr. Walsh in regard to it. As I said to Mr. Walsh and Mr. Despain in regard to the questionnaire which we answered in detail, I think it is a very good, far-reaching questionnaire, one of the best I have seen, as a matter of fact, because I think it brings out quite the salient facts that you want to know; that is, the relation to sales, pay rolls, profits, taxes, and the various questions that are asked in regard to the relationship of those to each other. I will comment on some of those, and I will be glad if you will interrupt me with questions, because I do not have anything prepared with me.

Senator Vandenberg. Mr. Swope, I think it would be very helpful if you will just generally outline these various plans that you have for facilitating better industrial relations. The questionnaire will not be an exhibit, and the oral testimony is the thing that will be read by those who are consulting it for information. I think if you will just chat with us about your general outlook and the fashion in which you implemented these various plans, I think it will be very helpful.

Mr. Swope. All right, sir. I will start with the earliest, but not in any necessary sequence, in 1912, when we established a pension plan for our employees. It is a very interesting development, because the pension plan of the General Electric Co., when it was established, was entirely a company plan; it was something that was given to the employees, depending upon their service. That was modified as time went along, but the most, to my mind, far-reaching and constructive changes that were made were two, and they were in the twenties. First, it was put on a contributory basis. Personally, I believe that workmen want to bear their share of the cost for their own security; and secondly, I believe particularly in a country like ours that is the right thing that they should bear a part of their responsibilities. So we made it contributory.

Second, we put it into a trust fund, quite separate from the organization of the General Electric Co. The General Electric Co. could disappear tomorrow and the trust fund would remain. It now has in it $41,000,000 which the company has, over these years, contributed, plus $11,000,000, which is the amount that the employees have contributed. They are in two separate trust funds, with diversified investments quite separate and outside of the balance sheet of the General Electric Co.

In addition to that, of course, each year the General Electric Co. must pay them the pensions that had accrued before that and add to the pension fund. Three years ago we added to that pension fund some $10,000,000, which, in accordance with the Federal law, we are taking down at 10 percent a year, or $1,000,000 a year.

In this last year two changes, as I was saying to Mr. Walsh this morning, have been made in the Federal laws and in the New York State laws, under which we are incorporated: First, that the Federal law says you must have your trust irrevocable. Before that, our trust was revocable on 400 days' notice so that no part of it could ever appear in the profits of any particular year, which the lawyers said was the thing to do at that time; and second, the New York State laws did not allow your trust to stand longer than two lives in being. This last year they modified that, so you can have your trust for such a length of time as would serve the purpose of the trust. So we modified our trust. Now it is irrevocable and continues for the length of time to serve the purpose for which it was created.

As I stated, we have now $41,000,000 in the trust fund created by the company, and some $11,000,000 in the trust fund that has been paid for by the employees. Over these 26 years $21,000,000 has been paid out for pensions. We have now a little over 3,300 pensioners and their average pension is a little less than $800 per year. That varies with their length of service and their earnings. Those are the two conditions—length of service and earnings. That is 1.5 percent per year, and the retirement age is 70, but with the optional retirement age of 65, if they wish. The company, of course, has a right to retire them earlier and in that case we give what we call a life retirement allowance, which merges right into the old-age pension, when they reach the pensionable age of 65.

Senator VANDENBERG. Are all these pensioners retired from active service?

Mr. SWOPE. Yes, sir. Furthermore—and this is interesting—it interests me, at any rate—we make a survey of our pensioners each year. In the middle of this year the survey was made; and of the 3,300 pensioners 88 percent were in good health, some of them age over 80—it varied, of course, but none less than 65—and there were only, out of the 3,300 cases, 23 of those pensioners in want.

We have, in addition to this, a relief and loan plan.

Senator VANDENBERG. Before you go to that, are you through with the pension plan?

Mr. SWOPE. No; I am not, not quite.

Senator VANDENBERG. Excuse me.

Mr. SWOPE. The relief and loan plan helps the pensioners, not only in the way of loans but also in the way of relief. This relief and loan plan is formed by the company and employees. Now, Senator, I am through.

Senator VANDENBERG. How many employees are covered by the pension plan?

Mr. SWOPE. A little over 50,000 today.

Senator VANDENBERG. Is it compulsory?

Mr. SWOPE. Well, it is not compulsory; no. In fact, if you do not come into the additional pension plan, that is the contributions, you do not get the company pension plan. But you do not need to come in. Now, this is interesting: Since the Social Security law has been passed, some of the employees have thought: "Well, it does not make any difference. I do not have to pay. The Government is going to take care of me anyhow," and they have dropped out of the additional pension plan, and that means they have dropped out of the company pension plan, too.

Senator VANDENBERG. Did the Social Security Act, in its formula, collide in any way with your pension plan?

Mr. SWOPE. Not collide. Of course, it complemented it. We made a modification of ours so as to groove right into the Social Security Act, the Old Age Pension part.

Senator VANDENBERG. So that the two are running now in complete gear?

Mr. SWOPE. Yes, sir. We made that modification after the social security law went into effect January 1, 1936.

Senator HERRING. Did it increase your cost?

Mr. SWOPE. Well, of course, to that extent, it increased our costs, I suppose, or took it out of profit, as you will, but it is very difficult to allocate increase in cost, because of course the hope of industry is constantly making improvement in its methods, so even with higher wages, your cost of the products are not increased.

Senator VANDENBERG. Well, how much does title II of the Social Security Act cost the General Electric Co.?

Mr. SWOPE. Title II?

Senator VANDENBERG. Yes. That is the old-age pensions.

Mr. SWOPE. It is now 1 percent of our total pay roll. Our total pay roll is $100,000,000, so it would be $1,000,000. That is very easy to figure. But that is only a part of our cost, you see, because our whole pension cost has been around $2,000,000 a year, and this is, as I say, taking the place of only a part of it.

Senator HERRING. And you have reduced the cost of your plan to that extent, have you?

Mr. SWOPE. Yes, sir. In other words, our pension plan complements or supplements the old age act.

Senator VANDENBERG. Your pension plan was the first one that you inaugurated in your social program?

Mr. SWOPE. Yes.

Senator VANDENBERG. What is the next one?

Mr. SWOPE. Profit sharing.

Senator VANDENBERG. Let us hear about that.

Mr. SWOPE. That is interesting, too. It just shows the experience of companies as they go through these various valleys and peaks, valleys of depression and peaks of prosperity. We started in 1916 the profit-sharing plan, and on two different bases for all people, depending upon their service with the company. That is, over 5 years of service they were given 5 percent supplementary to their annual compensation, and for executive departments, depending upon the profit. That really is a profit-sharing plan; the other, frankly, was not.

In 1931, when the pressure became pretty severe and the 5 percent on our pay roll amounted to a fixed annual charge, I did not think we would be able to bear that, so we did away with that scheme, which we had a right to do on a year's notice. The profit-sharing plan for supervisors continued.

Then in 1934 we went to our stockholders and said, "Now, instead of a fixed annual charge depending upon our pay roll, whether we make money or not, we want a really honest-to-goodness profit-sharing plan for our workmen." We had been paying $8 on the old par value, $100 par of the stock, and we said after we earned that fixed basis, which is the stockholders' return, we want to take 12.5 percent of the net profit, as shown by our books and as reported to our stockholders, and distribute that among the working people. That means the working people, in the first place, those receiving less than $4,000 a year, and, secondly, to no one who is on extra compensation, as we call it, which is profit sharing in the departmental sense. That was done. Of course, that is not a fixed charge, that varies with our profit. For instance, in 1937 we distributed $5,700,000. I am giving you round figures because I do not remember them in detail. In 1936 it was $600,000; in 1935 it was not anything; in 1938 I do not know that there will be anything, but if there is, it is going to be very small. That is a real profit sharing, and that is paid in cash to the employees. The extra compensation, as we call it, is to department heads. That is, we try to divide our business by departments and say to a man, "Now, you are responsible for the development of the business in this department, in the increase in sales, the reduction of expenses, and if, after paying the same fixed charge of 8 percent of investment in that part of the business, only your part, not the total, if you increase the business in your department we will take 5 percent, or 2 percent, or 3 percent, depending upon the department and the competitive state, and divide that among those who are in the supervisory positions of that department."

That has been in existence since 1916, and that has worked well. Of course, that scheme goes to the top executives, but it may easily come about that you will have people in a department—not only easily come about, but it does come about—that you can have people in a department who will get extra compensation because they have made a profit in that department while the company as a whole, or the company executives will not get anything. That has happened several times and will happen again, no doubt. You can see how that can come about.

Now, in the 22 years since this has been established almost $100,000,000 of profit sharing has been distributed. Now, that is profit sharing, that is not pensions, that is not for anything else. I mean, that is dependent upon the profits of the company, and that has gone to, oh, thousands of people, 50,000 or 60,000 people on the whole, over that period.

Now, this is an interesting part, Senators, that I think you would be interested in, and I was interested in, as I happened to see it the other day—in connection with that we established investment companies. I am going to speak of that later. A considerable part of that $100,000,000 is now in the form of capital of these employees invested in these various plans, roughly about 58 million dollars. That is what we tried to do. We tried to keep the profit sharing in the minds of our people quite separate from their salary or wages. Salary or wages they can use for living, but extra compensation or profit sharing does not happen every year. We do not want them to count upon it, because if they do they get into trouble, and therefore. if they can, and we try to encourage it, if they can put some of it aside in the way of capital investment we try to encourage it.

Senator VANDENBERG. But it is entirely at their own option, as to whether it is done or not?

Mr. SWOPE. With this exception; for the workmen, it is entirely within their option. They can blow it in the next day after they receive it. They get it in cash. We do ask them to invest it, but that is, as you say, entirely at their own option. However, the upper executives, there in some cases we will impound it for 5 years. At the end of 5 years they can have it and then spend it as they wish but by that time we hope that the thrift and savings encouragement has been effective and they will retain a good deal of it as part of their capital investment. That has been done. The test of it, as I say, is the fact that some $58,000,000 is in these investment companies, and of course that does not include the amount that they have put aside in their own investments. For the workmen, if they do come into this what we call the G. E. Employees Security Corporation, which I will speak of in a moment, as you said, it is optional. They do not need to invest in it, but they may. With the upper executives there, we have a portion of it going into a diversified investment, public utilities, good industrials, and so forth, which a committee of their own people manage, quite outside of the General Electric Co., and part of it in the common stock of the General Electric Co., which they are free to sell the day after they receive it, but we give it to them in the form of shares at the market price prevailing at the time of distribution. After that it is their property; they can keep it or sell it, or do what they wish with it. That is the profit-sharing plan in general.

Senator VANDENBERG. So far as the great mass of your people are concerned, they would be under this plan which divides 12.5 percent of the net after 8 percent has been paid on the stock?

Mr. SWOPE. On the book value. That is now about 2 percent on the market value. It amounts to about 83 cents per share, and our market price is around $42, or it was Saturday.

Senator VANDENBERG. How many employees, roughly, would be under that particular formula?

Mr. SWOPE. Oh, last year it was something like 60,000 people. People who have been there less than a year do not share; people over

1 year share. They do not share in the same proportion, though, but that was decided on with the employees.

Senator VANDENBERG. In your long experience since 1916 with this general subject, and your shifting from one base to another, have you some general views as to the wisdom or unwisdom of certain phases of profit sharing? Are there any general considerations that you would lay down as a rule of action for an employer to have in mind if he is considering a profit-sharing scheme?

Mr. SWOPE. Yes; there are two or three.

Senator VANDENBERG. I would like to know what they are.

Mr. SWOPE. First, profit sharing is not in lieu of fair wages and salaries. That is one of the great mistakes that sometimes has been made. It is not in lieu of, it must be in addition to.

Second—and we have run into this difficulty—if your profit sharing amounts to a large amount and the man does not save it you have really done more harm than good. You have got to associate it, it seems to me, with an educational program that it must not be regar' d as a part of their annual income; it is something extra and shoulu ve put aside for the rainy days that do come. That is a very important part of the program, and that is education to put it away.

Third, of course, with this educational program, to make it as largely optional in the hands of the men as possible; and, fourth, to have it intelligible to him, as to what the basis of profit sharing is, we make a report to our employees, a copy of which has been filed with you—I can give you another copy—which states, just in simple language—it does not give a balance sheet and various things that we do have to give to our stockholders in accordance with the rules of accounting—it simply says our sales, our profits, then the amount of profit sharing calculated, which they are at liberty to verify, because we have it verified by an outside auditor. Does that answer your question?

Senator VANDENBERG. Yes. Bearing particularly upon the fourth point, that part emphasized, would you agree, as Colonel MacNider said earlier in the day, that any plan for additional compensation must, in some way, be geared directly to the profits of the company, so that the employee can have a conscious reaction to the company's condition?

Mr. SWOPE. Certainly, because, just as I said, ours was a fixed charge, we were afraid we could not bear it, and therefore we have changed it. As I say, this has been evolutionary. I do not mean we have reached a finality in it even today, because changes will be made no doubt in the future, but that is the situation as it is today. At all events, it is fluid.

Senator VANDENBERG. I assume you not only get a social satisfaction out of dealing with your employees in this fashion, but you also find it is profitable to deal with them in this fashion? In other words, is profit sharing good business for you?

Mr. SWOPE. Well, I hope so.

Senator VANDENBERG. What do you think?

Mr. SWOPE. I think so, but I do not know so.

Senator HERRING. In arriving at the basis for any of these plans, was there negotiation with the employees?

Mr. SWOPE. No.

Senator HERRING. There was not?

Mr. SWOPE. No; not originally, but later I met with them and told them the basis of it. Of course, the employees would like to have a larger share than 12.5 percent, which is perfectly natural, perfectly human, and some day they may get more. I do not know what the development of those things is going to be. However, they like the plan. It has been in existence, as I say, for a long time, and the very fact that we have this plan and also have the investment of their savings plan, and that has almost 30,000 people—that is entirely optional with them—almost 30,000 people have gone into it and their savings in that plan are about $30,000,000, or a little less than that—$28,000,000—which all shows that they do take some interest in it.

Senator VANDENBERG. What has been your labor experience, Mr. Swope? Have you had any strike during this period since 1916?

Mr. SWOPE. Not yet [knocking wood]. We have had unrest, just like everybody has had, but no strikes. Some of our plants have been organized, but everything has been quite satisfactory. I mean early in 1937, or going back further than that, if you wish, in 1918, under the War Labor Board, the chairman of which was Mr. Taft, as you will remember, the plan of representation of labor was introduced in Lynn, in our works there. That was after a strike in Lynn in 1918. That functioned until 1934. Then there were some of the people at Lynn that thought they would rather have their own union quite independent of the A. F. of L.—the C. I. O. then had not appeared—and they asked for an election. I happened to be on the National Labor Board at that time. That was before, you remember, Congress had acted. That was the executive instrument to deal with that. That was formed in August 1933. We had a secret election under the Regional Labor Board in Boston, and the independent union went out, and they functioned under a very good management, as far as the workmen were concerned, and we had no trouble with them. Then later they had a charter under the A. F. of L., which they gave up later and joined the C. I. O., and have remained there ever since.

Now, in some of our other plants—labor asked for an election in Schenectady; they formed a union as part of the C. I. O. That is true in several plants. At several plants they had an election and the independent union won, and at other plants there has been no election. In all of the plants, whether they have company unions, independent unions, or no unions, we have had no trouble.

Senator HERRING. We had a witness the other day who favored profit sharing, but said the basis of profit sharing should be arrived at through collective bargaining. Do you think that would affect your plan?

Mr. SWOPE. Yes; it would affect it. We are willing to discuss our plan. I mean, we have discussed our plan with our work people. Of course, I suppose, as I said a moment ago, they always would like to have a larger share than 12.5 percent, which is perfectly natural and human; it is only a question of when the time has come that it is wise to do it. Don't you see, this is experimental. You have to feel your way in the thing. There was great doubt in some of our minds when we established it. The old idea was that all of the profits belonged to the stockholders, and the only way you could share was to have your employees interested in it, and in this G. E. Employees Securities Corporation, which I spoke of, they have some $70,000,000 investment, and the largest investment is in General Electric, where they have 532,000 shares, which at today's market value is over $20,000,000. We wanted them interested in the profits of the business through that capitalistic holding.

Senator HERRING. Do you feel that negotiation through collective bargaining might be a threat toward management in any way, or interference with management?

Mr. SWOPE. Yes; it always is, but it is only a question of how reasonable both sides may be in it. I do not think, on the whole, that labor wants to interfere with management, but sometimes they do impinge upon it.

Senator VANDENBERG. You also have a so-called cost of living-adjustment item?

Mr. SWOPE. Yes.

Senator VANDENBERG. What is that, Mr. Swope?

Mr. SWOPE. You see, through 1935, when business was beginning to improve, there was a good deal of unrest. Wages had gone up, we had increased wages, and the question was whether you were going to increase wages too rapidly, and when you do increase wages of course it becomes more or less rigid. It is very difficult, not only difficult but heart-breaking to reduce them, and of course the fear on the part of labor was the question of the cost of living. Mrs. Workman has to watch the budget, and if costs are rising and her income is just the same, she is constantly complaining, so we tried to adjust it and made this effort to do so; that as the cost of living, which is the index given out by the Department of Labor, as the cost of living rises over the standard which was in existence at that time, we would increase the earnings of all those people receiving less than $4,000 a year. No cost of living adjustment we thought was necessary for the people getting a larger income than that. That started with 2 percent in October 1936. That means a man who is getting $30 a week as his earnings would get $30.60. That rose gradually until it was 5 percent. In other words, a man getting $30 a week would get $31.50. Then earlier this year, when the index fell—and this was really the test of it—we reduced the 5 percent to 3 percent, again in accordance with the index given out by the Department of Labor, so now that $30 man would receive $30.90. The increase was never objected to for the cost of living adjustment, nor has the decrease been.

Now, in practice, of course, the cost of living adjustment simply keeps your standard of living the same, as nearly as you can measure it. It does not increase it, but at all events it removes that question in the mind of Mrs. Workman, you see, that when one item of her food or diet goes up then she thinks her entire cost of living has gone up. That is not always true, but they distort that, and it is perfectly natural. This study of the Department of Labor tries to balance those various items and makes the cost of living a true cost of living index, and we base their earnings on that and we have had no difficulty with it.

That means since it has been in effect, since October of 1936, through 1937, about 15 months, $5,000,000 has been paid out, or a little over that.

Senator VANDENBERG. You have been paying out with the 60-cent dollar?

Mr. SWOPE. Yes; we pay in the 60-cent dollar.

Senator VANDENBERG. Mr. Swope, will you discuss merit rating?

Mr. SWOPE. I suppose now you are talking about my favorite subject, the unemployment insurance?

Senator VANDENBERG. Yes. It is a form of incentive taxation, is it not?

Mr. SWOPE. It is a form of incentive taxation that I believe in very heartily. I have written to Mr. Walsh quite fully on it, and I have spoken on it. I was on the President's Economic Committee and on your committee, Senator, on this revision of the Social Security Act.

Senator VANDENBERG. Yes.

Mr. SWOPE. And, of course, the unemployment-insurance law is left to the various States to enact. The first State to enact it was Wisconsin, which was a pure merit rating. It was plant reserves, and therefore if the General Electric Co., or the "Podunk Electric Co." had no unemployment, after a certain reserve was built up, they had no expense. In a way, if you want to get employers to make an effort to regularize or stabilize a plant, that seems to me the way to do it. We have done that in workmen's compensation. If I am a careless employer and my injuries and deaths and fatalities due to accidents are high, I should pay for it, because if Mr. Walsh there is a corporation employer and watches his business, puts in safety standards and reduces his hazards and his cost of accidents is low, he is that much better off and he can undersell me. That is pure merit rating, is it not? I mean, he gets credit for doing a good job and I bear the burden of doing a bad job.

It is not only a question of doing a good job or a bad job, because some businesses are more hazardous than others, which is inherent. Where a business is more hazardous than others and society needs those products, I think they ought to pay the cost of them. There ought not to be a vicarious atonement, as it were, that because they are a hazardous business they ought to be subsidized by the less hazardous business.

As I say, the first State was Wisconsin. That has a pure merit rating. In some States, take my own State, notably New York, it has nothing of the kind. We pay in our business the same percentage for unemployment insurance, whether it is good business, bad business, hazardous business, or perfectly safe business, a retail business or a quarry, they make no distinctions. Personally, I think if you are ever going to get the intelligence of management fixed on this job of endeavoring to stabilize employment on the basis of an annual wage, you must give them some sort of incentive. I will give you two experiences.

Senator VANDENBERG. That is a fine statement.

Mr. SWOPE. In one department of our business, employing about 6,000 people, we had no stabilization plan. It was a comparatively simple business. It was in our own hands. Styles did not change, the product did not become obsolescent, and so I suggested finally that we guarantee our employees, after they have been with us a year, a certain minimum of employment. The question was immediately asked: "Why do that? They know that they are getting it." I said, "Well, we know it, but they do not realize that they are going to have work for 30 or 40 or 50 weeks next year." So we put into effect this scheme. It went along. It did not cost us anything after the first year. It cost us some money the first year, to put it into effect, because we did not know how. After that, it did not cost us anything. We guaranteed these people two-thirds of the number of hours of work that they are annually paid for. When the social-security law, or the unemployment law went into effect in those States where they had a merit rating, we were willing to continue it. In those States where they had none, we just abandoned the plan. As a matter of fact, our employees really are no worse off, except they do not have any assurance now from us that they are going to have that much, and of course that assurance is sufficient often to quiet the minds of people that they are going to have that much work in 1939.

In another case, in 1931, we said to our people in a very much more difficult end of our business—that is, in our big capital goods, where we build turbines, big generators and motors—that we would guarantee 6 months; that they would never get less than one-half of their wage per week. I was awfully glad when the 6 months rolled around, because we did not know how to do it with capital goods. It depends upon whether the public utilities can buy, depending upon whether they can finance their requirements or not, and so many things enter into it that you are perfectly familiar with, that might interfere with the conduct of that business. Therefore, as I say, I think there can be a far more constructive plan worked out, if you want to get the intelligence of different people concentrated on this job, by giving management an incentive to stabilize and regularize employment, and I do not think you will do it unless you do give them an incentive.

Senator VANDENBERG. Now, you suggested the merit rating in State unemployment-insurance laws as one practical means of doing it. Have you any other suggestion?

Mr. SWOPE. On unemployment?

Senator VANDENBERG. No; in respect to this use of the tax incentive to achieve the results you are talking about.

Mr. SWOPE. It may be extended to other forms. I mean, you have considered it in Congress, I know, in the tax on undistributed earnings.

Senator VANDENBERG. Yes.

Mr. SWOPE. Whether that portion of it which is used for maintenance or plant expansion should not be free from that tax, but you modified that tax anyhow so that really has been solved in another way.

Senator VANDENBERG. What would be your opinion as to the result?

Mr. SWOPE. I think it is wise.

Senator VANDENBERG. It is wise to do it?

Mr. SWOPE. Yes. I mean you really earmark that reserve. That does not go back to the stockholder, and therefore you really supply the additional capital for the company that is operating and giving more work to people, which of course is what you want to do. In other words, the moment that you fix profits in such a form that it does not go back to your stockholders, like if you have a pension trust, or build additional plants, or additional maintenance of plants, well, then, it does not go to the stockholders at all events in dollars.

Senator VANDENBERG. Speaking generally, then, you are heartily in favor of profit sharing on a practical basis and of incentive taxation on a practical basis?

Mr. SWOPE. Yes; but how far you can extend incentive taxation beyond the points I have mentioned I do not know. I mean it is a difficult problem.

Senator VANDENBERG. I think you made a very great contribution to us, Mr. Swope. Personally, I am greatly indebted to you.

Senator HERRING. Unless you have some suggestions you would like to give to the committee, Mr. Swope, we appreciate very much your coming here and the contribution you have made.

Mr. SWOPE. I do not know of anything else that has not been filed with you either in the document or the answers to the questionnaire.

Senator HERRING. We thank you very much, sir. We will adjourn until 1:30, when the next witness will be heard.

(Whereupon, at 11 a. m. a recess was taken until 1:30 p. m. of the same day.)

AFTERNOON SESSION

(The hearing was resumed at 1:45 p. m., pursuant to the taking of a recess.)

Senator HERRING. The hearing will be resumed.

Mr. Nunn—Mr. H. L. Nunn, president of the Nunn-Bush Shoe Co., Milwaukee, Wis.

Mr. Nunn is a pioneer in the field of the annual wage. He has the most unique plan that we have yet found.

We are delighted to have you here to tell us about that plan of yours.

Mr. NUNN. Thank you, sir.

Senator HERRING. Proceed in your own way.

STATEMENT OF H. L. NUNN, PRESIDENT, NUNN-BUSH SHOE CO., MILWAUKEE, WIS.

Mr. NUNN. We started in what you might call profit sharing back in 1917, with a plan very similar to that of Sears, Roebuck. In fact, we copied it after Sears, Roebuck. But when the hard days of 1932 came, we wondered whether we knew where to put anything that was safe, and we discontinued the plan. Those days of 1930, 1931, and 1932 caused us to do a great deal of thinking about our relationship with our workers. We couldn't help but be impressed with their insecurity and with the fallacy of a wage rate. We became convinced at that time that it was really the annual income of a man that amounted to anything, that what he made per hour or per week or per month was very immaterial. How many of the good things of life he could have depended on how much he made a year.

And we turned our minds to trying to think of some way that we could change this relationship that had always been in existence where we treated labor as a commodity, bought their labor at so much an hour, so much a piece, used them when profitable, and let them go when they were no longer useful to us; and we tried to think of some way that we could make them an integral part of the business, the same as a bookkeeper or a stenographer, so that they could feel more attached to the business.

We realized that it was impossible to guarantee an annual wage to a worker without having some guarantee of the amount of production that we could sell. As a matter of fact, we believe that that is paternalistic and it is unsound.

But we did go to the books and we discovered something that we have since found is not unusual at all, that the amount of money that we paid production workers ran very constant; at the time of high prices, low prices, good times and bad times, that that proportion of a dollar that they received for production had only varied very little. As a matter of fact, in our Milwaukee plant where we employ 900 men and women, it had only varied from 19 and a fraction percent to about 21. The average was just a little under 20. So we decided, after consultation with our workers—the fact is we went over it with them for quite a long time before we worked out this plan—that we would stop this senseless conflict of buyer and seller, buying labor at so much an hour, and that as long as they received a certain proportion of a dollar, why not agree upon that and that would settle the whole thing.

Senator HERRING. As I understand it, the percentage of the volume dollar only changed from 19 percent to 21 percent, that is, the percentage that went to labor?

Mr. NUNN. That is right, that is, on the wholesale price.

It is true in some industries that that would not perhaps be practicable, that it might be necessary to pay a percentage of the added value, eliminating the cost of raw materials, but I am convinced in my study of the matter, that one of the two systems can be used, either a percentage of the wholesale price or a percentage of the added value.

So we made a contract with our workers on July 1, 1935, that we would pay them 20 cents, as a group, out of every dollar's worth of shoes they produced, and since July 1, 1935, our workers have received a check that in no case has been less than 92½ percent of what a full 40-hour week would have been; and in addition to that they have received extra checks.

The plan called for regularizing their pay by estimating the yearly income and dividing it by 52, and paying them each week what we might call a drawing account, then keeping track each month of the amount of production, the earnings, and what they drew against that, and adjusting at the end of the year, if necessary—of course, it always was necessary because you can't estimate accurately.

In the fall of 1937—of course, up until that time the worker had always earned more than he drew—but in the late fall of 1937 business fell off and the workers, their drawing accounts, amounted to more than they made and they ran up a deficit. By agreement, however, with them, we permitted that deficit to run a little longer than we could have insisted by our contract, and only now has the deficit been wiped out. It will be practically wiped out the first of this month.

Senator HERRING. It is wiped out by increased earnings?

Mr. NUNN. By the fact that our production has gone up since the spring, and they have been earning, since May, more than they drew.

Senator VANDENBERG. When you say 20 cents out of every dollar produced, is that on the wholesale price?

Mr. NUNN. That is right.

You see, at the start, in July 1935, their drawing account for each week at the start was 92½ percent of what they would earn in a full 40-hour week.

The difference was that they received this every week whether they worked 40 hours or 30 hours, or didn't work at all. That was purely an estimate.

On the 1st of January 1936—you see, under this plan, their income increases automatically as the price structure increases, and as prices were going up their income would "up," and we increased the drawing account the 1st of January to 40 times what their old hourly rate had been, and we now call it a differential rate because they don't have a wage rate any more, but you do have to have a differential rate because some men are more skillful than others, and some do more work than others. They all have a rate that we call a differential rate, and that rate has varied.

I think that you can better understand it if I put it in relation to what they earned for 40 hours at the start of this contract. That weekly drawing account has ranged from 92½ percent to 112½. In addition to that, in the good years, they have received approximately 5 percent extra payments because they earned more than they drew.

If you will permit me to say so, I think that if American industry will share the gross dollar with the worker, it will prove a more satisfactory plan than attempting a scheme of sharing the net dollar.

I like the idea of removing that conflict. I like the idea of making it a common enterprise, which we have done. Now, you see, under this plan we don't buy the labor of our workers any more, they sell it direct to the people who buy our product. Our interests are exactly the same. We both have the same interests in putting in labor-saving machines, we both have the same interests in efficiency, we both have the same interests in eliminating any element in the factory that tends toward discord or inefficiency.

Senator VANDENBERG. Excuse me—how would you have the same interests in labor-saving machinery, assuming that it might throw a hundred of them out of work?

Mr. NUNN. No; it wouldn't throw them out of work under this plan; pardon me, Senator.

Senator VANDENBERG. That is what I am trying to get at. Why not?

Mr. NUNN. Under this plan we can't lay anyone off. I think maybe I should go back a little bit and explain that since 1915 we have had a system in our business of never doing anything arbitrarily. We have never hired a man, we have never discharged a man, we have never changed a rate or decided upon a vacation or a working day without the workers agreeing to it. Under this plan there isn't anyone laid off. If we put in labor-saving machinery that would cut down the labor necessary; it would mean that until we had a natural loss that we would have too many people, that is true, but there wouldn't be anybody laid off; they would just have less work to do until enough workers died or left, to bring it down to what was needed.

As a matter of fact, we have had that situation once or twice, although it hasn't been any large proportion of the workers. In the shoe industry we haven't had any radical improvements in machinery that would mean a big change, and it might be a little embarrassing if we were in an industry of that kind; it might be necessary to have in our contract a provision that would enable readjustments due to competition.

We recognize the fact that when our competitors are not on the same basis that if there were some revolutionary change in the process of making shoes, that we might not always be able to pay 20 percent out of the dollar; it might have to be changed.

Senator VANDENBERG. Is your contract with each worker individually or with the group?

Mr. NUNN. Oh, no; we have always dealt with our workers as a group, long before this plan went into effect, since 1915.

Senator HERRING. But because of the increased efficiency you turn out more of your product in shorter hours, less working time, and they would benefit in the same way from the profits, and would work less hours until you built up a bigger business?

Mr. NUNN. That is right, or until we lost employees.

Senator VANDENBERG. Unless you had such a revolutionary improvement that it would create a factor you couldn't overcome?

Mr. NUNN. That is right. But we believe thoroughly that labor in an industry should be an integral part of that industry. We believe that what is needed is more democracy in industry. We believe that the workers should not only have a voice but a vote in everything that affects their welfare.

We believe that both labor leadership as well as industrial leadership have been wrong in having too much power at the top. Of course our organization is a factory organization—I am talking about the workers' organization—it is one that was not imposed upon them. It is one that has developed in an evolutionary way since 1915. The management has been friendly to unions, has never opposed them. It has been entirely the will of the workers themselves that they have what they have.

But I think that the thing that they like about this organization is the fact that they control it, that they don't have imposed upon them leadership, they have developed their own leadership and they like to use that leadership. I think today that they would gladly associate themselves with an international union if it were not for that fact, and I think that that is a weakness in the national union set-up. I don't think they have enough democracy, and I think the same thing applies to industrial leadership. I don't believe in the open shop. I believe it is wrong to give to any man arbitrary power over other men. I think that when a man is given charge of a department, as is often done in an open shop, with the power to hire and fire and direct as he pleases, without recourse, that it is a dangerous thing; there is too much power in one man, and it leads to these things that we have seen over the last year or so. We don't want quite so many dictators. That is the way I look at it.

Senator VANDENBERG. At home or abroad?

Mr. NUNN. That is right, in political life or in industrial life.

Senator VANDENBERG. New Deal or old deal?

(Mr. Nunn laughing.)

Senator HERRING. Wisconsin or Michigan.

Senator VANDENBERG. Yes; or Iowa.

Mr. NUNN. And I would like to say this, too. I have been pretty close to the working people for the last 35 years. I am convinced that they are more interested in a job than they are in pensions and profit sharing; they are more interested in having a job and having security. I don't find that our people, even when they get old and rather weak, want a pension; they want their job, they want to be able to come to the factory and know they have a job. Security is what they want.

Senator VANDENBERG. Well, where does this Nunn-Bush profit sharing and retirement fund, that is described in this booklet, fit into this situation you are discussing?

Mr. NUNN. It fits in in this way, that even though we have agreed that 20 percent is a fair—under ordinary circumstances—a fair division, 20 and 80, there are years that we feel that the capital interests in the business have earned perhaps more in proportion to their necessities, let us say, than labor has received for their necessities, and that plan provides that the directors in those years can put into this fund a part of the earnings, which is credited to the worker at his retirement.

I will say frankly that I don't think very much of it. It is just a means we have found to do a little something additional, but I don't like it very much for the reason that it seems a little too paternalistic.

Senator VANDENBERG. It is entirely at the option of the management?

Mr. NUNN. That is it, exactly, and we are trying now to think of some better way to do it. I am not pleased with it or satisfied with it.

Senator VANDENBERG. When you allocated this 20 cents out of every dollar to labor, did I understand you to say that that was in agreement with labor itself?

Mr. NUNN. Oh, yes.

Senator VANDENBERG. Did you undertake to allocate the balance of the dollar?

Mr. NUNN. We have, to some extent; yes. The officers of the company receive a fixed percentage of the dollar; the office help receive a fixed percentage; the shipping department receives a fixed percentage of the dollar.

Senator VANDENBERG. Is there anything confidential about it; would you object to letting us have the figures?

Mr. NUNN. The only trouble is that I don't believe I have them, not being intimately connected with those departments; that is, I have been more responsible for the manufacturing end of the business. As a matter of fact, I know I haven't them with me. I would be glad to furnish them to you.

Senator VANDENBERG. Suppose later that you furnish them to the committee. It seems to me that that is a very essential part of your picture.

Mr. NUNN. I would be very glad to do that.

I would like to add one thing that I neglected.

During this period of some 3½ years there has only been one man separated from the pay roll. There has been one man discharged and no one laid off in that time. Of course, the man that was discharged—that was with the consent and approval of the workers.

Senator HERRING. Is there an increased reward based upon efficiency?

Mr. NUNN. Yes. This differential rate that I speak of goes up and down according to efficiency. If a man increases his efficiency, his differential rate is increased.

Senator HERRING. Well, as they get a certain percentage, of course, if the costs go down and the profits go up, they do get an increase as a result of that, although it is the same percentage?

Mr. NUNN. The same percentage, yes. It is possible that at times the prices might go up and profits increase faster, that is true, and that is the reason that we felt the need of some additional way to make a fair division, but that balances up pretty well. Of course, other years it is the other way.

Senator VANDENBERG. Do you recall, offhand, how much of the dollar is allocated to profit for capital?

Mr. NUNN. There isn't any part that is allocated; I can tell you offhand about what it has been. In 1937 it was approximately 3 cents out of every dollar. In 1936 it was a little less than 5 cents out of the dollar. Those are representative years, I would say. As a matter of fact, 1936 was above the average.

Senator HERRING. You have had no labor troubles, have you?

Mr. NUNN. No; we have never had any labor troubles.

Senator HERRING. These wages which you pay are as high as any paid in competitive shops?

Mr. NUNN. The average hourly income for 1937 was 33 percent higher than the average. The annual income of the workers, as far as we know, was the highest of any shoe factory.

Senator HERRING. That is, including the profit sharing?

Mr. NUNN. No; that is purely the 20 percent.

Senator HERRING. Purely the 20 percent?

Mr. NUNN. Annual income; that is right.

Senator HERRING. Wasn't there a Cooperative Shoe Co. up in Milwaukee that had six or eight hundred employees?

Mr. NUNN. Not that many. There was a Cooperative shoe factory there but they had only 75 or 100 employees.

Senator HERRING. They did away with management and then failed?

Mr. NUNN. Well, they had management, but they failed. I am afraid they didn't have very good management.

Senator HERRING. Well, just proceed and tell us anything you can recall of this unique system of yours, because it is most interesting.

Mr. NUNN. I think that I have covered what we have done pretty well. I might just call your attention to the fact, however, that we feel the wage-rate system is too rigid. As prices go up and as men fight for an increase in wage rate, they don't realize that they are not increasing their income. The very objective they are seeking is not obtained, because statistics show that as the wage rate goes up the number of hours worked goes down, and their income for the year isn't any more. But everything that you buy costs more.

Senator HERRING. What is your average annual wage, would you say?

Mr. NUNN. It was $1,346 in 1937.

Senator HERRING. And that compares favorably with the average annual wage of your competitors?

Mr. NUNN. Yes. About half of our workers are girls, shoe manufacturing is a very light industry.

Senator HERRING. So this is the average including four or five hundred girls?

Mr. NUNN. That is right.

Senator VANDENBERG. And that compares with about $1,000 a year for the 10-year average prior to 1935; is that correct?

Mr. NUNN. In our business?

Senator VANDENBERG. Yes.

Mr. NUNN. Well, I don't recall those figures, Senator. If we have gathered the figures, I don't recall them.

Senator VANDENBERG. Well, I think these figures from your records would indicate——

Mr. NUNN (interposing). I would presume that would be about right.

Senator VANDENBERG (continuing). They would indicate that your system has not only been successful from your point of view but has substantially enhanced the annual earnings of the employees?

Mr. NUNN. Well, it is bound to, because management now has an incentive to regularize their production. They have to look upon the workers as a part of the business. They can't just hire people indiscriminantly when they need them, with the realization that they can lay them off any day they want to, but we have to "stop, look, and listen" before we put on additional people, because they are ours when we put them on. So we have to constantly think of ways to regularize, to not manufacture more goods than we feel there is a reasonable chance that we can keep on making, and we think that any plan that gives management an incentive to regularize production is a good plan.

Senator HERRING. How much does your volume vary with the seasons?

Mr. NUNN. It varies a good deal. I would say that if we made goods just as we need them in this Milwaukee factory where we make 3,000 pairs of shoes a day, we would have to make 5,000 pairs at certain seasons of the year, and other seasons we probably wouldn't need over 1,000 pairs.

Senator HERRING. So you make them up in advance?

Mr. NUNN. That is right.

Senator HERRING. How do you control the styles; don't the styles change on you?

Mr. NUNN. There is a fixed part of our production that is staple, although it is true there are many businesses that couldn't do it to the extent that we do. I appreciate that. But that makes no difference, I don't care how seasonal the business, every concern can pay—there is a certain percentage of the dollar, either the added value or the wholesale price, that goes to production workers, and I don't care if they can only run 6 months a year, the worker has to live 12 months a year, and he has to pay rent every month, and has to buy food every day, and I think that his pay should be regularized, and I believe it can be done.

Senator VANDENBERG. Have you any information as to how this 20 percent labor factor in your dollar cost of production would compare with the labor factor in other industries and other businesses?

Mr. NUNN. Well, most of them run from 20 to 30 percent, I think. That is my observation, from what I know of it.

Senator VANDENBERG. Are all of your employees under this so-called annual wage?

Mr. NUNN. I am glad you asked that because I neglected to explain it.

At the time we put in this plan, every employee was under contract, but the contract provided that new employees would be temporary employees, would be classed as B class members of this organization. The older members would be A class. These new members would not participate in the contract; they would be hired on a temporary basis. They would have seniority rights, but could be laid off, but would have to be called back according to their seniority when they were needed, and they would be on that basis until, by agreement with the management and the class A workers, they were promoted from class B to class A.

About 10 percent of the workers are class B workers now, but even they have not been laid off.

Senator VANDENBERG. That is where you get your elastic?

Mr. NUNN. That is right; but last January when it developed that we did have too many employees and it would seem that the time had come to lay the B workers off, the class A workers asked the management not to lay them off, and so they never have been laid off; they stayed on.

Senator VANDENBERG. We have heard a great deal about the merit rating system under the Wisconsin Unemployment Insurance Act. Have you any comment to offer on that?

Mr. NUNN. I think, like a good many other things that Wisconsin does, it is a pattern that other States should follow.

Senator VANDENBERG. You are in favor of the merit rating system?

Mr. NUNN. Yes; and I agree with Mr. Swope entirely in his remarks on that subject.

Senator VANDENBERG. Do you think of any other tax incentives which might be offered to industry to encourage some of the social-minded objectives that you have been discussing.

Mr. NUNN. Well, in principle, of course, I can't help but feel that they would be good, but in practice I must confess I don't know how it would be done.

Senator VANDENBERG. Well, that is about where we stand on the thing.

Mr. NUNN. Yes; that is the trouble.

I do want to add just this one thing, that it seems to me that one of the great troubles in the past has been that during periods of recovery and rising prices, and increased wage rates, management naturally has been slow to increase wage rates because they realize the difficulty of reducing them when it turns the other way; and when they finally are forced to increase them, and prices have gotten to a point where consumption goes down, that they are again too slow in reducing wage rates, and reducing prices to meet the slackened demand, and that any system that will take care of this thing automatically and tie up the interests of capital and labor, in the business, is constructive—that is what we have found.

We went through 1920 and 1930, where we held up the wage rates long after it was to the interests of the workers for us to hold them up. They would have been better off if we had reduced them so as to have increased the amount of work we could have given them. We thought at that time that we were doing them a service, but we realize now that we were not.

Senator VANDENBERG. Do you think they realized it?

Mr. NUNN. They didn't at the time, but we try to do a good deal of educational work in our plant, and I believe today they do, and now, when the demand lets up we sit down with our workers and talk about reducing prices of our goods, and they know that automatically when we reduce the price of our goods that their share is reduced also, but they also know that it may keep up their annual income because it will increase sales presumably if we reduce prices.

And the same thing—we must be slow about advancing prices because even though that increases their share, if it is going to slow up business it is against their interests. We are thinking now in terms of annual income, and I believe that is what is needed for the worker to think of, annual income more and his wage rate less.

I believe that covers everything that I have to say.

Senator HERRING. Well, thank you, Mr. Nunn, we appreciate your coming here very much.

Mr. F. Eberstadt, president of F. Eberstadt & Co., New York City, investment bankers.

We understand you made quite an investigation in the subject of incentive taxation, particularly as it relates to industrial production and experiences abroad.

Mr. EBERSTADT. I did, Senator, and I took the liberty of preparing a very brief statement which I would be pleased, with your permission, to read to you, and then answer such questions as you care to have me.

Senator HERRING. Proceed in your own way.

STATEMENT OF F. EBERSTADT, PRESIDENT, F. EBERSTADT & CO., NEW YORK CITY, N. Y.

Mr. EBERSTADT. In one of his most famous decisions, the great Chief Justice Marshall said, "The power to tax is the power to destroy." The converse is also true, that the power to tax is the power to create. The incidence of taxation may be such as to retard or completely stop the wheels of industry or, on the other hand, to create and stimulate it. In my opinion, the recession of 1938 was due more to the effects of the undistributed profits tax than to any other single cause. The protective tariff is an example of the opposite effect of taxation.

Incentive taxation is in essence the reverse of the undistributed-profits tax. While the undistributed-profits tax, in one form or another, puts a burden on the manufacturer who desires to improve his plant out of earnings and thus raises, frequently to a prohibitive point, the cost of such improvement, incentive taxation would offer a particular inducement to those industrialists who devote earnings to plant improvement and thus stimulate employment in a productive field.

The term "incentive taxation" is being currently used in many senses. My remarks, however, are addressed to a rather limited field of application of the term inasmuch as it is my particular desire to make the committee a suggestion which I think is reasonable, simple, practical in application, and susceptible readily of embodiment in the next tax revenue statute.

Rather than attempt elaborate definition, I will paraphrase and file as an exhibit with the committee a brief item which I wrote for Printer's Ink magazine a short while ago.

The great questions which give concern to those who reflect on matters of Federal finance are how and when equilibrium is to be restored between income and outgo without severe penalty. In what manner is industry to be speeded up to a point where it will assume the extraordinary burdens which unemployment and relief now place on the Budget? It must be amply clear to all that economy, however important—that is, simple and outright reduction of Federal expenditures—is not likely alone to achieve this result. I submit that the desired result can only be achieved through a speeding up of private enterprise to a point where taxable income increases and private business takes off the Treasury the extraordinary burdens which it has been compelled to carry during the last years. To paraphrase the words of Secretary Morgenthau, "by releasing the driving force of private capital"—before it is too late.

In my opinion there is a sound and simple method of accomplishing a balanced Budget and stimulating a definite uptrend in business. The depression created an emergency of unemployment so serious as fully to justify immediate substantial direct Federal efforts on behalf of the most acute sufferers. The process consisted of the Federal Government obtaining funds through borrowing and taxation which, in turn, were disbursed directly and through a variety of projects, the process being a combination of relief and pump-priming. It was, so to speak, the reverse of ordinary business, and a process which obviously could not and cannot continue.

A permanent recovery lies only in the absorption of the unemployed in the normal channels of business by corporate and private employers, and the stimulation of business to a point where tax receipts become larger though proportionately less onerous.

It is clear that there can be no return to normal business so long as building and heavy industry are inactive. The present Federal tax structure contains elements which place definite obstacles in the way of expenditures for building or other permanent extensions, improvements, and betterments, and to the free flow of capital into enterprise.

The gist of my suggestion is that these obstacles be removed and the tax laws changed so as to create definite incentives for building and the capital goods industries. In a few words, it is suggested that in the impending revision of the tax laws Congress grant credits on the normal and undistributed profits tax to business over a period, say of 5 years, to the extent of X percent of annual profits for amounts spent on building or other permanent improvements, extensions, and betterments, including new and up-to-date equipment, and that like credits be given private individuals, whether such expenditures be for residential or business purposes.

In order to expedite resumption of the capital goods industry and building, it would seem advisable to give the largest credit for work commenced in 1939, reducing the amount of credit by a fixed amount during the subsequent years.

The effect of this would be that the funds in question, instead of being collected as taxes, paid to the Government, and disbursed by way of relief or pump priming, would be put to work directly to stimulate private business. Money collected by way of taxes, so far as the taxpayer is concerned, and to a considerable extent so far as the Government is concerned, is spent and gone and not productive.

To the extent that such funds are diverted into business channels they would be put to productive uses, creating further business and profits, or to improvement of home and living conditions. Thus, as indicated above, there would be an exact reversal of the process of the past whereby funds taken from the taxpayer, in many cases necessitating a restriction of his business, were disbursed unproductively by the Federal Government.

Such funds, under the above suggestion, would be spent by the taxpayer for productive purposes in the direct employment of labor on a permanent basis and would be an important factor in reviving the building and capital goods industries, without which there can be no real prosperity. Thus relief and pump priming would be reduced and automatically tax receipts would increase, permitting a balanced Budget with improving business without the deflationary effect indicated in a straight slicing down of Government expenditures and raising of taxes.

I do not suggest that incentive taxation, as I have outlined it, is in any sense a panacea. I do say, however, that the wheels of industry are still at dead center and that some inducement or incentive is necessary to start them turning. Without desiring to enter a controversial field or to assign blame or credit in any way, it cannot be denied that the industrialist and employer have had a pretty discouraging row to hoe these last years. Likewise there have been many reasons which have made inaction and idleness on the part of both employer and employee the more attractive and safer course. When one contrasts this with the past spirit and history of this country, it hardly seems that we are talking of the same place or the same people. History offers no more tragic spectacle than destitution and idleness in this country, which is still a land of great opportunity and great possibilities, with an eager and ambitious population.

It is obvious that in the long run under the capitalistic system no country can prosper unless there is a gradual increase in wages and other income, accompanied by a gradual reduction in prices of manufactured goods. This can only be accomplished through greater output per man-hour, what the economists call increasing productivity of labor. The route to this lies in putting more efficient machinery; that is, better capital goods, at the disposal of management and labor. Plant must be constantly improved if this objective is to be attained. Unfortunately the picture in the country over the past years shows retrogression instead of advancement. A study made by the American Machinist, one of the McGraw-Hill Publishing Co.'s journals, took count of the metal working equipment of this country rated according to age. The result showed that of 1,345,447 machine tools in use by American industry, 65 percent were over 10 years of age, thus unsuited to conditions existing today. I would like to file that study with the committee, together with certain other data and charts furnished me through the courtesy of McGraw-Hill Publishing Co., Inc., showing the volume of industrial building construction, building permits, the estimated total value of all construction in the United States, and the Engineering News-Record's construction volume chart (filed with the subcommittee). I present these figures to show the tremendous volume of business which lies at the threshold, provided private industry can be induced to go ahead.

No less impressive is the possible volume of business in the public utility field, about which so much has been said of late.

Quite apart from business considerations involved in a stimulation to industry through incentive taxation, the national-defense aspect of the present conditions of our plant and equipment in public utilities should not be left out of consideration. The sums required to accomplish this task from the point of view of national defense alone cannot possibly be allocated from the Federal Budget. The job must be done by the companies themselves, and, I think all will agree, in the national interest, should be done promptly.

I urge strongly consideration of incentive taxation in the form mentioned above so as to make it more attractive and more profitable for industry to go ahead than to stand still or retract; to make it more attractive and more profitable to labor to work than to be on relief.

I urge strongly that without relaxing in any way the fundamental obligations which an awakened social conscience put on the employer, the next revenue statute contain provision whereby it is to the unquestioned advantage of the employer to act in a manner which is at the same time to his advantage, to the advantage of his employees, and to the benefit of the Treasury.

I have no doubt that if Congress will adopt the suggestion outlined above, an important step will have been taken to stimulate business, to reduce unemployment, to cut down the Federal expenditures, and to increase Federal revenue without indulging in anything unduly experimental or which could by any possibility have any retarding or harmful effects on the economy.

Senator VANDENBERG. Now, Mr. Eberstadt, in your formula you suggested that X percentage of annual profits be immunized by this incentive taxation. Have you any idea what percentage X would have to be in order to produce an adequate incentive?

Mr. EBERSTADT. There are two very important considerations in determining the figure, and I shouldn't care to suggest any definite figure without a much more careful study of the actuarial ends of the question from the point of view of revenue production, but I should think it might run as high as 50 percent, say, between 25 and 50 percent. A fairly good measure is the converse of the undistributed-profits tax. That ran as high as 30 percent on the burden side. Possibly the opposite experiment might be tried, trying it at 30 percent, dividing the credit over 5 years, say, 30 percent, 25 percent, 20 percent, 15 percent, and 10 percent, as each year goes along.

Senator VANDENBERG. Under your formula there would be no incentive except if the corporation was making a profit, would there?

Mr. EBERSTADT. No; because normal depreciation ought to take care of the regular building, but one could imagine that in the spring of the year, for example, the corporation would be justified in going ahead on an incentive basis without knowing that disaster was going to overtake it in November. Profits are calculated on the arbitrary 12 months' basis, and a certain incentive would exist there because of expectation, if you will, of profits through the year.

Senator VANDENBERG. Well, if the theory is sound—of course, I completely agree with you—it seems to me that the formula ought to offer some inducement to the corporation which is still in the red and which perhaps can only hope to survive through encouragement of the nature we are discussing?

Mr. EBERSTADT. Well, Senator, far be it from me to suggest anything in opposition to that. On the other hand, as you know better than I, the problem is extremely complex and extremely widespread and full of ramifications and repercussions, and I desire particularly, in the hope of seeing the experiment, if you will, tried, to confine the suggestion to a rather reasonable and limited field. If it operates successfully, experience will offer the guide for expanding its operations. But I think perhaps to make it a bonus system, or, on the other hand, to make it a birch rod, because there have been authorities on incentive taxation who jumped very quickly from the incentive to the good boy to the spanking of the bad boy, and I think that when you get to the point of spanking, the incentive element has pretty well disappeared. So that my suggestion would be, and is, that the effort be confined to a very simple credit on corporate taxes.

Senator VANDENBERG. I share your anxiety to keep the problem simplified because, heaven knows, it is complex when you leave home base, but wouldn't it be true that if the formula were as limited as yours is, that the net result would be to make the rich richer, and the poor poorer—that is, the corporations?

Mr. EBERSTADT. I should doubt that. I hadn't thought of it from that point of view and I can't answer at once. On the other hand, your employment and your building is coming from those companies that are making money. Whatever inducements you hold out to those that are more or less consistent losers or even temporary losers, one cannot expect from them any great contributions to plant expansion and building improvements. However you phrase the act, and whatever its scope may be, your real contributions are coming from those companies that are in the financial position to make the improvements, and have a fair reason for anticipating that they can use them profitably.

Senator VANDENBERG. I think you are probably justified in saying that is the field in which to look for the improvements. I was thinking more of the equity which the Government owes to all of its citizens alike, and I am wondering whether it is justified in confining its incentives to the prosperous, and offering none to those who have got to struggle to be prosperous?

Mr. EBERSTADT. Well, Senator, the opportunities, I assume, would be equal, and if incentive taxation were used as a basis to bolster up tottering enterprises, to take the extreme case, I am rather doubtful as to whether that would work out because, take the marginal situation that survives merely by virtue of the incentive taxation, that is a bonus to that particular company and I hadn't thought of it in that connection. I had thought of it more as the exact reverse, if you will, to the undistributed-profits tax.

We were very much interested in the machine tool business in 1933–34, made a careful study of it, visited very many of the companies, got acquainted with the association and with certain of the companies. We saw the possibility of a substantial upswing in the machine tool heavy industry field, until the law was passed under which the man who retained his earnings and invested it in plant and property was penalized to the extent, possibly, of 30 percent for making that investment. In other words, instead of buying a lathe at list price, if he bought it out of earnings, which is the way business in this country has been built up, he paid, not 100 percent, but 130 percent for that lathe.

Well, it was quite evident that that was the death knell of that business so long as that continued.

Now, I have thought of this as the exact opposite. Where a man is ready to improve his plant, and it is essential that he must, not only to keep the national-defense point of view before us, but from the point of view of increasing the standard of living; it is impossible to raise wages to the extent that they have been raised over the last years, probably should be raised—I am not at all critical of that—unless you can at the same time keep your costs down; rising wages, falling prices on industrial goods.

The only way to make up the slack is through improved installations of a capital nature.

Senator VANDENBERG. Getting back to your formula and the problem we were discussing. Consider the United States Steel Corporation, which proceeds with a complete modernization of its plant out of its accumulated surplus in a year when it is actually operating at a deficit. Take the Pennsylvania Railroad, which electrifies itself at a time when it has no profits.

Don't you think that the same incentive by way of tax compensation should apply in that circumstance as it would if they were actually running at a profit?

Mr. EBERSTADT. As you stated, Senator, it appears to be worthy of thought. I had not considered that phase of the question. It may be that that could be accomplished by a tax credit available over a number of years. Certainly the Steel Corporation hasn't revamped its plants on the expectation of continued bad business, nor has the Pennsylvania electrified its roads on the expectation of a continuance of the present situation—and that might be met by an available credit to be taken any time over a certain number of years.

But that thought just occurs to me at the moment, I haven't considered that very important phase of the subject.

Senator VANDENBERG. Well, it is important, is it not?

Mr. EBERSTADT. Very.

Senator VANDENBERG. Did I understand that you had made some study of this problem abroad, as it has been developed?

Mr. EBERSTADT. Only in a very cursory way. This has been tried in certain European countries, notably Germany, and of course it has gone very much further there. The incentive has even gone to the extent of tax credits for the employment of labor, and while it is difficult to say that the extreme improvement of plant and the extreme uprush of industrial activity is due to one thing any more than anything else, let's say they coincided, you had so many other factors in that situation, a tremendous demand for munitions, that it is awfully difficult to say that it was one particular thing. But it was used with that in view.

Senator VANDENBERG. The incentive taxes you are speaking of in Germany preceded the era of the dictatorship, did they not?

Mr. EBERSTADT. No; they were just at the outset, the ones I am talking about came along in 1932 and 1933, just at the beginning of the upswing, before what I might characterize as the violent stages. They were more or less in the experimental stages of the dictatorship.

Senator HERRING. The practical repeal of the undistributed-profits tax was a step toward accomplishing what you have in mind, wasn't it?

Mr. EBERSTADT. Yes; as far as it went.

Senator HERRING. Then you believe that through subsidy or incentive taxation, industry should be encouraged to build plant improvements and extend their plant?

Mr. EBERSTADT. I hesitate to use the word "subsidy." I have so much confidence in the independent power of industry going ahead that I think the word "subsidy" is a little bit——

Senator HERRING (interposing). You don't consider it as incentive taxation?

Mr. EBERSTADT. I wouldn't consider that a subsidy.

Senator HERRING. I am wondering what we are going to do with the increased products when we get these plants all doubled up, who is going to buy them?

Mr. EBERSTADT. I don't think there is the least problem along those lines.

Senator HERRING. There is no shortage today, is there?

Mr. EBERSTADT. Very great indeed. Are you talking of the housing field, Senator?

Senator HERRING. Well, you know how that has been encouraged, of course.

Mr. EBERSTADT. You asked me if there is a shortage. I say that there is a perfectly tremendous shortage.

Senator HERRING. There is a shortage of buying power as well.

Mr. EBERSTADT. Not in my opinion, because the credit facilities are greater than this country has ever known. There is no shortage of demand and there is no shortage of need.

Senator HERRING. Why don't they buy?

Mr. EBERSTADT. They are timid, there is a lack of incentive, shall I say, buying incentive, incentive to go ahead. You have a population that, 10 years ago, was proud of everything in connection with our industry. Our plants were in condition, a condition which was regarded as the model for the world. Our industry was confident and you used to hear the word "idealism" used. I don't hear that used so much any more. It used to be that the simplest kind of an industrialist thought himself an idealist, a man with a great incentive. It is sort of unfortunate to see that gone. I say that it is gone only on the surface. If given some incentive, not an impoverished thing, I didn't mean subsidy, give him a return for his efforts, not a hand-out.

Senator HERRING. Of course, I am thinking more of the ultimate consumer, and his ability to pay.

Mr. EBERSTADT. Yes; I have no doubt of that either. Another reason I suggest is that the ultimate consumer is interested in constantly falling prices. It is impossible to have falling prices under our system of economy in industrial goods unless you improve your plant. Where a worker gets $10 a day, let us say, against $5 a day 10 years ago, it is a very fine thing that he should get it, but it is to his interest that he have at the end of his fingers a tool which will, without greater effort on his part, turn out twice as much product which can be sold to the consumer at half the price. That is my theory.

Senator HERRING. Would you favor incentive taxation to be used in encouraging profit sharing with employees?

Mr. EBERSTADT. Senator, I am not familiar with that field. I will have to be excused from commenting on it because I haven't had experience in that field.

Senator HERRING. That is one of the questions that has been discussed here.

Mr. EBERSTADT. Yes, I know; but I am sorry that I can't reply sensibly to it, and I hesitate to give an opinion.

Senator HERRING. I am not certain that anyone can.

Mr. EBERSTADT. I certainly can't.

Senator VANDENBERG. I am very much obliged to you, Mr. Eberstadt.

Senator HERRING. We will recess until 10 o'clock tomorrow morning.

(Whereupon, at 2:45 p. m., an adjournment was taken until 10 o'clock Tuesday morning, November 29, 1938.)

SURVEY OF EXPERIENCES IN PROFIT SHARING AND POSSIBILITIES OF INCENTIVE TAXATION

TUESDAY, NOVEMBER 29, 1938

UNITED STATES SENATE,
SUBCOMMITTEE OF THE COMMITTEE ON FINANCE,
Washington, D.C.

The committee met, pursuant to adjournment, at 10:10 a. m., in room 312, Senate Office Building, Senator Clyde L. Herring presiding.

Present: Senators Clyde L. Herring (chairman) and Arthur H. Vandenberg.

Senator HERRING. Mr. George T. Trundle, Jr., president, the Trundle Engineering Co., Cleveland, Ohio.

Just proceed with whatever you have to offer, Mr. Trundle.

STATEMENT OF GEORGE T. TRUNDLE, JR., PRESIDENT, THE TRUNDLE ENGINEERING CO., CLEVELAND, OHIO

Mr. TRUNDLE. We are management engineers, consultants, and while we employ only 50 men in our own organization, we do advise management, who employ several thousand people.

We have had, in our organization, a profit-sharing system since 1929. We divide our profits, one-third for the employees, one-third for reserves, and one-third for ownership.

Now that one-third for ownership may not always be paid out in dividends, it may be used for expansion; while the one-third for reserves is set up to insure steady employment and is used during dull periods when men are not on assignment.

Senator VANDENBERG. How is the third to employees divided among the employees themselves?

Mr. TRUNDLE. Percentagewise. It amounts to about 20 percent of their salaries and it is paid monthly. Now we are not sure that the monthly method of distributing profit sharing is correct. Next year we are going to try it quarterly. We find the engineers are inclined to treat that as a part of compensation rather than as additional compensation, and we believe a lump sum of money will be used to better advantage than the monthly rate—and we are advising our clients to follow the same procedure.

We have one client who employs about 800 people. We installed profit sharing there 3 years ago, and they are paying once a year.

Senator VANDENBERG. When you installed that system for the 800 employees, was it on this same three-way split?

Mr. TRUNDLE. No, we set aside 5 percent for capital, 5 percent of the net profits, and then on all profits beyond that, for every $10,000 increase we increased the chief executives' salaries. What I mean by the "chief executives" is those salaried people who are directing the work of that business, such as foremen, salesmanagers and superintendents and treasurers, and those people, keeping their wages, their salaries, down very low.

Then we have a junior executive group which participates, and then the workers as a whole. That amounts to about 12 percent for the workers in the shop, or 1 month's pay; and about 20 to 25 percent for the junior executive group; and then goes up to around 60 or 70 percent, or 80 percent, for the senior group.

Now that senior group is working for about one-half a normal salary, while those other groups that I speak of are working for full salary or better than they are paying in the community.

We found in all profit-sharing systems that you must not let it be a part of the compensation for anyone other than the chief executives. The workers down the line, or people under $300, must receive full salary.

Senator VANDENBERG. You prefer not to identify this employer with the 800 employees?

Mr. TRUNDLE. I would prefer not to; I don't believe he would like it. I urged them to send in the information and they refused to do it.

We have installed four profit-sharing systems in the last year and they all operated through 1937. In each case we found management very anxious to have a profit-sharing system. We have not been able to adopt a standard way of determining the amount of profit sharing. That is one of the real problems. Some of them want to take 10 percent, some are willing to take up to 25 percent, and some only 5 percent. Any profit sharing to me is very important in stimulating workers. In each case where we have installed profit sharing, whether it was a coincidence or what, I don't know, but I do know that their profits immediately increased, and a satisfied group of employees resulted. That has always happened. Even in 1938 when companies within an industry are off, these people who have profit sharing are considerably ahead of the whole industry. Maybe you cannot give profit sharing credit for it, but I do. I say it has had a lot to do with it, even with the workers in the shop.

So I am enthusiastic about profit sharing, and I find most of our clients want some form of profit sharing. They hardly know just how to proceed with it, but they are seeking counsel and working in that direction.

Senator HERRING. In how many industries have you installed a profit-sharing system?

Mr. TRUNDLE. About 12, now; and the largest number of employees has been 2,000 in any one industry.

We are now installing one in an industry employing 4,000, but that has not worked yet; but we are in hopes to persuade them to make it retroactive for this year. Whether they will or not, I don't know, but we are going to attempt it, and I think probably that will happen.

Senator HERRING. Do you find the same system will apply in most industries, or do you have to have a different system for each business?

Mr. TRUNDLE. We have a system that we feel should be universal, but we are not able to sell it. They bring up some reasons why it is not good, and perhaps rightly so.

Senator VANDENBERG. What is the system you think should be universal?

Mr. TRUNDLE. I feel that you should first set aside an amount of money for ownership. I think that is important. We will say 5 percent, as an illustration. And then for all moneys earned above that, a percentage of it goes to or should go to the employees. Dividing the employees into three groups we think is important. One group is what we call the chief executive group, taking in superintendents and the higher executives; and then the junior group of foremen and office workers or people making, we will say, from $3,000 up to $5,000; and then the group below that.

Senator HERRING. Do you base that upon the pay roll?

Mr. TRUNDLE. Yes; and pay it percentagewise. It is the easiest thing to do. You can take your total pay roll, and if you have got $100,000 to distribute you know what percentage that is of your pay roll, and then there is no question about the proper distribution of it.

Senator HERRING. The higher-paid employee, then, gets a larger share of the profits?

Mr. TRUNDLE. Yes; but is paid the lowest salary commensurate with the work.

We have found this—that the workers in the shop and the foremen and the workers in the office have to be paid the prevailing wage in the community or better.

Now, for instance, this one company that I was talking about—the highest-salaried man in the company is $6,000. I have cut their salaries down to $6,000—one from $25,000 and another from $18,000—to $6,000. They must earn their compensation through profit sharing. At first they didn't like it, but now you couldn't take it away from them, even though this year might be a considerable reduction over what was their normal salary.

Senator HERRING. They get a larger percentage on their salary than the employees then?

Mr. TRUNDLE. That is right. I endeavor to give them as a straight salary about half what that job should pay, and that comes in awfully nice during a depression and when there is no business, because you automatically cut wages. You don't have to go out and say you are going to cut wages; you have automatically done it.

Senator VANDENBERG. Have you given any consideration to the other problem we are discussing, namely, incentive taxation?

Mr. TRUNDLE. Yes.

Senator VANDENBERG. What have you to say about that?

Mr. TRUNDLE. I am very much in favor of it. However, I believe we do get that benefit now because in profit sharing we throw it back into compensation on our books. However, that does not induce other people to follow the same principle. If you have your incentive from a tax standpoint, I am quite confident that most manufacturers and businessmen will go to profit sharing, and wisely so.

Senator VANDENBERG. You haven't any specific suggestion as to how tax rewards should be created and applied, have you?

Mr. TRUNDLE. No, sir; I have not.

Senator HERRING. Those profits that you share in that way, of course, are treated as an expense, aren't they, in the business?

Mr. TRUNDLE. That is right; but an expense only if they are earned. It is not an obligation until they are earned, so that puts a very different view from an operating standpoint in the forecasting of what you are going to do in a business.

Senator HERRING. Do you have anything else, Mr. Trundle, that you would like to add?

Mr. TRUNDLE. No; I have nothing further that I can add. My experience has been that it does create a much better feeling with the workers, and they make every effort to put in economies and eliminate waste.

As an illustration I saw a sweeper pick up a piece of steel that big [indicating sheet of paper] that was thrown in a scrap barrel. He came to the superintendent and said, "You are throwing that piece of steel away; we should use it; that is part of our profits." Now when you can get workers to feel that way about it, it is really accomplishing something.

I find today—and have always found all my life—that you have got to take workers and your employees into your confidence and assure them that you are doing the best you can and you need their help, and then you can be assured of their cooperation.

Senator HERRING. Well, do you advise these clients of yours that they arrive at this through negotiation with the employees, or do you give them a definite plan and let them follow it?

Mr. TRUNDLE. In several cases we have discussed it with the employees; in others, we have not, we have just told them about it. We have found that the employees are rather at a loss when you go to them for help in working out such a plan. I find when you go to them with a plan, if that plan is sound, they will follow it very closely and add to it as you go along, and of course that is exactly what we want.

Senator HERRING. Do many of these plants employ organized labor?

Mr. TRUNDLE. There is one that has absolutely no union; the rest of the plants either have one of the organized unions or company unions, and it never makes any difference to me which it is because they are all reasonable.

Senator HERRING. Do you think you could apply this with collective bargaining?

Mr. TRUNDLE. Absolutely, I think it is one of the best tools we have. I am heartily in favor of that.

Senator HERRING. Well, your experience is, then, that it aids efficiency and lowers cost, increases profits, and does away with labor trouble?

Mr. TRUNDLE. That is right, that is right.

Senator HERRING. I don't see how you can ask for more than that.

Mr. TRUNDLE. Give me that and I will take my chances with labor troubles, because we don't have any anyway.

I was called in on a job yesterday, 80 miles out of Cleveland. The company union had made a demand. I looked at it. The management was all excited. I said, "Bring the group in." When they came in I said, "You can have what you want, you have demanded it and you can have it, but unless you will take steps to eliminate some of the waste that we know exists here we must naturally expect our prices to increase and therefore make us noncompetitive, and we must compete in order to stay in business."

The spokesman for the group, who was quite a radical, said, "Come on out and show us how to do it."

Senator HERRING. That was a company union?

Mr. TRUNDLE. Yes; a company union, but engineered from the outside I am sure, because I doubt if any group of employees with no experience with a union could have drawn up the demands in the form they were drawn up.

Frankly, I am not afraid of high wages; they have never bothered me at all, for wages usually only represent 17 cents on the sales dollar, and that is a small amount.

Senator HERRING. Seventeen cents?

Mr. TRUNDLE. About 17 cents—and that is a small amount to battle with.

Senator HERRING. Well, thank you very much, Mr. Trundle. We appreciate your having come and given us the benefit of your experience.

Mr. J. R. Ramsey, general manager of S. C. Johnson & Son, Inc., Racine, Wis.—better known as the Johnson Wax Co.

We understand you have some rather unique policies up there. At any rate you have been able to get along with competition that has put some of the others out of business.

Mr. RAMSEY. Not exactly; I think we have two or three thousand competitors left, but we are reasonably successful in the way of harmony.

STATEMENT OF J. R. RAMSEY, GENERAL MANAGER, S. C. JOHNSON & SON, INC., RACINE, WIS.

Mr. RAMSEY. I think possibly I could tell you about it best in a sort of historical way.

The firm is 52 years old. It was founded by S. C. Johnson, for whom it is named. He carried on for many years and then his son, Herbert, came in and when he died the grandson of the founder, the present H. F. Johnson, Jr., took it over 10 years ago, and they inaugurated these policies as a sort of human growth. Therefore, if I use the word "we" I can do it without blushing as it goes back to these people.

They always did that fundamental thing of paying good proper wages, and they always furnished their employees with security; that is, no lay-offs in dull seasons, and no big gangs taken on in peak seasons.

The more formal employee benefits began—well, such things as vacations with pay—back beyond our memory. I couldn't find anybody in the office who remembered when they didn't have any vacation.

About the first really formal gesture was in 1917, when they started paying a profit-sharing bonus, and that has been paid ever since then, every year that we made a profit. There were two unfortunate years, 1931 and 1932, when we skipped it, but otherwise it has been a continuous proposition.

The next thing that came along was in 1922 when they formed a mutual benefit association, to which the employees contributed half and the firm one-half. That took over the rather commonplace benefits of sick benefits, hospitalization, insurance, and the usual smaller chores.

Then in 1934, we put in a formal pension system. So the set-up now consists of three major elements, this mutual benefit association taking care of all the mine-run of doctors' bills, hospitals, sick benefits, and the miscellaneous sports, recreations, bands, and that sort of thing.

The pension plan takes care of future security, the men to retire at age 65 and the women at age 60, with a pension equal to 1½ percent of their annual earnings since the plan started in 1934, and in addition a past-service benefit of 1 percent of their earnings prior to 1934. That pension plan is also mutual, the same as their benefit association, insofar as services from 1934 on are concerned. For those past services the company is paying entirely.

The third thing is the profit-sharing bonus, which is paid the day before Christmas and which is quite a sizeable amount. Last Christmas there was $202,000 distributed to about 800 employees.

The J. M. B. A. and the pension plan are very, very definite things on which they can count, this benefit association for the current things, and the pension plan for the future.

The profit sharing depends upon the "ups" and "downs" of business; as to which is the most important, I don't believe I could say. It seems to me that all of those elements are necessary, that they all fill a certain need, and they coordinate with each other and have worked out our problem very successfully.

I think I could probably tell you more in the line of what you want to know if you have any questions you would like to ask about any of them.

Senator VANDENBERG. Well, I would like to go into a little more detail at the moment about the third factor, namely, the profit-sharing bonus. You said that $202,000 was distributed to 800 employees. Upon what basis was the $202,000 figured—how did it happen to be $202,000?

Mr. RAMSEY. Based upon three things—the earnings of the individual, the number of years he had been with the company, and his position in the company. There is a very definite schedule, starting at the end of 1 year of employment, 5 percent and 6 percent, depending upon the position.

A salesman, for example, would get 5 percent——

Senator VANDENBERG (interposing). You mean of his annual wage?

Mr. RAMSEY. Of his annual earnings. Office employers start at 6 percent. Then those percentages increase up to 10 years. After 10 years' service they remain the same. The maximums then range from 15 to 35 percent, depending upon the position of the employee in the company.

Senator VANDENBERG. Are those percentages fixed percentages regardless of the relative earnings of the company for the year?

Mr. RAMSEY. They are fixed for the time being, but the board of directors could change them in any year they so desired when earnings went up or down. For instance, in those bad years of 1931 and 1932 we couldn't pay anything. In one year we paid just half of the theoretical amount. If we make more than we are counting on at the moment, I suppose more might be paid. That is something decided by the board of directors each year. That system is merely a basic plan.

Senator VANDENBERG. In other words, there is no continuity in the formula itself except that a formula is going to be used?

Mr. RAMSEY. Except a formula as a basis for comparative fairness for all concerned.

On that point of continuity it might interest you to know that maybe one of the best things that ever happened was the 2 years when we didn't make any money and couldn't pay it. Everyone, including myself, I guess, had gotten in the habit of counting on it every year, and maybe bought a new car when we shouldn't, and one thing or another. And these 2 years without a bonus sort of brought the bonus quite forcibly to our minds that it was a profit-sharing proposition.

Senator VANDENBERG. Are all employees who have been with you 1 year or more included?

Mr. RAMSEY. All employees who have been there 1 year or more are included in that basic formula. Then those that have been there 6 months or less than 6 months get a flat payment of some sort, ranging from 10 to 50 dollars.

Senator VANDENBERG. Is there any explanation to the employee in dollars and cents to demonstrate to him why it was $202,000 that was to be divided this particular year?

Mr. RAMSEY. No, sir; that hasn't been done. Possibly the thought behind that goes back to the same thing that I just explained. Maybe the idea is that it is not too good to count on it exactly.

If you have the fundamental things of good pay, pay above average for all positions, and a sense of security in your job, this third thing psychologically may just as well be variable.

Senator VANDENBERG. I wasn't thinking so much about the variability of it as I was that an employee might wonder why it was $202,000 that was divided, instead of $252,000. Was there some explanation made to justify that particular figure?

Mr. RAMSEY. There hasn't been thus far, although it has been explained to them in relation to company profits. For instance, they know that it was more than was paid out to the owners in dividends. It was around 23 percent of the net profit before taxes.

Senator HERRING. Twenty-three percent of the total profits was distributed to the employees?

Mr. RAMSEY. Of the net profits before taxes.

Senator HERRING. You would distribute 23 percent?

Mr. RAMSEY. That is what it came to last year, in round figures, even before taxes. In simple sums, not the net figures on our balance sheet, suppose in actual operation we made $110. We paid out about $30 of that in taxes, leaving $80. Then we spent about $30 in sharing it with employees, that is this bonus plus those other benefits. That left $50. The owners got $20 in dividends, which left $30 to be plowed back into the business. It went about in that ratio.

Senator VANDENBERG. What is the net result of this combination of helpful relationships? Has it brought you industrial efficiency and industrial peace to a greater degree than you would have had without them?

Mr. RAMSEY. That is kind of hard to answer. You asked about that in your questionnaire and there just isn't any "before" and "after" picture, because the thing has always taken place and there has never been any trouble.

Senator VANDENBERG. You have never had any trouble whatever?

Mr. RAMSEY. Literally never.

Senator VANDENBERG. At least you can compare yourself with some who have had trouble.

Mr. RAMSEY. I don't like to do that. They will just get mad at us and think we are putting ourselves up on a pedestal.

Senator VANDENBERG. That would bear on the question as to whether or not there was any direct utility in these factors?

Mr. RAMSEY. There evidently is. You can't expect 800 human beings to go around waving flags and saying, "Yes, we are all enthusiastic," and use some of the nice words that were in your questionnaire. The best result, you see, is a negative result in that there is never any trouble, and I am certain that everyone is satisfied within the bounds of every-day human nature.

Senator HERRING. Your labor isn't organized, is it?

Mr. RAMSEY. No, sir.

Senator HERRING. Do you have anything else you think you might suggest, Mr. Ramsey?

Mr. RAMSEY. Our company is comparatively small and I know that what we may say may not fit the big companies, the biggest outfits in the country, but I do want to say that the flexibility of having three plans, and incidentally of having each of those plans flexible in themselves, is a more workable proposition than sitting down and fixing an iron-clad thing that you are going through with for 20 years.

Conditions change, and you are dealing with human nature, and you just can't set it down definitely.

In the bonus plan for example, we have 10 classes, as carefully outlined as we possibly could figure out. Then we have class No. 11, which is called "special." Mary Smith is not quite in this or that regular class, and it is left to the discretion of the president or general manager to adjust her in class No. 11.

And in the mutual benefit association, which is run by a board of directors, of whom four are elected by employees, two appointed by management, and one by the sales department to represent the outsiders, they change their bylaws. They have their rules but they have a meeting and decide that Ole So-and-So did have awfully hard luck and although we paid him his normal maximum 200 days' sick benefit, we will carry him on for another couple of months. They are all flexible and they are all human.

Or, take salesmen, under the pension plan—we ran along for a couple of years and found that a salesman can't work hot-foot until he is 65; his legs won't last even if his head does. And a salesman can't retire back to running an elevator, like a factory man can, or as an office person can go on to just detail work. So we modified that one day. If a salesman wears out at 45, 50, or 55, instead of giving him what he would normally get, his own contribution plus 3 percent compound interest, we throw in what the company contributed, too. So that salesmen who have left in the last year and a half have enjoyed the full benefit of the pension plan as far as it was built up to that time.

Senator VANDENBERG. What is the total amount expended by the company for all three of these plans?

Mr. RAMSEY. I figured up pension and J. M. B. A. contributions and some miscellaneous things, vacation pay—we even pay for holidays, Christmas, Fourth of July, and so forth—and it was $118,000, which plus the $202,000 bonus, made $320,000 for the year 1937.

Senator VANDENBERG. What relationship would that $320,000 bear to the profits of the company, in percentage?

Mr. RAMSEY. I figured it out after taxes, which isn't fair. That is around 60 percent. Let me figure it back. These round figures that I gave you before are the easiest to keep in mind. We made $110 total in operating profit, and paid out $30 in taxes—$30 to employees first, then $30 in taxes, and then $20 in dividends to the owners, and then $30 added to surplus which is plowed back into the business.

Senator VANDENBERG. Well, it is somewhere around 60 percent, I should think.

Mr. RAMSEY. After taxes, it is over 60 percent. On later consideration I decided that wasn't quite a fair way to figure it.

Senator VANDENBERG. You are familiar, of course, with the Wisconsin unemployment insurance law?

Mr. RAMSEY. Yes, sir.

Senator VANDENBERG. What have you got to say about merit rating, pro or con?

Mr. RAMSEY. Pro, I guess—not a very considered opinion because we haven't, as you can imagine, had a great deal to do with the law except building up the required surplus. If you reach 7½ percent of your pay roll you drop down to 1 percent contribution, and if you reach 10 percent, you cease contribution—and that has been about our only thought given to the law. Not hiring and firing a great many people, we don't have that problem to any great extent.

Senator HERRING. Have you any thoughts as to incentive taxation, Mr. Ramsey, as to whether it would be helpful or not?

Mr. RAMSEY. I have very definite opinions; yes. I might even call them prejudices, but they are certainly definite opinions. I think tax incentives toward two things would be excellent, toward continuity of employment and toward profit sharing.

I am naturally selfish in one way. If we are going to give that $30 out of the $110 to employees, that makes our goods cost that much more, and somebody down the street, one of these thousands of competitors, will hire some girls for $15 a week, and slap out some stuff which makes it a little more difficult for us to sell our product. And it seems to me inequitable that we should be penalized for it. Evidently some of the taxes we are paying are going to help underpaid people or people who are laid off. In the long run they must. Hence I think it would be very just and fair to put up some sort of incentive for both of those things that we are doing, profit sharing and assurance of continuity of employment.

I realize that there are some practical details in the way of it, but I think a reasonably simple formula could be propounded and could be tried for a year. You would run into some bugs in it, but no more than in the undistributed profits or any other tax law.

The percentage probably wouldn't mean an awful lot in a monetary way, but its psychological benefit would be wonderful. You have tried all sorts of laws to make us behave. I say "us," but I mean all employers. And they worked to a certain extent. But you can catch more flies with molasses than you can with vinegar, and I should like to see the other type of law or incentive tried for a change.

For example, if you allowed us to calculate our income return in a regular way, and there was some special allowance for these profit-sharing devices, take that $300,000, supposing you said, "Well, you can take a special deduction of 50 percent of that, or $150,000," that would really mean about 16 percent of that saved in taxes, wouldn't it? It wouldn't be an awful lot of money, but even if you chiseled that percentage down to where it didn't amount to many thousands, there would still be the psychological incentive and some feeling of—well, "they realize we are trying to be decent and they are giving us a little break." I think the psychological benefit would be even greater than the monetary benefit.

Senator VANDENBERG. Would that be equally true, in your judgment, if incentive tax credits were given for plant expansion and for equipment replacement, and so forth?

Mr. RAMSEY. Yes; but to a lesser degree. This profit sharing proposition is a voluntary giving away of your assets. If you are just putting them back into your plant, you are doing good, yes, in providing labor, in buying the materials and all that—but you still own the result. We have, however, felt the inequity of the present tax law very strongly in the last couple of years in building a new office building designed by Frank Lloyd Wright, and if you know Mr. Wright you know it costs a few more pennies than we started out to spend—and we have felt rather badly about the Government penalizing us for wanting to save up profits to pay for that. But we haven't crabbed to any great extent because the law has been very sensibly modified.

Senator HERRING. Unless you have something else, Mr. Ramsey, I think that is all.

Mr. RAMSEY. I can't think of anything else except to reiterate very strongly my belief in, and favor of, some tax incentive toward two things, profit sharing and continuity of employment.

Senator HERRING. I think you have made a very fine distinction there, too.

Thank you very much, Mr. Ramsey.

We had expected to have Mr. Babcock, the treasurer of the Endicott-Johnson Shoe Co., here this morning, but due to some causes that came up suddenly, he isn't here and won't be here today.

Tomorrow we will have Mr. Moss, the president of the American Sash & Door Co., of Kansas City, Mo.; Mr. Kennedy, the vice president of Cluett, Peabody & Co., of Troy, N. Y.; Mr. John L. Lewis, president of the United Mine Workers of America; and Mr. Walter Goodspeed, vice president, American Box Board Co., Grand Rapids, Mich.

Because of the inability of Mr. Babcock to get here today we will be compelled to adjourn now until 10 o'clock tomorrow morning, at which time we will resume with the hearings.

(Whereupon, at 10:50 a. m. an adjournment was taken until 10 o'clock, Wednesday morning, November 30, 1938.)

SURVEY OF EXPERIENCES IN PROFIT SHARING AND POSSIBILITIES OF INCENTIVE TAXATION

WEDNESDAY, NOVEMBER 30, 1938

UNITED STATES SENATE,
SUBCOMMITTEE OF THE COMMITTEE ON FINANCE,
Washington, D. C.

The committee met, pursuant to adjournment, at 10 a. m., in room 312, Senate Office Building, Senator Clyde L. Herring presiding.

Present: Senators Clyde L. Herring (chairman) and Arthur H. Vandenberg.

Senator HERRING. This is F. J. Moss, president, American Sash & Door Co., Kansas City, Mo.

STATEMENT OF F. J. MOSS, PRESIDENT, AMERICAN SASH & DOOR CO., KANSAS CITY, MO.

Senator HERRING. Mr. Moss, will you just give us a brief history of your business, when it was commenced, when you inaugurated this profit-sharing plan, and what your experience has been?

Mr. MOSS. We commenced our profit-sharing plan in 1919, and it has been continued up to this date. I might state that for the first 10 years we had profits to share, but for the past 9 years, as you are aware, the building business has been perhaps more depressed than any other line, the building and lumber business generally, so that there have been no profits to divide in the past 9 years. In spite of that fact there has been no expression of dissatisfaction on the part of our employees. They seem to understand and are just awaiting better times.

Senator VANDENBERG. How many employees do you have, Mr. Moss?

Mr. MOSS. Normally, 350.

Senator HERRING. They have access to the balance sheets and know exactly what the company is doing?

Mr. MOSS. Yes.

Senator HERRING. Is that one of the reasons why you have had no expression of dissatisfaction?

Mr. MOSS. We have our books audited by public accountants every year, and we pass out the report on the result of the past year's operation.

Senator HERRING. I think that might have quite a good deal to do with their being content under the circumstances. They realize you are not making money, and they believe you are telling the truth about it.

Mr. Moss. As far as we can determine, I would say 95 percent of them are entirely satisfied. Of course, out of an organization of 300 to 350 men there will always be a few discontents, but it is not enough to disturb the situation at all.

Senator VANDENBERG. Well, I suggest that you proceed with an explanation of the way your plan operates, Mr. Moss, the formula upon which you proceed.

Mr. Moss. I would first like to proceed to state what I had in mind when this plan was formulated, and then I will give you just a very brief outline of the plan itself.

I feel that we are dealing with a tremendous problem, one that has caused more disturbance in the last 100 or 200 years, perhaps, than anything else. I have very definite ideas as to the rights of capital and human beings. It might better be placed the other way, a human being versus capital. I approached the problem feeling that anything that might be accomplished, that was worthy, would affect millions of workers. Anything that will contribute to their contentment, to a feeling that they are getting that to which they are justly entitled, and then some direct returns in addition to the regular salary, would go far toward bringing about peace in the industrial world. In my opinion, we will never have industrial peace until some plan of fair distribution of capital growing out of business is arrived at. It cannot be brought about, in my judgment, by voluntary action on the part of capital or labor, or both of them, in the absence of some incentive, for the reason that we have men who are selfish and men who are inherently opposed to any kind of a profit plan. For that reason I have felt that we cannot make general progress in this sort of work unless we can enlist the support of many reputable concerns, preferably of course a large percent, and I think that can only be brought about by a measure of incentive offered by the Government in the way of abatement of an onerous income tax. That will effect a wide and fair distribution of capital among employees, and I hope my plan will prove to be fair and just.

Now, when we deal with capital, in considering this matter, we are dealing with billions, and I feel that we should keep in mind that anything that injures capital or labor will injure both. It cannot be otherwise. I feel that we must remove this cloud that has been placed on capital by reason of false propaganda.

For instance, in that period from 1931 to 1936 corporations in this country paid into the Treasury some $18,000,000,000 in taxes. Their total net earnings were only a little over $9,0000,000,000; the net result being the confiscation of about $9,000,000,000 of capital. And all the time that this was going on, capital was being lambasted from hell to Sheba as robbing the public, right at the very time that they were losing money by the millions. That, of course, was brought about by an effort on the part of the demigods to appeal to the voters, to get the elections. That has been indulged in by both parties. I am not speaking from the partisan standpoint at all, because one is as guilty as the other, as far as I know.

Senator VANDENBERG. Not quite.

Senator HERRING. I agree, not quite.

Mr. Moss. I mean some of them, some of each are as guilty as the other. So it must be our aim, it seems to me, to strive for more fair and square dealings in business and cry down the man that is crying down everything that is constructive.

Senator VANDENBERG. I would like to interrupt you just for a moment, Mr. Moss, to sustain your thesis with a figure that Senator Tydings offered in the Senate one day, because I think it is pertinent. He pointed out from the records of the Department of Commerce that America's business in the 8 years succeeding 1929 paid out $23,000,000,000 more than it took in. That was American business' voluntary contribution, by the way, in an effort to help meet the economic crisis. So that business is not always a robber, a horse thief, or a pirate.

Mr. MOSS. Those figures are about correct. While they differ from my own, you notice I dealt only with corporations, and he deals with all American business. That accounts for the difference between the two.

Senator VANDENBERG. Yes.

Mr. MOSS. Unfortunately, during that period when business was going in the red and that propaganda was being spread, people believed it, they thought perhaps that was true. They did not get at the fact. I think they are now beginning to be awakened, but there is a feeling, which is very general, that the corporations were robbing the public.

Now, of course, that was directed largely against the large concerns, although in the statement it was stated broadly business.

Now, I would not want to be understood as defending the actions of some of the corporations, the large corporations. I think we have bad members there, just as we have in churches.

Senator VANDENBERG. And in Congress.

Mr. MOSS. Oh, yes; I forgot to mention the Congress. I have, in the last 50 years that I have been in business, dealt with a good many thousand concerns, and I want to say that so far as the morals of the businessmen of this country are concerned, if the truth is known they need no further defense. I feel that I speak authoritatively when I say that American businessmen, by and large, perhaps 95 percent of them, are on the square. They conduct their business on the square, and as soon as we can get that message across to the people, the better it would be for all concerned.

Now, as to the suggestions I have to offer bearing upon the question of distribution of capital or earnings from business, I will read, if I may, from the memorandum that I dictated before I left my office.

The profit-sharing plan submitted herewith is predicated upon the fact that in the last analysis there are but two factors of cost in any product, or in the conduct of any business. One is invested capital, including surplus, which remains permanently in the business and the other is labor, including salaries, which is withdrawn as earned.

The plan contemplates that of a year's profits from the operation of a business there shall be first set aside 6 percent—I will wish to discuss that percent business a little bit later, if I may—upon the capital actually invested in the business, and that of the remainder of the profits, in excess of the 6 percent so reserved, a division should be made between capital and labor in the proportion that each relates to the cost of the operation.

CAPITAL

Capital is real estate, buildings, machinery, merchandise, and funds necessary for the proper conduct of the business; in fact, everything with the exception of labor necessary for the operation.

LABOR

Labor is the factor supplied as the result of human effort, whether mental or physical, and the plan implies that each worker should receive returns in the exact degree that his effort and qualifications contribute to the success of the business. There can be no more practical measure thereof than the amount of his wages or salary.

Thus it is the relation that the sum total of wages including salaries paid during the years bears to invested capital that determines the participation of each; i. e., if the total capital employed should be $150,000 and the total wages including salaries should be $50,000, then it follows that capital should first receive a 6 percent so reserved for it and then because it has supplied three-fourths of the cost, should receive three-fourths of the profit in addition to the amount so reserved. Labor having supplied one-fourth of the cost should receive one-fourth of the profit as adjustment of wages. Thus labor will have received all the profit on what it has put into the business. Under this plan is applied the same yardstick to labor that is applied to capital—so simple that a 14-year old boy can understand. Coupled with this division of profits there follows an abatement or lowering of income tax for the year in an amount equal to the wage adjustment paid to labor in accordance with the foregoing described proportions.

OBJECTIVES

1. An equitable distribution of profits growing out of the operation of the business.
2. Increased production due to mutual interest of labor and capital.
3. Less loss growing out of labor disturbances.
4. Reduced cost of production.
5. Increased purchasing power of those participating.
6. Reduced unemployment due to increased demand and production.

The extent to which a profit-sharing system is put into operation will largely determine its success for the reason that if generally employed, it will have the effect of establishing a standard. The effect on the income tax will operate as an incentive for industrial concerns to adopt the plan.

It is fully appreciated that the Government needs the money and could hardly afford to sponsor any plan the effect of which would be to lower taxes. It is, however, quite doubtful if the final result would be to materially reduce Government revenue as under this plan with the principal stockholders of a corporation, having in many instances large income from other sources, sharing in the profit on the salaries they may be drawing, the effect would be to raise their incomes to a higher bracket and the Government would realize a larger amount of revenue from their income tax than it would realize in the 19 percent on the corporation's earnings plus an indefinite amount from the individual taxpayer on its dividends. There would also be the increase in the income taxes of other employees and over and above all it would mean an impetus to business as set forth under the objectives mentioned above.

Note attached examples of the typical working out with various size corporations.

Here I have six or eight examples of the result as it affects labor and capital in various corporations.

Senator HERRING. That may be inserted in the record.

Mr. Moss. That will go into the record for your examination.

(The matter referred to is as follows:)

Examples

1. To illustrate results of a relatively small concern's operations in good year:

Capital and surplus	$50,000
Pay roll qualified to share profits	15,000
Net earnings before distribution of profits	8,000
Owner's 6 percent on capital and surplus	3,000
Amount distributed between ownership and employees	5,000
7.69 percent on $50,000 to owners	3,846
7.69 percent on $15,000 to employees	1,154

2. To illustrate results of medium-size concerns' operation in only a fair year:

Capital and surplus	$500,000.00
Pay roll qualified to share profits	200,000.00
Net earnings before distribution of profits	50,000.00
Owner's 6 percent on capital and surplus	30,000.00
Amount distributed between ownership and employees	20,000.00
2$\frac{6}{7}$ percent on $500,000 to owners	14,285.72
2$\frac{6}{7}$ percent on $200,000 to employees	5,714.28

3. To illustrate results of medium-size concerns' operation in good year:

Capital and surplus	$500,000.00
Pay roll qualified to share profits	225,000.00
Net earnings before distribution of profits	75,000.00
Owner's 6 percent on capital and surplus	30,000.00
Amount distributable between ownership and employees	45,000.00
6.2 percent on $500,000 to owners	31,034.43
6.2 percent on $225,000 to employees	13,965.57

4. To illustrate results of contracting concerns of small capital and extensive profitable volume:

Capital and surplus	$25,000
Pay roll qualified to share profits	250,000
Net earnings before distribution of profits	15,250
Owner's 6 percent on capital and surplus	1,500
Amount distributable between ownership and employees	13,750
5 percent on $25,000 to owners	1,250
5 percent on $250,000 to employees	12,500

Mr. Moss. That, in substance, is the plan under which we have been operating in every detail, except the suggested governmental participation, the abatement.

Senator VANDENBERG. Would you say, Mr. Moss, in your own experience, as the result of the use of this formula, that you had reached most of the objectives?

Mr. MOSS. We are confident it has had that effect, but as I have stated before, we will never get the full force of a profit-sharing plan until it has been established so as to satisfy the employees themselves that they are getting their just dues.

Senator VANDENBERG. That is absolutely so.

Senator HERRING. You have accomplished that through your plan, you feel?

Mr. MOSS. We certainly have.

Senator HERRING. You have not had any labor trouble?

Mr. MOSS. Not any labor trouble whatever.

Senator VANDENBERG. In spite of the fact that you have had no profits to share for 9 years?

Mr. MOSS. Yes, sir.

Senator VANDENBERG. Which is a rather remarkable tribute to your operations.

Mr. MOSS. Of course, I might state in that connection that one thing that has operated to save us from that sort of trouble has been the general knowledge of the complete cessation of building operations. Our business at one time went down to 10 percent of normal business, in 1933.

Senator HERRING. The wages you pay, not considering the sharing of profits, are equal to those paid by your competitors?

Mr. MOSS. They are, and must of necessity be, otherwise we could not get the workers; and not only that, we know that we are getting the first pick of labor because of the profit-sharing plan. Were it not for that we would feel we could not continue sharing profits even in good years; we would have to average it up, don't you see.

Senator HERRING. Have you given any thought to the suggestion of incentive taxation or compensatory tax benefits to those who are sharing profits?

Mr. MOSS. Yes. That is what I was suggesting here. I would suggest that of the profits distributed to the employees, the corporation's income tax would be abated in that amount.

Now, as I suggested earlier in the discussion, I want to make a few remarks bearing upon the interest rate of 6 percent, suggested in my notes. Of course, that is high as compared with the going rate at the present time, but it must be borne in mind that capital invested in an industry assumes all of the risks growing out of the depreciation of property or the change of conditions, growing out of a shift of source of supply, or any one of a hundred different causes, resulting in a shrinkage of property values, as I stated, which all goes out of capital. Of course, there has been an abnormal shrinkage, we are all aware of that. So that the investment on a 6-percent basis I think is fair, when you take into account the risks that is involved in tying up a lot of money in bricks, mortar, and real estate that might at any time become materially lower. I am offered literally hundreds of industrial plants at a mere fraction of their cost all over the country.

Senator HERRING. You are not familiar with this interest charge uniformly to be charged out before there is profit sharing?

Mr. MOSS. Only in this respect: As has been the case in the last few years, no profits have been made, there have been only losses. If no profit has been made, why, no interest on invested capital could be paid, and it should be carried over into the next year's profits.

Senator HERRING. That would be deducted in addition to the next year's interest before the employees would share?

Mr. MOSS. Yes. In other words, to average up the 6-percent investment on capital.

Senator HERRING. If you have nothing else you would like to suggest, I think you have given us a very fine presentation, Mr. Moss. Thank you. We will next hear from R. O. Kennedy, vice president, Cluett, Peabody & Co., Inc., Troy, N. Y.

STATEMENT OF R. O. KENNEDY, VICE PRESIDENT, CLUETT, PEABODY & CO., INC., TROY, N. Y.

Senator HERRING. Mr. Kennedy, would you give us a brief history of your company since the inception of the plan that you have in operation, and your experience with it?

Mr. KENNEDY. Mr. Senator, we have no definite profit-sharing plan, as it is formally known as such, but I am here today as the result of the formation of a plan based upon my concept of the objective of the committee. It is a very simple plan, and perhaps my concept is very simple too, but it is so simple that I have been able to put it on these three pages, and I am going to ask Mr. Walsh, if he will, to present that to you, and at the same time I would like to submit copies to you so you may be able to follow him.

Senator HERRING. Will you read it, Mr. Walsh?

(The plan presented by Mr. Kennedy is as follows:)

A SUGGESTION FOR CREATING AN INCENTIVE FOR INCREASING EMPLOYEE PARTICIPATION IN THE PROFITS OF BUSINESS

To stimulate the distribution of revenue from business by means of incentive taxation through reduction of income tax rather than by means of punitive taxation through increased income tax.

To direct such distribution into the lower-bracket incomes of the workers rather than into the higher-bracket incomes of the stockholders.

To assure business of governmental cooperation in its efforts to make a profit so essential for carrying on the business from year to year and thus providing employment.

It seems at first that such a distribution would deprive the Government of some tax income derived from taxation on the higher brackets of the stockholders. However, this thought is soon dissipated when one considers that the stockholders in the higher brackets are few in number and that such income is often frozen. In other words, is not put into circulation by purchasing that which would provide work for others and thus increase the revenue of business.

A further commendation of the general plan is the social service rendered through an impetus for the greater distribution of the revenue of business to those who need it most.

Broadly, the proposed plan is one to reward business for sharing to a greater extent with the employees the profits of business. Obviously, this cannot be confined to those few companies which have formal profit-sharing plans. If so, it would be possible for a company to pay mediocre wages and at the end of a year provide for a credit by a distribution, while another company with no profit-sharing plan might make a larger proportional distribution of its revenue through a higher wage scale throughout the year.

This presents the need of a plan that will provide an incentive for an increased participation by the employees in the revenue for the year.

It would be unfair to set this up on a basis of a reward in a reduction of income tax based on an excess of wage distribution over an arbitrarily fixed ratio covering all industries.

An industry such as the garment industry may have a high ratio of wages, while the paper industry, because of its automatic machinery, may have a low ratio, but it would be practicable to set up such incentive rewards based on the ratio of increased distribution in pay roll to the total of pay roll and net profit in excess of the ratio computed for a base period, say, the last 5 years, for any one company.

In computing this ratio it would seem fair to deduct from the net profits 5 percent of the actual investment, as shown by the balance sheet, or on the average of the actual investment throughout the 12 months. This would allow for a fair return on any increase in investment due to expanded facilities or improved equipment.

In computing the increased ratio against the 5 years' base it would seem fair to compute this on either the current year or the average of the last 3 years, whichever is the higher. This would provide an escape from the consequence of some contingency occurring in a single year, such as a temporary loss of market. It would also provide for possible rewards to those companies that already have begun a greater distribution.

	Company A	Company B
Basis, last 5 years:		
Net profit (less 5 percent on investment)	20,000	100,000
Wages	[1] 100,000	[1] 20,000
	120,000	120,000
Ratio of participation:		
	83	16
	120)100000	120)20000
	960	120
	400	800
	360	720
Next year or last 3 years:		
Net profit (less 5 percent on investment)	20,000	100,000
Wages	120,000	30,000
	140,000	130,000
	85	23
	140)120000	130)30000
	1120	260
	800	400
	85−83=2%	23−16=7%
	[2] 2% increase	[2] 43% increase
	83)2.00	16)7.00

[1] In computing the wage distribution eliminate all participation of individuals who receive $10,000 per year or over.

[2] Points.

To be deducted from tax on net income 2 points; 43 points but limited to 8¼ points. (See below.)

For every point of increase in percentage of distribution there shall be made a deduction on the net-profit tax of an equal number of points as represented by the reduction in percentage. In other words, if the percentage of distribution should be increased by 2 percent, there shall be taken from the 16½-percent imposition on net income 2 points, making 14½ percent, but there shall be no reduction in the income-tax imposition greater than 8¼ points. It is understood that in computing the increased distribution the current year shall be taken in comparing with the basic 5 years, or the average of the last 3 years—whichever is more advantageous to the taxpayer.

Mr. KENNEDY. That is almost too simple, is it not?

Senator HERRING. You might proceed, then, with your explanation of it.

Mr. KENNEDY. You can see that my problem in preparing that was to make something that was applicable to all industry. For instance, I know of one industry that does a business of $250,000,000 a year. It has 10,000 employees. Therefore its ratio of wage distribution to its total net profits would be rather small. I know very intimately of another industry that has 7,000 employees and is very happy if it can sell $20,000,000 or $22,000,000. Therefore you could not set up an arbitrary base on which to make a reward for an excess over that base. So we have selected here a 5-year basis for any one company as being the basis on which performance would be computed.

Another objective of the plan as outlined in the preamble is to put the money into the lower brackets, where its velocity would be greater, where it actually would be spent, because we know money in a fat envelope will buy those things beyond necessities, and the very providing of those things beyond necessities will make for more employment.

Then another feature of the plan is if a company wished to try to get the advantage of a reward because of increased participation and should increase its wages, and should at the same time increase the cost of its product, it would naturally increase its net revenue, which, in turn, would reduce the ratio of the participation of wages to the total of wages and net revenue. So it has a brake there. It seems very definitely to attain the objectives as I understood them to be of the committee, to reward those companies who did put into circulation more money, that put more money into those channels where it would be spent.

Senator HERRING. Well, you would make these benefits apply regardless of whether it is high wages or the sharing of profits?

Mr. KENNEDY. Yes. The wage participation would be the total of all wages paid, plus any profit-sharing plan, anything that accrued to the workers. We have eliminated in this particular plan those who received more than $10,000, because it might be possible for a company to take unto itself the reward of an incentive plan by increasing the higher salaries to such an extent that the total wage bills would be very high, simply because the high salaries were increased.

Senator HERRING. Those in excess of $10,000?

Mr. KENNEDY. Yes.

Senator HERRING. Do you think this would encourage profit sharing or higher wages?

Mr. KENNEDY. It would encourage profit sharing, as I understand profit sharing, and that is some continuity throughout the year. Profit sharing in a lump sum personally I am quite opposed to, for two or three basic reasons, one reason being the employee receives the amount in rather large sums, unusually large sums compared to his weekly wage, and it causes a false standard of living. He buys a new radio, or a new piano, on the installment plan because he has money on hand and then it is not recurring again unless there be profits. I like the company whose employees participate by a higher wage scale through the year. I think that company is rendering a greater social service and perhaps following a more prudent business policy than one which does share rather large sums after a mediocre wage scale. But this does provide that a company which has had an unusually good year at the end of the year will be adding to the pay envelope a wage distribution, all of which would be added onto that which the employees receive and would be included as the participation on the part of labor.

Senator HERRING. Of course, that has been the fear of labor, that profit sharing would be at the expense of wages.

Mr. KENNEDY. It ought not to be. I agree with them heartily on that. I do not think it ought to be. I think a higher pay envelope week after week is far better for labor and is really far better for the employer too, because he really knows what his costs are going to be to a greater extent. Primarily, I would say it would be a greater social service to pay high wages throughout the year. I concur fully with labor in that attitude.

Senator VANDENBERG. Then there is not any war between the policy of high wages and the policy of profit sharing?

Mr. KENNEDY. It would be better if you could have both the high wages and profit sharing, and they both fit into this plan. This plan is a rather omnibus plan because it takes in all of those things.

Senator HERRING. As a matter of fact, you could not have profit sharing unless you had reasonably high wages?

Mr. KENNEDY. I do not know of a company that makes profits and that does not pay good wages. I know a lot of companies that are just struggling along and that are just paying the bare living wage. I do not know what your point was, unless that was it.

Senator HERRING. I know unless you pay at least the prevailing wage scale you are not sharing profits.

Mr. KENNEDY. No; you are not sharing profits, and you are not staying in business very long.

Senator HERRING. We have had many men coming before us in the last few days who employ anywhere from 400 to 65,000 people, sharing profits and having no labor trouble, and all of them seem to be making some money, even in these times.

Mr. KENNEDY. I think those are the companies that are making money.

Senator HERRING. We find them all over the United States. Just in the last few days we have had men who said they have no labor trouble in their plants, and they are sharing profits.

Senator VANDENBERG. The conclusion to be drawn from the fact that Senator Herring has just correctly indicated seems to be that profit sharing, in its broad sense, in the sense they use it, is a good business investment.

Mr. KENNEDY. I think every good employer would concur in that.

Senator HERRING. Well, this is very fine. We are very glad to have this. We will include this in the record. If you have anything else, Mr. Kennedy, that you would like to say, we would be glad to hear you.

Mr. KENNEDY. There is nothing else I would care to volunteer. I would be glad to answer any questions, sir.

Senator VANDENBERG. You are not operating a profit-sharing plan in your own company?

Mr. KENNEDY. No; we are not. We have, Senator, on our books a plan that is about 15 years old, that does provide for a participation on the part of the major executives, on all income over, I think it is 7-percent dividend to stockholders, but that was in the halcyon days, it has never been reached, we have never tasted blood on it, and we never expect to. We believe we have expressed our profit-sharing plan through our weekly envelope. I hope you will pardon me, it sounds just a little boastful, but others have said it and I am just repeating, that we have the highest wage scale of any company in our industry.

Senator HERRING. You have a large percent of women employed?

Mr. KENNEDY. Eighty percent.

Senator HERRING. Eighty percent out of about 4,000?

Mr. KENNEDY. Out of about 7,000. We have about 4,000 in Troy.

Senator VANDENBERG. That is a very practical profit-sharing plan.

Mr. KENNEDY. I think it is exceedingly so, sir.

Senator HERRING. I think that is all, Mr. Kennedy.

Senator VANDENBERG. Mr. Chairman, while we are waiting I would like to put in the record a letter from Mr. F. E. Fusting, vice president of the Crown Cork & Seal Co., Inc., Baltimore, Md.

A letter from O. D. Donnell of The Ohio Oil Co., Findlay, Ohio.

A letter from M. H. Karker, president of the Jewel Tea Co., Inc., of Barrington, Ill.

A memorandum from the accounting department of the Pennsylvania Railroad, Philadelphia, Pa.; all bearing both upon profit-sharing and incentive taxation in a constructive way.

Senator HERRING. If there is no objection, they will be included in the record.

(The letters and memorandum referred to are as follows:)

CROWN CORK & SEAL CO., INC.,
Baltimore, Md., November 1[illegible], 1938.

Mr. T. I. WALSH,
Technical Advisor, Subcommittee of
Committee on Finance of the United States Senate,
Room 777, Federal Building, Chicago, Ill.

DEAR MR. WALSH: I wish to respond to your letter of October 25, and also your telegram of November 10, both addressed to Mr. McManus.

Broadly speaking, we are of the opinion that if a tax reward plan was adopted on a liberal basis, that it should have the effect of encouraging business expansion, and should also encourage expenditures for the purpose of engaging in new lines of endeavor.

We shall undertake to answer specifically the questions set forth in the closing paragraph of your letter.

(1) Would suitable tax rewards encourage you to—

(*a*) Increase your plant and equipment maintenance expenditures?

(2) We feel that a liberal provision would encourage us to make expenditures of this character.

(*b*) Expand productive facilities?

Our answer to this would be the same as our answer to (*a*).

(*c*) Adopt profit sharing; or

(*d*) Employ additional help?

(2) Could tax rewards be equitably granted? Because of the innumerable questions that might well arise in the operation of a law of this character it is difficult to determine whether it could be equitably applied.

(3) What other measures do you believe are essential for the encouragement of capital in the resumption of normal activity and progress? Any plan which will relieve or lighten the tax burden of a corporation, and thereby place greater funds in its hands for expansion or distribution among its stockholders, we believe will be beneficial.

Very truly yours,

F. E. FUSTING, *Vice President.*

THE OHIO OIL CO.,
Findlay, Ohio, November 22, 1938.

Office of the president.

Mr. DONALD DESPAIN,
Director of Survey, Subcommittee of Committee on Finance of the United States Senate, Room 777, Federal Building, Chicago, Ill.

MY DEAR MR. DESPAIN: Received your letter of November 10, wherein you refer to comment contained in Schedule of Information relating to profit-sharing plan submitted with our letter to you of September 7, 1938, said comment being as follows:

"Such corporations should be accorded a graduated reduction in normal and surtax rates in proportion that the amount distributed bears to the total net income."

You have requested that we fully explain the above by an example, and our Federal income-tax department has submitted the following:

	Corporation A	Corporation B
Net income	$7,000,000	$7,000,000
Capital invested	40,000,000	40,000,000
Salaries to employees	2,000,000	2,000,000
Reasonable return of 5 percent on capital	2,000,000	2,000,000
Total before profit-sharing plan	4,000,000	4,000,000
Subject to profit-sharing plan	3,000,000	3,000,000

The rate of tax on both corporations A and B is the same up to this point. If corporation A has plan of allowing employees to receive additional compensation of 10 percent of $3,000,000, the corporation tax is reduced by 4 percent; 20 percent of $3,000,000, the corporation tax is reduced by 8 percent; 30 percent of $3,000,000, the corporation tax is reduced by 15 percent; 40 percent of $3,000,000, the corporation tax is reduced by 25 percent.

Percentage figures used above are not based on necessary information to determine reasonableness thereof, but are used for purpose of illustration. You will note that corporation B, not having distributed any portion of its net profits to employees, receives no additional tax reduction or credit as does corporation A.

Yours very truly,

O. D. DONNELL.

JEWEL TEA CO., INC.,
OFFICE OF THE PRESIDENT,
Jewel Park, Barrington, Ill., September 12, 1938.

Mr. THOMAS I. WALSH,
Technical Adviser, Subcommittee of Committee on Finance, United States Senate, Chicago, Ill.

DEAR MR. WALSH: The subject raised by your letter of August 30 is both broad and difficult of solution. It is easy to agree with the principle that there be the incentive of tax advantage to those who contribute to the increase in employment and the distribution of larger benefits to workers, but it will be much more difficult to work out a plan which will be relatively simple of administration.

Without meaning to be trite, it seems clear to me that the best incentive to increased employment and to a resumption of American enterprise would be a decrease in the needs for tax receipts. If the present rates must be continued, then even the assurance that they would not need to be further increased might be enough to arouse some of the enterprises in the country, even in the face of the fact that many of the cards in the deck would remain stacked against the employer.

Before proceeding to the specific suggestions in reply to your letter, I should like to make two general observations:

(a) The present revenue act sufficiently penalizes the "feast or famine" industries—those in which there are wide fluctuations in employment and in earnings—but it penalizes such industries only if there are years of losses alternating with years of profit. From our point of view and as it affects our industry, I see no reason for a change in this principle although others may have a different point of view.

(b) Neither the law nor the regulations now provide a discount for the prepayment of tax liability, although interest is charged at the rate of 6 percent per annum on deficiencies. It is suggested that consideration be given to the provision of a discount for prepayment to the end that government may be earlier in receipt of taxes due.

There are three fields in which, it occurs to me, corporate and individual employers should properly be rewarded for increased efficiency. Employers with the best showing or with an improved performance over base, in these particulars, are contributing directly and measurably to the economic welfare of the country and would be further encouraged to do so by relatively small tax advantages. The tax concession need not be anything like enough to pay the cost to the employer but it should be sufficient to impress the fact that the contribution has been recognized and is valued by the Federal Government. The three factors which I believe to be important are these:

1. The average weekly employment during the tax year of larger numbers of men and women over those employed by the same business in the "base" year, with adjustments upward in the base for businesses or activities purchased but no adjustments downward for business sold.
2. For the maintenance or increase of full-time (52-week) employment.
3. For distributions to workers over and above established pay rates whether such distributions are by means of bonus payments, profit sharing, wage extras, or otherwise.

Purely as a suggestion as to the method by which such tax incentive might be made effective, it is suggested that the item (1), numbers employed, the base year be made 1929 and that for each increase of 10 percent in the number of full-time average employees per week one-half percent reduction be allowed in the income-tax rate on the profits of the employer with a maximum credit for 100 percent increase employment (i. e., a maximum reduction in the corporate tax rate from 19 to 14 percent, plus additional credits now allowed by law). This one suggestion of means is submitted with the realization that it is an encroachment on the field of the technical expert in the drafting and administration of the law, but I believe it to be entirely practical and to hold the promise of much good.

The tax incentive must be relatively substantial if it is to serve as incentive for further improvement in employment and not alone as reward for those few organizations which have already increased employment.

Sincerely yours,

M. H. KARKER, *President.*

THE PENNSYLVANIA RAILROAD, ACCOUNTING DEPARTMENT, PHILADELPHIA, PA.

INCENTIVE TAXATION

The Pennsylvania Railroad Co. has, of course, like other concerns, given consideration to profit-sharing systems for its employees, but the financial condition of the railroads in the last few years has been such as to preclude the possibility of its being seriously considered. However, if the definition of "incentive taxation" is extended to include the employment situation, then from a railroad point of view it should receive very serious consideration.

The spirit of incentive taxation is recognized by a number of the State laws which have merit rating provisions, such merit rating provisions providing for a reduction in the amount to be paid under such compensation laws, dependent upon the stability of employment. Forty-one of the State laws (including Alaska, Hawaii, and District of Columbia) contain provisions for merit rating laws of other States make provisions for its study, and only two of the States have no provision in regard to merit rating.

Proceeding upon the basis that employment would assist the Government by reducing the number of persons unemployed and on relief, then for those corporations which have provided employment beyond what might be considered normal or average, such corporations would receive some reward in the way of incentive taxation by a reduction in their Federal income, excess-profits and capital-stock taxes, the amount to be expressed in a reduction of their taxable income for the three taxes mentioned above.

In other words, any year in which employment, expressed in hours paid for, is in excess of the average for 10 years, or some constant test period, then there should be some allowance made in taxable income for such excess. However, the basis might start from the year 1931 and be for such period less than 10 years until the 10 years is reached, and then one year could be dropped and a year added, etc. No penalties should be added when the hours paid for by an employer in the railroads goes below the average, for the reason that the taxable income drops very materially as a result of a depression. However, such an incentive as suggested would have a tendency to keep up employment rather than decrease it.

As an instance of what took place on the Pennsylvania Railroad: In the 7 years ending 1937 the average per annum of hours paid for was 258,000,000 and in 1937 it was 289,000,000, 1937 being an increase of 12 percent over the average. For each 1-percent increase in the number of man-hours worked in any particular year over the average for the 10 years there could be allowed as a deduction against net taxable income an amount equivalent to one-half of 1 percent of the estimated increased compensation paid, which would be calculated by taking one-half of 1 percent of the increased man-hours and applying thereto the average rate of pay per hour. The following concretely illustrates the above statement:

Taking the year 1937:

(*a*) Excess hours of employment 31,000,000, or 12 percent.

(*b*) One-half of 1 percent for each 1 percent would be equivalent to 6 percent increase.

(*c*) Six percent of 31,000,000 hours would be 1,860,000 hours.

(*d*) One million eight hundred and sixty thousand hours at average rate of 70 cents per hour.

(*e*) Reduction in taxable income equivalent to $1,302,000.

(*f*) Reduction in taxes (income), $247,380.

It should be noted that the reduction is not in taxes but in the amount of taxable income.

The above specific illustration may not be the proper mathematical table to work out incentive taxation based on giving the employer a reward for the hours of labor he provides, but it contains the nucleus of an idea which could be worked out—perhaps it should be more, perhaps less.

Senator HERRING. This is Monsignor J. A. Ryan, of the Catholic University, Washington, D. C.

STATEMENT OF MONSIGNOR J. A. RYAN

Senator HERRING. Monsignor, we know of your work and your interest in some of the proposals in the resolution under which this committee was appointed. We appreciate your coming down here and talking with us about your experience. You may proceed as you wish.

Monsignor RYAN. The last few years have witnessed a considerable increase of interest in profit sharing, particularly among businessmen and legislators. While the majority of both these groups shrink from fundamental changes in the industrial system, some of them realize the necessity for some modifications. An organization of businessmen called the Industrial Relations Counsellors sponsored a study in the years 1936 and 1937 of profit-sharing plans in the United States and Great Britain and near the end of the latter year published their findings in a volume entitled "Profit Sharing for Wage Earners," published by the Industrial Relations Counsellors, Inc., New York.

In the spring of 1938 a subcommittee of the United States Senate was appointed to study the whole subject. Organized labor is mostly hostile, or at least indifferent, to profit sharing because it has, in a large proportion of instances, been used to discourage unionism or to serve as a delusive substitute for higher wages.

As a matter of historical fact, profit sharing has not been an important feature of American industry. According to the volume mentioned above "the record of profit sharing is mixed." The total number of plans initiated in both Great Britain and the United States have not exceeded 1,000; considerably less than 200 are now in operation in this country; and the arrangement "is only applicable in a business with a record of fairly stable and continuous profits." In general, this volume, or report, intimates that no rapid or widespread increase in the number of profit-sharing plans is to be expected.

There are only two existing types of profit sharing that seem worthy of the name or deserving of serious consideration. In one of these dividends are paid at the same rate on the stock held by the capitalist and on the annual sum of wages received by the workers. The other type divides the total profits which remain after stock dividends, wages, and all other expenses have been paid, equally between the owners of capital as a whole and the wage earners as a whole. Perhaps the best-known instance of this type is that carried on with considerable success for many years by the Louisville Varnish Co. under the direction of its president, Col. P. H. Callahan. However, the profit-sharing scheme there has not been actually working the last year or two, I think, and it was not during the greater part of the depression.

Neither of these plans nor any other is completely logical or scientific or capable of being widely successful. In fact, there is only one kind of profit sharing which meets these requirements, and it has never been put into actual operation. It resembles the second of the two plans just described inasmuch as it would distribute only surplus profits; that is, those which remain after the payment of reasonable dividends and reasonable wages. It differs from that arrangement inasmuch as it would give none of the surplus profits to the owners of capital stock as such. All the surplus would go to labor, that is, to the receivers of wages and salaries, to everyone who labors in the corporation in any capacity, from the president to the lowliest employee. And the division should be in proportion to the regular wages and salaries.

There are two reasons why the owners of capital should not share in the surplus profits: First, because they do not need this incentive in order to perform their functions as owners and stockholders; second, because, as such, they perform no significant amount of labor. If they receive a sufficient rate of dividends to induce them to place and keep their money in the business, there is no good reason from the viewpoint of either economics or ethics why they should get anything more. They are as well off as the preferred stockholders in any existing corporation, who never receive extra profits of any sort. It has been suggested that the dividends should be cumulative, that dividends which have been omitted or reduced on account of poor business in 1 or more years should be paid up before any new surplus profits are distributed. In view of the grave and increasing evil of fixed bonded indebtedness in our industrial system, however, this suggestion is of questionable value. The necessary protection for the stockholders could be provided by an adequate dividend rate. Ethically, the method is unobjectionable, as Pope Pius XI points out: Capital has a right to a share in the product but the amount of its proper share is determined by the common good; if the capitalists are willing to place and keep their money in a concern the common good is adequately safeguarded.

On the other hand, giving all the surplus profits to those who perform any active function in a business concern would relate rewards to efforts and provide the strongest kind of incentive for more and better efforts. After all, one of the principal merits of private operation of industry is that it encourages the entrepreneur, the active director, of a concern to do his best because his rewards or profits will be large or small in proportion to his efforts. To be sure, his best efforts do not always bring proportional returns, owing to his own incompetence or to risks which he did not adequately estimate; but the number of instances in which this inducement has been effective and fruitful is so great that there is still an abundance of business men who are willing to take the risks for the sake of the rewards.

Since this principle or policy has proved itself in the case of the directors of business, why should it not be equally effective with regard to all classes of employees? The practice of giving surplus profits to owners and stockholders merely as owners and stockholders, when they are already adequately remunerated for their ownership function, is uneconomic and unscientific. To give this variable and contingent share of the product to all classes of workers in proportion to their wages and salaries would be at once economic and scientific. It is unnecessary to emphasize the increased interest in their work and in the good fortune of the employing concerns which would be created in the great majority of employees if this additional remuneration were made available.

Another reason, and a more fundamental one, for adopting this type of profit sharing is the effect that it would have upon the distribution of the product as between capital and labor and the consequent good effect upon industrial prosperity. Any device or arrangement which gives labor more and capital less will help to achieve and maintain full employment and full operation of our industries.

The recent, or present, business recession became inevitable on account of the chronic disproportion between saving and spending which has existed for the last 50 years but has greatly increased since the beginning of the present century. In the volume on America's Capacity to Consume, the Brookings Institution attributes the recent increase in the rate of saving to the notable increase in the national income which has enabled the population to save more, and particularly to the relative increase in the incomes of the upper classes. Too much of the national income or national product is saved and too little is consumed. Too much goes to capital and too little to labor and the farmers. Three-fifths of the savings in 1929 were made by that 10 percent of the population having incomes of over $5,000. Of course, almost all the savings of this 10 percent came out of interest and dividends. If the members of this group had received considerably less interest and dividends, the total savings of the country would have been smaller, the excessive capacity for production would have been lower, the incomes of the wage-earners would have been higher and their volume of purchases larger. Thus more business would have been done, a smaller productive plant would have been operated more nearly at full capacity and there would have been less unemployment.

Under this plan, the conduct, direction, operation, of an industry would obviously be in the hands of its workers of all classes. These powers might be exercised, as in the present system, by the board of directors, acting alone, or in cooperation with a part or all of those who are ordinarily called employees.

In 1932, the late Robert S. Brookings, the wealthy man who founded the Brookings Institution, advocated the enactment of a law by Congress which would require corporations operating in interstate or international commerce to take out Federal charters.

> The new articles of incorporation (he proposed) while securing to capital a fair return at a fixed rate of interest and dividends, risk considered, would divide all additional profit or accretions in the form of labor shares between the employees (management and labor) in the ratio of their individual contribution, probably as recorded by their wage or salary compensation.

That is taken from his little book, The Way Forward, pages 17 and 18, published in 1932 by the Macmillan Company, New York.

The only notable difference between the Brookings plan and that described in the paragraphs immediately preceding is in the requirement that the surplus profits should not be distributed in cash but take the form of a special kind of securities, called "labor shares." On these the holders would draw dividends. The shares held by a person who had ceased to be an employee (through death or otherwise) would be sold to the company at their book value.

Apparently, Mr. Brookings derived this plan from the "Companies Empowering Act," which was passed in 1924, in New Zealand. Although the labor shares do not form part of the capital of a company, nor have any nominal par value, they enable to holders "to attend and vote at meetings of shareholders, * * *." In other words, the New Zealand law combines labor participation in profits with labor participation in management and control. Undoubtedly, this would contribute greatly toward making labor, to quote Mr. Brookings, "in reality the partner and ally of capital." There is no reason why the labor shares provisions of the New Zealand Act should not be included in the Federal incorporation bill which has been introduced in the United States Senate by Joseph C. O'Mahoney.

Senator HERRING. Do you have anything else you would like to suggest, Monsignor?

Monsignor RYAN. No. I was very much interested in this particular kind of device for profit sharing, in fact, I wrote about it in a magazine 14 years ago. Shortly before he died, Mr. Brookings sent me a copy of a booklet—not a booklet, just a pamphlet—in which he had this plan outlined. Very nicely bound, this particular copy was, too. He wanted me to send it to the Pope, because the Pope had shortly before that published his encyclical on reconstruction of the social order. I sent it to the Secretary of State to be given to the Pope and got a nice letter back, and gave it to Mr. Brookings, but I said to Mr. Brookings, "I had this thing about 10 years ago." I sent him a copy of it.

Now, of course, this revolutionary proposal, as I say in the text, is not in existence anywhere, but I think it is the only profit-sharing scheme that will amount to anything, and I cannot see anything unsound about it. Of course, the dominant consideration is that there are not any surplus profits to distribute until fair wages are paid and capital is getting enough interest to induce it to stay in the business.

Now, that is the theory, anyway. How it can be worked out, or when, or if ever, I do not know.

Senator HERRING. I was interested in the figures you gave as to the profit-sharing plans in effect in this country. We made quite a search. It refers to 100 or 175, or something, but, as a matter of fact, to show the inadequacy of those figures and the wisdom of this survey, we have located over 2,500 profit-sharing plans in effect in this country in one form or another, depending upon the judgment of the management as to what is best for their employees, and we have located already 490 direct profit-sharing plans in effect in America today.

Monsignor RYAN. I got these figures from this publication.

Senator HERRING. That is true; and until this survey was commenced and partially completed no other figures were available anywhere. We will have something that is very definite and will show that profit sharing is increasing in this country much faster than it has been generally believed.

Thank you very much, Monsignor. We are mighty glad to have your contribution.

STATEMENT OF WALTER GOODSPEED, VICE PRESIDENT AND TREASURER, AMERICAN BOX BOARD CO., GRAND RAPIDS, MICH.

Senator HERRING. We will appreciate your giving us a brief history of your business from its inception, how you came to put in the system that you are employing, and so forth.

Mr. GOODSPEED. Well, our business started about 1903, I believe, and we are in, I figure, six separate industries, and I mean by "industries" types of business in which we have separate types of competition, and I think it is an important point to bring out in explaining the type of wage-payment methods that we have as compared with others, because our problem is to compete in six different industries and it makes a different problem on profit sharing, I feel, than other companies are facing.

I wonder if I understand fully just what is meant by profit sharing as your investigation discloses. I may be incorrect in that understanding, and I would like to have some questions answered. Is it not a wage-payment method that is adjusted on fluctuation in profit and losses?

Will not the payments to labor under these plans be deductible as expense under the income-tax laws? Is that true?

Senator HERRING. I think that is now true.

Mr. GOODSPEED. It would seem to me that these systems would tend to result in higher wage payments in prosperous times and in lower wage payments in periods of losses than other wage-payment systems.

If a company is paying a fair return to its employees and stockholders, and has an efficiency incentive system that is fair to its employees, a change in its wage-payment method cannot, it seems to me, over a period of years, increase the total pay roll on the average, or the total dividends.

The wage-payment method of the American Box Board Co. can be explained as follows: The company agrees to pay all employees, wages (hourly earnings) equal to the average paid by competition per division. It is to be noted that each division is a part of a separate competing industry. If our efficiency is found to be higher than the average, we agree to pay higher hourly earnings, and if efficiency is below the industry average, hourly earnings will follow. In such cases where it is impossible to compare efficiency, it will be assumed that our efficiency is equal to the average of competition. In comparing efficiencies, employees must not be penalized because they are working on less efficient machinery than competitors, nor will they be rewarded because they are working on more efficient machinery.

Rates within each division will be balanced by the use of job analysis. By this method job analysis is maintained as a factor in rate determination, and at the same time the average rate per man per hour by division is kept in line with the industry. Jobs on which industry comparisons are impossible will have their rates set by job analysis.

The result of this system or method of wage payment in our company over an 8-year period, 1930 through 1937, inclusive, has been as follows: Total pay roll, $5,603,635.54; total earnings on the common stock, $625,252.75. It should be noted, however, that in 1932 our company paid considerably higher wages than the average of competition. I would like to stress that point and have it kept in mind.

The amount earned by the common stock represented a 4-percent average earning per year on its appraised book value of $15 per share. However, the common stock received in dividends only 1.6 percent, or $250,726. The balance of the earnings was placed in capital additions and in increasing working capital. I sincerely feel that had any wage-payment method been used by the American Box Board which would have resulted in a material increase over these years in the pay roll at the expense of the common-stock holders, more than 50 percent of the jobs of our present 550 employees would have been lost for the reason that the common-stock holders would have sold a substantial part of the company and its operations would have been shut down and moved to other locations.

It should further be noted that the earnings on the common stock varied from a plus 15 percent on its book value to a negative 10 percent. It should also be noted that the tax which was paid over that 8-year period was $433,604.91.

I feel that the wage-payment method we are using in our company is to be preferred to so-called "profit division systems" because—

1. The wage earner under our method is not penalized by the inefficiency of management, the inefficiency of machinery, the inefficiency of location, the size of the working capital, and so forth. These things he has no control over or responsibility for, and therefore we feel that as these factors fluctuate he should neither be penalized nor rewarded.

2. Under our system, efficiency of labor is promptly rewarded and guaranteed. Under profit-sharing systems usually it is necessary to wait until the end of the year when profits are determined to arrive

at their divisions, and if there are no profits, high efficiency may never be rewarded.

3. It seems to me there is an incentive under profit-sharing systems to postpone the payment of as much of the wages as possible until the end of the year. In prosperous years this will allow bigger tax rewards, and in unprosperous years postponed wages may not have to be paid at all. Under our system, within 7 days all employees are paid in full for their services and efficiencies.

4. Further, our system, if adopted by our industry, would tend strongly to prevent recurrent "competitive wars" (sales as low as 50 percent below costs) being fought off the wages of the industry's employees. Most profit-sharing systems, it seems to me, would encourage this type of competition, because the employees would be forced to join in carrying this burden.

5. Our company is divided into six divisions, and we compete in six industries. Often one or more of our divisions show losses, while the total operation of the company shows a profit. Those employed in divisions or in industries which are showing losses would, it seems to me, also share in the profits, and thereby obtain higher wages than competing workmen in companies having their business in a single industry. The result would be that our costs would be higher than our competition, and we would obtain less work for our men. Our wage method has been established to carefully avoid this serious and disastrous result.

In short, I feel that the profit-sharing systems may make for happier industrial employee relations until these employees learn that it is more than a glamorous title, and that they have much to lose and little to gain by changing from their present wage-payment methods. Is not sharing of the profits also a system to share the losses, to share management's inefficiency, to share a company's possible poor location, or to share the losses or gains from inventory speculations? There seems to be more to say against profit sharing from the employees' point of view than from the employer's; however, no wage-payment method that is unfair either to employees or stockholders will work.

Our employees asked for a "split in profits" after the termination of the prosperous year of 1937, and upon the above explanation overwhelmingly decided to keep our present wage-payment method. Why should our employees and stockholders be penalized by incentive taxation because of their decision?

Senator HERRING. You have about 550 employees?

Mr. GOODSPEED. Yes, sir.

Senator HERRING. About what is your average wage?

Mr. GOODSPEED. You mean hourly, weekly, or yearly?

Senator HERRING. Either way; I don't care.

Mr. GOODSPEED. Our minimum wage at the present time is 45 cents for men to about one-half of 1 percent of our employees, the base rate, without premium or bonus. For men: average hourly rate, 63 cents; average weekly rate $26.32.

Senator HERRING. Is your labor organized?

Mr. GOODSPEED. No, sir; it is not.

Senator HERRING. Do you have any labor trouble?

Mr. GOODSPEED. No, sir. It has been organized; and they gave up their charter some 2 years ago.

Senator HERRING. Do you know about what percent of your wholesale price is paid to labor?

Mr. GOODSPEED. Our wholesale price happens to be our retail price. They are the same.

Senator VANDENBERG. How much of your production dollar goes to labor?

Mr. GOODSPEED. I would say about 35 percent goes to pay roll.

Senator, might I ask you a question about this incentive taxation? In our correspondence I have felt that I have not fully understood it, and I would appreciate any enlightenment. Perhaps badly stated, it sounds to me as though incentive taxation is a threat to those companies who do not accept a voluntary course of action, that they must carry the tax load of those that do. We feel that we are sharing profits as much as it is possible to do so, and still keep our company going, but in our own manner and in our own way, and it may not be called profit sharing according to your later definition. You may have a group of industries and, let us say, it is 50 percent that have a wage-payment method; that is, within the definition of profit sharing, and you have 50 percent that have not. Now, all that industry together must bear a tax burden of, let us call it, an artificial figure of $2,000,000,000. Now, as you give tax awards and relief to the one group, is it not true that that tax must be raised, must fall over on this other group? So, it becomes a punitive tax not to follow the voluntary course of action that is offered, because this later group of industries and companies must carry the tax load of these people or these industries that have been relieved.

As a matter of fact, it may be so burdensome that this group of companies will be forced to fall into a profit-sharing system and that result will be accomplished.

Senator VANDENBERG. The best answer to you would be to carry the example into the analogous field of State unemployment compensation laws. You are familiar with the fact that some States have the so-called merit rating in connection with fixing the unemployment compensation?

Mr. GOODSPEED. That is right. I think Michigan has, has it not?

Senator VANDENBERG. Do you believe in merit rating?

Mr. GOODSPEED. Absolutely.

Senator VANDENBERG. That is precisely the thing that incentive taxation is. That is incentive taxation. That is a reward to the industry which, through its own operations, succeeds in keeping its unemployment to a relative minimum, whereupon the tax rate rewards it in degree for its success.

Mr. GOODSPEED. Yes.

Senator VANDENBERG. Now, under your previous statement, of course, that seems to throw an alternative burden on the inefficient employer who has not earned the merit rating, but still you say you believe in a merit rating, so it would seem to me that you believe in incentive taxation.

Mr. GOODSPEED. As I understand the merit rating, the method of taxation is the setting aside of a fund of money by each company to take care of their own unemployment, their problem. Now, if they are able to minimize the amount of that unemployment through their own efforts it seems to me that that is setting aside their insurance program, because their risks, like a fire risk, are less. It seems to me that is in an entirely different category than incentive taxation as attached to profit sharing.

Senator VANDENBERG. I think the analogy is rather clear. I do not want to debate it with you here. I would like to say this to you, Mr. Goodspeed. I know Mr. Goodspeed's company in our city, a thoroughly progressive company, and Mr. Goodspeed is a thoroughly progressive businessman. The mere fact he appears to disagree with what we are calling profit sharing is no sign that he is not socially minded in his attitude, so far as I am concerned, because I know better. I think, Mr. Goodspeed, it was very fine of you to come down here at your own request to present your criticism of the theory of profit sharing, because the theory certainly is not 100-percent sound, and it is just as important to identify the pitfalls as it is to find the advantages.

Now, what I get out of your testimony is this: You are actually profit sharing in your own way at the present time, under your own wage system, only your form of profit sharing has not fallen within what you deem to be our definition of profit sharing.

Mr. GOODSPEED. That is right.

Senator VANDENBERG. That is the only difference between us at the moment.

Mr. GOODSPEED. Of course, Senator, perhaps I do not understand what profits are. Profits, it seems to me, are the increment that goes to the stockholder, and the only way I know you can split it would be to have the stockholders disgorge and give back to the employees; that we get a certain amount of money from our sales and divide that up between our stockholders and our employees. If that is what is meant by profit sharing, we certainly share profits.

Senator VANDENBERG. You certainly are. You have indicated that in your judgment a more limited formula of profit sharing is not wisely applicable. That might be true. Senator Herring and I have started upon this journey with the distinct understanding that we would not propose to try to dictate any formula to anybody, because we completely recognize the fact that industry is so complex and diversified in this country that you cannot standardize a formula of this sort. What we are endeavoring to do is to create a record of authentic experience of American industry with profit sharing, so that out of that record the employer who voluntarily wants to use any of the information by way of application to his own operations can do so with the feeling that he is consulting a dependable source of information.

The fact that you doubt the wisdom of the application of this theory in your particular industry would not lead you certainly to quarrel with the businessmen who paraded across this forum in the last week to demonstrate clearly that direct profit sharing has increased the efficiency of their plants, has actually increased the earnings of their companies, has not only produced industrial peace but has made a progressively expanding prosperity possible, and frequently they credit profit sharing with a substantial portion of this happy result.

Now, the businessman who finds himself in that attitude I am sure you would be happy to have him continue upon his own way.

Mr. GOODSPEED. Absolutely, providing I would not have to share in any of his taxes.

Senator VANDENBERG. Exactly. Your story is on the record now, and those that do enter on the things you do, and those that enter on the things that the other fellow does can have the benefit of the parallel, and can do just as they please, as far as we are concerned. Personally, I am very much obliged to you for coming down.

Mr. GOODSPEED. I have enjoyed it, and I hope I have given you a little picture of our industry, which is an interesting one because of its wide fluctuations. We are in a prince and pauper industry. Our industry makes boxes for all industries. We have sharp competitive conditions, particularly during these times because of the rapid expansion in the South of the Kraft operations.

There is one point that I left out that I would like to make. I am wondering if under a profit-sharing incentive taxation system, whether or not the inefficient management would not be a favored operator, because his cost would be lower than the efficient management's cost, because his wage rates would be lower because he had no profit to share. That would be an unhappy result if that was the case, I think you would agree.

Senator HERRING. It would be if that would be the case; yes, sir. I suggest you might obtain a copy of the evidence that has been collected from these other men who have taken a different position. It would be of interest to you.

Mr. GOODSPEED. I would be glad to study quite carefully the final findings of your committee.

Senator HERRING. We will see that you get it.

Mr. GOODSPEED. Thank you.

Senator HERRING. We will recess until 2 o'clock.

(Whereupon, at the hour of 11:40 a. m., a recess was taken until 2 p. m., of the same day.)

AFTERNOON SESSION

Senator HERRING. We will next hear from Mr. Lewis.

STATEMENT OF JOHN L. LEWIS, PRESIDENT OF CONGRESS OF INDUSTRIAL ORGANIZATIONS

Senator HERRING. Mr. Lewis, I know you are fairly familiar with the purposes of the resolution and what we are attempting to do.

Mr. LEWIS. It is very complimentary on your part to say so.

Senator HERRING. I think you said you have a statement prepared.

Mr. LEWIS. I have a very brief little statement, if you will allow me to read it.

Senator HERRING. If you will do so, please.

Mr. LEWIS. Mr. Chairman, and Senators, consideration of plans of profit sharing between employers and employees presupposes the existence of profits to be distributed. However, labor has not been afforded, in the past, any opportunity to participate in the affairs of management which may result in either profit or loss. The price policy and volume of production of any corporation, to mention but two determining factors in the question of profits, are never negotiated with the labor unions representing the employees. The rate of profit lies entirely in the hands of management.

Yet testimony has been adduced before this committee urging a policy that labor accept as part of its just compensation a participating share in profits which are completely beyond its control or influence. Labor's disillusioned experience in regard to profit-sharing plans has been that they have been used as a device to avoid the payment of an immediate decent wage and made labor dependent upon haphazard industrial and financial policies of management.

The Congress of Industrial Organizations presents, as its contribution to the stability of industrial relations, collective bargaining with employers in regard to wages, hours, and working conditions. Labor organizations are a necessary instrumentality to achieve the economic strength to obtain wages which will afford a decent standard of living for the working men and women of this country.

In engaging in collective bargaining labor unions must give heed to the economic factors which prevail at the time of such negotiations. However, a worker and his family must live and his only source of income for livelihood is his wages. A period of falling income and profits for industry due to its own miscalculations or mishandling of its affairs of management must not carry with it an equivalent slashing of wages for the workers.

The maintenance of the wage standards of this country through the efforts of the Congress of Industrial Organizations has been one of the greatest contributing factors to the brevity of the depression out of which we now seem to be emerging. Increased wages and higher standards of living for the workers of the country mean increased purchasing power for the real consumers and thereby increased demand and productivity for the benefits of industry.

Labor cannot eat or live on hopes of participation in profit-sharing plans. Immediate higher standards of living achieved through collective bargaining with labor unions is the best guarantee policy for the continued expansion of industrial activity and profits from management.

That is my formal statement, Mr. Chairman.

Senator HERRING. If you have any other observations you may go right ahead, Mr. Lewis. We would be glad to have any suggestions you have. You have read the testimony that has been presented, or some of it, have you not?

Mr. LEWIS. Only sketchily, Mr. Chairman. I have not been able to keep up with it entirely.

Senator HERRING. There was some suggestion as to profit sharing also meaning the sharing of management. Many of these men who testified here have had the most satisfactory results, and they have testified they arrived at the sharing of profits through negotiations with labor, and even some of them, I think, by collective bargaining.

Mr. LEWIS. Unfortunately, these profit-sharing devices have been too frequently put forward as a substitute for bona fide collective bargaining. Those plans have oftentimes been used to augment or bulwark the company union or employee plan of representation, and have been used as a substitute for modern collective bargaining. The result of the inability of the workers to have very much to do with the question of the ratio of profits, or the earning of profits, and the policy of management in sales volume and other things of importance bring about a lack of confidence on the part of the average man, the average worker, in those plans.

Senator HERRING. Do you happen to know of any industry that is sharing profits with employees whose employees are members of your organization?

Mr. LEWIS. I think there is a substantial number of such employees who have become identified with our organization subsequent to the establishment of the profit-sharing plans. I do not at this moment recall the name of any corporations who have instituted profit-sharing plans since they have made collective bargaining contracts with unions of the employees.

For instance, the General Electric plan has been established for quite a long time. However, that was instituted years ago, before the General Electric made collective bargaining agreements with legitimate union organizations, and that plan, which has been spoken of probably before the committee, gave very little participation notably in 1935, and perhaps this year, and there is very little coming to the employees of that corporation, which, of course, is one of our premier corporations, perhaps one of the best managed and most progressive corporations.

Senator HERRING. As I recall it, it was testified that they have organized labor and this plan was arrived at through negotiation, and they had no difficulty in arriving at what each agreed was a fair basis.

Mr. LEWIS. We believe if any industry or a concern is making profits that would permit them, if they desired, to share those profits with the employees, that they will have no difficulty at all under collective-bargaining practices in making the necessary adjustments of the wage structure so as to permit the employees to have a higher wage. In fact, I think the unions will cooperate at all times on any suggestion from the corporations that they wanted to modify the wage structure upward.

Senator VANDENBERG. That is the interesting point, Mr. Lewis, at which the equation enters. Most of these employers who have been here, who are profit sharers, so to speak, have started out by insisting that profit sharing cannot be a substitute for adequate wages. We can all agree on that, I assume. Now, after, let us say, completely adequate wages have been established by collective bargaining, is there not a——

Mr. LEWIS (interposing). You bring up the question there, Senator—pardon me——

Senator VANDENBERG. Yes.

Mr. LEWIS. As to what may be a completely adequate wage.

Senator VANDENBERG. Let us assume, for the sake of the argument, that you would say it is a completely adequate wage.

Mr. LEWIS. I could only say that for the moment, but at some other time that may not be true.

Senator VANDENBERG. I understand. What I am reaching at is this: After you have stabilized the wage at what could fairly be said is adequate, is there not then inevitably a fluctuating profit and loss in every business which cannot possibly be followed by a fluctuating wage factor in addition to this standard wage, and is there any more satisfactory way to measure that final fluctuating factor than through profit sharing? Do you see what I am trying to say?

Mr. LEWIS. I think I follow you, Senator. You want to protect the interests and at the same time maintain stability there.

Senator VANDENBERG. Yes.

Mr. LEWIS. I think it is true, however, that the best way to measure those equations is, from time to time, when new wage agreements are negotiated in the light of the operating record on the profit record of the industry or corporation during the tenure of the agreement. I do not know how you can fabricate any reliable yardstick other than the record of performance, the same test that our banking institutions apply to a borrower. They want to see what his concern is doing on its operating statements.

Senator VANDENBERG. I wonder if I have made myself plain. Suppose a corporation has an extraordinarily good year, which obviously is extraordinary, that cannot be the basis for a permanent wage structure, because the prospects are that that extraordinary prosperity will not be continued. Now, if wages are adjusted upward to fit an extraordinary year, are they not calculated to stay at that extraordinary point and not be reduced commensurate with the average year that follows:

Mr. LEWIS. I think even that difficulty can be surmounted merely through the device of the corporation or company conferring with the representatives of the employees, and if the situation is such that they want to give them an immediate participation of any amount in the profits of that year, I have no doubt but that arrangement could be immediately negotiated without the necessity of having it apply to the basic wage structure, and, as you say, constituting a real problem as regards future operations. I think that the average man who works for a living does not want to be the recipient of this paternalistic generosity, Senator. He thinks his labor is worth so much. He is willing to discuss the question of how much it is worth, the same as the seller of a commodity discusses with the possible buyer the price of the commodity, and he prefers to have it himself; he prefers not to wait for it. He needs it day by day, and he is more satisfied, and he is quite enthusiastic, too, if under that wage scale the company prospers and the investors receive a return on it, and as he measures their return he becomes more capable of estimating the value of his own service to the industry.

I think that in profit sharing—oh, there is too much of a theory of the distribution of largess, there is too much of the proposition of dropping a dollar in the plate or $20 in the pot as an act of generosity, whereas, as a matter of fact, the employees in that industry who operate the industry had a great part in the production of the materials and the commodities to make possible the profit.

I know that from time to time through the years well-meaning men, leaders of an industry, perhaps especially fortunate or deriving special benefits at the moment, have voluntarily, on their own motion, wanted to give employees some participations. Those experiments have begun way back, but I do not think that out of those experiments has come any crystallized basic principle that could be applied with success today.

In some ways this profit-distribution proposition is related to the so-called flexible wage scale, or what we used to call the sliding scale. The sliding scale in the anthracite-mining industry was introduced as far back as 1869 or 1870, and the wages of the men were tied to the price of coal at certain points, and from time to time through the years the wages would fall or rise, but always the wokers had no power of influencing the factor of change; that power always rested with the industry, with the operators. If they came to an agreement that for reasons of their own they would reduce the price of anthracite at destination point or the basing point 25 or 50 cents a ton, or for any reason that seemed to them valid, down went the wages. The workers were not consulted; they had nothing to do with it. If they were making good margins of profit and wanted to satisfy a local situation they would raise the price and raise the wages 25 cents a day.

The workers were constantly at the mercy of a few statisticians employed by the operators who computed the tonnage and set down the factors that controlled the wage scale.

That same proposition runs into any kind of a sliding scale, any kind of a flexible wage, any kind of a profit-sharing patronage. Through the years representatives of labor have given very earnest consideration to it, from the standpoint of determining whether or not there was some virtue there that might be set forth in a perfectly fair way to all parties interested, but, frankly, after all my experience, I think the profit-sharing idea is rather a delusionary snare, as far as modern industry is concerned.

Senator VANDENBERG. Have you given any consideration to the other phase of our inquiry, namely, the possibility of encouraging employment through incentive taxation?

Mr. LEWIS. On the whole I would be opposed to the suggestion, because I think it disturbs the competitive factors of all industry, and I think it leaves the workers open to the inequities of the various arrangements that might be instituted in A industry or X industry, or A plant or X plant. I think the variables there are so great that it would seriously affect the competitive relationships within an industry.

Senator VANDENBERG. Consider for a moment the so-called merit rating in State unemployment laws. Would your criticism run against the merit-rating system also in respect to State unemployment laws?

Mr. LEWIS. What particular phase of that do you have in mind at the moment?

Senator VANDENBERG. I mean in which the employer with a good employment record has a more favorable charge against him than an employer with a poor employment record. I think it is the so-called Wisconsin idea.

Mr. LEWIS. I rather think that those equations would run right in on the same basis, except to what modified degree it might be profitable. I think one of the great essentials in giving attention to our industrial problems is to maintain some degree of parity as between producers in the same industry throughout the country, and I think our recent commission that has studied conditions in Great Britain stressed the tendency there to make industry or trade agreements so as to not impose undue burdens on sections of the industry, or units of the industry, and I think any tendency toward legislation that gives immunity or special privileges to individual corporations or individual producers would inevitably result in the end in disarranging the whole basis of competitive production and sales.

Senator HERRING. You said, Mr. Lewis, that, of course, profits could not be shared unless there were profits?

Mr. LEWIS. Yes.

Senator HERRING. That statement has been made several times. You also questioned, from your experience whether or not labor would be satisfied to wait for the profit. That it would prefer to have the profit each week in the pay envelope. We have had quite a number of witnesses, as you know, employing from 450 men to 50,000 men, and they have testified that they are completely convinced that their profit-sharing plan not only is acceptable to their employees but it has resulted in increased efficiency and increased loyalty, and in turn that has helped to bring about the profits to be shared.

Mr. LEWIS. Well, perhaps that may be their individual experience. I think it hardly runs to industries, or hardly to a sufficient number of any producing units in any one industry to be of compelling logic. There are a great many other elements that enter into this, I think.

We have thousands and thousands of corporations in this country which are organized as operating concerns and designed to show no profit. In the coal industry, for instance, one of our large industries, we have thousands of corporations that have been organized by the same people who own the land and who own the coal rights, and they function as operating companies, and they are designed always to show either a loss or no profit, while the holding companies levy charges and royalties against the operating companies, which eats up its substance as it makes it, so the coal company can always show that it is in a terrible financial condition.

I think we would find too many subterfuges on the part of certain corporations if we got into the realm of giving preferred consideration to companies which, voluntarily or otherwise, institute profit-sharing plans. And then there are profit-sharing plans and profit-sharing plans. Some of them only apply to the executives. I would not have any difficulty in identifying some of the corporations, or some of the individuals. I do not think the Senators would think it is necessary at the moment, but we have had a great number of these profit-sharing plans that only apply to the major executives of the corporations and not, of necessity, at all to the employees, and in many instances where they do apply to the employees they are insignificant and, relatively speaking, of unimportance.

Senator HERRING. I do not recall that we have had anyone before us who has testified as to that situation in his plant. We would like to get the names of some of those, at your convenience, if you will do that.

Mr. LEWIS. Thank you.

Senator VANDENBERG. Mr. Lewis, you spoke about the average employee's objection to anything that was paternalistic, in respect to these factors of employee relationships, and I can quite understand that feeling. I was wondering if you would carry that criticism down to pension plans and health plans?

Mr. LEWIS. On the part of government?

Senator VANDENBERG. No; on the part of the employer.

Mr. LEWIS. I think that very largely is true; and yet, in their unorganized condition in many industries and many plants, the workers have no alternative than to accept those arrangements. Some of them are meritorious, some of them are a distinct contribution. They are probably met out of the resources of a very successful company, and the executives of those companies oftentimes want to make a real contribution, if they can; and yet, do you see, Senator, that there is no security about those plans as far as the individual is concerned? He has nothing to do with the management—the individual employee. He may work 20 years for the company; the best part of his life has gone into the service of that corporation; he is looking forward to a participation in their pension plan, which, however, is a purely voluntary proposition; and if, through mismanagement or through a world crisis or domestic confusion and all of the other things, that company is unable to carry through, the man's 20-year equity in that pension plan is lost. There have been numerous such instances. He may have paid his part through the years, a participating part, through monthly contributions in support of the plan, the company contributing so much and the employee so much, but his only guaranty for safety in the future and for a right to live in his old age depends on the management of that corporation and the policies that control it. There is no security there as far as security is concerned, and when things get bad the minds of those employees are constantly filled with fear and apprehension as to what is going to happen with their pension plan. That is true of the greatest corporations.

Since 1929 many of our major enterprises have had periods when things looked very dark for them. Their pension plans, sick plans, hospital plans, and anything else, in many instances, went by the board. Others were able to pull through, but not without causing considerable apprehension among the men who contributed to it.

Senator HERRING. You believe in order to have real security it must be a Government plan?

Mr. LEWIS. I do not know anything else that would guarantee security to the man who works for a living, because our corporate structure is a fearful and wonderful thing. I could deliver a monologue on that, but I will not; but the average individual who works in one of these plants cannot follow the complexities and intricacies of the corporate set-up, the corporate structure, the relationships of holding companies, operating companies, service charges, bonuses and salaried executives, and all these sort of things. It is a realm he is not permitted to enter. He cannot feel secure about what its executives will do at the next board meeting or what the stockholders will do at the annual meeting, providing some one group gets control of the proxies and are able to dominate the situation. He is merely a pawn. As far as security is concerned, he only hopes. That is one of the principal things in the mind of the average man with a family—is what shape he is going to be in tomorrow, and next month, and next year, and what the situation will be if anything happens. That is one of the reasons why we see great masses of the population supporting these various plans to attain security, which may or may not be practical, but the thing is there; it is in their minds. These workers want participation in the natural bounties of our country, in the increased productivity, the increased productve efficency, of the country.

As far as efficiency is concerned, that is one of the things that we are suffering from right now. Our workmen are the most efficient in the world. Our engineers, our management and supervisors in industry, our chemists and technicians, from the industrial standpoint, are the most efficient that the world has ever seen.

In our mining industry our miners turn out every day five times as much coal per man per day as is turned out in Great Britain. You can take almost every industry and compare its productive facilities with every great country and find our efficiency per man per day in industry is the greatest in the world, many times exceeding other countries, and constantly increasing day by day as our scientists, technicians, new formulas, new methods, new machines, greater utilization of power, and faster tempo of operation have been able to do it. So we are suffering from efficiency, because our industrial plants are producing so much in goods that the country cannot sell it or consume it, and the rest of the world will not take it. So one of our greatest problems today is as to whether these Americans are going to have a job in this country and a participation in the work that remains in this country. If we become so superlatively clever and brilliant, as we are in the realm of material sciences and their application to the modern production methods, we are abolishing work as such, and gradually decreasing the number of man-days of work per year that is available in our country to house, feed, transport, amuse, medically attend, and clothe the population, and there is only one answer, and that is to give the adult population, able and willing to work, a right to part of the work that remains. That is our outstanding question today.

If we had a perfect system of profit sharing, for instance, in our modern industries, not the miscellaneous or the model industries, for instance, just taking a basic industry, that would not enable the man who is going to be displaced next month because some brilliant chemist evolved a new formula, or some exceptionally able engineer outlined new methods of production and one-third of the men in that industry or that plant are laid off or dispossessed and separated from that industry, the profit-sharing thing would not help him at all.

We are modernizing our industry today, and while quantity production is coming back we are not reemploying those who have been deprived of employment in a like ratio, and we will not. It is a very serious question, and I think the major question that confronts the Senators and the rest of the country, in which we all have an obligation to make a contribution. Substantially speaking, we have got almost the same number of unemployed right now as we had in 1932 and 1933. After all these years of experimentation we have made no contribution toward that. We have got so many million on relief and so many million on public works. Their dependents make a great cross-section of America. They are practically displaced from consideration of participation in our modern internal economy. So until we can first arrange to stabilize our economy to the point where all Americans have a right to participate, I do not think we can work out a just or a logical or meritorious or stable system of sharing the profits, when we are not even sure there are going to be any profits. As a matter of fact most of our major industries are running in reverse, and we cannot look forward to any profits. That is true of the railroads, that is true of the shipping industry, that is true of the mining industry, that is true of our major enterprises. We have some exceptional enterprises that have not been hard hit yet, but the question of profits in many industries is just out of the way. There are not going to be any, that is, in the reasonable future, until we can reorganize and revamp our method, come to new understandings and work these problems out.

The railroads are employing 1,300,000 men less than they did in 1920. That is just one institution. They are not making any money as the result of dispossessing a great number of men, and those 1,300,000 men are on relief, or something else has happened to them.

Practically all our modern industries are modernizing and continuing to displace. Our economists tell us industries spring up and absorb these men displaced by modern methods in other industries. The answer is it does not happen that way. The record is it is not true. In the Pittsburgh industrial area, which is one of our great workshops, there has not been a new industry start in 15 years; and if a new industry did start, it would not take a man displaced through improvement in efficiency production in other industries; they would take the man with good muscular and nervous reactions, with great aptitude, the men who are young men who come and stand there in line waiting for employment as against the man who has been stiffened up for 10 or 15 years in the steel industry, in the coal industry, in the glass industry, or what not. They are displacing these people.

Take our aircraft industry, one of our new industries that is flourishing, comparatively modern. It is impossible for a man who has been displaced in the steel industry, coal industry, shoe industry, glass industry, to get a job in the aircraft industry. They want a young man of aptitude, susceptible of being trained along the special lines required in that industry. We have 600,000 men and women every year available for entrance into industrial enterprises that are not picked up.

I appreciate the Senators are making an earnest effort to find the equities in this situation, and it is well to consider how there can be a greater sharing, a greater participation in an improved industrial efficiency in the natural boundaries of the Nation, but my own judgment is that we can scarcely do it by merely encouraging, well, the many different brands of profit sharing that might be projected by employers in this, that, and other industries.

Senator HERRING. We recognize, of course, that we cannot solve all the problems that you have given to us. We thought we might have one bite at the apple, though, to get a start. A suggestion was made that a corporation create a retirement fund through an irrevocable trust; and if that was invested in Government bonds, that might give security through a pension fund.

Mr. LEWIS. I suppose there could be a plan devised, Senator, that would tie a corporation squarely to the thing, but there would be so many corporations that could not get a trust company to trust them that it would offer some difficulties.

Senator HERRING. Of course, if it all rests upon the good faith of the employer, no system will work.

Mr. LEWIS. I mean in a financial way. I did not mean trust them as far as the work is concerned, but financially, because many of them would not be financially able to institute the plan that required indemnification or security.

Senator HERRING. If you have any other suggestions or ideas, we would be delighted to have those.

Mr. LEWIS. I do not know that anything pertinent comes to me. I ask the forbearance of the Senators for wandering so far afield in my testimony here, except that the set-up is all interlinked, interwoven.

Senator HERRING. It is all interesting to us.

Mr. LEWIS. Thank you.

Senator VANDENBERG. Have you any comment, Mr. Lewis, on the so-called Westinghouse plan, which is supposed to permit wages to follow the production and profitable operation of the corporation?

Mr. LEWIS. Yes, sir; generally familiar with that, Senator, but, by and large, our thought is this, that if labor agrees to a fluctuating or flexible wage it is tied to some factor of control, whatever it may be, whether it is profits, whether it is volume, or whatever it may be, that presupposes that the wage at the moment is an adequate wage and a proper wage, and I have held that that sort of an arrangement will wreck our internal economy and prevent America and American industry from expanding, from developing, will prevent the building up of a necessary buying power in the country sufficient to absorb our production, our constantly increasing production. We must increase the annual income of Americans, we must increase our buying power if we are going to keep these plants of ours going, and to pin the wage structure to any sort of a factor involved in an industry or plant means that the worker will have no more than a fixed participation at any time, that he will continue to occupy the same kind of house, wear the same kind of clothes, give about the same kind of education to his children, and suffer to the same degree for lack of medical attention as he does today. So the workers are not just inclined to accept that status, and we do not think it is sound economics, because every producer of every commodity in our country looks forward to expanding his model, expanding his production, expanding his sales, and expanding his profits, if possible.

Senator VANDENBERG. To what extent do you think the annual wage might be practical?

Mr. LEWIS. The annual wage is a very desirable objective to obtain, but the circumstances affecting the average employer of labor in competition with others in his industry are such that it is impossible for him to guarantee the payment of so much a year to his employees, because circumstances may result in him not being able to operate his plant the requisite number of days. If it could be worked out, it would probably have many virtues, and the effect of it would be, well, valuable in many ways, but I do not see how an employer, whether he is in the contracting business, manufacturing business, mining business, or what not, can undertake to pay so much a year except as he has a rather constant assurance of production. That is the first requisite, Senator, he would have to have that constant assurance.

The idle time charge in America is a tremendous one as it affects the cost of industry. It is in all our major industries. That is the plant equipment, the major upkeep, supervision, taxes, insurance, all of those things. They create a fixed charge on the industry, and the fewer number of days the plant operates the lesser output there is to distribute those fixed charges over an annual wage. If you had an annual wage I suppose the corporation would not go to 77B but something worse.

Senator VANDENBERG. 77A, probably.

Senator HERRING. I think that is all. We appreciate very much, Mr. Lewis, for the contribution you have made.

Mr. LEWIS. Thank you indeed.

Senator HERRING. Mr. Moss.

STATEMENT OF F. J. MOSS, PRESIDENT, AMERICAN SASH & DOOR CO., KANSAS CITY, MO.—Continued

Senator HERRING. Go right ahead, Mr. Moss. You wanted to add some remarks.

Mr. MOSS. Before making any remarks, I wish to ask if it is in keeping for me to comment on any suggestion that has been made? I do not want to be out of order or discourteous, or anything of that kind.

Senator HERRING. Certainly. There is no limit to your comments. You may give us anything that would be helpful.

Mr. MOSS. Well, one of the witnesses this morning suggested that all of the profit in the profit-sharing plan should go to labor. I am wondering where the profit-sharing feature comes in on that. It seems to me under a plan of that kind it would be profit-taking by one factor and no profit sharing, and in my judgment would fail, because I do not believe it would attract capital under any circumstances.

Now it has been suggested, and it has been said to me on previous occasions by labor representatives, that they want their profit in the pay envelope Friday night. Of course they do. Capital wants its profit every week, or every month. Of course they do, but that cannot be done. There is not a profit until the profit is made, and that is not usually determined until the end of the fiscal year. So that there must be an acceptance of conditions that cannot be changed, and that is one of them.

Now the paternalistic feature has been commented upon, and I am in full accord with what has been said, namely, that labor objects to that. Now in a proper profit-sharing plan there is no paternalistic feature, because labor gets that which it is entitled to, not as a gift but as its right. There is no paternalistic feature to it at all, and there should not be, because it is demoralizing.

A retirement fund is desirable from one standpoint, but to my mind is wholly impracticable, because of the difference in the conditions of the employees. Furthermore, there are hundreds of thousands of small institutions who cannot proceed on that theory of setting up a retirement fund, and it would be no good if they did. They would not be responsible. It is our position that labor should have what it is entitled to, and have it to do with as they see fit.

The annual wage is another impractical proposition, because that depends upon conditions, and the natural procedure is that the wages are more or less affected according to the demand. The merchant will reduce prices in order to stimulate demand. That is logical, that is sound, it is both helpful to labor and helpful to capital.

Now any profit-sharing plan that is sound must be on the same basis as a group of people entering into a corporation and buying stock. We should say to labor, "You are on identically the same basis as the stockholder, except you do not draw interest on the money that you do not keep in the business." That is the only difference in the sound profit-sharing plan. Capital should have interest paid on its capital, because it remains permanently in the business. Labor draws its wage out each week, and of course would not expect interest, but after that is done labor shares in its profits exactly as capital does, in proportion that labor enters into the cost of the product.

Now that is the final word on what I have to say on the profit-sharing plan.

Senator HERRING. Thank you, Mr. Moss.

Tomorrow morning we will have Prof. Willford I. King, professor of economics, New York University, and Mr. A. L. Marsh, president, Hoskins Manufacturing Co., Detroit, Mich. In the afternoon we will have Mr. Frank Gannett, publisher, Gannett Newspapers, Rochester, N. Y.; Mr. Lammot du Pont, president, E. I. du Pont de Nemours & Co., Wilmington, Del.; and Hon. John D. Moore, commissioner, New York State Labor Board, New York. We will recess until 10 o'clock tomorrow morning.

(Whereupon, at the hour of 2:45 p. m., a recess was taken until 10 a. m., of the following day.)

SURVEY OF EXPERIENCES IN PROFIT SHARING AND POSSIBILITIES OF INCENTIVE TAXATION

THURSDAY, DECEMBER 1, 1938

UNITED STATES SENATE,
SUBCOMMITTEE OF THE COMMITTEE ON FINANCE,
Washington, D. C.

The committee met, pursuant to adjournment, at 10 a. m. in room 312, Senate Office Building, Senator Clyde L. Herring, presiding.

Present: Senators Clyde L. Herring (chairman), and Arthur H. Vandenberg.

Senator HERRING. Mr. Frank Gannett of the Gannett Co., publisher of the Gannett Newspapers, Rochester, N. Y.

STATEMENT BY FRANK GANNETT, PUBLISHER, GANNETT NEWSPAPERS, ROCHESTER, N. Y.

Senator HERRING. You have a statement, I think, Mr. Gannett, have you?

Mr. GANNETT. Yes, Senator. If I could read this, then I would be glad to have you question me afterward. I think that would probably expedite it.

Senator HERRING. You may go ahead.

Mr. GANNETT. I am glad to appear before this committee because for many years I have had a deep interest in profit sharing. I should be glad to feel that my suggestion made 2 years ago that the Congress should promote profit sharing in America may have had something to do with the creation of this committee. I am hopeful that the findings of this committee will lead to some definite legislation on this subject, but even if nothing in the way of legislation came of this investigation which, of course, is unlikely, it would still be well worthwhile because the publicity given has stimulated throughout the country, thinking about profit sharing.

This committee has heard a large number of witnesses and I have read assiduously all the reports that the newspapers have carried. I know that there has been a difference of opinion expressed by the various witnesses, and I know that there has not been full agreement on many debatable points.

At the risk of repeating some of the testimony that has been given, I should like to read a few paragraphs from an address that I made in Buffalo about 2 years ago before the National Association of Secretaries of Chambers of Commerce, which seem to me to be pertinent to this inquiry. At that time I said in part:

Everyone wants to see purchasing power increased. If the people could buy the things they need and want, our present production capacity would not be adequate. As the Brookings Institution research proves, we have not been overproducing, even with all our machines and manufacturing plants. Our ills are due to underconsumption, lack of buying power. Lack of consuming power causes curtailment of production. This in turn causes more idleness and makes the situation worse. Low production means high prices, and this again brings more disaster.

What we must do then, to solve our major problem, is to increase purchasing power, make it possible for our people to share in the abundance of everything that we can produce. We should not have, as we have today, restrictions on the production of goods, but instead we should increase our wealth so there will be more wealth to share.

Our Government makes the great mistake of believing that taxing wealth or the production of wealth accomplishes this purpose. Nothing of the sort. Taxes do not increase purchasing power. They destroy it. They put a burden on business and make production more costly. Taxation provides money for the Government to spend, often, of course, for desirable services, but many times it is squandered. Taxes burden everybody and lessen the citizen's share in the wealth a nation produces.

One trouble with our present economic system which causes many to condemn it is the feeling that too large a share of the wealth produced goes to capital and not enough to the worker and consumer.

We must have, first of all, a real partnership between capital and labor. There is often much lip service to this idea, but not often enough has it actually been in effect.

In the last 2 years we have had an epidemic of strikes, some of them serious. Not only has enormous financial loss resulted, but something equally disturbing has been the development of bitter class feeling and prejudices as if the two groups represented conflicting interests. Of course labor and capital should be working together, not against each other.

It is my belief that the bitterness that has developed between capital and labor is due largely to the feeling on the part of labor, promoted by men in high places, that it is not getting its just share of the rewards that come from production of wealth. We all must recognize that we cannot produce anything without capital. The farmer's plow, hoe, and horses are his capital. The tools of the mechanic are his capital. The machines in the factory are capital. Labor, of course, can do nothing without this capital. On the other hand, all of these tools, farms, and manufacturing plants would be idle and nonproductive but for labor. It is absurd to think that either one can do without the other, or that one should have all consideration and the other no consideration in any adjustment of the rewards of production.

Most of us—perhaps not all—will agree that capital, after fair wages have been paid, should have the next reward and a fair reward. Every laborer should be willing to give something for the use of tools that will make his work productive. Every laborer must recognize how necessary it is to have the implements which capital alone can provide. The trouble arises when capital asks, and gets, a larger return than labor thinks is fair. Many of our labor troubles are due to this feeling on the part of the workers that capital is receiving more than a fair return.

Since the development of corporations and since industry has become impersonal, we have an entirely different situation from what prevailed when capital was provided by an individual employer with a personal interest in the man who worked for him and with him. A corporation has been described as "an entity that is soulless and heartless." We all know that unfortunately too often this is quite true; it accounts for some of the feeling on the part of labor toward employer when that employer is a corporation.

With the development of the corporation came an issuance of bonds, preferred stocks, and common stock. Bonds yield a definite fixed income and the same is true of most preferred stocks. The return on the common stock, however, is indefinite and variable. The aim of the management of our corporations generally has been to provide, first, a definite return on bonds and preferred stock as required, and after that to give as large a return as possible to the common-stock holder. We all must concede that the interest of the holder of common stock has been one of the first considerations of the management, because the management of the concern usually rests with the holders of common stock.

As corporations became prosperous there developed an inflation of common stock. There were split-ups of shares of common stock which had the effect of concealing the actual primary investment in the corporation, its real capital, and thus concealing the actual return on the investment represented by the common stock. Split-ups of common stock have brought about tremendous inflations in the capitalizations of our large corporations, because the value of the stock has been based on earnings rather than on actual investment.

In its intense desire to increase the yield on the common stock of corporations the management unfortunately has, in my opinion, too frequently taken the wrong attitude toward labor. If the management of our corporations had been as eager to increase the earnings of labor as it has been to increase the earnings on the common stock, we would not today have this feeling against capital on the part of labor.

Although the idea did not originate with me, I came to believe years ago that our perplexing labor problem could be solved by the adoption of the following policy:

First: Give capital a fixed and fair return, varying, of course, with the risks involved. This return always should be high enough to coax capital into business ventures, to induce investment. In some cases 4 percent may be a fair return, in others 10 percent or 15 percent or even much higher might be necessary. The reward must be high enough to justify the risks. This return in some cases could be represented by the dividends on the preferred stock or the interest on the bonds.

Second: After capital has received its fair return, then the profits of a corporation would be shared with: (a) The workers; (b) The consumers; (c) A limited bonus to management.

The worker would get his share of the profits through a wage dividend. The consumer would share in these profits through lower prices or a better product. Management's dividend would differ little from that to labor except it would be, in addition to a reward, an incentive for promoting efficiency, economy, and wise operation of the business.

In some lines of business where the purchasing price of a commodity is relatively large, like an automobile, piano, or radio, the buyer or consumer might be given a certificate of participation in the profits. In other lines the consumer's benefit from this plan would come in a frequent readjustment of price schedules.

First of all, however, participation in the surplus profits, that is profits after capital has had its fair reward, should go to the workers. The management could determine from time to time how much this participation safely and fairly should be.

Of course, the future of the business enterprise would have to be protected. Reserves would have to be built up for expansion, obsolescence, and replacement. Under the undistributed profits tax (especially so before it was amended in the last session) companies are penalized for not distributing all the profits to stockholders, regardless of the future needs of the company. This plan has weakened many concerns, put them out of business and thus lessened employment. The management of a corporation can tell better than anyone else how much of the profits should be distributed to insure continuous employment for the worker and promote the business. But, in any event, the worker should have his share in the profits as I have outlined.

Instead of taxing companies for not distributing all their profits to stockholders, I would give additional tax relief, that is still more deduction for the wage dividend, to those companies that distributed profits to their employees. It would be easy to devise an incentive of this sort which would encourage companies to give workers a wage dividend, thus increasing their purchasing power.

For several years now I have been preparing to put in operation this policy in my own business and at last have been able to make a start. I have set up a foundation which will ultimately control all the common stock of the Gannett Co. Whatever comes into the treasury of the foundation will go to charitable, philanthropic, and educational purposes. This being the case, there will be no incentive for the directors of the foundation, who will also make up the board of directors of the company, to increase the dividends on the common stock beyond a reasonable, safe, sound, and modest figure.

At the close of the year's business in 1936, after careful consideration of the profits which our company made for the year, the board of directors decided on a dividend for the worker. With the dividend I sent out a note saying that this was not a bonus, a gift, or a Christmas present, but it was the worker's share in the profits of the company as we had been able to compute them.

The reaction of the employees to this arrangement has been marked. The workers know that I am sincere in my desire to give them the highest possible reward for their services. They see that under this plan they are actually sharing in the earnings, the same as does capital.

It is true that other corporations have provided stock dividends and bonuses to employees, but the employees too often are not convinced that this is their just share or that it is anything more than an attempt to pacify their demands for a larger share in the earnings.

Today I might add to this that I feel that it is necessary, of course, in any profit-sharing plan that the workers be taken into confidence and that they be given a full report of the company's business so that they may understand exactly how they have participated in the profits. Of course, all concerns that have securities listed on the New York Stock Exchange already furnish full information about the conduct of the business.

And, here I might say incidentally that it was only a few years ago when businessmen thought it was nobody's business how they conducted their affairs, and it is reported that when Theodore Roosevelt first urged fuller reports on corporation earnings, one of the great financiers indignantly said "He wants us to walk around with glass pockets"; yet, in a couple of decades what then was resisted, is today the accepted practice. In my judgment the corporation in the future may recognize a broader responsibility—to include not only stockholders, but labor and the consuming public. In the annual report under such circumstances, the number of days of employment, the regularity of employment and the income per worker would be reported in addition to the profits for stockholders. At the same time the corporation might publish or have available records showing its relation to the consuming public. In reality, the responsibility of a corporation runs in three directions—to the stockholders, to its employees and to its consumers. This is being recognized by the leading corporations in America to a degree unequalled elsewhere in the world.

Of course, we all know there are many corporations sincerely interested in the welfare of their workers, and in which the management is trying to give labor the fullest possible return, but these efforts and intentions are in vain if the worker is skeptical. There must be absolute confidence on the part of the worker that he is getting his just return. Once he feels this is true, he will understand that he is working, not for some intangible, theoretical entity called the "corporation," or "company," but for himself as well. Give the worker this assurance, and his attitude toward capital will change immediately.

If most of our corporations would work out such a policy as I have described, we would have few strikes, for the worker would understand that to tie up the production of a factory would be to lessen his own reward.

A policy of this kind, I am convinced, would mean the dawn of a new day for America. At last we would get full cooperation between labor and capital; class feeling would subside; the worker, through getting the maximum return for his toil, would have his purchasing power increased; this increased consumption of every product that would follow would bring about more employment; and this increase in employment again would further enlarge purchasing power. All of this increase would bring about a higher standard of living, and the country would prosper as never before.

The treasurer of our company has already reported in full to your director, Mr. Donald Despain, how the Gannett Co. has carried out my ideas on direct profit-sharing. In brief, we reported this:

In 1936, when we started profit-sharing, it was done on the basis of giving each employee with 5 years' service or more, 2 weeks' additional salary; employees with 3 years' service, but less than 5, 1½ weeks' salary; employees with 6 months' service, but under 3 years, 1 week's salary.

In 1937, when we had a little more time to study this problem, we set aside 10 percent of the profits of each company after all charges, to be divided among the employees of that company on a pro rata share of their earnings for the previous 5 years. In order to participate, an employee had to have at least 1 year's service. In most cases this profit-sharing amounted to a little over 2 weeks' salary for a 5-year employee, or a little over 1 percent of his earnings for the previous 5 years (or, 5 percent of his average annual earnings).

We have not made any commitment to our employees that the profit-sharing will be continued, but in all probability the same amount will be set aside from this years' profit, and we hope to make it a permanent plan. There is a possibility also that the amount of profits set aside may be increased.

I hope that will be the case.

As a matter of fact, the amount of wage dividends distributed last year to the employees was almost as large as the total dividends on the common stock representing the equity ownership of our 18 newspapers.

My experience was that this division of profits was highly satisfactory and received with great appreciation and gratitude. Without the slightest doubt, it developed a deeper interest on the part of the employee in the company's affairs and gave to the employees a feeling that they had a real interest in and a responsibility for the success of the company.

I realize that my suggestion that this profit sharing be promoted by incentive legislation has been debated before this committee. My general idea is that there should be provided further tax relief than is now possible for those concerns that share their profits with their employees. Of course, I realize that under existing laws wage dividends or profit-sharing allocations can be put in as an operating expense and thus be deductible from income-tax levies. In my opinion, it would be a simple matter to provide that there be a further reduction of some percentage of the amount so allocated in wage dividends. In addition, any corporation setting aside a portion of its earnings as a buffer for periods of low employment, pension funds, unemployment insurance, and similar sums for the benefit of its employees should have all such sums exempted from taxation.

Some will say that they are opposed to tax incentives on principle and that the Government should use its taxing power solely for raising revenue. However, we have gone a long way in providing tax incentives. The protective tariff was an incentive tax levied on all the people in order to stimulate manufacturing enterprises thus to benefit certain corporations or business concerns. In our tax plan today we are allowed to deduct on our income tax all sums paid for charitable, philanthropic, or educational purposes. This, of course, is an incentive tax, as this provision was enacted in order to stimulate the distribution of money for charitable purposes. All of our subsidies are incentive taxes in one form or another. The undistributed profits tax, to which I personally objected strenuously, was an outstanding example of threatening taxes for those corporations who did not distribute their earnings to their stockholders. If this tax had exempted reserves and sums spent for expansion, plant extension, and so forth, and stimulated distribution of earnings to workers, rather than to stockholders alone, I might have endorsed it.

I might interject here that I appeared before the Ways and Means Committee of the House in the last session and urged modification of the undistributed profits tax along these lines, and also urged that profit sharing with employees be definitely stimulated by the Government.

Some of those who appeared before this committee, men for whom I have great respect, representing labor, have apparently the erroneous impression that establishing profit-sharing might affect the wage level. I doubt if any of us have any such conception of the idea. Wage scales are pretty definitely established in all of our industries. I hope that in a short time we shall adopt that part of the British labor relations system which provides for an organization of employers as well as employees, who voluntarily negotiate and establish a wage scale and working conditions throughout the industry concerned. My idea of profit sharing would apply, of course, only to profits made after fair wages have been paid, and I can't conceive how sharing in profits would affect in any way the current wage scales.

Labor must recognize that over every business there is an element of uncertainty. Wages cannot be set so high as to put business into the red, but when with a wage scale which may be as high as the industry can bear with safety, conditions are favorable and profits accumulate, workers through profit sharing would get an additional income that they could not otherwise have.

It has also been suggested that labor have a part in the management of business. My long experience has convinced me that one of the rarest things in the world is ability to manage any business efficiently and successfully. That's why high wages are paid to successful executives. I know of cases where two plants of similar capacity have operated in the same city, producing a like product, with one concern most successful and the other a failure due solely to the difference in the management.

The American corporation is about 100 years old. Under our corporate system more new development in products and processes of production have taken place than in all the thousands of years before. We should go slow before tampering or changing this machinery which has worked with such effectiveness. I doubt whether banker management, politician management, or labor management would produce anything comparable in its results for the consumer, for labor, or for the country as a whole.

Senator VANDENBERG. That is a thoroughly splendid and constructive statement, Mr. Gannett.

Mr. GANNETT. Thank you, sir.

Senator VANDENBERG. I emphatically agree with your conclusion. We have tried a little banker management, we have tried a lot of political management, and we have tried a little labor management. If we should return to business management we would be better off.

Mr. GANNETT. I am glad you agree with me.

Senator VANDENBERG. I judge from the whole tenor of your statement that you feel that the basis of this whole employer-employee relationship is the necessity for absolute candor.

Mr. GANNETT. Candor?

Senator VANDENBERG. Yes.

Mr. GANNETT. Oh, yes; I think that is absolutely necessary.

Senator VANDENBERG. And the lack of candor not only is probably responsible, in your opinion, for some of the industrial frictions we have had, but it is also responsible, is it not, for creating a situation which permits the demagogue to misrepresent the relationships between labor and capital?

Mr. GANNETT. Absolutely.

Senator VANDENBERG. It would be then a matter of enlightened selfishness if capital would be more frank with its own people?

Mr. GANNETT. I think business has made a great mistake in not being frank. It takes time to develop that.

Senator VANDENBERG. I want to ask one thing in detail, if you refer back to your statement at page 7.

Mr. GANNETT. Yes.

Senator VANDENBERG. (Reads:)

In 1937, when we had a little more time to study this problem, we set aside 10 percent of the profits of each company after all charges.

I want to inquire about the phrase "after all charges." Did that include anything for reserves?

Mr. GANNETT. No; that is for depreciation, obsolescence, etc. We of course computed that we should set aside a reserve, and after doing that we thought 10 percent was a safe percentage to give to the employee.

Senator VANDENBERG. Well, for instance, would there be an allocation to surplus before the 10 percent is deducted?

Mr. GANNETT. No; there was no reserve for surplus, but there was a reserve for needs of the company, which we contributed, what we thought we would have to have in the ensuing years for expansion, development, replacement, etc.

Senator VANDENBERG. The fundamental question, without going into too much detail, that that raised in my mind was this, as to what you consider to be fair charges in behalf of capital before the time arrived to start sharing profits with labor.

Mr. GANNETT. Well, before we start sharing with labor, I would say a charge for depreciation—well, that pretty near covers it. I think after you get that you get your net profits. How much we should distribute to the workers and to the stockholders resulted from a consideration of how much of that profit we should set aside for the needs of the company, and as a safety margin for operation during the following year, but in answering your question directly I should say that the sum from which we computed the employees' share was based on the net earnings of the company, as would be shown in an income-tax return to the Government, which would be after depreciation. It would not take in any plant expansion. That was something we had to consider afterward.

Senator VANDENBERG. I take it that you completely concur in the general theory of incentive taxation?

Mr. GANNETT. Yes, I do. I think it would be a great thing. I know you have had opposition to it, and arguments against it. The tax relief a profit-sharing corporation would get would not be a burden on any other corporation. When you take the full budget of the expense of Government this little relief would be an infinitesimal percentage of the taxation on corporations. I do not think any of us would feel it, or know about it. We have gone a long ways, as I say, in incentive taxation, and why not?

Senator VANDENBERG. I think you make a very interesting point when you suggest that the undistributed-profits tax was in reality an incentive for distribution to stockholders.

Mr. GANNETT. Exactly. It was a great incentive, in fact, it was almost compulsory.

Senator HERRING. You have about 2,300 employees, do you not, Mr. Gannett?

Mr. GANNETT. Yes; 2,323.

Senator HERRING. Many of them are in organized labor groups?

Mr. GANNETT. Yes; practically all except the editorial rooms and business offices.

Senator HERRING. We have had quite a bit of testimony as to the need for negotiating this profit sharing, so that the employee has full confidence that he is getting a fair division. Do you negotiate in any way with your employees or is that set arbitrarily by the management?

Mr. GANNETT. Yes; it is arbitrarily. Of course, our financial report is submitted to the stock exchange and they can see that. We publish it in the house organ, so they can all see what the profits of the concern are. You have got to develop full confidence, of course, that you are on the square with them, and that is not an easy thing to do, always, with a large corporation.

Senator HERRING. Collective bargaining did not have any place in this profit-sharing plan?

Mr. GANNETT. No.

Senator HERRING. That has been suggested here as being necessary for a fair profit-sharing plan.

Mr. GANNETT. Well, I at one time in my life thought we should give labor representation on the board of directors, and I took it up with several labor leaders. They said:

> There is no need of our going on the board of directors. We do not know anything about the finances, the financial reports; it would not mean anything to us at all.

I should say that some outstanding labor leaders expressed that opinion to me. I have discarded the idea. I did not think anything would be accomplished, except possibly it would be a gesture, and anyone who has attended an ordinary directors' meeting knows they do not go into details; that is left to management.

The other idea would be to have representation on a management council, which is an entirely different thing, but the management must be frank with the employees and gain their complete confidence. They know we were giving them all we could last year, and they know this year we will give them all that we can.

Senator VANDENBERG. When you distribute wage dividends almost to an extent equivalent to your distribution of common stock dividends I should think it would be reasonably impressive.

Mr. GANNETT. Yes; they know that as a fact.

Senator VANDENBERG. You say that your experience, as the result, was that the plan was received with general appreciation and gratitude. Would that include members of labor unions?

Mr. GANNETT. Oh, yes.

Senator VANDENBERG. In other words, the local labor union reaction that you have experienced in connection with your type of profit sharing would not indicate any of these skepticisms or criticisms that we have been told about.

Mr. GANNETT. In many cases the workers in one department would all sign a letter thanking me for what had been done, showing the appreciation; and that has come from union workers. Men in the press room, composing room, and so forth, in many cases did that, and I have had scores of individual letters from workers saying that this dividend meant so much to them, that it made it possible for them to do something that otherwise they could not have done for their families. Some of them were very touching.

Senator HERRING. With 18 plants in 5 different States, and organized labor among your employees, you must have been in different places where they were having labor trouble, and you never had any in this time?

Mr. GANNETT. I have never had any labor trouble yet. In all my experience in the publishing business I had one strike, which I was not responsible for. It was a strike caused by the other paper in the town, and it occurred just as I had purchased the paper in the town. That was in Albany, a costly strike, which was finally settled. We have never had any real labor trouble. We have had negotiations, yes, all the time, constantly. As Senator Vandenberg knows, there are questions of wage scale in the printing industry, but these negotiations are friendly and the management tries to derive a scale of wages and working conditions that will make the company prosper. If we do not prosper, then there might not be any employment for anyone.

Senator HERRING. You think your policy, Mr. Gannett, has had quite a good deal to do with not having labor troubles?

Mr. GANNETT. I think it has.

Senator VANDENBERG. You think it increases efficiency?

Mr. GANNETT. Oh, yes. Of course that was not the purpose of it, but I know the men are working for the company and they know if the company prospers they will prosper.

I might say, incidentally, I went to England this summer to study the British labor relations system, and in talking to some of the workers there in some of the plants, they said:

> We want the company to prosper for we know if it does prosper we will get a good wage.

That is a feeling I found in England which should prevail more extensively in America. I was very much impressed by it. I know from many, many acts on the part of the employees that they are directly interested in the company, in its welfare, they are interested in the development of the company, and in business development. They offer suggestions here and there, which is a very healthy and wholesome spirit. It gives me a great deal of satisfaction to see it.

Senator HERRING. You believe that we should encourage efficiency. We had some testimony here yesterday that one of the troubles in this country is we are too efficient.

Mr. GANNETT. I cannot go along on that. If we become more efficient, if we produce more there will be more to divide; there will be more jobs if you keep up your wage scales and purchasing power, and efficiency is necessary, of course, to do that. Our company would be in the red if we did not have efficient methods of operating, efficient machinery, and the latest in everything. Efficiency makes our profits possible. I cannot go along with that other school of thought. Our profits are not insignificant, either.

Senator HERRING. I agree with Senator Vandenberg. This is a splendid contribution. We appreciate your being here, Mr. Gannett. If you have any other suggestions we would be glad to have them.

Mr. GANNETT. I appreciate your commendation. I am intensely interested, and I hope out of the committee will come some definite development.

Senator VANDENBERG. When you suggest a definite development out of the committee I am sure you do not mean that you would have us write a compulsory profit-sharing formula for America.

Mr. GANNETT. No, no. I should say I would be absolutely against compulsory legislation of any kind.

Senator HERRING. That would be a return to political government, would it not?

Mr. GANNETT. Oh, yes. That was the trouble with undistributed profits taxes; it was almost compulsory.

Senator VANDENBERG. I think that is the general trouble we are up against today.

Mr. GANNETT. Too much compulsory legislation.

Senator VANDENBERG. Yes.

Mr. GANNETT. That is what I found. The British labor relations system is all voluntary, the men take care of it themselves, the employer and employee. That is getting off the subject, but that is the spirit we must have here, more voluntary action and less compulsion.

Senator VANDENBERG. Senator Herring and I started out on this adventure with the solemn promise to each other that there would be no legislation on profit-sharing, all we would do would be to present the record for the information for the record and intelligent guidance of the American manufacturers to take advantage of.

Mr. GANNETT. I hope somebody does produce some legislation that will give us some incentive for it.

Senator VANDENBERG. I feel that with incentive taxation we may be able to develop specific proposals, and personally I think we shall.

Mr. GANNETT. That is fine. It would be very gratifying. Last year in our company we had a profit of $1,075,000, and I think altogether we paid in taxes something like $700,000. If a portion of that could have gone to the employees it would be a different thing, but our total taxation was almost as much as our profits. When these figures were given to the men they were amazed at the amount of taxes the company paid. If we got relief from some of that taxation that would have meant in this case more wage dividends to them, and it would have been a considerable sum.

Senator VANDENBERG. Well, don't you think that incentive taxation can be developed far beyond the point of mere relief?

Mr. GANNETT. Oh, yes, more than relief; it should be made a real incentive.

Senator VANDENBERG. Yes. And the result of the operation might well be to so stimulate commerce and the buying power in America through reemployment and expansion that the net tax effect to the Government would be a far greater tax revenue?

Mr. GANNETT. Exactly.

Senator VANDENBERG. We would not lose money by it; we would make money by it?

Mr. GANNETT. Exactly. You would have more income taxes as the result of the increased business all along the line. Oh, yes, that is the direction to go in, instead of the opposite direction. Is that all?

Senator HERRING. Yes. Thank you very much.

Mr. GANNETT. I hope something will come of it.

Senator HERRING. Thank you. We will next hear from Prof. Willford I. King, professor of economics, New York University, New York City.

STATEMENT BY PROF. WILLFORD I. KING, PROFESSOR OF ECONOMICS, NEW YORK UNIVERSITY, NEW YORK, N. Y.

Professor KING. I understand that the inquiry here is concerning profit sharing. When we consider profit sharing the question is what aim we wish to accomplish; why we should have profit sharing. One object, of course, would be to encourage a more harmonious relationship between the employer and employee. That is highly desirable. Another aim would be to secure better earnings, higher income for the employees. That is also highly desirable. Plans would differ according to which one of these was the principal aim.

The difficulty of securing better relationships between the employers and the employees has been greatly enhanced recently by the attempt to outlaw, or to discourage, the union existing within one enterprise only. When unions of employees cover a wide field it obviously becomes more difficult for the employer to have harmonious relationships with his employees than when he is dealing with his own employees. The Bible says that no man can serve two masters, and in this case the employee, when he tries to serve two masters, namely, the employer and the labor union leader outside of his firm, naturally gets into difficulties. As long as we have laws tending to increase friction between employers and employees it is somewhat futile to favor profit sharing from the standpoint merely of promoting better relationships between the employer and employee. That would seem to leave, as the primary object of profit sharing which would have a clear field, that of securing a better income for the workers. I think that that can be accomplished also, and to secure better earnings for the stockholders as well. If we can do this we are benefiting all parties concerned.

If we were merely to share profits as they now exist, we could not go very far toward benefiting the workers of the country as a whole. In certain successful plants we might convey a good deal of benefit to the workers, but on the whole it would not help employees in general very much. For example, in 1935, the last year for which we have figures on corporations in the United States, we find that the total corporate net income, after taxes, was $4,430,000,000. That represented the income of corporations having net capital assets of $100,480,000,000. That is, all the corporations earned something less than 4½ percent on their net assets. 1935 was, of course, not a very prosperous year, neither was it a very bad year—probably, under present conditions, about an average year. That means that the corporations, on their net assets, were earning something less than 4½ percent. Out of that you could not take a very large sum to give to the wage earners in the hope of enlarging their earnings materially.

Senator VANDENBERG. Have you broken those figures down to indicate how many reporting corporations made no profit at all?

Professor KING. No; but the figures are right here. Would you like me to give them?

Senator VANDENBERG. Yes; I would like to have them. I knew them once, but they have escaped me.

Professor KING. In 1935, according to Statistics of Income, page 13, there were 164,231 returns that showed a net income. There were 312,882 returns that showed no net income. That is, roughly, twice as many corporations showed no net income as showed a net income. Now, obviously these corporations that showed no net income would not benefit their workers by sharing profits, and one of the difficulties with most profit-sharing plans that have been proposed in the past is that there is no way that the workers share the losses, they only share the profits.

Senator VANDENBERG. Of course what you say about the fact that those statistics indicate a sharp limitation upon the possibilities of advantage to the employees at the moment is really no argument against the main theme, however, because all of those other corporations would not be in business if they did not expect to make a profit one of these days, and therefore hope to be in the position where the establishment of such a plan would ultimately produce benefit to the employees.

Professor KING. That is undoubtedly true. However, I think it is also true that, year after year, we have seen a large number of corporations operating without profits, hence it could not be expected that in any particular year any very large proportion of the employees would secure any considerable amount of benefits financially from a profit-sharing plan.

Senator VANDENBERG. I agree with you, particularly under the present dispensation, as long as it lasts.

Professor KING. It seems to me that the only way that one can really expect to benefit the employees very much is by getting more production, having more to distribute, and I think that is exactly the point which you make. That is, when the employers prosper the employees prosper.

Senator HERRING. A just profit-sharing plan might have increased the number of corporations which had profits to share last year, might it not?

Professor KING. If you have a right kind of plan, I think that is exactly what it would do.

Senator HERRING. We have had evidence here from employers of many thousands that they believe the prosperity of their business was due to a large extent to the fact that they did have a just profit-sharing plan with their employees.

Professor KING. I think that that is correct, and that it is possible to arrange a profit-sharing plan which will increase greatly the output of industry in the United States, and increase greatly the income of labor, as well as the income of the proprietors of the enterprises, and that is the kind of a plan which seems to me to be worth while. Incidentally, I believe that it is possible to have a profit-sharing plan which will tend to stabilize employment, and, to my mind, the stabilization of employment in the United States is the greatest economic problem confronting the Nation at the present time. We have had millions of people out of work off and on, some of them steadily, for a number of years, and to my mind that is a hardship which is extreme and which should be avoided in every possible way.

Now the question is how, if at all, can we accomplish anything of that type? The fundamental point to be considered in that connection, it seems to me, is that the law of supply and demand rules the whole field of economics. We can try to evade it as we will, but we do not have any luck, it continues just exactly the same, just as does the law of gravity. When we legislate rules saying that labor is not a commodity we do not get labor out from under the law of supply and demand in the least. We know that when the merchant finds the shelves in his store overstocked with goods he has just one method of getting rid of them he lowers prices until he moves the goods. If he does not lower the price he cannot be sure that he will get rid of the stock. We know that when farmers raise a large wheat crop, and when the demand is very slack they still get rid of their wheat. The only way they do it is by lowering the price sufficiently to move the crop. Every year the price does go down to the place where the crop moves and the farmers get rid of practically all their wheat and all their crop every year. Now if the farmer is determined to get a certain price for his wheat and says, "I will never sell my wheat for less than $1.50 a bushel," as long as he holds out he will accumulate wheat until the price in the market goes above $1.50 a bushel; and some farmers do accumulate wheat, but not many, because they cannot afford it.

Now it is just exactly the same with any other product. If the price is held high enough the stock of that product tends to accumulate, for it cannot be sold.

In the United States we have a system of prices which, in many fields, tend to be inflexible. As you well know, Gardiner Means, of the Department of Agriculture, published several monographs showing the inflexibility of prices. I think that his evidence is incontrovertible. Some prices are flexible and some inflexible. We find that the farmers' prices are extremely flexible, and we find that the manufacturers' prices tend to be quite inflexible. We also find that in all the fields where the prices are flexible we have very little trouble with tie-ups of production and very little trouble with unemployment, but in all the fields where the prices are inflexible we get rigid prices, but we get extremely flexible employment. Sometimes we have people at work and at other times we have them not at work.

It has been charged that this price inflexibility is all due to monopoly. I do not believe that that is the case. I think occasionally it is due to monopoly. We know, of course, in the fields of public utilities and railroads monopoly is recognized and we have commissions regulating the prices, and those are rather rigid prices, they are fixed by Government, and might be fixed by monopoly if they were not fixed by Government. In either case they are fixed. We know that in many highly competitive manufacturing industries we have just as much price rigidity as we do in an industry that is being monopolized, because the customs of industry are to fix prices and let the buyer take it or leave it. That is not merely a foolish custom, but it comes largely through the accounting system. The manufacturer keeps a set of accounts, he finds out how much it costs him to produce an article and he adds on a margin which he thinks is necessary to keep solvent. He says to himself, "This is what I must get for the product. Take it or leave it." If he can sell many of the items at that price, for example automobiles, he sells them. If he sells a few, all right. When he sells a few he can lay off the laborers, he dose not have to pay them, he does not have to buy raw materials, and for that reason he is able to get rid of a large part of his expenses at the moment. That does not help the laborers any. Their expenses go right on, but he does not worry about that, he does not need to financially, and so he maintains his prices and cuts his expenses for labor and for raw materials.

Now, the farmer is no different in his point of view toward the public weal from the manufacturer, he would like to do the same thing, but in most cases he does not have any laborers to lay off, except the members of his own family, and that would not help very much. He does not buy very many raw materials. He has his investment there in his land, and his livestock; he cannot get rid of it, he has to keep it and pay the expenses of raising it. He has no large reserves in cash, in most cases, and when the time comes along he has no option except to sell his goods for anything he can get, and he does it. Now, I think the automobile manufacturer may have no more monopoly than the farmer, but he has more cash resources and he has employees that he can lay off; he can cease buying raw materials, and so he adopts this policy of inflexible prices and very flexible demand for labor. I think that is decidedly antisocial. Understand, I am not condemning the automobile manufacturer at all as being an antisocial being; I think he is probably as public spirited as anyone; in fact, those that I know are probably more public spirited than the average, but it is the custom of the industry in this country, that is the way the thing has gone in the past, it is the way the field has operated, but I am not sure that that makes it desirable to keep them operating that way in the future.

We need to distinguish between the two different types of commodities that are manufactured. Some commodities are such that the demand for them is extremely flexible, and other commodities have a demand which is very inflexible. If you have the first class of commodities and you vary the price of those commodities you can change the volume of sales. I believe that most people agree that when you cut the prices of automobiles you can sell more automobiles. If you cut the prices sufficiently, you can sell many more automobiles, but suppose you wanted to adopt the same idea in the case of locomotives. If the Baldwin Locomotive Co., in a year when business was declining and the railroads had a surplus of locomotives in their yards would say, "We will sell you a locomotive for one-third of the regular price," the railroad company might say, "Why, we are not interested in the slightest. We have too many locomotives now. We do not want a locomotive at any price." So that a plan of stabilizing employment which would work for an automobile company would not work for the locomotive company.

You have certain types of demand which are derived from other demands. That is true, for example, of the demand for carrying freight on railways to a very large extent. When the factories of the country are busy they demand much freight and they demand it without very much regard to the price, but when the factories are idle they do not care to have the freight carried, hence the railroad demand is weak. So that the railroad demand is largely a derived demand. That is not true in the case of passenger traffic. If you can cut the rates on passenger traffic sufficiently, you can induce passengers to take long trips on the railroads, but you cannot get more freight in many fields by cutting the rates on freight traffic.

Now in the particular fields of industry in which the demand for the goods is elastic I feel that we can adopt a plan which you might call a profit-sharing plan, which would work wonders in improving the conditions of both labor and employer. We have had in the past a theory in economics that the entrepreneur took the risks, that labor was to be given a fixed wage, labor was not to take risks. When the business was good the entrepreneur was to have large profits, and when business was bad the enterpreneur was to have small profits. That sounds well when you read about it in the book, but I cannot find that it has ever worked out that way in practice. That is, when times get bad the laborer loses his job and his nominal fixed wage is fixed only as far as the rate per hour is concerned. He may not have an hour's work, and if he has work he has only part-time work, so that the fixity of his income becomes a myth.

When the country prospers everybody prospers together, all classes, all employers prosper, all stockholders prosper, all bondholders prosper, and the laborers prosper; they all prosper at the same time. If you take an index of production and compare it with the index of the total wage bill of the country you will find that the two indexes run right along together. Whenever the production is high in the country the wage earners are prosperous, and when the production is low the wage earners are having hard times. So that the notion that you can actually separate the welfare of the worker from the welfare of other classes in the country it seems to me is purely mythical. They are all tied up together no matter what we wish about it or what we think about it. The interests then of the employers and employees are, for the most purpose, identical. Their conflicts are minor and their common interests are major.

We have heard recently about some plans of profit sharing in which it was proposed to give to the laborers a fixed annual wage.

Now, in some companies they have succeeded in giving to the laborers a fixed annual wage. If you have a product the demand for which is extremely stable, as for example soap, you can probably give to the majority of your employees a fixed annual wage and keep them employed and not be in danger of bankruptcy, but if you have a product the demand for which is elastic, as for example automobiles, and you try to guarantee to your employees a fixed annual wage you would probably find that you could only guarantee it to a fraction of your employees, because variations in demand for automobiles would bankrupt you if you tried to guarantee it to all of the employees that you have working at peak periods, and after the company went bankrupt it would not help the employees any to have a nominal fixed wage. So that any kind of a plan that is worth anything must be one which will not bankrupt the company, and that means that in a great majority of industries it cannot be a fixed annual wage. That is only applicable to a few companies or to a part of the employees of the company, and from the standpoint of the social welfare these other employees that do not receive the fixed annual wage, it seems to me, would be just as much part of the body politic as those who do get a fixed annual wage. Their interests are to be considered.

If you are going to get any kind of a workable plan for guaranteeing a fixed income, it seems to me that it must depend upon having the employees producing something to cover their income all the time. We know that as a matter of fact in the United States, as well as in other countries of the world, that demand for goods in general fluctuates from time to time in cycles; it goes up and down. The reasons why it fluctuates are being worked on by a number of scientists, and they are making some headway on it, and I do not know that we need go into them at the moment, but the fact is that the demand does fluctuate very rapidly from time to time. It is not necessary, however, that when demand fluctuates your volume of production shall fluctuate with demand. We see that clearly in the case of farm products. That is, the demand for farm products fluctuates just as much as does the demand for manufactured products, and yet the production of farm products is affected very little by the changes in demand, it goes along at just about the same rate; whereas the manufactured products have tended to fluctuate tremendously in response to these changes in demand. That means that if we are to avoid fluctuations in sales of goods, fluctuations of employment, we must introduce into the manufacturing field flexible prices, such as the farmer has in the agricultural field, but the manufacturer will tell you at once, if you speak to him about flexible prices, he will say:

> I cannot do anything about this because wage rates are fixed, and if I were to cut the price on the automobile that I manufacture, for example, and I pay the same high wages, why my costs would outrun the selling price and the company would go to the wall.

It is nonfeasible. So that any kind of a plan for making prices flexible in the manufacturing field must include making wages flexible in the manufacturing field as well. It must have as much flexibility as the prices on the products that are sold.

I believe there is no doubt that in the production of automobiles, clothing, and a great mass of articles used by consumers, that by sufficient price flexibility you can keep production constant, just as the farmer does. If you keep production constant, that very fact tends to stabilize demand, because when a worker has a job his demand for goods does not fall off at all as it does when he loses his job. So if this plan is generally adopted of having the flexible prices you would not need to have as large a degree of flexibility as it appears you would have to have now under our present system.

I have noted, in looking over the figures from time to time, that there is a strange stability in the share of the gross distributable income from industry that goes to labor, and a strange stability in the share that goes to capital. It is not exactly fixed, but it does not have anything like these huge fluctuations that you see in the total share of labor and total share of capital. That is, when the total amount of wages paid is going up and down like this [illustrating] the percentage that labor gets out of distributable income is waving along wildly.

In this particular boom in 1929 the percent of the net product of industry that went to labor was approximately the same as the percent that went to labor at the trough of the depression in 1932. It had not changed even according to the national income figures put out by the Department of Commerce. it had not changed even 1 percent. I know perfectly well that those figures are not precise, that they are merely estimates, so it may have changed more than 1 percent, but, at any rate, it was about the same fraction of the gross income at the peak as at the trough.

Why not recognize that fact? Why not agree that the thing to do is to divide up the gross income of industry between the laborers, between the executives, between the technical force, between the stockholders, divide that all up so that they get approximately fixed shares in the total? It would be about the same as they do now, but if done on that scientific basis it would have tremendously different results. That, I think, you would find would be about the same story, if you take and apply it to a single corporation or apply it to industry as a whole, that there is not so much difference in the shares going to the different claimants, in the different stages of the business cycle, as there is in the absolute amounts; that is, dividends go down and wages go down together, dividends go up and wages go up.

Suppose, for the purposes of our inquiry at the moment, that we define the gross distributable income as the amount left over out of the total value of goods sold, after paying for the raw materials, after paying fixed charges such as taxes, interest, and rent, and after setting aside appropriate reserves. Now, the balance is the amount that is ordinarily paid to labor and to the stockholders, and by "labor" I would mean all the employees from the president down in this particular case. Now, if we apportioned that amount equally from year to year it would not work so well as it would otherwise, because of the fact that we have variations in the type of labor employed from time to time, and we have variations in the amount of capital invested in the industry from time to time.

So the plan which I propose would be this, that we calculate at any point where that plan is started the number of units that each kind of goods or service is contributing to the operation of the plant at that moment. Now, let us see what we mean by "unit." Suppose that we took a dollar's worth of the item at that particular date as being a unit; if a laborer was getting 50 cents an hour, then we will say that 2 hours of that particular kind of labor we would call a unit. From then on until the contract was changed we would have 2 hours of common labor equal to one unit. Now, here is a skilled employee; he is getting a dollar an hour; we would say then that thereafter 1 hour of that type of labor would be counted as one unit. Here is an executive that is getting $10 an hour, and we would say one-tenth of an hour of his labor would be counted as one unit, and during the same period of time the stockholders are getting a dollar on five shares of stock, we would say then that five shares of stock would be counted as one unit. So that each class of employees would have their work specified in number of units for any particular time. Or, for example, take the amount of production. For example, a man would get a dollar for making a coat in a coat factory, then the amount of work on that coat would be one unit. At the end of the period, say a month, the accountant would figure up how many units of work, how many units of stock, had been employed during that particular month. He would find out how much money was left over for that particular month out of the sales, after they had paid the fixed charges, after they had paid for the raw materials, what they had left, and that would be the gross distributable income. Knowing how many units of stock and of work were employed during that period he would then divide the total gross distributable income by the total number of units and find out what the return was to each unit for that particular period, and that would be the rate that would be paid to that unit. So, during the next month there might be some little delay necessary for accounting purposes, but, in general, the compensation per unit would depend upon the returns per unit which the company had in the immediate past.

If this were done, the company could, when necessary, cut the prices on its products in such a way as to move the products and keep everybody employed. They could, if that were done, guarantee stable employment to their regular working force year in and year out, because they could change the prices enough to keep employment stable; and I think that, from the standpoint of the employees, it would be highly desirable that they have a contract which would mean that the employer would employ his regular working force year in and year out, but paying them such wages as the industry could afford—not impossible wages but the wages that were possible. Under those circumstances the employee would always get wages, the stockholder would always get dividends, but he would not get the same amount of wages each month and the stockholder would not get the same amount of dividends each month, but if wages went down 10 percent dividends would go down 10 percent, or if wages went down 20 percent dividends would go down 20 percent. It would be as fair to one as it would be to the other.

The more concerns that adopt such a stabilizing policy, the less would be the tendency for industry to fluctuate. If this plan were adopted by the concerns that produce goods for which the demand was elastic, stabilizing their employment would automatically tend to stabilize employment in the indirect-goods production.

For example, if the automobile companies were producing steadily from month to month, the steel companies would produce more steadily because the automobile companies would buy steel, the rubber companies would produce more steadily because the automobile companies would buy rubber; and if the steel companies produce steel more regularly the railroads would have a more regular demand for hauling coal, and that would stabilize employment there.

So, if you had stability in the consumption-goods industries, where you do have a relatively elastic demand, you would automatically get a very considerable degree of stability in the other industries where the demand is not elastic; that is, it would bring stability in the indirect industries.

Now that, you see, would be to the mutual advantage of the employers and employees. I think that it would be very well, indeed, to have the employees given full access to the books of the companies, so that they could see how things were going, so that they could see why it was necessary to reduce wages at a given time, and why the wages were raised at another time. That would not necessarily mean participation of the employees in the management, but they should be allowed to see what was going on.

I agree with Mr. Gannett's statement that the employees, in most cases, are not very competent to participate in the management. Mr. Hapgood, as you probably know, in the Columbia Conserve Co., turned the company over to his employees, and he found difficulty in doing so. They did not know how to manage the company. It was a long, arduous job to educate them so they could run the company, but they adopted a plan similar to the plan outlined by me now. They were the only company that went through the 1932 depression that did not lay off any workers. There may be other companies that did not lay off any workers, but that is the only one that I know of that went through the depression and did not lay off any workers at all, but they had large variations in wages.

The fewer companies that adopt this plan, of course the less would be its effect on other industries. The more companies that adopt it the more it would affect other industries. I am inclined to believe that if this plan could be generally adopted by the industries producing goods the demand for which is elastic, that it would go further toward stabilizing industry in general, and further toward keeping permanent prosperity than almost any other single measure that I can think of.

Now the question is: Can you get employers to adopt a plan of this kind under the circumstances? Well, one of the obstacles that they immediately run up against is the fact that the labor unions are likely to oppose it. I think that is a mistaken policy on the part of the labor unions, because I think this plan would be just as advantageous to the labor unions as it would to the employers, it would merely mean a change in their policy. There is nothing in this plan that would in any way hinder collective bargaining. The labor unions could sign their contracts exactly the same as before, but it would mean they would not need to sign a new contract very often, because having agreed upon the size of the unit there would not be occasion to modify the size of the unit except at relatively rare intervals. So that the friction between employer and employee which now occurs at every change in the business cycle would largely disappear.

Now from the standpoint, of course, of the corrupt labor leader who wanted to cause trouble, that would be a bad thing, but from the standpoint of the honest labor leader who was really interested in the welfare of his group I should think it would be an admirable thing. It would lessen friction, it would increase by a large amount the total annual income of the members of his union, and we think in the long run would benefit everybody concerned and would not interfere in any way with collective bargaining.

The employers, also being relatively conservative people, are likely to oppose this plan, because of the fact that it is different from what they have done in the past, which would be a perfectly natural reaction. Hence it may be necessary for the Government to use considerable pressure of one kind or another in order to get any kind of a plan adopted which will insure stabilization of employment.

Now my general feeling is this, that when Adam Smith pointed out in his Wealth of Nations the advantages of laissez-faire he did a wonderful service to humanity, and most of the things which he says in that book hold just as well today as they did in 1776, that is, in general. Laissez-faire has proved the most workable plan of getting prosperity that has ever been devised. All kinds of regulations tend to be cumbersome, awkward, and wasteful, but there are certain limitations on laissez-faire which we have learned through the centuries. You cannot have it absolutely, you cannot say, for example, that any man should be allowed to acquire wealth in any way he desired, because then any bandit would rule the community. We would have to put a restraint on it.

There are certain things in the laissez faire that have not worked out well in any country. We have found that in control of money and credit laissez faire has not worked well; that Government has got to intervene in order to stabilize money and credit; and I think that we can say also with considerable positiveness that laissez faire has not worked well in regard to the question of employment. In all the countries in which we have had a relatively large amount of laissez faire we have had these great swings in employment going down into the depths, with thousands and millions of people looking for jobs at one time and a little later a great boom, people working overtime, and then another depression in the amount of work, and I feel that these swings in employment are so important, from the standpoint of the social weal, that it is necessary to sacrifice a certain amount of our liberty in order to overcome the evil which is prevalent under the laissez-faire system. Now we want to sacrifice just as little of that liberty as is possible and overcome the evil, because I think that laissez faire, in general, is far superior and ought to have just as little bureaucratic interference as we possibly can get, but I think that we should overcome this very decided evil of unemployment. Just as in automobile traffic we do not like to be interfered with any more than necessary, and yet we do have to tolerate the traffic policeman and red light in order to make them go; so I think in this field of employment we have to tolerate a certain amount of Government interference in order to make it operate.

So I would suggest that anything that could be done in the way of incentive taxation to produce stability by getting employers to adopt a plan for stabilizing employment and making wages and the share of capital operate together would be highly beneficial and would greatly increase the income of both capital and labor. We should not adopt any kind of scheme that takes away from capital and gives to labor or that takes away from labor and gives to capital, I do not think we want to take away from either one, we want to keep them producing, turning out the goods and increasing the shares of each.

I believe that is about all that I have to say in my preliminary statement.

Senator VANDENBERG. You put your entire emphasis, Professor, on the necessity primarily of a variable rather than a fixed wage factor in the production unit.

Professor KING. That is correct.

Senator HERRING. Thank you very much, Professor King. We appreciate your being here.

Professor KING. I am very glad to be here.

Senator HERRING. We will next hear from Mr. A. L. Marsh, president of the Hoskins Manufacturing Co., Detroit, Mich.

STATEMENT BY A. L. MARSH, PRESIDENT, HOSKINS MANUFACTURING CO., DETROIT, MICH.

Senator HERRING. Mr. Marsh, we understand you have got an interesting story to tell us. We would like to have you give us a brief history of your company and how you became interested in this plan of yours, and tell us what your experience has been.

Mr. MARSH. This is a new experience to me. I did not know just what would be expected of me, so I made a few notes coming over on the train last night, and I think I would like to read those first and then I will discuss any phase of it. I will give you a history of our business, or any other thing that may be interesting, but these few notes describe the philosophy that I have of profit sharing, and I think a lot hinges on that point of view.

Profit sharing is a very timely subject. There are many indications that management is about ready to give up the old idea that labor is a commodity, subject to the laws of supply and demand and to be hired and fired and generally abused so long as profits were made. The new viewpoint admits that labor is an essential part of industry.

Profit sharing is not a good name for what we are doing. The thing that we do is to agree at the beginning of any year that all employees will have a raise in pay if the year's business turns out to be good; and the better it turns out to be, the bigger the raise. The measure for a good year is the amount of profits made.

Since 1923 our plan has been the same. After 6 percent on capital has been deducted from profits, a sum equal to 25 percent of the remaining profits is set aside to be apportioned to all employees according to a definite plan. To show what this amounts to under our plan, a clerk or factory employee who has been in our service continuously for 5 years has received as extra compensation, as high as 50 percent of his annual pay in the best years. In the worst year, and only 1, no extra compensation was paid. The average is about 30 percent over the last 10 years, including the 1 bad year. No reductions in basic-rates were made.

The extra compensation is paid in cash in February of each year after the company's books are audited. The employee lives on his basic wages during the year. If he has sickness in the family or other extraordinary expenses the extra compensation is his mainstay. If he is more fortunate, he has the cash to buy needed things and provide for the future. An essential feature of the plan is the certainty of extra compensation if business is good and profits are made. There are many advantages to such a definite plan of paying all employees a fixed salary or wage plus additions in accordance with the company's ability to pay. One important result is the interest, efficiency, and loyalty of all the employees. The effects are amazing even to one who has observed the operation of the plan for 15 years. There have been no labor troubles and the turn-over of labor has been extremely low. There is a different spirit than you will find in the average factory. All this results in extra profits. All employees are made to feel that they have earned the extra pay and of course they actually have. There is no paternalism in this.

Another important result is the increased security of the company and the employees' jobs. Since the salaries and wages are moderate. the cost of manufacture is kept low and the company is better able to meet competition and to carry through bad years. Yet, on the average, the employee is better paid than under a fixed wage system.

A third important result is a tendency to correct the violent swings in our economic system. It is a plausible belief that these swings are caused by a great piling up of profits and capital goods in boom years with too little increase in consuming power. The division of profits with labor is just what is needed to reduce the piling up of profits and to increase consuming power at the right time. It can be done in approximately the proportion that it is needed. Over expansions and depressions should be less severe to the benefit of everybody.

Another advantage to labor and to society lies in the fact that wages paid out of profits as extra compensation has increased purchasing power over the same total paid as fixed wages.

The basic part of wages goes into the cost of manufacture while the extra or variable part is a direct deduction from gross profits. High fixed wages means higher costs of goods, higher personal property taxes on inventories and equipment, larger amounts of money invested and higher mark-up for profit due to higher cost. If fixed wages were generally raised 50 percent the employees wages would buy less than before the raise. Those who got the 50 percent would have an advantage only if a large number did not get it. With the extra compensation method, even the fixed part of wages will buy more. It is simply a matter of turning back some of the profits for the purchase of more and lower-cost goods.

Higher fixed wages will reduce the value of a dollar. Waste and extravagance are already making inroads.

All people dislike to take cuts and cuts are seldom made fairly. This results in much dissatisfaction. With the extra compensation method we all go up and down together and do it automatically.

There are other benefits but this is enough to show that benefits are widespread. Even the much abused farmer will benefit from the increased purchasing power of his dollar and the increased purchasing power of labor. Higher fixed labor rates certainly react against him.

That is the result of a few notes I wrote down last night, and now I am ready to go into a history of our company, or any other subject you would like.

Senator HERRING. I think it would be well to start out with a history of your company. You have about 200 employees?

Mr. MARSH. We have about 150 on the average, 140 to 150 in the factory, and somewhere around 200 total, including the salesmen.

Senator HERRING. They are not organized?

Mr. MARSH. None of them are organized. You see, we started this in 1923, and anything started back there, as fair as this thing is, resulted in their not wanting to be organized.

That brings up a point that to my mind is very important. People have come to me and asked:

> We are threatened with labor trouble. Let us know about your profit-sharing plan and maybe we can avoid it.

I say:

> No, do not start it now for immediate results. This is the wrong time to begin anything like that. If you want its effect on labor start it before you have to do something about it.

Senator HERRING. What is your basic wage?

Mr. MARSH. Our basic wage we have kept raising over the years, because we found that our business was sounder and sounder. We set up a considerable reserve, which I understand is disagreeable to some people, but we set up a pretty good one, so that our company is safe and the jobs are secure. Then we raised their basic wage so that we are paying practically all that other people are paying, and the extra compensation on top of that.

Senator HERRING. Well, your basic wage is what?

Mr. MARSH. Our basic wage is now 60 cents an hour for janitors and common labor, and you see in 1937, when we paid out a 50 percent extra compensation to the 5-year men, all our janitors who had been with us for 5 years and show they are faithful, and all that, they got 90 cents an hour for that work.

If we believe in capitalism, and I certainly do, there is no other system that has ever proved to be very good, and I do not believe it will, but if we want a capitalistic system we must let a larger number of people have profits. Now when you pay them a fixed wage and then pay them extra compensation on top of that, then the laboring man is making a profit on his work.

Now, if we make an investment in stock, we all like big profits, at least I never saw anyone who did not. We are well plased if it turns out better than we thought it would, but what do you think about the laboring man? Supposing he goes through the year, he knows business is pretty good and he knows he is going to get something pretty good. We do not post notices every day, because we do not know. I took this attitude about it. If we do not have good profits in the first 4 months I do not like to tell them the next are bound to be good and he is going to get a whale of an extra compensation. It does not pay to let him down. He knows how business is going, he knows the things that are depriving them of getting any extra profits; that it is not going to be as much as he would like.

Senator HERRING. You furnish them full information as to the condition of the business each year, though, do you not?

Mr. MARSH. Each year we give them full information, and our earnings are published in the papers quarterly, so if they read the papers they know what we are doing. I do not talk to them any more because I understand it is against the law to talk to a workingman, because I might influence him in not joining a union.

Senator HERRING. That was passed before I came down.

Senator VANDENBERG. Don't look at me.

Senator HERRING. Was the profit shared arrived at, the percentage or the amount, through negotiation of any kind with the employees?

Mr. MARSH. No.

Senator HERRING. It was not?

Mr. MARSH. No. I figured it out in advance, and I figured it out for this reason, as I explained in a letter that I wrote to Mr. Despain: I was manager for about 7 years or so, I guess—I have forgotten the number—and every time business began getting a little bit better our employees just simply hounded us for money, and it was an awful job to keep them down. So after 7 or 8 years of that kind of experience I began to wake up to the fact that human nature wanted to share in prosperity. When the country is up and you read in the newspapers that the YZ Co. trebled its earnings, and here he is getting his little 40 cents an hour, that does not look fair to him.

Senator VANDENBERG. And the president draws $200,000 salary.

Mr. MARSH. Yes.

Senator HERRING. The president of the company, he means. [Laughter.]

Mr. MARSH. I want to talk; and if I forget to do it, I hope you remind me—I want to talk about salaries, because there is a very important thing about legislation connected with salaries, I think. Now I am not a legal man, so don't take me too seriously when I begin to get into the legal phases of it; but to go on with this thing I realized that something had to be done. There might be no profit. The year started out good. I did not know whether it was going to be good or not; I did not know whether we could afford to raise them. I saw the disadvantage of getting high-cost goods on our shelves, and so I just figured this thing out and told them, "All right. Now, we are not going to raise you; but if the year is good, we are going to; we are going to pay you and let you have a portion of the profits." Fine; but there was quite a lot of skepticism, I will say, for the first year, because they had heard of other companies doing it and just as soon as extra pay amounted to a few percent they would withdraw the plan and then they were finished from there on. From there on the employees will not trust them again.

So I convinced our directors that it was a perfectly safe plan; it was a fair plan to labor and if we paid them big money. We were going to make big money, so why should we object, and the more they could make for themselves and us the better we should like it. So they finally gave me permission to put it in, and it has worked wonderfully. We are all convinced we are making more money than we would have made any other way.

Our employees are efficient. We did not make any point about selecting people with tremendous ability, or anything of that kind, but we took them as they were, and when they get into the spirit of the place they certainly produce the goods. Now everybody benefits from that. Our customers benefit.

When we started this in 1923, I had an idea that all our employees ought to get this extra profit on their labor, because we were making good profits and everybody contributes. I made up my mind that everybody should join in on it, because 1 year I might contribute something notable in the production of profits and the next year maybe the efficiency of labor, in the saving of spoilage, and things of that kind, contributes, so I could not tell who is doing the most and it costs too much money to find out, so we made the distribution general. The Packard Motor Car Co. put in an efficiency plan in their plant a good many years ago, maybe you remember about it, and it took so many men to determine their ratings and what they ought to get that they finally had to abandon it.

So our plan is perfectly simple. Everybody contributes. We do not have an employment department, we do not seem to need it any more for those few people anyhow. I tell our foremen, "Now you take these men that you need, look them over carefully for the first year and if there is anything the matter with them let them go, don't hang on to them, because after they have been here 5 years I do not want you to let them go, so be careful," and they have been careful.

Well, that is about the way we started into it and figured it out, and we just adopted it as a fair all-around plan.

Then, getting into the intimate details of our business, during 1923, 1924, 1925, 1926, 1927, and 1928, they were pretty prosperous years, and we decided to divide whatever benefits we were getting all around. The stockholders were getting a big return, so we cut prices nearly every year. Nearly every year we reduced the price of our goods voluntarily, without any pressure to do it, simply because we thought it was good business, and I will say that nearly every year that we reduced—of course we were fortunate in that period—nearly every year after we reduced the price we made more money than we did the year before.

Senator VANDENBERG. State for the record what you manufacture, Mr. Marsh.

Mr. MARSH. Our main business is the manufacture of electric resistance wire for the heating element of electric household appliances like toasters, flatirons, and electric ranges. Our company years ago owned the basic patent on that, and if you do not mind getting off the subject a little bit, I would like to state just a little bit about the early history and its relation to the laws of today. We started up on this patent, and naturally there was a tremendous struggle to keep going and get the thing introduced. It is an awfully long, patient job. I want to tell you I have been working on this one thing since 1904, and it was 1915 before we saw any real money out of it. Some people advocate the shortening of the term of patents. I tell you that most patents just cannot be made to produce profits in any short time. We had to fight patent suits, and we had our own troubles in developing the alloy. The thing did not behave; it was new. So our company was founded on this patent, and a number of others, but there was one basic patent on this resistance element. But the point that I wanted to make is that we had to have capital to fight the patent suits, and one thing and another, and to carry on a business, and it was carried on at a loss for a number of years, and we had to induce capital into the belief that it would be a pretty good thing eventually. We could promise nothing as immediate results. Well, we succeeded in doing that, but we could not have started our company today, it would have been impossible. Only wealthy men can afford to take those long risks. Perhaps 1 out of 10 will make good, and perhaps less than that. There is no incentive for a wealthy man today to take the risk, because if he makes a profit, if the company turns out good, like ours happened to turn out, what would he get out of it? Very little because he would have to pocket the losses from the other 9 or 10 and be taxed heavily on the successful venture. I just bring that up to show that our kind of a company could not have started under your present conditions.

What I would like to recommend before I get through is about some of the laws. Remove some of the barriers. Profit sharing will almost take care of itself, I tell you, because there are real advantages in it to everybody.

You might argue that the low cost of goods could be carried on indefinitely, the lower you pay labor the better off you would be. Maybe that is true. It is impractical to go too far. We would have to have a drawing account or a living wage as the basis. Then I think capital should have a slight drawing account. So we deducted 6 percent, at first it was 8 percent and now it is 6 percent—interest rates have dropped—and we deduct that for the security of the company. That is, the company needs a little money to build up safety, so that you can continue to give jobs to the employees. Then after that we make the division, and it is my opinion unless that division is substantial it is not much good, it will not accomplish enough of these benefits. A small one will satisfy labor reasonably well for a little time. People have made them very small and got along with them fairly well, but it will not accomplish these other things, the benefits to society. It is too small. It is too small to have the effect of taking the big profits off of the company.

Here is my belief, and here is where we get a little bit radical. I have always been known as being conservative, but I am just a little bit radical in some of my ideas. I believe in the safety of a company. I am extremely cautious. I believe they should be allowed to build up safety so we can run along under all conditions.

Now, after safety is obtained it is not so important for a company, and it is not very beneficial for the country either, in my belief, to build up enormous profits. Look at the nature of a manufacturing business. We have taxes and we have various fixed expenses in certain salaries, and those fixed expenses make it necessary to do a certain volume of business before you can make any profit at all, and that is a pretty big volume. In the steel business it is somewhere near 50 percent of plant capacity before they can begin to run into any profit. In our business it is just a little under 50 percent, probably.

Now, it ought to be possible to set profitable prices in some way, because a great many years are subnormal. You cannot have prosperity all the time, we never will. Depressions have been with us for at least 200 years; they started before we ever had anything to do with money, railroads, or other modern things, we always had them and we are always going to have them. We may modify them somewhat, but we are always going to have them, and I guess it is an inherent property of nature, because people have their ups and downs, too, they do not always feel the same each day. But, anyway, we have those things.

Now, a company, to have safety, should charge that rate of profit so that if he is in some subnormal business it will still let him keep alive, let him keep afloat. If you do that and then raise your business to a high level, what have you done? You have piled up enormous profits. To whom do those profits belong? I think they should be distributed. I think it is the only safe thing for our capitalistic system. We managers are not responsible for them. People should have buying power. They come in and buy our goods and they all buy with a rush at times and they just pile up our profits because of the nature of our business—small profits at half capacity and large profits at full capacity.

Some people talk as though if you sold a dollar's worth of goods you should get 10 cents profit, and if you sold $2 worth of goods you should make 20 cents profit, but that is not true, and it cannot be. So I sometimes wonder why the Government is so set on strict competition, cutthroat competition, which seems to be desired, to keep prices down, so that many companies cannot make money.

Now, my idea is that less severe competition would be better for everybody, if they adopted the profit-sharing scheme, because supposing they did build up a little too high and made more money? All right, it will go right back into society. It will go right back, so where is the danger?

Then in addition to company competition we have very severe industrial competition. You might say, "All right, there would be a monopoly formed and people would charge exorbitant prices." All right. Take some of the metals that I know something about. Supposing they put the price of, for example, tungsten up, let them raise that up. Very well, we will quit using it. There are other metals that may be used. Molybdenum is one of them, and we also could use nickel, we know a lot about those things now, so there isn't anything necessarily gained by any high price for the tungsten. That tends to limit monopoly. It does not do it entirely, I know.

Now it seems to me that we could benefit the capitalistic system to some considerable extent if we could permit more companies to make money, and then require that they spread this money, these extra profits in the good years, where it belongs and where it will do some good. Then there is no harm done to society at all. It all goes back and it is spread around in this way.

Now industry cannot possibly absorb all labor. It is simply nonsense to say that manufacturing industry has got to absorb all these millions of idle people. It cannot be done. If you go into profit sharing you are going to get greater efficiency, and that is desirable, too, because the more goods you make the more there is to spread around, if you give them buying power so they can get them. Then the extra buying power will provide more service jobs.

Senator HERRING. You went through the epidemic of sit-down strikes in Detroit, did you not?

Mr. MARSH. Yes, we went through the epidemic, and they were thick all around us.

Senator HERRING. Is that the time they presented you with a loving cup, your employees?

Mr. MARSH. Where did you hear about that?

Senator HERRING. Is not that true?

Mr. MARSH. That is true, yes. I do not want to waste your time, but I will tell you how that worked out. I do not know much about it, but many companies at the end of 1937 were inclined to cut wages and pull in their horns and drop benefits, savings plans, and drop everything that they had done for their employees, and our employees knew me for a great many years and they did not think that I was likely to do it, because I never had. We pay them without question. Sometimes a factory employee will get 5, 6, and a few of them 8 hundred dollars, all in one cash check. Well, it came along February, nothing was said about it, I did not talk to them. As I said, it is against the law, you cannot talk to the men any more. I know a lot of them by their first names too, but I cannot talk to them.

Senator VANDENBERG. Excuse me. That is a very interesting point that Mr. Marsh raises, because we have been told repeatedly this morning that candor is so essential between management and labor.

Mr. MARSH. Yes, it is very desirable.

Senator VANDENBERG. It is possible we outlawed candor by penalizing it.

Mr. MARSH. A lot of your laws make it difficult for a manufacturer to get along.

Senator VANDENBERG. Go ahead and tell us about your loving cup.

Mr. MARSH. Well, we went ahead in February; we figured it up, we had the auditors come out and check our books, a national auditing company, and we paid the extra compensation and it happened to be bigger than they expected, because business dropped off rapidly towards the end of 1937, but we had made big profits in the first half of the year, and it was a lot bigger check than they expected. Well, they were so aghast about our going through with it completely that there was some kind of a spontaneous movement to do something for me. I do not know why. I did not deserve it particularly, but they wanted to show their good will, I suppose, and as I was ready to go out to lunch one day, I had an appointment downtown that I had to meet, and the superintendent came in and said, "You are wanted out in the office." I said, "I am sorry, but I haven't time. I have an appointment and I do not like to be late." He said, "Well, you are wanted out there." I said, "Who wants me?" He said, "Never mind. You are wanted out there." "Well," I said, "I will go out a minute, but I cannot give any time to it." When I stepped out into the main office the room was just full of working men in their working clothes, practically everybody from the factory. I knew there was not any strike going on, because we never had any indication of it all through the year, but I want to tell you you could have pushed me over quite easily [laughter] because one of their number stepped out as though he was going to make demands, one of the oldest employees that had been with me for something over 30 years, but instead of that he began to tell about the wonders of this company, and pulled out this big silver pitcher with engraving on it. That is what we got instead of a C. I. O. strike. [Laughter.]

Senator VANDENBERG. I think that is marvelous. I think they ought to have given you a silver bathtub.

Mr. MARSH. Well, they did try to work on our plant. I did not dare ask our men about it, because that is against the law. So the rumors reached me, though. There were strikes down the street in some of the smaller plants, and, of course, they all knew about the automobile plant strikes and the disrespect of property rights. Incidentally, you give some of these men a little property and they are strong for property rights, don't overlook that. Maybe we better spread that around, if we want our property to be pretty good. Well, they waited on our plant and saw a number of the men and asked them to join, and they said no, they did not want to. That is what was told me. I have not asked them. They did not want to. "Well," they said, "Buddy, you are going to have to join, so you might as well sign up." They said, "Well, we will not sign up today. We will sign up when we have to. Maybe we will, but we are not sure we have to." I have not seen any indications of any labor union in our plant. We hire union men, I suppose, from time to time. I never ask them whether they are union or not, I never bother with that.

Another thing—is all this thing being written down?

Senator VANDENBERG. Yes.

Mr. MARSH. What are you going to do with it, may I ask?

Senator VANDENBERG. Present it to posterity. All this is for the benefit of American employers who have not been as far-sighted as you are.

Mr. MARSH. It is not going to be published, I hope.

Senator HERRING. There are four or five young men right behind you there. You will have to tell them that.

Senator VANDENBERG. I do not think there is anything you need be ashamed of, Mr. Marsh.

Mr. MARSH. Well, I am not ashamed of it particularly.

Senator VANDENBERG. I think it would be quite stimulating if it is published.

Mr. MARSH. I do not think I have done much of anything. It is just a fair proposition, and it has resulted in pretty good returns. I imagine that that happens nearly all the time, and maybe all the time, and the same thing would happen if we got laws of that kind. If everybody would think, "Now what is the fair thing to do for everybody concerned," I think it would turn out better. When you create opposition and pit one class against another you are just storing up more trouble, because one fight brings another one on, and it just keeps on continuing; nothing is settled. So what we better do is to reverse that process and get people feeling better toward one another, and we have succeeded in doing that in our plant.

Senator HERRING. And you made money by doing it?

Mr. MARSH. We made money by doing it, and I suspect other people will do it. I have not argued it with a great many people, but once in a while I run into somebody who wants to know about it and argue the thing a little bit. They said, "Well, it will not apply to all companies." "Well," I said, "how do you know it will not?" I said, "I can cite you companies that were broke and that came out of it all right when they began to treat their men fairly."

Incidentally, I am in an interesting experiment right now. I have no desire to be a director of other corporations; it does not appeal to me; I am just busy in our own company. Our men all want to make more and get more profits, and so I am busy with them, helping them do it. There was a company that I happened to own a few of the bonds in, and they came around and asked me if I was interested. I said, "Yes; I am interested to the extent of that many thousand dollars." Well, we discussed how to set up a plan that might bring the company out of trouble. He happened to be the receiver appointed by the court, and he was a very fine, capable man. After they worked up a plan that seemed to be reasonable all around he wanted me to serve on the board, and so I did. I said, "I do not want to serve on it forever, but if I can do you any good for a little while I am willing to try it with you." He was in favor of treating employees well. They have a great big outstanding bond issue that they have got to liquidate. People said, "Well, it will not work with all that debt." Maybe not, if you intend to keep that debt going forever. I tell you, debt is one of the menaces in this country. We go into long-term debt without any regard to how we are ever going to get it paid.

Senator VANDENBERG. You do not include the Government in that by any chance, do you?

Mr. MARSH. I hate to mention that, but I do. Well, anyway, the question came up of what we should do for the employees. There was a little argument, maybe we should not start anything right now. I said, "Yes; we should start right now," and so we did. I told him the best thing he could do was to let them know we were going to start this sort of thing. There would not be much; but if we would get that debt cleared down a little bit, then it would be more. So he worked out a scheme that fitted that kind of situation, so as the debt worked down their share goes up. They are busy getting the debt down; and if we have any good years, if we ever get through with this anxiety period, all kinds of propaganda schemes, if we ever get through with them and then have 2 or 3 years of good business, I will tell you the bond issue will be paid and the employees will begin to make money.

Some of the railroads could do the same thing, I am sure. Others are so far in debt and have gone on with so little regard to their earning power and piling up debt—I do not want to give any thesis on the subject, but I can not see anything but the wringer for them. Any company that has a desire to get out of debt and has got a chance, all right; let us give it to them.

Senator VANDENBERG. Your testimony has been very refreshing, Mr. Marsh, and very helpful, and I think very significant.

Senator HERRING. If you have anything else, Mr. Marsh, we would be glad to listen to you.

Mr. MARSH. Well, is there anything else you want to know? There is a lot more to it, but I do not want to keep you any long time going into the various phases of the thing. I want to talk about salaries.

Senator VANDENBERG. Oh, yes.

Mr. MARSH. But I can talk about that at lunch, because I do not want it to be published. Somebody suggested that I was going out to lunch here. Mr. Despain, I think.

Senator HERRING. You do look at profits, don't you? I haven't anything definite in mind.

Mr. MARSH. I have ideas about taxation, perhaps not very valuable, because I am not a legal man, as I said.

Senator VANDENBERG. That adds to value.

Mr. MARSH. Naturally you can gather from what I have said that I do not like the Wagner Act.

Senator HERRING. I got that impression; yes.

Senator VANDENBERG. You are satisfied with everything else?

Mr. MARSH. We must either repeal that sort of thing or else patch it up and make it fair. Give one man as good a standing before it as another. Why show favorites? The manufacturer is no worse than the workingman. I find we are more or less alike. Some are not very honest, and that applies to both classes. I do not know whether you want to go to lunch now.

Senator HERRING. I think we better. Maybe we can go along with you. I do not have anything else definitely in mind. I think your presentation has been very helpful.

Mr. MARSH. On this idea of a variable wage, I know what the arguments will be. Unions do not like it, and I know why. I can tell you that it will work. The variable wage is better than any fixed wage, because the fixed wage is going to run up the cost of goods; if that is done generally, and that is what we are going to do. In figuring out any kind of problem of that kind you must not figure you are going to be the only one that is going to do it, and you will get by with something. You must figure whether they will all do it and see if it is any good. They will tell you whether it is going to work or not.

Senator HERRING. Through your plan you have achieved the content and efficiency of your employees, you are making money, and have no labor troubles?

Mr. MARSH. We have no labor troubles, and the plan really works. Everybody is happy under it, and it does a considerable benefit. Now, our plan does not achieve all these benefits that I mentioned here simply because not enough people are doing it. We cannot increase the buying power of the people of our country with our 150 employees, but if all the others would do it look what will happen. I would like to have you think about that one phase of the thing—the fact that if it all goes into fixed wages, and with the pressure always on to raise and raise wages, what will happen to our dollar? What will happen to our buying power? You know that is what a union leader has to do, because he must show something for his men; and all they think of is higher wages, higher fixed wages. They do not like this variable scheme, but I believe if they understood it better they would even like the variable wage plan.

Now, what I am saying here does not necessarily mean that you should not have any unions. I believe that maybe unions do serve some good purpose for those who want to go into it. I do not think any man should be made to go into it. Those who are satisfied and do not want to should not have to, but there may be cases where people want to organize, to work things out. Maybe there will be some questions of the basic rate to be worked out, and when that comes about, that has to be worked out, then you should consider that manufacturers should organize, be allowed to organize just the same as labor, because it does not do this country any good to have a labor union concentrate on one plant and force extraordinary demands against all this competition elsewhere in the country. When it is adopted, when the scale is considered fair for one company, then the whole industry ought to adopt it, or at least in a certain locality where the living costs can be considered. All the questions of living costs should be gone into, and one thing and another. It has not been quite as simple as I tried to make it sound, but the principle is there; and the other things can be worked out comparatively easily, I think. When you get on the right track the troubles just kind of fade away. They have that habit. There are a lot of troubles that we think of now, that we think we have to face, that if we did this thing generally they would just evaporate and you would not have to face them.

Senator HERRING. You have given us a very fine presentation. We will recess until 2 o'clock.

(Whereupon, at the hour of 12:20 p. m., a recess was taken until 2 p. m. of the same day.)

AFTERNOON SESSION

(The hearing was resumed at 2 p. m., pursuant to recess.)

Senator HERRING. Mr. Du Pont, we will be delighted to hear from you.

STATEMENT BY LAMMOT DU PONT, PRESIDENT, E. I. DU PONT DE NEMOURS & CO., WILMINGTON, DEL.

Senator HERRING. Just proceed in your own way, Mr. Du Pont. You have a statement, I understand.

Mr. DU PONT. Senator, I have here a prepared statement. It is not very long, and if it is agreeable to you I would like to read it.

Senator HERRING. Yes, sir.

Mr. DU PONT. I have copies here. Perhaps you could follow it better if you use them, because there are a few tabulations in it.

First I wish to thank your committee for this opportunity to discuss briefly with you certain methods and policies aimed at the betterment of our economic and labor conditions.

In correspondence I have already told your committee that I may not be a desirable witness from your point of view, because our company has had no experience in profit sharing as commonly interpreted and understood by businessmen and by the public, although in 1937, the Du Pont Co. gave to or expended for employees approximately $21,000,000 over and above the nominal wages and salaries paid for time actually worked. Also, although I have given a good deal of thought to the matter, I am unable to convince myself that so-called incentive taxation would as a general proposition be either practicable or desirable.

I would like to interject here, Mr. Chairman, to tell you what my understanding of profit sharing is, what I think is the common definition of the term, namely, the distribution of the profits of the business among employees generally on some basis other than merit or accomplishment. If you distribute profits on the basis of merit or accomplishment then it becomes an incentive plan or a bonus plan, or perhaps a piecework plan, or something of that kind, it is no longer generally understood to be profit sharing.

Senator HERRING. Unless it might be a distribution based upon the annual wage, and the annual wage might be arrived at through merit.

Mr. DU PONT. Yes.

Senator HERRING. In that way it would be profit sharing.

Mr. DU PONT. Yes; but the annual wage as a basis of distribution is not a distribution on the basis of merit, if you distinguish merit from earned wages.

Senator HERRING. Except that the annual wage might be increased by reason of efficiency on the part of the employee.

Mr. DU PONT. But then the increased amount becomes the wage.

Senator HERRING. That is true.

Mr. DU PONT. However, I am informed that your committee is in reality primarily interested in discussing ways and means of removing the tax obstacles to business expansion and of improving employer-employee relationships. With this understanding and in this spirit, therefore, I am glad to explore with you any reasonable proposal for improving the lot of the average worker and for expanding employment.

I shall also ask your indulgence while I indicate briefly what the DU PONT Co. has tried to accomplish along these lines by methods which to date have, we believe, produced substantial progress toward satisfactory results.

INCENTIVE TAXATION

In the first place, let me say, as indicated above, that, after careful consideration and discussion with our experts, I have not yet been able to discover what seems to me a practicable method for the Federal Government to introduce any plan of rewards or penalties in the tax system which will promote the exercise of sound business judgment. It seems to me that the raising of revenue should be the primary aim of direct Federal taxation. Even with this as the sole objective, it is sufficiently difficult to work out a reasonable and equitable plan of taxation.

To reward one line of action through tax abatement is equivalent to penalizing an opposite policy. Conditions vary so widely from industry to industry, from company to company, and from time to time, that the problem of incentive taxation seems to me a very ticklish one. Although at one time such a policy might seem to encourage certain portions of the business community, yet, once the principle is established, it can readily be used for ends definitely harmful to business—thus creating even greater uncertainty.

It seems to me that such a plan might, on the one hand, tend to encourage unwarranted expansion in periods of rising business activity, and might, on the other hand, tend to reward unnecessarily industries which are naturally growing rapidly as compared with more stabilized or actually declining industries. Further, I fear that there would be danger of too much administrative interpretation of such tax laws, and of consequent bureaucratic interference with the conduct of business enterprise. That would not only be bad in itself, Senators, but it would engender the fear of further interference.

While it would, of course, be tempting to many businessmen to be given an abatement in their taxes because of the addition of employees to their pay rolls, yet such a reward is probably unnecessary. Usually companies are beginning to make money when their business expands sufficiently to warrant substantial additions to the pay roll.

To my mind, the best tax incentive to business will result from—

(a) Simplicity of our tax laws;

(b) Certainty and reasonable freedom from frequent changes in the laws;

(c) The lowest possible tax rate, based on economically administered Government activities;

(d) Taxation for revenue only, rather than for purposes of punishment or reform;

(e) And, finally, a tax system both for individuals and corporations which does not penalize success through progressively higher rates as the income increases, but which recognizes that, under our competitive system profits are usually large only where the risks have been great, and management has been sound and progressive.

If such general requirements in our tax system are met, business should have sufficient incentive to go ahead and hire more people.

PROFIT SHARING

Profit sharing, as commonly understood and practiced has, I believe, frequently proved to be unsatisfactory because it has sometimes been used as a substitute for higher wages, and has at any rate usually introduced an added element of uncertainty in the worker's income.

Directly or indirectly, it is difficult to share profits without sharing losses.

I believe in paying high wages based on efficient performance, and I believe in rewarding well those who carry the responsibility and accordingly take the biggest risks in business.

At any given time, external business and political conditions and the decisions of management, frequently and usually have a profound influence on the rate of profits earned by a business. To the extent that the average employee contributes to such profits, he should be regularly rewarded in his pay envelope. However, at a given time he may have little direct responsibility for a higher rate of net income, just as at another time his own degree of efficiency may have little to do with losses incurred.

Hence, it seems to me that in general those directly responsible for the management of a business, as well as the stockholders or owners, should properly share the greater risks. Their rewards should be higher when the business is prosperous, and less when times are hard. Whereas I believe the aim should be to make the worker's income as stable as possible at a relatively high level, always with opportunities for personal advancement as merit is demonstrated.

In order to be constructive, I should like to call your attention briefly to the industrial relations policies which have been followed by the Du Pont Co. with a view to improving employment conditions.

ESTIMATED ANNUAL VALUE OF THE INDUSTRIAL RELATIONS PLANS AND POLICIES AND SOCIAL SECURITY PAYMENTS OF E. I. DU PONT DE NEMOURS & CO. FOR THE YEAR 1937

The Du Pont Co.'s interest in the general welfare of its employees is a policy of long standing.

I might interject here, Mr. Chairman, that during the company's one-hundred-and-thirty-odd years of existence, the general policy of employee welfare has been customarily followed, but it was only about 35 years ago that the policies began to be formulated into definitely written-out and published plans.

For many years the management of the company has endeavored to improve the employees' working conditions and to cooperate in protecting employees and their dependents against the results of physical disability, increasing age, and death.

An examination of our different industrial relations plans and policies indicates that for the year 1937—1937 is used not because it is an exceptional year, but because it is the last complete year, and as plans have been added from time to time, obviously the most recent year is the best illustration—for the year 1937 our company and its controlled subsidiaries either gave to or spent for employees at an annual rate of at least $20,000,000 over and above the nominal wages and salaries paid for time actually worked by employees. The total amount so spent was equivalent to approximately 19 percent of the company's wage and salary roll of approximately $107,500,000. Of this amount, $3,249,628 was required payment for unemployment compensation and Federal old-age benefits under the Social Security Act. There remained an annual rate of voluntary expense around $17,000,000 for various employee relations plans and bonuses, all paid for by the company.

The total estimates are made up as follows:

Group life insurance	$441,705
Group accident and health insurance	212,090
Pension (interest paid for use of fund)	1,215,811
Pension ("set-aside")	975,058
Pension trustee's compensation	10,000
Benefit plan (voluntary awards)	158,022
Disability wages (annual rate—excluding workmen's compensation cases)	1,200,000
Full or part pay during illness (excluding disability wages)	476,428
Medical department	700,000
Vacations for wage roll employees	2,503,187
Vacations for salary roll employees	1,309,781
Stock investment (extra payments)	17,178
Savings (interest)	42,421
Service pins	17,536
Du Pont Country Club	10,017
Bonus awards for unusually meritorious work	7,593,000
Unemployment compensation taxes (State and Federal)	2,281,964
Federal old-age benefits tax	967,664
Total	20,131,812

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This total is made up of a large number of items. I would like to call your attention to the items by reading this list, and show you, to some extent at least, how they should be grouped together.

The first is group life insurance, $441,000, in round figures. The second is group accident and health insurance, $212,000. Next follow three pension items which, in the aggregate, are $2,200,000. The items that go to make up the $2,200,000 show the working of the pension plan. We set aside every year a sum of money out of the company's profits or earnings which is designated as the "set-aside," for 1937; this was $975,000 in round figures. The accumulation of those "set-asides" is placed in the hands of the pension trustee, who you will note from the last three items is paid a fee of $10,000 for the year for handling the fund. The funds in the hands of the trustee accumulate interest through being loaned back to the company for use in the business. That interest on the accumulated fund during 1937, was $1,215,000.

Senator VANDENBERG. How much is the accumulated fund, Mr. Du Pont?

Mr. DU PONT. It is something like $17,000,000, I think. I do not have that figure in mind. It is something like that.

Senator VANDENBERG. Are these all paid up by the company without contributions?

Mr. DU PONT. That is correct.

Senator HERRING. And it is in a separate trust, it is not in the balance sheet of your company at all?

Mr. DU PONT. Dr. Lincoln tells me it is $22,000,000 and not $17,000,000, accumulated in the fund.

A trust company is the trustee. It is entirely independent of the Du Pont Co.

Next there are three items designated as benefit plan, disability wages, and full or part pay during illness. Those are all similar. They aggregate $1,834,000. The first one, $158,000 is paid out under our benefit plan which, to some extent at least, is in the nature of an addition to the pensions. Where a pension, according to the regular plan, seems to be inadequate something is paid out of the benefit plan to give that employee or dependent an appropriate income. There are other items included in that $158,000, but they are all in the nature of voluntary payments due to some type of disability.

The next, disability wages of $1,200,000—which, by the way, is partly estimated, because that plan was not put into effect until about the middle of the year 1937, hence the amount that was paid out in 1937 does not represent the full year's working of the plan, and this $1,200,000 is the estimated amount that would have been paid out had the plan been in effect throughout the year 1937. That consists of payments to wage earners who are absent from work due to accidents or illness of a nonoccupational nature. It has nothing to do with plant accidents or occupational diseases, or anything connected with the work, but due to illness or injury outside of the man's work, and is all paid to wage earners.

The next item is a similar one paid to salary earners, $476,000.

The next item is our medical department, which is estimated to cost about $700,000 a year, and consists of general medical examination and attention given to employees in connection with their work.

We make no attempt to treat employees in their homes for ordinary diseases, but our medical department is always on duty insofar as the man is employed in the plant, and in some of our departments where the health hazard is very serious the medical examinations are very frequent.

The next is vacations for wage roll employees, $2,503,000.

The next is vacations for salary roll employees, $1,309,000. I was criticized for leaving that item in this list because vacations with pay for salaried employees are so generally in effect that they have become almost universal, and many people do not regard them as an employment relations plan at all, but they certainly are in the same nature as the other items.

The next four items are of minor consequence, aggregating only $87,000, and I need not spend much time on them.

The next item, $7,593,000 is a large item. It consists of the payments under our bonus plans. There are two plans, or two parts to the bonus plan which we designate as the A bonus and B bonus plans. The A bonus is for spectacular performance or accomplishment by any employee, usually outside of his ordinary line of duty. The B bonus, which is the far larger portion, is for conspicuous service in the line of duty, which is felt to have contributed very materially to the company's success during the year.

Senator VANDENBERG. Do you have any idea how many persons are represented by way of participation in that $7,500,000?

Mr. DU PONT. If you look on the next page, Senator, there are some figures on that.

Senator VANDENBERG. If I am anticipating I will wait until you get to it.

Mr. DU PONT. I think it is further over in the text. Perhaps while it is in your mind I might give you those. It appears on page 8, about the middle of the page. You will see that for 1937, the reward having been made in 1938, there were 1,889 employees rewarded, of which 249 received "A" bonuses, and 1,640 received "B" bonuses.

Senator VANDENBERG. Out of the total of how many employees?

Mr. DU PONT. The total employees of both salaried and wage earners together were some 40,000-odd. Now all of those employees, both salaried and wage earners, are at least nominally eligible. There is no restriction on the eligibility for either "A" bonus or "B" bonus, except that any employee who has been in the service less than 2 years must have performed in a far more conspicuous manner than an older employee in order to receive consideration, and in the natural working of the plan it is true that a low-salaried or wage-earning employee is much less likely to receive bonus recognition because his opportunity to perform an outstanding service which contributes materially to the company's success is very much smaller.

Senator VANDENBERG. Could you personify the type of thing that is concerned in one of these awards?

Mr. DU PONT. Under the "A" bonus plan an invention, especially an invention that is out of the research department. If an operating foreman or supervisor, for instance, in the plant would make an outstanding invention, that would be the subject for an "A" bonus award. The "B" bonus awards are more for general outstanding performance in the line of duty, and that is judged by the man's superiors in consultation and in a group. The recommendation for an award is not in the hands of any one individual.

Senator VANDENBERG. How is the total amount of the award arrived at? Does your decision to distribute so much of this award depend upon the number and merit of those who are entitled to recognition?

Mr. DU PONT. The amount available for the "B" bonus is fixed by the finance committee under the plan. It must not exceed a certain sum, which has been fixed by the stockholders approving the plan. That sum is 20 percent of the earnings which remain after setting aside 6 percent on the capital invested. We set aside out of earnings a certain amount on the capital employed and then of the remaining earnings we distribute a percentage as a bonus not in excess of that amount, but the actual amount distributed is fixed by the finance committee in the amount of whatever circumstances seem appropriate.

Senator VANDENBERG. In relation to earnings?

Mr. DU PONT. Yes.

Senator VANDENBERG. I call that profit sharing on a merit-rating basis.

Mr. DU PONT. That is probably a very good definition. If that covers that bonus point, we will return to the bottom of page 4.

The next item is unemployment-compensation taxes, both State and Federal, $2,281,000, and old-age-benefits taxes, $967,000. There might be added to that list two other items which I thought better to leave out, however, namely, workmen's compensation for permanent injuries as distinguished from compensation while recovering. That amounted to $370,000 during 1937, and another item of safety work, which amounted to about $500,000, to prevent those injuries which result in compensation of various kinds. I will have something more on that subject, which I can go into now.

Referring to this safety work, in addition to the cost of the various industrial relations plans and policies of the Du Pont Co. as formally outlined, an estimated sum approaching $500,000 was spent in 1937 for safety work, which has for 26 years been an important feature of Du Pont policy, but which has not ordinarily been thought of as any direct addition to employees' compensation. However, it is a direct and voluntary expenditure by the company over and above wages and salaries, and the primary purpose of the expenditure is to protect employees to the greatest possible extent from the natural hazards of their work. The success of this activity is attested by the fact that whereas the frequency rate—I will stop a moment just to explain what is meant by the frequency rate. It is defined as the number of lost-time injuries per million of exposure hours per pay roll. There are about 2,000 hours a year, 40 hours a week, 50 weeks a year would make 2,000, and a thousand employees would be 2,000,000 man-hours of exposure to accident. Now, if that plant had suffered 10 accidents during that time, their frequency rate would be 5, that is, 10 divided by 2, 5 per million.

The success of this activity is attested by the fact that, whereas the frequency rate of American industry as a whole for the year 1937 was 13.85, the frequency rate in the Du Pont Co. was 1.85. That is, we had something like one-eighth, is it not, or one-seventh of the frequency of accidents that the average of American industry had. Since a comparable ratio has been maintained for the past 10 years, this figure is of significance.

It is a very usual record for industrial concerns to keep the frequency of their accidents and also other statistics, and it is usual to compare the statistics for different injuries in different companies, and there is quite a friendly competition to get the rate reduced.

Senator VANDENBERG. What do you mean by "safety work"? Is it educational, or is it competition?

Mr. DU PONT. Well, both. I think the success of our safety work has been more due to getting the men to take an interest in the problem themselves than through any ordinary educational work, or any accident guards, or regulations, or anything of that sort.

Senator VANDENBERG. Is there any cash incentive to avoid accidents?

Mr. DU PONT. Substantially none; no. We do have a competition among plants for which a prize is offered, but it is nominal in dollar value. We have been able to create a great deal of interest among the employees, and the supervisory force also, in this question of accident prevention, and that is what has done the trick. Our rate has been reduced to 0.1 of what it was comparatively a few years ago.

There is no question about something having taken place.

PRACTICAL RESULTS OF DU PONT POLICIES

Your committee may be particularly interested in the practical results of the personnel and managerial policies followed over the past decade, as shown by the increase in the number of employees and in the wages paid, together with the decrease in our average selling prices.

After reflecting back the effects of later acquired companies, the following comparisons between the year 1937, and the previous general business peak year 1929, are noted.

I would like to explain what is meant by reflecting back those effects. Since 1929, we have acquired, in some way or other, other companies, so the direct comparison between now and 1929 between earnings and in number of employees would not be a fair comparison. We have attempted to adjust for that in a more or less arbitrary manner; i. e., by adding back for 1929, the statistics of latter acquired companies.

The total number of Du Pont wage workers increased 28 percent, as compared with a decrease of 0.2 percent for all manufacturers. That is, from 1929 to 1937 we have increased 28 percent. Total wages paid increased 48 percent, as compared with a decrease of 7.6 percent for manufacturing generally; while *average* wages per hour increased 52 percent, as compared with an average increase of only 24 percent for all manufactures.

Because of the decline in the cost of living, the purchasing power of wages paid increased even more rapidly, so that our *real* total wages paid were actually 75 percent higher than in 1929; and notwithstanding a 20-percent decline in the number of hours worked per week the purchasing power of our weekly wages actually rose 38 percent.

At the same time our average selling prices declined 24 percent, as compared with a drop of less than 7 percent for the prices of "all commodities except farm products and foods," as reported by the United States Bureau of Labor Statistics.

These and other interesting relationships are shown in the following tabulation, which is offered for your further information. I think I need not read those figures in detail. The gist of them has been given in the earlier text.

Senator VANDENBERG. I suggest they be printed in the record, however, at this point.

(The figures referred to are as follows:)

	1937 compared with 1929 percent change	
	All manufactures	Du Pont
	Percent	*Percent*
Number of wage workers	−0.2	[1] +28
Total wages paid	−7.6	+48
Average wages per week	−7.4	+17
Average wages per hour	[1] +24	+52
Purchasing power of wages:		
Total	+9	[1] +75
Weekly	+9	+38
Hourly	+46	+79
Output:		
Total	−8.4	+49
Per wage worker	−8.3	+19
Per man-hour	[1] +15	[1] +51
Sales price	−6.9	−24

[1] Partially estimated.

Mr. DU PONT. Now there follow two or three pages of description of the various industrial relations plans in a brief way. Those are more completely set out in printed copies of the various plans which have been turned into your committee earlier along with the questionnaire.

Now I think that will complete my formal or prepared statement, Mr. Chairman. If there is anything I can do in the way of explanation, or touching on other points, I would be glad to do so.

Senator HERRING. As I understand, this increase of 20 percent in wage workers is in no way accounted for by the new companies taken over? You have allowed for that?

Mr. DU PONT. Allowed in both years?

Senator HERRING. Allowed in both years.

Mr. DU PONT. Yes.

Senator HERRING. It is really an increase.

Mr. DU PONT. But those industries which we have evolved ourselves during the interval, there was no adjustment for them.

Senator HERRING. No; certainly.

Senator VANDENBERG. I hope this definition of these various plans is going to be printed in the record at this point, Mr. Chairman, pages 6, 7, and 8 of Mr. Du Pont's memorandum.

Senator HERRING. Those will be included in the record.

(The matter referred to is as follows:)

Summary of more important industrial relations plans of the Du Pont Co. as of the end of 1937 (from information contained in the annual report for 1937).

1. The group life insurance plan, adopted 19 years ago, provides protection for the dependents of employees through a group life insurance contract with a leading insurance company. The amounts of individual insurance range from $700 after 1 year of continuous service to $1,500 after 5 years of service, with provision under certain conditions for the payment of the amount of the policy to the insured employee in case of permanent total disability. The entire cost of this plan is paid by the company. At the end of the year 45,539 eligible employees were holders of policies aggregating approximately $55,790,000.

2. The salary allotment insurance plan, in effect for 13 years, enables employees at their discretion to purchase, under favorable conditions, standard forms of life insurance as a further protection to their dependents beyond that afforded by the group life insurance plan. The entire costs of this insurance are paid by employees through monthly deductions of the premiums from wages and salaries. On December 31, 1937, the total amount of insurance carried by employees under this plan was approximately $22,600,000.

3. The group accident and health insurance plan, in force for 8 years, provides, after a 7-day waiting period, weekly benefits during disability due to nonoccupational illness or injury, for a maximum period of 13 weeks for any one disability. This plan is carried under a contract with a standard company, and the insurance is offered to all employees with 6 or more months of continuous service, on a contributory basis, at very low cost to them and without medical examination. At the end of the year 97.3 percent of all eligible employees were insured under this plan.

4. The disability wage plan, adopted June 15, 1937, provides, after a 2-day waiting period, payment of full wages to wage-roll employees having 1 or more years of continuous service, during periods of nonoccupational illness or injury, up to a maximum of 3 months for any one disability. Payments under this plan are in addition to benefits payable under the group accident and health insurance plan. The entire costs of the plan are paid by the company. Comparable treatment is extended to employees paid on a monthly salary basis through the medium of leaves of absence with pay.

5. The benefit plan, in force for 29 years, was originally adopted in order to provide employees having 15 or more years of continuous service with assistance during extended periods of nonoccupational disability; to supplement workmen's compensation requirements under certain conditions; and to provide relief for the dependents of employees who lose their lives in the course of their employment. This plan was broadened in its scope on May 19, 1937, in order to provide employees, having 1 or more years of continuous service, benefits for disability due to occupational illness or injury comparable to that afforded by the disability wage plan for disability due to nonoccupational illness or injury.

6. The pension plan, in effect for 33 years, provides monthly pensions to employees who become unable to work because of physical or mental incapacity after 15 years or more of continuous service. The entire costs of this plan are paid by the company. In 1937 a total of $620,789 was paid to pensioners under this plan, and as of December 31, 1937, the pension fund amounted to $22,001,174.

7. The vacation plan for wage-roll employees, in effect for 4 years, provides annual vacations of 2 weeks with full pay for wage-roll employees having 1 or more years of continuous service and satisfactory attendance records during the 12 months preceding their vacations. Comparable vacations with pay are granted to employees paid on a monthly salary basis.

8. The savings plan, in effect for 13 years, provides a convenient opportunity and an incentive for employees to save and to accumulate a fund for future investment. Any employee who has 6 or more months of continuous service, and whose annual earnings do not exceed $3,000, is eligible to participate under the plan at his discretion. Deposits in the savings account are made through monthly deductions from wages and salaries, and interest at the rate of 6 percent, compounded semiannually, is allowed on all deposits up to the maximum limit of $500. At the end of the year 7,040 employees had $1,149,587 standing to their credit under this plan.

9. Bonus plans in the company have been effective for the past 33 years. The A bonus plan is open to any employee in the company who performs conspicuous

services of a specific nature out of the ordinary line of duty. The B bonus plan is now open to all employees of 2 or more years of service, who, in their regular line of duty, have contributed most in a general way to the company's success by their ability, efficiency, and loyalty.

Early in 1938 under these two plans there was awarded to 1,889 employees a total amount of $7,593,000. Of this number, 249 received A bonuses, and 1,640 received B bonuses.

10. *Medical service.*—The company has a well organized medical division, providing medical service for all of its employees through full-time or part-time doctors. At the larger plants the staff of full time physicians will run as high as 6, while the total medical personnel on such plants, including nurses, technicians, etc., may run as high as 23. At present, in addition to the routine physical examinations, chest X-rays are made of all employees when hired, which fairly well assures a normally healthy employee at the beginning. Physical examinations at intervals ranging from 10 days to 1 year, depending upon the nature of the employment, make it possible to discover early symptoms of organic or other illnesses, thereby decreasing the time required for treatment and recovery, thus avoiding suffering and loss to employees from preventable illness.

Senator HERRING. Of course, you have organized labor to deal with, do you not?

Mr. DU PONT. Oh, yes.

Senator HERRING. As I recall it, you have not had any serious labor trouble.

Mr. DU PONT. No; I think it would be correct to say that we have had no labor trouble. I have been head of the company now for 12 years and there certainly has never been any strike or labor trouble that I recall, so there has not been anything very serious of this nature.

Senator HERRING. As to any of these methods, do you discuss them with the employees, or with their committees, or do you negotiate in any way?

Mr. DU PONT. Very frequently, in taking up the consideration of a new plan, we endeavor to get the reaction of the people who are supposed to be benefited before we adopt such a plan, but there is no formal submission to employees in any way. We regard these plans as a voluntary adoption, and although we want to know what the effect is going to be before we take the leap we do not feel that there is any obligation to discuss it with the beneficiaries. We have a great many suggestions from employees for work of this nature, or improvement in the plans.

Senator HERRING. You have workmen's compensation in the State, do you not? You have a State law on workmen's compensation?

Mr. DU PONT. I think there are laws of that kind in practically all the States, Senator. You see we are installed in a great many different States.

Senator HERRING. Yes. I was wondering if you received any credit on what they call the merit system for this low percent of accidents, or whether you are paying just as much as the employer who is having a larger percent of accidents?

Mr. DU PONT. I do not think there is any recognition of that. I do not recall having heard of it.

Senator VANDENBERG. There is in some States.

Mr. DU PONT. There used to be in the State of Washington, but that did not go by companies; I think that went by industries. There also was something of the kind in Wisconsin, I believe, but it seems to me that went by industries also. Different industries pay a different rate of tax, dependent on what the record of that industry is; but I do not think they ever carried it as far as the individual employers were concerned.

Senator VANDENBERG. Would not you think that was logical?

Mr. DU PONT. Oh, yes; it is logical. Naturally, there is a tax applied for an expense of that kind. Those that do not produce the expense certainly ought to be relieved of the charge, but I do not think it is a practical thing, Senator.

Senator VANDENBERG. I am trying to get you to say it is logical, because then you have to say incentive taxation is logical. I warn you in advance.

Mr. DU PONT. I think there is merit in that thought. It does seem logical, especially if you grant that the cost of government ought to be borne by those who are benefited by government.

Senator VANDENBERG. Certainly.

Mr. DU PONT. Not very many people recognize that, either.

Senator VANDENBERG. No; but if that is true in respect to a matter like unemployment insurance, I cannot see why it is not equally true in regard to any other spectacular contribution that an employer makes for regularizing and stabilizing employment. I grant you it is very difficult to effect a practical formula; but, speaking of the theory, I fail to see much difference between the two. It seems to me they are perfectly sound. Is not a tariff an incentive tax?

Mr. DU PONT. A tariff?

Senator VANDENBERG. Yes.

Mr. DU PONT. Why, I never regarded it as such.

Senator VANDENBERG. I rather think it is, in a broad sense. The purpose is to permit an employer to provide employment for American workmen.

Mr. DU PONT. I think that is stretching the idea pretty far.

Senator VANDENBERG. Well, all right.

Mr. DU PONT. I suppose that a tariff on one's raw materials is an incentive to our domestic material.

Senator VANDENBERG. Well, a tariff on chemicals is an incentive for you to put up a chemical factory so you can make the chemicals, so I think it is incentive taxation.

Mr. DU PONT. I think it is a little far-fetched. I think the weakness of incentive taxation is that government determines what is to be encouraged, and government may make an error in that determination with respect to a lot of different industries and a lot of different units, and the thing is really worse than that sounds, because after there is a demonstration given of the theory no one in industry knows what to expect next, and it is the fear of something that is going to happen that is worse than the thing when it does happen, in the way of killing the incentive to take business risks.

Senator VANDENBERG. Well, I suppose, speaking generally at the moment, their idea of government offering any incentive to business is so shockingly novel it is difficult to comprehend anyway.

Mr. DU PONT. Why, no, Senator, I do not think it is a novel idea. But novelty does not make it either good or bad.

Senator VANDENBERG. That is right.

Senator HERRING. Mr. Du Pont, could you give us, in a general statement without a lot of detail, any information as to the new products which your extensive research has developed and which have contributed to increasing employment and the general welfare?

Mr. DU PONT. Well, there are quite a few. I do not think they are all new, strictly speaking. They are new with us, and some of them are new to everybody.

Senator HERRING. We had some evidence here in the last 2 or 3 days that industry has done very little, if anything, they have developed to a very small extent, if at all, in new employment opportunities or resources, and the thought has been expressed that that is not true as to many of the major industries, including your own, that you have contributed to the general welfare and of course employment by developing it.

Mr. DU PONT. There is no doubt about that. I can refer you to our annual report for 1937, which has quite a little reference to the new industries. They are mentioned by name. This is only a short paragraph, and perhaps I might read it to your advantage.

Senator HERRING. We would be glad to have you do so.

Mr. DU PONT (reading).

In conformity with its general policy, the company endeavors to increase consumption of its patented and other new products by aiming at a low profit per unit on a large volume of sales rather than a high margin on a small volume. A review of 12 of the company's more important development lines over the past 10 years affords an interesting insight into the actual working of this price policy.

The 12 groups of products in question, with the year of introduction shown in each case for those not in production at the start of the 10-year period, in 1928, are as follows: "Duco" finishes: "Dulux" enamels (starting in 1930); neoprene (1932); synthetic camphor (1933); "Ponsol" dyes; anhydrous ammonia; synthetic methanol; urea (1935); titanium pigments (1931); viscose rayon; acetate rayon (1929); "Cellophane" cellulose film. These 12 lines accounted for about 40 percent of the company's total 1937 sales volume; and their production and sale are now directly giving employment to approximately 18,000 workers, as compared with about 10,700 employees in 1928 in the same groups of products. During the same period the company's investment in facilities for the manufacture of these products has increased from approximately $65,000,000 to approximately $174,000,000.

That is, it has required over $100,000,000 of investment to bring those products into active production and sale.

Senator HERRING. Well, then you have really made some contribution toward solving our unemployment problem during these years.

Mr. DU PONT. The mere putting of $100,000,000 in the plant means a good deal of jobs, but it has resulted in an increase of 8,000 directly employed people. It might be interesting to note the next paragraph:

The composite, or weighted average, reduction in sales prices for these 12 groups of products from 1928, or the year of introduction if later than 1928, up to and including 1937, has been approximately 40 percent.

I think that that is an interesting question, as to what employment has been furnished by new industries. You can see the thing working all around, but the extent to which that works is dependent on the amount of enterprise and enterprise capital that is available. You cannot go into a new industry on borrowed money or bank credit. Somebody has got to have the idea for the new thing and somebody has got to have some money that he is willing to take a long chance on and somebody has got to know how to do the trick, and that combination happens so seldom that we have, unfortunately, few new products brought out. It would be the finest thing in the world if we could just create enough new products and a demand for them. We would create more jobs than there are workmen. If you ever get into that situation, it would certainly be a utopia for labor, and there would be always a vacant job.

Senator VANDENBERG. I guess the only known scheme is a war.

Mr. DU PONT. That works temporarily.

Senator VANDENBERG. That is what I mean.

Mr. DU PONT. But it is awfully hard going, to be continually at war. That even applies in the home, you know, Senator.

Senator HERRING. If you have any further observations we would be glad to have them, Mr. Du Pont. I do not think I have any more questions to ask you.

Mr. DU PONT. Well, I do not think I have anything further, Senator. This memorandum I think covers the subject pretty thoroughly, together with the other data that we supplied your committee in that questionnaire, and the supplementary matter connected with it. We covered, it is true, briefly, but I think very thoroughly, and much to the point, our reasons for feeling that this principle of incentive taxation is bad. It puts into the hands of government, whoever the individual may be, the control or attempted control of affairs that are strictly business affairs, and therefore ought to be left in the hands of those who are responsible for the business and who are risking their money in the business, if for no other reason just for the sake of encouraging other people to put their money into some kind of a new venture. They are much more likely to do that if they have the feeling, thoroughly grounded, that when that venture started they would be able to run it themselves and not have to take some suggestions or orders from somebody else that may kill the whole thing.

Senator VANDENBERG. Why is that factor involved, let us say, in a tax credit for plant expansion or machinery replacement?

Mr. DU PONT. Well now, suppose the industry in question gets to too large proportions and for some business reason they think it should be shrunk, not expanded, then by not being able to get this tax reduction that industry is penalized.

Senator VANDENBERG. That is correct.

Mr. DU PONT. All those that expand get a rebate, but my business, that for good business reasons I cannot expand and must decrease, I must shrink it up somehow, I have to pay the penalty. Now that does not encourage me to go into some other line of business that may get struck by lightning in the same way. There are enough catastrophes happening without adding a whole series that may be imposed by governmental authority. It does not do so much harm to the fellow it would hit as it does in discouraging a thousand other people from taking a chance and going ahead. That is why we have no new jobs available, because too few people have courage to go into business.

Senator VANDENBERG. It all depends on the point of view. There appear to be literally thousands of those small employers in the country who feel they would be very greatly encouraged by some sort of tax abatement or reward, who would be very greatly encouraged to replace their equipment and modernize and expand their plants. That is their statement. From their point of view it would be a very great incentive and would not contain any of the discouragements that you are discussing.

Mr. Du Pont. No doubt any definitely suggested scheme for incentive taxation does appeal to a group of people, and maybe quite a large group.

Senator Vandenberg. Of course, the mere fact it appeals is no assurance it is sound, I concede that.

Mr. Du Pont. No. The reason it appeals to some will be the reason that it does not appeal to a number of others, because they do not happen to be in the peculiar circumstances that make that particular relief interesting, but I repeat that the fear of something which is coming along is more harmful than either the tax incentive or the punishment where it does not exist.

Senator Vandenberg. I can agree, speaking generally, with you. The fear of something else coming along is the thing that is holding business back.

Mr. Du Pont. And it really goes deeper than holding business back. It holds back people from saving up their money to go into business. What is the use of denying yourself what looks attractive and interesting if by that denial your savings are of no use?

Senator Vandenberg. Well, that is a general indictment of the fact that thrift has ceased to be popular under the new dispensation.

Mr. Du Pont. But incentive taxation adds one more straw to the load.

Senator Vandenberg. Of course, I am not agreeing with you on that.

Senator Herring. You may not call this profit sharing, but when you voluntarily distribute $20,000,000, or about 20 percent of the annual wage among employees in one form or another, it comes pretty close to profit sharing, does it not, even though it may be good business to do that?

Mr. Du Pont. There is no doubt about that, as to the distribution of that which comes out of profits, but profit sharing has come to be known in industrial circles very definitely as a plan of distribution to substantially all of the employees prorated to their hours or their wages, or something of that kind.

Senator Herring. Well, everyone in your employment benefits in some way from this, of course.

Mr. Du Pont. Why, surely, there is no doubt about that. They have all participated in the benefits in some respect.

Senator Herring. The larger employers that have profit sharing have all testified it was really good business, it has helped their profits, and that is one of the reasons they did it.

Mr. Du Pont. You understand, Senator, what my criticism of profit sharing, as I define it, is, that you put a lot of money into employees that does you no good. If you take a bonus system, you only put the money where it will do you good.

Senator Herring. You reward for merit?

Mr. Du Pont. You reward the fellow that does something for you. If you distribute your profits and bonus among all employees you reward the poor ones along with the good ones.

Senator Herring. Yes; I can see that.

Mr. DU PONT. In other words, you are scattering your shot and wasting it.

Senator HERRING. There is a point I tried to make a while ago. If wages are fixed in accordance with ability and merit and profits are distributed as a percentage of the annual wage, then there is, to some extent, that element of rewarding merit.

Mr. DU PONT. Yes. That reminds me of another point that I think is important, and I would like to call your attention to it. For manufacturing industry as a whole through its various stages from raw materials to finished product, about 85 percent of the value of the product, according to the United States Department of Commerce, was ultimately paid out to employees in a recent year ("National Income in the United States, 1929–35," p. 100). The remaining 15 percent must cover various overhead items such as taxes, insurance, depreciation, and so forth, in addition to return on the investment, or net profit, if any. On the average, there have been virtually no profits in manufacturing over the past decade, and even in the supposedly prosperous 20's the rate of profit in manufacturing did not amount to more than 5 to 6 percent of the sales value of the product. It is obvious, therefore, that a distribution of the entire amount of "profit" would have a negligible effect on the income of the average employee, although such a distribution would wipe out the entire return on the capital invested.

In other words, you have very little to work with, and the thing that people do not have in mind is that the profits of business are so small as compared with the wages. Labor in some form is already getting 85 percent of the whole, and you cannot afford to give them very much of the remainder, for the principal reason that by doing so you discourage anybody else going into business, and if nobody goes into business, why, it is just too bad for labor. It does not hurt the capital owners so much, because they can live on their capital, but the wage earner cannot live without his job. It is far more important for labor to have more capital invested than it is to have increased wages.

Senator HERRING. What percent of your dollar volume goes to labor?

Mr. DU PONT. Why, the figures are in here approximately. Our pay roll is $107,000,000, and our gross sales are about $300,000,000. That is the gross sales. Now we have to take our materials out of that. Now, our net profits were something like $53,000,000 for 1937, roughly one-half of the pay roll.

Senator HERRING. Your percent paid in wages to the dollar volume exceed that of many that have testified here.

Mr. DU PONT. Well, they jump all over the lot. I think our profits related to pay rolls are exceptionally high.

Senator HERRING. Yes.

Mr. DU PONT. I think that is due to the fact that we are in so many specialty businesses, where the invention, the idea, the development accounts for so much.

Senator VANDENBERG. Well, you spent $20,000,000 on profit sharing on the merit basis compared to about $50,000,000 net earnings, so as one who is critical of profit sharing you are one of the largest profit sharers I ever saw.

Mr. Du Pont. Think how well we would do if we believed in it.

Senator Vandenberg. It would be perfectly marvelous.

Mr. Du Pont. Senator, so that at some later time you will not get confused, in giving you these earnings or profits I have deducted from the figures in the report the amount that we received from the General Motors Corporation. You see we did not have any employees that brought that in; they are General Motors employees, but we got a very substantial amount in dividends from them, and I have eliminated them from the total shown, the total being around $88,000,000 and the General Motors portion about $36,000,000. The difference is about $53,000,000.

Dr. Lincoln has just reminded me of something that had a bearing on the last few remarks, that our investment in manufacture is extremely high. It is always high in the chemical industry, but ours is high even for the chemical industry. Therefore, in order to make a return on capital the profits have to be larger than they otherwise would.

Senator Herring. Do you have much loss from the loss of these chemicals because of careless handling by employees?

Mr. Du Pont. Why, I have no doubt that we have a good deal of that. At one time we made quite a study, to try to determine what that was and whether it could be avoided, but there is no way to find out what it is.

Senator Herring. I only mention that because one witness testified that by putting in a profit-sharing plan in reference to those handling high-priced chemicals he had reduced his losses and made almost as much money out of his savings as he had made out of the conduct of his business. He said that was due to the fact that he shared with those handling high-priced chemicals, acids, and so forth, the savings which he made over the past 10-year average.

Mr. Du Pont. That is a very sound principle, but it is very difficult to locate the loss, and to catch it when you do locate it.

Senator Herring. Well, I have nothing else.

Senator Vandenberg. Thank you very much, Mr. Du Pont.

Senator Herring. We appreciate your coming here. It was a very fine contribution.

We will adjourn until Monday morning at 10 o'clock.

(Whereupon at the hour of 3 p. m. the committee adjourned until 10 a. m. Monday, December 5, 1938.)

SURVEY OF EXPERIENCES IN PROFIT SHARING AND POSSIBILITIES OF INCENTIVE TAXATION

MONDAY, DECEMBER 5, 1938

UNITED STATES SENATE,
SUBCOMMITTEE OF THE COMMITTEE ON FINANCE,
Washington, D. C.

The committee met, pursuant to adjournment, at 10 o'clock a. m., in room 312, Senate Office Building, Senator Clyde L. Herring presiding.

Present: Senators Clyde L. Herring (chairman) and Arthur H. Vandenberg.

Senator HERRING. We will hear from Mr. Joseph M. Friedlander, treasurer, Jewel Tea Co.

STATEMENT OF JOSEPH M. FRIEDLANDER, TREASURER, JEWEL TEA CO., INC., BARRINGTON, ILL.

Senator HERRING. Mr. Friedlander is treasurer of the Jewel Tea Co. They have some 90 branches, as I understand it, in the United States, and they have had a profit-sharing plan for some 15 years. We would like to have you tell us, Mr. Friedlander, briefly, the history of your business, your profit-sharing plan, why you put it in, and how it is working.

Mr. FRIEDLANDER. Yes, sir.

Senator HERRING. Go right ahead.

Mr. FRIEDLANDER. First of all, I would like to say, if I may, Senator Herring and Senator Vandenberg, that we are very happy to cooperate with the work you are doing on this committee, and I personally feel privileged and delighted to be here to tell you anything I can.

Senator HERRING. Will you speak just as loudly as you can?

Mr. FRIEDLANDER. The Jewel Tea Co. was incorporated in 1916, in its present state, having been originally started in 1899. It is a business that operates in 42 States and the District of Columbia. We call it a Nation-wide business, delivering a line of quality groceries and premiums direct to the housewife through a system of motorized routes, and we also operate a group of stores in the city of Chicago and its suburbs. The company employs now a little over 3,600 people. We are proud of the fact that for more than 10 years we have given employment to more people each year than in the preceding year and in 1937 Jewel provided jobs for 1,311 more people than it did at the height of prosperity in 1929. We ascribe much of the credit for this to our profit-sharing plan and our general employee relations policy.

We have 90 branches, from which our 1,548 routes are supplied, and 109 retail food stores.

You probably are interested in the early history of Jewel, which is part of the reason for the profit-sharing plan which we have in operation today. In 1919, our company lost $1,847,000 on sales of 16½ millions. The following year it lost $2,180,000 on sales of 17½ millions. That was in 1920. In 1924, our directors adopted a profit-sharing plan, which is still in effect, and the second year after that adoption the company earned a profit of a million and a quarter on sales of only 14½ millions. In other words, it converted a loss of $2,180,000 on sales of 17½ millions to a profit of a million and a quarter on sales of 14½ millions.

Senator VANDENBERG. Was that just a *coincidence or was* that cause and effect?

Mr. FRIEDLANDER. We like to think, Senator, that it is partly cause. The company has continued on that road and has earned a profit every year since without exception, and the profit since 1926 has exceeded a million dollars in every year but one, which was 1933 and which was just under a million, $909,000. In 1920, prior to the adoption of the profit-sharing plan, the company was deeply in debt. It had 2½ million dollars in gold notes outstanding. It had bank loans of half a million dollars. There had been no dividends on the common at all, and the preferred-stock dividends were in arrears, and, as some of our officers sometimes say, it was kicking dust in the face of the sheriff. I remember the employees tell how they used to run over to the bank as soon as they got their pay checks so as to be sure they got their money on them. Today the company has retired all of the gold notes, all of the bank loans, cleared up all of the preferred dividends in arrears, and retired the preferred stock, so that today we have only one kind of stock, and that is 280,000 shares of common. Thus our capital structure is quite simple. Dividends have been paid on our common stock without interruption since 1928, and never at any rate lower than $3 per share.

Senator HERRING. Just what is your profit-sharing plan, Mr. Friedlander? How does it operate?

Mr. FRIEDLANDER. I was going to say, Senator, you would probably be interested in some of the philosophy of Jewel that led to the profit-sharing plan and its maintenance throughout these years.

First of all, our management believes that profit sharing is something over and above a fair wage structure. In other words, we think that wages should be a charge against cost of operation, and that wages should be set fairly and in keeping with competition, locality, and in proportion to the production of the individual, and within the company's ability to pay as soon as those things can be determined, and that sharing of profits should come from the earnings made over and above that cost of operation.

We put out a little booklet on our labor policy in which we have said that Jewel tries to put full wages in the pay envelopes of all employees, and it tries to provide 52 weeks of work every year for every employee in good times and bad, and the principle which our company has always followed and which it intends to continue if it can, is to make the weekly pay for each kind of work not only equal to the pay for the same kind of work, given by any other employer in the same locality, but to make it as much larger as the production of the individual and the prosperity of the company permits. On that principle our company has operated, and when we have had excess profits we have distributed them in a number of ways, not only under our profit-sharing plan itself but also under a plan which we called wage extras, or wage dividends.

Since our profit-sharing plan has been in operation we have distributed $2,521,000.

Senator VANDENBERG. That is since 1924?

Mr. FRIEDLANDER. Since 1924; yes, sir. In addition to that, we have distributed in wage extras, so to speak, $459,125. In the last 10 years for which I have more comparable figures on several factors, we have distributed under this profit-sharing plan $2,171,000, and wage extras of $459,000, plus salaries in accordance with this principle I have just mentioned of $40,289,000, or a total to the employees of $42,919,000, in the last 10 years. That figure, incidentally, is about 25 percent of our sales dollar, and about 300 percent of our net profits.

Now, as to the profit-sharing plan itself, under the plan we provide that a fixed amount be earned for the stockholders first, which is a base figure, and over and above that a definite percentage, 20 and 25, depending on the amount of profit made, is set aside for distribution to the employees.

Senator VANDENBERG. What is the base figure?

Mr. FRIEDLANDER. $770,000, which is about $2.75 a share.

Senator VANDENBERG. What would that be in percentage, dividend percentage?

Mr. FRIEDLANDER. We have no par. Last year, Senator, our dividends were $4.75 a share.

Senator VANDENBERG. On stock selling at what?

Mr. FRIEDLANDER. Seventy.

Senator VANDENBERG. $2.75 a share on $70 would be about 4 percent.

Mr. FRIEDLANDER. Yes, sir.

Senator VANDENBERG. That is what I am getting at. That is not a very heavy capital charge. You certainly cannot be criticized for that.

Mr. FRIEDLANDER. One thing I think that stands out, in looking over the record of our corporation, has been the effort of the management to keep things in balance. Rather than distributing extra dollars under the profit-sharing plan itself, when we earned extra profit in 1934, 1935, and 1936, we distributed them in the form of a wage dividend. We review the salaries of every person in the business twice a year. Every person's salary in the company is reviewed twice a year.

In an effort to keep our wages at the level we think they should be, we do the same thing with dividends and with prices to our customers. We have what we call a profit-sharing credit that goes to Jewel customers on our routes, and that credit has been increased over the years from approximately 10 percent to 18.9 percent last year on the amount of Jewel groceries that a customer buys. That is credited to her account, and she may use that credit in the selection of premiums. Thus you see we try to maintain a balance between the amounts distributed to stockholders, employees, and Jewel customers.

Senator VANDENBERG. Let us go into the profit-sharing plan now. After approximately 4 percent is paid on capital, then what happens?

Mr. FRIEDLANDER. Then 20 percent of the remainder is distributed under the profit-sharing plan.

Senator VANDENBERG. To all employees?

Mr. FRIEDLANDER. To all employees who meet a minimum service requirement, except those in certain food store departments and those whose compensation is related directly to their sales production by means of a commission scale. The sales force, including those engaged in direct selling as well as the sales supervisory staff—branch managers and assistant managers—are paid a base guarantee plus additional amounts depending upon their sales volume. Guaranties to salesmen vary in relation to the section of the country in which they work. If they work North their base guaranty generally is $1,170 a year for 52 weeks' work, and $1,092 a year in the South. Their compensation is increased above these amounts by varying percentages of their sales above a base figure. The profit-sharing plan takes in the executives, the home office employees, people in the main plant, branch offices and branch warehouses, including cashiers, stenographers, and stockmen, as well as traveling district managers, supervisors, and auditors.

Senator VANDENBERG. How do you distribute the 20 percent among them? What is your formula?

Mr. FRIEDLANDER. There is no formula. It is determined by a board of review and approved by the board of directors, and it is based on the employees' length of service and on their salary.

Senator VANDENBERG. In other words, it is an arbitrary assignment based on your best judgment of the merit of the individual?

Mr. FRIEDLANDER. Yes, sir. The sales forces, however, are guaranteed their base rate as a living wage, whether they earn it or not, and then they share in the profits above those figures through their adjusted pay based on sales.

You would be interested, I think, Senator Vandenberg, in that we are in some measure changing our profit-sharing plan, I should say, we are broadening it. We used to pay these amounts direct to the employees in cash. We started putting part of it in trust for them, and we had very good results from that. We found that a few people would prefer to have cash, and probably on first thought most of them would. I have asked them and their immediate answer would be that they would rather have cash, but our experience has been that setting aside something for the future seems to benefit not only the people but we think the company and society in general benefits from it, and the people, after we have gone back and asked them the second and third time, have liked it so much that we have extended it each year after we started it, bringing in a broader and broader group of people whose part of the profit-sharing is going into a trust, and our board of directors just last week adopted a plan, which has not yet been worked out in detail, but we are in the midst of it right now, working out the details, and in principle it will be the same plan that this one is. The base figure must be earned and then 25 percent of every dollar over that will be put into a trust by the company and it will be a separate corporate trustee. It must be a bank with a capital and surplus in excess of $5,000,000. I believe all the leading Loop banks in Chicago qualify. The trust company will be one of three trustees, that will be the corporate trustee, then there will be two individual trustees. The contributions by the company will be put in the trust, and in order to share in them we are putting in another new provision of employee contributions. Employees are to contribute from a dollar a week to $4 a week of their salary, and the funds will be paid to them on retirement. We are having a very low retirement age of 50, at the option of the company, and 57 at the option of the employee, and there will be provisions in the plan whereby, if an employee leaves before the age of retirement he will get all of his own funds back, plus varying percentages of the company contribution.

Senator HERRING. That is going to take the place of a cash profit-sharing plan entirely?

Mr. FRIEDLANDER. Yes, sir; we intend that to take the place of the cash payments. The sharing of the profits will continue on the same basic principle that we have maintained since 1924.

Senator HERRING. Will they be able to give up this cash profit which they have been getting and $4 a week in addition?

Mr. FRIEDLANDER. I think they will, Senator Herring, because we have had, in conjunction with our profit-sharing plan—that is, our so-called profit-sharing plan—another plan which I might mention. We call that a savings plan, a straight savings plan, in which the company has taken deposits and guaranteed 3 percent interest on the deposits. That fund has grown from, I think, less than 1 percent of the people the first year in the savings fund, to now over 70 percent of our employees that have deposits in the savings fund, and that fund has increased from $1,200 to $500,000. All of the interest that the securities earn in that fund is paid to the employees in addition to the 3 percent. One year, I think, they got 14 percent.

In addition to our so-called savings plan we have a number of welfare benefits. We have group life insurance, which the company has carried for a great many years on the lives of its employees, after having completed a minimum service requirement, at no expense to the employee.

We also have, in addition to the group life insurance, the sick compensation plan, and we for a great many years—I do not know how far back it goes—have given vacations with pay to our employees, 1 and 2 weeks, depending on their length of service.

Senator HERRING. That has all been in addition to the 20 percent?

Mr. FRIEDLANDER. Yes, sir. In addition to that we have given over the last 5 years an average of 4½ percent—I would like to refer to that figure to be accurate on it—in welfare benefits, exclusive of these other benefits I have just mentioned. I beg your pardon. It is 3.93 percent of the annual dividends that have been paid out in other kinds of contributions to the employees, special rewards for meritorious service and contests and campaigns, and so forth.

We have for years tried to report what has actually happened in the company to the employees. It started out, I think, 10 or 12 years ago, when the treasurer of the company called all the employees together and read what he called the common-sense balance sheet. He made up the regular balance sheet and then he prepared what he called the common-sense balance sheet, which would explain to the employees, in language that they could understand, just what the company had done. In 1936 we changed the form of it a little bit and we put out what we call a report to the Jewel family and sent it to each employee, in which we told them everything there is to know about the company, and we reduced the balance sheet to a personal basis and brought out the fact that each job has invested in it $2,875. We have carried that on, and I think probably will continue to do so.

Last year it took the form such as this [indicating]. We call it the "Business in a Basket" because the men on the routes carry their merchandise in baskets, and people in the Jewel food stores in Chicago shop with a basket, and so we call it the "Business in a Basket." We continue to report to the employees all of the vital statistics in the business, so each one can know just what is happening each year. They will receive under the new plan a detailed statement, so that they may know from that how they have helped in the production of the company's profit and how they share in it.

Senator HERRING. In arriving at the method and the amount of the various benefits, you have negotiated and discussed with the employees the form it should take and the amounts?

Mr. FRIEDLANDER. Yes, sir. In the development of this new trust fund idea of our profit-sharing plan, for example, we have been having meetings now for a number of weeks with representatives of the employees. We have an organization in each branch and one in our home office of the employees. They are called the Jewels, and they have chosen their own representatives. Incidentally, they have made some very constructive contributions to the development of this trust instrument.

Senator HERRING. How many employees did you say you have?

Mr. FRIEDLANDER. Three thousand six hundred.

Senator HERRING. Three thousand six hundred?

Mr. FRIEDLANDER. Yes; which, as I said before, is 1,311 more than we had in the peak of 1929.

Senator HERRING. Are any of them members of labor organizations?

Mr. FRIEDLANDER. Yes, sir. In the food stores, that is the only place in which they have their own union, but outside of that, they do not belong to any outside union. They are not affiliated with any national union.

Senator HERRING. None of them?

Mr. FRIEDLANDER. No, sir; outside of the food stores in Chicago.

Senator HERRING. Have they insisted on collective bargaining in arriving at any of these benefits?

Mr. FRIEDLANDER. No. We have always discussed it with them. We have had, I should say, very little labor trouble of any kind.

Senator HERRING. You have had no labor trouble since you put in this plan?

Mr. FRIEDLANDER. No, sir. Except in our Cleveland, Ohio, branch where, after a minority of our men had joined a local bakery drivers and helpers union we were notified they had been authorized to act as bargaining agent. Negotiations were started promptly and continued several months. Because their demands were such as to have resulted in a loss to the company and were impossible to meet, the business in that branch was discontinued. Our employees have been solicited and even threatened at times in other cities, but the Cleveland incident is the only one in which demands were made which required the cessation of operations. We have had no other labor trouble that I know of, of any kind, in our main Mid-West plant or home office headquarters.

Senator HERRING. Had you had any before?

Mr. FRIEDLANDER. No, sir; not to my knowledge.

Senator HERRING. Well, I think that is a fine statement. I am very glad to have you tell us your experience, Mr. Friedlander. If you have anything else, it would be of great value and interest to us if you would give it to us.

Mr. FRIEDLANDER. I could tell a great deal more about the company, but I do not think there is anything more of vital importance here, Mr. Senator.

Senator VANDENBERG. You consider, Mr. Friedlander, that all of these investments that you have made in employee benefits and in employee partnerships have paid their own way and have been a good business investment, do you not?

Mr. FRIEDLANDER. Decidedly so; yes.

Senator VANDENBERG. And, as I understand, you attribute a substantial part of your present success to the fact that you have pursued these policies?

Mr. FRIEDLANDER. Yes, sir; definitely so.

Senator HERRING. Thank you very much, Mr. Friedlander.

We will next hear from Mr. Henry Dennison, president of the Dennison Manufacturing Co., Framingham, Mass.

STATEMENT OF HENRY S. DENNISON, PRESIDENT, DENNISON MANUFACTURING CO., FRAMINGHAM, MASS.

Senator HERRING. I understand you have had a profit-sharing plan for a number of years, Mr. Dennison. There has been some report here that you have discontinued it.

Mr. DENNISON. It has discontinued itself, because our history has been almost the reverse of the Jewel. Our experience might prove the opposite, if I wanted to take the thing on its face value, as proving or disproving anything on profit sharing.

We started our plan in 1911. There are a good many special features connected with it, and I do not think it would profit us very much to talk of it in general. For instance, we have emphasized very heavily from the beginning managerial profit sharing. We emphasized from the beginning rather the structure of the corporation, the voting stock being held within the management group.

We had much more in our minds in the early days than what is ordinarily understood as profit sharing. We did extend, after the war, the same type of profit sharing, after a discussion of the matter by the employees, but almost wholly on an experimental basis, and personally I do not consider it has gone long enough to prove or disprove any effectiveness of that type of profit sharing.

Under our plan the profit sharing is primarily by the distribution of stock rather than cash. Our experience with cash payments has been about the same as the experience of Jewel, that is, that cash distributions had a great deal against them. Anything that favors a balance of construction generally is felt to be against cash distribution. That illustrates one of the main features in my own mind on this problem, that it is a very special and highly particular problem and to generalize is extremely hazardous. For instance there is a cash distribution profit-sharing plan in one of the best concerns in the country. Leeds & Northup, in Philadelphia, which has gone on for some time and nobody in the world can call it anything but successful, and yet I think you will find other types of experience in other places. It is sometimes extremely difficult to say why the scheme seemed to work all right in A company and will completely fail in B company.

Senator HERRING. Do I understand you correctly to say that when you did have that plan it extended only to the managerial force and not to others?

Mr. DENNISON. We went beyond the managerial force in the glow of 1919, and included the same type of profit sharing, that is by distribution of nonconvertible stock to manual workers over 5 years in our employ and operated on that basis continually from 1919 to 1930. The plan is still on paper, but since 1930 we have run into the experience that Jewel had some years ago, apparently, and we went into the red. If you want to connect the two things, which I do not think is good logic, why, after 19 years of experience with profit sharing we went into the red for the first time in our history. It could be said flatly that to me it is simply an illustration of the fact that one wants to be careful in making a statement of that kind.

Senator HERRING. Were all of the employees included in the plan?

Mr. DENNISON. The managerial group was included from 1911 to 1919, and all of the rank and file with over 5 years' service from 1919 on.

I think it is much more likely to say that the management of Jewel Tea Co. was extremely able and the management of Dennison Manufacturing Co. was extremely mediocre at least. I might argue that much more cogently than argue the question of profit sharing pro and con.

I saw right at the beginning that my appearance here would be of doubtful help, and it took some little persuading to come at all, because I do regard the matter as being quite special. To put in a plan in a company depends on the morale at the moment, and the background of the set-up, on what these employees are doing, what are their relationships to the profit account, as to whether it is remote or whether it is direct. For the typical worker in the factory our own belief is that his relationship is so remote from net profits, buying, selling, inventing new goods, advertising, all of the possibilities, to say nothing of the swing back and forth of the cycle of business, on the cycle of various styles, goods that come in and go out, that all those things intervene between the worker on the bench and the net profit account. The worker on the bench I say particularly, because if you are driving a milk route, or possibly in the tea route, your relationship may be much more immediate. It is pretty remote, and in trying to connect it up with our own company we said immediately, in proposing a plan, that we should not accept any factor upon production of the daily work.

Senator VANDENBERG. Mr. Dennison, is it not unfortunate that the connection between the manual worker and the profit motive is so remote; is not that one of the hazards of the economic system, and if there is anything that could make the manual worker more profit-minded, would not it be to the advantage and to the stability of the economic system under which we are trying to operate?

Mr. DENNISON. If we are in for more and more violent fluctuations, which we thought was likely for the last 40 years, when we first began to look into the business cycle, it looked as if fluctuations were becoming more violent and more frequent, if that is the case I very much doubt that you should want to have that connection. It might increase and intensify the swings quite as much as the other; whereas, if you have profit sharing for them of a more flexible wage basis—that is, if the wages go down in bad times and up in good times, you have got an intensification there. Possibly one of our stabilizing factors has been particularly wages in distribution, in retail or wholesale and the like, that it has been fairly stabilizing, and it has stabilized us somewhat during this period. I am not sure that it would be the case, but my point, Senator, is the actual physical relationship that the man can feel the cause and effect of it, that his efforts can do something to producing net profits, that it cannot be a very effective payment, not effective on his daily work. We believe that a bonus and properly arranged piece rates, and other similar incentives are much more effective than profit sharing would be. Profit sharing might have some effect on morale, but there are other factors that affect the morale of the employees. Foremanship, for instance, is one of the principal factors, and the whole industrial relations problem enters into the picture. I, myself, would hope that we would not raise too much expectation of the practical results of profit sharing in regard to the manual-worker group.

Senator HERRING. Is it not possible that the bonus and piece-work system might result in a speed-up?

Mr. DENNISON. No. It can be that, and it can be quite the contrary. That depends entirely, of course, on how it is worked out and how it is applied.

Senator HERRING. There seems to be quite a lot of objection to that on the part of labor.

Mr. DENNISON. It has constantly diminished, ever since the early days when it was forbidden by the Congress in the arsenals, the objection among the workers has diminished steadily. Many of the larger unions insist on setting these rates and demand them. Others, of course, have not been habituated to that, and object. It depends entirely on the technique of working it out.

Senator HERRING. I notice there is a strike in Detroit now because of piece work.

Mr. DENNISON. Very frequently, on its first introduction, if it is too suddenly introduced, or if it is inadvisedly introduced, there will be difficulties, and you will not have those difficulties later on. We have always, for years and years, in setting such rates taken care to see that they are jointly set, and they are subject to review by representatives of the employees. I am talking about properly set rates on a more immediately related effort to reward, and I think that is very necessary. If they feel this reward is remote and accidental you will not get then the morale effect of profit sharing unless it happens you have very irregular profits.

Senator HERRING. Are your employees organized?

Mr. DENNISON. Some are and some are not. There are unions for some and there are not for others. We have had an employee representation plan since 1919, and joint and collective bargaining has been going on since 1919, when the shop has actually organized itself, but there are also outside unions within the shop, wherever there is a craft that allows it. For most of the workers there have not been unions until the last few years.

Senator HERRING. Having the profit-sharing plan or not having it, has that had anything to do with any labor troubles that you may have had?

Mr. DENNISON. Not in the least. There is no relationship at all. We have not had any strike since 1903, at which time we had a short strike that taught us a good deal, as to whose fault it was. We have plenty of labor troubles, but that is to be expected. We also have selling trouble and customer trouble. That is what human relationships partly are, and we assume we are going to have them, and we set up a special department constantly to deal with those problems and attempt to keep them at the small stage. So that they have not come to any explosion point yet, although that might happen at any moment as it might anywhere or to anyone else.

The first question you ask indicates that profit-sharing might be thought of as simply a contribution to a fund, like a dismissal-wage fund, or disability or vacation plan. Where profit-sharing is some payment, contribution, or renewal of a fund, or whatever it might be, or cash payments, that it depends on your profits, that they may be more if you made more profit and less if you had less, and none if you had none, that is much more complicated, it seems to me, and if you could separate those two, the problem could be more easily faced. In other words, your practical proposal, as I understand it, is possibly some device, through an adjustment of taxes, so that these things might be cultivated and encouraged. I cannot see why, to encourage the development of a fund, whether your contribution to that fund could be called profit sharing or not, if we make that regularly anyway. We did have an unemployment-relief fund that we started in 1915. It really was a seasonal unemployment relief proposition, and when we came into the true unemployment in 1930 and 1931, with thousands of people laid off and the rest of them on part time, we found in spite of the fact we were making less, the pressures on our own judgment, on our hearts, if we had any, were such that we had to pay dismissal wages. The unemployment fund was used up at that time. It was inactive, because there had been too much unemployment for it, and yet in that time we thought the actual dismissal without the 2 weeks' payment at least was just too raw for even our hardened nerves. That was definite sharing, that was very definite financing in those years, when we actually paid dismissal wages. Now, that was a payment for that kind of purpose, vacations, or additional unemployment compensation.

Many English companies still add to the unemployment relief. There would be many possibilities in those fields, and I suggest that they be considered for cultivation, for encouragement, whether they happened to be profit sharing or not. Profit sharing, to my way of thinking, is so complicated, so difficult in its worth-while applications, so much a matter for special diagnosis in each case, it would be terribly difficult to find what would be the best profit-sharing scheme that you would want to cultivate.

Senator VANDENBERG. I think we can agree with you on that, Mr. Dennison. The only purpose we have is to create a record which the employer, at his option, can consult, to see where the merit is and where the pitfalls are.

Mr. DENNISON. That is very decidedly worth while, because there is a reviving interest in profit sharing in the last year or two. You cannot very well have profit sharing if you do not have profits to share. It is now beginning to come back with renewed interest. I think it is very desirable to have every record possible as to the pitfalls and the helpful factors, to have as much analysis as possible, to show where they actually lie.

Senator HERRING. Do you think there is any value in the compensatory tax rewards or incentive taxation?

Mr. DENNISON. I think it would be of some value, but it seems to me not a very important matter, hardly important enough yet to have it get into the tax system as an exception. It would be highly valuable certainly in the development of talks, that is the one place it seems to me that it might have its place, but it would not seem to be nearly as important as a thoroughgoing study of this subject. That is very much more important than the tax submission either for pensions, or anything of that kind. I would not speak against it, against the remission of taxes on such funds, but I would not make it a major issue of any moment, because I think it is not of maximum importance, or nearly so much important as the study that you are making.

I hope in the study there will be enough developed to warn against undue expectations. That is, does profit sharing stop strikes? I think that probably profit sharing alone, perhaps, never did. The same type of mind and consideration to the personnel problem that might develop a profit-sharing scheme in a company might also develop a good, sound personnel policy which would make strikes less likely. The proposition that profit sharing itself did stop strikes, I think, is wholly doubtful.

In your questions here, would that change the attitude on the destruction of the employer's property, the preservation of his own property? I think that is too remote. It would be silly to think that the employee would think of the property of the employer if his Irish got up high enough. Your questions would indicate the possibility of raising the expectations too highly.

I say it is rather an intricate and delicate question of management. I think it is enormously more important to have effective foremanship, educated, considerate, understanding foremanship than just to have any scheme of profit sharing that could ever be worked out.

Senator HERRING. You do not think there is a place for profit sharing then?

Mr. DENNISON. I think it should be understood as a helpful device, but not as a main lead. I personally have known, of course, since 1911, a good many bitter disappointments that never should have existed if the men had analyzed the situation fully to begin with. If he did not expect anything he would not have been disappointed. I think it has done a great deal of harm. I put in this profit-sharing scheme and the blankety-blanks struck. Well, the strike was probably materializing long before it was put in, and the profit-sharing scheme could easily be felt as a red herring, as something that might be put in as a defense against them, and that would immediately probably incite to riot more than it would quiet it. I think you have heard that point of view from labor. It has frequently been expressed and it has frequent justification in history. I do not think it is valid against all types of profit sharing by any manner of means, but it is something to be looked out for.

Senator VANDENBERG. I am very glad to have your warning on the record, Mr. Dennison, because I think we need warning as well as stimulation.

Mr. DENNISON. I think we would get a great deal further by viewing this matter from the technical standpoint, with less violent enthusiasm than I have known some people to go into it, with lower expectations, to work out a scheme that will be the right one under the precise circumstances, and then handle it right. If it is to be badly handled, it is better not to do it at all. I hope ours will come back into activity. As I say, it is still on paper, because our profits have not come back sufficiently to pay for 1931 and 1932 yet. I hope you go on continuously in the experimentation of profit sharing until we do find a scheme which will work, but I believe we shall have to find out more about the whole art and the whole technique.

Senator VANDENBERG. Thank you.

Senator HERRING. Mr. Chapman.

STATEMENT OF T. S. CHAPMAN, CHAPMAN & CUTLER, 111 WEST MONROE STREET, CHICAGO, ILL.

Senator HERRING. Mr. Chapman, I understand, passes on all of the bond issues that are sold out my way, in my part of the country, and I suppose you can tell us how the utilities can share profits when they do not have them?

Mr. CHAPMAN. Senator, I can not. We are lawyers, you know, and not industrialists. I do not know anything about profit-sharing plans. I naturally have done a little thinking about it, I suppose maybe more than some. I remember near my native town of Jerseyville, Ill., in Leclair, over in Madison County, where there was a large industry manufacturing plumbing supplies, operated by a very fine man, Mr. N. O. Nelson. He conceived that there ought to be some profit-sharing plan, and the interest of the employee in the business and success of it should be encouraged, so he decided to raise the wages of the whole body of employees, the labor, and to invest the raise in wages in stock of the company. I understand that he had a strike immediately for the raise in cash. Maybe I thought of it more by reason of this experience, because the lad that I visited sympathized with the troubles he had. He had a great deal of labor trouble.

Senator HERRING. I would be glad to have your expressions, Mr. Chapman, upon any phases of this survey that may occur to you.

Mr. CHAPMAN. It seems that whether or not profits are enjoyed in the operation of any business depends upon the intelligence of the management and the courage and ingenuity of a few of the employees, relatively few. They are prompted to exert themselves, those men that are endowed, so they can exert themselves emphatically by an expected profit. In a large way, profits are the results of ingenuity, courage, and hazards and should go to those men who produce those results. Now, the labor at the bench, in the broad way, does not produce the results.

Senator HERRING. You would be interested, I think, in the statement made by the head of a big organization here the other day, employing 15,000 men, with 38 years of experience, in which he said the vast improvements which had been made in their methods—the savings and economies—had not come so much from the front office; it was from the shop, where the man actually doing the work could see the opportunities for these improvements.

Mr. CHAPMAN. That is true. In an established or going business, or rather, lines of industry that are known throughout the years and generations, the improvements of those must necessarily be in the minute details of manufacturing and handling, and I imagine if you get into the minutia even of them you would find those suggestions emanate from superintendents, bosses, and other men who ultimately, in the next generation, will be the dominant factors of those industries. They are the thinking men. It is just pure human nature. If the superintendent comes to the head office and says, "We can save one operation by resetting this machine," the old man is going to bear in mind that that fellow is an observer, has some ingenuity, and ultimately he is going to sit up along with the old man.

Senator HERRING. Would you care to express yourself, Mr. Chapman, upon this question: What would you think of promoting, as a deduction from taxable income, the amount expended for labor and wages by increases, and the payment to the employees of the amount of such taxes as a dividend?

Mr. CHAPMAN. I doubt whether today any contributions made by corporations are not a deduction from gross determined taxable income.

Senator HERRING. Would you think a plan of that kind would stimulate industry?

Mr. CHAPMAN. No; because I think it is already in effect. I think any special dispensation or special deduction is going to operate either as a preference or an exception in the law to particular parties. That is bad. Taxes should be as nearly equal as they can be.

Senator HERRING. You would not favor compensatory tax benefits, then, to assist companies in installing profit sharing?

Mr. CHAPMAN. To the extent that it can encourage it, it already does, because they are deductions from gross in order to determine that today.

Senator HERRING. You do not think any additional tax benefits, or incentive taxes would be of value in the encouragement of profit sharing and benefits that might come from profit sharing?

Mr. CHAPMAN. I think it would be a little, but I think it would be overbalanced by the preference or exceptional position that one taxpayer would occupy as against another. It would create more discontent.

Senator VANDENBERG. That same criticism, Mr. Chapman, can be leveled against merit rating in workmen's compensation laws and in unemployment-insurance compensation laws.

Mr. CHAPMAN. I say that expense of operation is deductible.

Senator VANDENBERG. The merit rating permits the employer with a good record to enjoy a lower contribution, tax contribution, than the employer with a poor record.

Mr. CHAPMAN. I am sorry, but I do not get your reasoning.

Senator VANDENBERG. For instance, under the merit rating system in the Wisconsin unemployment-compensation law, the employer with a steady record of employment is treated more favorably than the employer with an unstable record.

Mr. CHAPMAN. That is true.

Senator VANDENBERG. Is not that all right?

Mr. CHAPMAN. I think that is all right in that case.

Senator VANDENBERG. Then there is a point at which it is all right to have the tax law?

Mr. CHAPMAN. That has already been demonstrated. That is already included in the cost of operation.

Senator VANDENBERG. We fully understand that. We are talking about an additional incentive.

Mr. CHAPMAN. I think that would be a special preference, that would be liable to put one employer in a preferred position as against another.

Senator VANDENBERG. Why is not the merit rating that we have just been discussing preferential?

Mr. CHAPMAN. It is very minor in amount, and it is determined upon a past history, the Federal income taxes, and annual determination.

Senator VANDENBERG. I am discussing with you the principle of discrimination. I am not quarreling with you; I am just interested in your point of view.

Mr. CHAPMAN. I understand.

Senator VANDENBERG. You are asserting there is no tax, preferential tax, which creates what you call a discrimination that is justified.

Mr. CHAPMAN. I think it would be very hard to design one.

Senator VANDENBERG. But we were discussing whether or not it is justified. You are asserting that it is, as I understand you.

Mr. CHAPMAN. I said I have very grave doubts whether it would be justified. We do not, any of us, know what is going to happen in the future. We can only have judgments.

Senator HERRING. If you have any other observations, we would be glad to have them, Mr. Chapman. We are not looking just for favorable evidence. We are glad to have these objections.

Mr. CHAPMAN. It always has seemed to me that industry is really dependent upon a very small percentage of men, because only a small percentage of men are endowed to be good administrators, good executives. It is awfully hard even to get a good shop superintendent. They are relatively rare. If we are going to better our conditions of living, it is going to depend upon those men who are able to better it, and, in a broad way, those are the men that should be encouraged and thus raise the living of the masses.

Senator HERRING. I have found some difficulty in finding good lawyers, too.

Mr. CHAPMAN. It is very hard, sir. I have employed a good many, and it is very difficult.

Senator VANDENBERG. Good Senators are equally difficult to locate.

Senator HERRING. They were not until a few years ago.

Mr. CHAPMAN. There was a good deal of truth in life in the story about the soldier that kicked the rabbit out of the way and said, "Let somebody run that can run."

Senator HERRING. Thank you very much.

Mr. CHAPMAN. I am sorry I cannot help very much.

Senator HERRING. You have helped very much. Mr. Hazelett, president of the Hazelett Metal Co., New York.

STATEMENT OF C. W. HAZELETT, CHAIRMAN OF THE BOARD, HAZELETT METAL CO., NEW YORK, N. Y.

Senator HERRING. Mr. Hazelett, you are president of the Hazelett Metal Co.?

Mr. HAZELETT. Chairman of the board.

Senator HERRING. You are the author of I. T., are you not?

Mr. HAZELETT. Yes.

Senator HERRING. I want to thank you for the copy you sent me.

Mr. HAZELETT. I hope you enjoy it. Would you like me to discuss my viewpoint?

Senator HERRING. Give us a brief description of your company, its operations, any profit-sharing plans you may have, and your interest in incentive taxation.

Mr. HAZELETT. May I say, my prime interest is in the making of profits, and then in profit sharing. Incentive taxation is an idea which I have studied for many years, and finally committed to writing in the hopes that it might solve the problem of profit for all of us, both management and labor. The book that you mentioned, the title of is not really a new idea. Incentive taxation is practiced by the policeman when he gives you a ticket for speeding; it is an incentive to promote better driving. Looked at the other way, it is a punitive tax for bad driving. In my opinion, incentive taxation as a policy offers the opportunity for solving the problems of unemployment and balancing the Federal Budget, and the solution of many of the essential problems of the country at the moment.

In my opinion, all democracies are going to fall if they do not find a permanent solution to the problem of unemployment. Every democracy in Europe has practically disappeared for one reason and one reason alone, that is, that they have failed to solve the problem of unemployment for their people. France is almost on the point of going into a dictatorship for the same reason. The two great democracies which are left, England and the United States, are not in any too good a position with respect to the dictatorships of the world.

In my opinion, this committee has the opportunity of getting at the very basis of this problem by means of incentive taxation not only of making profits but of sharing them. I define incentive taxation as a policy of reducing tax rates which are now high on all forms of productive property as its use increases.

All business is engaged in making a profit. Incentive taxation makes it possible, if properly applied, to make it profitable, or more profitable to be in a high rate of production and less profitable or more expensive for business to be in a low rate of production.

The problem of this country, both economically and politically, is to put our men, our property, and our money at work for as long as they remain at work there can be no depression. Now, there is a peculiar thing about an industrial civilization, which Senator Vandenberg will recognize as it applies in his State. An automobile manufacturer in Detroit cannot function, it cannot employ its normal quota of men unless a thousand other industries are in production at the same time. The steel industries have to be at work, the glass plants have to be in production, the railroads must be hauling freight, money must be in circulation, and the customers of the automobile business must be in production in order to be able to buy the product of that concern. That looks like a large problem.

In order to solve the problem of unemployment, we must find some power which can be exerted over every single one of those producers, and if you will look into the division of our form of government, or any other form of government on the face of the earth, you will find there are only two departments which can exert any real power except force. There is, first, the judiciary, which can carry out its power by means of a fine, which is one form of punitive taxation. The other department, and the only department that has any real control, that can exert real pressure over all of these productive facilities, is the tax department. Now, the only way you can use taxation to promote a high rate of production is to make it more profitable to be in a high rate of production than not to be.

Since we already have a high rate of taxation on every kind of business, I suggest that we reduce the tax rate on all business as it increases its employment toward its capacity, as an incentive to do this job. This will require a lot of explanation and I want to discuss it briefly, with respect to its effect upon the major classes, that is to say, labor, business, Federal revenues, and then as to profit sharing.

We have two problems. We have the "haves" and "have-nots." For the "haves" it is a reduced tax rate, and for the "have-nots" it is permanent employment, so they can have something and become one of the "haves." It cannot be done by any other process that I know of.

That is the problem, both economically and politically in this country. To gain support you must offer something which will reduce tax rates for the "haves" and which gives employment to the "have-nots."

I want to give you the logical application of this, as I see it, and I have taken the trouble to have a few forms printed which indicate how this might be done. If the committee would like to have a pair of these to look at it while I discuss them, I think it might add to the clarity of the discussion. One is just a rough draft of the proposed corporate tax return for incentive purposes, and one of the individual tax return.

PROPOSED INDIVIDUAL INCENTIVE TAX RETURN

1. All disbursements for personal or family use during year		------------	------------
2. ------% of value of all real property, not used for business purposes, less mortgages		------------	------------
3. Total real income (add items 1 and 2)		------------	------------
4. Personal exemption	------------		
Credit for dependents	------------		
5. Total exemptions	------------		
6. Taxable real income (item 3 less item 5)		------------	------------
7. Tax rate per table I		------------	------------
8. Income tax (item 6 multiplied by item 7)			------------

TABLE I

Taxable income Item 6	Tax rate per centum Item 7
$2,500.00	8
5,000.00	12
10,000.00	18
20,000.00	27
30,000.00	40
40,000.00	60
50,000.00 or more	90

INCENTIVE TAX

9. Average monthly cash balance	------------	
10. Disbursements for all purposes	------------	
11. Turnover rate (item 10 divided by item 9)	------------	
12. Incentive tax (item 9 multiplied by rate table II)	------------	------------
13. Business and social security tax, ------% of item 10		------------
14. Total tax (sums of 8, 12, and 13)		------------

TABLE II

Turnover rate	Incentive rate
½ or less	8
½—1	4
1—2	2
2—3	1
3 or more	0

All figures are indicative only

PROPOSED CORPORATE INCENTIVE TAX FORM

1. Average monthly cash balance during taxable year	------------	
2. Real disbursements for all purposes	------------	
3. Turnover factor (item 2 divided by item 1)	------------	
4. Incentive turnover tax rate per table I	------------	
5. Turnover tax (item 1 multiplied by item 4)	------------	------------

(NOTE.—If item 3 exceeds 3, item 5 is zero)

TABLE I

Turnover factor	Incentive tax rate
½ or less	8%
½—1	4%
1—2	2%
2—3	1%
3 or more	0

INCOME TAX

6. Maximum man-hour capacity per annum------ ------------
7. Man-hours actually worked during year----- ------------
8. Employment factor (item 7 divided by item 6)- ------------
9. Incentive income tax rate per table II------ ------------
10. Net income---------------------------- ------------
11. Income tax (item 10 multiplied by item 9)---------------- ------------
12. Total tax (sum of items 5 and 11)---------------------- ------------

TABLE II

Employment factor	Incentive tax rate
Less than 50%	24%
50—60%	21%
60—70%	18%
70—80%	15%
80—90%	12%
90—100%	9%
More than 100%	30%

NOTE.—Item 6 to be determined at the beginning of each taxable year by the taxpayer and can only be changed during the year with the consent of the commissioner and because of a change in the productive facilities owned by the taxpayer corresponding to such change.

Since idle surpluses, capital gains, and excess profits are taxed as above it is proposed to eliminate these taxes on the adoption of Incentive Taxation.

All figures are suggestive only

The logic of this thing—I want to repeat for emphasis, and I may mention it more than once—is that we must find a power which applies to all of these productive facilities. There is only one power in the Government, and that is the tax power. The only way it can be used to promote continuous production is to reduce tax rates, to make it more profitable to be in high rate of production, and it means a high tax rate, which we already have, for business, which is in a low rate of production.

These forms which I have given you show two items. I will take the income tax at the bottom first. I ask industry to state its practical man-hour capacity, and at the end of the year to state its actual man-hours employed; divide one into the other to get the percentage of capacity at which the firm operates, and the more nearly its capacity it operates the lower the income-tax rate. This is intended as a Federal form. I do not want to take any responsibility for the figures because I do not have sufficient information to even suggest them, but I believe we might even decrease the tax rates from present rates on business 50 percent if they were in full production.

I will discuss that from the standpoint of Federal revenue in a moment. I want to call your attention to the fact that idle property of any kind is of absolutely no value to the owner. If it is money which is idle, it does not bring him any interest, or bring him anything which he might ordinarily purchase with his money; when it is idle, it is of no use to him.

Senator HERRING. It would be much more difficult for him to pay the tax if he operated at low capacity than at full capacity.

Mr. HAZELETT. He is paying the high tax now because he is operating at low capacity. He is paying the high tax in order to support the people that are idle because his facilities are idle. When those men were at work for him they earned something for him, and now he supports them just the same through high taxation, but the only thing he earns from those people is their enmity. Idle money is of no value to the owner. The idle factory, or part of an idle factory has no value at all to the owner. That applies to idle men, idle buildings, and so on.

By bringing pressure on not one form but every form of business, through taxation, to be in a high rate of production gives us everything that business requires.

I might say that I am a sort of Mr. America. I was raised on a farm, I still operate a farm. I worked in the mills as a worker and I still don my coveralls regularly in my shops. I have handled a substantial amount of money. My business is engineering. I have done some manufacturing, and I have spent much time, like other Mr. Americas in the past few years, in making out tax returns. I shall speak as a manufacturer and a farmer for a moment.

First, as to the unemployment problem. No one can give jobs but the taxpayer, that is those people who have money and who have productive property. The only time they will give men jobs is when it is more profitable for them to do so than not to do so, so I propose, first, that we reduce the tax rate on business for increasing employment.

Second—and this will take some explanation to make clear—I am sure you will agree with me when you see what I mean. I propose a tax on what I define as idle money. In both the corporate and the individual tax returns you will notice these items. The taxpayer is required to state his average monthly cash balance, and to divide that into his total real disbursements for all purposes through the year, to get the turn-over rate of his cash. If that turn-over rate exceeds a certain point there is no tax; if it is less than that, there is a tax on idle money.

I hope you will not form your judgment regarding this until I present a few facts in that connection, because I know this is a rather radical suggestion. I want you to see how it is to the advantage of the man who owns money, and to everybody else.

I said the only people who can give jobs are taxpayers. We have in this country methods of creating money which is substantially counterfeit by raising prices, by money being loaned by banks to the Government to finance materials which are destroyed by war, by money being loaned by banks to finance relief, which produces nothing. The money is in existence but there is nothing to buy with it, and when money is created as it is under these processes, without anything to buy with it, that money is counterfeit. The result is we have artificial prices, and then capital proceeds to strike for artificial income, just the same as labor strikes for artificial income. The owners of money insist on 6 percent as the minimum money rate, just as the employee insists on a certain wage or he does not use his hands, just as the landlord insists on certain rent or he lets his property to lie vacant.

I want to call your attention as to how this may affect the working conditions of labor, as it will promote jobs in such a way that jobs are created, and that is by the men who have money spending it for something. Not in any other manner can jobs be created.

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So I propose the tax on idle money, to require the man to use his money, to bring pressure on him to use his money for his own benefit as well as others.

Now, the real wages of labor does not mean so many dollars a day. You and I know what happened in Germany when they were paying a man a million marks a day. They were not real wages, because the real wages in any group of labor are the products of other groups of labor. They had no purchasing power. The labor of a man in an automobile factory is really paid for by the product of other labor, which is food by the farmer, clothing by the textile workers, refrigerators, automobiles, furniture, gasoline, and what not. His real wages are the product of other labor. Therefore, his real wages cannot be increased by any means in the world except to increase production, nor can they be maintained without maintaining production. That is the purpose of incentive taxation.

You will find that the curves of wages go up just a few months behind the chart of production. Why? Because real wages are the results of production. Production has to be raised first before dollar wages can be raised. The only way production can be raised is for men, money, and property to go to work. You will find that wages have always been the highest when production was the highest. They fall in spite of all the union scales in the world when production goes down, because real wages are production.

We have certain union men who draw very high wages today, but if you look in their homes, look at what they have. They are supporting their father, who is perhaps over 50, because he is too old to get a job when there are few jobs; you will find he is supporting his children because they are unable to get jobs, most of the youngsters have never worked; you will find him supporting his daughter because her boy friend cannot find a job so he is able to marry her and take her off his hands; you will find that his living standards have not increased even in spite of the high wages. These idle people have to be supported by the man who has work. If they were producing he would get some of the benefits of their work, but now he is doing all the work and having to support these relatives either directly or through taxation indirectly.

I want to take up the question of technological unemployment briefly. There is a perfectly clear answer to that question: If an inventor—and I work in the field of labor-saving machinery—makes and develops a machine which, let us say, will supplant $100,000 worth of labor per year, the inventor may make $5,000 or $10,000 of that as royalty, the manufacturer may make $40,000 or $50,000 as extra profits by the use of this process, and the customers may get the product at slightly lower prices and thereby save a substantial sum of money for a given quantity of the product. There is a perfectly clear-cut solution of that problem if all of us are required to use the money which we save or which we make by this process.

Let me illustrate. If I let my royalties accrue, if I let my cash balance build up, as practically everybody has been doing in recent years, and if the corporation that uses the process permits a surplus to build up as an idle surplus, and if the customers of the business do not use that extra money which they have saved by buying the product at less cost, we find we have about $100,000 worth of labor out of work by this invention. But if I, as the inventor, am required to use my royalties, if I am required to go out and buy something which puts people to work, and if the corporation is required to use the profits which it accumulated and not let them lie idle, you immediately find a demand for the same amount of work some place else corresponding to the profits, and if the customers who have saved a certain amount of money do not use it for building up their bank balances, such as they have been doing, if they are required to use that by incentive taxation, you will find just as many men put to work either in increasing the production in that field because of the lower cost and wider markets, or in some other field, immediately that that money goes to work, and we would have all the advantages of the automatic machine. Gentlemen, the solution of the problem of technological employment is strictly an incentive tax on idle money. It is a complete answer, in my opinion, to that problem.

Senator HERRING. What distinction do you make between the punitive tax and incentive tax?

Mr. HAZELETT. A hill looks up from the bottom and looks down from the top. What I said about incentive taxation and the policeman awhile ago is probably as clear a statement as I can make on it. We already have a punitive tax in a sense, because we are now taxing the men who are producing to support people who are idle. We penalize a man, and we increasingly penalize him in proportion to his service to the public. I want to take that up a little more in detail in connection with profit sharing.

So by the process of incentive taxation you require money to be at work to give jobs, you require factories, in order to reduce their tax rate, to get in the higher rate of production. No manufacturer likes anything so well as the condition of maximum production of his customers, of his sources of raw material, of transportation and the like, nor does he like anything better than the fact that people are spending their money instead of hoarding it either in the sock or in the bank. If you can put these men to work you can make workers into capitalists, all of them, because after all a capitalist is a man who has accumulated something over and above the need of subsistence. A worker can do that when he has continued employment and when products can be produced in great quantity for him.

Senator VANDENBERG. If you force the investment of idle money just what are you undertaking to do? Are you not tremendously multiplying the probabilities of loss through hasty and ill-considered investments?

Mr. HAZELETT. I do not wish to rush unwisely the proposal of incentive taxation. I do say this, however, that since a man would pay higher taxes on idle facilities than he would on facilities in use he would be very careful not to put money into a property if there was no market for its services. There is an unlimited demand for certain things. Those people that think they have everything still would like to have yachts, or better yachts, they would like to have planes, or better planes, they would like to have golf courses, tennis courts, they would like to travel, and what not. There is no limit to the demands from people for products or services. So it does put a penalty on a man for investing money unwisely immediately.

Let us assume that we have more facilities for producing shoes in the United States than it is possible to consume. Incentive taxation puts a pressure on business to be in production so people can buy all the shoes they want, because that is the only circumstance in which they can do it, but it says to the men with capital, "Don't put any money into the shoe business, because there are far more than enough facilities, because people have all the shoes they want, because you are going to pay a high rate of taxation on that property, because you cannot dispose of the output." I mean incentive taxation brings pressure to be wise in one's investments.

Senator VANDENBERG. It brings pressure to be both wise and speedy, and that is a rather difficult combination.

Mr. HAZELETT. I agree with you. I do not think we have been necessarily very wise about our investments in the past, and I do feel that there are few fields in which there is not room for improvement. If we build office buildings like the Empire State Building they would have to rent them under incentive taxation to avoid unusually high taxes. That means that people move from the lowest class of shacks to the better places, people would move from the better offices into the modern buildings, and you have income from this property in use. You have no income even from the one single room in a building which is idle.

Senator VANDENBERG. I can follow you a little better in the field of incentive taxation as it applies to the industrialist himself. I can see you completely there. I am not clear about applying it to idle money as such.

Mr. HAZELETT. It will take a little time to make that clear. I want to answer that question now, or in the future, on that subject.

Senator VANDENBERG. Go ahead.

Mr. HAZELETT. I want to look at incentive taxation from the viewpoint of the farmer. The farmer is the one class of industry who sells his services at the best price he can get for them. He cannot store his product indefinitely and for that reason he sells just at what he can get for the product. Whereas, capital holds money out of production if it cannot get the price it asks. That is to say, capital may, in that sense, strike. Labor, if organized, does the same thing if it cannot get an artificial price.

I hate to think what might happen to our country if the farmers should use the same methods that labor and capital did and state to the public, "Gentlemen, we will not send you fruit or potatoes or corn unless you pay us $5 a bushel for it, regardless of quantity or quality."

Strikes do not occur in those industries which are so highly decentralized as farming. I want to show you what happens in the depression to the farmer. The farmer feeds the unemployed. The banks write interesting entries in their deposit and loan accounts to the Government, but the farmer feeds the unemployed, nobody else, and he gets absolutely nothing back from them, because you cannot get anything from an idle man. The income of the farmer is the product of industry. No doubt about that. We raise the food on the farm which feeds us, perhaps, and the balance we exchange to the city for the products of industry, that is to say, clothing, furniture, refrigerators, automobiles, tractors, farm implements, and the like.

I think probably two of the most remarkable curves that come from any group of statistics are the directly parallel curves of farm income and industrial production. You will find that farm income always goes up as industrial production goes up, and it always goes down as industrial production goes down, for the simple reason that the income of the farmer is the product of industry. So the solution of the farm problem is not on the farm, it is in industry. Industry has been playing pick-a-back with the farmer almost since the beginning of the industrial era, and for that reason you can never expect fair prices for the farmer, unless the farmer either organizes and uses the right to strike as much as capital is organized and as much as labor is organized, or unless we bring pressure to stop the strikes both of capital and labor.

There is another point in the solution of the farm problem. Many, many men have gone back to the farm in this depression to get closer to the sources of food. We have a tremendous overproduction, perhaps, of food products in this country, but a solution of that problem is to put all industry into production, and by the process of incentive taxation, open up the closed brick factories, the glass factories, the steel plants, put them in a high rate of production to permit expansion of industry, so as to take thousands and thousands of men from the farm where they are producing something that we already have enough of to the cities, and put them to producing something of which we do not have enough.

Consider the cotton surplus in the South. I have been through the Cotton Belt more than once. No place in the world have I ever been where I saw so few decent dresses on the women, even if they were made out of cotton, than in the Cotton Belt. No place in the world have I seen so few draperies, so few rugs, even cotton rag rugs, so few cotton sheets, blankets, mattresses, and so on, as in the Cotton Belt; and we gentlemen in the North have been scrapping our textile plants, our railroad rolling stock has been rusting on the sidetracks instead of carrying the cotton to the textile mills and carrying it back to the cotton farmer and other farmers in finished products.

What is true generally of the cotton farmer is true of all industry. If we kept the textile business in operation, weaving it and putting it back into the hands of the people that need these cotton products, we would have the answer. If you put pressure on the textile mills to stay in operation, if you put pressure on money to be in circulation, you can solve the problem. Incentive taxation will do this.

I want to say a little more about idle money, because that is the most controversial issue that I raise. Counterfeit money is better money if it circulates than the purest of gold lying idle, so far as money is concerned. Money that is idle earns no interest for the owner. I want to show you how it depreciates exactly as a machine depreciates when it is idle, or an organization depreciates when the organization is idle, and so on. Whenever private capital fails to go to work, the Government is forced to inflate. It is not a question of quantity of money in the country; it is a question of quantity times the rate of turnover which determines business. As long as private capital continues to heap up in the banks and lies idle, just so long must the Government continue to inflate by one means or another. We thus see that the dollars in our banks and in the socks of the country are depreciated in value because they are idle. But money at work appreciates; it earns interest; and if compounded could have almost doubled during this depression. You and I know of millions that have practically not been touched during this depression.

Money is like a freight car, it simply facilitates the exchange of goods and services between people and places; and, like a freight car, when it is idle it earns nothing for the owner, it stops business and it depreciates, and nothing is being earned for its replacement.

The earnings of our banks are strictly determined by the turn-over of the money. You find every man in a banking institution is engaged in one of two things, paying out money and taking it in, or in loaning it. The bank's service to the community is finding the proper credit risk and turning over money. That is why we think we should have taxes on idle money, to promote bank profits. They cannot make any money, or their customers cannot make any money with idle money. If we had a tax on idle money in my opinion we would have accomplished all the things that are now accomplished by the excess-profits tax, the undistributed surplus tax, and capital-gains tax. And all these taxes could be discontinued. We would say to a corporation under an incentive tax plan, "You can have any amount of surplus you like, but it cannot lie idle." They must do one or five or six things with it. They can pay it out in dividends, in which case the stockholder must use the money to escape the idleness tax; they can pay it out in wages to escape the tax; they can pay it out in plant expansion, and all these things would keep people at work; they can turn it over to their banker on time deposit to avoid tax, and the banker then has this increase asset for business purposes generally. Placing an incentive tax on business precipitates the best possible demand for capital by industry and business, and they get the benefit of lower taxes. So I say if we tax idle money we immediately put capital gains back into production and tax the profits from such production. You put your undivided surpluses into production and tax the profits of production. You put your excess profits into production and tax the profits of the production.

I do not like to see the Government discourage excess profits. If there is anything in the world I think we should have, I think it is excess profits. For these reasons: A corporation earning excess profits is probably employing everybody it can employ, and certainly we want that. It must be turning out a large quantity of products, that the public wants and should want in order to earn the excess profits, and certainly we want both of those conditions, so let us not penalize them.

So by a process of taxing idle money, in my opinion, you could simplify our whole tax structure tremendously and abolish these controversial issues. We have the highest bank deposits practically in the history of our country, but still business is at low ebb and the turn-over rate on money is extremely low. To tax idle money relieves the pressure the man with money can bring on a debtor, because if the debtor pays his debt the owner of the money has got to find somebody else to make use of that money. He is required to keep his money in use at all times. It will stop bank runs in times of lack of confidence, because a man taking his money out of the bank would be subject to the tax unless he made some use of it, and if he made some use of it, that is for goods or services, he immediately puts people to work, which is the basis of confidence, and the money goes right back into the banks. The incentive tax will, therefore, give the owner of the money interest on his money, or some goods or services for it. It gives the banker greater working capital by requiring the depositor to permit the use of his money, and it gives business the benefit of the use of the money, and confidence, gentlemen, is based on nothing in the world but the certainty that the man with whom you invest money is going to be in a high rate of production. The banker is not going to lend money to idle men, because he cannot get it back and he would not put money into idle businesses unless they are going into production with it.

Now, much has been said about taxation for revenue only. Gentlemen, I insist a policy of incentive taxation is a basic revenue policy. For this simple reason: You cannot collect taxes except by confiscation from idle property. You can always collect taxes from property which is in use. You can collect the maximum amount of taxes from property which is operating at its maximum capacity. If you reduce tax rates on industry so as to increase their production to the maximum, you will find the increase roughly from 60 to 100 percent of capacity will quadruple the profits of a business, and if you cut the tax rate in half for a concern, with all concerns operating at full capacity, you can probably collect twice as much revenue for the Federal Government, and I will show you how it will reduce the expenses of the Federal Government at the same time that it increases its revenue.

I will give you a pertinent illustration. I try to practice what I preach. Last summer I had an extra amount of money in the bank. I did not want to look after a greater variety of investments than I had that were subject to the control of other people. I proceeded to build a building with it and equip it for certain work in which I am interested. These things happened: We took a number of men off the relief rolls to build the building, so that Federal expenditures went down for relief; the contractor, whom I know personally, made a profit on the building, and the equipment people in general made profits, and the Federal Government taxed those profits; I got the benefit of the building. So that three things happened; Federal expenses went down, due to taking men off the relief rolls; Federal income went up because of the profits of these people building the equipment and the building, and I got the benefit of the building. The three of us were benefited.

Now, let us assume that under incentive taxation the contractor and the equipment manufacturer are under obligations to put their money to work right away to avoid a tax. The contractor might go out and buy a steam shovel, and immediately men are put to work to build it, immediately profits are earned by the manufacturer who builds it, and immediately men are put to work to use the steam shovel, and every time the Government gets increased revenue. If, however, I had let the money lie idle in the bank, the Government would have received no revenue whatever, except by confiscation, and I do not think the American public are ready for confiscatory measures yet.

The stability of any Government is seldom questioned when we have good times, when practically everyone is in a high rate of production; the stability of every government is questionable when a large percentage of its people are unemployed for any great length of time. Such a condition we now have.

There is only one solution to the balancing of the Budget that I can see, and that is a policy of promoting great profits to be taxed by reducing tax rates on the production, when people go into production with all of their facilities—land, money, and men.

I do not believe the Federal Government has any constitutional right to tax idle property. I would urge States to adopt such a policy, in other words, to tax idle property at a high rate, to put it into use for the benefit of the owner and the public, and to reduce tax rates on property that is used.

A government of such wealth as ours can always carry on unsound tax policies for a long time, but if an emergency such as war develops, or internal difficulties, you will find that the safety of the government is dependent upon production of war materials, production of men, production of organizations, and production of money; and when we strike one of these crises we are going to find our organization for war is in very bad shape. Our organizations for production in many fields are in bad shape. National defense is based on the production of our steel mills, our shipyards, our electric equipment producing facilities. Nothing in the world can build up a national defense except to have our airplane factories working at maximum production, and the only time they are going to do that is when it is profitable to do so.

Incentive taxation offers a plan for business to get labor at a price it can pay. Relief cannot be abandoned unless business gives men jobs, and if we bring pressure to bear on business and the owners of money to do that then, and only then, can we abolish relief to able-bodied men and, gentlemen, in my opinion we can never get a satisfactory labor market for business until relief is abolished for able people, and the only way relief can be abolished is when these men can be put to work.

Business would get materials at prices they can pay. The producers of raw materials, being under the same pressure to operate at a high rate of capacity, would put a price on the product the customer could pay. Practically all people would be under the same obligation to use their money to buy some product, and as long as business is producing something that people want, it has a market for his product. These are the things that business requires.

Now, as to price policies, incentive taxation as the policy of the Government would force every class to put the maximum price on their services, which permits maximum production. As soon as their production drops below their capacity, their tax rate goes up. I made, I think, a very thorough study of income to various classes, and I made these deductions, that the income of every class goes up with increased production and down with decreased production, but there is no relation whatever between the income of any class and the prices it asks for its services, and that causes its production to drop below capacity. That applies to union labor, it applies to manufactured goods, it applies particularly to the durable-goods industry. You find in the depression durable-goods industries did not decrease their prices anything compared with the consumer goods, such as the farmer, but the income of the durable-goods industry is down much more than that of the farm class or the consumer-goods industries who maintain their production at a high rate although they decrease their prices much below that of the durable goods.

This brings to our attention, I think, the possibility of totally automatic regulation of monopoly by incentive taxation without any addition to these present policies. A monopoly is nothing in the world but a union of business. A business is an employee of the public, the public is the employer. The most that you can expect of any business or employee is to produce to its maximum capacity. What we want, for instance, from a railroad, is the maximum of travel and the maximum of freight haulage. What we want from a telephone company is the maximum of telephone calls for our use. What we want from an electric-power company is the maximum of power. You will find that their income goes up as they go up to their capacity, the same as any other business. But supposing that we apply incentive taxation to monopoly as to say, "As long as you operate at your practical capacity you shall pay lower tax rates than you pay now, and you may set your own rates." But assuming that you increase your rates for your service to the public, stop regulation of rates entirely. Let them set any rate they like on their services, the instant that they raise their rates to the point where the public stops using the capacity of their services their tax rate goes up so rapidly that their income goes down, and the result would be that they would not raise their rates to the public unduly.

Let us take the other condition, that they do not have sufficient facilities to take care of the demands on the part of the public for their services. They can immediately raise their rates for their services and make extra profits.

Under an incentive-tax plan profits cannot lie idle. What does the businessman do with profits when he knows there is a call for additional services at a profit? He expands his facilities.

I am sure you will find, on a study of this, that an incentive tax on monopoly of a fairly steep gradient will solve the problem without all the difficulties of trying to evaluate these properties. Let them set any valuation they want on their properties, they will only pay a correspondingly higher property tax in their particular States. What we want is a maximum service for the public, and this can be achieved by a straight incentive tax such as we propose.

The question of purchasing power. There is only one kind of purchasing power worth considering, and that is permanent purchasing power. If you give a man $100 today and he spends it, that money immediately goes into the pocket of a producer, and you haven't done anything for the man. Purchasing power can only come from permanent income which comes from permanent employment. You cannot permanently give a man money without receiving anything in return.

The tax on idle money is important for the reason that the people who can purchase things are only the people who have money, in such a system as we have. We bring pressure on him to use the money, and as soon as he pays it to another group they have to use it, and, as soon as that group pays it to another group, they have to use it, and so on. So you have permanent purchasing power. As soon as production goes to zero you do not have any purchasing power. Regardless of the quantity of money, your purchasing power is based on producing something to purchase and not on the quantity of money in the system, but on the circulation of the money which you may have. Incentive taxation can bring about great and permanent purchasing power.

Let us look at social security. When I get to the point where I feel I cannot work, one thing I want is some assurance that I shall have food. I cannot get it unless land is in production, unless people that are handling food are in production. I want shelter. I cannot get it if houses are permitted to lie vacant. I want clothing. I cannot get it unless men are making clothing. I want the results of production, continuously as the one thing for social security. We have ample producing facilities in this country for everybody—the old, the young, the disabled and able, providing we use them. The essential thing is to find a policy which will promote their use to the maximum amount, and their continued use. Incentive taxation on this basis, in my opinion, could be a permanent policy, and would permanently solve this problem.

A three billion or four billion dollar beggarly pittance to the unemployed, in my opinion, is ridiculous. We should pay them 15 or 20 billion dollars in real wages. At the same time getting 15 or 20 billion dollars worth of production. That means real wages and not pieces of paper.

The error in the relief policy of an able man is this: Whenever you put a man on relief, he is taken out of work. The people who supply him with food and clothes, primarily the farmer, are already at work and nobody is put to work to keep him on relief.

Let us consider a man working on a conveyor in an automobile factory. It takes 100 men to supply a man with parts to work on that conveyor line, and as soon as he is taken off the conveyor line those 100 men are idle. If he is put back there by industry you will find 100 men employed, as well as this man.

Senator HERRING. Well, if he is building a viaduct where does the cement come from, where does the reinforcing come from that is used in that viaduct, even though he may be building it on relief?

Mr. HAZELETT. That comes from the production of other people. Do not misunderstand me in this respect. Wherever Government builds efficiently with money taken from the taxpayer, I mean that at a reasonable cost, anything which the public desires over and above something else, if it is bridges, well and good, but in my opinion the consumer should be the employer of business. If he wants a bridge let him say that we shall have a bridge.

Senator HERRING. We are all agreed on that, if you can work that out.

Mr HAZELETT. The institution, gentlemen, of private property, in my opinion, is almost at stake in the world today. The Communists and Socialists have been shooting at this question for generations. In my opinion there is a thing which is wrong in our present system of private property, but not in the title to it, and that is the right of the owner to take it out of production. When it is in production it benefits everyone, and, when it is idle, it harms other people and does the owner no good. Incentive taxation, in my opinion, is an answer to that almost age-old problem by requiring that productive facilities shall be used always.

Senator HERRING. I assume under your theory that production is out of balance, otherwise you would not contend that we compel maximum production in industry, production to capacity, that if we did so it would cure all our troubles, because agriculture is producing to capacity and they are in trouble.

Mr. HAZELETT. Exactly. Agriculture is staying in production and therefore would not be affected by incentive taxation at all.

Senator HERRING. If they are in capacity production now then they should benefit by incentive taxation.

Mr. HAZELETT. I think they should, from the standpoint of taxation, but the facts are taxes will get reduced if you get rid of unemployment. Taxes generally can be reduced if you get rid of unemployment.

Senator HERRING. Sure.

Mr. HAZELETT. I still think the problem of the farmer is to put industry into production. I want to emphasize the tremendously important relationship between the farmer income and industrial production.

Now, then, the housing problem. The housing problem is nothing in the world but the question of keeping money in production, and keeping everything—steel, lumber, sawmills, and so forth—in production, and furniture plants to equip them. Incentive taxation, if applied by the State on idle property, would immediately force the use of all the good houses, requiring the owner to put a rent on them that would rent them. Then they would live in the good houses and the bad tenements would be empty.

Senator HERRING. Why not go to Henry George's theory right at one jump?

Mr. HAZELETT. Henry George's argument is my argument, with this exception: He insisted that all production is of, by, and from the land. I insist it takes money in our country; I insist it takes management; I insist it takes machinery, buildings, locomotives, and so on, so I would apply the philosophy of Henry George to all of these productive facilities.

There are precedents in many fields. You will find that miners' claims are a type of title to property by use. If you fail to use it, it is taken away from you and returned to the public domain. The same is true in regard to squatters' rights, the use of a piece of property for a certain length of time gives title to it. The domestic tariff is a tax to promote domestic production, and in my opinion is a precedent for incentive tax policies.

Senator HERRING. You think a protective tariff is an incentive tax then?

Mr. HAZELETT. It is during the development of an industry. After the industry is developed, I think it becomes primarily a revenue proposition. My ideas on that are a little different, perhaps, than others, but I would not want to bother you with them at this time.

Now, let me explain what I feel is basic profit sharing. I insist that sharing of profits is the sharing of living standards by those who have high living standards with those who have lesser living standards. I have concentrated on the question of getting industry into production to produce a high rate of profit.

The individual tax form, you will find that I have asked the taxpayer to state the amount of money spent on himself and family, that is to say, his personal expenditures. My description of real income, personal income, is the living standards at which the taxpayer lives, and for that reason I would take what we now call his income and exempt that part which is reinvested in business, which does not lie idle, but I would raise the rate on the amount of money spent on himself and family in the higher brackets to promote profit sharing at that point where profit sharing is real. The only way a man could reduce a tax of that kind would be to reduce his living standards and put his money into business to produce more wealth for those of lower living standards. I insist that a man's real income cannot be anything but that which he spends on himself.

The present income tax is a penalty on the service that he performs to the public, because a man is taxed on how much he produces for the public. A man who earns a large income from business is generally doing a great public service, by producing a great deal that people want.

So if you want a basic profit-sharing plan, in my opinion it should be at the point of the individual income tax, and exempt what he reinvests in business. Do not permit it to lie idle by incentive taxation. Corporations do not enjoy income, only individuals enjoy it by consuming that income. A tax on idle money would tend to cause people to either put their money into business or to give it to charitable institutions, to welfare groups, to churches, hospitals, and the like. Actually, incentive taxation makes great riches a burden to the owner, and my belief is when people have security they prefer honor to the riches.

This is the distribution phase of incentive taxation: I would not recommend an incentive based on personal income unless you had some form of incentive taxation which gives security in business by keeping business in production.

I want to say, in recapitulation, that in my opinion a policy of incentive taxation offers an opportunity to solve the problem of unemployment, to solve the problem of security for investments, to solve the problem of old-age security by keeping everything in production so we have everything employed by everybody, to solve the problem of the farmers' income by raising industrial production. I want to point out that in my opinion it is the only method by which Federal revenue can be made to balance Federal outgo and thereby actually cause some stability to the economic structure of our Government.

Incentive taxation has an ethical basis. I believe the basis of all ethics, the basis of all religions, is the simple statement that we should love one another. Now, to me that is a meaningless phrase unless it says we shall serve one another. And incentive taxation says to every form of business, to every man who owns money and property, he must serve with that property, he must be a good steward for that property, for his own benefit as well as for the benefit of others.

As I see it, the tax on idle money is exactly the same as the parable of the talents. It says to the man who has money, "You cannot hoard it; it is no good to you when it is buried in the ground. Put it to work and earn interest on it for yourself, or it should be taken away from you." It is no hardship upon a man to take anything from him if he hasn't any use for it.

I thank you for the honor of appearing before the committee.

Senator HERRING. Thank you, Mr. Hazlett. We will recess until 1:30.

(Whereupon, at 12:03 p. m. a recess was taken until 1:30 p. m. of the same day.)

AFTERNOON SESSION

(Hearing was resumed at 1:30 p. m. pursuant to taking of the recess.)

STATEMENT OF NORMAN J. MESSICK

Senator HERRING. You are an employee of the Westinghouse Co.?

Mr. MESSICK. Yes, sir.

Senator HERRING. Of Wilkinsburg, Pa.?

Mr. MESSICK. Yes, sir.

Senator HERRING. We understand that you have had quite a little to do, from the employee standpoint, of working out their profit-sharing plan?

Mr. MESSICK. Well, I was quite instrumental in having the plan worked out. It came, I might say, originally from the employees. It was based on the fact that when a company has a tendency to lower wages, they gave us a cut, but when it came to putting them back, the employee had to go after them in order to get it back, so I suggested to our management that they devise some plan whereby, when it became necessary to cut, instead of giving us a 10-percent cut all at once, that as profits go down we would get 1 percent and 2 percent and up to 10 percent, but when profits showed improvement, cuts would automatically come back the same way, and it would not necessitate any argument between management and employees.

Management, as we found, was cautious in putting the money back. They did not know whether business was going to keep on going up, and, on the other hand, the employee was impatient—he wanted the money back. So it created controversy between them.

They worked this plan out themselves, and I believe Mr. Marshall had the most of that to do, and it was submitted to the employees. At first, of course, naturally, like all things new—and I don't believe there was anything in existence like it—we did not know just how it would work out, but we finally studied it out for ourselves, and we did it mostly in this way, we figured it down to a small business—for instance, I thought if I had a small grocery store and an employee asked me for a 15-percent increase in wages, that I would hesitate, although I might be able to grant it, but I would figure, "Will my sales permit me to do it next month and the following month?" Well, I thought I would be cautious in granting 15 percent, and I would come back and probably grant 10 percent, and it would later prove that I could have given the 15 percent. So we found that this plan took the guesswork out of the employer's argument. He set this up so that if his business from month to month warranted it, he could give the increase in wages.

In other words, we do not consider it altogether a bonus plan. We call it an automatic wage adjustment every 30 days, based on the employer's ability to pay, and from that we find that all our employees, I might say without fear of contradiction, because I know that this will go back to Westinghouse, that in my travels throughout the plant I have only met one employee out of the thousands there ever say that he disliked the plan. They are all heartily in favor of it.

Senator HERRING. What is your position there?

Mr. MESSICK. I am a production clerk. I work on a salary. Mr. Stritmatter, who is with me, is paid by the hour. One of us is an hourly paid employee and the other is a salaried employee.

Senator HERRING. How long has this plan been in effect with the Westinghouse Co.?

Mr. MESSICK. Less than 2 years.

Senator HERRING. Less than 2 years?

Mr. MESSICK. Yes. And I believe it averaged 13 percent last year. I would say, based on what I said before, if we had gone after a general increase at that time in our wages, I feel sure that we would not have gotten 13 percent. We might have gotten around 8 percent or 10 percent, and as I say, the management playing safe, would maybe have granted that, but as it worked out, we got 13 percent, and I think that any plan that takes the guesswork out of industry and creates better employer and employee relation is something that we should have.

Senator VANDENBERG. You think it takes the friction out as well as guesswork?

Mr. MESSICK. That is right. It takes the friction and impatience of the employee out. He wants his money back. He does not mind, when a company gets in trouble going down with them, but he wants to come right back as soon as they do.

Senator VANDENBERG. It is very essential to the operation of the plan that the employer should be completely frank in his disclosure of all of the information.

Mr. MESSICK. They do that. I will say that the books are open to their employees, and at the end of the year their annual statement that is published by an outside firm of certified accountants will prove we did get our actual money, and that statement also is one that is looked over by the Government in order that they see that the Government gets its proper tax, so we feel pretty sure about that, and outside of that I do not believe that the Westinghouse Co. would manipulate their books.

I still think that we have a check further than that, because when I was on the committee representing the employees, those books are handled by common workmen, accountants and auditors just like we were, and we had friends up there that would have watched any angle like that. I don't think that there was ever any question about it, but in some people's minds I can see that there might be some question about some companies doing the right thing.

Senator VANDENBERG. You consider the plan a complete success from the employees' standpoint?

Mr. MESSICK. Yes, sir; entirely so. I might mention one thing that we ran into that I think will be ironed out, or at least we are going to try to have it so. Like all plans when you come to a depression, something happens, and we ran into a share-the-work plan out there; that is a group of employees, instead of laying one off, we divided the work, and each took a day off and kept unemployment down. That would have a tendency under that plan to take money out of the pockets of those sharing that work and being furloughed, and those that did not take a furlough. There was a saving on myself, for instance, if I was furloughed, and it helped to increase the profits, which increased the percentage to those that did not get the furlough. That was one thing that was never foreseen, and we have called that to the attention of the management and they will have to take some steps to correct that. I think that we shall all take a furlough, and that possibly would take care of that.

Senator VANDENBERG. On questions of that kind, you negotiate and sit around the table with management and they discuss it with representatives of the employees?

Mr. MESSICK. That is right. We have two systems out there now. We have the C. I. O. in the plant, too. They represent the check people, but they do that, too. And the salaried employees, we have our own little organization that did negotiate for the salaried employees. But we have always kept the two very closely allied, the check employee and the salaried employee. A former committee was composed of both and sat in with the management.

Senator VANDENBERG. But you say that the plan has met with the general employee approval?

Mr. MESSICK. Yes.

Senator VANDENBERG. Does that include the members of the C. I. O.?

Mr. MESSICK. Yes, sir; all of them. And I know thousands of them, and I have talked to a great many of them, and they are heartily in favor of that plan.

Senator HERRING. Do they negotiate through collective bargaining with the C. I. O.?

Mr. MESSICK. Yes; they do. They have collective bargaining rights for hourly paid employees of the Westinghouse Co.

Senator HERRING. Do you think they gain any advantages through that method that you do not enjoy through yours?

Mr. MESSICK. No; I would not say that they have.

Senator HERRING. They are all treated fairly alike?

Mr. MESSICK. Do you mean whether they have gained more advantages for the employees?

Senator HERRING. For themselves; yes.

Mr. MESSICK. No.

Senator HERRING. They are treated the same way by the employer?

Mr. MESSICK. That is right; they are. They are treated just the same as we were treated and are treated now. They are consulted on all matters pertaining to employee relations, and the salaried people, while we had no representation there for a while, the management did call different men in and talked problems over with them, trying to arrive at a proper solution of them. Even for a while when we did not have representation. We, the salaried employees, now have a union.

Senator HERRING. That is very fine. Thank you, Mr. Messick. Unless you have something else that you wish to suggest?

Mr. MESSICK. No; I have not anything else.

Senator VANDENBERG. You have been very helpful.

Senator HERRING. We appreciate your coming in.

STATEMENT OF EMIL A. STRITMATTER

Senator HERRING. You are an employee of Westinghouse of Pittsburgh?

Mr. STRITMATTER. Yes, sir.

Senator HERRING. Just what department do you work in?

Mr. STRITMATTER. Maintenance department.

Senator HERRING. How long have you been there?

Mr. STRITMATTER. I have been there 27 years.

Senator HERRING. And you are paid by the hour?

Mr. STRITMATTER. I am paid by the hour.

Senator HERRING. And you approved this profit-sharing plan or wage plan as it is called?

Mr. STRITMATTER. Yes; we did—very much so. I speak personally on the feeling of the other men, that is the check men. It does not affect our base pay, that is the hourly rate, whether it goes up or down. It is the profit that the company makes after they are earning about $600,000 per month, after they are paid their salaries and their buildings and all of that, that is taken out, and then whatever profit is made, out of that they pay us a percentage. As Mr. Messick stated, they have about an average of 13 percent.

Senator HERRING. You are satisfied that your base wage is not affected?

Mr. STRITMATTER. It does not affect our wage base, but on top of that, we got a 10-percent raise at that time. If we had gone after them for a raise, it might be that we would have gotten a raise of 5 or 8 or 10 percent. This way it runs on the average—like this month—we make it up on the 8th of every month, and it is not paid every 6 months, but we get paid every month. This month it is 3 percent, and as the business goes up, naturally the percentage goes up.

Senator HERRING. Do you think in any way your base wage is affected by that?

Mr. STRITMATTER. No; our base rate is not affected. We get our absolute rate and we have what we call a classification card, which is a key sheet, and that key sheet runs from A, A–1, B, B–1, C, and C–1, D1–D2, E1–E2. And the girls, it runs EW–DW1, DW2–CW2–CW1, and all of that. That is the classification card according to a man's ability, what that is, and he gets paid according to the class of work he performs.

Senator HERRING. There is no confusion in your mind as to the rates?

Mr. STRITMATTER. No. The men feel they are getting something for their earnings, and also the fact that it gives a man a chance to earn something and better himself too. And also with scrap material and things like that, which they are watching more. It builds him up and makes the workman use his head more.

Senator HERRING. You think this gives you a chance to make better than a living wage to that extent?

Mr. STRITMATTER. That is right.

Senator HERRING. And you feel that you are entitled to that if the company can make it?

Mr. STRITMATTER. Yes. There is another bonus there. From the superintendents up, they get a bonus on the production, a separate bonus, at the same time they get a bonus on what we earn. That is, they get two bonuses, which they feel for the position they hold that they are getting a bonus for extra efficiency, and they don't mind them compensating them in the bonus that we earn, but they do not believe in the bonus separately that they have, too. It is the same way when they brought this Social Security Act in, which I myself say it is a very good law, but I believe that they should have looked into the things and the matters pertaining to it before they had taken action.

For instance, our annuity plan provided a minimum of one unit per year's service. This increased by the man's earnings to 1½, 2, and so forth. He also had the opportunity of buying annuity units in addition to those given by the company. For every employee who bought annuity units to a number not less than the scheduled number of company annuity units that the company provided for him for 1 year, he received as a bonus one-fourth of a company unit.

At the inception of the social-security plan all annuity units to any employee were set aside for him and we picked up the social-security plan. Had we been allowed to continue the Westinghouse plan, at the maturity or at the date of a man's retirement, he would have received more money from the Westinghouse plan than he would by the discontinuance of the annuity units on the company plan plus what he might have gotten on the social security. This is the general opinion of all our employees and effort was made at the time to have the Clark committee consider our request. Evidently our Senator did not submit our telegram.

In addition to this we have a relief department which pays benefits for illness; also upon the death of a member they pay to the family from $125 to $175 and the company duplicates this amount. This is greatly appreciated by those of the families where death occurs.

Our employees placed on pension receive their free insurance at the time of death; i. e., in the past when the insurance provision was first started all employees with more than 10 years' service were given $1,000 and if they participated in the savings plan were given $100 additional each year. Many of our men have $2,000 free insurance. All employees, at least after 6 months' service, have $500 free insurance. Furthermore, all employees pensioned are given an opportunity to retain their group insurance, which is at a very low rate, and without any physical examination can continue on by paying the monthly premium. In other words, they still continue to get this group insurance at the same rate as regular employees.

Concerning the number of veteran employees, if I remember right I said there were 8,000. I desire to correct this statement. The total number of veteran employees with over 20 years' service is 6,650, and there are approximately in the East Pittsburgh district between 3,500 and 3,600.

Senator VANDENBERG. You mean that you had a pension plan which was far superior?

Mr. STRITMATTER. Yes, sir. A very good plan.

Senator VANDENBERG. And has that been dropped?

Mr. STRITMATTER. That has been dropped. As soon as that social security came in, naturally the company dropped it, because in other words, it ain't costing them anything. We are paying on it now.

Senator HERRING. There is no reason why they could not supplement that by the difference between that and the plan that they had had before, by the amount that they were willing to pay before?

Mr. STRITMATTER. That is a question. Why should they do that? In other words, they want to go along where they are supposed to go along with it; in other words, it is saving them money. That is only human nature, that anybody will do that.

Senator VANDENBERG. Do you agree with Mr. Messick and the employees generally throughout the plant, that they are happy and satisfied by this arrangement?

Mr. STRITMATTER. That is right.

Senator VANDENBERG. And you are a member of the C. I. O., are you not?

Mr. STRITMATTER. That is right.

Senator VANDENBERG. And you think that the C. I. O. members in the plant feel that this is an equitable and satisfactory arrangement?

Mr. STRITMATTER. Well, that is a question that you are asking me and I am going to be honest and answer it, and it is this.. They claimed a membership at one time of about 8,000 people, and today their membership is very light, and I would not like to quote, but they are not paying any dues on account of this, and they are being accused of this, which we had a good set-up, because I know that I have been on the pan about it, because I have criticized it, but I believe when we do things and learn about them, that it has a good effect. But as the remarks were made here last week, I believe before the Senate, that they do not believe in this bonus system because at the end of the year nobody can trust anybody—well, that is true sometimes, but I believe that you Senators have got it boxed up pretty close so that there is nobody can steal or do anything else about it, but do the right thing, so I do not think there is any company, that is, any big concern, that would belittle themselves to do that.

Senator HERRING. Do you think that there is any connection between this satisfactory profit-sharing plan and the failure of the membership of the C. I. O. to continue to pay their dues?

Mr. STRITMATTER. It is just as I mentioned before, just now it is my opinion, and I have got a job where I get pretty well around dealing with all of them pretty near, and naturally, when a workman had something before and had it taken off of them, they don't naturally feel so good about things, and when they do that, naturally they believe, the level-headed people figure for themselves and they are not going along with things they are being hurt with, and that is the friction there.

Senator HERRING. Do I understand now that you are referring to that reduction due to the Social Security Act?

Mr. STRITMATTER. No; I believe you have asked with regard to the C. I. O.

Senator HERRING. Yes; I wanted to make it clear that that was what I was asking you about.

Mr. STRITMATTER. That is right. Of course, I want it to be understood that the Social Security, we have needed that for years, but I think it should have been based on something just like what you are doing here at the present time, and it should have been investigated and found out what the best system was in these different plants, then work up something that would fit.

Senator HERRING. You think that some provision should have been made that nothing that you already have should be taken away from you?

Mr. STRITMATTER. Naturally, to be selfish about it, a person doesn't like to lose something that he already had. They say, "Well, the younger population might benefit." Well, we might benefit by it, too. They might be smarter than we are and maybe they will have something better than we have, so why should we suffer when we get to be 70 years old?

Senator HERRING. That is all most interesting, a most interesting viewpoint. I think that is very helpful. Thank you very much. We appreciate very much your coming.

STATEMENT OF L. M. GIANNINI, PRESIDENT, BANK OF AMERICA, SAN FRANCISCO, CALIF.

Senator HERRING. We appreciate your coming, Mr. Giannini. I understand that you have recently put a profit-sharing plan in your bank.

Mr. GIANNINI. Yes; we have, Senator. We started a plan about 8 months ago which is a voluntary plan, inaugurated by our board of directors.

I want to say first of all that I have not any prepared statement and did not know until just a short time ago that I was to talk with you. I understand that Mr. A. P. Giannini suggested to Mr. Despain that I was here and that it might be helpful if I were to convey to you our views on profit-sharing.

Senator HERRING. That is right. He wired.

Mr. GIANNINI. I am happy to do so, if it can be helpful, and I am glad to make any contribution that I can. As I say, I have not a formal presentation to make. If it suits your pleasure, I will summarize roughly the provisions of our plan.

It applies to approximately 8,000 employees, all of our full-time permanent workers in the Bank of America. In order to attain that status, they have to have been there for a period of 3 months or more. Anybody with a period of service less than that is on a temporary basis and considered not a part of our permanent staff. The profit-sharing plan is based upon the salary of the individual employees and officers. No distinction is made for years of service or seniority. We approached this matter from this angle, that we felt that an officer or employee's salary determined what was, in the opinion of the management, his value to the institution, and took into consideration his past services and the effectiveness and efficiency of his work, so that we thought the simplest plan and the most equitable one would be to pay them a flat rate of bonus on their salaries.

The board of directors sets the rate each month. It started at 7½ percent for salaries up to $6,000 a year, and on that part of that salary that exceeded $6,000 a year, the rate of bonus or profit sharing is 5 percent. The funds are credited to an account that is maintained by the Board of Trustees who administer the plan for each employee. The proceeds of the bonus plan are invested in the stock of our bank. No investments in fractional shares are made. The investments are made only when a man has accumulated in an individual account an amount sufficient to equal the current value of one full share of stock.

The stock is held in trust for the employees for a period of 5 years, but the employees have the voting rights and receive the dividends that are paid on the stock, our purpose being to give them a sense of proprietorship and to have them accumulate a substantial interest in the institution. Then at the end of 5 years their shares that were accumulated 5 years previously are released to him complete and clear, and each year thereafter the next succeeding year's bonus stock is released to him. There is a provision for withdrawal of the funds in the bonus accounts on a proper showing to the board of trustees, and really to the executive secretary to the board of trustees. There is one individual who is an executive secretary of the board of trustees, and he passes on the merits and needs of the individual, and if, in his opinion and the board concurs in it, the employee should receive the funds instead of having them impounded, he may have them. That is discretionary with the board.

In the event of death, the person legally entitled to receive the funds or stock receives it, and in the event of resignation, the employee must wait for a period of 30 days, after which, in the discretion of the trustees, he may receive his cash or stock. The reason for the 30-day withholding is so that an employee would not resign for the purpose of getting his bonus if he was confronted with an emergency and wanted it immediately.

We have adopted the rigid policy to the effect that the bonus shall in no way affect current salary adjustments. They are made without giving any consideration to the amount of bonus the employee is receiving. We had a few years previously, a bonus plan in effect in our bank, and the results were very satisfactory. We hope to accomplish through the present plan a deeper interest in the affairs of the institution on the part of the officers and employees. There have been evidences of a greater interest, although I must say that the whole of our employees have been entirely loyal and interested and have resisted outside efforts to reduce or alienate their interests from the institution, almost 100 percent. It is more in gratification over the attitude of the employees that this plan was instituted than anything else. We feel that we are paying our employees more than the average institution engaged in the same business, based upon years of service and academic training and demonstrated ability.

We have had for a number of years other plans of employee benefits. We have a pension plan which costs the bank $350,000 a year, and provides for the retirement of our employees. It is discretionary with them as to whether they will join that plan or not. We started it about 4 years ago. We have practically a hundred percent participation. Then we have a group-life-insurance plan which provides $1,000 free of group life insurance on each employee receiving $2,400 a year or less, and the benefits under that plan run as high as $15,000.

Amounts in excess of $1,000 are paid for at low group rates by the individual officer or employee. The amount of insurance that you can secure is dependent upon the salary that you receive, and, as I say, the maximum is $15,000. There is a conversion privilege without medical examination for officers or employees who leave the service of the institution.

Then there is the sickness disability benefits plan, which has been in operation for probably 20 years, and provides one-sixteenth of the period of service of the employee, that is a salary equal to one-sixteenth of his term of service. If the man served 10 years, he could be ill for a year and receive full salary. However, that is discretionary with the committee which passes upon the need of the employee, the amount of his salary, and whether it should be accelerated or retarded. Sometimes if he is going to be ill for a longer while, they will divide his salary in half, if that is sufficient for him to get along on. Instead of paying it to him for a year, they will pay it to him in 2 years.

We have a group hospitalization and medical plan which entitles the employees to hospitalization and medical services at greatly reduced rates. The enrollment in this plan is now 65 percent of our personnel. It is increasing steadily. That has just been inaugurated.

Senator VANDENBERG. Is there any contribution by the employee to these later funds that you are describing?

Mr. GIANNINI. This one is entirely employee participation. The sickness disability benefits are 100 percent institutional benefits. And then that plan also provides, the sickness disability benefits, that if an employee is able to return to work for 3 months and then becomes ill again, the period begins to run anew—the period of his disability payment begins to run anew from that time. If he is out for 2 months and comes back and has withdrawn half of his benefits, he may withdraw the remaining half if he becomes ill in the lapse of a 3-month period.

I think that that substantially outlines our program with regard to benefits that we have provided for our employees.

Senator HERRING. I think you have stated that one of those was institutional benefits. You meant supported by the institution?

Mr. GIANNINI. Yes. The employees sickness disability benefits?

Senator HERRING. Yes.

Mr. GIANNINI. That is entirely institutional. That is supported by the bank 100 percent, and the salaries are paid out of current pay rolls to those employees.

Senator VANDENBERG. Is there any connection between the percentage of profit-sharing dividends and the earnings of the bank?

Mr. GIANNINI. Yes. The same percentages have been paid since the plan was inaugurated. It was inaugurated in May or June of this year, effective on last November 30, so that at the end of November of this year, it was in effect for a full year. The rate then was fixed by the board at 7½ percent, and 5 percent on the salaries over $6,000, and each month since then it has been similarly fixed at 7½ percent and 5 percent, because the earnings have remained constant during that period or on about the same level.

Senator VANDENBERG. Would it be your expectation that you had established a basic formula meaning that the earnings have entitled the employee to a 7½-percent dividend, and if those earnings were doubled, they would entitle him to a 15-percent dividend? Do you see what I mean?

Mr. GIANNINI. Well, I should think so. That would, of course, be discretionary with the board of directors. They, of course, would act upon the recommendation of the management, and certainly it would be my inclination if the earnings were doubled, to recommend a proportionate increase in the bonus.

Senator VANDENBERG. In other words, the 7½ percent on the existing earnings would be something of a yardstick?

Mr. GIANNINI. Yes. And, of course, there is no certainty that the 7½ percent would be—that the present bonus plan would be continued indefinitely. It depends largely upon the relations of the employees with the management and their loyalty to the institution. If we felt that there was any question about that, or outside influences entered into the affairs of our institution, then the board might very well change its opinion in regard to those matters.

Senator VANDENBERG. Is there always a floating supply of stock that can be purchased by trustees?

Mr. GIANNINI. Oh, there are four million shares of the stock outstanding. There is always a broad market in it.

Senator VANDENBERG. If a smaller institution were to proceed on your formula, where the stock is closely held and is not generally dealt in, it would be difficult if not impossible to operate on your theory, would it not?

Mr. GIANNINI. Not if those who were interested in the institution were willing to have the employees participate in its ownership and were willing to release stock to them at some agreed figure. Our plan provides for them to secure their stock on the open market or private sale or through new issues. There would be nothing to stop any institution from putting out new issues of stock to be acquired by the employees in this manner.

Senator VANDENBERG. Well, what I was thinking was if the bank's capital structure was adequate and complete and closely held, sales on the open market might be at a fictitious value—probably would be—and they would have to have some protection, would they not, of the price at which the trustees were to purchase it?

Mr. GIANNINI. Well, I cannot conceive of a plan like that being put in by a board of directors that was calculated to victimize the employees. They would have to have that attitude if they did not fix a proper price on the stock for the employees to buy it at. They could not put a price on it that would be way out of reason, and expect to sell it to the employees on that basis.

Senator VANDENBERG. I was not thinking of them being deliberately victimized. I was thinking of the possibility that they might be victimized by the sheer effect of the law of supply and demand in the stock market if there were very few shares available for sale. Your situation, with your large reservoir of stock, protects itself automatically.

Mr. GIANNINI. Yes; that is so. But as I say, I would imagine that a plan adopted in a smaller institution, would have to have the approval of the management, of the directors and stockholders, so that provision could be made to secure the stock at what would then be considered an equitable price.

Senator HERRING. Is this stock entirely at the disposal of the individual employee after 5 years?

Mr. GIANNINI. Entirely.

Senator HERRING. And if he quits before 5 years, is his equity measured by the market value of the stock at the time that he quits?

Mr. GIANNINI. Yes. The trustees have the alternative of giving him the stock that has been accumulated for his account, plus any uninvested amounts of cash or the cash that was deposited for his account within the 5-year period. After the 5-year period, he gets the stock willy-nilly.

Senator HERRING. We appreciate your coming, Mr. Giannini. If you have any other suggestions, we will be glad to have them.

Mr. GIANNINI. No; I have no other suggestions. I am very happy to have been able to tell you what I have.

Senator HERRING. You have been very helpful.

Mr. GIANNINI. Thank you very much.

Senator HERRING. Tomorrow at 10 o'clock we will have Mr. Willard H. Dow, president of the Dow Chemical Co.; Mr. Miles E. Robertson, general manager of the Oneida Community Co., New York; Mr. Edsel Ford, of the Ford Motor Co. of Dearborn; Mr. Herbert Daniel Brown, of Glendora, N. Y.; Mr. Lloyd Riford, vice president of the Beacon Milling Co., Cayuga, N. Y.; Mr. Walter Schwartz, president of Procter & Schwartz, Philadelphia, Pa., and Mr. Diedrich Gristede, of Gristede Bros., Inc., New York City.

We will take a recess until 10 o'clock tomorrow morning.

(Whereupon, at 2:20 p. m., a recess was taken until the following day, Tuesday, December 6, 1938, at 10 a. m.)

SURVEY OF EXPERIENCES IN PROFIT SHARING AND POSSIBILITIES OF INCENTIVE TAXATION

TUESDAY, DECEMBER 6, 1938

UNITED STATES SENATE,
SUBCOMMITTEE OF THE COMMITTEE ON FINANCE,
Washington, D. C.

The committee met, pursuant to adjournment, at 10 o'clock a. m., in room 312, Senate Office Building, Senator Clyde L. Herring (chairman) presiding.

Present: Senators Clyde L. Herring and Arthur H. Vandenberg.

Senator HERRING. Mr. Gristede.

STATEMENT OF DIEDRICH GRISTEDE, GRISTEDE BROS., INC., PARK AVENUE AND ONE HUNDRED AND TWENTY-EIGHTH STREET, NEW YORK, N. Y.

Senator HERRING. Mr. Gristede, I understand you have had a profit-sharing plan for a great many years.

Mr. GRISTEDE. Since 1897.

Senator HERRING. Will you give us a brief history of how you came to adopt it, the policies, and how it has worked out?

Mr. GRISTEDE. We started in business in 1891, my brother and I, and we had two stores up to 1897. In 1897 we started our third store, and we thought it would be a good idea to take in the manager—at that time it was only the manager—as a partner in profit sharing. We started right in with our third store, made the manager profit sharing. Later on, when we grew bigger, or had more stores, we thought it would be a good idea to take every one of the employees in, and today we have every one of our employees in profit sharing.

Senator HERRING. How many employees do you have?

Mr. GRISTEDE. Around 1,600. We find in taking them in profit sharing that there is no waste, that they are careful to make profits. In fact, we tell them at the beginning that in order to get this bonus and be in with the profit sharing they must produce the profits. They are very careful, as I say. There is hardly any waste. In our business there can be plenty of waste if they are not careful, because we sell fruits and vegetables, which you know are perishable, and it is remarkable what profits we can produce that way.

Senator HERRING. You have a standard, basic wage that is equal to what is paid elsewhere?

Mr. GRISTEDE. We do not pay on the percentage basis, as a good many others do, because we have a small business only. At the end of the year we find out how much money we have made, and we set aside a good portion of it. In fact, in the last 2 years, since we have the undistributed profits tax, we have been giving more liberally, in fact, we have paid nearly all the profits.

Senator HERRING. You have a drawing account?

Mr. GRISTEDE. Yes; we pay each man a living salary. In fact, we pay him as high a salary as anybody in the business pays.

Senator HERRING. Before there is any division of profits?

Mr. GRISTEDE. Before there is any division of profit.

Senator HERRING. That division of profit is made once a year?

Mr. GRISTEDE. We used to do it twice a year, but when the depression came along we found at the end of the summer the profit was not so big and we passed it, and now we give it once a year. We have paid a profit, and a good and liberal one, every year.

Senator HERRING. Is it based on the base wage?

Mr. GRISTEDE. Practically, yes; but it is not on the percentage basis, because once in a while a man may do an outstanding job during the year and we compensate him extra.

Senator HERRING. What would you estimate the annual wage is that you pay?

Mr. GRISTEDE. The annual wage, you mean of the clerks?

Senator HERRING. Yes.

Mr. GRISTEDE. We pay the clerks from about $21, for junior clerks, up to $35.

Senator HERRING. Per week?

Mr. GRISTEDE. Per week. That is for the clerks. Of course, the manager receives up to $50 a week, and one-third of the profit in the store which he manages. For instance, we open a new store today and put a manager in there, and we pay him so much a week, say from $35, if it is a small store, up to $50 in these big markets, and one-third of the profit that that store produces. Then we bill him according to the overhead, and whatever profit he makes he gets one-third of that.

Senator HERRING. The manager receives that?

Mr. GRISTEDE. Yes.

Senator HERRING. What about the clerks?

Mr. GRISTEDE. They get paid on the bonus. All the clerks are paid on the profits that is produced by the firm.

Senator HERRING. What bonus would you estimate a man would get that is making $21 a week, the junior clerk, what would you estimate he would get?

Mr. GRISTEDE. The junior clerk may get from $100 to $150.

Senator HERRING. In addition to that?

Mr. GRISTEDE. Yes. I have a list here from which I can tell you pretty nearly what it has been. The salary of all the employees—that is the expense of the business in salaries, you understand—amounts to about 14 percent. That is including all the high-priced men, of course, the executive bonus amounts to about 2.79 percent. That is what it was exactly for the last 10 years.

You see before we started in business, I worked for a firm where there was not any profit sharing, and I felt I was entitled to a little more (if I was ambitious) than I was really getting. I was getting a straight salary, and I know if I was looking for a position today, I would want to get some of the profits, if I was worth it, and if I was not worth it, I would be ashamed to take the salary.

Senator VANDENBERG. You mean each one of the 1,600 employees is individually rated?

Mr. GRISTEDE. Well, the order boys bonus is small.

Senator VANDENBERG. I mean do you make an individual rating for each one? Do you apply individual merit rating to each clerk?

Mr. GRISTEDE. Yes. You see, we have districts, and at the end of the year we take it up with the superintendent. He puts in the list. We give him the amount of what he is supposed to distribute, and then he gives us a list of what he thinks each man should have. It is generally done on a percentage basis, but as I said before, some of them are a little better than others and we give them a little better bonus.

Senator VANDENBERG. You encourage your employees to buy stock in your company, do you not?

Mr. GRISTEDE. We do, but we do not let them buy any stock with foreign money. That is, we would only let them buy stock with money that they have made in the company, because we are not anxious to sell stock. You see, we pay them about 7 percent on the stock, and we can borrow money for a lot less. In fact, we do not need the money, but we do it more for the morale purpose of getting their interest.

Senator VANDENBERG. Do you offer any inducement to them to buy your stock? Do you make it easy for them to buy it?

Mr. GRISTEDE. Well, yes; we let them buy as little as two shares. That is about the least we sell. In fact, we have today—I believe you have the record there, I believe we gave you that, as to the stock owned by the employees.

Senator VANDENBERG. Six hundred eighty-one thousand seven hundred dollars worth of stock owned by your employees.

Mr. GRISTEDE. Yes.

Senator VANDENBERG. Out of a total of what?

Mr. GRISTEDE. Well, I think we have sold in the neighborhood of about $1,000,000 worth of stock. That is the preferred stock. Of course, the controlling stock, some of the executives own. We do not let everybody in on the controlling stock, of course.

Senator VANDENBERG. Is this preferred or common stock that the employees buy?

Mr. GRISTEDE. Preferred stock. That pays a guaranteed dividend of 7 percent, and during the good days we used to pay them as much as 9 percent on it, giving them $2 a share extra. We employ all nationalities, and we find it is good business to employ all nationalities.

Senator HERRING. Well, on an average wage for a clerk of about $1,000 he would get about $150 bonus?

Mr. GRISTEDE. He gets, according to this, $150. That would figure that way. We have been very liberal with our bonus all the time, because we figure you cannot take it with you, as you heard, I guess, so we have been very liberal. Of course we are getting a good salary ourselves and we are satisfied.

Senator HERRING. Is that bonus increased by length of service?

Mr. GRISTEDE. Yes.

Senator HERRING. Do you think it has reduced your turnover and increased loyalty and efficiency of the employees?

Mr. GRISTEDE. It certainly has.

Senator HERRING. You are satisfied it is good business?

Mr. GRISTEDE. One thing, as I said before, it saves waste, because they are very particular, they know very well if they throw anything away they are going to lose one-third of that. That is the managers, of course.

Senator HERRING. Of course they start pretty low, $1,000 a year.

Mr. GRISTEDE. What is that?

Senator HERRING. They start pretty low with $1,000 a year.

Mr. GRISTEDE. Well, they are practically the boys, the order boys, you see. The order boys get from $17 a week, up to the clerk. The junior clerk starts around $21, but he works his way up very quickly if he is good.

Senator VANDENBERG. You also have group life insurance?

Mr. GRISTEDE. We have group life insurance.

Senator VANDENBERG. Is that all paid by the company?

Mr. GRISTEDE. At the company expense. We have group life insurance, we have endowed hospital beds, we have a social club, our boys have a social club, they have about 1,000 members, and they have in the treasury quite a little money. They bought here some years ago a bed in the hospital, they provided for that, and, in fact, we have two there now. If any of our employees get sick, they go to the hospital and do not have to pay anything. We try to make it very interesting for our employees, and that is why we have all these activities. In fact, these boys have meetings every 3 months, and they have different little activities in there. As you see from your record there, Senator, we have been very liberal. In fact, we have been so liberal that the income-tax man checked up on our records one day and he thought we ought to have our brains examined, because we gave so much money away. He thought they would not appreciate it. I would like to meet him today.

Senator HERRING. The only organization you have is just your own company organization—labor organization?

Mr. GRISTEDE. It is our own organization; yes.

Senator HERRING. Is the amount of this bonus—is that ever discussed or negotiated with representatives of the employees, or would you just arbitrarily set it?

Mr. GRISTEDE. The salaries?

Senator HERRING. The bonus.

Mr. GRISTEDE. No; we set the sum aside. There are never any questions asked that the bonus is not big enough.

Senator HERRING. Do you discuss it with them—that is, do you get their ideas?

Mr. GRISTEDE. We discuss it with our superintendents, the superintendents of the different districts.

Senator HERRING. There really is not any negotiation with the employees?

Mr. GRISTEDE. No.

Senator HERRING. All right, thank you, Mr. Gristede. Mr. Dow?

STATEMENT OF WILLARD H. DOW, PRESIDENT, THE DOW CHEMICAL CO., MIDLAND, MICH.

Senator HERRING. I am glad to meet you, Mr. Dow. I have had several letters in the last 2 or 3 months from an employee of yours asking why we did not talk with his boss, that he is the best boss in the world.

Senator VANDENBERG. This is one of the best institutions in one of the finest States in the Union.

Senator HERRING. You just proceed in your own way, Mr. Dow, and tell us about this system of yours.

Mr. DOW. It is a little difficult to know how to start a discussion like this, but maybe the best way to proceed would be to comment in general on the idea that in chemical manufacture there is a rather exacting need for careful control. There is a need for exacting control and supervision of the processes more than in many other instances of other manufactures, and so in the early days when the company was quite small and it was realized that the necessity for personnel supervision was a bigger item than equipment, the thought of developing profit sharing came into being. That was some time before the war. The company organized in 1897 and it did operate under some sort of a profit-sharing system way back in those early days, covering as few as two or three men in the organization, and then as the company grew the principle and the advantages of a type of profit-sharing were apparent and the system was elaborated on.

Beginning with about 1916, I believe, the present system has been in operation, or approximately the same general system, the general form.

That system, in brief, is designed on the principle of—I do not know whether you want me to repeat anything that is in this report or not?

Senator VANDENBERG. Go right ahead and make a complete record.

Mr. DOW. That system is designed on the principle of paying the profit sharing after all allowances for taxes and depreciation, and also a return on capital.

That factor, right there, is a rather interesting one. In the early days we felt that a return of 12 percent on capital was a justified return. In about the last 3 years, I think it is, maybe about 1935, that was changed to a 10-percent return. When I say "return on capital" I refer to those general items including interest on capital and all other charges, amortization, and factors of that sort.

After earning the 10 percent, we then take the net earnings in any one month period, plus any other profits received, like dividends from subsidiaries; then we take 20 percent of the difference between the 10 percent return on the capital and the total earnings, and this is then considered the bonus allocation. That item is divided into two parts, 40 percent for supervision and 60 percent going to the men in the plant, I mean, going to all others.

Senator VANDENBERG. Let us just see how it works out. First you would take off your 10 percent capital charge, that leaves you 90 percent of the net earnings, and you take 40 percent of the 90, is that right?

Mr. Dow. No, that is not quite correct.

Senator VANDENBERG. I mean 20 percent of the 90 percent?

Mr. Dow. Just put it down the other way around.

Senator VANDENBERG. All right.

Mr. Dow. The total earnings, and then we deduct from the total earnings the 10-percent item for the monthly period, and 20 percent of the remainder.

Senator VANDENBERG. Well, is that not 20 percent of 90 percent?

Mr. Dow. No, it actually is not, because the 10 percent is 10 percent per year and this is on a monthly basis.

Senator VANDENBERG. Yes.

Mr. Dow. In other words, the monthly statement is five-sixths of 1 percent.

Senator VANDENBERG. Then the 20 percent is again divided 40 and 60, is that right?

Mr. Dow. That is right.

Now it may seem strange that we pick a figure like 20 percent, but over a period of years that has seemed a proper figure. It might be that that would have to be a modified percentage, but it has seemed to be about accurate. We did modify the 40- and 60-percent division. Some years ago it used to be 50–50. That really started with the N. R. A. days. We thought the proper allocation was 40 and 60. That is, may be a little too much in detail, as far as that general item is concerned.

Senator VANDENBERG. Before you leave it, how many employees, Mr. Dow, do you have? About 4,000?

Mr. Dow. The maximum was up to 4,340, and at the present time it is around 3,600.

Senator VANDENBERG. And do all of the 3,600 participate in either end of the distribution?

Mr. Dow. All except the president and the treasurer of the company.

Senator VANDENBERG. And what would that mean?

Mr. Dow. And that includes some directors who are not full-time employees.

Senator VANDENBURG. What would that mean in dollars and cents, in a typical average employee's case?

Mr. Dow. Maybe I could answer it a little differently than that. In 1937, our average annual wage was $1,935. Of that about $60 to $80 was the bonus, the profit bonus.

It possibly does not seem like such a big item, but paid in monthly installments it represents enough of an item so that it is very beneficial. We do not pay on the annual basis. As a matter of fact, we do not believe in the annual bonus. We believe that a bonus to be successful should be paid as soon after the money is earned as possible, which in our case usually is during the month following the earnings.

Senator VANDENBERG. Now, when this 60 percent goes to the mass of your employees do they all share equally in it?

Mr. Dow. Yes; with this qualification: a man has to be employed 6 months before he participates, and then he participates on one-half the normal basis. At the end of 1 year he is on a full profit-sharing basis or bonus basis, whichever you want to call it.

Senator VANDENBERG. Well, now, in addition to this you have both the pension and insurance plans?

Mr. DOW. That is right.

Senator VANDENBERG. Are those financed primarily by the corporation, or are they contributory?

Mr. DOW. The pension plan only covers that group of employees who do not participate in Social Security, in other words, 60 years or older. The insurance plan is participated in by all the employees, and there is a sick-accident benefit along with that, which the employees contribute to. The company buys the insurance.

Senator VANDERBERG. What do you think has been the effect on employee morale and employee loyalty, and your general employee relationship?

Mr. DOW. We feel very keenly on that subject. We think that a bonus system is a very vital and important factor in our organization. I do not mean to imply by that statement that it necessarily is a foregone conclusion that it applies in every industry, but we feel it does in our industry. We have had very satisfactory employee relationships.

Senator VANDENBERG. You not only got the social satisfaction out of it, but you also feel it was good business?

Mr. DOW. We certainly do.

Senator VANDENBERG. Have you given any thought to the possibility of incentive taxation in respect to any of these problems?

Mr. DOW. Yes; I will say we have given thought to it.

Senator VANDENBERG. I would be glad to hear any ideas you have on the subject.

Mr. DOW. Well, I think it would be a good idea to be perfectly frank about it.

Senator VANDENBERG. Exactly.

Mr. DOW. Although incentive taxation is bound to be beneficial in certain instances, we would hate to see this the beginning of a trend of government getting into telling an industry how to develop a profit-sharing or bonus system.

Senator VANDENBERG. I agree completely on that.

Mr. DOW. The vital thing about a successful profit-sharing plan is to have one that fits the needs of the industry that it serves. I do not know as I would personally understand how the Government could put in a broad form of incentive taxation without at the same time dictating what the regulations would have to be in order to conform to that. On the other hand, to go a step further, it seems to me the principle is a whole lot like expecting a board of directors consisting mostly of bankers to run a technical industry that they do not know much if anything about. I think the vital thing is that an industry that is best run is certainly one that is run right within the industry itself.

Senator VANDENBERG. That—there is not any doubt in the world about that.

Mr. DOW. The same principle applies on bonus, profit sharing, or any of the other things. If they are analyzed from the immediate needs of the company in question, they are bound to be the most successful.

Senator VANDENBERG. I was thinking of incentive taxation in a little broader sense when I submitted the interrogatory to you, Mr. Dow. Do you think in the larger field of encouragement to plant expansion and encouragement to equipment replacement a system of tax compensation could be helpfully created?

Mr. DOW. I think I could answer that question by best saying that it is a vicious cycle. When business is off from its normal, in order to improve business we look to the idea of spending money and raising taxes, and hope that by spending money and creating new work which costs money that we will pull ourselves out of the depression. Actually, I think everybody will agree that the facts of the case are quite the opposite. Suppose I am in a depression personally and I do not quite have finances enough to meet my obligations, I do not have any sugar daddy to go to to get funds to keep me going, I must necessarily curtail my expenses, because if I do not, why, things get worse and worse. I feel that that is the situation we are in right now. The worse off we are, the more we want to expand, and the more we want to expand, the worse off we are. It keeps on indefinitely

Very frankly, I cannot see where this incentive taxation could especially relieve, in a very big way, the present depression on business. Everybody knows that money is scared. Any number of industries right at the present time should be developed, but it is almost impossible to get the capital to develop them. There are good things that should go ahead, but there is uncertainty and they do not do it.

Senator VANDENBERG. The incentive you prefer is to have government mind its own business?

Mr. DOW. I think that is properly stated.

Senator VANDENBERG. Considerable can be said for that. Thank you very much, Mr. Dow.

Senator HERRING. Mr. Dow, your average wage is about $2,000. That would indicate that you are paying the prevailing wage scale. There is no question about that, is there?

Mr. DOW. Our prevailing wage scale is quite considerably above the average for the country. I have here a statement that the average wage scale for the country is $1,266, and ours is $1,935.

Senator HERRING. You have never had any labor troubles?

Mr. DOW. We have never had any labor troubles until the C. I. O. activity in Michigan. They brought about a hearing with the National Labor Relations Board.

Senator HERRING. Are your employees organized under C. I. O.?

Mr. DOW. No; they are not. They have an organization that they created themselves.

Senator HERRING. The National Labor Relations Board hearing has not been held yet, has it?

Mr. DOW. The final decision has not come down.

Senator HERRING. What I was trying to get at was this average wage being at least the normal wage.

Mr. DOW. That is above normal. As a comparison, the hourly rate with us, the average is 88.4, and the national average is 74.2.

Senator HERRING. Then what they get in addition to that is clearly profit-sharing.

Mr. DOW. Yes.

Senator HERRING. What percent of $100 profit goes to stock dividends and what percent to the employees? Could you estimate that?

Mr. Dow. I do not know that I have that figure. The ratio is the pay-roll dollar to the net-profit dollar, and those items are in here. Did you want that?

Senator HERRING. We have that.

Mr. Dow. I could give it this way: In 1937, the pay roll of employees was 6½ million dollars, approximately, the dividends paid during that same period were just under 3 million dollars.

Senator HERRING. And the bonus to the employees in addition, do you have that?

Mr. Dow. That would be included in that total pay roll. I do not have that separately.

Senator VANDENBERG. I noticed one statement in one of your letters, which is an interesting comparison: "You will note that we refer to the bonus earned by the men over an average so-called normal year is approximately equal to the dividends paid to the company on 20 shares of stock."

Mr. Dow. That is right. Unfortunately, during the last 10 months, I believe, we have not paid any bonus or profit-sharing.

Senator VANDENBERG. Why not?

Mr. Dow. We haven't had the earnings.

Senator VANDENBERG. That is very conclusive reasoning.

Mr. Dow. In other words, we operate the profit-sharing on the basis of when there are profits there is a bonus, and when there are losses there is no distribution, or to put it in another statement, that the earnings have to be at a certain ratio in order to pay a bonus. We feel that that is the only safe way to run the bonus system because otherwise it could leave one rather high and dry.

Senator HERRING. The most profitable years, though, have been the last two or three, have they not, up until 1938?

Mr. Dow. That is right; beginning with about 1934.

Senator HERRING. I think that is everything that I have in mind, Mr. Dow. Thank you very much for coming here.

Mr. Ford.

STATEMENT OF EDSEL B. FORD, FORD MOTOR CO., DEARBORN, MICH.

Senator HERRING. We know that the Ford Motor Co. were pioneers in high wages and sharing everything, and if you will just proceed in your own way, Mr. Ford, we would appreciate it. Tell us about the beginning of it.

Mr. FORD. We have had a policy since 1914 of paying what we think is above the going rate of wage in our industry. We started out by announcing what was called a profit-sharing plan in January 1914, and that was when the so-called $5 a day minimum wage was introduced. I think the going rate at that time was 34 cents an hour, and we raised it an additional 28.5 cents an hour, which made a total of $5 a day for an 8-hour working day.

This profit-sharing plan continued in force until 1920, when a minimum hourly rate of 75 cents per hour, or $6 a day, was established, and the profit-sharing factor, so-called, was changed to a straight $6 a day minimum wage, not dividing it between the going wage plus the additional compensation, so-called profit sharing.

The rates were changed on various occasions and the minimum has been increased from $5 to $6 a day, which prevails at present, although there was one time during the depths of the depression when we got down as low as $4 a day. I am talking about minimum wages now, not average wages.

Senator HERRING. Yes.

Mr. FORD. I have some statistical figures here as to the amounts paid out, and that sort of thing, if that would be of interest to you.

Senator HERRING. We would be glad to have it in the record.

Mr. FORD. During the period in which the profit-sharing plan was in effect the amounts paid out in excess of the established wage was approximately $77,565,000.

Senator VANDENBERG. That is up to what year?

Mr. FORD. That was during the time the profit-sharing plan was in effect; therefore, that would be from 1914 to 1919. Then after that we went on a straight daily wage.

Senator HERRING. You continued paying the same amount, and even more, but you just did not charge it up as profit sharing?

Mr. FORD. We changed the method of procedure, but it amounted to practically the same thing.

The next scheme that was put into effect was the so-called cash bonus plan. This was paid to the employees in the years 1920 and 1921 for the years of 1919 and 1920, respectively. These bonuses were based upon employees' rates of pay, together with length of service, and amounted to approximately $6,750,000 a year for those 2 years that that scheme was in effect. The bonus plan was discontinued on January 1, 1921, in lieu of which salaries and wages were increased proportionately in accordance with the schedules. In other words, we started this plan, and then after we had been with it for a certain time we felt by simplifying it we could operate better, so we averaged it up to what we had paid and went on from there.

Senator HERRING. You just paid the wages afterward?

Mr. FORD. Yes. We have at the present time a so-called investment plan. The employee's investment plan was inaugurated in January 1920. This plan, in brief, extended to each and every employee the privilege of depositing with the company a percentage of his wage or salary, on which he received a guaranteed rate of interest, originally 6 percent and subsequently on March 1, 1933, reduced to 4½ percent, which is the rate now in effect, plus a special return paid semiannually as determined by the board of directors. The special return has amounted to as much as 10 percent per annum plus the 6 percent. I know we have paid up to 16 percent. We have had as high as $22,000,000 in that fund at one time, and at the present time, as it stands today, there is about $14,000,000 in the fund. The employee is allowed to invest 25 percent of his wage as he receives it. He is paid this minimum interest plus the bonus, and it has run, as I say, from 16 percent down.

Senator HERRING. What percent of the employees would you estimate took advantage of that?

Mr. FORD. I asked for those figures before I left, but it was impossible for me to get them. There is a substantial percentage, I should say, of the older employees that perhaps have been there longer and can put aside a certain portion of their wage, without hampering them too much. They are taking more advantage of it than the men of more recent employment, who require all they earn to maintain themselves.

Senator VANDENBERG. What is the fund invested in?

Mr. FORD. Well, it is not invested in anything in particular. We carry it as a separate account.

Senator VANDENBERG. I see.

Mr. FORD. It is payable on demand. It is a company fund, of course.

Senator VANDENBERG. A company fund?

Mr. FORD. A company fund. That was $14,203,000 as of October 31, 1938.

Up to and including the payment to June 30, 1938, the total of interest and special return under the investment plan amounted to $27,813,000, being made up of guaranteed interest of $15,773,000 and special return of $12,039,000.

Senator HERRING. That is clearly profit sharing.

Mr. FORD. That is profit sharing.

Senator HERRING. In addition to that, you have the hospitalization, the old-age pensions?

Mr. FORD. We have whatever laws require. We have no plan of hospitalization of our own.

Senator HERRING. You do not?

Mr. FORD. No; we do not. We have always been of the feeling that, if we paid our men as well as we could, that they were more independent and willing to take care of their own responsibilities, and they liked it better than if we had some of these plans that might be somewhat paternalistic.

Senator VANDENBERG. Well, that equally applies, evidently, to your theory of profit sharing, for it seems to have had an evolution, and you have come to the point where your theory of profit sharing today is through the direct highway.

Mr. FORD. That is the way we feel, Senator.

Senator VANDENBERG. Of course, that holds true with profit sharing as well as anything else.

Mr. FORD. Anything above the prevailing rate in an industry, I suppose, might be called profit sharing.

Senator VANDENBERG. Exactly.

Mr. FORD. We have been very strong believers in the very highest possible wage we could pay.

Senator HERRING. I recall very well when the $5 minimum went in everybody else thought it was profit sharing.

Mr. FORD. That was a great increase over the prevailing rate.

Senator VANDENBERG. We have been interested, Mr. Ford, in the subject of incentive taxation along with this subject of profit sharing. I am not tying the two up together in my question to you. In the larger field of incentive taxation, have you ever given any thought to the possibility, speaking generally, of American business that tax credits for plant expansion, tax credits for equipment replacement, tax credits for regularizing employment might be a useful public policy and an encouragement to these achievements?

Mr. FORD. Well, my feeling would be that a reduction in taxes in general would be as good an incentive as any. I suppose with incentives of that kind it always has an appeal, no question about that, but it leads to complications, and I should think the consequences that would follow might be difficult to handle. I do not know, really. It is a question that might be debated for a great length of time.

Senator VANDENBERG. You fear we might create more problems than we would solve?

Mr. FORD. I would feel that you might.

Senator VANDENBERG. I think that is all.

Senator HERRING. In all these years, with all this profit sharing, the Ford Motor Co. has never had any labor trouble?

Mr. FORD. That is right. We feel we never have.

Senator HERRING. Undoubtedly part of it is due to the fact that they have been fair in their wages and profit-sharing methods.

Mr. FORD. Well, we have tried to be more than fair. We have believed earnestly in paying just as high a wage as we possibly can and producing at just as low manufacturing cost as we can, therefore creating large volume. That has been our cardinal policy, as you know, for a long time.

Senator HERRING. Yes. That seemed to be the general opinion, too, I think. If you have any other suggestions we would like to have them.

Mr. FORD. I do not at the moment, but I would be very glad to furnish you with any data that we have for the record.

Senator HERRING. You have given us a lot of valuable information.

Mr. FORD. If there is anything further that you think of, we would be very glad to supply it.

Senator HERRING. Thank you, Mr. Ford.

Mr. Robertson.

STATEMENT OF MILES E. ROBERTSON, GENERAL MANAGER, ONEIDA, LTD., ONEIDA, N. Y.

Senator HERRING. This is one of the oldest cooperative organizations in the United States. It was established in 1850, originally on a communistic basis and later changed to a commercial basis in 1880. Is that correct?

Mr. ROBERTSON. That is approximately correct.

Senator HERRING. Do you have the profit-sharing plan now?

Mr. ROBERTSON. No formal plan. Some years ago, in 1923, we did formulate a plan. In fact, the perfectly formal plan was a profit-sharing plan, based on service as well as base wage. We are believers in service. At that time our formula was that after net profits and taxes were paid, and preferred dividends paid, then 7 percent was set aside for common stock and surplus. Of the remaining balance, 50 percent was distributed to the employees of the company as a profit-sharing plan. The distribution was based on 25 percent of the year's wages earned of all employees and 75 percent on the service wage.

The service wage may bother you a little bit. We pay not alone the regular wage but we pay a service wage, depending on the length of service in our company. After 1 year of service the employee gets

5-percent service wage; after 2 years, 6 percent; after 3 years, 7 percent; after 4 years, 8 percent; after 5 years, 9 percent; after 10 years, 10 percent; and after 20 years of service, 11 percent. That percentage is based on weekly earnings. That service wage is paid to all employees other than salaried employees.

That profit-sharing plan was abandoned, so far as the straight formula is concerned, in 1930. A profit-sharing plan without formula has been reinstituted in the last 3 or 4 years, and we paid a profit-sharing bonus in 1935, 1936, and 1937. In 6 of the 7 years between 1923 and 1930, we paid $1,450,000, and in the last 3 years about $300,000.

Senator VANDENBERG. And on what basis was the profit-sharing dividend paid the last 3 years, did you say?

Mr. ROBERTSON. No particular basis. Perhaps I should explain that we were not in a financial condition to warrant setting up a formula in advance, due to the distressed conditions resulting from 1931, 1932, and 1933. We felt there were other things to do which were even more important, such as medical help to our employees, and so forth.

It was a matter of how much money we earned, and that determined how much money should go back to the partners in the business, on whatever basis seemed wise.

In the last 3 years approximately $300,000 has been distributed among 2,500 people.

I might say that while we like profit sharing and think it very necessary, we do not think it of primary importance. We think it comes after many other things. It seems to us that we must pay a basic wage which is at least the prevailing wage or above it; that we must have ideal working conditions; that we must have pension plans; that you must have group insurance; you must have medical help; we must have your social activities; that we must have such relations in our plant that there is a free interchange of information. Sometimes that costs money, depending on the way it is done. In other words, the profit-sharing plan itself is not the important thing. The main feature to us is whether we have the confidence of our employees. We do not believe that profit-sharing plans are the cause of anything; they are results. If we have the confidence of our employees to start out with, and we must do these other things to obtain that confidence, then profit sharing is valuable. We believe in it as a principle, but it must come following certain other definite things.

Senator VANDENBERG. In other words, it cannot be a substitute for fair play?

Mr. ROBERTSON. It cannot be a substitute for all those things that the average manufacturer must do to take away distrust and suspicion which are naturally between stockholders and employees, or between employers and employees.

Senator HERRING. Well, although you discontinued it in 1930, in a formal way, you are still sharing profits, are you?

Mr. ROBERTSON. Yes, sir.

Senator HERRING. Just why did you discontinue the formal plans that you had at that time?

Mr. ROBERTSON. We ran into red ink, and there were no profits to distribute. When we were ready to pick it up again with the resumption of profits, there were other things that had to be done with our working force, the people we were working with, which were more important at the moment than anything else, such as medical help. We have about 2,500 people, and this is only one point.

To illustrate my statement, we found they had neglected their health, their teeth, eyes, tonsils, hernias, and so forth, all of these ills that come forward in the manufacturing business. So one feature we call profit sharing was to have our doctor examine every person in the plant; and where he found they needed medical help, our board appropriated enough money to pay half of the expense and to loan the other half to the employee, so he could be put in good condition again. In the depression the average man, with a short week in his envelope, is pretty apt to neglect his wife, pretty apt to neglect his children, and himself. He is pretty apt to neglect his children first, his wife next, and himself last.

I do not believe such plans can be formularized in any sense of the word. We are very fortunate. We live in the country, we have our own city, our own town, and therefore can be a community in every sense of the word, and therefore can live with our people and know them intimately.

We have a policy of building entirely from within. We do not hire from the outside, in the sense of hiring experts. Every man has an equal opportunity to go as far as he will. We do not pay exorbitantly high salaries. We believe in less at the top; we believe that there should be more at the bottom. Obviously, all those things having been done, it is natural that we should have the confidence of our people.

Senator VANDENBERG. What happened during the depression, when it became necessary to discharge employees, or lay them off? Did you share the work or did you lay men off?

Mr. ROBERTSON. Between 1929 and 1932 we both shared the work and laid off. The lay-offs we made on the basis of service and, to some extent, where there were two in the family employed; in other words, our personnel department is supposed to know intimately as to the family situation of every employee, and perhaps if a man and wife were working, or man, wife, and boy were working, the lay-off would be conditioned by that. Since 1933 we have gone even stronger on the question of sharing work. For example, this past spring business was slack, and the sharing of work was done by a division of work, and it affected everybody on the pay roll, as far as that could be done. I should say out of 2,500 people we kept perhaps 400 extra people on the pay roll.

Senator VANDENBERG. Were wages reduced during this period?

Mr. ROBERTSON. Not during this period, but during the depression period wages were materially reduced. There is no particular difficulty in that. We believe in disseminating information all the way through the plant. At the end of each year we have a meeting with all employees. We do not do anything by proclamation. We call together 2,500 employees, and the president of our company and myself tell them of the year's results, whether they are good or bad. We make a report to our employees before we make a report to our stockholders. We tell them exactly what happened, whether there is a profit or whether there is not a profit, whether there is to be a wage change. If we have to make a wage change downward, we call them together and tell them why. No one is left uninformed.

Then through the year we have foremen's meetings, perhaps 100 of our foremen and minor executives, and those men are kept in touch with the condition of the company, the sales, and what is going on; or if we are about to institute any new policy of any kind, it is thoroughly explained and discussed. In fact, a policy would not be put in that our average man in the shop did not think was a wise policy.

Senator HERRING. Your statement shows that the amount of annual pay roll has dropped from 3½ million plus in 1929 to about 2 million in 1933.

Mr. ROBERTSON. That was a joint product of two things. One was lay-offs. In 1929 we were paying about 27 to 28 percent above the average of the higher paid in our industry, and we reduced it down at that time perforce to about the average pay in our industry. Of course, our people are perhaps a little bit better off in the sense that they live in a small town and they have, therefore, a lower cost of living.

Senator HERRING. In 1934 you paid $4,000,000, or double what it was in 1933. Was that due to increased wages or increased employees, or both?

Mr. ROBERTSON. It is a combination of both, Senator. We had to drop the service wage at that same time, and the service wage has been reinstituted. As I indicated, we believe a service wage is even more important than the profit sharing. That has to come first.

Senator VANDENBERG. Have you had any labor trouble?

Mr. ROBERTSON. We have never had any labor trouble.

Senator VANDENBERG. Do you find, when you make this frank disclosure to the employees that you have a bad year and there is a necessity for readjustment downward, they accept your statement at full face value and are willing, on the basis of your frankness with them, to cooperate without complaint?

Mr. ROBERTSON. I believe so, sincerely. Of course, we are very frank with our employees.

Senator HERRING. You tell them the facts about business?

Mr. ROBERTSON. We tell them the exact facts, even more than we print in the newspaper. We tell them the exact facts as well as conditions, as to why we do it; we tell them those things very frankly. This policy dates back to 1932. We told them then that the continuance of a company, the continuance of a place to work, was more important at that moment than perhaps a large wage, and I think our employees generally know that. By "employees," mean everyone on the pay roll—we are all employees in that sense. Everyone knows we could price ourselves by what labor is worth in the market. We try to dissemble that information.

Senator VANDENBERG. One witness a few days ago, who similarly believes in complete frankness between employer and employee, raised the interesting point that he found himself restricted by the Wagner Act in his discussions with his employees; he was afraid he could not talk to them quite as frankly as heretofore, unless he be suspected of trying to mold their attitudes.

Mr. ROBERTSON. He may be right. We have had no such fears.

Senator VANDENBERG. You have not been indicted yet.

Mr. ROBERTSON. If you walk your normal course, that is one thing; but if you should decide to do something today that you had not been doing yesterday, or the day before, that might be another thing.

Senator VANDENBERG. I think that is an excellent discrimination.

Senator HERRING. Your employees are not organized, are they?

Mr. ROBERTSON. Our employees are not organized. All employees belong to a club; that is, everyone from the president to the office boy. We do not believe in any caste system of any kind. There is one club which has a town house and a house in the country, a place on the lake, that 25 of our parent plants belong to, and our Canadian plants are also subsidiaries of this club. This club is run entirely by the employees. Every person is a member. There are 12 bowling alleys, pool and billiard rooms, ladies' rooms for society parties, cooking parties, educational classes, and then at the lake this club has about 16 acres on which there is a large hotel, a bathing beach, and a place for boating on the other side. It is a spot where people may go to take their families, or where people who are recuperating from illness may go at no cost; there is no cost at all, except the rent of the cottage.

Senator HERRING. When you found it necessary to lay quite a number off in 1932 and 1933, did they come back?

Mr. ROBERTSON. Yes. We keep an exact record of each person, and if they are satisfactory—and by "satisfactory" I do not mean necessarily that they may or may not be ill, have physical ailments—if they have been employees, and good employees, good partners in the business, their records are kept, and when we rehire we rehire on the basis of those whom we lay off.

Senator HERRING. I think that seems to cover everything unless you have something you would like to put into the record, Mr. Robertson?

Mr. ROBERTSON. Only one thing on this question of incentive taxation. Frankly, I do not see how that can be formulated if we discuss profit sharing in its narrow sense, but if we discuss it in its broader sense, which is perhaps the way you are thinking of it, it seems to me that there are several different things which must be gone into. For example, I believe there is an interpretation by the Internal Revenue as to pension payments. I think the Internal Revenue would prefer and accept more easily payments that are made to a pension plan if they are made regularly. You should not make it $100,000 one year and $10,000 next year, and nothing the following year. It is conceivable that the company's profits vary that same way, and therefore in very good years they might build up their pension plan reserves, and in their bad years they might do as little as they had to. I believe that is somewhat frowned upon. So the thought of incentive taxation might go toward some thought on that particular phase.

Another point—and I am only using these as examples of the field rather than in its narrowness—I do not believe there is any incentive taxation on profit sharing in its narrow sense.

Another point: In the social-security taxes now which are paid on pay roll, if we keep 300 or 400 people on our pay roll, that means we are paying an unemployment tax on that pay roll. The other manufacturer who might eliminate those 300 or 400 people would have no pay roll, and therefore no tax. Those people would go on relief. It seems to me that there is a fertile field there for incentive taxation.

So that where we find ourselves on incentive taxation is that we would dislike formulas, because we think there are many things that come before profit sharing which have to do with the partnership between us, and there are other areas where we are accorded aid today even in certain of our desires to help people. They would have to be sought for, however, in other areas.

Senator VANDENBERG. I think those are very constructive suggestions.

Senator HERRING. All right. Thank you, Mr. Robertson.

Mr. Riford, president of the Beacon Milling Co., Inc.

STATEMENT OF LLOYD S. RIFORD, PRESIDENT, THE BEACON MILLING CO., INC., CAYUGA, N. Y.

Senator HERRING. You have a plan, I think, of either profit sharing or wage dividends. We find so many terms for it, however, that I do not know just how to refer to it.

Mr. RIFORD. We have no direct profit-sharing or general profit-sharing plan in effect. We have several features of profit sharing, because they provide income to employees beyond what we consider liberal or high wages. We have had it in effect for some 14 years. We call it the workmanship bonus, which is based upon volume and several other factors, and this has equaled from 3 to 5 percent of the plant pay roll.

We have a salesmen's bonus which is in effect, which has equalled from 3 to 6 percent of the sales salaries. We have for the last 2 years reimbursed all employees in our plant and office, 1 year with a week's compensation, another year with a half week's compensation, which was, in effect, profit sharing. Then for this year we have taken a step which is somewhat of an experiment, leading toward possibly a general profit-sharing plan, which is a management bonus on a predetermined formula, in which all management and foremen, the supervisory group, are included. Those are the features which we have made use of and which are beyond what we consider to be high wages.

Senator HERRING. This plan of yours has been a bonus plan purely, has it not?

Mr. RIFORD. That is true; yes.

Senator HERRING. It has not been based upon merit or production?

Mr. RIFORD. Well, it has had a bearing. The plant bonus, for example, is based on the quality of workmanship, in which the entire group shares.

Senator HERRING. The plan this year is based on a definite percentage?

Mr. RIFORD. That is correct; yes, sir.

Senator HERRING. Your labor is not organized?

Mr. RIFORD. No, sir; it is not organized.

Senator HERRING. You have had no labor troubles?

Mr. RIFORD. None whatever; no, sir. Of course, we are a very small company. We are located in a small country village with no other industry there. It makes our conditions quite the exception, I expect.

Senator HERRING. Well, as contrasted to the dividends to the stockholders, how would your profits or wage dividends compare?

Mr. RIFORD. I could not give you the exact figures, sir. Roughly 15 percent, I would expect. In the early years of our business we paid no dividends, and each year a large proportion of our earnings have of necessity gone back into the business.

Senator HERRING. About what is the average wage that you pay?

Mr. RIFORD. I have the exact figures here for the year ending August 1, 1937. For strictly the mill employees, without any supervision figured in, that was $1,631.

Senator HERRING. There is no profit sharing until the adequate wage is paid? It is well to get that into the record.

Mr. RIFORD. We have paid a going wage, or better than the going wage, and have constant employment, so that the weekly earnings have been considerably higher than the general situation.

Senator HERRING. Unless you have something more, Mr. Riford, that you would like to put into the record, I think of nothing else.

Mr. RIFORD. I have possibly one or two comments. I believe any profit-sharing plan must be considered absolutely independent of the wage level, or else no advantages accrue to either employer or employee. That has been our thought in any of the plans which we have devised.

Senator HERRING. Have you any thought about the compensatory tax benefit to those who share profits, or incentive taxation?

Mr. RIFORD. In my opinion, a tax incentive would undoubtedly encourage profit-sharing plans, but I cannot see where a tax incentive (for purely selfish reasons) would bring a company to install profit sharing.

Our business is the manufacture of feeds for all types of farm animals. The business is somewhat seasonal, although tending to become less so in recent years.

We are a small company and are located in a small country village where there is no other industry. For these reasons and possibly others, our problems are not particularly representative.

We employ about 130 people at our mill and office, with a sales force in the field.

Since the organization of our company in 1920, our business has rather constantly expanded which has required increasing amounts of capital and this made it necessary to turn all of our annual earnings back into the business for many years. A large proportion of our annual earnings each year has, from necessity, remained in the business.

For this reason, although a general profit-sharing plan has been given consideration, such consideration has been more academic than specific until during the last year or two.

Our company has always paid good wages, possibly high wages. Our scale of wages and weekly earnings up to 1929 compared favorably with the going rates in our locality. Since then, our wage scale has been higher and because of steady employment, weekly earnings have been much higher than have prevailed generally.

We have never installed a complete and direct profit-sharing system. We have taken steps in that direction and have enlarged upon various features which, in effect, create for the employee a share in the profits in that these various plans have provided income beyond liberal or high wages and salaries.

Since 1923, group insurance has been carried at the company's expense for graduated amounts depending upon length of service up to $2,000 insurance per employee.

For 14 years, plant employees have shared in a quality-workmanship bonus based upon tonnage and other features. This has run from 3 to 5 percent of the plant pay roll.

Our salesmen have received a bonus for many years for improved quality and quantity sales in their respective territories and, during recent years, this has equaled 5 to 6 percent of sales salaries.

At the end of 1936, each office and mill employee, exclusive of executive officers, received an extra week's compensation as a recognition of his contribution to a successful year. At the end of 1937, half of a week's salary was received by each similar employee.

The apparent advantages of these isolated features of a general profit-sharing plan, both to the company and to the employees, prompted consideration of still further steps leading toward a complete and direct profit-sharing plan.

Early in 1938 a formula was established and approved whereby the management group would share in the profits for that year. All the executive, management, and foremen group are included in that plan, with the exception of two of the officers, who are the largest stockholders but still quite active in the management of the company.

From our experience and from observation and careful study, there appear to be advantages resulting from a profit-sharing plan which accrue both to employee and employer. Employer and employee have a mutuality of interests which is too often overlooked.

Some of these advantages are:

1. The employee's income is increased if there are profits to share. This is by no means a disadvantage to the employer.

2. In adverse years when there are no profits to share, the employee should gain a realization of the risks of business and the possibilities of losses as well as profits.

3. There is created in the mind of the employee a sense of partnership in the business.

4. There is an improvement in efficiency and a decrease in waste, resulting in an increase in the possibility of profits, thereby stabilizing the business and creating a sense of security for the future. This should work both ways, as the elimination of worries for the future should also increase the efficiency of the employee.

5. Self-imposed or automatic supervision is stimulated, which is beneficial to both parties.

6. A spirit of cooperation between employer and employee is perpetuated, allowing the free discussion of problems of mutual interest and thereby promoting the peace of mind and happiness of the employee, reacting as well to the benefit of the employer.

A profit-sharing plan, both for practical and ethical reasons, should be considered entirely independent of wage and salary levels. Wages and salaries should be regulated by general business conditions, particular conditions surrounding a given business, cost of living, and other factors that enter into a situation. Should there be the slightest tendency to consider an employee's share in the profits as part of his wages, or having any bearing upon his wage level, then immediately the advantages of a profit-sharing plan are partially or entirely removed.

It is an accepted fact that labor should receive liberal wages and that capital should receive a just return. It would seem reasonable that earnings accruing beyond an amount to take care of these two factors should be shared by both capital and labor. By labor, because it has contributed to those earnings. By capital, because it also has contributed to those earnings and because it is bearing its share, possibly more than its share, of the risk; labor ordinarily receiving its full wages before capital receives any return. What proportion of earnings, beyond liberal wages for labor and a just return on capital, should be shared by capital and by labor is undoubtedly a debatable question.

In my opinion, compensatory tax exemption or some form of tax reward on the part of the Federal Government would encourage the voluntary establishment of profit sharing. However, I see no reason why such a tax incentive should be a controlling factor with any individual business. It would seem unlikely that a tax-exemption plan could be sufficiently attractive to induce any company, for purely selfish reasons, to install a profit-sharing plan in order to secure such a tax reward.

A tax incentive plan for companies having in effect a profit-sharing system becomes a punitive plan for companies not sharing profits. The principle may be a dangerous one.

Senator HERRING. You think it is safe to rely on the employer with his own good business judgment and humane instincts to put it in?

Mr. RIFORD. That would be my opinion. It would not be a determining factor in our case, and I could hardly see where it would be a determining factor with any company. That is my opinion.

Senator HERRING. Thank you very much, Mr. Riford.

Mr. Schwartz.

STATEMENT OF WALTER M. SCHWARTZ, PRESIDENT, PROCTOR & SCHWARTZ, INC., PHILADELPHIA, PA.

Senator HERRING. Proctor & Schwartz manufacture driers, textile machinery, household electrical appliances, and so forth. Do you have a profit-sharing plan, Mr. Schwartz?

Mr. SCHWARTZ. Not now, no. We share profits, but there is a difference, a decided difference between a profit-sharing plan and sharing the profits.

Senator HERRING. Give us your idea of that.

Mr. SCHWARTZ. In 1910 we adopted a profit-sharing plan. I would like to call your attention to the fact that at that time there were no taxes of any sort, either on corporate profits or on individual incomes.

Senator VANDENBERG. It does not seem possible there was such a case.

Mr. SCHWARTZ. It does not. I only point that out to indicate that taxation had no bearing on our adopting the profit-sharing plan. The company did not obligate itself under this plan. It adopted a policy, after deducting 6 percent for the capital, of taking 10 percent of all profit above that and distributing that money among those employees in the establishment who did not have an opportunity to work on premium. All the men in the shop worked under a premium system, where they directly shared, if they did a good day's work, but about a half of the organization was salaried people, and it was among those salaried people that this profit sharing was distributed.

The plan continued until the excess-profits tax was enacted, I judge around 1917, 1918, or 1919. We were advised that the money that we distributed among the employees in accordance with the profit-sharing plan was not chargeable as a part of the expense of operating the business, and that we would have to pay the excess-profit tax on that, just as though we had not paid it out to the employees. I am under the impression that there was a stage where if we had earned $100,000 extra, which we felt we might distribute over and above the computation, that we would have had to pay $80,000 of that in taxation under the original excess-profits tax, so that it left practically nothing to distribute.

We were informed that if we obligated ourselves a year in advance so we had to pay that to the employees, then it would be chargeable. So for a while we adopted such a policy, and it developed into being regarded just as extra compensation and the profit-sharing feature really was pretty much eliminated.

In 1921 we discontinued the plan altogether. Now, I am not really prepared to say just how valuable the plan was. In other words, I am not clear in my mind whether it was a good thing or a bad thing—yes, I am convinced it was not a bad thing. I am also convinced that any money that we have ever distributed has been money well spent.

After we discontinued the profit-sharing plan, we commenced to share profits; not in accordance particularly with any preconceived plan, but at the end of the year if we had had a good year we did something for the employees. Back in those days it was a very unusual thing for a workingman to have a vacation with pay. Well, we started in paying them for Christmas Day, and Thanksgiving, and Fourth of July, and then to give them a full week's vacation with full pay. Then we bought life-insurance policies for all the men, starting off with about $1,000 policy apiece, and things were going pretty well, and the next year we doubled that.

Senator HERRING. That was group insurance?

Mr. SCHWARTZ. Group insurance, paid for entirely by the company. Incidentally, we never have felt inclined at all toward any plan that kept anything out of the man's pay envelope, except this Social Security Act where it is withdrawn, which seems to me all right, but if the company would do it, I think the men would not like it, and it does not appeal to me at all, so we pay for all these things ourselves.

Senator HERRING. Under this bonus plan, are the employees getting as much or more than they did when you had the profit sharing?

Mr. SCHWARTZ. They are getting a great deal more, not only in money, but much greater value. For example, if we had distributed the money and they had to pay for their own life-insurance policies, they would have been able to secure perhaps only half of the life insurance that they are now getting. Under our plan of group insurance, I think the amount of money we distributed in that manner gave them almost double the value that they would receive had we paid it directly to them. At the outset the men did not like it particularly well, they were a little bit skeptical. They said, "We would rather have the money in our pay envelope." After two or three men died and they saw their families get this money, the whole organization were keen about it and liked it. That is true of almost everything. Sometimes things that are done are a little misunderstood, but if the employer takes the trouble to really have the men completely informed, it seems to me they are very understanding and cooperative.

Last year we gave everybody in the establishment an extra week's pay in cash. Everybody had a week's vacation, plus those other holidays with full pay.

We took out accident and sick insurance for the men, so that they would be covered if anything happened to them away from their work, where they were not covered under the compensation laws.

We placed a fund in trust, an irrevocable trust, so the company had no control over the fund whatsoever, to protect our men during the interval before they would come under the Unemployment Act. There is a 3 weeks' interval before the men commence to receive compensation under the Unemployment Act. This fund was set up to cover that period, and after, I think it is 13 weeks that they are covered in this manner, they would then receive from this fund again. That fund is really handled by a shop committee, elected by the men from among the workingmen in which the company has no voice whatsoever.

All those things in the aggregate amounted to approximately, I think, $50,000. Mine is a pretty small company. The total amount paid out in dividends was $90,000, so that a little in excess of 50 percent was paid to the employees.

Now, while we have no announced plan, and I am just a little bit reluctant to talk about it on that account, yet I feel as though I must in order to explain precisely what we did. The company had paid no dividend for 6 years on the common stock until last year. We had paid the back dividends on the preferred, and we had a good year. Now, we felt that the stockholders were entitled to 6 percent, just as the employees were entitled to the average pay that existed in the community. We kept that pay always I think a little in excess of the average.

Now, we felt that the conditions warranted our paying more than that 6 percent to the common-stock holders, in fact 12 percent. Our financial condition and earnings we felt warranted 12 percent, so we divided that in half and gave one-half to the employees and paid the 3 percent extra to the stockholders. The reason the figure of distribution amounts to more than half is that the life insurance and sick and accident benefits, and those things, went on just the same. This was an extra distribution.

I never have heard one word of dissent upon the part of any stockholder in our company about any money that we have distributed, and we have been doing it since 1910, extra distributions that we were not obligated to make, and that is even notwithstanding the fact that they were without dividends for 5 or 6 years prior to 1937.

It is my opinion that the employees appreciate it a lot; that it is an excellent investment for the company to make on behalf of the stockholders.

There have been times that we have had some slight misunderstandings with our workmen. We never have had a strike, we never had a misunderstanding that we were not able to straighten out by taking the men completely in our confidence and having them really understand the situation.

We were cited before the Labor Board in June 1937, and the thing dragged along. I acknowledged the letter from the Labor Board and told them I would very much welcome having them come in there and investigate the whole thing, that my only desire was that our men should have what they wanted, and if an investigation indicated that they wanted to join any particular union, that that was exactly what I wanted them to do. Well, the thing dragged along and it dragged along, and last year I wanted to make this distribution of cash to the employees and I was afraid to do it, for fear it would be alleged that I was trying to influence the employees. So I called up the Labor Board three or four times, and I could not get an answer, although they had said within a week we were going to have a vote, they were going to show me how to build the boxes and everything, the booths, just how it was to be done, but they kept delaying, and finally one day they called me up and told me the charges had all been withdrawn. That was the end of that episode.

I do not like very much to appear to be attacking anything. That proposition, on the face of it, would look like an exceedingly fair proposition upon the part of the Labor Board, but I am convinced that the people who made the charge withdrew the charge because they found they were going to be completely defeated in the vote, and that did not seem altogether fair to me, because it would not have worked the other way around, I am quite sure.

Senator VANDENBERG. So you had no election?

Mr. SCHWARTZ. We had no election. It was all called off.

I mentioned a fund that we set up last year—I am leading to the question of taxation—to cover unemployment, the fund that we paid out irrevocably, we have no control over it, and yet there is a very serious question whether we are not going to be taxed on that fund just as though we had not paid it out; in fact, I am almost certain that we are going to be taxed upon it. That was a distribution to the employees, which they appreciated as much as anything we had ever done in our lives. It was something to help them if they became unemployed. Likewise, that fund undoubtedly reduced, to some extent, the expenses of the Government in relief rolls and the like.

The one definite suggestion that I would like to make would be that it be completely clarified in the tax law, as to distributions made, when an employer has had a prosperous year and feels optimistic, that they shall be regarded as a part of the expense of operating the business, even though the employees might, in subsequent years, get the benefit of it. I believe it is wise to safeguard it. It would have to be safeguarded so the people did not utilize that means of escaping taxation, but certainly when you have had a mighty good year and everybody has cooperated, you are inclined to do things that you would not feel otherwise you might be able to do, and that is what I would like to see made perfectly clear in the tax law.

While I think it is a fine thought and most creditable to those who have conceived it, to place some special tax reward to those who share profits or adopt a profit-sharing plan, yet I am sorry to say that I am opposed to it. In the internal economy of the country I am not inclined to use the tax power for any other purpose than raising of revenue. The undistributed-profits tax looked to me like an awfully good thing and I was strong for it at the time it was enacted, yet I think it has been a vicious thing as it turned out to be, and I am inclined to think it is not a good thing to use that tax power for economic ends other than to raise revenue for the Government.

Am I talking too much, sir?

Senator VANDENBERG. No, indeed. It is very interesting.

Mr. SCHWARTZ. Of course, in any kind of a profit-sharing plan or any encouragement toward a sharing of profits, the first fundamental is that there shall be profits, and it is in that direction that I would like everybody to give his attention.

There are two things that I have in mind that would seem to me to be conducive to profits. One of them is rather an obvious thing, and that is that the relationship between an employer and employee is rather a delicate matter, and any statements that are made from any source whatsoever that would lead the employees to believe that the employers are responsible for all their ills is like throwing sand into the gear box. It is bad. I would like to see that really stopped, and I think, in turn, that it might be quite appropriate if the businessmen and employees will stop attacking also. That is a cooperative measure that would really have weight, I think, in bringing about better conditions.

I am far from being an expert on the subject of taxation or of government, but I would like to offer this suggestion that has come to my mind. From what little knowledge I have of history, it leads me to believe that a constantly rising taxation spells ultimate disaster. The Budget is out of balance, and I do not see very much hope of getting it into balance in a hurry. My theory is based on a recognition of that fact, and what I would like to see done is to have the Treasury Department make a computation upon what taxes would be required if the national income were operating at about 80 to 90 billion (whatever they would consider a normal national income). Make a computation of what taxes would then be necessary in order to bring the Government sufficient revenue, taking into consideration that in the national income reaching that scale it relieves the Government enormously of the relief rolls, it relieves the necessity of these projects which are not self-liquidating.

Taking those two things into consideration, the tax that would be necessary then, and to put that tax into effect now and let the Budget go out of balance, as it will do temporarily, because I firmly believe that the boost that would give business would rapidly cut down the expenses of the Government, that the lower tax rate would cut down the expenses of the Government, and then we would get business into a healthy condition, after which we would start to work and try to balance that Budget. It may sound awfully radical, but I would love to see a real study made of such a proposition, and if those things are done I am pretty well convinced that profit sharing would grow like wildfire without any special tax.

Senator VANDENBERG. In other words, you mean a lower taxation on business is the essential incentive to stimulate recovery?

Mr. SCHWARTZ. Yes, sir. It is my view, also, that that money being in the pockets of the people will produce a great deal more, and it will produce more economically than it can in the hands of the Government, and I think if we should be given such encouragement that all of us would lose all fear about going ahead. I cannot see how it could help but work. If it did not, why, then, something else could be tried. We have tried so many things.

I think I really have practically completed all I have to say, except I repeat that I think it is a fine thing for this Senate committee to be doing what it is doing, as it relates to profit sharing. I think the publicity will bring to the attention of those employers who have not done it that they better get to work and do so because it is a good thing to do; and, no matter what decisions may be reached, I think you have achieved something good.

Senator HERRING. The value of our services would depend upon such evidence as you have been giving this morning, which I think is very helpful. We appreciate your coming, Mr. Schwartz.

Senator VANDENBERG. I would like to ask one question, based upon a sentence in the general remarks reported in your answer to our questionnaire, which is: "We think it would be a fine thing if industry made a practice of dividing half and half with employees the dividends over and above 6 percent on their common stock and surplus."

Mr. SCHWARTZ. Yes, sir. That is not a practical thing for every concern. I wrote those answers, and that answer is a practical thing for me. It happens that my pay roll per annum is about equal to my capital, so that an equal division there is an equitable thing. Now, some other manufacturer might only assemble; he might buy most of his products from other people; he might have a small pay roll; and it would be far beyond all reason. I think, however, that on a percentage basis it is a practical thing. If an employer found his profits warranted paying more than 6 percent to stockholders, he would divide such additional percent in half and give half to employees and half to stockholders. For example, if the profits warranted 6 percent extra to stockholders, only 3 percent extra would be paid in dividends and 3 percent of the pay roll would be distributed to employees.

Senator VANDENBERG. What I wanted to ask you was whether you would think this 6 percent on the common stock and surplus should be cumulative over the years before the subsequent 50-50 division?

Mr. SCHWARTZ. It would be my thought that as the surplus increases you increase the profits. That is, if we kept adding to our surplus we ought to keep adding to the profits and make more money disposable to the employees.

Senator VANDENBERG. Suppose you paid nothing on common stock for 5 years, would you say the stock was entitled to 30 percent then before the rule of division applied?

Mr. SCHWARTZ. That is, whether it is entitled to 6 percent on the accumulations?

Senator VANDENBERG. Yes.

Mr. SCHWARTZ. I would think so. If that gave a proper return it would have made just the same relationship between the employers and employees. All the money goes into surplus and it would be distributed afterward partly to the employees and partly to the employers. I would be very fearful of a plan, although we had it ourselves, involving payments based on earnings and not upon cash payments, because there are times when it is in the interest of employers and employees both to spend money on plant and equipment, and possibly enlargement, and it might embarrass them financially if they had to pay out when they had low earnings and were not paying anything to the stockholders, but when they could pay to the stockholders what is a reasonable rate, then over and above that I should certainly like to see the employees share, and the employees certainly help to produce those profits.

Senator HERRING. Your reason for thinking that is that the employees have received their wages while the common stock has had nothing?

Mr. SCHWARTZ. That is it.

Senator HERRING. And, therefore, if you are going to divide the residue also, that they ought to be brought up to date to be even with the employees before the division is made?

Mr. SCHWARTZ. I would say in our case last year we did not take the surplus into consideration. Our stock has a book value of $175 a share, and we just took the $100, but what fits one might not fit another. We did fairly well. The employees contributed so much that we wanted to make the distribution. We ignored the surplus. The stockholders did not get anything on that surplus, but I would not want to suggest that some others do that, that might not be in the position to do that.

Senator HERRING. Thank you very much, Mr. Schwartz.

We have Mr. Herbert Daniel Brown as the only other witness today, and we might just as well hear Mr. Brown.

STATEMENT OF HERBERT DANIEL BROWN, GLENORA, N. Y.

Senator HERRING. I suggest you might give us an outline of your services to the Government, Mr. Brown.

Mr. BROWN. Yes, sir. If I may do so, Mr. Chairman, I perhaps would like to go a little further back than that. My interest in personnel problems began back when I was a boy in Iowa. My father was a paper manufacturer. That is a long time ago. Later when I came to Washington, I was employed as an examiner in the old Bureau of Corporations. That was during President Theodore Roosevelt's administration. He appointed what was known as the Committee on Department Methods, and I was assigned to the subcommittee that handled personnel problems. Later on when Mr. Taft became President, he appointed what was known as the President's Commission on Economy and Efficiency. I was a member of that organization and worked with Dr. Goodnow, who was a member of the Commission. Dr. Goodnow, you may remember, was afterward president of Johns Hopkins University. When President Taft's commission went out of existence, the work which they did was turned over to a new organization, of which I was made the head, called the Bureau of Efficiency. That organization continued until 1933, when the Bureau was abolished. The name was very unfortunate.

Senator VANDENBERG. You mean we abolished efficiency in 1933?

Mr. BROWN. Well, Senator, if I may be permitted to limit my statement to the Bureau, I should like to do so.

Senator VANDENBERG. All right.

Mr. BROWN. I wanted to add, in reference to that, the name was very unfortunate. It was one that challenged the intelligence of everybody else but ourselves. It should have been called a planning bureau, because that is what our work really was.

During my service for the Government, I also acted as a consultant to several big organizations in pension problems and other personnel problems, nights and Sundays, and since the Bureau was abolished, I have been a consultant and have moved from Washington and now live in my summer place at Lake Seneca.

That, in brief, is my history. I have prepared a brief statement here, which I should like to read and then you may ask me any questions you like, or while I am reading, if you prefer to do so.

It is a great pleasure to be asked to share in the deliberations of this committee, because I have recently been studying the matter of profit sharing in connection with other personnel problems to which I have given a great deal of attention for years, both while I was in the Government service and since.

In the first place, I would say that I am in entire sympathy with the general principle of industry sharing profits with its workers but I believe that the money distributed under the profit-sharing plans which have been developed up to this time could be used to better advantage if given the employees in another way.

DEFINITION OF PROFIT SHARING

The term "profit sharing" has a pleasant sound in the ears of the altruist but it behooves us to ask just what is meant by it. "The essential characteristic of true profit sharing" according to a report of the National Industrial Conference Board issued in December 1937, on "Profit Sharing and Other Supplementary-Compensation Plans Covering Wage Earners," "is that payments to employees under the plan must bear a definite relation to the profits of the company." As pointed out in this report of the Conference Board, the term "Profit sharing" has been applied to plans as diverse as "insurance, supplemental bonuses, employee stock ownership, and even wage incentive plans." The Conference Board decided, however, to include in their use of the term "profit sharing" only those plans that provide to participating employees payments in cash, stock, or future credits that bear some definite relation to the profits earned by the company during a definite period. It seems to me that this definition of the term "Profit sharing" is good and I am willing to accept it.

After careful study of the general industrial situation and the testimony of employers who have tried to establish profit-sharing plans, I am convinced that it would be better to apply industrial profits that might be distributed among the employees to building up a system of reserves to be used to supplement wages in times of business depression or recession, thus avoiding the necessity of throwing large numbers of employees out of work when the markets will no longer absorb all of the goods that all of the employees can make when working full time. Since such an employment-assurance plan would seem to come within the definition of profit sharing adopted by the National Industrial Conference Board, the profits shared being reserved for distribution among the employees at times when most needed and in such ways as to prevent or at least to minimize the major catastrophe to which the average wage earner and his dependents is subject—that is, unemployment—such a plan would seem to be essentially a profit-sharing proposal.

EXPERIENCE OF PROFIT-SHARING COMPANIES CONFLICTING

The experience of profit-sharing companies has varied greatly and their conclusions are conflicting. The experience of the active plans studied by the Conference Board was reported by the companies in respect to the objectives which they sought, namely, improved morale, increased efficiency, greater interest in the company, improved labor turn-over, adjusted compensation, encouragement of thrift. Some objectives were more successfully met than others.

SIGNIFICANCE OF EXPERIENCE OF PROFIT-SHARING COMPANIES

The report of the Conference Board comes to no clean-cut and positive conclusion in regard to the significance of the experience of industry with profit-sharing plans except that "Actual experience proves little or nothing in respect to the practical value of profit sharing."

Senator VANDENBERG. What was the date of the conference report?

Mr. BROWN. That was 1937. I think I have the exact date here. December 1937, Senator.

Emphasis is laid on the fact that the discontinued plans outnumber those still in active operation, but the point is also made that the companies that continue to have active profit-sharing plans endorse the system warmly as an aid to management.

Senator HERRING. Mr. Brown, does not that same report list 167 profit-sharing plans?

Mr. BROWN. That is right.

Senator HERRING. We found about 500 already in this survey, so we could not rely too much on their report.

Mr. BROWN. Well, I would not rely too much on theirs. It should be borne in mind that that report is made by an organization that is supported by industry, and it may be that their slant is from the industrialist's point of view.

Senator HERRING. I would think so, inasmuch as you suggest that reserves be built up for profit sharing in times of depression. With whom would you leave those reserves?

Mr. BROWN. I have worked out a plan for the care of the reserves, Senator, if you will bear with me.

Senator HERRING. I was wondering if the depression went along long enough and got bad enough that probably there would be no reserves left.

Mr. BROWN. That is the first question every industrialist asks me when I talk to him about putting up reserves to take care of people when business recedes. I have something on that subject, and if you will bear with me, I will take it in the order in which I have it here. Is that all right?

Senator HERRING. Certainly.

Mr. BROWN. As Edward S. Cowdrick says succinctly in an article entitled "Shall Workmen Share in Profits?" published in the Nation's Business of January 1937:

> Of this whole line of argument, about all that can be said is that, for a particular company, profit sharing is a good thing if it works. If it doesn't work it is useless or worse.

In other words, when it does work, it may be said to serve one or more of the objectives of "improved morale, increased efficiency, greater interest in the company, improved labor turn-over, adjusted compensation, and encouragement of thrift," listed in the conference board's report; but in the majority of cases considered, it has not worked.

MERIT OF EMPLOYMENT ASSURANCE AS FORM OF PROFIT SHARING

In view of the conflicting results of profit-sharing plans as reported by different employers of labor and the dubious attitude also of organized labor in the matter—I believe that Mr. William Green and Mr. John L. Lewis, for instance, showed no marked enthusiasm for the idea of profit sharing when interrogated recently by this committee—I am more than ever convinced that the general principle of industry sharing profits with its workers can better be served through the adoption of employment assurance plans such as I have in mind than by any so-called profit-sharing plan that has yet been proposed. Not only might such a plan be applied so as to clear up some of the major personnel problems now puzzling leaders of industry, but it would, I believe, commend itself strongly to the mass of workers.

My own observation has been that where the profits are distributed at frequent intervals there is a tendency on the part of the employees soon to treat the bonus, or share, or whatever you wish to call it, as part of their regular wage, and to increase their standards of living to the sum of the wages plus this bonus.

Senator HERRING. We have had some interesting testimony about that, and I think you would be interested in reading it, on both sides.

Mr. BROWN. Yes; I shall be glad to read the testimony on both sides.

Senator HERRING. Many employers deny it has had that effect on their employees, while some have indicated as you do.

Mr. BROWN. And if the profits are distributed at long intervals, there might be a tendency, and I think it would be human nature if it asserted itself, to anticipate the distribution and to mortgage one's self for an automobile or radio, or some other substantial expense, so that when the unfortunate time of unemployment arrived, the employee might be no better off than if he had not participated in the profits, except he would have an automobile, or some other thing.

Senator HERRING. You come in conflict with two views on that, as to whether we try to wet nurse them or let them take care of it, become capitalists, and learn how to handle it.

Mr. BROWN. It would seem that the small pay of most of the workers puts them in a very dependent position soon after they leave their jobs, and so I would be in favor of helping them in every way I could without being too paternalistic.

Senator HERRING. I think the best example of that is the experience of Sears, Roebuck, where they paid immense sums in 1929 to pensioned employees, and 95 percent of them are back at work now.

Mr. BROWN. I think that is human nature, and such a big hazard and so important to society in general that it seems to me some systematic program should be worked out to help the employees to protect themselves against the hazard of unemployment without being too paternalistic. I am not a Socialist by any means.

The polls that have been taken by the Gallup Institute of Public Opinion indicate clearly that, more than almost anything else, the American workman craves security in his job. I can imagine that if one were to stand at the front gate of any factory in the United States with cards on which were printed, say, a half dozen questions that have a bearing on the economic status of the working man, and one of the those questions related to "Security in his job," and the men as they left their work were asked to sit down with their wives after supper and number the questions in the order of importance to them, that "Security in his job" would be placed at the head of the list in almost every case.

If this is true, then it would seem as if any moneys that might be set aside out of profits for the benefit of the workers might better be used to help build up reserves to piece out their reduced wages when the market will no longer absorb all of the goods which all of the workers could produce if working full time.

In the past, in times of economic depression, it has been the custom, to a great extent, to continue the regular hours of work and, if the market did not absorb all of the goods produced by the entire force, to lay off as many employees as necessary to bring production down to the required amount. Under this arrangement, the employees who were so fortunate as to be retained were often, temporarily at least, better off than they were in good times, because their dollars would buy more than in normal times, while the employees who were laid off soon exhausted their resources and frequently became public charges.

The unemployment-insurance laws of the various States sponsored by the Social Security Act were intended to change this unfortunate condition by providing certain benefits, but those are only paid after the man has lost his job. In contrast to this, under such a system as I propose, if orders fell off, hours of work per day or per week would be decreased; and when the fewer hours of work multiplied by the regular hourly rates of pay produced a wage below normal, or some prearranged percent of normal, the employees' wages would be supplemented from a reserve fund which had been built up in prosperous times partly from profits. The practical effect of this would be to hold employees on the pay roll in contrast to the effect of existing laws, which have a tendency to encourage employers to throw employees off the pay roll rather than go to the trouble of stabilization. That employers sometimes have no scruples in doing so is undoubtedly due to the fact that they think the individual employee is protected under the unemployment-insurance laws. Even if he were—and the protection is only for about 15 weeks—society is not protected under this system from the evils of unstable employment conditions.

OUTSTANDING CHARACTERISTICS OF PROPOSED EMPLOYMENT ASSURANCE PLAN

The plan which I propose for assurance of employment has two general outstanding characteristics:

First, it provides that the number of working hours be varied according to the demand for goods, lay-offs for lack of work being discontinued as far as practicable, and the number of employees kept constant as far as practicable. This is the reverse of the general policy of employment which has prevailed in the past. From time immemorial it has been the general practice of the industrial world to keep working hours more or less constant, while letting the number of employees be more or less variable.

Second, the plan provides that wage rates per hour shall be maintained; but if those rates for the reduced number of hours produce a wage with a lower purchasing power than the wage of normal times, the difference shall be made up out of reserves established for this particular use.

The feature of this suggested plan of spreading work which distinguishes it from other share-the-work proposals is that while reductions in actual pay may be entertained, if need be, the purchasing power of the employee's pay is held substantially level, and therefore the criticism sometimes brought against a part-time basis of employment for all employees during a slack period as not beneficial, if long continued, to either workers or employers, does not apply.

The heart of the problem is to determine the amount of the reserves that should be set up, since the obvious need is for a total reserve sufficient to maintain wages through times of depression at a rate having the purchasing power of normal times.

CALCULATIONS MADE TO DETERMINE AMOUNT OF RESERVE NECESSARY FOR ESTABLISHMENT OF AN EMPLOYMENT ASSURANCE PLAN

While recognizing that the contingency of unemployment is not an insurable risk, I have found that it is entirely possible to calculate the amount of reserve that would be necessary to retain employees on the rolls during a depression of a particular pattern and duration on wages at a predetermined level, as, for example, the pattern and duration of the depression that began in 1929, and a level of wages having the purchasing power of normal times, or, say 80 percent or 90 percent of the wages of normal times.

Some time ago I made rather an elaborate and I think interesting set of calculations from statistics that had been given me by various industrial companies for other purposes. These calculations when completed showed that a reserve equal to 75 percent of the wage roll of 1929 (1 year), if added to the wages actually paid between 1930 and 1935, would have been sufficient to enable this hypothetical company to retain on the rolls to the end of the depression in 1935 (a period of nearly 6 years) all employees who had a year or more of service on January 1, 1930, or who thereafter acquired a year of service, and to have given those employees wages that would have had the purchasing power of their wages of normal times.

Now, by the expression "purchasing power" I mean that in making those calculations, I took into account in those calculations the index of cost of living.

Senator HERRING. Have you given any thought to what would be done with the production? In the automobile industry, for example, if automobiles do not sell for 2 days, there is no place for them.

Mr. BROWN. What I intended to convey on that point is that the hours would be shortened even if the plan would not cover every employee.

Senator HERRING. Would the hourly wage be increased?

Mr. BROWN. You would not increase the hourly wage. You would have shortened hours. If purchasing power was less than in normal times, or some percentage of it, you would have shortened hours, which would cut down the cost, and then this reserve would be drawn upon.

Senator HERRING. I just have difficulty in understanding what we are going to do with the production that is created.

Mr. BROWN. If you shorten the hours and reduce the output you have less to sell.

Senator HERRING. I do not see how you are going to keep them busy.

Mr. BROWN. If you do not work them so long, they will not produce so much. If the working day is 8 hours and they only work 4 or 5 hours, by staggering, you would reduce the output in two, or in half. In other words, it seems to me, Senator, it is really very important that people should not be thrown off the pay roll, because it disorganizes business. It is an expensive thing to train employees for new jobs. They lose their continuity rights to all of the other plans that are in existence.

Senator HERRING. I am certain that everyone agrees with that, but it is the method that I am questioning.

Mr. BROWN. I want to make clear, Senator, the point that you have raised, that the heart of the plan I propose would require that the hours of the people who came under the plan should be shortened and staggered sufficiently so that the product would not be greater than could be disposed of.

Senator HERRING. Is not that exactly what happens?

Mr. BROWN. No.

Senator HERRING. If the product could be disposed of they would continue to work.

Mr. BROWN. Yes; but the trouble is in the way in which this plan of spreading the work has operated in the past. You get the men down to a wage where they cannot live on it. Now, it is proposed under this plan that there shall be a reserve which shall be used to sweeten up the wages to a point where they can exist and preserve the organization that they have, ready to do more business when there is a market for their goods. This percent (75) could be reduced by providing for wages having a purchasing power of some percent of their normal wage. That is what I said before.

The degree to which the business of these companies whose statistics I used fell off during the years 1930 to 1935 was, I believe, about the average of industry generally. The reserves required for the building trades, for steel and automobile manufacture, and so forth, would, of course, have to be considerably greater to give the same protection while the reserves for the consumer-goods industries would probably be somewhat less. I think I should add at this point that it would not, of course, be necessary to set up the full reserves at one time. Such reserves could be built up over a period of years.

On that point, Senators, I would like to say it seems to me that any move in that direction would have a pretty good effect upon the employees, because they would feel that the company was trying to provide for them and keep them on the rolls instead of throwing them off.

The calculations which I made fixed the amount of reserves which must be established to pay supplemental wages through an economic depression similar to the last one. While that is probably the most serious and prolonged depression known to history, it is conceivable, of course, that a future depression might be even more severe and of longer duration and that, the established reserves becoming exhausted, employees would be laid off. If that occurred, they could then look to the unemployment benefits provided under the laws of the States in which they work; but it would seem unlikely that this unhappy extreme of events would come to pass if industry generally could be induced to make the provisions proposed.

I am confident that it is entirely feasible to ascertain the actual money involved in stabilizing other classes of industry in America on a similar basis.

Although for many years industry has made it a practice to set up reserves to cover almost every phase of business that involves an uncertainty such as the occurrence of fire, accident, explosions, bad debts, depreciation, obsolescence, and the like, and has developed splendid systems of benefit plans that cover almost every human contingency to which the working man is subject, such as death, sickness, accident, disability, old age, and the like, yet, so far as I am informed, no attempts have been made to provide adequate reserves based on careful calculation to piece out the wages of employees when the market will no longer absorb all of the goods that all of the employees can produce.

The result of the failure to provide such reserves is that the contingency of unemployment falls almost entirely upon the worker and must be met from savings out of his earnings which are too often barely enough to provide himself and his dependents with the necessities of life in normal times. That is, in my opinion, not a fair distribution of the hazard of unemployment.

PROPOSED PLAN OF BENEFIT TO INDUSTRY, LABOR, AND PUBLIC

It seems to me that such an employment assurance plan as I propose would be of advantage to all concerned.

To industry, because it would relieve it of part of the cost of unemployment insurance and would tend to maintain business.

I might say also right at this point, gentlemen, that this ties in very closely with the Social Security Act, so far as the old-age benefits are concerned, and also unemployment insurance, and if you are interested in what I am saying, I would be glad, after the meeting, or some other time, to talk with you on that point. It is a little out of line of your immediate study.

It will be beneficial to labor, because it contemplates keeping workers on the pay roll as distinguished from plans that contemplate laying them off, as is the case with unemployment-insurance plans in various States.

To the public, because employees, being relieved of the fear of dismissal, would continue to make purchases at more nearly the normal rate, and this, in turn, would help to maintain the purchasing power of the Nation.

Since industry, labor, and the public would all be benefited by the establishment of such employment assurance plans, all might properly be asked to contribute to them.

SUGGESTIONS FOR THE COMMITTEE

You may want to know at this point what I would suggest that your committee do in connection with profit sharing to promote the plan I have outlined for stabilizing employment.

Well, in the first place, I would suggest that, whatever exemption you recommend be given employers for other forms of sharing profits with employees, you also recommend be given to employers who set aside a part of their profits as a reserve to stabilize employment. I believe your committee could render a great service in the problem of unemployment by directing the efforts of socially minded employers along the line I have indicated.

In the second place, I should like to see you recommend that the Secretary of the Treasury be authorized to receive and hold such funds in trust, subject to withdrawal on demand whenever needed by the employer for the purpose of the trust; that is, to piece out wages. The employer might invest this money as he does his other reserves, and if sufficiently skillful, he might suffer no loss, but the chances of loss would be above average since an employment assurance reserve would be accumulated principally in good times and be spent in bad times. The Federal Government is the only agency in a position to receive such funds and hand them back dollar for dollar, regardless of the investment market. Hence the suggestion that the Secretary of the Treasury receive and hold such funds if the employer wishes to deposit them with the Government.

I should like to see the Secretary of the Treasury authorized, also, to add interest to such funds at a somewhat more favorable rate than is ordinarily paid by the Government. Under the law authorizing the Secretary of the Treasury to issue United States savings bonds, the Government pays interest on such bonds at the rate of about 2.9 percent per annum compounded semiannually if the bonds remain outstanding until maturity—that is, for 10 years. If drawn at an earlier date, the rate of interest paid is less. In view of the social and economic importance of keeping employees on the pay roll and the saving to the Government in relief payments that would follow any general adoption of such a plan, it would seem as if the Government might well pay (1) a definite rate of interest regardless of the length of time that the money might remain with the Government, and (2) a rate of interest somewhat higher than it is required to pay on current borrowings or than is paid on United States savings bonds. I realize the fact, of course, that any excess in interest paid on such funds above the rate which the Government is required to pay on current borrowings would be just that much of a subsidy to the system, but it seems to me that, in view of the benefits to be derived by industry, labor, and society from such a system, that subsidy would be justified. I should like to see the Secretary of the Treasury authorized to pay not less than 3 or 3¼ percent interest on such money compounded semiannually.

I might say also at this point that I think it would be desirable to also extend that same privilege more definitely to pension plans than is now provided, so there would be less question about them and any similar plan. In other words, that provision ought to be quite broad.

If the trust were terminated at any time and the funds were withdrawn by the employer, it would be reasonable for the Government to require some notice in advance of such withdrawal, and, in such case, a lower rate of interest should be paid on the money so withdrawn. The money should also be treated as income if withdrawn for any other purpose than paying supplemental wages and should be taxed as income in the year in which it was withdrawn. This provision would be similar to the provisions of section 23p of the internal revenue law providing for pension trusts.

Senator HERRING. Well, that is a very interesting statement. I shall be glad to go over that.

Mr. BROWN. If there are any questions you want to ask, I would be glad to try to answer them.

Senator HERRING. I think not, Mr. Brown. We appreciate your coming.

That disposes of the witnesses today, so we will recess until 10 o'clock tomorrow morning.

(Whereupon, at 12:25 p. m., a recess was taken until the following day, Wednesday, December 7, 1938, at 10 a. m.)

SURVEY OF EXPERIENCES IN PROFIT SHARING AND POSSIBILITIES OF INCENTIVE TAXATION

WEDNESDAY, DECEMBER 7, 1938

UNITED STATES SENATE,
SUBCOMMITTEE OF THE COMMITTEE ON FINANCE,
Washington, D. C.

The committee met, pursuant to adjournment, at 10 a. m., in room 312, Senate Office Building, Senator Clyde L. Herring presiding.

Present: Senators Clyde L. Herring and Arthur H. Vandenberg.

Senator VANDENBERG. The chairman of the subcommittee, Senator Herring, made a most excellent radio address Monday evening, officially presenting for the first time the viewpoints and objectives of the committee itself. It was an authentic, significant, and effective presentation, and I wish that it might be printed in full at this point in the record.

(The address referred to is as follows:)

May I express my appreciation for having placed at my disposal again the splendid facilities of the National Broadcasting Co. and the Radio Forum of the Washington Star.

At the last session of the United States Congress, a Democratic Senate, by unanimous vote, adopted a Senate resolution, introduced by Senator Arthur H. Vandenberg, Republican, of Michigan, which provided for a subcommittee of the Senate Finance Committee to be appointed by the chairman, Senator Pat Harrison, of Mississippi, and charged with the duty of making "A complete study of * * * existing profit-sharing systems between employers and employees * * * in the United States * * * with a view to the preparation of an authentic record of experience * * * and to consider what favorable contribution, if any, may be made to the encouragement of profit sharing by the Federal Government, including the grant of compensatory tax exemptions and tax rewards when profit sharing is voluntarily established, and to consider any other recommendations which may prove desirable in pursuit of these objectives."

Senator Harrison accordingly appointed one Republican and two Democratic Senators, Senator Vandenberg, Senator Edwin C. Johnson, of Colorado, and myself, to conduct the survey.

This committee, immediately upon adjournment of Congress, communicated with several thousand firms, whose schedules of information are on file with us, having been solicited on an entirely voluntary basis.

Open hearings are now being held in Washington. No subpenas have been or will be issued. Employers and employees alike are being invited to appear before the committee at hearings open to the public to give their experience in profit-sharing and extra-compensation plans.

Whereas little authentic information on the subject was available prior to the commencement of this survey, it already appears as disclosed by the facts that instead of 167 profit-sharing plans in operation, as had been reported previously by private sources, several hundred employers have been found to be employing some form of profit-sharing plans in their businesses, while the companies employing extra compensation plans of some kind number several thousand.

It is most encouraging to have men, employing from a few hundred to 65,000 employees, come from various parts of the United States to testify that they have found industrial peace, increased efficiency, and larger profits through voluntarily sharing the results of their joint work with all workers connected with the enterprise.

We find employers testifying to the loyalty, honesty, and efficiency of their employees, and employees asserting the fairness and generosity of their employers.

Profit sharing with employees is not profit sharing unless a fair and just wage is paid before there is a division of net profits. The suggestion that sharing of profits might be used as a substitute for fair wages may, in some instances, be justified. However, not in one single case reported to date, has such a condition been found to exist. As a matter of fact, the record made thus far discloses that the type of employer who voluntarily shares profits with those working for him is not the type of employer who would pay his employees less than a fair wage.

It has been repeatedly stated that a fair wage, plus a fair division of the profits, is not only humane and right, but good business.

Most of the business executives having profit-sharing plans, who have testified, report an absence of labor difficulties, and that, that if entered into in good faith, with sincerity on the part of both employer and worker, and in such form as to apply to the conditions of the particular business, the results will be mutually satisfactory, and the volume dollars increased, often sufficiently to make profit sharing actually profitable to management.

Their balance sheets appear to support that contention.

When the record of the application of a successful profit-sharing plan is placed beside that of a plan which has failed, the reasons for the success of the one and the failure of the other are usually apparent and indicate the value of the survey which we are conducting, and the necessity for care and discrimination in the selection of a plan.

It seems to be quite generally accepted that our present economic difficulties rest largely upon unemployment and consequent lack of buying power. It may well be contended that a general sharing of profits in industry may be the answer to these distressing problems.

Upon such a policy industrially the future of the Nation may depend. If it be true, as is so frequently asserted, that improved methods, new inventions, and the almost universal use of power have permanently displaced millions of workers who can never be returned to gainful occupation, the challenge to our system of private capitalism is at hand.

A way must be sought which will enable the workers to believe not only in their futures, but in the methods of private industry as well.

The capitalistic system must be continued in America because only under such a system can the liberty of individual enterprise and a free society be maintained. This system has made America the foremost industrial nation of the world and the greatest nation of history.

We boast of the fruits and benefits of the capitalistic order but we leave to the comparative few the task of defending private capitalism. We could win large support by extending its benefits and increasing the numbers of men and women who are direct beneficiaries of a system through a broader and more equitable distribution of wealth at the source of its creation, shared in by those workers who help to create it.

An important fact to be borne in mind is that 70 percent of all workers are employed in establishments having less than 500 employees. While profit sharing exists in a number of major companies, it has likewise proved a wise policy for many small firms wherein it has been tried. To assist little business to prosper and grow is a primary obligation of all of us. The one, two, or three extra employees put back to work by the neighborhood grocer or tailor in every shopping center might swell the ranks of the employed more rapidly than by constant appeals to big business to put men back to work, although every one should be appealed to do his part.

Profit sharing in little businesses as well as large concerns would seem to provide a partial answer to the problem of unemployment and the proper and just distribution of wealth.

The struggle for existence is as old as creation itself.

The problem of the distribution of wealth is one which has plagued the conscience of men since the beginning of time.

We cannot persuade the workers to actively support capitalism without incentive—the conscious joy of being a capitalist. Conditions favorable to his becoming an independent man of means should be encouraged, and he in turn will take his full share of responsibility to carry on and render a good account of himself.

Capitalism must continue to earn the support of inspired defenders. The existing order can support itself only with concrete proofs of its achievements and benefits to the masses of people.

We should make personal possession the ally of statistics indicating wealth, if we are to reach the vast numbers of underprivileged men and women who are groping toward an uncertain future.

We have in America every factor necessary to the more abundant life—machinery, power, natural resources, the ambition and energy to work, the genius to create, the ability to produce, and the desire to consume.

Our energies, properly coordinated and directed, would find the Nation with new and restored purchasing power—a goal toward which we have steadily moved during the past 5 years—and our people busily engaged in doing those constructive tasks which make radical attacks upon industry and Government impossible.

No population ever revolted on a full stomach. Anarchy is not found among workmen who own their jobs and can rely upon an annual wage. They are capitalists in the making.

A capitalist is one who has a stake in the existing order—a home, property, a savings account, bonds that tie into permanency—something of which he may be certain at the end of the road.

To rest our case on the statement that a man has the right to be a capitalist is equivalent to the answer of Marie Antoinette to the people's cry for bread—"If they cannot get bread, why don't they eat cake?"

1. Why a special survey and study of profit sharing? Because the "profit system" is the heart of capitalism and the American system of government. We can only save capitalism and the benefits of American democracy by bringing the advantages of the profit system directly home to the mass of the people, thereby earning their sympathetic understanding and intelligent support. The fundamental principles of democracy and those of a free economy are one.

2. The application of those principles is our real concern. Sound policies are essential to wise and fruitful administration. Profit sharing where intelligently applied with attention to the all-important psychological factors and in such form as to keep the "shared profits" separate and distinct from wages, has proved more effective in securing permanent satisfaction, developing cooperation, and creating the consciousness of real partnership in the minds of the employees than any other form of employer-employee policy.

The committee entered upon this fact-finding survey with a free and unbiased desire to assemble the experiences of profit-sharing plans—their advantages and disadvantages—in order that a reliable and authentic record thereof might be made available to all employers and employees.

We have sought to accumulate definite facts and information as to the experience of business enterprises in the United States based upon the actual figures relating to annual earnings and the proportion of gross income which is allocated to salaries and wages and to taxes, State and Federal.

An important feature of this survey is to ascertain from the experiences of going business concerns, not alone what is the desirable earning on capital invested, but what is the actual earning; not only what is an estimated living wage, but what is an adequate and paid living wage, and, if possible, what the contribution of the worker may be, which would entitle him to a wage dividend or share in the profits of the enterprise over and above his contractual wage.

The survey is primarily concerned with the history of profit sharing and extra compensation plans, the success or failure of such plans, and the reasons for their continuance or abandonment.

These facts are not unrelated to the broader aspects of unemployment and reduced national income.

The report should aid those employers who may wish to adopt policies for strengthening the relationship between employer and worker, and to insure industrial peace and the preservation of independent enterprise.

The voluntary adoption of profit-sharing plans by employers requires no legislation. Legislation would be necessary only if compensatory tax exemptions or rewards, in addition to those already granted, where deemed desirable to encourage the voluntary establishment of profit-sharing systems by employers, or incentive tax measures to encourage the employment of workers, and the investment of additional capital in plant expansion and betterment.

It is conceivable that we shall recommend no further legislation, should it be the judgment of the committee, based upon the evidence, that the ends sought can best be achieved by a helpful attitude on the part of Government without additional laws.

Equal to the confusion existing among employers as to the ways and means toward industrial peace is the misunderstanding and divergent views on profit sharing, what it means, what it will accomplish, and how it should be applied.

Some declare "you cannot share profits without sharing management"; still others are fearful that "profit sharing transfers ownership." These fears seem to be unfounded, since signally successful plans are reported as having been in operation from a quarter of a century to a half century or more.

It is argued by some that "profit sharing will of necessity raise wages." Others assert that "its operation will reduce wages."

As to the effect on wages, the one positive result of profit sharing, except as affected by broad general economic changes, appears to be that it tends to stabilize wages, and provides such permanency of employment as to reduce the labor turn-over to a fraction of normal.

There are those who claim that "the sharing of profits cannot be differentiated from wages," hence that it all is added to the wage scale and that the strife to secure more and more will continue.

The testimony of employers with most successful plans indicates that this result does not follow. We are familiar with plans under which the employee attaches no relationship whatsoever to his wages and his share in the profits.

There is the quite prevalent belief that employees will support and approve a profit-sharing plan while profits are being made, but that they will become resentful when losses occur and profits are not available for distribution under the plan. A number of companies have testified through their executives that no such condition prevails among their workers.

The record of profit-sharing experience indicates its application requires intelligence and study. Too many overlook or ignore psychological factors which are as important, if not more so, than the dollars involved.

The principle of profit sharing is grounded in the traditions of the American system. To broaden the base and increase the number of participants, and to instill personal consciousness of the individual's interest in the "profit system," is to mobilize an unbeatable defense of the American capitalistic system and made democracy triumphant.

The triumvirate of industry—capital, management, and labor—should now, as never before, be united against the enemies who seek to destroy them.

The brilliant success achieved by many companies which have adopted profit-sharing plans suited to their needs is perhaps proof that others can do it if they have the will to do it.

Voltaire said: "If a nation be made to think, nothing can stop it!" Undoubtedly Voltaire meant nothing could stop the nation from achieving success, progress, and prosperity, and the fulfillment of the highest destiny of mankind. Conversely, I would submit—if a nation ceases to think, nothing can prevent its ultimate degeneration, dissolution, and decay.

Who can estimate with accuracy the cost of the misunderstandings between employer and employee—not alone to them—but to the American people? The financial burden of strikes and lockouts—the inevitable antagonism with their moral consequences—the loss in many days and workers' wages—the enforced curtailment of output, which affects the entire system of production and distribution all the way down to the clerk and delivery boy in the retail store—the reduced purchasing power—the increased relief load?

The total cost probably would be a sum sufficient to pay the entire public debt in less than a decade.

The paramount question therefore is: Will profit sharing aid in meeting the problems involved in employer-employee relationship in the more than 99 percent of the 2,000,000 business enterprises in the United States which do not now employ a profit-sharing plan?

Since the system of private capitalism is expressly designed to provide opportunity for each and all to invest with that measure of economic independence, which under a free government and a free economy enables a man to be and to do his best, the fair distribution of newly created wealth at its source on an equitable basis offers a just and proper division of the fruits of industry, consonant with the principles upon which American democracy is founded.

I cannot emphasize too strongly that this survey is a mutually helpful enterprise—and that we have solicited the cooperation of both employer and worker on a voluntary basis only.

After several months of investigation and research, we are encouraged by the completely satisfactory results obtained thus far, wherein industrial leaders and their employees have given the committee the fullest measure of helpful cooperation. The committee deeply appreciates the assistance which has been received from all sources and they are many.

When this survey has been completed the Government will have made available to all interested employers and employees a report of the experiences, favorable and otherwise, of all profit sharing and extra compensation plans operative in the United States today, and likewise the argument for and against any suggested legislation in connection with compensatory tax exemptions and rewards and incentive taxation.

The members of the committee hope it will be as fruitful of results as the survey itself has been valuable. We believe that a solution of our grave problems of unemployment and reduced national income can be found. We believe that the profit system can be made to work in the interest of employer and employee. Profit sharing may be the answer.

Senator HERRING. Mr. Beavers, vice president of Peoples Drug Co.

STATEMENT OF T. N. BEAVERS, VICE PRESIDENT, PEOPLES DRUG CO., WASHINGTON D. C.

Senator HERRING. Your schedule of information shows you have quite an interesting profit-sharing plan operating in all of your stores. Will you please give us a brief history of it?

Mr. BEAVERS. Well, sir, we have a company that was started in 1905 from one store here and has grown to 135 in 7 adjoining States and the District of Columbia. During that period we have utilized several profit-sharing plans, some of which have been successful and some of which have not. At one time we had a very fine plan, it seemed at that time, the acquiring of stock in the company itself for the employees. I think that was a complete failure, because in one way it prompted each individual to watch the stock market reports rather than to think of his business; and, secondly, anything that happened to the market in relation to that stock immediately accrued to the ill will of the company, and notwithstanding the fact that today, if that stock was in the hands of the individuals, it would have shown a very handsome increment, there was so much complaint of it, that we retrieved all of that stock and paid every individual all that he paid for it, plus 8 percent. I mean we felt it was that much to our benefit to get that plan out of the way.

Senator VANDENBERG. How long did you operate that kind of a profit-sharing plan?

Mr. BEAVERS. About 2 years, sir.

Senator VANDENBERG. And to what extent was it participated in?

Mr. BEAVERS. Well, it was a rather broad proposition. The employee acquired this stock at a price of about one-third of what it was in the market at that time; that is, it would have been his net cost, including what the company participated in. The only strings attached to it was the fact that they must remain with the company for a definite period. That period was from 3 to 5 years.

Senator VANDENBERG. How many employees did that involve?

Mr. BEAVERS. It was open to all.

Senator VANDENBERG. How many took advantage of it, in a general way?

Mr. BEAVERS. I do not know exactly. I should say probably 75 percent at that time.

Senator VANDENBERG. In what years was this?

Mr. BEAVERS. That was back in 1928 and 1929.

Senator VANDENBERG. Would the fact that those were particularly calamitous years for stock values have anything to do with that?

Mr. BEAVERS. I think it would; yes.

Senator VANDENBERG. In other words, perhaps your experience was not as typical as it might have been?

Mr. BEAVERS. It might have been the time rather than the plan.

Senator VANDENBERG. And the objection that you found chiefly was that the fluctuation in the stock values reflected the fluctuation in employee loyalty and interest?

Mr. BEAVERS. That is right. In other words, they sort of seemed to blame the company for those things, notwithstanding the fact that the company was doing just as well then as it ever had, but it was a stock-market fluctuation rather than a company policy.

So we abandoned that. Since that time, and, of course, way before that time, that was in addition to what we now have, our plan was largely what we might term a bonus plan. It is a preconceived or predetermined amount, and it runs something along this line:

To our managers and assistant managers of the various units we devote 3 percent of the store operating profit for distribution. Now store operating profit is before any taxes, and that sort of thing, it is simply the operation of the store itself. That was with only one alteration, and that is an equalization of rent. That is the one thing in the operation of that unit which they have no control over, that is something that we do ourselves. If a man is operating here at a very high rate of rent, that is equalized to the average. Three percent of that operating profit is divided then 75–25 between the manager and assistant manager of that store.

Senator HERRING. There is no charge for executive management outside of the store?

Mr. BEAVERS. Yes: that all goes into the store operation, but it is before any tax deduction of any type.

Senator VANDENBERG. You mean 75 percent goes to the manager and assistant manager, and 25 percent to the company?

Mr. BEAVERS. No, sir; the 3 percent is divided 75 percent to the manager and 25 percent to the assistant manager. That is paid yearly. Then we have a plan of the same type for the men who operate the soda fountains in the stores. However, that is paid monthly, and, of course, being paid monthly it more or less becomes a part of compensation. It has that tendency. I think it would be better, as a profit-sharing plan, if it were paid possibly semiannually or even annually, because anything that is paid too often becomes too much a part of compensation, although it is not considered that.

Senator HERRING. What does that average, on the soda-fountain plan, in monthly wages?

Mr. BEAVERS It varies very greatly, Senator, according to the size of the store, the volume of business, and so on. It would be pretty difficult for me to say what the average is. In some stores it amounts to as much as $40 or $50 a month, and in other stores perhaps not more than $10.

Senator HERRING. And your base wage as paid is as high as in any other drug store without that plan?

Mr. BEAVERS. That has been one of our principles—to keep our base rate always as high or higher than any of our competition. I think that is very essential for organization purposes.

Then, in addition to that, we have what we term the "wage dividend." This has been paid at the end of the year and has amounted to—well, our formula is this: 50 percent of the month's salary for those people who have been with us over 2 years, 35 percent of the month's salary for those between 1 and 2 years, and 25 percent for those between 6 months and 1 year.

Senator HERRING. That applies to all employees?

Mr. BEAVERS. All employees other than those on a bonus plan. That is, it would not apply to the manager and assistant manager.

Senator HERRING. I see.

Senator VANDENBERG. Does that apply regardless of the earnings of the company?

Mr. BEAVERS. It has so far. We, of course, reserve the right to discontinue it. If we did not make money we could not pay it. However, there has never been any percentage arrangement relative to earnings. Fortunately we have been able to earn enough to pay that.

Senator VANDENBERG. I should think if you had a standard formula which was not geared in any way to the profit ratio of the company itself from year to year that that definitely would be accepted as a part of the compensation and would substantially lose its reward value.

Mr. BEAVERS. Well, that is possibly true. I think you are probably right in that. In other words, if we came to a year when we did not earn we would get a very bad kick-back from that. That is possibly true. One of the things in our company that is perhaps not true of the average is the fact that we have a very steady employment and our income has been very steady.

Now, in addition to that, we have the executive bonus that applies to what we call juniors and seniors, which is participated in by everybody except the president of the company. That is a predetermined amount and is taken at 5 percent of the net earnings of the company after all of these other charges, plus taxes—these others come, of course, before taxes—and that is distributed on the basis of their salary percentage to the total.

Senator HERRING. How long has this plan been in effect?

Mr. BEAVERS. About 10 years.

Senator HERRING. About 10 years?

Mr. BEAVERS. Yes, sir.

Senator HERRING. You are satisfied it has had good results, that it is good business?

Mr. BEAVERS. I think it is; yes, sir. I think we have a very splendid personnel, we have a personnel that we are very proud of.

Senator HERRING. Your statement confirms that it is good business?

Mr. BEAVERS. I think all of this has been very good business. These distributions that you might term profit sharing have amounted to in the last year about 20 percent of the net earnings of the company. It fluctuates some, but it has amounted to approximately that.

Senator HERRING. All of those taken together amount to about 20 percent?

Mr. BEAVERS. Yes.

Senator VANDENBERG. And what percentage of the net earnings of the company would be contributed as dividends?

Mr. BEAVERS. About 63 percent.

Senator VANDENBERG. You are really sharing in the ratio of about 1 to 3?

Mr. BEAVERS. That is right.

Senator VANDENBERG. How many employees have you?

Mr. BEAVERS. About 2,750.

Senator VANDENBERG. On the subject of incentive taxation I notice this comment in your reply to our questionnaire:

> We favor encouragement of business and establishment of profit-sharing and employe-welfare plans, and believe if a method could be worked out whereby a standard tax advantage would accrue to those meeting certain requirements in this respect, it would be highly desirable from every standpoint.

Is that your point of view?

Mr. BEAVERS. Yes, it is, sir; with this addition. I think it is entirely impossible to work out such a formula. I think if the formula could be worked out that would be true, but I do not believe that it can. There are a lot of other things that enter into it. For instance, I am led to believe that we are one of only two companies that have complete insurance coverage on our employees. I think that has worked out to great advantage also, and it is done without becoming paternalistic, which is, in my opinion, very important. All of our employees are covered by group life insurance, ranging from $1,000 to $10,000, which at the present time, due to good experience, is 25 percent in excess of that.

In other words, the base value of those policies today is $1,250 and $12,500.

Senator HERRING. Is that all paid for by the company?

Mr. BEAVERS. No, sir; that is a participation.

Senator HERRING. That is a participation?

Mr. BEAVERS. Yes. The company pays for about 30 percent of it.

Senator HERRING. Is that 30 percent included in the 20 percent?

Mr. BEAVERS. No.

Senator HERRING. That is in addition?

Mr. BEAVERS. That is entirely in addition to the bonus plans, the profit sharing that I mentioned.

Senator HERRING. Yes.

Mr. BEAVERS. We also are fully covered with accident and health, with benefits running from $7.50 a week up to $40 a week. That has a 7-day waiting period, which the company has always paid, and it is the policy of the company to pay full wages for 7 days. In other words, they lose nothing on that. We also have a hospitalization plan which is in no way in conflict with the present controversy here. It covers 70 days of hospitalization plus a very wide range of physicians' operating expenses.

We have not had that in effect long enough to give you any particularly good record of it. By the same token, we are unable to say just what the cost is going to be. That is paid for entirely by the company; there is no participation in that whatsoever. Our first year of that the cost was approximately $30,000, but, as I say, we have not developed an experience on that sufficiently to give a good account of it.

In addition to that we have an annuity plan, which has been in effect about 6 years. Our own limitation on that is age 30, and 2 years with the company. That, of course, would not be necessary, but in our business our great turn-over comes in the young people who work on the fountains. They have not established themselves, and a good many of them just take it as an interim job until they find another place. So there is where our large turn-over comes, and in any plan of this type it is essential that we eliminate them from it, because it would be complicating it to such a great extent that it would probably nullify it.

Senator VANDENBERG. Do you think that the institution of these group life insurance and bonus plans has reduced the turn-over?

Mr. BEAVERS. I believe so; yes. I believe they have a very material effect in that way.

The annuity plan was also introduced. The company picked up all back services at its own expense, back of the 30 years of age and the 2 years' service with the company, and the present payments are 50-50—that is, the company pays half and the individual pays half, and the general benefits of it would be approximately half of their current wage—that is, that would be the retirement pay. It is not hide-bound at 65, it is elective between 55 and 65. It is quite an elastic plan.

Since the average age of our employees is only 27 years, of course, that is affected very largely by the large number in the low-wage bracket. We have only two or three people at present that are retired on that, so there is not much to be said about it, except we feel it is going to work out fine.

Now, in addition to those things, of course, we have the usual vacations with full pay—2 years and over, 2 weeks, and 1 year to 2 years, 1 week.

We have a selective arrangement whereby we finance several students through college every year, that is making a maximum of 28. Those boys come out of there clear. We do that by holding examination. We sidestep the responsibility of picking them by letting the college hold the examinations.

Senator VANDENBERG. They learn professional subjects? They study professional courses to create pharmacists?

Mr. BEAVERS. Professional courses. We find that is a fine thing in the company, because as a rule we find some underprivileged boys that do not have any opportunity, and those are the boys that make the best students. We usually have 50 or 60 applications for those, and we pick 7 each year.

Senator VANDENBERG. How long have you been doing that?

Mr. BEAVERS. The first class will graduate this year.

Senator VANDENBERG. I suppose you expect that they will return to you after they graduate?

Mr. BEAVERS. That is not at all necessary.

Senator VANDENBERG. There is no obligation?

Mr. BEAVERS. No obligation; no, sir; but we naturally feel that they will, because they have been boys that we know well in the company before they are accepted.

We maintain a credit union in the company which has been very successful. The only thing we do on that is to pay the expenses of it—that is, we pay for the man who administers it—otherwise it is the ordinary, regular Federal credit union.

We finance various picnics and furnish uniforms for baseball teams; you know, all of those things that go to promote athletic activities in the company.

This might sound funny to you, but it is really a good thing, and I would like to have you read some of the letters that we get sometimes from them. Every child that is born in the company we furnish a complete lay-out, not clothing, but all the hospital necessities, and so on. It is a small thing, but a nice thing.

I think, sir, that covers about the extent of our participation in the profits.

Senator HERRING. The sum total of all of these things, in addition to the 25 percent, would run into quite a figure, would it not?

Mr. BEAVERS. Yes; it would. I would say that those things, in addition to the profit sharing, would probably amount to $100,000, easily.

Senator HERRING. Who was responsible for inaugurating all of those plans? There must be somebody in your organization that is at the bottom of it.

Mr. BEAVERS. Well, the man who founded our company is still the president of it—he is still very active and still can call most of the people by their first name—Mr. Gibbs.

I have been a member of the company since 1919, and I feel rather proud that I had something to do with all those things, too.

Senator VANDENBERG. Well, the net result of it all is to create, in your judgment, not only an effective and happy employee relationship but it is also a good business investment.

Mr. BEAVERS. I think so; yes. I believe if there is any virtue in those things that this is one place where virtue has had its own reward. I think it has been rewarded by a good company.

Senator VANDENBERG. That is a very fine statement.

Senator HERRING. That certainly is.

Mr. BEAVERS. I rather doubt, however, whether things of that kind could be made a part of a formula to be administered by some outsider. I think, as you have just expressed, Senator, those things come from within. They come from a genuine desire to promote welfare and a sense of security among people, and I think, in addition, that they promote a sense of confidence, trust, and appreciation between management and employees.

I would like to give you an example—and I am not trying to be facetious at all. Perhaps one of the things that promote good domestic relations is the fact that you kiss your wife in the morning before you go to work, but I doubt very much whether it would be very efficient if you had some Government agent stand over you to see that you did kiss her.

Senator VANDENBERG. I do not know why in the world they have not thought of that.

Mr. BEAVERS. I really mean that; and, as I say, I am not trying to be facetious. I believe the moment you try to write this into a formula—and naturally if you wrote it into a formula you would have to have somebody administer it, because unfortunately we are not honest, all of us, enough to do what we say we should do.

Senator HERRING. Perhaps that is the reason it has not been inaugurated; we would have some difficulty to get somebody to administer it.

Mr. BEAVERS. I believe it would be somewhat difficult.

Senator VANDENBERG. Well, we agree with you, I am sure, Senator Herring and I both, that you neither can regularize and standardize a profit-sharing formula in this country, nor can you dictate one under compulsion.

Mr. BEAVERS. That is right. It takes the real meaning out of it then.

Senator HERRING. I was wondering to what extent your annual increase in business for the last 10 years might be due to these policies or to expanding your operations in new stores.

Mr. BEAVERS. Of course, that is very difficult to say. As a matter of fact, in the last 5 years we have not added materially to the number of stores.

Senator HERRING. You have not?

Mr. BEAVERS. No, sir. We have devoted our time and money to improving the stores, enlarging them, and that sort of thing. We have added very few in the last 5 years.

Senator HERRING. Your volume increased about $5,000,000 in that 5-year period?

Mr. BEAVERS. Yes, sir.

Senator HERRING. There must be something behind it.

Mr. BEAVERS. Well, sir, we believe that anybody can buy merchandise and anybody can rent storerooms, but we do not believe that everybody can build up an organization.

Senator HERRING. Thank you very much, Mr. Beavers. Unless you have something else to suggest, that will be all. I am grateful to you for coming over here.

Senator VANDENBERG. I hope we do not start this K. Y. W. A., Kiss Your Wife Authority.

Senator HERRING. Mr. Wilson, of the Hammermill Paper Co., Erie, Pa.

STATEMENT OF NORMAN W. WILSON, GENERAL MANAGER-VICE PRESIDENT, HAMMERMILL PAPER CO., ERIE, PA.

Senator HERRING. We do not seem to have a schedule here from your company. Do we have that?

Mr. WILSON. Yes. There is a general statement on profit sharing or bonus system, sent in response to Mr. Despain's correspondence that began in August, and also a Schedule of Information. For that reason I have not prepared any particular statement, but I would proceed in any way that you would like me to do so.

Senator HERRING. In the absence of that Schedule, you may just proceed and give us a brief description of the plan, when it was inaugurated, and tell us all about your business. Perhaps that is the best thing to do.

Mr. WILSON. Thank you. Our business at Hammermill Paper Co. is the production of what you might call business papers, correspondence papers, office and factory forms, and a variety of that type of papers, made for increasing the efficiency of operating offices and factories, and businesses at large.

I would like the privilege of saying that while I appreciate the invitation that came to the president of our company, and the privilege of appearing here, I do not extend myself as an expert upon the subject.

We at our company, the officials and keymen, all believe so profoundly in the spirit that is back of the committee that we are glad to appear, and we want to do anything we can to be of practical assistance.

Senator VANDENBERG. That is greatly appreciated.

Mr. WILSON. Now, beyond that, how would you like me to proceed?

Senator HERRING. Just with an expression of the inauguration of the plan, what the plan really is, and what effect you think it is having upon your business.

Mr. WILSON. I would be presuming upon your time if I take up some of the details.

Senator HERRING. We have all day. Just go right ahead.

Mr. WILSON. The plan goes back to the earliest days of the company, which was founded in 1898. The founders of the business brought an innovation in paper to this country through refining wood pulp to a degree that it was a good raw material for the production of fine papers, which up to that time had been produced entirely from rag fibers, or a combination and rag fibers and wood pulp.

You understand, of course, the difference between coarse papers and fine papers made from wood fibers. It is principally in the refinement. For the finer grades the peeled log first is reduced to thin chips, which in turn are chemically reduced to pulp, and then carefully screened so that nothing is retained but the pure cellulose, all of which entails a loss of approximately 50 percent of the original log, whereas in producing newsprint, for instance, the peeled log is mechanically ground to a pulp, which then is mixed with a small percentage of a chemically prepared pulp.

The public did not take immediately to the new product, and the early years of the company were very precarious. As a matter of fact, the trade papers, or at least one of them, carried a story on the "Hammermill Folly," first, because of where we located the plant; and second, that the kind of product we were aiming to make would never be popular with the public.

The location of the plant was chosen partly because of economic soundness, availability of coal and pulpwood, and a very good shipping center to the principal markets of the country. It also was chosen because of consideration for the men and women who were to work there.

Up to that time the practice had been, particularly with paper mills which made their own pulp—there were not very many in those days—to locate in what we might call the hinterland, where wood was plentiful particularly, and where there were few opportunities for the employees outside of working hours. Erie was selected by Mr. Behrend, the president of the company, and his brother, who is the treasurer, very much out of consideration for the employees, believing that they should have hospitals, schools, churches, and other means for good living.

Senator HERRING. How many employees have you, Mr. Wilson?

Mr. WILSON. Approximately 1,400. In actual number of employees, of course, we are not a very large company; in the actual production of paper our volume, of course, is not great as compared to grades as newsprint, but in our field of paper we are a very substantial producer.

The introduction of the kind of paper to which I refer was of great benefit to the people of this country. It provided a less expensive paper, so that it could be used in a volume that was impossible under the cost of what fine paper had been produced up to that time.

Senator HERRING. Are your employees organized at all?

Mr. WILSON. They are not.

Senator HERRING. No union association?

Mr. WILSON. No.

Senator HERRING. Your prevailing wage scale is as high as paid in other industries in your town and throughout the country?

Mr. WILSON. Our prevailing wage scale ever since I can remember—not ever since, but let us say easily for 30 years, has rated high in the industry, at times the very highest, and at some times because of the peculiarities of smaller areas, not the very highest, but always above the average.

Senator HERRING. What would you think the average would be, the average annual pay to the individual?

Mr. WILSON. That is a broad question. I wonder if you would mind if I send you that information rather than attempt to answer offhand, and perhaps go astray.

Senator HERRING. It is probably in your schedule.

Mr. WILSON. I think so.

Senator HERRING. What is your profit-sharing plan?

Mr. WILSON. Would you like to know how it came to be introduced?

Senator HERRING. The plan itself?

Mr. WILSON. Yes; how it became introduced.

Senator HERRING. Yes.

Mr. WILSON. The policy of the officials of Hammermill is not intended to be paternalistic nor philanthropic except in the best sense of the term. Basically, we believe that each employee should be paid as well as his contribution and ability of the company will permit.

Each of the many things that have been done for the employees in addition to their wages came from the belief of the founders of the business, and the entire management, that such action was sound from a business standpoint.

There is a good deal of sentiment at Hammermill. The founders believed in courtesy and good ethics. They believed in fair treatment of their customers and of their sources of supply. When we have had a difference of viewpoint with our distributors or those from whom we buy, we settle these differences by personal negotiations, searching for a solution satisfactory to all concerned. We believe in, and attempt by our conduct to demonstrate, the same consideration for all employees. The natural result is that Hammermill employees repeatedly exhibit an understanding of company problems and a give and take which is an inspiration to the management to be more and more considerate of the men and women who work for and with us.

As to our profit-sharing plan, we thoroughly believe that its installation, more than 35 years ago, was the foundation upon which good will within the company and the actual success of the business have depended to a substantial degree.

Well, it came about in this way: In these earliest years while we were struggling to keep our heads above water—I was just a boy in the plant in those days, but I knew something about it and, of course, I became more familiar with it in later years—our machine tenders, as the head man is known on each of these large paper machines, and the back tenders and beater men who prepare the pulp for those machines, desired a raise in pay.

As I recall it, at that time the going wage for such skilled paper makers was $3.25 a day for 12 hours' work, and they desired to get 25 cents a day more. We were paying at that time at least as much as anybody in the industry was paying. We were competing terribly for our existence, and the president of the company explained that to the men. They talked it over at length, and finally he offered to commence a sales bonus, taking the present sales, the sales up to that time, as a basis, and offering to give them a share in any increase in sales.

Well, they could not see it, it was too indefinite. He explained to them the opportunity they had for economies. There were two paper machines side by side, and when there was a break on one paper machine—and in paper machines the web will break down—there would be an opportunity for the crew on the other machine to help to get it started; or when they had to change wires, for the two crews to do it together, or when the clothing would have to be replaced to do it together, to have team work, and in the production of the paper to use greater care, so there would be less wastage in its finishing and less paper returned from the customers.

Well, they still could not see it, so he proposed to them that they try it for a 3-month period, and if they did not get at least their 25 cents a day, he would guarantee it, or if they did not like the plan for any reason at the end of 3 months it would be discarded. It immediately showed results, and that gradually worked into our present bonus and profit-sharing system.

Senator HERRING. What is the present system?

Mr. WILSON. It is very hard to describe, because it certainly is not exclusively profit sharing; it is a combination of wage and bonus.

As described in the material which we sent to you, the officials, the department heads, the superintendents, the foremen, all participate in the same system. Those who can contribute most to the earnings of the company obtain the larger percentages, and those who can contribute less obtain the smaller percentages.

As it has developed, I would say our employees do not obtain the full going wage for this, that, and the other type of work, but with the wage and bonus combined they are better paid considerably.

Senator HERRING. Than those who do not have a profit-sharing plan of any kind, you mean?

Mr. WILSON. No; than the industry, than other people who do not have this system.

Senator HERRING. Do all of the employees share in this bonus plan?

Mr. WILSON. No; we tried it all the way through the business at one time, and we found that there were enough people who did not understand the principle, that it could not apply to all. It was all right when income increased, nobody questioned it, but when income of the company decreased, and therefore the income of the employees, some of them could not understand it. They considered that their wages were being cut, and we withdrew it.

Now, we have, with the exception of 81 people out of this roughly 1,400, everybody either on profit sharing or on a premium of some kind and many of them on both.

Senator HERRING. And the 81 have a chance to get upon that?

Mr. WILSON. Yes; if they develop into fields where they can participate they are eligible.

Senator HERRING. As compared to the dividends, how much is distributed to the employees?

Mr. WILSON. Well, I have tried to make a break-down of that on the basis of profit sharing itself, and I would not want to get into your record a confusing element without a word upon it.

Keeping in mind my statement as to wages and salaries, there are no high salaries at Hammermill Paper Co., but we are all well paid in good times. The actual bonus participation during the past 2 years has just about equaled—did you ask whether it has exceeded the dividend?

Senator HERRING. Yes; whether it did in dollars and cents.

Mr. WILSON. Yes. For the 2 years combined, that is right, and it has about equaled the earnings. In explanation of this fact, may I state that when our sales bonus was converted to a profit-sharing plan more than 20 years ago, the management realized that there would be dissatisfaction if payments were based upon net earnings. Our plan is based upon gross profits before depreciation and tax on income. Keep in mind that this is not a profit sharing upon the gross base rate for any job, whether it is or is not a salaried job.

Senator HERRING. Is it a percentage of the annual wage?

Mr. WILSON. This is paid at the end of each month, just as soon as the estimated monthly figures are completed.

Senator VANDENBERG. Well, you tie your wage incentive directly into the regular system of compensation?

Mr. WILSON. Exactly. We feel that there is nothing that is quite equal to individual opportunity and incentive.

We never bring a pulp or paper maker into the business from the outside when he can be developed from the inside. We never appoint a foreman from the outside. When I say "never" it is so long since that I cannot tell you how many years. Those men have developed into foremen, the foremen have developed into superintendents, the superintendents and department heads into officials of the company.

The founders of the business built a modest home on the mill property and lived there while they were both bachelors. One of them married, and he and his wife lived there the year round, until the last recent years. There are five company executives today, who live right on the mill property and, of course, know the employees intimately.

I believe that only part reference or no reference was made to a few things that you want on your record. I am not certain, but I believe that Hammermill Paper Co. was one of the first to sense the unfairness of leaving to foremen, or even superintendents, the right to fire people, particularly on short notice. You know, the custom that prevailed years ago, a foreman or a superintendent might have had illness in his family, or maybe he had indigestion in the morning, or something happened that displeased him, and he might send the man home indefinitely or actually fire him on the spot, or the employee might be grievously at fault temporarily, a little brainstorm, and lose his job. That was sensed by the president of the company, and even at the displeasure of the superintendents and foremen, he appointed an industrial relations director, and no man from then on could be discharged without an opportunity for a hearing before that director. In fact, no man is discharged without a hearing by the superintendent or foreman and the chief of the industrial relations department.

As I say, I do not believe we are the first on that, but I know we are among the pioneers.

Paid vacations for people began at Hammermill Paper Co. many years ago. They had to be stopped temporarily at the depth of the recent depression, I mean the former depression, if that would make it any clearer.

Senator VANDENBERG. What one are you talking about?

Mr. WILSON. I am talking about that one that began in 1929. More recently, however, 3 years ago, we faced the thing as a matter of right, as a matter of soundness, and reached the conclusion that if our mill employees were not entitled to paid vacations neither was anybody else in the business. It was a class distinction which did not fit into the spirit of our relations between employers and employees, and so paid vacations for our mill employees were renewed, and I believe they will continue until such time as we cannot have any paid vacations at all.

Group insurance goes back quite a number of years. That is participated in by both employees and employer; the cost, I mean.

Now, as to the dismissal wage. Any person who has been 1 year with our company—and a year is a very short period in our plant—receives a dismissal wage if he leaves the company for any cause not his own. There is a schedule set-up for adjusting that.

Senator VANDENBERG. What is the dismissal wage, speaking generally, in dollars and cents in relation to the full wage previously earned?

Mr. WILSON. The minimum weekly payments are $10, and the maximum are $30, and may be anywhere between, depending upon the age of the employee and the years of service that he has given to the company.

Senator VANDENBERG. And for how many weeks?

Mr. WILSON. The maximum length is 26 weeks. It will range anywhere up to 26 weeks, depending upon the factors I have given you.

There is a service annuity which is not fixed, because we see no way to secure the Hammermill Paper Co. for all time, and, therefore, have not committed ourselves to any pension, but men and women who reach the age of 65 and who have been there 20 years are entitled to service annuity, if they want it. Many of them do not want it, they want to continue to work.

I believe the record we sent you will show we have 85 people over 60 years of age.

Senator VANDENBERG. Still working?

Mr. WILSON. Oh, yes. There are 192 over 50, besides this other 85, and in addition to those groups we have 354 over 40. That is not extraordinary, but it compares pretty well, I think, with other industries.

Loans are made to the mill employees without any interest charge at all.

As an evidence of the understanding between all of our people that this is a partnership, that it requires the united effort of everybody connected with a business to make it successful, particularly in these days, perhaps you would not mind if I told you of two circumstances, one that occurred on the twentieth anniversary of the company, and one that occurred on the fortieth anniversary. Naturally, the twentieth anniversary for the company is the twentieth anniversary for the founders, and the mill was shut down and the founders were asked to appear in the open with all of the employees, and this bronze plaque presented to them. May I read it?

Senator VANDENBERG. Yes.

Mr. WILSON (reading):

> This tablet was cast on the twentieth anniversary of the founding of the Hammermill Paper Co. out of pride in the institution and admiration and affection for Ernst R. Behrend and Otto F. Behrend whose vision, ability, and business ideals have been an inspiration to our work and our lives. Erected as a pledge of future effort by the men and women of Hammermill, June 28, 1918.

Every person in the organization, excepting the two recipients, helped to pay for that bronze tablet. That is on one of the entrances to our main office, so the employees see it, the officials see it, and the visitors see it.

I might read to you a tablet which is on another entrance:

> Hammermill has been built on individual enterprise, respect for the rights of others, law, and order. These are the fundamentals of our civilization and the protection of our home.

That is signed by the president, Ernst R. Behrend.

On the fortieth anniversary, the president and his wife—may I reverse that, Mrs. Behrend and the president, because she is really the boss of the family anyway——

Senator VANDENBERG. That is no novelty. [Applause.]

Mr. WILSON. There seems to be some married men present. At any rate, they invited all of the employees to spend the day on the little farm they have 4 or 5 miles from the plant, and the employees all accepted. Arrangements were made to feed them and to have games, and also a little ceremony at which there were presented service pins, or whatever recognition they were to get for that particular year.

Beginning a great many years ago, at the end of 3 years each employee receives a little pin. It merely states the name of the company and the number of years of service. At the end of 5 years the 3-year pin is replaced with one specifying 5 years of service; and at the end of 10 years there is another replacement; and another one at the end of 15 years; and at 20 years there is a certificate of service and a choice either of a watch of standard make or a share of the preferred stock of the company, which is worth somewhat about par, or at least people seem to think it is.

Each year some kind of ceremony is held, and all those entitled to the 3-year pin, 5-year, 10-year, or whatever the year is, are presented with these tokens.

Now, it being the fortieth anniversary, Mr. and Mrs. Behrend thought it would be nice to make that presentation with all the employees present. Well, this is the interesting thing I want to bring out to you. Shortly after this invitation went out, one of the men from the mill, who had been there quite a number of years, not in a high position but a skilled mechanic, came to the chief of the industrial relations department and said they were taking up a collection in the plant, they wanted to buy something for Mr. Behrend and Dr. Behrend, and out of that developed two books having a reproduction of this [indicating] on the cover, this bronze tablet of the twentieth anniversary and the signatures of each employee, whether in Erie, New York, or San Francisco, or wherever they were employed, and a statement at the bottom, "A rededication to service by the men and women of Hammermill at the end of the second 20 years," and after the ceremony where the president gave out the service pins, they surprised him by presenting those books, one to him and one to his brother.

There was nothing in those books whatever, except the signatures and a reproduction of this tablet that I read to you. I think perhaps the Senators might take a minute to look at some of the pictures taken at that picnic, to see whether it looks like a happy family or not.

Senator HERRING. What has been the effect of your low base wage upon the attitude of the employees?

Mr. WILSON. The low base wage?

Senator HERRING. Yes.

Mr. WILSON. We have no low base wage.

Senator HERRING. I understood you to say that you had a low base wage.

Mr. WILSON. Our base wage—that means for unskilled employees—is not low; it rates high, at least equal to, and usually higher than the industry pays, and at least equal to or higher than our local institutions pay.

Senator HERRING. That is, without the bonus?

Mr. WILSON. Absolutely. What I meant was that those who participated in the bonus do not have the maximum pay for that; they have somewhat less, and then the bonus on top of it, and over the period of years they have averaged much above the competitive rate.

Senator HERRING. You have slack periods, I suppose. How do you distribute your work during slack periods?

Mr. WILSON. Well, in a paper mill you must run continuouly, and if you do not have enough business to run full you cut down the number of days that you run. If you only have 5 days' work instead of 6, you only run 5 days, but you run day and night.

Senator HERRING. That affects the sharing plan also, does it not, if the man is not working?

Mr. WILSON. Oh, yes.

Senator HERRING. I think unless you have something else, that gives us a very good record, Mr. Wilson. Thank you, sir.

Mr. Tily, president of Strawbridge & Clothier, Philadelphia, Pa., which is a large merchandise and dry goods house.

STATEMENT OF H. J. TILY, PRESIDENT, STRAWBRIDGE & CLOTHIER, PHILADELPHIA, PA.

Senator HERRING. Mr. Tily, you have a pension fund, employees' relief association, and other benefits?

Mr. TILY. Yes.

Senator HERRING. I think you do not have a definite profit-sharing plan, do you, Mr. Tily?

Mr. TILY. No; not definite. We have considered it over the years.

The pension fund has been in existence since 1907. It is classified as the joint contributory type of organization. All employees between the ages of 20 and 50 are eligible for membership. The pension fund is an employee-controlled organization, electing its own officers and board of directors. The employee's dues are nominal, and the total annual contribution represents not more than 20 percent of the total income. The balance, or 80 percent, is contributed by Strawbridge & Clothier. Over the last 10 years the total income has averaged about $30,000 per year. These funds are used to pay benefits. Pensions are paid to members who have been employed for 15 years. The maximum pension is $40 per month. There are approximately 1,500 employees contributing to the pension fund, and 90 are now receiving benefits.

I want to add to the letter that I sent, that during the last 11 years we paid out $120,000 to superannuated and sick executives in addition to the other sum mentioned above.

In the spring of 1937, the time of the old-age pensions, we made it optional with the people whether they would stay in or not. Two-thirds of them voted to stay in.

The employees' relief association——

Senator VANDENBERG (interposing). What does that mean? That they carry both, those who stay in the fund?

Mr. TILY. Yes; but with this understanding, that when they are eligible for pensions the difference between what they get from the Government and what they would be entitled to would be paid by us.

The organization has been in existence since 1880. The employees' relief association is supported jointly by Strawbridge & Clothier and individual employee members. Employees under the age of 60 are eligible for membership. The dues are assessed on a graduated basis from 37 cents to $1.25 per month. Based on the last 10 years' experience, the average income has been approximately $20,000 per year, of which Strawbridge & Clothier has contributed 35 percent.

Benefits are paid for sickness at specified rates from $6 to $20 per week. A death-benefit settlement is made on the basis of $200 per member. The officers and board of directors are elected by the employees.

I think we were pioneers in this in the United States. We started way back in 1880, and we have paid since that time $612,000, out of receipts of $617,000, of which Strawbridge & Clothier contributed $237,000.

Senator VANDENBERG. Well, in that long period since 1880 you have had a fine actuarial experience with this plan. Have there been any times since 1880 when there was an extraordinary drag upon the funds and there had to be an extraordinary assessment, or anything of that sort?

Mr. TILY. The largest number of assessments we have had were 19, in 1900. That is the greatest number. Of course, it varied with the years, according to the number of people we had, but that is the greatest number of assessments. In that year the assessments were $4,921, and we paid $7,905. Strawbridge & Clothier's contribution was a little over $3,000. That compares with $4,200 the year before and $3,600 the year afterward. I think that answers your question, Senator.

We have a vacation fund and Christmas fund. Strawbridge & Clothier pays 6-percent interest on employees' deposits. We used to have a permanent savings fund. We could not stand the pressure there during the dull time, so we abolished the permanent savings fund. We raised the interest, though, from 5 to 6 percent, and it now closes out each year on that basis. We used to take their money back and keep it in a perpetual fund, but in the strenuous times we could not stand 6 percent on that permanent basis, and we just pay it on an annual basis.

We have a medical and health department. A group hospital plan is now being organized. We maintain an employee cafeteria, which serves a noon-time meal at cost. All employee purchases are discounted at the rate of 10 percent.

The number of employees over a 10-year period averages approximately 3,500 per year, with an annual pay roll of $4,900,000.

Now, Senators, may I give the personnel background of Strawbridge & Clothier? In 1868 two young Quakers, Isaac H. Clothier and Justus C. Strawbridge, founded that business, and from the outset they worked on the principle that good personnel management was a good paying proposition; it paid in satisfaction to those who were doing the work, that is, those who were employed; it paid dividends in goodwill inside, which meant goodwill outside. It was in this atmosphere that I grew up. I went there as a boy, and my parents chose it. I had to go to work very early, and I was fairly good material for the kind of training these people gave me in personnel work, because although my parents were pretty well fixed at one time—they were English people—my father failed, and I went to work at 14. Prior to that time I knew what it was to be hungry.

One Christmas my mother told us the night before that Santa Claus might not come—she had nothing to give us—and on Christmas morning our stockings were full, because some friend evidently knowing the circumstances had done something for us.

So my parents chose this for me, because they understood it was a fine Christian store and that their personnel relationships were the very finest. I mention this only as a background, because I am going to come to some conclusion and tell you, if I may, what I think about profit sharing.

I am somewhat of an artist and a musician, and I made an address to the Philadelphia Chamber of Commerce sometime ago, and also to the State college. I just give you this to show the background of the store and its effect on me. I told them that artists who work for money do not paint good pictures or write good compositions, because their heart is not in it, they are thinking of something else than the picture or the composition. I spoke of the joy that goes into creative work, and that a merchant can be an artist in that sense, that his whole soul is put into it, his job is looking beyond the immediate reward.

Joy need not be confined to humble workers and the more basic trades. It can, it must, and, I believe, it does animate countless numbers of executives who, in our complicated modern life, direct great numbers of workers. They develop these workers not alone for their own profit and the profit of the stockholders they represent but for the general good of humanity, the advancement of civilization, the raising of the standard of living, the reduction of hours of toil, and the general bettering of the conditions under which all perform their tasks.

I am a member of the Bell Telephone board of directors, the Pennsylvania Bell Telephone, a corporation with a soul if there ever was a corporation with a soul; and after I spoke of what they do for their 300,000 men and women, and the standards they set up in its choice, its training, its paying of this great army, that have made its personnel the marvel and envy of all idealistic industrialists, I went on to say:

"Is not this the practical fulfillment of an ideal, and are not all these laboratory workers, inventors, managers, and members of the rank and file who really think of the ultimate significance of their jobs, getting the joy, the thrill, the satisfaction that an artist gets in his art?

"The idealistic retail merchant, like the heads of other industries, gets a thrill out of his activities in contemplation of the ramifying good that follows his efforts to serve the three groups I have already mentioned—employees, customers, and society. Within the limits of common sense, of course, and if unhindered by unenlightened selfish competition, the nearer he approaches his ideals the larger his profits.

"If there be cynical doubts as to the sincerity of this statement, or friendly doubts as to its truth, many facts can be offered in its proof.

"It is the avowed purpose of good merchants, and one to which they religiously adhere, not only to pay people what they are worth but also to assume full responsibility for training them so that they may be worth more.

"This policy, successfully carried out, makes a best store for its personnel and its customers. It enhances the welfare of the employees by increasing the quantity and improving the quality of their work.

"If the store is in a community where its competitors have not the same ideal, or, having it, cannot achieve its fulfillment, then it inevitably becomes the best store. And best stores are the ones which attract the greatest number of customers.

"Better salespeople make each a larger volume of sales, and their nonselling colleagues perform more service tasks per capita, consequently they all earn more.

"Then the quality of selling and service being enhanced, the resulting increase in goodwill and character makes for larger sales, with a consequent increase in net profits.

"Service for the good of the community, accomplished by intelligent adherence to this policy, pays substantial dividends. No one can have greater reason to be civic-minded than a merchant—he prospers in direct ratio to the prosperity of his community.

"Philanthropy should be a constant urge. Nowhere more than in business is there a continuing opportunity to show not only a love of mankind, but an opportunity to get joy from the daily grind necessary to make a practical use of such love. A practical day by day philanthropy is better than a lifetime spent in the amassing of money."

Gentlemen, I made a few notes on the train coming down. Although I have had a sleepless night, I may be able to read this, and may be able to add to what I have said.

I have spoken of competition. The 10 percent chiselers which have been spoken of in some cases make it impossible for the right-thinking merchant, if he wants to keep his business going, to pay the wages that he wants to pay, and, on the other hand, we found that a sacrifice, a reasonable sacrifice which affects only the owners of the business and does not affect the permanency of the business, pays good dividends.

We feel in our business that we are not only responsible for the welfare of our own workers, but there are things we can do that benefit all workers. For instance, during the sweatshop period—thank God they are gone, we hope—it was well known in the store that no matter what competition was, any buyer who bought sweatshop merchandise could no longer work for us.

Now as to the personnel question, I have painted this background for you, to let you know it is sincere, and I hope you think it is sincere. I told you my own background and why I have a love for the fellow who works.

I do not believe that profit sharing is possible. If it were, these 90 percent of right-thinking people in the United States would have pretty generally adopted it. It has been tried in many places, and, so far as I know, may continue in some places. We have thought it over, schemed about it every way we could. We have always turned it down. We wanted it. We have told our people, in meetings we have had, that we wanted it, and if we ever see our way clear to put it in, if it was in their interests, we would put it in, but it is our belief that nothing so directly appeals to the employee as the fat pay envelope received weekly.

One other thing which very definitely hurts all business in its ability to pay employees is taxes. In ratio to income the largest percent is paid by small wage earners. In Philadelphia we have now an evidence of this, we have a sales tax there. The city is in financial straits, due to political mismanagement in this Republican government—and I am a Republican—but I call a spade a spade.

Senator VANDENBERG. You are talking about Pennsylvania.

Mr. TILY. I know. I am talking about Philadelphia at the moment.

Senator VANDENBERG. There are a lot of other spades in Pennsylvania, too, are there not?

Mr. TILY. Well, I want to keep away from it. Of course, you know a merchant is so vulnerable he cannot go into politics, but there are sinners in both parties.

Senator VANDENBERG. Oh, yes.

Mr. TILY. And there are also people who preach against sins in each party.

The sales tax, which is not only hurting business in Philadelphia—the local sales tax in Philadelphia only, and, of course, people go outside—it applies very much more harshly upon people with a small income than it does on people with a large income. The last was a graduated tax. They cannot graduate it.

The 1½ percent occupation tax, which is even worse on the poor people, and despite the fact that the sales tax hurts our business and that we would lose less if we pay this 1½ percent occupation tax, I express myself as being utterly and entirely opposed to it, because it is what it is.

One trouble is that workers do not understand that they pay the bulk of taxes, and so they return year after year legislators who increase the indirect taxation, which they do not recognize. Do you suppose, notwithstanding the fact that in my experience the average worker, or the workers generally are much more generous proportionately than is the average rich man; do you suppose that they would have, if they had known that they paid the soldiers' bonus, do you suppose that they would not have marched here in great droves against it?

The average man on the street does not understand economics. It is a most inexact science, because science can organize knowledge of things, but who can chart human nature?

There is no difficulty in understanding the crookedness of the legislator who professes to work for the poor man, trades on his ignorance, and sells him down the river for that modern mess of pottage—votes. Not one party alone is a sinner in this regard. The sincere legislator, fortunately, is not absent from our legislative halls, but very often the sincere legislator who is really working for the good of the poor man, because of specious arguments to the contrary, and because he is trading on the ignorance of the economic situation of this man, sells the poor man out.

Senator HERRING. You are still referring to Philadelphia, are you not, Mr. Tily?

Mr. TILY. No, sir; I am referring to the country generally. I wish, if I may, Senator, to tell you that even though I could afford to be a partisan, as a merchant one sometimes is vulnerable all over. Achilles was vulnerable in his heel only, but a merchant is vulnerable all over, and if he expresses his honest opinion, while he may please some people, he offends a great many others.

Senator HERRING. No one has accused you of lack of courage, though, have they?

Mr. TILY. Well, I have been accused of it by some people; yes. I have been asked why in the world I did not come out strongly for one side or the other. I have at times, and may again.

The poor man has, in the aggregate, a larger stake in business than business itself. Retailers should, of all classes, be civic-minded. They prosper as does their own community directly in that ratio. So it behooves us, I think, to consider very carefully what we are doing and why we are doing it, but, above all—and again there is no political significance, sir—who is doing it? I think the "who" is the answer. The "what" you are doing when you come to the economic situation is comparatively easy. The "why" is difficult, because economics is the most inexact science for the reasons I have named, because you cannot chart human nature. The honest people, honest legislators—and there are a great many in your party, Senator—a great many in your party——

Senator HERRING (interposing). Thank you.

Senator VANDENBERG. They have got a monopoly now.

Mr. TILY. There are a few at least in the Republican Party, Senator, at least a few, a half dozen, maybe, but there are some who are not only sincere but who know. Unfortunately there are many legislators who are perfectly sincere but they do not know, and that is true of both parties, and consequently they do wrong things. But the "who" of it is the extremely important thing for the poor man in this country to consider. Who is doing this work? Who is going to honestly, without regard to the votes that may be obtained, who is going to honestly inform the people of the real significance, of the utmost sincerity of the things that are avowedly done for him? If that "who" is thoroughly understood by the people, whether the man be a Democrat or a Republican, if he is right, if he is honest, he deserves and will get the votes of the people in America.

Senator VANDENBERG. The public has answered that on November 8, as I understand it.

Mr. TILY. You cannot trap me into it, as much as I would like to, but this is not the rostrum on which to do it.

That is my speech, gentlemen.

Senator HERRING. I am interested in what you said in reference to profit sharing. You say you are opposed to profit sharing because you think the employees prefer the fat pay envelope.

Mr. TILY. Yes.

Senator HERRING. We have had a number of executives here who are practicing profit sharing, and each and every one of them made the statement that no profit sharing was profit sharing if it affected the fat pay envelop; that there could be no profit sharing unless an adequate or better-than-adequate wage was first paid.

Mr. TILY. Well, unfortunately, in the retail business nobody has any monopoly, there is no patent right on anything, and you are up against your competition. If profit sharing is understood by the people—they do not understand it I think in many cases—and if profit sharing plus the fat pay envelope was possible in our business, in the face of competition, we would put it in, but we would kill the goose that laid the golden egg, not only for ourselves but for them, if we closed down.

Senator HERRING. I am glad to have your expression. I am just quoting what other men said they have found in their business.

Mr. TILY. I would be glad to read it, because if it is ever possible to put it in safely, we will put it in.

Senator HERRING. May I say that the service we expect to render is to put before you and other men throughout the United States a complete survey of what other men have tried, what they have failed and succeeded with.

Mr. TILY. We will do our utmost to study it in all sorts of ways.

Senator HERRING. When you are considering the constantly increasing taxes, we must consider who it is that asks for the constantly increasing services which make necessary the constantly increasing taxes? We can give up these things, our old-age pensions, the social security, and a lot of these things, and not have the taxes, but who is insisting upon those?

Mr. TILY. Well, I will leave that to you. On the other hand, might I say in connection with Philadelphia again, it is not a good Republican city, it is a bad Republican city. There are some good ones, some good Democratic ones, too. Senator Vandenberg may not agree with that. I think there are some, Senator.

Senator VANDENBERG. I agree with that.

Mr. TILY. Just as there are good men in both parties. To whatever extent this is true—and it is true—there was a classic in one of the Philadelphia papers some time ago in connection with this situation there. Some fellow who worked for a great many years in the pay of the Government and pay of the city finally retired, and he said he could not collect enough in all the years that he was there to pay his salary for 1 year. Now, to whatever extent that is true—and I think it is—I think positions are made solely for political reasons. I think the cost of government in this country today is killing—it is hurting business. I am for reforms in business, but to play up reform as a fetish, especially if it is insincerely played up, it is doing only one thing—it is stopping the one thing that you are trying to accomplish; that is, the stability of employment. The employee, the laboring man, has a larger stake in business than business itself.

I would like to offer this telegram I just received for your record.

Senator HERRING. It may be printed in the record.

(The telegram referred to is as follows:)

HERBERT J. TILY,

Care Donald Despain, Director of Survey, United States Senate Subcommittee on Finance, United States Senate Building:

Division of gross earnings between taxes and net profit, 1928, 16 percent for taxes, and 1937, 47 percent in our business for taxes. Increase in total amount taxes, 152 percent in '37 over '28. Cost of living in Philadelphia, according to Government figures, all items, June 1930, 97.6. June 1938, 83.1. Our per capita nonexecutive wages, June 1930, 22.27; June 1938, $22.

Senator HERRING. Thank you very much, Mr. Tily.

Mr. McKenna is accompanied by Mr. Underwood, the secretary of the Vanadium-Alloys Steel Co.

STATEMENT OF R. C. McKENNA, PRESIDENT, VANADIUM-ALLOYS STEEL CO., LATROBE, PA.

Senator HERRING. Mr. McKenna, you are president of the Vanadium-Alloys Steel Co., of Latrobe, Pa.?

Mr. McKENNA. I am.

Senator HERRING. Mr. McKenna, we have your schedule of information here which shows you do not have any labor trouble, you do have a very interesting profit-sharing plan and that it has had a very desirable effect upon your business, and we would appreciate it if you will briefly outline your plan, its inception, what you have accomplished with it, and so forth.

Mr. McKENNA. The Vanadium-Alloys Steel Co. was founded in 1910. I came to the company as president in June 1915. Our profit-sharing plan was adopted in 1920, although it did not become effective until 1923, on account of the depression in business in 1921.

Stated simply, the plan is: At the close of each fiscal year a calculation is made to determine the working capital to be used as a basis for bonus calculation. This base is the capital stock and surplus less the cost of securities owned.

There is set aside from earnings prior to any bonus calculation, 7 percent of the working capital thus arrived at, and the amount of dividends and interest received on investments; and a reserve for Federal and State taxes.

The net profit for the year is reduced by a total of said reservations, and 25 percent of the remainder is set aside as a bonus to employees.

The distribution of bonus calculated is arrived at as follows:

The amount of each employee's participation in the bonus is figured on three factors: Responsibility of position, value of service, and length of service.

Calculation of each employee's participation in the bonus is arrived at by multiplying his annual salary or total wage, his value of service, by a factor representing rating as to responsibility of position, by a factor attributed to length of service.

Each employee who has been in the employ of the company for not less than 6 months to 1 year receives a rating of 10; 2 years, a rating of 12; up to a maximum rating of 20 for those who have been in the service of the company 5 years or longer.

The value of a unit is arrived at by dividing the total bonus by the total number of units. Upon the assumption of a bonus of $200,000, and total units for all employees of 30,000,000, then the value of each bonus unit would be two-thirds of a cent.

An individual employee's participation in the bonus would be his annual salary or wage, multiplied by his rating for responsibility of position and by his rating for length of service, by the value of the unit as determined.

I will say that this plan has been in effect since 1920; it has not been changed. It positively has been understood by our employees, and it has been very helpful to the company. Our labor turn-over is practically nil.

In the financial statement which we issued on June 30, 1937, I made the statement that the men who participated in the bonus in the operating department—that is, every man who had been in the employ of the company 6 months or longer—that there were only six men that did not participate in the bonus of 1937. In the period of 7 years we only had six men that left the company, and two of those had died.

Senator VANDENBERG. I notice from your answer to the questionnaire that it is optional with the employee whether to accept cash or certificates of investment. Will you explain what you mean by that?

Mr. McKENNA. In 1920, when this plan was adopted, we did not know whether a condition may arise where the company may be making money and at the same time expanding, and whether we would be able to pay the bonus in cash, and also we wanted to have an incentive for saving on the part of our employees. In the early years of the bonus plan a great percentage of the bonus was accepted in certificates of investment, which paid 4 percent interest if the employee was not in the employ of the company, and a premium of 3 percent if he continued in the employ of the company, or the certificates of investment paid 7 percent interest. We always gave the employee the option to accept in cash or to accept in certificates of investment.

Senator VANDENBERG. Are there still certificates of investment out?

Mr. McKENNA. Yes; there are some out. There were some issued this year, but not very many.

Mr. UNDERWOOD. About $80,000 outstanding.

Mr. McKENNA. About $80,000 outstanding now.

Senator VANDENBERG. Are you still paying 7 percent on these certificates?

Mr. McKENNA. No; it is 6 percent now. We pay 3 percent plus 3 percent if they are employed in the company. The reason that we discontinued the certificates of investment idea was there was some opposition to the company paying 7 percent interest on the money when we did not need it, and also in the taxes of the State of Pennsylvania they interpreted those certificates of investment the same as money borrowed from a bank, and it was subject to a 4-mill tax. That was from 1920 practically up to the present time.

Since the year 1920 our company has paid out in profit sharing an amount equalt to 75 percent of our capital stock. We have paid bonuses, from the first bonus in 1923, in 13 of the 18 years. The bonus and profit-sharing plan was also put into effect at a time when this country had very little labor agitation.

Senator HERRING. There is no question of the basic wage being equal to the prevailing wage, is there?

Mr. McKENNA. We have always paid the basic wage of the steel industry, and our rates for the other men are above that for the industry as a whole.

Senator HERRING. They have what has been referred to us the fat pay envelope each week before you go to the profit sharing?

Mr. McKENNA. Well, we have some employees who will testify to that.

Senator HERRING. That is what I understand. They are to appear today. How many employees do you have, Mr. McKenna?

Mr. McKENNA. Approximately 500. I think the exact figure is 480.

Senator HERRING. Four hundred and eighty in the plant?

Mr. McKENNA. Yes.

Senator HERRING. You have had no labor trouble?

Mr. McKENNA. No; we never had any labor trouble.

Senator HERRING. Are your men organized?

Mr. McKENNA. They are not organized.

Senator HERRING. As I understand it, you feel that this policy of yours gives you the selection of the best men in the community?

Mr. McKENNA. It does.

Senator HERRING. Or in the business?

Mr. McKENNA. It does.

Senator HERRING. You feel it pays from the business standpoint?

Mr. McKENNA. It pays from the business standpoint, and it enables us to run our company without nearly as much supervision as would be necessary if we did not have such a plan.

Senator HERRING. Is there any negotiation with the employees in arriving at this dividend bonus?

Mr. McKENNA. No.

Senator HERRING. Or profit sharing?

Mr. McKENNA. No. It is set forth right in the 25 percent, and how it is figured.

Senator HERRING. But it is not arrived at by discussion with the employees?

Mr. McKENNA. No. It is absolutely secret. No man except myself and Mr. Underwood, no one knows what anyone else gets, because we rate this responsibility of position, we pay a skilled man a higher rate on his responsibility rating than we would an unskilled man.

Senator HERRING. And in spite of that there is no suspicion on the part of any of the employees that they are not being fairly treated?

Mr. McKENNA. Absolutely. That has worked to perfection. We have no evidence, except in one case, where any information as to the amount of bonus has been given out up to this last summer.

Senator HERRING. I make that comment because a number of employers and executives have stated here that they believe the success of a profit-sharing plan depends upon full information being given to the employees frankly, so that they may know they are getting a fair division.

Mr. McKENNA. I believe our employees thoroughly understand our plan, and I believe they approve it.

Senator HERRING. They know of your net profits, of course?

Mr. McKENNA. It is published.

Senator HERRING. They know that?

Mr. McKENNA. Yes.

Senator HERRING. Do they know the total amount that is given to the employees as compared with the dividends given to the stockholders?

Mr. McKENNA. Well, there are a great many of our employees that are stockholders and they would get our statement.

Senator HERRING. I wonder if you have any idea of the relation between the amount annually distributed to the employees as profit sharing and the amount distributed as dividends?

Mr. UNDERWOOD. We can supplement that report and mail it in.

Senator HERRING. In 1937 what was the bonus?

Mr. McKENNA. The bonus was $247,000.

Mr. UNDERWOOD. We distributed $960,000 in dividends and the bonus was $247,000.

Senator HERRING. You distributed $247,000 in bonus and $960,000 in dividends?

Mr. McKENNA. Yes. We paid out every cent we made in dividends in those years, on account of the undistributed-profits tax.

Senator HERRING. That looks like a fair division.

Senator VANDENBERG. It is a ratio of about 4 to 1.

Mr. McKENNA. In 1929 the proportion paid as bonus would have been higher, on profit sharing.

Senator HERRING. In 1929 it would have been higher?

Mr. McKENNA. Yes. You see there is a 7-percent reservation, so the company would earn 7 percent before we would have any profit sharing.

Senator HERRING. Then your profit-sharing plan was really giving more to the employees than the former bonus plan?

Mr. McKENNA. What is that?

Senator HERRING. Your profit-sharing plan was really giving more to the employees than the former plan, when you did away with it?

Mr. McKENNA. We never did away with any plan. The plan was adopted in 1920 and it has continued exactly as it was started in 1920 without any change.

Senator HERRING. I understood you were calling in the 7-percent certificates of investment.

Mr. McKENNA. That is optional with the men. They can still accept the certificates of investment, if they so wish, but the company has always been ready to retire those at any time. We found that the men used those certificates of investment to buy things that they wanted, and they generally were desirable things. It has been stated—I have not checked it, but probably close to 90 percent of our men own their own homes, and many of the men took those certificates of investment for the purpose of buying the home, and for whatever purpose they wanted them. We never refused to give them cash for the certificates.

Mr. UNDERWOOD. May I say on the semiannual interest period we always offered to redeem any outstanding certificates of investment.

Mr. McKENNA. You see, the pressure on the company was rather to retire those certificates of investment, rather than have them outstanding. Because, first, the interest was 7 percent when we could have borrowed money at much less than that, and, second, before the manufacturers' exemption on the capital stock tax in Pennsylvania we felt it was very unfair to consider that as borrowed money, when we had Government bonds and other bonds of a greater amount, and it was evident we were not borrowing that money because we needed it—we were doing it for the benefit of the employees, but they never would recognize that.

That is one of the taxes that we were very much disappointed in.

Senator HERRING. In spite of that disadvantage to you, you still permitted them to invest in it?

Mr. McKENNA. Yes.

Senator VANDENBERG. In 1933 you paid no dividends to stockholders? Were there any bonuses in 1933?

Mr. McKENNA. In 1931, 1932, and 1933 there were no bonuses, and our employees did not expect them, because they knew the conditions of the plant almost as well as our accountants did.

Senator HERRING. You had the profit-sharing plan at that time, did you not?

Mr. McKENNA. Oh, absolutely.

Senator HERRING. Do you think the profit-sharing plan had something to do with your being able to pay the profit sharing to the employees after that?

Mr. McKENNA. I have no doubt that our profit-sharing plan has increased the efficiency of operations of our plant sufficient to justify it to our stockholders. Our stockholders, directors, and management are all of that opinion. Plans identical, or not identical but modeled after this plan, have been adopted in two other industries in our own town, Latrobe, and they work successfully, and they have been adopted by a plant in Pittsburgh, a larger plant, and have worked successfully there.

Senator HERRING. I think you have made a real contribution. We appreciate your coming, Mr. McKenna. I understand two of your employees are in the room, and they are going to testify for themselves.

Mr. McKENNA. Yes.

Mr. UNDERWOOD. I would like, just for your own information, to give you some indication of how it has worked out. This is a secret bonus.

Senator HERRING. This is Mr. Underwood, the secretary of the company?

Mr. UNDERWOOD. Yes.

Senator HERRING. We would be glad to hear from you, Mr. Underwood.

Mr. UNDERWOOD. In 1929, just as an illustration—you asked us whether or not we paid the wages in addition to the bonus. This is not an outstanding example. It comes to mind simply on account of my familiarity with the old gentleman. He was 80 years old. He was a janitor in our building, and with his bonus he made for the entire calendar year of 1929 something over $179 a month. Laboring men, hammer men, men working on labor rates range from $160 to $170 up to $275 and the more skilled men on up from that.

We have the record of having paid a blacksmith as a bonus in 1 year over $1,100.

Senator HERRING. $1,100 bonus. How much did he get in wages that year?

Mr. UNDERWOOD. I do not know what the wages were.

Mr. McKENNA. About three times that much.

Mr. UNDERWOOD. Approximately that.

Senator HERRING. He had a fat envelope, then, in wages?

Mr. UNDERWOOD. Yes; about $3,700, I think, in addition to that.

Senator VANDENBERG. Do you need any more blacksmiths?

Mr. UNDERWOOD. That is not an isolated example.

Senator HERRING. Go ahead.

Mr. UNDERWOOD. Here is a man on the milling crew, $1,019 bonus. The master mechanic drew over $2,000 bonus for that year. Here is a laborer, $235.44. These are some of the smaller bonuses. Here is a bonus of $64. That meant probably that the man only worked 6 months of that year. Men in the rolling mills drew from $180 up to, some of them, over $1,100.

In addition to that, I just want to tell you about the white-collar people in our office. We have 15 girls, and before the last reduction, effective April 1, the average of those 15 girls was $152 a month. That 10-percent reduction affected the girls getting $100 a month or less. Now, with their bonus for 1937, they averaged $182 a month, or a little over that.

I am not going to make any oration here, but this was written by Roy McKenna at the inception of this thing. He says:

The prosperity of any company is due to a combination of reasons. Prosperity is not always due to good management; it is really more often due to trade conditions of a particular industry being favorable, and in these periods of prosperity even companies poorly managed make large profits. The employees have as much right to share exceptional prosperity due to trade conditions as the stockholders.

That was a little over 18 years ago that he wrote that.

Paying the basic wage and fair wages, and dividing such profit with your employees, I am unable to see how any objection to that can be based on anything other than absolute selfishness of one kind or another.

Senator HERRING. Your men have reasonable permanency throughout the year, do they?

Mr. UNDERWOOD. Just as much as we are able to give them.

Senator HERRING. More than 6 months?

Mr. UNDERWOOD. Naturally, when conditions arise that create more work, we must enlarge the number of our employees. That is the unfortunate part of it and the reason that we cannot maintain it definitely at the standard rate. We could not possibly employ all of those employees today.

Senator HERRING. I understand they have a fairly steady annual working period.

Mr. MCKENNA. We ran steady and gave full employment to our men for a period. After 1922 to 1929 I do not believe we ever had any man miss a day's work on account of the company not having business. Of course, in 1931 and 1932, and particularly this last year, our operating conditions have been bad.

Senator HERRING. I think you have made a very fine statement. We have two employees of your company here, and I think we will recess until 1:30, so you may have a chance to go home before they testify.

Mr. UNDERWOOD. I was going to suggest that myself.

Senator HERRING. We will recess until 1:30.

(Whereupon, at 12 o'clock, a recess was taken until 1:30 p. m. of the same day.)

AFTERNOON SESSION

(The hearing was resumed at 1:30 p. m. pursuant to taking of the recess.)

Senator HERRING. Mr. Martin A. Lawlor, hammerman from the Vanadium-Alloys Steel Co. of Latrobe, Pa.

STATEMENT OF MARTIN A. LAWLOR, LATROBE, PA.

Senator HERRING. You are employed by the Vanadium-Alloys Steel Co. of Latrobe, Pa.?

Mr. LAWLOR. Yes, sir.

Senator HERRING. How long have you been with that company?

Mr. LAWLOR. I have been in the service of that company 23 years.

Senator HERRING. Mr. Lawlor and Mr. Hummer came here entirely voluntarily to appear before the committee and speak from the employees' standpoint. I will be glad to hear from you, Mr. Lawlor.

Mr. LAWLOR. Senators, you have heard the report of Mr. Roy McKenna and Mr. Underwood beforehand, which I am very truthful in saying that every word of those two gentlemen is absolutely the truth.

I will give you outline of the profit-sharing and how it has benefited the employee how he has participated in it.

In 1920, when Mr. Roy McKenna put this profit-sharing plan into effect, he sent each and every individual employee of the company a typewritten letter, and he explained and outlined how it was going to be operated. For the first 3 years we were in bad luck, but in 1923 we were paid. Each and every individual who received this bonus—my next door partner to me does not know what I draw and he does know that I don't know what he draws. That is in absolute confidence among ourselves, and furthermore our own wives are not even allowed to know. And we don't tell them.

Gentlemen, to make it brief for you, I have been with firm for 23 years and I hope to remain the next 23 years, as long as I live, with them. It is the greatest company in the United States. We are only a small institution, but I think we can set an example to the world, that we have challenged the whole State of Pennsylvania or the outside to compare with this system that we have.

Our system of bonus does not mean a wage. Our wages are separate from our bonus, and as we go along in our plant, we know nobody as a laborer. Our plant is operated and supposed to be known as all skilled labor and mechanics, and we don't like to call a man a laborer, because that kind of belittles a man. No man likes to be called a laborer. That is our attitude toward him.

In our 27 or 28 years, I think it is today, we have never had one ounce of trouble in that company. And, gentlemen, there is a reason for that. That comes from the standpoint of the leadership of the men whom you are working for. It is Roy McKenna. He is the greatest man that I know in the United States today at the head of an industry. He thinks first of his employees. If he makes a dollar, his employees are going to benefit by it, and as I am sitting right here today, or yesterday, a bonus was paid by the Vanadium-Alloys Steel Co. Can you understand that, and with the bad year that we had? The first 5 months we made money, and the last 7 months we lost money, but Mr. Underwood mailed a bonus check out to 467 employees yesterday, which was a bonus paid, which is in no way to compare it with our yearly salary. As Mr. Underwood outlined to you, our blacksmith received $1,100 bonus in 1929, which was absolutely the truth. He did.

Now, I know this bonus situation, what it has done for me individually. I bought my own home out of my bonus money. I never bought an automobile with money that I actually had to go out and work for, because it was bought out of my profit-sharing plan. If I worked for anybody else, I could not have those things.

That is why I am down here today telling the truth of what Mr. McKenna's plan is outlined by. I want you to know that our men have spoken about the bonus that they have coming to them. They were worried that they were not going to get it. They did not mean any harm by that, but they heard that there was going to be a little bonus, and they had been waiting so long and they kind of got worried, but last night they were taken off their feet, and they were presented with their checks.

Whether a bonus would be paid in the Vanadium-Alloys Steel Co. or not, there would never be any discontent among our men. We have the greatest bunch of men in Pennsylvania in our plants. We are not organized. We are not against organization, but we have something better than organization. There is no organization in the United States that can compare with this system which Mr. Roy McKenna has given to his employees. This man did not have to give us that. He just voluntarily, 20 years ago, made that up himself and it has worked out and worked faithfully and truthfully, and, as I said, the next man to me does not know what I am drawing, or I don't know what he is drawing. If he draws $1,000, that is his business, and if I draw $1,500, that is my business. Nobody knows.

Furthermore, we don't like anybody to go out and broadcast what they are making, because we don't think that is fair. If a man makes $15 or $20 a day, we believe that is his business, and it will create that kind of confidence among the men. That is why we have such great cooperation and harmony among our employees with the man who owns the plant. Each and every individual in our plant today—I will say 90 percent of our employees—are all property owners, and they look forward to this little bonus, because it has pulled many a man out of a hole; it has built many a man his home and paid his taxes and paid a lot of doctor bills which otherwise that poor man would not have been able to do.

In the last 10 years in our company it is almost impossible to get a job in our plant. We have lost 5 men in 10 years. Four of them retired and one of them died. That is the way we lost those men.

So, gentlemen, I have given you the history of what I think, which is absolutely the truth, of our profit-sharing plan, and every word that I have told you in that respect is absolutely the honest truth.

Senator HERRING. You are a hammerman. I don't know much about the steel industry. What does a hammerman do?

Mr. LAWLOR. That is one of the hardest jobs in the steel industry. That man faces nothing but hot heat all day long, and it is nothing but hard work. To be a good hammerman, you are supposed to have strong arms and a strong back and be weak in the head. You have got to have lots of muscle.

Senator HERRING. And a good voice?

Mr. LAWLOR. And a good voice.

Senator HERRING. That is most interesting. We are very glad to have your contribution.

Mr. Hummer is the next witness. Thank you, Mr. Lawlor.

STATEMENT OF HARRY R. HUMMER, LATROBE, PA.

Senator HERRING. You have had 26 years of service with the Vanadium-Alloys Steel Co., I understand, Mr. Hummer. You also come here voluntarily?

Mr. HUMMER. Yes, sir. Do you want me to give a brief outline?

Senator HERRING. What do you think of this policy?

Mr. HUMMER. The bonus system, or profit sharing, as we like to call it better, is something that was put into effect back in 1921, and all down through the years, as has already been testified—the first 2 years were bad years, and there were no bonuses—but since that time there have been paid 13 bonuses, and we have looked forward to it and expected its coming each year, and, as was testified by Mr. McKenna, we all know practically what the bonus or the profit sharing is going to be, because the amount is published in the financial statement. If, for instance, the total amount is $25,000 or $30,000 short this year from what it was last year, we can very easily with a pencil and paper figure out what we are going to get, what percentage of the previous year. It is altogether regulated on the profits of the company; 25 percent of the net profits are distributed among the workingmen.

Sometimes in campaign affairs or things of that kind—Mr. McKenna happened to be a candidate for Congress this year—they tried to create the impression that it was for only the big shots of the company. That is not true. The smallest-paid employee participates in the profit-sharing plan, and the actual fact in the matter is that 77 men employed in the company received more of the profits than the directors. When I say the directors I mean the unemployed directors. Some of our directors are employed and get a salary, but 77 men in the plant received better profit sharing than the directors themselves did, and so it is distributed rather equitably all the way around.

To me and to all of the rest of us I think we have observed this—that the profit-sharing system sort of puts a position of trust on us; in other words, we are looking out for the company's interest, naturally, and we try to do our best work. We have never in any way been coerced; it is not a speed-up proposition; in fact you cannot speed up a tool-steel business, as it is quality rather than quantity. There is no coercion or any speeding-up process at all in order that this profit sharing or bonus might be larger. For that reason there is practically very little supervision over the men. By that I mean that each man feels that he is or has his own particular work to do, and he takes the responsibility upon himself, and the superintendent or the works manager possibly does not speak to us so far as work is concerned more than half a dozen times in a year. I can truthfully say that for myself. I have my work to do and I know what it is and I go about doing it.

Mr. Underwood did disclose about some of the wages; that is, the profit sharing in proportion to wages. What Mr. Lawlor said is so, that we do not disclose to each other how much we get. The men themselves feel very kindly about that. For instance, perhaps the electrician draws the same wages or within a few dollars a month of what I draw, and the profit sharing would come along, and he would get $15 or $20 more than I, or he might get $15 or $20 less than I do. It might, we think, cause trouble if we actually know what each fellow got. So that has never been brought up or is never, I believe, really thought of, and we try to keep that matter quiet so far as we can. Personally, I have drawn as much as 37 percent of my wages in profit sharing in a given year. That means in plain English that I got 16 months' pay for working 12 months. That is not telling very many details out of school, but if you know what you get in the percentage, you know very well that it would be added on to your salary. That is what it amounts to, that much, that I have actually gotten as much as 16 months' pay for working 12 months.

The matter of the home owners that has been mentioned is true. Most of the men of the plant own their own homes.

As to organization, the matter of organization, the C. I. O. or the American Federation of Labor—during the troubles when they were trying to organize other places, they never even approached us. They never even interviewed any of our men; they never came near the plant. They made no attempt to organize us. They knew very well that there was no use.

Another thing—our plant is not enclosed; our watchman does not carry any revolver or any gun. We have one watchman, and about all that he does is to go around and punch the time clock as a safety against fire or something of that kind.

We have never had anything in the way of labor trouble over all of these years, and it has always been from the beginning that I could go down and walk into Mr. McKenna's office; or I could walk into Mr. Bowman's office, the works manager; or I could go down and say to Mr. Underwood, "I am hard up, and I need $100 or so to run me over for 3 or 4 months," and it was handed out to you and very few questions asked about it.

In addition to our profit-sharing plan, we have a bathhouse, a recreation room, which cost in the neighborhood of $30,000. Every man has a locker. We can go to work with our good clothes on, hang our street clothes in the locker, and put on our working clothes. We have a steam-heated building, a recreation room, a reading room, and we have shower baths—probably upward of 25 shower baths. That is our recreation room at the plant.

Then in the summer—in fact, we have it all the year round, but principally used in the summer—we have what we call a recreation farm. That is for the use of the employees without any charge. A little group of men, half a dozen or so, can get together and they can have the use of that room for the evening for their own crowd, provided they ask for it ahead of time. Otherwise, it is open to anybody in the employ of the company to go in at anytime, but we make that as one of the features of the company.

There were 461 that participated in the bonus this year.

I think that has covered it fairly well. I would be glad to try to answer any questions that you might ask me.

Senator HERRING. Perhaps I should have asked this of Mr. McKenna, but is your production limited to vanadium alloy steel?

Mr. HUMMER. Sometimes that is confusing. It is not the vanadium ore itself. That is simply the name of the steel company. The company manufactures tool steel and vanadium is one of the ores that enters into it.

Senator HERRING. You use vanadium, do you not?

Mr. HUMMER. Yes; but there are other things used quite largely, such as cobalt and tungsten ore and things of that kind.

Senator HERRING. There is no monopoly upon the supply of vanadium that your company holds over any other company?

Mr. HUMMER. No; that vanadium really hardly means anything to us. It has nothing to do with the supply of vanadium or anything like that.

Senator HERRING. It does not?

Mr. HUMMER. It is just merely a trade name, because one of the component parts of tool steel happens to be vanadium, but it is not the outstanding part. Tungsten and cobalt and some others are very important, too.

Senator HERRING. You don't know of any reason, then, why any other plant in the same line of business could not operate with the same kind of policy? In other words, your company has no advantage in that way over what any other company might have?

Mr. HUMMER. Absolutely not. There is no monopoly in any sense or in any way. We have another company in the same town, the Latrobe Electric Steel Co., that approximately does the same kind of work and makes the same kind of steel—approximately the same—tool steel. And they are continually having labor trouble. They do not have a profit-sharing system. During the strike or during the—spasm of sit-down strikes, they came in and organized the other company in our town, and they did not do any good by organizing them and only made a lot of confusion, and as I said, they never even bothered us. They knew there was no use.

I want to create this impression also, that Mr. McKenna and the other heads of the works told us that at any time that if we wanted an organization, it was all right to go ahead. He told me that personally that if we wanted to organize, it was all right, and I even asked him if he wanted us to organize, and he said "That is up to you; if you want to do it, all right."

At any time that any person has a grievance he can walk into the office and state his grievance and be assured of a good hearing.

I think another thing that I might mention that reflects the character of the men in the plant—we take up a community-chest fund in our town every year, and the Vanadium-Alloys Co. is outstanding in the amount of money they contribute to it. We feel that the men have been educated up to a system of sharing with others, simply because Mr. McKenna has shared with us, and it has always reflected it in these other things. Even a hard year like this when wages were somewhat reduced, the cards in the plant averaged about $2.75 apiece to the community chest. The highest contributed by a workingman, not a foreman or a boss, was $18, and from that down to $1, but the average was $2.75 per card. I think that speaks for contented employees.

Senator HERRING. You do not think it requires any great knowledge of economics to show that you are satisfied and contented with this system?

Mr. HUMMER. No; it is not necessary for us to understand that, because it shows of its own accord.

I am just going to just step over the line and tell you that in the 13 years I drew in bonus $7,559.43. That is an average of $584 a year. I would just as soon that not be published in the papers.

Senator HERRING. How much experience do you have to have to be a good roll turner? I understand that is your assignment or your work.

Mr. HUMMER. My work differs a little from Mr. Lawlor. He says he has to have a strong back and a weak head. Mine is a little bit the other way. My work is not heavy or laborious. A roll turner—I told a person one time that I was a roll turner, and he asked me what bakeshop I worked in. So if any of you have been in a rolling mill, you necessarily know that there has to be rolls or shapes for the steel to pass backward and forward through in order to shape the steel. That is what I do. Take these rolls and turn grooves in them so that the steel can be reduced from a 4-inch square down to a 1-inch round or any particular size. We roll down as small as a quarter of an inch, and that has to be within three one-thousandths of an inch perfect in a ¾-inch round.

Senator HERRING. This is most interesting. We appreciate very much your coming here and telling us about it.

Mr. HUMMER. I would like to emphasize that too—I am a lathe man. Roll turning is done on a lathe, something similar to machinist work. I have two bum fingers that have been bunged up working at it.

We have been so fortunate, I think, compared to a lot of other workingmen that we are just bubbling over with enthusiasm because we feel we have been treated white.

Senator VANDENBERG. That is a very good contribution and a very good tribute to this employer.

Senator HERRING. We appreciate very much you and Mr. Lawlor coming down.

Mr. HUMMER. Thank you.

Senator HERRING. The next witness is Leo M. Cherne.

STATEMENT OF LEO M. CHERNE, EXECUTIVE SECRETARY, TAX RESEARCH INSTITUTE, NEW YORK

Senator HERRING. Mr. Cherne is executive secretary of the Tax Research Institute of New York City. Mr. Cherne has voluntarily conducted a survey of his own as to sentiment in connection with this survey which is being made here, particularly as to incentive taxation, and he will give us a review of that, will you not, Mr. Cherne? Is that your purpose?

Mr. CHERNE. That is correct, Senator. I might amplify on your last comment and state that this survey conducted by the Tax Research Institute, relies entirely upon independent figures and analyses utilized by ourselves, and in no way required or received any recourse to your own records or the records of this committee.

Senator HERRING. Will you just briefly state what your organization is, what it consists of, and what your purpose is?

Mr. CHERNE. Yes, sir. Our organization was organized under the laws of the State of New York as a corporation approximately 4 years ago, for the purpose primarily of pooling contributions of experience and adjustments of businessmen, professional men, labor-union executives, social workers, and members of the various governmental agencies throughout the country. It was our belief at the time, and our belief has been justified by experience, that the new legislation within the last 6 years has created problems with which the average businessman and even the average professional man is not competent to cope without guidance that is very frequently not forthcoming from any source. It was our object therefore to form an organization without economic, political, or social bias for the purpose of disseminating every available bit of information on legislation and governmental activities. To that end, we have cooperated with every governmental agency, Federal and State, that has requested our cooperation. We in turn expect cooperation from them in the dissemination of the information that is the backbone of governmental activity.

In the course of this survey up to last night—our tabulation was completed at 1:30 this morning, and at that time we prepared this analysis. Up to that time, 3,200 businessmen and professional men largely, were represented in the final tabulations. Of those 3,200 executives and professional men, they represent companies which employ approximately 600,000 people.

I may mention at this point that in every answer to our questionnaire, which I ask to be inserted in the record in connection with my testimony (the questionnaire will be found at the end of Mr. Cherne's testimony), we have broken the answer down to determine how many employees are either represented or affected by the answer to that question. On the basis of the tabulation on the first 3,200 questionnaires, we have been able to find what can be accurately recorded as the opinion or the desires or the action of employers throughout the country employing approximately 6,000,000 employees, all members of the Tax Research Institute. We have found consistently in all of the surveys conducted by the institute that from the time that 2,000 questionnaires were tabulated to the time that 10,000 or any number are tabulated, there is a deviation of less than 1 percent, so that we can accurately regard this survey as representing the opinion of this group, this group of employers and professional men, labor unions, trade associations, and others, who employ approximately, on the basis of the projection we made of this questionnaire, 6,000,000 people in the United States.

Senator VANDENBERG. Do you think this would be a little more reliable index to industrial thought than the resolution adopted by the executive committee of the National Association of Manufacturers?

Mr. CHERNE. Senator Vandenberg, I might say that you put me on the spot with that question, but I will try and answer it indirectly. We have found in our contact with the business executives in the course of this 6 weeks' survey, that asking this question: "Are you in favor of incentive taxation?" the larger the income of the corporation which the executive represented, the more quickly would the answer be forthcoming, "I am not in favor of incentive taxation." But we then asked these executives, "We should like your opinion of the following four legislative proposals," including among them the repeal, for instance, of the excess-profits tax in order that business might be free of the cloud of a possible 12-percent penalty for business that is too good and unanticipated at the time the original value was declared. With equal speed in each of those cases, the executive replied that he is not only in favor of it, but he has been advocating it for years. To which our answer immediately was, "Well, that is incentive taxation."

We have found that of the 14 legislative proposals or suggestions that the institute has formulated, as close to a unanimous opinion as is capable of being found in the business world, demonstrated to us support for those legislative proposals. I may be putting the cart before the horse in that case. The institute is not primarily interested in preparing legislative proposals. It is not interested in legislation of any kind or the fostering of legislation. It is interested in the securing of opinions of businessmen, and when that opinion is made vocal, the opinion of our membership, to prepare alternative methods of accomplishing those things and presenting them to the proper governmental bodies for whatever action they care to take on them.

With that point of view in mind, we have prepared legislative suggestions, alternatives, and some even contradictory, for any action that this committee or any consideration that the subcommittee might care to give to them.

Senator VANDENBERG. The answer to my question is "yes"?

Mr. CHERNE. That could be the answer to your question.

Senator VANDENBERG. All right.

Mr. CHERNE. Now, may I stress just one more point before I go into the survey itself?

The institute has no political or economic opinion. I mention that briefly. The best testimony to that fact is the fact that among our membership we have, as I have stated in our report, a large number of Wall Street bankers and the most powerful labor unions, the eastern manufacturers, western wholesalers and retailers, Democratic newspapers and Republican newspapers, corporate executives, and social workers.

Senator VANDENBERG. You are running a coalition.

Mr. CHERNE. Ours is perhaps the most effective caucus in the country, and I might add that more than 200 members of the United States Congress are receiving the biweekly reports of the institute.

May I take the liberty of prefacing the survey conducted by the Tax Research Institute of America with several introductory comments which will clarify the institute's position in relation to the information about to be presented?

The institute's purpose in cooperating with this committee, as with every other committee or agency of the Federal and State Governments which has requested its assistance, is in consonance with the purposes for which the institute was founded. The institute is a corporation, organized under the laws of the State of New York. Among its purposes, as quoted from its corporate charter, are:

> To disseminate information and statistics with respect to the tax and revenue laws * * * to procure uniformity and certainty in the administration and application, and to advocate coordination of the tax laws and revenue acts of the States and of the United States * * * to facilitate the pooling and open discussion and promulgation of the most economical and effective methods of tax control. * * *

Thus, essentially, the purpose of the institute is to bring about a better understanding by businessmen of Government activities and by the Government of businessmen and their activities.

The annual survey conducted by the institute among its members has enabled the pooling of the best individual business and professional brains, and the mutual enjoyment thereby of the pooled information of thousands of business and professional organizations.

The institute, in its dissemination of information both to subscribers and members, has no opinion, is not guided by any political, economic, or legislative conclusion. Its sole function is to analyze existing and prospective legislation and governmental developments.

In the course of the analyses, the more than 40 tax and legislative experts in the institute's research division are directed to reach a conclusion as to what a proposal means, what its effect will be, and what the institute's membership should do about it.

The nonpartisan and unbiased character of the analysis is best guaranteed by the fact that the membership includes the greater number of Wall Street bankers, as well as the most powerful labor unions, thousands of western industrial organizations and thousands of eastern business firms, corporate executives, social workers, Democratic newspapers, Republican newspapers, more than 200 members of the United States Congress and officials in almost every State government.

To summarize the survey itself:

First. At the request of your committee, the questionnaires were confined to the following broad national problems: What does the taxpayer think about today's tax law? What are the effects of the 1938 Revenue Act upon business, professional activity, or all other activity?

The second phase of the inquiry was directed to the possibility and advisability of incentive taxation for business expansion and improvement. Under this phase of the study, the institute sought to find out what business would actually be willing to do in return for tax alleviation or tax rewards.

The third phase of the survey was directed to the examination of profit sharing and employee benefits. The questionnaire at this point analyzes the plans, benefits, and facilities which are now in existence; the expense of such plans, the effectiveness and the value of profit sharing;—and what to me is perhaps most important—how many of the businesses now utilizing the profit sharing principle would discontinue their plans were there no employee resentment over the discontinuance.

Fourth. The Institute proceeded to determine how many business organizations would voluntarily establish a plan of sharing profits with employees if compensatory tax benefits were allowed to such businesses.

Fifth. This survey will show how many and what type of business men favor tax rewards for profit sharing, plant expansion, and increased employment, and how many of the institute's members do not favor the use of our taxing system for these purposes.

In conclusion: I will respectfully submit the legislative proposals, prepared by the institute, which are designed to effectuate those tax plans which the institute's membership favors.

In this specific analysis, despite the fact that less than 6 weeks have elapsed from the time the institute questionnaire was sent to members, more than 3,200 business and professional organizations are represented in the tabulations, and these firms employ more than 600,000 employees. The institute has found in the answers of each of the surveys conducted by it that after the first 2,000 questionnaires have been analyzed there is invariably less than 1 percent deviation in the answers from that point on to 10,000 or any number of questionnaires answered. Thus, the findings I am about to present may be accurately regarded as representing the plans as well as judgments of the entire membership in the Tax Research Institute—employers throughout the country employing more than 6,000,000 employees.

Whom does the survey cover? Of the 3,200 questionnaires tabulated and analyzed, 1,506 are from manufacturing businesses, 754 wholesale, 719 retail, 362 service organizations—we will show how many and what types of businessmen favor tax rewards for profit sharing, plant expansion and increased employment, and how many of the institute's members do not favor the use of the taxing system for that purpose—now to continue—179 financial firms, 28 law offices, 28 accounting offices, and the balance, labor unions, trade associations, and nonprofit organizations. It will be noted that several hundred of the business organizations have indicated they serve a dual function, such as wholesale-retailer.

Of the business organizations, 336 of them operate as individuals, 154 as partnerships, and 2,668 as corporations.

Among the corporations which are involved in the tabulated survey, 1,545 have incomes of $25,000 or less, while 1,123 show more than $25,000 income.

I might state in passing that in the compilation of this survey the institute utilized the assistance of almost every one of the 40 of the legislative and tax experts who are on our staff.

Senator HERRING. And how many questionnaires did you say that the survey covered?

Mr. CHERNE. About 3,200 were returned. As I stated, among the corporations which are involved in the tabulated survey, 1,545 have incomes of $25,000 or less, while 1,123 show more than $25,000 income. We broke the corporate income at that point for the reason that the 1938 Revenue Act also breaks it at that point in its application of the undistributed profits tax.

Now, as to the handicap by the undistributed profits tax: The fourth question asks corporations: "Have you been handicapped by the undistributed profits tax?" One thousand six hundred and seventy-seven of the corporations state yes and 681 no.

Breaking this problem up, the institute asked whether the tax on undistributed profits restricted the following business activities: 945 organizations find that the undistributed profits tax has restricted plant improvement, while 681 find that it has not; 796 have been restricted in plant expansion, 470 have not; 967 have been restricted in the retirement of debt, 371 have not; 1,521 have been restricted in the retention of reserve for future needs, 238 have not; 630 have been restricted in enlarging employment, 489 have not.

The lack of 1938 profits, I might mention at this point, is unquestionably an important factor in several of the cases for the indications that the undistributed-profits tax has had as slight—if the word "slight" can be used—an effect as these statements would indicate. The identical question was asked at the close of 1937, the year when business was good, and we found that at that time 78 percent of the business and professional men answering as to the undistributed profits tax found that it did handicap their business, while at that time only 22 percent answered that it did not.

Of the entire group we find that 101 organizations have been restricted in no way by the undistributed-profits tax.

Of particular importance in the above is the fact that the undistributed-profits tax has apparently, or is believed by businessmen, to have most seriously restricted the creation of a backlog for future business needs, depression or adversity.

That one effect is the one which elicited the greatest number of affirmative answers to the question "Has the indistributed-profits tax handicapped you in that respect?"

The seventh question asks whether the 1938 tax law will compel these business organizations to distribute dividends in excess of the amount they would have ordinarily distributed in accordance with corporate policy. Nine hundred and fifty of the organizations say that it will, as against 1,287 who say that it will not.

Bear in mind in this connection that under the 1937 Revenue Act, corporations with income of $25,000 or less are not obliged to distribute dividends, and even if they do distribute dividends, there are no tax credits which will compensate them for such voluntary distributions.

In this connection it must be pointed out that the corporate organizations showing an income of $25,000 or less are not compelled by the 1938 Revenue Act to distribute any dividends and there are no credits in the 1938 Revenue Act for corporations of this size for the distributions. It is interesting in this connection that the institute's survey conducted in December of 1937, before the undistributed-profits tax was modified, shows that 72.2 percent of all business organizations surveyed were compelled to distribute dividends in excess of the amount they would have distributed if they had followed their own business judgment, while only 27.8 percent stated they would have distributed that amount anyway. The 1938 Revenue Act has therefore already had its alleviating effect upon this problem.

Is the complaint the high tax or the type of tax: One of the most important questions in the entire survey asks business, in essence, whether it is the high rate of tax which disturbs business activity, or uncertainty created as a result of the nature of the tax. Thus, the questionnaire asks:

> Which would you prefer; a corporate tax of 19 percent reduceable to 16½ percent if you distribute your profits to stockholders. as is provided in the 1938 Revenue Act, or a flat tax of 18 percent with no credit for distributed profits?

Thus, in the first case, business could pay 16½ percent, while in the second case it would have to pay 18 percent.

One thousand, one hundred and five of the organizations stated that they would prefer the more complicated and uncertain method of taxation, while 996 preferred the higher flat, uncomplicated corporate tax. Thus, almost half of the corporations would pay a higher tax if it were flat.

Incentive taxation for business improvement: We now turn to the second phase of the institute's survey concerning incentive taxation for business improvement. The questions concern this committee's study of the feasibility of tax rewards for the voluntary expansion of business.

The ninth question asks: "If additional deductions or credits were allowed for prudent improvement or expansion in industry, would you make improvements?" One thousand, eight hundred and four say they would, as against 383 who say they would not.

Senator VANDENBERG. That is a very eloquent figure.

Mr. CHERNE. May I emphasize there that we prepared specific proposals rather than merely ask whether they were in favor of incentive taxation, or the result might very well have been the contrary. Then later we present for the first time the question, "Are you in favor of incentive taxation," having conditioned the replies to the specific proposals.

Would you make replacements: 1,596 say they would, as against 368 who would not.

Would you start plant expansion: 1,118 say they would as against 641 who would not.

Would you, as a result, employ more people: We find here that 1,622 of the business organizations would employ more people, as against 571 who would not.

Thus, on the basis of this question, additional deductions or credits would have, or the businessmen believes it would have, its most important business effect in reemployment, rather than in the stimulation of the durable goods industries through replacement of heavy machinery or expansion of plant.

The tenth question inquires whether the business organizations would be induced to make improvements if they were permitted to take increased depreciation deductions on any new plant equipment or property. One thousand, three hundred and seventy of the organizations would improve if given this additional tax inducement, as against 1,135 who would not.

Thus, there is apparently the conviction that increased credits or deductions would stimulate improvement more than would increasing the depreciation allowance on such improvements themselves.

We have already had experience, or the experience is about to start in the first of those, the provision for additional credit in the Social Security Act and for merit rating under the State unemployment insurance acts. And we now go further.

As to incentives for stabilizing employment:

We find in answer to the eleventh question that 1,169 of the organizations tabulated in this survey at present shut down or reduce employment during certain periods of the year, as against 1,748 whose employment during seasonal operations remain relatively stable; if they were allowed tax rewards to give some compensation for plant and equipment operating expenditures during such slack season, 415 of the firms representing 124,660 employees would still close down, while 549 of the firms who now close down, depriving 110,690 employees of earnings during that period, would remain open.

We find, secondly, that 511 of the firms representing 179,515 employees would still reduce employment while 483 employing 60,025 people would not reduce employment. And we find that 660 of the unstable organizations believe that they would, to some degree, stabilize their employment and affect thereby 126,355 employees, as against only 238 organizations employing 74,015 people who would not stabilize their employment.

If there were such tax rewards for remaining open in slack seasons, we next asked business whether they would be able to sell their products made in such periods profitably. Only 445 of the organizations believe they could sell such products at a profit, while 536 do not.

If, therefore, this question is to be credited, we must assume on the basis of these answers that businessmen would be content to remain open or not reduce employment while selling the products manufactured during such periods without profits.

Tax rewards for operating during slack seasons. On the entire problem of tax rewards for plant and equipment, operating expenditures during slack seasons, 838 of the business organizations are in favor of the plan, as against 480 who are opposed.

This quesiton is probably the only question or one of the few questions in the entire survey which many organizations who have sought to seek for large group of employers have apparently been speaking accurately. To some extent, though, the statistics included under this question are perhaps even more dramatic than those which have thus far been assumed by political or economic commentators.

What they think of the present tax law. Let us now turn our attention to the opinions of these 3,200 business and professional organizations about our tax system in general.

The thirteenth question asks whether they are in favor of continuance of the present tax law without change, and we find that only 179 are in favor as against 1,799 who are opposed to the tax law.

Of this group we must also realize, in fairness to the law itself, that a substantial portion of those would be opposed to any tax law.

Are they in favor of a flat rate of tax on capital gains? 1,448 favor a flat rate as against 435 who do not.

Do they favor the right to carry over losses from year to year? Two thousand five hundred and thirteen do as against 168 who are not in favor of such loss carry-over.

Are they in favor of a higher tax on undistributed profits? We find that 148 of the business organizations are in favor of the higher tax, while 1,992 are not.

A higher tax on capital gains elicits the approval of 138 business organizations, while 1,595 are opposed.

Are they in favor of repeal of the excess-profits tax? We find here that 2,164 organizations are in favor of the complete repeal of this tax as against 366 who would keep it—and on the repeal of the undistributed-profits tax, 2,409 of the business organizations would repeal it as against 208 who would not.

Summarizing this phase, therefore, we find that:

(1) The first step suggested by business opinion—in drafting any new tax legislation—is the permission to carry over losses from year to year.

(2) The legislative proposal in which they are next in favor is the repeal of the undistributed-profits tax, and

(3) The repeal of the excess-profits tax and a flat rate of tax on capital gains.

The carry-over of business losses. Let us now analyze the proposal in which the answers display the most interest—the carry-over of losses.

The fourteenth question asks: "If you were allowed to carry over operating losses from year to year, would that encourage you to risk a possible bad year or two in expanding production?" One thousand five hundred and sixty-seven of the organizations would take a "flyer" in expanding production as against 492 who would not; 1,802 of the organizations would expand their sales efforts to seek new markets as against 324 who would not; 1,518 would make an effort to develop and market new products as against 436 who would not.

President Roosevelt, in his Arthurdale address earlier this year, when he permitted the 1938 Revenue Act to become a law without his signature, discussed the possible legislative differentiation in taxing capital gains between productive capital assets as distinguished from speculative capital assets.

The fifteenth question asks: "If lower capital gain rates were made applicable to gains on the first sale of stock issued for purposes of business or plant expansion—that is, a completely nonspeculative issue, would that provision encourage you to expand plant and equipment?" Five hundred and forty-eight of the replies state "yes," while 791 say "no"; 479 of the organizations would be encouraged to expand, by that provision, production against 801 who would not; 618, however, would be encouraged to develop and market new products as against 749 who would not.

May I mention that President Roosevelt's name was not mentioned in connection with the question in the survey, so that the answers reflect reaction to the question rather than reaction to our Chief Executive.

Senator VANDENBERG. That would relieve you of any charge of contumacy.

Senator HERRING. I notice that you have four different questions as to the elimination or reduction of various taxes and everyone seems to be in favor of the reduction of taxes. I do not find any of them yet that are in favor of taxes. Did you ask any questions as to the method they would suggest to make up the revenue which is necessary if their suggestions are complied with?

Mr. CHERNE. Frankly, we did not, because equally frankly, we did not expect contributions which would interest either this committee or ourselves, first; and secondly, it would be absolutely impossible for us to tabulate or analyze those recommendations. I may say though, in passing, that I have with me approximately 600 letters from members sent with their questionnaires, where each of them gives his individual panacea for the improvement of our national economy. I do not speak in derogation of these, because a substantial number of them represent considerable effort and considerable thought. It is our intention to prepare a summary of all of those suggestions, all of those that have any merit at all, and submit that to your committee for your personal study or for incorporation into the record.

Senator HERRING. As reflecting the opinions of some 6,000,000 people, I thought that information of that sort would be helpful to the entire Finance Committee when they consider the next revenue act.

Mr. CHERNE. You may find that some of the suggestions for increasing revenue will flow from legislative proposals or legislative suggestions that follow the questionnaire.

Incentive taxation for reemployment. We now turn to the two questions which search the broadest possible uses for incentive taxation. The sixteenth states: "Suppose it were provided that the present tax rates remain until private business reemploys a stated percentage of workers from the national relief rolls, at which time the excess profits and undistrubted profits would automatically expire?" Nine hundred and ninety-seven organizations favor this plan, as against 1,033 who do not.

Would they reemploy idle workers to hasten the lowering of the corporate taxes. Five hundred and seven would, while 1,001 would not.

Thus, the 587 who would reemploy idle workers to hasten tax aleviation which is made contingent not on their individual effort, but on the employment record of the entire country, represent approximately 107,495 employees, while those who would not take this voluntary step represent 305,265 employees. As to the percentage of the present personnel which these firms would voluntarily increase, if such were the law, 243 would increase up to 5 percent of their personnel; 245 up to 10 percent; 139 up to 20 percent; 42 up to 30 percent; 1 up to 40 percent; 3 up to 50 percent; and 14 over 50 percent.

The seventeenth question is very similar, except that in this case each separate corporation can earn exemption from excess profits and undistributed profits taxes by increasing the number of its own employees by a stipulated percentage. Thus, under this plan, national reemployment would not be necessary before an individual corporation could secure exemption from the excess profits and undistributed profits taxes.

The number of organizations who would favor an incentive taxation plan of this kind is 1,438, employing 373.440; those opposed are 546 firms, employing 154,620.

Senator VANDENBERG. That question would be rather comparable to the merit question in unemployment insurance?

Mr. CHERNE. Correct.

Of those in favor of the plan, 220 of the organizations would increase their personnel by 5 percent; 260 by 10 percent; 114 by 20 percent; 61 up to 30 percent; 1 up to 40 percent; and 5 of the organizations would increase their personnel over 50 percent if they could thereby secure immediate exemption from the undistributed-profits and excess-profits taxes.

Present profit-sharing plans: The third phase of the survey concerns profit sharing and employee benefits. There are few phases of American industrial activity about which less is known than the successful and unsuccessful attempts which have been made to share profits directly and voluntarily with employees.

First, of the firms surveyed we find the following plans in operation at the present time: (*a*) 275 of them have a profit-sharing plan which is not primarily designed to act as a stimulus for sales or production; (*b*) 229 of the organizations have employee savings plans; (*c*) 125, wage-dividend plans; (*d*) 843, bonus plans; (*e*) 164, pension plans; (*f*) 17, annuity plans; (*g*) 139, stock-ownership plans; and (*h*) 109, some other form of employee-benefit plan.

In each of these cases the number of employees involved are as follows: (*a*) 65,650; (*b*) 47,140; (*c*) 19,840; (*d*) 173.405; (*e*) 92,440; (*f*) 7,310; (*g*) 47,890; (*h*) 52,694.

In addition to full company profit-sharing plans, we find that over and above the wage scale the following are provided for employees: 1,319 firms with 515,155 employees have group insurance supported in whole or in part by the employer; 432 firms with 201,310 employees provide death benefits; 427 with 164,795 employees provide hospitalization; 2,071 with 530,220 employees provide vacations with pay; 192 employers provide an employee credit union for 124,945 employees; 75 have gymnasiums for 41,510 employees; 313 provide social activities for 191,700 employees; 536 employers with 150,265 employees make disability payments; 565 with 215,050 employees give medical care; 1,292 firms employing 318,120 people have sick pay; 903 with 250,435 people make loans for their employees; 262 have athletic activity for 207,100 employees; 83 firms provide 62,225 employees with clubrooms; 129 provide housing for 79,900 workers at lower than the prevailing rent; 686 of the organizations provide 196,950 employees with general merchandise at lower than retail prices; 213 provide restaurant service for 167,805 employees at either reasonable prices or entirely free.

We believe that we have there given the most common of the methods both of profit-sharing and employee benefits.

Of the total number of firms, 1,898 of them employing cumulatively approximately 494,425 employees, grant these extra benefits to all of their employees.

Three hundred and sixty-six of them with 72,250 employees have established them only for key employees. Seven hundred and fifty-five firms with a personnel of 261,045 grant these extra benefits, not only to their regular employees but to hourly waged employees as well.

Of the firms who are now utilizing profit sharing and the extra employee benefits, we find that the percentage of net earnings the companies have spent, aside from wages, for employee benefit and welfare during the past 2 years are as follows: 609 of the organizations, employing 179,480 people, spent up to 5 percent of their net earnings on employee benefits; 328 of the firms, representing 134,690 people, spent up to 10 percent; 128 of the firms, employing 39,535 people, find their cost from 11 percent to 20 percent of net earnings diverted into employee benefits; 31 firms, with 10,320 employees, spent up to 30 percent for this purpose; 9 firms, with 3,345 employees, up to 40 percent; 3 firms, with 5,000 employees, up to 50 percent; and 7 firms spent more than half of their entire net earnings on employee benefits and profit sharing in this case for 625 employees.

Here is contained that information which will possibly do more to educate the average executive in the wisdom and advisability of voluntary profit sharing than any other phase of this survey.

Effects of employee benefits: Let us now for a moment turn to the effects experienced by businesses which operate profit-sharing plans or encourage employee benefits over and above the wage scale.

Nine hundred and fifty-five of the firms find that they have less labor turnover; 612 have the same labor turnover as before while 44 have more; 602 of the firms note less strikes or labor disputes; 403 of the same number of disputes.

In only 26 cases have there been more labor disputes after the inception of profit sharing or employee benefits.

In 617 of the cases, there were less requests for wage increase.

In 774 of the cases, the same requests as previously.

And in 113 of the cases, there have been more requests.

Three hundred and thirty-five firms find that there is less breakage of machinery as a result of the plan.

Six hundred and sixty-one find the same amount of machinery breakage.

While in only 19 cases has there been more machinery breakage after the inception of a profit-sharing plan.

As to the effect upon increased production, we find that 140 of the organizations have a greater production than previously; 592 show the same production; while 447 show a drop in production after the profit-sharing plan.

In this connection, the drop in production after the profit-sharing plan within the last 2 years, may have little reflection upon the profit-sharing plan itself.

Senator HERRING. You give a very wide interpretation to the term "profit sharing"?

Mr. CHERNE. Yes, sir.

Senator HERRING. You include group insurance and all of those things?

Mr. CHERNE. We call them "employee benefits" over and above the wage scale, but in answering this question, we have asked employers that wide question, "What have been the effects of profit sharing and employee benefits over and above the wage scale?"

A not very marked effect of the employee benefit plan is on the care of handling products. One hundred and thirty-five of the organizations find less care, 707 find the same care, 356 find more care.

As to the loyalty to the company and supervisory employees, 243 of the firms find less loyalty, 534 the same, and 958 of them find greater loyalty.

The attendance record of these firms has not been substantially affected. One hundred and forty-five of the organizations find an adverse effect in attendance, 733 approximately the same percentage of attendance, and 470 a beneficial effect.

Now we come to the question which summarizes all of the effects.

The twenty-third question asked these businesses, whether the profits shared or benefits given are taken for granted by the employees with a previous attitude recurring, despite the existence of the plan and the cost incurred. We find here that the answers do not entirely agree with the specific effects stated by the firms. Eight hundred and twenty-three find that the previous attitude is recurring while 743 find that it is not.

Senator HERRING. Don't you think that if this had been limited to direct-profit sharing, without including these many other benefits, such as group insurance and all these things, that your compilations here would be entirely different perhaps as to the statement they would make as to the labor turnover, as to labor trouble, and those things? Don't you think they would have obtained a greater response from a direct profit-sharing plan than they would from these group-insurance benefits and these other things which are rather common as you know?

Mr. CHERNE. I think that is entirely true, because the most important characteristic of profit sharing is that sharing the earnings directly ties the employee up with the profits of the company, while the other plans, in almost every instance, do not do that. It is still possible for us to find out, if the committee is interested, what the specific effects have been in both the groups of profit-sharing and employee benefits.

Senator HERRING. I think it would be interesting.

Mr. CHERNE. Next is: Reasons for profit sharing failure. In an effort to determine the reason for the discontinuance of profit-sharing plans in those firms which had them but ended them, we find that 15 firms discontinued them because of the faulty operation of the plan itself; 14 because of the excessive cost; 48 of them because of the failure of expected benefits from the plan to materialize. My own observation of this is, in many instances, that it is the faulty operation of the plan itself. Forty-seven of them discontinued the plan because the plant was subsequently unionized; 72 of them, the greatest group, discontinued the profit-sharing plan because of business difficulties which were not connected with the profit sharing at all; 23 of them discontinued the plans as a result of employee discontent or apathy; and the second largest reason for the discontinuance of profit-sharing plans was the enactment of the Social Security Act, which impelled the discontinuance of profit sharing in 70 organizations.

Of the firms which are now employing a profit-sharing plan, we find the following response to the question: "Would you like to discontinue the plan, except for employees resentment?" And bear in mind that we have previously asked these firms, "Is the previous attitude recurring in spite of the existence of the plan?" Fifty of them would, while 1,102 of them would not, even where there were no employee resentment for the discontinuance.

As to the tax rewards for profit sharing: We now turn to the feasibility of tax rewards for the encouragement of voluntary profit sharing. The twenty-sixth question in the institute's survey asks the following:

> If you were permitted a credit against the corporate tax, similar to the credit now provided for dividend distribution, would you establish an employee profit-sharing plan? Consider in answering this question the tax benefits plus the employee stabilization and other advantages, against the cost of the plan and the profits distributed.

We find that if there were a compensatory tax credit, 226 would definitely establish the plan—these 226 organizations represent 34,405 employees; 546 representing 125,300 employees would not; but 1,072 firms representing 387,775 employees would seriously consider establishing a profit-sharing plan.

"Do businessmen favor incentive taxation?"—perhaps the most controversial question to be raised at this particular session.

Studying further the effect of tax rewards on profit sharing, plant expansion, and improved employment, we asked the direct question: "Do you favor such tax rewards for these purposes?" The institute, in seeking to secure as intelligent an opinion on this question as possible, prepared in cooperation with this committee an "unfavorable" comment and a "favorable" comment on such systems of taxation. We tried to divide equally the strength in the poll. As a matter of fact, we made a particular effort to see that one did not run even a line longer than the other on our questionnaire, for fear of giving the impression that there was more emphasis in mind on the "favorable" than the "unfavorable" or vice versa.

After reprinting both comments, the questionnaire stated:

> As will be noted, the quoted conclusions are diametrically opposed. So that we may consolidate accurately the consensus of businessmen as to the advantages and disadvantages of tax rewards, will you answer the following: "Do you agree with the 'unfavorable' opinion?"

Seven hundred and fifty four find that the system of tax rewards is not wise. But 1,787 agree with "favorable" and therefore approve tax rewards for profit sharing, plant expansion, and improved employment.

In answer to the twenty-eighth question, we find, in addition, that tax rewards would encourage 1,533 firms representing 397,510 employees to increase expenditures for plant and equipment, as against only 338 with 101,200 employees who would not.

We find 1,012 encouraged by tax rewards to adopt profit sharing as against 377 who would not. The 1,012 firms in this case employ 96,370 workers.

We find 1,259 firms would be encouraged to employ additional help. The present personnel of the 1,269 firms is 99,475. Only 357 firms would not be encouraged to employ additional workers.

Nine hundred and ninety-eight of the companies state that tax rewards would encourage them to market new products, as against 395 who would not find this the effect of tax rewards.

One thousand and twenty-nine firms representing 162,545 employees would be encouraged to increase production, against only 359 who would not increase production.

The other phases of the institute's report. This, Senators, is the total tabulation of the institute's survey. There are three other phases of our activity in connection with this survey, which are as follows:

First, we have prepared legislative recommendations for specifically carrying out those phases of the tax program or tax plan which the members of the institute have indicated that they, by substantial majority, approve.

Second, we are preparing a compilation of the individual comments from important individual members on their own profit-sharing plans and on their own opinions of the existing revenue act, their desires for future tax amendment, and their opinions on the wide subject of profit sharing and incentive taxation. This, if the committee is interested, can be submitted in the very near future.

Third, we have taken the entire survey and have broken it into 24 smaller and more closely studied units. Thus, we have prepared the answer to each of the questions according to the size of the corporation's income, as well as for those organizations which do not function as corporations. Similarly, we have tabulated the entire result separately for 10 separate groups of business, depending upon the number of employees which constitute their personnel. It will probably be the desire of this committee to take these smaller break-downs and include them in the record, rather than go into them at this hearing.

May I at this time therefore summarize as briefly as possible the institute's specific legislative recommendations for translating into law the effects which are desirable to American business and professional activity as represented by the membership of the Tax Research Institute. In several cases we have prepared alternative legislative methods of procuring the same results.

Tax incentives to promote business activity and recovery are logically classified according to the desired objectives.

Objectives: It is respectively submitted that the objectives to be reached through incentive taxation are as follows:

(1) To foster amicable employer-employee relations through the establishment of profit-sharing plans.

(2) To encourage greater expenditures for the purchase of new machinery and equipment, the construction of new buildings, the development of new enterprises, and general business expansion.

(3) To stop any increase in the ranks of the unemployed and to transfer to business pay rolls those now on home and work relief rolls who are employable.

(4) To encourage the investment of private capital in industry and also to increase the revenue from the taxation of income by eliminating the present exemption in respect to income from certain Federal and all State and municipal securities.

(5) To increase and stabilize Federal revenue by stimulating and stabilizing national income at a high level.

Let us now summarize the incentives which may be used to accomplish results which have just been mentioned.

Tax incentives for the following:

(1) Tax credits and deductions to promote employees' profit-sharing plans.

(2) Tax credits and deductions and liberalized depreciation and capital gain provisions:

(*a*) To promote capital expenditures and plant expansion.

(*b*) To encourage investment in new enterprises.

(*c*) To promote the purchase of new business property.

(*d*) To encourage business expansion.

(*e*) To restore the purchasing power of the railroads.

(3) To provide for additional deductions in computing taxable income by employers in proportion to the increase in the average employment of each business enterprise for each taxable year over the average employment for the preceding 3 years.

(4) To promote industrial recovery by removing the shadow of the excess-profits tax from American business, thereby permitting business to take unanticipated steps toward business amendment, particularly in the expansion of facilities without risking thereby a possible 12-percent penalty imposed by the excess-profits tax for unanticipated substantial increases in business income.

(5) To divert income and investment funds into private enterprise rather than into exempt securities by ending the tax-exempt character of Government securities.

Incentives for employees' profit-sharing plans. The tax incentives to encourage the maintenance of profit-sharing plans include the allowance of credits and deductions to employers who establish and maintain bona fide plans for sharing business profits with their employees, thus making for more stable employer-employee relationship. The tax incentives should be allowed to employers who maintain such profit-sharing plans regardless of the form of business organization, so that any employer, whether a corporation, partnership, or individual proprietorship, may secure the tax advantages accorded to those who comply with the statutory provisions.

It is believed that employers should be permitted considerable latitude in formulating and adopting specific profit-sharing plans for which tax incentives are to be allowed, but there should be certain requirements common to all such plans.

Provisions which should be common to all plans:

(*a*) It should be essential to the allowance of the tax incentive credit and deductions that the profit-sharing plan include all regular employees who have worked for the particular employer at least 6 months.

(*b*) The incentive should be allowed regardless of whether the profits are distributed to the employees by means of a "profit-sharing trust," or directly, or by other means.

(*c*) Employee contributions to the plan should be permitted regardless of the particular plan maintained without any reduction in the tax incentive for such contributions.

(*d*) Sharing of profits should be in addition to regular compensation whether or not fixed by collective bargaining.

In order to operate as incentives for the establishment and maintenance of employees' profit-sharing plans, deductions and credits must be allowed for distributions in connection with such plans, in addition to allowances available under the present law. It is proposed that corporations be permitted to deduct from gross income all distributions in the year in which made pursuant to the provisions of a bona fide employee's profit-sharing plan, whether directly to employees or to employees' profit-sharing trusts. In addition such corporate employers should be allowed to include in the computation of the dividends paid credit the amount of such distributions. For other than corporate employers, it is proposed that deductions of such distributions, limited to 15 percent—or other equitable percentage of net income—be allowed from gross income in addition to the deduction of the entire amount under section 23 (a) (1) as an ordinary and necessary business expense.

Proposed changes in law: It is suggested that section 27 of the 1938 Revenue Act be amended to include in the computation of the dividends paid credit the amount of distributions made by the corporation to employees pursuant to bona fide profit-sharing plans. It is suggested that section 25 of the 1938 Revenue Act be amended to include, in the case of taxpayers other than corporations, a deduction limited to 15 percent—or other equitable percentage—of net income, for a distribution of earning made to employees pursuant to a bona fide profit-sharing plan, provided that such distribution is also allowable as a deduction for ordinary and necessary business expense under section 23 (a) (1).

Employees' profit-sharing plans; profit-sharing trusts: Since contributions to profit-sharing trusts are now deductible from gross income in reasonable amounts, additional tax incentives are needed to encourage the establishment and maintenance of such plans. These incentives should include the full allowance, for the year, for payments in the amount of cash, and the value of capital stock or other property transferred or paid by the employer into such trusts during the taxable year, in accordance with the terms of the trust instrument. There should also be permitted the allowance as deductions of all earnings and profits transferred to such trusts during the taxable year, whether or not in the form of dividends on the stock of a corporate employer. It is probable that the objectives cannot be obtained in this respect by amendment of section 23 (p). Therefore, it is considered more desirable to add a new subsection to the revenue act, to accomplish both of these legislative proposals.

Rewards for employees' profit-sharing trusts: It is proposed that a new subsection, 23 (t), be inserted in the revenue act to provide that any employer who establishes and maintains a profit-sharing trust for any taxable year beginning after December 31, 1938, for the distribution of earnings and profits of his particular trade or business to his employees, shall be allowed a deduction, in addition to the amounts allowable as deductions as regular business expenses, of the full amount of cash and the value of capital stock or other property transferred to such trust during the taxable year, and that the earnings and profits of the employer transferred to profit-sharing trusts shall be allowed as deductions, even though in the form of dividends on the capital stock of the employer corporation.

Proposed addition to the revenue act, section 23, deductions from gross income: In computing net income there shall be allowed as deductions:

(*t*) Profit-sharing trusts—

(1) General rule: An employer establishing or maintaining a profit-sharing trust for any taxable year beginning after December 31, 1938, for the distribution of earnings and profits of the trade or business in which the employer is engaged, to the employees thereof, shall be allowed as a deduction in addition to amounts allowed as deductions under subsection (*a*) of this section the amount of cash and the value of capital stock or other property transferred or paid into such trust during the taxable year pursuant to the terms of the trust agreement, but only if such amount (1) had not theretofore been allowable as a deduction, and (2) the agreement of trust provided for the distribution of the trust income received in each taxable year either during the taxable year of receipt of such trust or before the close of the taxable year beginning before December 31, 1943.

(2) Deductions for dividends: Any amount of the earnings and profits of the employer transferred or paid into such a profit-sharing trust, exempt under section 165 of this title, whether or not in the form of dividends on the capital stock of the employer corporation, shall be allowed as a deduction in computing net income under this title.

(3) Exemption of trusts under section 165: The provisions of paragraphs (1) and (2) of this subsection shall be subject to the qualification that the deduction under either paragraph shall be allowable only with respect to a taxable year, beginning after December 31, 1938, whether the year of the transfer or payment, or a subsequent year, of the employer ending within or with the taxable year, of the trust with respect to which the trust is exempt from tax under section 165.

Rewards for stock-distribution plans: The fact that the amount of earnings and profits distributed by employer corporations on employee-owned stock is not deductible for purposes of the excess-profits tax and the corporate normal tax has no doubt discouraged the adoption of employees' stock distribution plans by many corporations. To eliminate this objection it is proposed that the new corporate employer be allowed a deduction for the amount of dividends paid on employee-owned stock, as reasonable compensation paid to such employees, where the distribution is made in connection with the maintenance of a profit-sharing plan by means of the distribution of stock to qualified employees.

Proposed change in law: To amend section 23 (a) (1) of the revenue act to provide for the allowance of deductions in computing net income, in addition to a reasonable allowance for salaries or other compensation, for the amount of dividends paid to employees upon stock of the employer corporation provided the employer has, pursuant to a bona fide plan of profit sharing with his employees, agreed to by a majority of said employees, distributed its capital stock to qualified employees under such a plan. This deduction shall be in addition to all other deductions and credits allowable by reason of the payment of such employees' profit-sharing dividends.

Incentive to promote capital expenditures and plant expansion; deductions for capital improvements: That the revival of the heavy goods industries and the construction industry is a prerequisite to a sustained high level of business activity has almost become an economic axiom. In order to encourage expansion of plant facilities, construction of new industrial buildings, additions to existing industrial plant facilities, repair and restoration of the depreciated buildings and the purchase of new machinery and other equipment, it is proposed that special limited deductions against gross income be permitted on account of expenditures made for these purposes. The revenue act now specifically provides that amounts expended for capital improvements in restoring property and making good the exhaustion thereof may not be deducted from gross income.

If a limited deduction is permitted on account of such expenditures, an incentive to expand profits and earnings for these purposes in order to reduce tax liability will be presented. In order for this incentive to be effective, it is necessary that deductions from gross income, taken on account of these expenditures, shall not affect the basis of the property thus acquired, either for the purpose of computing gain or loss on subsequent disposition thereof, or for the purpose of computing annual depreciation allowances on such property.

It is specifically proposed that 50 percent of amounts expended for these purposes shall be made deductible from gross income in computing the taxable net income for the year in which paid or incurred with the limitation similar to the limitation for charitable institutions, that amounts deducted during a given taxable year for any and all of such purposes may not exceed 15 percent of the taxpayer's net income as computed without the benefit of this new deduction.

It is submitted that although these provisions would make available to business additional offsets against gross income, they would result in an actual increase rather than a decrease in revenue. The purchasing power and high level of business activity generated by construction encouraged by these provisions would ultimately result in increased income to the taxpayer making the deduction, so that his net income would be at least equal to what his net income without the new deductions and without the new plant and equipment facilities would be. Further, new taxable compensation and business income would be created by increased employment and stimulated business activities, arising out of construction encouraged by this liberalization of the revenue laws.

Proposed changes in law: It is suggested that section 23 (a) of the 1938 Revenue Act be amended to permit the deduction of "50 percent of any amount paid out for new buildings or for new machinery and equipment, or for permanent improvements or betterments, to be used in the taxpayer's trade or business, whether or not having the effect of increasing the value of any property or estate, and any amounts expended in restoring property or making good the exhaustion thereof whether or not an allowance is or has been made, provided that the total of such amounts permitted to be deducted during a given taxable year for any and all of such purposes may not exceed 15 percent of the taxpayer's net income as computed without the benefit of this deduction." It is suggested that section 24 (a) (2) (3) be modified by adding the provision "except as provided in section 23 (a) (1) as amended." It is also suggested that section 113 (b) be amended to provide that no adjustment in basis be made for any deductions allowed under the provisions of section 23 (a) (1) as amended, for the purposes stated above.

Alternative plan for tax benefits where expenditures are made for new facilities, equipment, and so forth. The undistributed-profits tax and its counterpart in the 1938 act have compelled business corporations to distribute dividends and profits which they would prefer to have used in the purchase of new equipment and the expansion of plant facilities. The plowing back of corporate earnings and surplus into plant, equipment, and business expansion would result in the national industrial expansion necessary to liquidate relief rolls. Corporations using earnings and surplus for this power should receive tax credits at least equal to those received by corporations distributing dividends.

Proposed changes in law: It is proposed that provisions be inserted in section 27 providing for the inclusion in the dividends paid credit of a stated percentage—2½ to 5 percent—of amounts paid or incurred by a corporation during the taxable year's (1) expansion of plant facilities; (2) purchase of new equipment; and (3) development and exploitation of new products.

Senator HERRING. I think we should keep pretty close to the suggestion of profit-sharing incentive taxation. Many of these things would be very helpful, I think, to the Finance Committee, but I wonder how pertinent it is to the investigation that we are attempting to make.

Mr. CHERNE. Before we started the preparation of these legislative proposals we first studied the introductory statement of the resolution which created this committee and assumed that any form of incentive taxation, or the feasibility of any form of incentive taxation, would be within the direct interest of this committee. It is not our suggestion by very long means that this committee approve of these suggestions.

Senator HERRING. We appreciate that you have done a splendid piece of work here and we appreciate it. It is just a thought that I had.

Mr. CHERNE. I think you will find from this point on that the incentive taxes proposed are directly tied up with employee benefits and employment, so that we will get back to that phase in which you are primarily interested.

Incentives for increases in employment; deductions for reemployment: The problem of increasing employment and liquidating relief rolls is the most important problem which challenges the business and legislative resources of the Nation. Increased employment is an objective which should be considered in fashioning every piece of legislation. Talk of business and Government cooperation has been widespread; action in that direction has been notably scant. Here is a concrete proposal for Government-business cooperation to further reemployment. It is specifically proposed that the Government make available to industry tax deductions which shall be conditioned upon reemployment by industry—a merit rating system applied to income taxation.

The Government gives tax benefits only if, as, and when business absorbs idle men and liquidates relief rolls, thereby curtailing Government expenditures and reducing the need for Federal revenue. If Government gives business tax advantages, business can afford to reemploy idle men. If business reemploys idle men, the Government can afford to reduce tax rates. Again, if business absorbs idle men, a lower tax rate will bring an equal or an increased amount of revenue as taxable income is increased. If industry does not absorb idle men, the tax rates are not changed and the Government loses no revenue.

These prefatory remarks are made to demonstrate that one objection to the plan—the loss of Government revenue—cannot be proposed in this connection.

Here, then, is a sound practical program offering business cooperation, encouraging business to go forward with expanding industrial pay rolls, and rewarding the employer who is able to plan work for men now unemployed. This is plain good business for both Government and industry.

It is proposed that all taxpayers conducting business in which four or more are employed should be allowed a deduction from gross income in an amount which shall be based on the increase in the average employment of the taxpayer for the particular taxable year over the taxpayer's average employment index for the 3 taxable years beginning 3 years prior to the effective date of this enactment. This average employment index will be computed on the basis of an information return containing employment data for such years. The average employment index thus established will then form the basis for the employment deductions for the subsequent 3-year period. The deduction which will be allowed will be a fixed percent of the operating gross income of the business for a given percent of increased employment in the taxable year over the average employment index.

Now, in our report, we have prepared in very general terms the legislative method whereby this can be accomplished. The information return which will be required, the operations of the revenue act which need to be amended for that purpose. And as an alternative to the provisions, it could be provided that each employer's average employment index could be computed according to the rules and regulations to be promulgated by the Commissioner, rather than that 3-year period. There we were forced arbitrarily to take a specified period of time for a base index.

Proposed changes in law: All employers of four or more persons are required to file an information return with the Commissioner of Internal Revenue on or before March 31, 1939, or if they report on a fiscal year basis, on or before the last day of the third month following the close of the fiscal year ending in 1939. This return must state the average number of employees employed by the taxpayer during each month of the 36-month period beginning with the first month of the taxable year commencing in 1936 and ending with the last month of the taxable year beginning in 1938. If the taxpayer has not been in business for the full 3-year period provided by the return, he will file a return showing his average number of employees during each month of the period that he was in business. This return must also contain any additional information which the Commissioner may require.

The employer's "average employment index" is the average number of employees employed by him during the period covered by the information return required by this section.

Taxpayers employing four or more employees in their business will be allowed a deduction from gross income as follows: On an increase of —— percent in employment during the taxable year over the employer's average employment index, a deduction —— percent of the gross income derived from such business; and for each additional increase in employment of —— percent during the taxable year over the employer's average employment index, an additional —— percent will be allowed. The average employment index will form a basis for this employment deduction for a period of 3 years. At the expiration of this 3-year period a new average employment index will be computed on the basis of employment records for the preceding 3 years.

Taxpayers commencing business during the 3-year period beginning with the taxable year commencing in 1939 are required to file an information return on or before the 30th day of the third month following the close of their first taxable year which comprises a full 12-month period. This information return must include data as to their average number of employees during each month of such taxable year. On the basis of this return the average number of employees for the period covered by the return will be computed. This computation will then constitute the employer's average index upon which deduction for the remainder of the 3-year period beginning with the taxable year commencing in 1939 will be based.

NOTE.—As an alternative to the provisions of the last paragraph, it could be provided that such employer's average employment index could be computed according to rules and regulations to be promulgated by the Commissioner.

Incentive to encourage investment in new enterprises; liberalized capital gain and loss provisions for new investments: The high rate of tax upon capital resulting from the fact that capital gains usually accrue over a long period of time but are realized for tax purposes in the year of sale, thus becoming subject to high surtax rates, has been frequently cited as an obstacle to business expansion. It is especially unfair to the investor in new stock who incurs, in most cases, a high risk; who provides capital for the new enterprise which is essential to a healthy expanding economy and whose stock investment becomes valuable not in 1 year but over a term of years. If his risk is bad, he loses his investment. If his gamble is successful, the value which his stock investment has gained by virtue of several years of effort will be taxed at almost confiscatory rates in 1 year—the year of sale. To encourage the investment of capital in new enterprises and the investment of new capital in existing business and corporations for the purpose of new equipment and the expansion of plant facilities—and there is the relationship of the activity of this committee, the encouragement of capital in new enterprises—it is proposed that more favorable capital gains and losses provisions be inserted in section 117 to apply to the initial purchaser of stock originally issued after December 31, 1938, for the purpose of raising capital for such purposes. That, it is expected, will encourage taxpayers to take the risks incident to the purchase of such stock. A maximum tax of 10 percent is proposed on any gain derived by such purchaser on the sale of such stock, while it is proposed that 50 percent of any loss sustained on such sale is deductible from long-term capital gains, short-term capital gains, or ordinary gross income.

The provisions will first encourage investment in the capital stock issued by corporations on entering into new enterprises or on expanding old enterprises. The tax rate, at which gain realized upon the sale of such stock may be taxed, is reduced, but the amount of taxable gains would be increased, because investment in and sale of new stock will be encouraged. Revenues will also be helped by the fact that the investment of capital in new enterprise will generate new activity and new employment, thus creating once more increased taxable compensation and business income.

Another attractive effect of this provision is that it encourages stock financing rather than bond financing. Some economic doctors diagnose as one of the foremost ills of American business, the fact that it carries too great a burden of fixed charges. When business contracts, the income decreases but fixed interest charges remain. It is advocated that railroads and other business corporations rely to a greater extent upon stock financing and to a lesser extent upon bond financing. Stocks increase in value to a far greater extent with business success than bonds, and thus stock investments are hit much harder by the present capital-gains provisions than are bond investments. Liberalization of the capital-gain provisions of the revenue act along the lines suggested below, though not a deciding factor, will leave stock financing and stock issues in a more favorable position than they now occupy as opposed to bond financing and bond issues, in the eyes of the investor and the business corporation seeking funds.

Proposed changes in law: Specifically, it is proposed that losses realized by the first purchaser of stock originally issued after December 31, 1938, shall be deductible as follows: 50 percent of the loss sustained may be deducted from either long-term capital gains, short-term capital gains, or ordinary operating income. Gains realized on the disposition of such stock by the first purchaser thereof shall be taxable as follows: 50 percent of the gain shall be either added to the net income from other sources and taxed at the applicable normal and surtax rate or shall be taxed separately at a maximum 20-percent rate. Whichever method shall result in the lesser tax may be used. These provisions shall apply only to gains or losses sustained by the original purchaser of stock originally issued by the corporation after December 31, 1938, and shall be applicable only if the capital raised by such issue of stock is used in (*a*) the construction of new plant facilities; (*b*) the purchase of new equipment; (*c*) the development and exploitation of new products; (*d*) expenditures for the purpose of restoring property and making good depreciation thereof; and (*e*) the undertaking of an entirely new business enterprise.

Now, as to the carry-over of losses—if you will recall that question, if the businessman had his own way to work on the 1938 Revenue Act, the first thing he would do would be to provide for the carry-over of losses.

It has been the complaint of the American business community that the failure of the revenue laws to permit the carry-over of operating losses sustained in one year against income earned in succeeding years is oppressive and a positive deterrent to normal business and economic activities. Until the revenue laws permit the application of operating losses sustained in one year against income realized in other years it will be possible for taxpayers to sustain heavy losses over, for example, a 3-year period and yet be subject to heavy income-tax liability. American enterprise has hesitated to exploit new products, to undertake new business ventures, and to expand production, and to invest enterprise capital, because it is frequently true that such ventures result in losses for the first, second, or third years; and if profits are forthcoming, they do not make an appearance until 1, 2, or 3 bad years have been experienced. Thus, we are frequently told about the situation where a corporation exploiting a new product will spend 2 years educating public opinion to favor the product, sustaining a loss of $300,000 in the first year and $100,000 in the second year. In the third year the investments and the efforts of the 2 previous years finally bear fruit, and the corporation earns $300,000. Obviously, over the 3-year period there has been no real income; but, on the contrary, there has been a $100,000 loss. Nevertheless, the corporation is faced with a tax liability which will run in the neighborhood of $50,000, so that instead of a $100,000 loss for the 3 years, it has a $150,000 loss. That a prospect of this sort is a positive threat to a new enterprise cannot be denied.

Again we are not seeking to rip up the entire revenue act nor are we suggesting that that be done. That is not a phase of work in which this particular committee is concerned. We believe this committee to be primarily interested in expanding the employment rolls, and giving increased betterments in employer-employee relationships.

Proposed changes in law: It is proposed as an incentive to encourage business expansion that sections 23 (e) and (f) be amended to provide that taxpayers initiating an entirely new business enterprise, expanding plant facilities, or investing capital in the purchase of new equipment after December 31, 1938, may deduct from gross income any net operating losses by reason of such new business enterprise or expansion incurred during any taxable years beginning after December 31, 1938, and not prior to 3 years preceding that in which the deduction is taken.

The result of this change in law: It is submitted that while these provisions will give business the benefit of additional offsets against gross income, their stimulating effect upon the national economy in encouraging new enterprises, expanded production, and the expansion of plants and equipment—and necessarily, employment—will actually result in (1) an increase in the net income of the taxpayer receiving benefits over a period of years, arising from expansion efforts, which otherwise would not have been undertaken, and (2) increase in taxable salaries and other income arising from increased employment and increased business resulting from new ventures encouraged by this liberalization of the revenue laws.

Incentives for the purchase of new business property; depreciation deductions: A common complaint of the businessman is that frequently he does not get the benefit of depreciation deductions for the full expenditure for his depreciable assets. He is restricted to the deduction of a relatively fixed proportion of the cost during each year of the useful life of the property. This deduction must be taken yearly, irrespective of whether or not the taxpayer has taxable income and thus irrespective of whether the deduction has the effect of causing any reduction in tax liability. Under this method, if newly purchased machinery has a useful life of 10 years, and during the 10-year period the business sustains losses without the benefit of deduction for depreciation during 4 years, the taxpayer has effectively been allowed a depreciation deduction to the extent of only 60 percent of the cost of the machinery. Further, if a taxpayer fails to make an adequate depreciation deduction in one year, he cannot add it to his depreciation in a later year. An amendment to the law in this respect, more favorable to the taxpayer, will, it is believed, furnish an incentive to the purchase of new or additional property such as machinery used in the taxpayer's business.

Three alternative proposals are advanced to effectuate this purpose. The first is to permit taxpayers to take depreciation deductions on property acquired after December 31, 1938, in any amount in any year during the expected life of the property until the entire cost has been recovered. The second proposal would permit depreciation deductions in the same manner as at present, except that on depreciable property acquired after December 31, 1938, the taxpayer will be permitted to carry over the deduction or any part thereof which is not needed to show no net income for the year to the next taxable year, during the useful life of the property, in which a net profit is realized. The third proposal is to retain the provisions of the present law with respect to depreciation allowances intact, except that depreciation allowable on depreciable property should not reduce the cost basis of such property unless the depreciation has been or could have been utilized to reduce tax liability.

Proposed legislation, section 23 (1), a reasonable allowance for the exhaustion, wear and tear of property used in a trade or business, including a reasonable allowance for obsolescence: With respect to such property acquired after December 31, 1938, the deduction for exhaustion, wear and tear may be taken in any amount in any year or years during the expected useful life until the entire cost has been recovered.

Alternative: Section 23 (2). A reasonable allowance for the exhaustion, wear, and tear of property used in a trade or business, including a reasonable allowance for obsolescence. With respect to such property acquired after December 31, 1938, the deduction for exhaustion, wear and tear, may be carried over from a taxable year to the extent that it is not needed to show a net loss for the year to the next taxable year, during the useful life of the property, in which a net profit is realized. This carry-over may be continued during the useful life of the property until the accumulated depreciation not previously utilized as a deduction against gross income is absorbed.

Alternative: Section 113 (b) (1). In respect of any period since February 28, 1913 for exhaustion, wear and tear, obsolescence, amortization, and depletion, to the extent allowed (but not less than the amount allowable) under this act or prior income-tax laws. However, with respect to exhaustion and wear and tear on property, used in a trade or business, purchased subsequent to December 31, 1938, adjustment shall be made only for the amount actually allowed.

Incentive to encourage investment in private industries; taxation of interest on governmental securities: It is proposed that the tax exemption now granted to the income on certain types of securities be abolished. The beneficial effect of this would be twofold. First, it would increase Federal revenue. Secondly, it would encourage the investment of capital in productive enterprises by taxpayers in the high surtax brackets. The present law places too great a premium on the purchase of exempt Government obligations as contrasted with investment in productive enterprises. While the gross yield from the latter may be greater than the former, the latter's net yield after taxes is frequently lower.

Capital-stock and excess-profits taxes: The excess-profits tax has proven a poor revenue producer. For the fiscal year ending June 30, 1938, the receipts from this tax amounted to only $36,653,233.78. Despite the relatively small amount of excess-profits taxes paid, corporations have been loath to tie up additional capital in their plants with the shadow of an additional 12 percent tax hovering over any profits that may result therefrom. Despite the high tax rates on profits in excess of 10 percent of the adjusted declared value of the capital stock, taxpayers have tried not to declare values any higher than necessary in order to keep their capital stock tax liability down.

Probably most declarations of value made this year were estimated on the basis of facilities and business expectations at the time the declaration was made. As a result, corporations fear the additional tax liability that any expansion might bring. This condition of stagnation is equally harmful to Government, employer, and employee. Bearing in mind particularly the fact that only $36,000,000 is brought into the Government in the way of revenue. An additional objection to the tax is that it is the nature of a game of chance in which the taxpayer must stake his tax liability for 3 years on a guess made in 1938 as to future profits. It is therefore proposed that this excess-profits tax be eliminated and the Revenue

Act be amended so that a tax be levied on the actual value of a corporation's capital stock instead of on the fictitious declared value as it is imposed under this 1938 Revenue Act.

The last suggestion we have made provides a tax incentive to restore the purchasing power of the railroads—that particular industry.

The financial rehabilitation of the railroad industry is a prime essential for national economic recovery. However, the reduction in fixed interest charges on long-term obligations is essential to recovery of the majority of the railroads. To assist in such rehabilitation it is proposed to amend the Revenue Act to permit railroads to purchase their outstanding interest-bearing obligations in 1939 and 1940 at less than par or face value without incurring income-tax liability on such transactions and without affecting the basis of any of the railroad's property. The following section is proposed to be inserted in title I of the 1939 Revenue Act to permit the railroads to reduce outstanding, interest-bearing indebtedness without incurring income-tax liability.

Section 122, gain or loss to a railroad corporation from purchase and retirement of its own obligations:

(*a*) In computing net income under this title, no gain shall be recognized to a corporation from the purchase and retirement by such corporation of its own obligations at less than the par or face value of such obligations, provided that the corporation is either (A) a corporation whose principal business is that of a common carrier by railroad; or (B) a corporation the assets of which consist principally of stock in such corporation and which does not itself operate a business other than that of a common carrier by railroad. For the purpose of determining whether the principal business of a corporation is that of a common carrier by railroad, if a common carrier by railroad has leased its railroad property and such properties are operated as such by another common carrier by railroad, the business of receiving rents for such railroad properties shall be considered as the business of a common carrier by railroad.

(*b*) The provisions of subsection (*a*) shall apply only to transactions described therein consummated during the calendar years, 1939 and 1940.

That concludes the institute's report.

(Sample of questionnaire sent to members of the Tax Research Institute:)

(Questionnaire to members:)

WHAT SHOULD THE 1939 TAX LAW BE?

The important Subcommittee of the Senate Finance Committee, now studying *profit-sharing systems in industry* and the possibilities of *incentive taxation*, has requested the Tax Research Institute to find out from its members (1) what they are now doing in the way of profit-sharing and (2) what they would like to see in the new tax law. (See page 7 of this November 12th T. R. I. Reports for a discussion of the Committee's activities.)

The Institute is therefore requesting all members to fill out this brief questionnaire with the assurance that individual names, replies and opinions will, as usual, be kept confidential. The Institute's findings will be presented to the Subcommittee's hearings at the end of this month.

Your cooperation will be an important influence on the character of any new tax legislation.

INSTRUCTIONS—PLEASE READ CAREFULLY

A. You may omit answering any questions which would violate your company policy.

B. Omit answers where questions do not apply to your business.

C. Attorneys and accountants should attempt to give replies which reflect the situation in which their most important clients find themselves.

D. If you care to dictate a letter amplifying or supplementing the questionnaire, it will be appreciated.

E. Please return questionnaire to the Tax Research Institute, 292 Madison Ave., New York, as quickly as possible so that it may be tabulated and ready for the Committee hearing, which starts November 21st.

1. It is desirable (but not obligatory) that you give the Institute your firm name. *At least indicate your State.* Use the space below:

Firm: ----------

Individual: ----------

Address: ---------- State: ----------

Approximate number of your employees: ----------

2. Exact nature of your business or activity:

(a) manufacturing ---------- [ ]	(f) law office ---------- [ ]
(b) wholesale ---------- [ ]	(g) accounting office ---------- [ ]
(c) retail ---------- [ ]	(h) labor union ---------- [ ]
(d) service ---------- [ ]	(i) trade association ---------- [ ]
(e) financial ---------- [ ]	(j) non-profit organization ---------- [ ]

3. If your organization is a business does it operate as a

(a) individual ---------- [ ]	(c) corporation ---------- [ ]
(b) partnership ---------- [ ]	(d) other form ---------- [ ]

4. If a corporation, is the corporate income

(a) $25,000 or less ---------- [ ]	(b) Over $25,000 ---------- [ ]

5. If a corporation, have you been handicapped by the undistributed profits tax ---------- YES [ ] No [ ]

6. Has the tax on undistributed profits restricted:

(a) plant improvement ---------- YES [ ] No [ ]

(b) plant expansion ---------- YES [ ] No [ ]

(c) retirement of debt ---------- YES [ ] No [ ]

(d) retention of reserve for future needs ---------- YES [ ] No [ ]

(e) enlarged employment ---------- YES [ ] No [ ]

(f) or has it restricted none of these ---------- YES [ ] No [ ]

7. Will the 1938 Tax Law compel you to distribute dividends in excess of amounts you would ordinarily have distributed in accordance with corporate policy ---------- YES [ ] No [ ]

8. Which would you prefer:

(a) a corporate tax of 19% reduceable to 16½% if you distribute your profits to stockholder ---------- [ ]

(b) a flat tax of 18% with no credit for distributed profits ---------- [ ]

INCENTIVE TAXATION FOR BUSINESS IMPROVEMENT

The following questions concern the Senate Committee's study of tax rewards for the voluntary expansion of business.

9. Additional deductions or credits were allowed for prudent improvement or expansion in industry—

(a) would you make improvements ---------- YES [ ] No [ ]

(b) would you make replacements ---------- YES [ ] No [ ]

(c) would you make plant expansions ---------- YES [ ] No [ ]

(d) would you, as a result, employ more people ---------- YES [ ] No [ ]

10. If on any new plant equipment or property, you were permitted to take increased depreciation deductions, would that induce you to make improvements? ---------- YES [ ] No [ ]

11. Is it your present practice to shut down or reduce employment during certain periods of the year?........................ Yes [ ] No [ ]

12. If you were allowed tax rewards to give some compensation for plant and equipment operating expenditures during such slack seasons—

(a) would you still close down.................. Yes [ ] No [ ]
(b) would you still reduce employment.......... Yes [ ] No [ ]
(c) would you stabilize your employment......... Yes [ ] No [ ]
(d) would you be able to sell your production made in such periods, profitably........... Yes [ ] No [ ]
(e) are you in favor of this plan............... Yes [ ] No [ ]

13. Are you in favor of:

(a) continuance of the present tax law without change.................................. Yes [ ] No [ ]
(b) a flat rate of tax on capital gains........... Yes [ ] No [ ]
(c) carry-over of losses from year to year........ Yes [ ] No [ ]
(d) higher tax on undistributed profits........... Yes [ ] No [ ]
(e) higher taxes on capital gains................ Yes [ ] No [ ]
(f) repeal of the excess profits tax.............. Yes [ ] No [ ]
(g) repeal of the undistributed profits tax........ Yes [ ] No [ ]

14. If you were allowed to carry-over operating losses from year to year, would that encourage you to risk a possible bad year or two in:

(a) expanding production........................ Yes [ ] No [ ]
(b) expanding your sales efforts to seek new markets.................................. Yes [ ] No [ ]
(c) developing and marketing new products....... Yes [ ] No [ ]

15. If lower capital gain rates were made applicable to gains on the first sale of stock issued for purposes of business or plant expansion, would that provision encourage you to:

(a) expand plant and equipment................... Yes [ ] No [ ]
(b) expand production........................... Yes [ ] No [ ]
(c) develop and market new products............... Yes [ ] No [ ]

16. Suppose it were provided that the present tax rates remain until private business re-employs a stated percentage of workers from the relief rolls, at which time the excess profits and undistributed profits taxes would automatically expire—

(a) would you favor such a plan.................. Yes [ ] No [ ]
(b) would you re-employ idle workers to hasten lowering of the corporate taxes................ Yes [ ] No [ ]
(c) what percentage of your present personnel would you voluntarily increase, if such were the law:

0-5% [ ]	11-20% [ ]	31-40% [ ]	over 50% [ ]
6-10% [ ]	21-30% [ ]	41-50% [ ]	

17. If it were provided that *your* corporation could earn exemption from excess profits tax and undistributed profits tax by increasing the number of *your* employees by a stipulated percentage—

(a) would you favor such plan.................... Yes [ ] No [ ]
(b) what percentage of your personnel would you increase to obtain exemption from these taxes:

0-5% [ ]	11-20% [ ]	31-40% [ ]	over 50% [ ]
6-10% [ ]	21-30% [ ]	41-50% [ ]	

PROFIT-SHARING AND EMPLOYEE BENEFITS

18. The Committee is studying the feasibility of tax rewards and incentive for firms voluntarily establishing bona fide employee profit-sharing and benefit plans.

These questions concern this phase of the Committee's activities. Indicate by check mark if you have any of the following plans in operation:

(a) Profit-sharing plan (not as a stimulus to sales or production) [ ]
(b) Employee-savings plan [ ]
(c) Wage-dividend plan [ ]
(d) Bonus plan [ ]
(e) Pensions plan [ ]
(f) Annuity plan [ ]
(g) Stock-ownership plan [ ]
(h) other employee-benefit plan [ ]

18a. If convenient, indicate details of your plan, on a separate page, to whom it applies, how long in existence, what percentage of the net earnings is distributed, what are its effects, etc.

19. Do you provide any of the following for your employees, over and above the wage scale:

(a) Group insurance supported in whole or in part by employer [ ]
(b) Death benefits [ ]
(c) Hospitalization [ ]
(d) Vacations with pay [ ]
(e) Employee credit union [ ]
(f) Gymnasium [ ]
(g) Social activities [ ]
(h) Disability payments [ ]
(i) Medical care [ ]
(j) Sick pay [ ]
(k) Loans [ ]
(l) Athletic activities [ ]
(m) Club rooms [ ]
(n) Housing at lower than the prevailing rents [ ]
(o) Merchandise (general) at lower than retail prices [ ]
(p) Restaurant service at reasonable prices (or free) [ ]

20. Are all employees entitled to these extra benefits [ ]
Are only key employees entitled to these extra benefits [ ]
Are hourly-wage employees entitled to these extra benefits [ ]

21. What percentage of net earnings has your company spent (aside from wages) for employee benefit and welfare during the past two years?

0–5% [ ] 11–21% [ ] 31–40% [ ] over 50% [ ]
6–10% [ ] 21–20% [ ] 41–50% [ ]

22. State effect of your plan on:

	Less	Same	More
(a) labor turnover	[ ]	[ ]	[ ]
(b) strikes or labor disputes	[ ]	[ ]	[ ]
(c) requests for wage increases	[ ]	[ ]	[ ]
(d) breakage of machinery	[ ]	[ ]	[ ]
(e) increased production	[ ]	[ ]	[ ]
(f) care of handling of products	[ ]	[ ]	[ ]
(g) loyalty to company and supervisory employees	[ ]	[ ]	[ ]
(h) attendance record	[ ]	[ ]	[ ]

23. Are the profits shared or benefits given taken for granted by the employees with the previous attitude recurring despite the existance of the plan and the cost incurred? Yes [ ] No [ ]

24. If you have had a profit-sharing plan, which is not now in existence, was it ended because of:

(a) faulty operation of the plan [ ]
(b) excessive cost [ ]
(c) failure of expected benefits to materialize [ ]
(d) subsequent unionization [ ]
(e) business difficulty not connected with the plan [ ]
(f) employee discontent or apathy [ ]
(g) enactment of Social Security Act [ ]

25. If you now have a plan, would you like to discontinue it except for employee resentment? Yes [ ] No [ ]

26. If you were permitted a credit against the corporate tax, similar to the credit now provided for dividend distributions, would you establish an employee profit-sharing plan? Consider, in answering this question, the tax benefits plus the employe stabilization and other advantages against the cost of the plan and profits distributed.

Would establish plan [ ] Would not [ ]
Would seriously consider establishing a plan [ ]

27. Do you favor tax rewards for profit-sharing, plant expansion, and increased employment?

Unfavorable Comment	Favorable Comment
"A subsidy or reward such as suggested might tend to stimulate activity in building and expansion which, when completed, would prove to have been unwise and the expenditure harmful rather than beneficial. "The temporary business activity would create an artificial prosperity which would have an unfortunate reaction. "Consumption could not keep up with the stimulated production."	"We have been thinking for years of several major installations, but feel we could not afford them as it would be putting too much money in brick and mortar and machinery, based on the Federal Tax Policies. "Tax exemptions on the earnings invested in buildings, machinery and equipment would encourage us to make these extensions, promote employment and start a real prosperity based on private rather than Federal pump-priming."

As will be noted, the quoted conclusions are diametrically opposed. So that we may consolidate accurately the concensus of businessmen as to the advantages and disadvantages of *Tax Rewards*, will you answer the following:

I agree with-------------------------- "Unfavorable" [ ] "Favorable" [ ]

28. Tax rewards would encourage me to:

(a) increase expenditures for plant and equipment-	YES [ ]	NO [ ]
(b) adopt profit-sharing-------------------------	YES [ ]	NO [ ]
(c) employ additional help-----------------------	YES [ ]	NO [ ]
(d) market new products--------------------------	YES [ ]	NO [ ]
(e) increase production--------------------------	YES [ ]	NO [ ]

Please return this questionnaire as quickly as possible to the Tax Research Institute, 292 Madison Avenue, New York, N. Y.

Senator VANDENBERG. Mr. Cherne, as far as I am concerned, I think you have done a monumental piece of work in an amazingly persuasive way, and I am greatly indebted to you. Nothing could be more helpful.

Senator HERRING. I join in what Senator Vandenberg has said. This is most helpful. If you have anything more to contribute, we will be glad to receive it.

Mr. CHERNE. Anything that comes our way we will send down to you. I will leave with the committee the complete individual breakdowns of the entire study.

Senator HERRING. Thank you very much. We will take a recess now until 10:30 o'clock tomorrow morning.

(Whereupon, at 3:05 p. m., a recess was taken until the following day, Thursday, December 8, 1938, at 10:30 a. m.)

SURVEY OF EXPERIENCES IN PROFIT SHARING AND POSSIBILITIES OF INCENTIVE TAXATION

THURSDAY, DECEMBER 8, 1938

UNITED STATES SENATE,
SUBCOMMITTEE OF THE COMMITTEE ON FINANCE,
Washington, D. C.

The committee met, pursuant to adjournment, at 10 a. m., in room 312, Senate Office Building, Senator Clyde L. Herring presiding.

Present: Senators Clyde L. Herring and Arthur H. Vandenberg.

Senator HERRING. Mr. Robinson.

STATEMENT OF JOHN ROBINSON, CINCINNATI, OHIO

Senator HERRING. Mr. Robinson, you are an employee of Procter & Gamble, are you not?

Mr. ROBINSON. Yes, sir.

Senator HERRING. Of course, you are familiar with their profit-sharing plan from an employee's standpoint?

Mr. ROBINSON. Yes, sir, I am a member of that plan.

Senator HERRING. Please tell us about it, how it has affected you and what you think about it?

Mr. ROBINSON. Would you like me to start from the beginning?

Senator HERRING. Yes, please.

Mr. ROBINSON. Well, before coming to Procter & Gamble Co. I was a coal miner and I traveled the country, quite a bit, following up the coal mines, but I always found it was a feast or a famine. What I mean by that, it was seasonal work. We had to save money while we worked to get through the times we were out of work. Most of the time we could not save enough. The last time we had a strike in the coal business in Ohio, I was about 18 months without work; it happened in traveling, trying to get work, I got in line at Procter & Gamble Company's plant in Cincinnati. Well, there was such a tremendous lot of people in this line, that it took 2 or 3 hours for the employment man to see us all, but I kept going and about the tenth day, I think it was, he gave me a job as a clean-up man, cleaning the machinery at night. Well, it was a job to me. I needed money; I was down and out, my family were without clothes. So I started there on that job. It was just a job to me. After I had been there a few weeks first one man started talking to me and then another to tell me the ideas or plans that Colonel Procter had fixed for his employees. They first started to tell me: "How, after you have been here 6 months you will be given the privilege of joining this profit-sharing plan to buy stock." Well, I tried to get more information and everyone was eager to give it to me. That is employees, not just the foremen and management, the employees themselves; they were selling the thing to me.

They were telling me about the guaranteed-employment plan. Well, you know how I felt after being on part-time work, struggling along to save a little money and then spending it in off time. When they told me I was going to get my wages anyhow 48 weeks in a year, that alone sounded good to me. I felt: "Well, I am really in a good place. It is going to be all right."

Then they told me all about this profit-sharing plan; that I would pay 5 percent of my wages every week and the company would put an equal amount in the book for me, that would be 5 percent. At that time the plan was they would buy enough stock for you equal to 1 year's salary, which amounted to at that time five shares, at $275, which since then has been split 5 to 1, and it amounted to 25 shares at $55. Well, anyhow, I got a little book and a certificate saying I belong to this plan, and every pay day there was 5 cents taken out of every dollar, and each quarter I turned my book in and got it balanced. After awhile I got like the other fellows; I turned my book in, and then I was anxious to get it back to see what I had. There would be what I paid, what the company had given me in profit sharing. If it was $10 the company gave me $10. The company started out giving me 5 percent, but after a certain period they raised it to 6, and then they were paying in 1 percent more than I paid, and I was getting dividends put in my book on the stock I had paid for. So then I got the idea, after I got working there a couple of years, that this might easily stretch into the period of time when I would get that paid for, and that would be 6 years. That was the plan at that time.

As time went on, I brought my family to Cincinnati; I told my wife all about the plan, and she thought it was just a godsend that I got there. Of course, she was going to lay out the wages every week and budget. There was nothing to worry about. We could look a year ahead; we could be sure we would get the 48 weeks wages.

What makes the guaranteed employment so good, our profit sharing was based on what we got; so if we got wages every week our profit sharing was more; the more money we made the more profit sharing we got.

So after 6 years I was called over to the office and the management said: "Well, your time is up. You have got so much money overpaid. It is not enough to buy a share, but we will settle with you; we will give you your shares of stock." They gave me the extra money I had paid, and then the next 3 months after that, when it came profit-sharing time, instead of going in the book the company handed me a check of around $30. Well, it was a gift. I went home with my money. My wife said: "I never heard the likes of this, getting money as a gift. I don't know what you have done for it," she said, "but think how we had been struggling along here all these years trying to get along. Here we have a place where you have a steady job, a nice income, we are doing fine. We paid the back debts that we had incurred at the place we came from during the strike. Here we are able to send the children to school, give them good clothes, and here the company turns around and gives us a check out of the clear sky for $30."

Likely she planned she was going to buy shoes and things for the children.

So we just sat down and figured the thing out, and we thought, "Well, we are here to stay."

I tried to find out more about these plans and made it my business to understand them. Then we had a pension benefit plan. One percent was taken out of our wages and that guaranteed us two-thirds of our wages if we were sick. Well, my wife says: "When you worked in the coal mines if you got sick that was just a day lost. We just got by the best way we could. I don't know," she said, "this is real security." She said: "We are guaranteed our wages, we get a little extra on the side, we are guaranteed when we are sick, we are guaranteed by the old-age pension and the benefit plan. When you get old what more does a workingman want? That is security." That is my idea, gentlemen. That really is social security, in my way of looking at it. If a workingman is protected in his work, in his salary, and when sickness comes his family does not have to be without food, and then when he gets old he is protected. I don't know what other things people want.

I have been with this company for 11 years, and I want to say that I am absolutely sold on their policies, and I can speak for the people that work there. I work among them. I represent them in their conditions, their labor troubles, different things of that kind, and I know the people. I have had reasons to get among them and find out just what their situations are, and I have never found a person yet that is not sold on the Procter & Gamble policies. Not because it is Procter & Gamble, but they really have a system whereby their employees are benefited, and it makes the people want to work for a company like that. If you are a part of a company and you are receiving these benefits, they don't have to have a lot of supervision to force you to work. You do the work. You would feel, like if there is soap on the floor being wasted, you would make up your mind to take care of it; you pick up the soap. It is going to be automatic to you; you are part of the firm.

Now, there is another system attached to this profit sharing. Say your block of stock is 30 shares; well after you have got it paid for there comes a time in your life, which often does in a workingman's life, that he has sickness, hospital bills, such things as that, where it takes a few hundred dollars to pay for it. You go to the management and say: "I am not in shape to pay that. I would like to sell a little of my stock to pay that bill." The management is very willing. They allow you to sell 50 percent of your stock and still retain your membership in the profit-sharing plan. I tell you, there have been a lot of people that have been saved a lot of worries through that very thing. Most of them, after selling 5 or 10 shares, when they get on their feet they go right over and they say: "Now, I've got straightened out; I want to start in and buy those shares back." There is nothing to force them to do that, but they just feel it is something worth while; it is a security. They don't worry about the market going up and down. It is there; it is safe. They believe it is just as good as gold in the bank. They feel secure with the people who are running it, the management. I think when you have a confidence in people like that I do not see what more you want. Those policies must be worth while.

Senator VANDENBERG. That is a very human statement, and a very intelligent and helpful one.

Mr. ROBINSON. I want you to understand, gentlemen, I am not coached to say this. I am speaking from the heart.

Senator HERRING. We can tell that all right.

Mr. ROBINSON. Thank you.

Senator HERRING. Well, we thank you very much, Mr. Robinson. We appreciate your coming.

Mr. ROBINSON. I will be glad to answer any questions you wish to ask me.

Senator HERRING. How much stock do you own in the company now?

Mr. ROBINSON. Twenty-five shares. I was born in England. I came over in 1913. My mother lives over there. I have a sister I had never seen, because I never could get enough money together to go back and see them; but after I got with Procter & Gamble I was able to save enough money and made a trip 2 years ago to England, which would never have happened if I had been following the other kind of work. I also paid big hospital bills, and I am still in the clear on those—all through Procter & Gamble Co.

Senator HERRING. And your base wage without the profit sharing is as high as you could get anywhere else?

Mr. ROBINSON. Absolutely. It is the average-plus in the community on corresponding work. That is the agreement we have with the management—that they will pay us the average-plus of similar types of work in the community. Every 6 months they make a survey of that type of work, and they present it to us; and if we are on a par—on an equal basis with them—they will put us up ahead. We are always on the plus side of the community. They keep the prices up with the community or a little bit ahead, and in that way they have a good class of people; and I can say, gentlemen, that every day there are 100 or 150 people lined up looking for work, although they are not hiring people at present—just one or two once in awhile. People would do anything to get a job in that plant. I see them go up and down the road. I meet people that work 2 or 3 months, and then they are out of work; and they say, "Oh, boy, you are lucky. You've got a job you know is steady."

We don't stick to 48 weeks. Since I've been there we always got 50, and we got 1 week's vacation with pay; and this year, December 1, we signed an agreement with the management giving us 2 weeks, 1 week in the summer and 1 week in the winter, so that we get 50 weeks' work and 2 weeks' vacation with pay; we have got 52 weeks. We can't get any more.

Senator HERRING. That is right.

Mr. ROBINSON. I don't see what else a man would want. We've got individual representation, we've got almost anything within reason. We've got a hospital that the management gives us time to go to, we've got medicines—anything for first aid. They give us cough medicine if we've got a cold, or anything like that. They let us lie down if we've got a pain in our back or if we don't feel good they put us under the light. If the doctor says it will take a half hour, it takes a half hour, and we get paid our time.

Senator HERRING. That is a fine story. We appreciate your coming, Mr. Robinson.

Mr. ROBINSON. Thank you.

Senator HERRING. Mr. Morris is with Procter & Gamble, of New York.

STATEMENT OF JOHN H. MORRIS, NEW YORK, N. Y.

Senator HERRING. Mr. Morris, you have 31 years of service with Procter & Gamble, of New York?

Mr. MORRIS. Yes, sir.

Senator HERRING. Just tell us your experience with Procter & Gamble. You have been with them 31 years, and you are located in the New York office?

Mr. MORRIS. That is right; the Staten Island plant, New York.

Senator HERRING. Yes.

Mr. MORRIS. I went to work with the company on the 27th of June 1907. I went to work as a rigger. After I went to work there they were just building the plant, and some of the old-timers came from Ivorydale—that is the Ohio plant—and they started to tell me about the stock proposition, the profit sharing, but in some way or another I could not seem to swallow it; I did not think it really could be sold. So finally, after awhile, in 1909, I took out my first stock. Then after those times they used to issue a book. So every 6 months we sent our book in, so when the book came back we found out probably we were worth $100 more, and the next 6 months maybe we were worth another $150 more; that is $250; and as we went along through the profit sharing, you know, finally I had my first batch of stock paid up, somewhere around 1913, and I took out the second batch. I did not take any more so far; I was turning it back into stock.

So in 1917 I took my first check, because there was something coming up that I needed the money. In fact, the house I was living in was going to be sold at an auction sale. I got my 6 months' check then of $310. The house was sold at an auction sale, and the down payment was $290. I remember he gave me $20 change out of my $310 check. That is how I started my home.

So then I went in for stock again, and I have been buying stock all the way through, getting profit sharing. So not only myself, but all the employees—all our employees, oh, I don't know how many, but probably 95 percent—own stock in the company and receive their profit sharing all the way through, and through this profit sharing about two-thirds of our employees own their own homes or are buying their own homes—no; I am wrong there. About three-fifths of our employees own their own homes, and about two-thirds of our employees have cars, and it all came through saving money through the profit sharing.

Then after awhile somehow, I don't know just exactly how, Mr. Procter felt that he would still want to do better for the employees, so he started the sick benefit, so that when we get sick we receive two-thirds of our wages as long as we are sick. Death was $1,000 to your estate, and then a pension went in with that, with all those things, and then after that he set up a guaranteed employment.

Now, that is the history, as far as I am concerned. I think Procter & Gamble is a wonderful company. They have not only treated me that way, but they have treated all their employees that way. They want everybody to be treated right, and they want the foremen to treat the men right, and they stand up for their men all the way through.

Senator HERRING. You have a feeling of loyalty that you would not have otherwise?

Mr. MORRIS. I would almost live and die for Procter & Gamble; that is how I feel about them. That is the concern that put me on my feet, anyway.

Senator HERRING. Well, that is a fine story. Thank you very much, Mr. Morris.

Mr. J. M. Frank, president of Ilg Electric Ventilating Co., Chicago, Ill.

STATEMENT OF J. M. FRANK, PRESIDENT, ILG ELECTRIC VENTILATING CO., CHICAGO, ILL.

Senator HERRING. Mr. Frank, you have a profit-sharing plan, have you?

Mr. FRANK. Yes, sir.

Senator HERRING. Will you please tell us about it?

Mr. FRANK. I have covered it in a written statement to your secretary, but I will summarize it briefly. I think that our plan may be of interest to you chiefly in that it was started when our company began. Our company was incorporated in 1906, and the plan was put into effect in 1908, when we had seven employees; and the same plan, with no change whatever, has been in continuous operation up to this date.

The plan is a very simple one. The employee is given a percentage of his salary at the end of the year, that percentage being determined by the management, and based, of course, on the company's profits for that year.

Then there is an addition to the percentage that increases yearly after the second year and reaches a maximum addition after the eleventh year, which means that an employee who has been with the company 11 years at a given salary would get 50 percent more profit sharing than an employee with the same salary who had been with the company 1 year. In other words, it goes up in 5 percent increments for a total of 10 years.

The plan is successful, we believe, due to the fact that it has failed to pay in 8 years of those 30 years. Perhaps that sounds strange to say that it is successful because it has failed, but we feel that the 8 years in which the plan did not pay provided the real test for the plan. In other words, the plan of paying profit sharing in profitable years sold itself to our employees sufficiently well that it carried over in those years when the profits either were not sufficient or there were no profits, so our men felt it was quite proper not to have profit sharing. Therefore, I point to that particularly as being significant, that the plan must be a sound one if it carried through the years that it did not pay.

Senator VANDENBERG. In other words, as stated in your answer to our questionnaire, your profit sharing made all your employees profit-conscious?

Mr. FRANK. That is right. That is exactly what it did. They must have the feeling that it is based on profits; in other words, that it isn't something else.

Now, as to our method of pay. We issue at the end of the year a certificate, an interest-bearing certificate. The rate of interest has varied with the changing times, and the day on which the certificate comes due has varied, depending on the company's financial condition. As a rule, those certificates are due and payable within a year within the date of issue, and after that date they may be cashed, or they may be left on deposit with the company. In the main, however, the certificates have been exchanged for common stock in the company periodically, and we think that is a vital part of our profit-sharing system, that there is a tie-up between profit sharing and stock holding.

The result of that policy, practiced now over 31 years, is that we have 202 employee stockholders out of a total of 277 employees, and those employees own approximately 60 percent of the stock, other than officers, the officers own 40 percent of the stock and, of course, the officers are also employees. Our stock is owned entirely by employees; there are no outside stockholders.

We feel if that can be done, if there can be a tie-up between profit sharing and stock holding, that it is a very highly desirable feature.

We have in our company one or two things that may perhaps be of interest to your committee. We have a loan fund, which has been accumulated from time to time by company gifts, and we loan money to employees in time of need, just as a bank would lend money, and we urge them to put up their company stock as collateral. In that way we prevent, or tend to prevent the sale of stock, because inasmuch as we have gone to great trouble to put the stock into the hands of the employees, we naturally go to more trouble to keep it in their hands.

Senator VANDENBERG. What happens when an employee leaves?

Mr. FRANK. He may sell the stock if he wishes, of course, or he does not have to sell it. There are no strings tied to it. The result of it is we have a few ex-employees, some of them even working for competitors, who are stockholders in our company. As far as we are concerned, we feel that is probably desirable. Part of your question, Senator, is answered by the fact, though, that we do not have very many leave.

Senator VANDENBERG. In other words, your plan reduces your turn-over?

Mr. FRANK. Almost to nothing.

Senator VANDENBERG. When your board of directors has its annual meeting and determines how much of the profits are to go into profit sharing, is that a standard ratio?

Mr. FRANK. No, sir. We have not developed a fixed formula. We have no ratio of profit sharing to dividends, if that is what you mean.

Senator VANDENBERG. Yes.

Mr. FRANK. No, sir; but if it is of any interest to you, I could give you an approximation over-all figure over a period of 30 years on the relation of the total profit sharing to the total dividends. Would that be of interest to you?

Senator VANDENBERG. I would be glad to have that.

Mr. FRANK. The total profit sharing in that period—and that includes, of course, the years when there was no profit sharing—is $638,000, and the total dividends paid to stockholders in the same period is $1,551,000.

Senator VANDENBERG. That is about 2½ to 1.

Mr. FRANK. 2½ to 1. But it must be borne in mind that something more than two-thirds, perhaps 80 percent, of the men that receive the profit sharing also receive the dividends, because 80 percent of our employees are stockholders.

Senator VANDENBERG. After you have set that amount aside which is to go into profit sharing, is that paid uniformly under any formula to the employees, or is it on a merit-rating basis of distribution?

Mr. FRANK. No, sir. Only with the condition that I pointed out, the employee must have been with us 3 months to qualify, and then a percentage of profit sharing is determined on. Let us say that percentage is 10 percent. If the employee has an annual salary of $2,000 and has been with us 1 year, his profit sharing would be $200. If he has an annual salary of $2,000 and has been with us 11 years, it would take a 50-percent increment. In other words, he would be credited for his length of service, so he would get $300. The merit, of course, is implied in the fact that he has been with us a number of years and it is obvious that his service has been satisfactory.

Senator VANDENBERG. Have you had any labor trouble?

Mr. FRANK. No.

Senator VANDENBERG. The profit share must be taken in stock, is that right?

Mr. FRANK. Oh, no; no, sir. There is no obligation there whatsoever. The profit sharing, as I explained, is an interest-bearing certificate which becomes due and payable on a given date. Here is an actual form [indicating]. From time to time—we have not done it at regular intervals—from time to time when we felt it was desirable for the company and the employees we have issued stock, and those issues of stock could be taken up in cash or in profit sharing.

Senator VANDENBERG. Well, now, at the end of the year when you make your distribution, the employee gets this certificate?

Mr. FRANK. He gets this certificate; yes, sir.

Senator VANDENBERG. He could not take cash at that time?

Mr. FRANK. Not at that time; no.

Senator VANDENBERG. Now, when can he get his share of the profit in cash, if he wants it?

Mr. FRANK. I will answer that question in this way: This certificate, we will say issued on January 1, would become due and payable approximately a year later, it may be a year and 2 months later so as to give us a little leeway; then if the employee wants to cash this certificate, he merely notifies us a few days in advance, I believe it states on here how many days, and anytime after that date it may be cashed. On the other hand he may, if he wishes, let that remain on deposit and it bears a varying rate of interest. That interest rate has been as high as 5 percent, and it has been as low as 3 percent.

Senator VANDENBERG. Well, if he elects to take stock, what fixes the price of the stock?

Mr. FRANK. In a company like ours, where the stock is unlisted, we simply have to fix that arbitrarily from time to time when the stock is issued, and we have to arrive at a figure based on book value and earnings.

Senator VANDENBERG. That is a varying figure?

Mr. FRANK. Yes, sir.

Senator VANDENBERG. Determined by the board of directors?

Mr. FRANK. Yes.

Senator VANDENBERG. On the basis of book value?

Mr. FRANK. Book value and earnings.

Senator VANDENBERG. Yes. I suppose the stock has the same voting rights as any other stock?

Mr. FRANK. Yes, sir. We have just that one form of common stock, and we have a few issues of preferred, a very, very small issue of preferred that comes ahead of it.

Senator VANDENBERG. Inasmuch as your stock is not listed, I suppose you do not have any trouble with unhappiness through fluctuating quotations?

Mr. FRANK. We try to avoid that by arranging to lend the employees money on stock, or to arrange for sales from one employee to another, if there seems to be a real need; but I think you will see, with a loan committee of the type that I described in a small company, we can keep pretty close to the employees, and we can usually work out the case for them, so they do not have to sell their stock. Obviously, it is implied that the situation is such that the employee does not want to sell his stock.

Senator VANDENBERG. What happens in lax times when your employment has to be reduced?

Mr. FRANK. We have attempted to work out a stationary number of men as nearly as it is possible in the manufacturing business. When we come out of a peak period, as in 1937, into a slow period like part of 1938, we begin to slow down on hours, and the newer and younger men bear the brunt of it first. That may sound a little complicated, but we feel that the older men, the men who have been with the company the longest, are in a corps of employees, if you please, and we attempt to shorten the time in the factory by shortening the weekly time for a few of the newer employees first. So that if the times got harder and harder, it would eventually, of course, affect all of the men, the older men included, but the men of longer service, the men in the inner corps, would be given the preference.

Senator VANDENBERG. Have you any pension plan?

Mr. FRANK. We have been creating a pension fund for about 20 years, and so far, we have done nothing but create the fund. We have no formulated plan at present, although we have had occasion, up to date, to pension a few men, and we have worked out a plan for those men. That is not necessarily a standardized plan.

Senator VANDENBERG. I notice one of your comments on the questionnaire is that you believe a yearly profit-sharing plan is greatly superior to a monthly or quarterly plan.

Mr. FRANK. Yes, sir.

Senator VANDENBERG. Why?

Mr. FRANK. Because it seems to me that it is only through a yearly plan, and in fact only through a yearly plan, that has been good some years and bad some years, that you can really get across the idea to the employees that it is truly a profit-sharing plan. You used the words I would like to use, to make them profit-conscious.

Let us start with the weekly plans, suppose profit sharing is weekly, well, it is practically impossible to detach the employee from the idea that that is not a wage bonus.

Senator VANDENBERG. Part of his compensation?

Mr. FRANK. That is right. Now, if it is monthly, that is a little less that way, but still a wage bonus; quarterly, the same. So it is merely a matter of degree. If I was consistent, perhaps we ought to pay profits every 5 years, but that would not be logical, because all business is run in yearly intervals, and we think the yearly payment is about right.

Senator VANDENBERG. Do you pay your stockholders by the year?

Mr. FRANK. No; we have quarterly dividend periods. However, we do not hold strictly to those periods. We use the system that seems to be current nowadays of declaring a dividend if, as, and when.

Senator VANDENBERG. Well, if the profit-sharing dividends were geared to the same system that you used with the stockholder, would it not accomplish the purpose you are describing, even if it were quarterly? Suppose you paid your dividends to your employees always at the same time you paid them to the stockholders, would not that gear it to the profit?

Mr. FRANK. Offhand, I can see no reason why it would not, if it were carefully explained.

Senator HERRING. Have the unemployment-compensation laws caused you to attempt stabilization of employment?

Mr. FRANK. Will you repeat that?

Senator HERRING. The unemployment-compensation laws, have they caused you to attempt stabilization of employment?

Mr. FRANK. They have caused us to make no change, because we had been attempting it long before.

Senator HERRING. You believe your plan could be followed by other employers to their advantage, do you?

Mr. FRANK. I am not sure about that, and I am sure it would be dangerous to say "yes" and just let the answer stop there. I feel that our system has been successful in a small company, or a relatively small company, principally because we started it when we were a very small company, with seven employees, and built up a background while we were small. Now, I doubt if you or I could take that system and implant it today as a new thing into, let us say, a good sized company. It would be quite difficult.

Senator HERRING. You have no retirement benefits or disability benefits, or old-age insurance or pension of that kind as a definite plan, have you?

Mr. FRANK. We do not have a definite plan. We have one in fact that is definite, and that is purely gratuitous. We have an entirely gratuitous life-insurance policy that reaches a maximum of $1,000. If the man has been with us 10 years, it becomes $1,000. It goes up $100 a year, I think, after the first year, and that is purely intended as a little benefit for his heirs if he dies in our service.

Senator HERRING. Your thought is you will pay them a good wage and let them share in the profits and let them buy those things themselves? You think that is a little better policy than to hold out a little out of each dividend check and build it up for them?

Mr. FRANK. With the exception of the fact that we issue the profit-sharing and interest-bearing certificate, and to that extent encourage the employee to save his money. Beyond that I would answer your question "Yes," namely, that we pay them a good wage, we pay them a liberal profit sharing, and beyond that the money is his.

Senator VANDENBERG. Mr. Frank, on the question of incentives, you made a rather interesting publicity suggestion in your letter to the committee. Would you care to say a word about that?

Mr. FRANK. Well, I will speak guardedly about it. I can see, of course, one of the purposes of your committee is to try to determine whether there is a feeling for incentive legislation, or whether there is a possibility of that thing. In my written comment I think I said that as far as I had gone with the subject I could not favor incentive legislation, because it is not clear to me how incentive legislation can be framed that will serve the purpose. Now, of course, if incentive legislation can be framed, that would encourage a company like ours to do what we are doing, and then would reward us in a financial way for doing it, why, we could hardly be opposed to it, but I am a little bit afraid of abuses under such a system. I fear that a law of that kind would have to be constructed very, very carefully at least to prevent abuses. Therefore, I did not want to be completely destructive, so I thought I would try to be constructive and suggest something else. As far as we are concerned in our company, frankly, we think the virtue of having a good profit-sharing system is its own reward, and that is not for any altruistic reasons at all, but it is purely and simply good business. We have succeeded in a modest way. We have succeeded to the extent that we build a product that is well thought of, and the employees remain with our company. We consider it is well off. They like to own stock in the company and live and die happily with our company. So it seems to me that that in itself is enough reward.

At the same time, if this business of profit-sharing is a gospel that ought to be spread to others, either because they have not heard of it or because they do not understand it, then perhaps it would be wise to have some kind of reward, and I suggested there, in my letter, I believe you might give some form of publicity, because, after all, nearly everybody, every company can use publicity, and likes publicity. I have not tried to think that through. I do not know what form of honor roll it would be, what type of button or insignia could be used, but it seems to me that something like that could be worked out.

Senator VANDENBERG. Now, bearing upon your suggestion, which you do not need to be too timid about, I happen to have a very interesting letter from Mr. Charles Baird, president of the Council of American Industry, with headquarters here in Washington, and from that I will quote the following sentence:

> For example, there is, as you well know, a wide, latent good will among consumers toward the plan of sharing profits with labor. If even a few manufacturers would now unite to publicize the fact that their profits are made under profit-sharing conditions, a tangible beginning would have been made, a center established around which a great movement might grow.

In other words, here is a suggestion that those who are profit sharers might well afford to say so themselves to their consumers, and that it would rebound to their definite advantage.

While I am on this letter it would be interesting to add the following: This Council of American Industry, points out that while general wage advances increases consumers' prices approximately $1\frac{1}{2}$ times faster than wages rise, yet that payments through profit sharing do not enter into the production cost base, and therefore do not increase consumers' prices.

That is another reason why the consumer might well be interested in the institution of profit sharing.

Mr. FRANK. Yes.

Senator VANDENBERG. On the question of direct incentives, Mr. Frank, I think the subject is not very well understood either by the public or by us, because it is a rather nebulous thing as yet, but suppose, for instance, you were permitted to set aside extra profit in profitable years for reserves to provide unemployment and other benefits in bad years, would not that be a definitely advantageous thing not only for business but also in building up the resources with which to combat unemployment periods?

Mr. FRANK. My inclination is to say "yes."

Senator VANDENBERG. Well, that is what we seem to find in connection with incentive taxation all through the discussion. I can fully understand why a business man would be very skeptical and critical in confronting the general abstract question, yet when you break it down and start in with concrete facts, there is immediately a hospitality for the idea, which frequently is lacking in respect to the general aspect.

Mr. FRANK. I can see that.

Senator HERRING. Unless you have something else that you would like to suggest, Mr. Frank, we appreciate very much your being here. Thank you.

Mr. Reith.

STATEMENT OF GEORGE REITH, HOIT, ROSE, AND TROSTER, NEW YORK, N. Y.

Senator HERRING. This is Mr. George Reith, formerly statistician for the National City Bank of New York.

Mr. REITH. Thirty-three years ago.

Senator HERRING. We have this statement. Did you wish to put this into the record?

Mr. REITH. I want to read that, if it is all right with you.

Senator HERRING. Just go right ahead.

Mr. REITH. Perhaps I might preface what I want to say by saying that my story here has to deal with theory and not with any practical relation to profit sharing. Is that all right?

Senator HERRING. Yes, sir.

Mr. REITH. I have had more or less practical experience during my life. With the City Bank, as the chairman said, and after that I was a bond broker, a foreign exchange broker, a dealer in bonds, and an employer and employee, as most people have been, and 12 years ago I retired from business. I have been thinking a great deal about this matter for 20 years, and in the last 2 years I have been trying to put my ideas into concrete shape. It may not meet with your approval, but I will do the best I can.

Senator HERRING. Yes, sir.

Senator VANDENBERG. Your thesis is not directed to profit-sharing, is it, Mr. Reith?

Mr. REITH. Profit-sharing is the central motive in it.

Senator VANDENBERG. All right; go ahead.

Mr. REITH. I greatly appreciate the invitation of this committee to state my views on certain aspects of profit-sharing and incentive taxation, about which I have been thinking for many years. I have a plan. It is distinctly pro-capitalistic and democratic, but yet, because it is based upon some original ideas, it may seem to be radical upon first consideration. Perhaps, if I state at the outset that its central objective is balance, balance between consumer buying power and producing capacity, the need for novel treatment will be revealed. For no one, so far, has been able to crack that nut, least of all the New Deal administration, which spent 15 or 20 billions of dollars in experimental attempts to do so. The plan I propose is on a pay-as-you-go basis and it demands of citizens the surrender of only those rights which, I maintain, have been of imaginative benefit to them. I may not be able to convince you at this time that my plan is feasible, but I hope that a thought or two may emerge which will aid in your survey and perhaps sow the seed for the correct solution of several pressing problems.

Because men live in large communities, their natural individualism requires control by government. One of the important purposes of government is to encourage productivity, because it is the chief foundation of comfort, culture, and happiness. Production in a high degree can be attained only by cooperation between many individuals. I think you will agree that increased production is really a prominent purpose of the legislation contemplated by this committee.

To bring about cooperation, two methods have been utilized by society, through government, in the past. One was based upon physical force. Of old, the means were called autocracy, oligarchy, feudalism, slavery, or serfdom. Now we recognize them in communism, fascism, and nazi-ism. I call that method enforced cooperation. The antipathetic objections to it by those who prefer democratic institutions need not be reviewed.

Senator VANDENBERG. Does that include the N. R. A. and instrumentalities of that nature?

Mr. REITH. I would not call the N. R. A. that exactly. It was a sort of in-between. That is New Deal stuff. It was an attempt to use force without the ability to use force, I should say. Is not that a correct description of it?

Senator VANDENBERG. I do not know. The little tailor went to jail.

Mr. REITH. The other method is based upon freedom, upon the belief that, by wide latitudes and incentives, unstinted exertion is inspired. I call that method voluntary cooperation. The great benefits that follow from it, however, are tempered by serious defects which often threaten its very existence. Laissez faire and demand and supply laws do not always function to the best advantage. Many claim that distribution is inequitable and therefore oppressive. I choose to disregard the question of equity and to criticize this method because of certain economic inefficiencies which persist under uncontrolled laissez faire. I firmly believe that these inefficiencies can be remedied, and that by remedying them more just equities would follow as a natural byproduct.

For many years it has seemed to me that the best way to obtain that cooperation and yet retain freedom, without its anarchical tendencies, and yet preserve incentive for effort in place of force, could be found in a third method—one which has never been attempted on a comprehensive scale. To distinguish it from the others, I call it induced cooperation, for its purpose would be to persuade each individual to compel himself to cooperate for the common good. That laudable objective would be accomplished by adopting devices for mutual benefit which, if departed from by the individual, would work out unfavorably for him.

Thus, there would be no need for force, nor for reliance upon the vacillating moods of voluntary consents. And yet, by the adoption of such devices, the principles of democratic institutions need not be impaired, for they could and should be accomplished by the deliberate will of the people, as by constitutional amendments. All functions of government impose upon individual rights, which are sacrificed to gain greater benefits. The most obvious of all is the power of the police and the courts. In each case it is only necessary to demonstrate that the advantages to be gained outweigh the sacrifices required. This proposal is not as fantastic as it may appear, for the legislation you contemplate is an excellent example of the devices I am trying to describe. Your committee has been making a survey to determine, in the first instance, whether general profit sharing would be importantly desirable. If determined favorably, you would try to induce more employers to adopt it by offering the incentive of tax exemptions as a reward for doing so. Conceivably, if the incentive could be sufficiently alluring, few employers would refuse to adopt a policy from which they would almost certainly profit incidentally on account of the psychological effects it might have upon their employees.

I am not here to give testimony to prove that profit sharing does produce psychological effects which can be translated into terms of money profits. I know you have heard from many representatives of industry who, from practical experience, are able to judge the advantages in efficiency and loyalty which are promoted by profit sharing. Since I have the opportunity, however, I would like to say that from my own experience with human nature, it is my opinion that a worker who has a stake in the business from which he gains his livelihood, does better work than if he is on a flat wage; that the salesman or trader on commission is nearly always a better producer than one who has only a fixed salary. The opinion is often volunteered that the lowly worker has no ambition to share profits and that he could never understand why he should share losses. It is asserted that his sole concern is to demand higher and higher wages. Now, when that narrow view is expressed by an employer, I believe it may be attributed to lack of experience with profit sharing systems, coupled with disagreeable experiences in dealing with representatives of labor. When it is expressed by a labor leader, I am inclined to suspect that it is inspired, in part at least, by the fear that the labor leader himself would lose prestige. How would labor leaders employ themselves if workers and employers could find a basis of harmony of interests? Sharing in profits and losses is the willingness to take a risk, a willingness that every man who goes into business for himself assumes. Certainly, the intelligence of most workers in this country is high enough so that they could acquire that sporting attitude toward life by education and habit.

Nearly all the enactments or proposals to improve the relations between capital and labor since the beginning of the depression, 9 years ago, have been unilateral in character, because of which they could not possibly produce good results. It would not be just to characterize your plan with that defect. As a step toward solving the problems, which so far have defied solution, I am certain that you are moving in the right direction. Because these problems, as I view them, cover a wider range than that implied by your agenda, I cannot get very enthusiastic over the prospective benefits of any contemplated legislation. Yet, I realize that, even if more radical measures are conceded to be necessary, it is still a practical accomplishment to take a sure short step, if by so doing it is likely to lead to the necessary long one later.

The broader objectives to which I referred, are these: Balance, harmony, efficiency, and increased production.

1. Balance: To attempt, through the means of profit sharing, to provide balance between effective consumer buying power and the existing capacity to produce, whatever that capacity may be.

The ancient idea that labor is a commodity, to be purchased as cheaply as possible is not now the creed of all managers of industry. Mr. Ford and others have been stating constantly that wages must be relied upon to provide buying power for the goods produced by labor. Yet one gets the clear impression that they have no plan in mind by which that buying power can be maintained. Nor is it necessary to dispute the claims of those who, like Prof. Willford I. King, assert that in the long run labor gets its full share of the income of production. It is my contention, which is confirmed by the statistics of the United States Department of Commerce, that labor often receives too little and that sometimes it receives too much. That is the true cause of unbalance, and I believe you must concede that, so long as wages are determined by negotiations between the representatives of labor and individual employers, the problem of unbalance will not be solved. Hence, the concern expressed by Mr. Ford and others as to the share received by labor must continue to be academical. Is it not desirable, therefore, to face the problem squarely in its broad aspects and attempt a solution? This is what happens. When capital takes too large a share of the income of production, as it does during periods of rising prices, the surplus goes into excessive productive facilities and we get top-heavy booms, followed by depressions. When employed labor gets too much in a single industry, production in that industry is restricted. When labor gets too much in the aggregate, as it does after depression has progressed, capital is discouraged from enterprise and recovery is delayed. Obviously, the indicated solution is to keep the national pay roll at a constant ratio to the national income and the medium for doing that is profit sharing on a national basis and by centralized direction.

2. Harmony and employee efficiency: To merge completely the interests of the workers and their employers, by removing all the superficial causes for conflict which now exists.

Universal profit sharing would be one factor. Scientifically adjudicated standard wage schedules for classified workers would be another. Actually, wages are not paid by employers. In anticipation of a profit, wages are advanced to the workers by their employers. They are included in the cost of and are recovered from the proceeds of the product when it is sold. Yet, workers and employers continue to quarrel about rates. By the adoption of proper devices, the real basis of conflict could be placed where it belongs—between groups of workers in relation to each other. (This is feasible, because the overwhelming majority of workers should be classified for their own protection and be dealt with as classified groups.)

Because a few craft unions, by monopolistic organization methods, and the rail workers, under the favoring wing of legislation, have succeeded in attaining special advantages, regardless of the ability of employers to pay, is no proof that all workers could fare so well. In fact, a little consideration will show that in the long run these special advantages are obtained at the expense of the other workers in the higher prices they have to pay for the products. To be sure, for the moment, the relatively high wages being received by the railroad employees are being confiscated by Government out of the assets of the holders of railroad securities. The railroads can be squeezed without national calamity, because the whole transportation industry supports only 8 percent of all workers, and not all the railroads are bankrupt—as yet. If, however, the same policy could be applied to industry and commerce, which together employ 43 percent of all workers, private enterprise, and with it democratic government, would be a thing of the past. The fear that labor backed by a sympathetic and, at the time, all powerful administration, intended to make such demands, in disregard of the employers' ability to pay, was undoubtedly an important cause of the prompt return of depression in 1937.

I believe it is because many people in labor, business, and Government still believe, subconsciously, that wages are paid out of capital and not out of products, that such foolish ideas persist. Real balance is the most important goal of all. Owners must realize that when business is good the means should be found to keep them from committing financial suicide by taking too large a share of the profits. Workers must realize that when business shrinks they must accept less all around to prevent wholesale discharges and acceleration of the progress of depression. The so-called right of free bargaining is a pure delusion to the great majority of workers. They never did have that right, haven't it now, and never will. As has been stated, a few workers have placed themselves in preferential positions with relation to other classified workers. If the truth be known, though I have never seen it stated anywhere, that situation is the real cause of the bitter enmity between the two large groups—labor groups—which the President believes he can compose.

Another mirage, now being demanded by spokesmen for labor, is security of employment combined with stability of wages. It must be evident that, except to a very limited extent in special industries and to a limited number of employees, that is a boon that cannot be granted. It might be approximated, that is to say, security of employment might be approached by the means of the fluctuating wage scale which I advocate.

3. Capital efficiency: To provide unlimited incentive to the owners and managers of business, by completely removing the burden of taxes from the back of production efforts.

Income taxes, taxes on corporations, and pay-roll taxes are restraints upon productivity. By removing them—

(a) Capital would seek remunerative employment in the field of production, instead of hibernating in tax-exempt securities.

(b) Corporations, which under proper control, could be made into and limited to their natural function, that of a free implement in the process of production, would be released from present hampers upon enterprise to earn profit and, therefore, to expand production and provide employment.

(c) Creative brains, now in cold storage as the result of punitive tax policies, might be enticed to be withdrawn and put to work. (I shall revert to the subject of taxes later, when I suggest the desirable substitute for penalizing work, in order that government may be provided with revenue.)

4. Increased production: Through the combined operation of these measures, supplemented by such other similar devices as will be necessary, productivity should expand rapidly, for—

Workers would be more ambitious and conscientious. There would be fewer objections from them to inventions and technological improvements. Less insistence upon short hours of work.

The impact upon the owners of capital and entrepreneurs is too obvious to require recital of details.

The mitigation of depressions should cause the volume of productive goods to expand at a faster net pace than that by the violently interrupted curve we have endured in the past.

I have prepared a plan by which I believe these purposes may be attained. I realize that it must be inadequate in details and that it would require much amendment. I submit, however, that it is designed to encourage people to work, that it is consistent with democratic principles and that if adopted, the means could be found to make it operate feasibly. Such a plan is confronted with these obstacles:

1. The requirement of wide educational publicity.
2. The inertia of people who, concerned with their own affairs, are unwilling or unable to give the required attention for understanding.
3. The difficulty of obtaining agreement upon any complicated procedure, even if proof of advantage were undeniable.
4. The opposition of those who consider only the contributions required from them. Cooperation implies giving as well as taking. In this plan, nearly all groups would be required to yield something in order to make gains in other directions. The normal tendency is to magnify a concession and minimize a boon.

VOLUNTARY VS. UNIVERSAL PROFIT SHARING

To be effective in accomplishing the purposes I have outlined, profit sharing would have to be general and be controlled by centralized regulation. It is improbable that profit sharing would be adopted universally, by voluntary decisions, even with tax exemptions. If operated by individual decisions as to rates, its effect on balance would be only casual. Hence, I strongly advocate direct legislation to enforce it. I know that a business executive recoils from the term compulsory as from a malignant disease, especially after the experiences of the past few years. I know also that this committee has emphasized the voluntary feature of its objectives. This is merely my argument in favor of compulsory profit sharing to gain the broader objectives.

I maintain that any form of legislation is, ipso facto, a form of compulsion. In the final analysis, it will not matter much whether profit sharing is directed by law, or whether, by taxing or withholding taxes, employers may or may not be compelled to adopt such systems. If the inducements are strong enough, there will be compliance. If not, the law will be ineffectual. I maintain that compulsory profit sharing would come within the definition of induced cooperation, because employers would be compensated for the payments made by each, through the increased purchasing power for their own products provided by the profits distributed by all other employers.

The following is a brief outline of some features of the plan I propose:

A standardized contract of employment: All employees, classified and unclassified, are to be hired under a uniform contract which will include these fixed conditions.

1. A contract wage or salary for any agreed upon term.
2. Part of the wage to be paid in cash at customary intervals.
3. Part of the wage to be withheld and paid only when and to the extent earned by the employer.
4. Provision for participation in the excess profits of the employer at a localized modification of the national rate, which will be declared periodically.
5. There should be no restriction upon the right of the employer to discharge a worker, or of a worker to quit his job, within the terms of the contract.

Rates of wages: Classifiable workers are to be classified as labor unions are now. The wages of each class are to be fixed upon an hourly basis, by adjudication and determination before the national supervising body. The salaries or wages of unclassifiable workers, such as executives, salesmen, experts, and others with distinguishable individual characteristics are to remain open to free negotiation as now.

Hours of work: To be subject to direct negotiation between employers and employees; but to be limited to determined standards of health for each vocation, with provision for overtime rates beyond those standards, in emergencies.

Capital exemptions: A valuation is to be placed upon each business, with allowances for capital hire, replacements, depreciation, etc. The resulting income requirement would be a prior charge over the payment of the portion of wages withheld. (The latter to be called deferred differentials.) Any surplus, after the payment of the latter in full, to be called excess profits and to be subject to division between employees and the employer.

Deferred Differentials: The rate to be withheld from each employee would advance progressively according to his contract wage rate. Hypothetically, say 5 or 10 percent on wages amounting to $1,000 per annum; 15 or 20 percent on $5,000; and 40 to 50 percent on $100,000. The fixed schedule would be determined, either by law or by the national supervising authority.

Profit sharing: The national authority, after a preliminary survey before the expiration of the distributional period, would determine the required national profit-sharing ratio, based upon the estimated national excess earnings indicated, to maintain the national pay roll at the desired ratio to the aggregate national income. The announced rate would be paid by each employer out of his excess earnings, if any were available. However, the national rate would be modified in each case by the proportion of the local labor cost to the national labor cost. Each employee's participation would be the calculated percentage of the wage or salary earned by him during the period.

Minimum wage: There should be provision for a minimum wage on an hourly basis, as determined by a study of living costs.

The supervising authority: A national board is to be selected by means appropriately to ensure competent and distinguished personnel. Most of the details of administration would be performed by local boards, in a national organization similar to that of the Federal Judiciary. The main duties of the Supervising Authority would be:

(*a*) To fix the wages of classified workers, and to make such later adjustments as may be desirable.

(*b*) To supervise the valuations of employers' businesses.

(*c*) To determine and announce the national profit-sharing ratio.

(*d*) To adjudicate differences between employers and employees, and between different groups of workers with each other.

Permanent Government relief: In view of the great producing capacity of this country, I am assuming that no citizen, however unworthy, will be allowed to starve. Hence, the cost of relief should be a public charge out of the general revenue of Government. The temporary or permanent relief extended to unemployed or unemployables should be at minimum subsistence rates. No person, able to work, should be tempted to prefer relief. Old-age pensions should be provided to all who can prove personal inability to provide themselves with comfortable support. The rates of old-age pensions should be determined by the ratio of the number of beneficiaries to the aggregate productivity of the country. Thus, such pensions might be meagre under present conditions; whereas, at some time in the future, they might be very lavish. I guess that has been very hard to follow.

Senator VANDENBERG. It sounds a little like Henry Wallace and the triple A to me.

Mr. REITH. No; I do not think you follow it really, because I started in an argument with Mr. Wallace and I found he was on one side of the fence and I was on the other.

Senator VANDENBERG. That encourages me to read what you have written.

Mr. REITH. I wish you would.

GRADUATED CONSUMPTION TAXATION

I would like to amplify, briefly, the reference I made earlier to taxation. The radical tax policy, which I advocate, is not indispensable to the operation of the profit-sharing plan, so, for that reason, I prefer to discuss it separately. Nevertheless, I observe that your committee recognizes that there is an affinity between the policies of taxation and labor-capital relations, by proposing to combine them in legislation.

Tax gathering has always been a crude business. The old way was to shake down those who could offer little resistance for whatever could be taken from them without destroying them. I do not think it has changed much, for I believe the present methods are unscientific, inequitable, and even hypocritical. Lawmakers proclaim lofty aims, such as taxation "in proportion to ability to pay," and for the purpose of "social security," but under analysis taxes generally are found to be levied where they are easiest to collect. People are taxed whose squeals annoy the least. But the most serious indictment of the present taxing policy is that it is a blight upon the productive energies of the Nation as a whole. Surely, if it is conceded to be desirable for government to encourage citizens to work it cannot also be wise to penalize them because they do. The chief sources of revenue for government at present are income taxes, corporation taxes, and pay-roll taxes. All of them penalize human exertion.

Now, the common reply to that criticism is that taxes must be collected from those who can pay, but that is merely an admission that they are sought where they are easiest to collect. Those who oppose incentive taxation on general grounds must assume that taxpayers are just so many milch cows, without emotions or impulses. The fact is that all taxes impel actions of some kind by the taxpayers, which implies that it is logical that those actions be directed to beneficial rather than to harmful ends.

The obvious alternative to taxes on production are taxes on consumption. I know that spendings taxes are not new. We have many of them now in the form of the unpopular sales taxes, which are visible, and the many ingeniously concealed taxes, which are paid unsuspectingly by consumers. These, however, are levied horizontally, and as a result fall with great severity upon people with low income while those with high incomes do not notice them; and, in fact, keep asking for more taxes of that kind. Is that right? I think that is right. There is a demand generally for a means to extend the consumer taxation.

Senator VANDENBERG. That is right.

Mr. REITH. An equitable consumption tax would be one graduated geometrically to the aggregate annual spending of each taxpayer; for by that means the monopolizers of the labors of the masses would pay adequately for the privilege. Moreover, there is an equitable and feasible way of collecting according to ability to pay.

I know that the idea of progressive spendings taxes is also not new. Economists and lawmakers have proposed such taxes in the past. But I believe that the tax, in the form in which I advocate it, is new. Former proposals were imitations of the income-tax principles, with many exemptions, including the usual exemptions of, say, $2,000 and

$4,000 for single and married taxpayers. With such exemptions 80 percent of all spending would escape, so that there would be inadequate foundation for Government revenue. That 80 percent which is always proposed to be exempted because it is visible is now taxed by the invisible, inequitable, and hypocritical methods now in vogue.

The common antipathy to paying taxes, inherited from government by force, is fanned by many of the guileful methods now in vogue. I feel certain that the citizens of this Democracy could be taught to pay taxes as cheerfully as they now pay the cost of rent, groceries, or the movies, if each could be made to believe that he was paying his proper share. I also believe that the popular recognition of such an obligation would tend to make better and more alert citizens of all.

I would propose that the head of each family or single individual should be required to report his total annual spending for consumptive purposes, allowing no deductions except amortization on articles of slow use. The rate of tax would be very low for the small spenders, and would rise in rapid progression proportionate to high spending. For example, the rate might be as low as 1 percent in the low areas and as high as 100 percent in the high altitudes.

By this method, taxing would be simplified. Within the practical limit of aggregate ability to pay, the graduated consumption tax rates could be made to fluctuate with the Government budget. Tax lobbying would also be simplified for the sole opponents would be the high and low spenders. The bulk of Government revenue would thus be provided for by the graduated consumption tax, being supplemented by heavy inheritance and gift taxes, customs and excises to discourage the consumption of articles of a deleterious nature.

It is conceded that a tax on spending would restrain spending somewhat. Compared with the influence of taxes on production, however, it would be negligible. The impulse to work is easily discouraged, whereas the impulse to spend is imperative. Statistics show that a great majority of the people spend nearly all of their incomes anyway. It is also true that an alarming number frequently spend more than their incomes, by installment buying, especially in periods of prosperity.

I hope I will be excused for digressing somewhat from the immediate subjects of your survey. I thank you.

I also want to add that I do not expect that you are going to approve of what I am recommending here. I think I am about 50 years ahead. It will not happen during my lifetime, I am sure, but I do believe it will come at some time. I will appreciate it if you will read it over carefully later on.

Senator VANDENBERG. It is a very interesting discussion, Mr. Reith.

Mr. REITH. Is there anything I could add to it?

Senator VANDENBERG. No; I think not.

Senator HERRING. Unless you have some other suggestions, or anything else you would like to put into the record, Mr. Reith, I think that is all. We appreciate your coming here. We have been watching for your new book. When does it come off the press?

Mr. REITH. Mr. Despain has a copy of the manuscript. It provides the argument in detail for the things which I advocate. I hope that your time has not been wasted.

Senator VANDENBERG. No indeed.

Senator HERRING. We appreciate your contribution very much. Thank you, Mr. Reith.

We will recess until 1:30.

(Whereupon, at 11:30 a. m. a recess was taken until 1:30 p. m. of the same day.)

AFTERNOON SESSION

(The hearing reconvened at 1:30 p. m., pursuant to the taking of a recess.)

Senator HERRING. Are you ready to proceed, Mr. Joslyn?

Mr. JOSLYN. Yes, sir.

Senator HERRING. This is Mr. M. L. Joslyn, president, Joslyn Manufacturing & Supply Co., Chicago, Ill.

Proceed in your own way, Mr. Joslyn.

STATEMENT OF M. L. JOSLYN, PRESIDENT, JOSLYN MANUFACTURING & SUPPLY CO., CHICAGO, ILL.

Mr. JOSLYN. I am going to be a little personal, which I hope you won't mind.

In spite of the serious illness of my wife, I have come here from Los Angeles and brought my private secretary from Chicago, Mr. Joseph Roeder, in response to your call. If the remarks I make appear somewhat rambling and disconnected, I am going to plead lack of leisure to make them otherwise, and I hope my good intentions will be some excuse.

I was handed a copy of the Wall Street Journal of last week with an article on our plan so clearly presented that I was tempted to abandon my own statement and read theirs to you, but after all I am a witness and so must give original testimony, even if it could be presented or better expressed elsewhere.

I understand it is permissible to read a statement and as I am not a speaker but a plain business man, I am taking advantage of that permission.

Senator HERRING. Yes, sir.

Mr. JOSLYN. The scope of your inquiry includes a study of existing profit-sharing systems, and I assume you wish from me a full frank statement of my experience under such a system, maintained by the interests which I represent.

It is customary for any witness giving evidence of an expert nature to properly qualify—I hope it will not be mistaken for egotism if I proceed to do so.

I was graduated from the University of Notre Dame in 1893, and from Harvard Law School in 1896. Very shortly thereafter, I abandoned law for business, because, strange as it may seem, I regarded business as the higher profession, affording more intimate, vital, and permanent contacts with human nature, stripped of all pretense and make-believe.

I think I was, at least potentially, a Socialist. I certainly believed in the best possible for the greatest number, but I also had an abiding faith in the scientific method of finding the best possible, by trial and error, through patient and cautious experiment.

My business ventures were steadily successful and a basic factor in their success was the profit-sharing idea, which was invariably present in all my plans. I believed that no business deal was of permanent value unless it involved a profit, not only to me and my interests, but to all parties concerned and a profit equitably shared, and I found this prospect of sharing brought out unknown values in my associates and proved a powerful incentive to their utmost development.

Every joint effort in which I was involved seemed to secure better than average results, through this cementing and strengthening of individual endeavors, by profit sharing. People told me that I was uncommonly lucky—that I had a rabbit's foot. I did! My rabbit's foot was profit sharing.

As employees in my charge grew in number, I was determined to use this human laboratory for experiments in extending the profit-sharing idea, even to common labor.

So much for my personal qualifications and the attitude I assumed 40 years ago toward this problem now under your consideration.

At the beginning of this century, not very much was being done in this direction, but we proceeded to try some of the most obvious methods.

One by one they ran up against humanity as it actually exists, not as we would like to have it, and were disposed of as impractical or inadequate.

Many features of plans that are being tried or considered today, went through our tests and were discarded, and it is my conviction that the great number of failures of profit-sharing plans in the past is largely attributable to inherent weaknesses in the plans themselves, not to the principle involved in profit sharing. Wishful thinking is desperately attractive, it is so much easier than factual demonstration, but things worthwhile have to be built on facts, not on desires or hopes.

After some 20 years of sincere honest trial and error had eliminated cash bonuses, employee control of business policies and of casualty liabilities, cooperative merchandising, short maturity plans for social betterment, and many other ideas, we adopted our present plan in 1919 and are just closing its twentieth year of operation.

Here is a digest of the main features of the plan, established, as its preamble reads—because the Joslyn Co. was desirous of distributing among its old and tried employees, a certain portion of its net earnings, thereby stimulating in them a keener interest in its successful operation and at the same time encouraging a spirit of economy and thrift, which may stand as a protection against the vicissitudes of old age.

Employees who have been in continuous employment with the company for 3 calendar years must sign the plan agreement or leave the company. We were told that was very arbitrary, and we replied that any employee who hadn't brains enough to see the tremendous advantage to him in the proposal that we were making, was a man we didn't want in our employ.

The agreement provides that there shall be deducted from the wages of the employees not more than 5 percent, nor less than 2½ percent, of their wages each pay day. That is an option which, in the entire 20 years of the operation of the plan, has never been exercised. One hundred percent of the employees have paid the 5 percent.

These deductions are paid in to the employees savings and profit-sharing fund and are held and controlled by a trustee, acting with the approval of an advisory board of five, the trustee being one of the five, two officers of the company appointed by them, and two elected by the employee members. The yearly payment to the fund, by a member, is limited to $200. That amount is 5 percent on $4,000. We are not so much interested in the men who earn or get more than $4,000. The company agrees to pay to the fund, at the close of each year, not less than 10 percent of its net operating earnings, but not exceeding four times the amount paid in by the members for the same year.

I might make the comment here that we started that with 5 percent, that at the end of three years the plan had done so much for us that we kept on overpaying each year, and at the end of about 13 years, we had averaged 9 percent, so we changed it and said, "If we voluntarily pay 9 percent, let's make ourselves pay 10," and by the way, we are paying 12½ this year, though our agreement says 10.

It is required that the funds, paid in by members, must be invested in securities approved by the State of Illinois for investment of trust funds. The funds paid in by the company and accumulated interest may be invested as approved by the trustee and advisory board. Under that clause in our experience we have invested almost exclusively that portion of the fund in our own preferred stock, having five times its value in security and the fund now holds one-half of our issue of one million and a half dollars of preferred stock.

When a member becomes 60 years of age, or is disabled, he receives from the fund the entire amount to his credit there. We do have a clause which perhaps some people call paternalistic, under which, if the advisory board decides, after consulting a man as he is arriving at 60, that he is going to throw away this money, we have a right to exercise an option to pay him in 11 yearly payments with interest, carrying him through his seventieth year. If he is discharged or leaves the employ of the company before reaching 60, he receives all that he contributed to the fund, with compound interest, and one-half of the company's contribution, with compound interest, the remainder falling back into the general fund, and going to increase the credits of the other members—no part of it ever coming back to the company.

You will note when Mr. Roeder, my secretary, gives you the figures, which I am not going to try to give you, that in 20 years the fund has averaged an earning of over 8½ percent, which is a very important factor in the accumulation to the benefit of the profit sharer, and that comes from the men who fail to go through with the plan. It is the old "reward and punishment."

If a member dies his entire credit goes to his appointed beneficiary. The members interest is not attachable for debt. Our provisions in that respect have been tested in the courts three or four times and they have been held to be absolutely unassailable. No one can touch the money for debt.

There is a provision for cooperative life insurance during the first 7 years of membership, in progressively decreasing annual amounts, so as to insure at least $2,000 to the beneficiary if death occurs during these early years of membership.

While loans to members from the fund are discouraged, the advisory board may, in emergencies, make such loans, but until repaid, the member ceases to share in company contributions and his own payments to the fund apply first on his indebtedness.

During the great depression we made loans—I think Mr. Roeder will check me on this—up to $20,000 or $30,000, didn't we, Mr. Roeder?

Mr. ROEDER. About $32,000.

Mr. JOSLYN. Not a man, not a profit sharer in our company ever took a dollar from State or Government or city or anybody else, or had any difficulty in going through the depression. The public was relieved entirely from any charge of those men, and at the present time there is $4,000 due the company. In other words, they paid it back rapidly as soon as they were reemployed. They were enabled to take care of any small temporary unemployment that occurred entirely from their own resources. They didn't need the company or anybody else.

The fund agreement may be amended on recommendation of the board of directors of the company and approval by members representing 51 percent of the fund credits.

The advisory committee may formulate rules and regulations for the management and distribution of the fund, not inconsistent with the provisions of the agreement.

This is the substance of the agreement aside from provisions for carrying it out. There is nothing complicated about it, nothing elaborately contrived or hard to understand. It was not the result of any brain trust. It grew out of long operative experience. Voltaire was once asked to condense his philosophy in a few words. He replied, "Work in your own garden." That was what we did and this natural product resulted.

We sought no praise or criticism. It was not enough to make something that looked good. It must be tried by long experience. After 18 years, including the great depression, not a cog had slipped. The Rockefeller Foundation employed the University of Pennsylvania early in 1937 to investigate all existing profit-sharing plans and report on same. Prof. C. Canby Balderston was in charge of this investigation, and his book, Profit Sharing for Wage Earners, was the very competent result.

During his researches he ran onto our plan, which he published in full in his book, writing me a letter in the course of our correspondence from which I am very gratified to quote, with his permission, as follows:

> Of the 165 American plans that I have uncovered so far, yours appears to me as the one that I would be most willing to bet on.

I hope I have qualified as entitled to testify. The above quotation is expert qualification for the plan itself.

Neither of these qualifications would be enough without the knowledge of how the plan has worked.

That I propose to give you both directly and in response to any questions you desire to ask. Before welcoming those questions I am going to impose a little further on your time and indulgence by a few statements and quotations from past addresses, which will tend to throw light on our plan and the atmosphere in which it was created and is being carried on.

Quotations from an address to our own sales convention in 1937, with extensions bringing it up to date:

One of the most serious responsibilities of administration is the equitable distribution of earnings between capital and labor, and between various classes of labor. The old idea that capital should get all it could squeeze out and still keep labor functioning is rapidly fading out and in its place is the new one that labor should get all it can secure and at the same time keep capital functioning. This change of emphasis is a complete industrial revolution and a distinct moral advance.

Our profit-sharing plan is simple, as all things are which work smoothly. It accomplishes several desirable ends It enforces saving and makes it very acceptable by returning an unusually high rate of interest. It offers a reward for continuous satisfactory service, and a penalty for failure to give it. It provides adequate life and disability insurance. It protects old age, and even operates to relieve unemployment, because of borrowing possibilities, either within or outside the fund, based on the standing of the member in it.

For 20 years we had always been striving for some practical plan to progressively advance the standing of employees in the corporate structure, without at the same time so weakening that structure as to endanger its very existence. We tried all kinds of temporary plans. One was to give every employee at the first of the year a certificate which stated the amount of his wages for the year just completed. This certificate was held a year and then turned in to the company and its holder received in cash the same share of the year's earnings of the company he would have received if he had held a stock certificate for an amount equal to his earnings.

That was something like 35 years ago, and it was received with such astonishment that—well, they didn't think it was possible. And to give you an idea of just the effect it had, we had a red-haired German stenographer. We happened to have an exceptional year, one of the best years we ever had, and her share was $360. We handed her a check for $360. She took it home. The next morning she came in and laid the check down and said, "I am sorry, my father told me to bring this check back, hand it in to you, and to tender my resignation." We said, "Well, why?"

"I would rather not tell you."

Well, we pressed her, and at last she told us:

Father said that any company that were damn fools enough to pay a stenographer $360 more than her wages in a year was either about to go into bankruptcy or they wanted something from her besides stenography.

[Laughter.]

We managed to convince them that our intentions were honorable. [Continuing:]

These dividends on wages were well received, but coming in a lump sum, were usually spent quickly, often wasted, frequently badly invested and lost. There was no continued improvement, no constant incentive to good work and no accumulation of property and protection for old age. They did carry out to some extent our idea that everything the worker receives should be definitely determined, as a right in return for service, not in any sense as a donation, but they built up no permanent security or benefit. This was only one of a dozen similar plans tried and discarded, until we finally began to see the outlines of a system that would be foolproof and automatically get the desired results.

It seemed to us that constant turnover of labor was bad for both company and employee. In 1919 only a small percentage of our ordinary laborers had been with us 3 years. We were in the heart of an industrial district in Chicago and with the after-the-war restlessness, labor drifted from one employment to another. Could this be changed and a real loyalty to the company interest be created? We believed it could if men could be convinced that the company was loyal to them and was building toward something better for them than they could get anywhere else, and yet something entirely possible and within the limits of sound business procedure.

There was at the time much confusing talk of partnership between labor and capital, but little real attempt to move in that direction, because the difficulties in the way were enormous. Capital in emergencies could live on itself for a time or take great losses; labor, having no reserve, could not do that. Any real partnership could only be based on the laborer first becoming a capitalist himself, but how was that to be accomplished if his weekly wage was just enough to pay his bills every Saturday night, or if his small savings were the prey of a hundred get-rich-quick schemes, which his experience gave him little ability to avoid.

We believed the common laborer, working year after year for a normal wage, with nothing but Saturday pay day to look forward to, with no consciousness of steadily bettering himself, lost hope and energy and delivered to his employment only part of the value he was capable of producing under happier conditions.

We believed that the view ahead of a penniless old age, dependent upon relatives or charity, cast a shadow of fear over his life, and that the removal of that fear would actually pay in dollars and cents to the company with whom he labored.

Then, again, men with nothing have little reason to protect property—why should they? Men growing steadily well-to-do, building a strong security for themselves and their families and feeling that they are doing it from the product of their own efforts are proud and happy in their achievement and will fight for its protection.

These are a few of the many thoughts from which our profit-sharing plan was born. Remember this was not a charitable idea at all, it was a proposal to see whether ordinary men could respond to a certain betterment of their condition and prospects, to an extent that would actually make it pay. We believed they could and within reasonable limits, the more unusual the betterment, the more certain the response.

We wanted to protect old age in our plan. It was the fashion then to grant pensions after 60 or 65, usually a small percentage of the wage at the time of retirement, never the full amount.

Placing ourselves in the position of the worker, this gave us no picture of a happy old age, but of an old dog in a corner being thrown a crust. It might be a lifesaver, but it certainly was not an inspiration. No man would work better and more cheerfully all his working years because this was his final reward. So such pensions seemed to us to actually be bad business investments. A man in his prime can do without much money. Health and strength enable him to laugh at hardships, but as age comes on and strength begins to fail money can do more than ever before to make life acceptable, even to make it enjoyable. It can create independence and command the respect that independence always merits; it can buy suitable climate and food and surroundings, command complete care and expert attention; it can carry one pleasantly through without asking or requiring favors of anyone. So, we reasoned, under our plan, to get a real response, we must have a prospect in old age, not of less of the good things of life, but more, so that the vision ahead is of something better than ever experienced. We were told this was impractical, an unrealizable dream; but we proposed to try it and see whether it would pay. We have tried it for 20 years, and it does pay.

We estimated the fund would average to earn 6 percent, with the benefit of the money left to the credit of others by members discharged or resigning. We hoped to pay as high as four times as much into the fund each year as the members paid. On this basis we figured that a member contributing $100 a year would have to his credit at the end of 20 years about $22,000, and if he started in the plan at 30 and retired at 60 he would have nearly $45,000. This meant a fortune for the worker, providing him 6 percent on $45,000, or $2,700 a year for the rest of his life, or giving him a capital of $45,000 to handle as he pleased, or having it available to leave to his family for their protection, or; as many do, using it to buy a large interest in the company's premier security, as he thought best. This is actually creating capitalists from workers and thus making it possible for them to become real partners in industry.

But could it possibly work? We have now 20 years' experience. For 11 years, and until the great depression, we always paid 20 percent of the member's pay roll to the fund. In 1930 we were compelled to reduce this to 6½ percent; in 1931, 1932, and 1933, in the worst times ever known, the company made no profits and could pay nothing. In 1934 it paid 2 percent; in 1935 it paid 5 percent; in 1936 it paid 10 percent; in 1937 it returned to its 20-percent program; and while 1938 was a much poorer business year than 1937, we will pay a large part, at any rate, of this percentage.

The depression cut down our 20-year estimate, made at the beginning; but on the other hand our earnings on the fund during 20 years, instead of averaging 6 percent, have been over 8 percent. We actually have to the credit of a member who has paid in $100 a year for 20 years $19,718. So with 5 of the worst years ever known we are about $2,300 short of our $22,000 estimate. Another 20 years is likely to average better. Putting it another way, the member has approximately 10 times the amount of $2,000 he contributed in the 20 years, and on our actual experience he will have over double that in 30 years.

From an address to the Illinois Manufacturers Association which I prepared in California and which Mr. Roeder delivered, and after which, by the way, by noon the next day six Chicago corporations adopted our plan, I take the following:

> Our experiments over a long period of years, before adopting our plan, developed certain convictions. We had established goodwill and loyalty, especially with our white-collar men, and had gathered an exceptional management. But with the rank and file results were transient or doubtful and not in proportion to the expense involved. We decided that business must operate entirely apart from any philanthropic purposes, and proceed only when, after looking all the facts in the face, it was reasonable to assume the procedure contemplated would pay adequate returns to the capital employed.
>
> Religion has been defined as emotionalized morality. In the realm of ideals that emotionalizing is undoubtedly stimulating and effective; but in the realm of economics, we decided that the greatest error, at least in our experience, had been just that attempt to emotionalize a machinery which must run steadily under all kinds of conditions, foreseen and unforeseen.

Emotion is from its very nature unreliable and as varying as the wind, both in force and direction. It may prompt ideals, but to expect a uniform response from its application on a large scale to vastly varying individuals, being molded into a cooperative effort, is reaching for the moon and you just don't get it.

We decided, therefore, to try to evolve an unemotional plan, based on hard facts, and universal motives, as far as they could be discovered and made adaptable to the ends we deemed desirable.

Here was our background of facts, as we saw it. Our plan must appeal to and be workable with capital, management, and labor, without impairing the interest of the public who make up our market, and if possible containing an appeal to them as well.

Capital has been much and improperly maligned because of abuses which are inherent possibilities in every instrument through which power can express itself. Only a misanthrope would condemn life because of its disappointments. The normal mind would welcome it as an opportunity, striving to grasp all its good and minimize its unsatisfactory features or developments. Capital was the forerunner of democracy, the instrument for smashing the rigid class molds of feudalism. It is today the common meeting ground where all men may strive alike with no prize impossible. But, whether we like it or not, this is still a capitalistic age and it must be so recognized, until in the slow evolution of ideas something better has taken its place and proved workable.

Capital has one invariable purpose, always to be relied upon, the securing of as large dividends as possible.

Labor also invariably seeks the best possible wages and working conditions, as does management as well.

The public always is vitally interested in getting the best product at the least expense.

In spite of all the pretty assumptions as to the probable behavior of men, there is just one thing we can always rely upon, self-interest, and a working hypothesis must appeal at all points to this incentive, if it expects a response.

Our plan must therefore promise to develop larger or more reliable dividends or capital would not respond, it must hold out the prospect of improved conditions to the workers and management to retain and stimulate them, and it must result in service to customers meeting their quality and cost requirements. A pretty large specification it would seem.

Above all, the plan must be simple and work automatically toward the desired results.

We had a large labor turn-over just after the war. Everyone was suffering from the same conditions. From the standpoint of capital, the plan was an experiment worth making, if for no other reason than to correct this evil. It went into operation January 1, 1919. At first it met with some doubt and suspicion that it was designed to offset low wages. We promptly announced that our wages would always be as high as those paid by our leading competitors, as they had been in the past, usually higher. This wage integrity is an essential foundation for the plan which would be a sham without it. At the end of 3 years all abnormal labor turn-over was ended and efficiency increased so greatly that every foreman reported its increased value exceeded the cost of the plan. This profit result has continued ever since, capital, therefore, has been satisfied.

We have produced better and better material at lower cost, our business has grown, our customers praise our quality and service, the plan has satisfied our public.

We have never lost a manager, salesman, or office man of any standing during the last 20 years. Management must be satisfied.

Coming to the question of labor's reaction, we have never had one moment of labor trouble in 20 years.

I might add that we have never had a demand of any kind from workers. They seem to have such perfect confidence that they are getting a square deal that we have never had anyone demand anything. [Continuing:]

For every $100 per year paid into the profit-sharing fund for this period, there stands to the credit of the employee $19,718 as of the close of 1938. He ought to be, and he is, satisfied.

Is there anything unusually favorable to these results in our business? We think not. It is openly competitive. We have practically no patents or special privileges. Anyone can do anything we are doing and a great many are doing the same things.

Senator VANDENBERG. I think, for the record, you might indicate what your business is, Mr. Joslyn?

Mr. JOSLYN. It is very hard to do so. Our original business was the manufacture of everything that goes on power lines outdoors—that is, the poles, the hardware, the insulators, the strand, everything that goes on a pole except the wire; but we are very diversified. We have two steel rolling mills and an electric furnace. We make stoves; we make refrigerators; we are the largest manufacturers of little dispensers and sprayers that go on the tops of bottles, in the world, ship them all over the world. We wreck buildings. We wrecked the World's Fair. We bought the World's Fair in Chicago and wrecked it. We deal in machinery and do a great variety of things tied in together. Our theory has always been that we would do anything that happens to pop up, whether it was in our line or not. [Continuing:]

We are paying 20 percent bonus to our profit sharers this year (this was last year that this was written) on wages fully up to competitors, which means in many lines we are actually paying 20 percent more wages. How can we do this and compete after assuming the tremendous tax burdens and restrictions to which all business is subject? The best answer is our balance sheet. Our 150,000 shares of common stock, 30,000 shares of which were issued to the public at $45 a share in 1937, earned in that year over $5 a share and will earn in 1938 over $3.50. Certainly, our plan needn't frighten capital. We do not think we have the only plan or the final best shape in which to formulate it. The thing we do have is something that has worked, and we offer our experience for others to build upon, modify, or improve as men continue to think clearly toward better ends.

I confess to approaching my subject in a very roundabout way, but after all that may be the most certain method of encompassing it.

I must now refer to the provision in our profit-sharing plan that the advisory board may enact temporary measures not inconsistent with the agreement itself, and may interpret the terms of the agreement. This provision really gives the board a limited legislative and a considerable judicial power. It may fairly be said that our fund agreement is our constitution, and our advisory board our judiciary, our trustee our executive, with restrictions of judicial council, and at the same time the board and trustee together may evolve experimental legislation which, after trial, may in time become a constitutional amendment to our basic contract, by submission to all the members, and a majority approval.

When the pronouncements of the advisory board do go beyond clarification and interpretation, or methods of procedure, and take on an original legislative aspect, there should be a provision that on petition of one-third of the membership such legislation shall be put to a vote of the entire membership; and if disapproved, immediately nullified or withdrawn.

In actual practice, we find it desirable and practical to submit such proposals, informally, to the entire membership before adopting them, asking especially for objections, and endeavoring to be certain of general approval before the board takes any action. The board retains the power immediately to discontinue such a measure, the moment it seems undesirable. Thus, we have the power to experiment tentatively, adopting later, in our basic agreement, only measures amply tested by experience. Here are some samples from rules approved by the advisory board and now in force—and you will note that they are all for the benefit of the common man. [Continuing:]

In case of the discharge by the company of any employee who, at the time of discharge, is a member of the fund, in good standing, such member may, within 3 days after such discharge, file with the advisory board a written protest, setting forth his reasons why he considers the discharge unreasonable or unfair, and on receipt of such a protest, the board shall at once notify him of a time and place of meeting, at which the advisory board will hold a hearing on the case and a vote of the board be taken, and unless four of the five members of the board sustain the discharge, the member so discharged will be at once reinstated, otherwise the discharge will stand as made.

I call your attention to the fact that one of the company employee members of the board must vote for the discharge, because they have two out of the five members. Therefore no man may be discharged without his fellow worker's vote. [Continuing:]

The provision in the fund agreement by which a member may be retired for "disability,' with payment to him of his full credit in the fund, permits of the interpretation by the advisory board of the meaning of "disability," and under that permission the board usually holds it to mean complete physical or mental collapse, but in exceptional circumstances may interpret it to mean inability to perform any of the kinds of work which the company has available.

That, similar to our other measures, was the result of experience. A man was working in a galvanizing department, which is more or less dangerous. His work was over a big kettle of molten metal. He had to move quickly, and he was 54 years old, and it was reported that he was slowing up, that it was very dangerous to have him do that work. He was a foreigner and could talk very little English. He usually had an interpreter to talk to us. We asked if there wasn't some other work he could do in the plant. Everybody said "no," that he knows nothing but galvanizing and is good for nothing else; that we couldn't use him at all. We said, "Well, are we going to discharge this man at 54? He has a credit in the fund of $15,000, and we will hand him $9,000 under the terms of the fund because he has been discharged before he reaches 60."

So we passed this resolution enabling us to interpret this man as totally disabled because unfit for any work that we had available, and we paid him the $15,000. [Continuing:]

If any specific investment of the fund is objectionable to its members, such objection in writing and signed by one-third or more of the members shall, when presented to the trustee and advisory board, cause them to at once submit such investment to a vote of approval or disapproval of all the members; and if a majority disapprove, they shall liquidate this investment as soon as they consider it practical to do so, and refrain from additional investments of the same character for at least 1 year after such disapproval, unless in the meantime the investment has been resubmitted to the membership and a majority vote of approval secured.

That has not been of the slightest use to us, but we passed it on the advice of a union official who said to us:

Well, what have the workmen got to say about an investment that they don't think is good? Perhaps you are investing in your preferred stock and the company is slipping and slipping and slipping and it could be liquidated perfectly well, but you have three men on this board, three officers of the company, and they may vote to continue this investment, even though the two workers object to it.

So we made this clause providing a means by which an appeal might be made to the full membership and the investment discontinued if the workers voted against it.

Senator VANDENBERG. But the appeal has never been made?

Mr. JOSLYN. Never; oh, no.

With the exception of such supplementary rulings, we have made very few changes in our plan during 20 years, none of any fundamental nature, though we have constantly welcomed criticism and constructive advice, both from within and without our organization.

The depression of the early thirties made us recognize the danger of agreeing to pay all maturities in cash, which conceivably might some day cause an unwarranted sacrifice of securities, so this was changed to permit of payments part in cash and part in securities, if deemed necessary. This option, while never used, is a very wise safeguard against extreme conditions.

Another suggestion was that the early years of membership were not sufficiently protected from the contingency of death, thus making supplementary life insurance desirable for care of dependents.

We secured from insurance companies a rate applicable for $2,000 policies at the average ages of members in their first 7 years in the fund, which ran about $10 per $1,000. Our company then donated $10,400 to the fund as an insurance reserve, and a provision was made for deducting $20 from a member's credit at the end of his first year and adding $2,000 to that credit in case of death during his second year, and similarly, each year, but in diminishing amounts, up to his seventh year, by which time his own profit-sharing credit would be ample and require no further reinforcement.

Experience has shown that the deductions are probably twice requirements, and the reserve is rapidly growing; and backed, as it is, by the entire credits of all members up to 7 years, it is fundamentally sound from any accounting standpoint.

In similar manner the fund has established a hospitalization reserve for all members, at a charge to them of about 60 percent of the amount insurance companies are charging for exactly the same protection, and our first year's experience would indicate this charge is more than ample for the purpose and may prove enough to take care of their dependents as well.

There is nothing in this to warrant criticism of the insurance-company charges. They must pay large premiums to soliciting agents and general agents, and must carry heavy expense of operation and investment on low-interest rates, and besides we have a preferred risk in men of independent resources and the company pays for the physical examinations in connection with its casualty insurance on the same men, which is carried with regular insurance companies.

In this connection I might tell the story of one of our early experiments. From a sentimental standpoint it seemed unfair to turn an injured employee over to a casualty insurance company. Accordingly, we appropriated an amount somewhat larger than our premium would be: Had our employees elect a committee of three workers to settle all accidents, and agreed that any surplus at the end of the year from our appropriation would be divided among all the workmen.

To our astonishment the weeks went by and there were no accidents reported. We quietly investigated and discovered that when a piece of lumber fell on John Jones' foot the committee called on him that night and said, "Damn you, if you make a claim we'll knock your block off." So he made no claim. We ended the experiment. The casualty companies have always had our insurance since. We learned how self-interest can upset any plan founded on the assumption of brotherly love; because, much as we would like to have all men friends and brothers, the facts are otherwise.

Mark Twain said in substance: "Friendship is the noblest thing in the world; it will stand against every vicissitude except a loan."

So the best social plan will stand against anything but self-interest, and failure to recognize that fact brings disaster. Intelligent profit sharing combines self-interests of all concerned. That is its strength. It doesn't palaver about brotherly love. As an idea, as a result, we may hope for that; but as a foundation, the morals of men are not that reliable. Things worth while have to be built on facts. Men are not brothers, and plans founded on that idea go all awry.

Here are a few facts: The average worker has little financial experience or judgment and must not be relied upon for something he doesn't have. Neither has he much managerial ability, and it is folly to expect him to have it. Every man does enjoy steady financial betterment, constantly increasing security for himself and his dependents.

The statement that the worker is not entitled to a share of the profits because he does not materially or measurably influence them is only theoretically tenable. Experience demonstrates that with adequate incentive he can and does increase profits to an astonishing degree. No such incentive is warranted in the long run, as a corporation measure, unless offset by at least an equal profit advantage, but experiments based on favorable experience records of others are thoroughly justified.

A corporation has three distinct interests, ownership, management, and labor, and each of those interests is essentially selfish. There is just one way to weld them into a common cause, by devising a plan which secures better results to all those interests at the same time, and making that plan so simple it will work in spite of the prejudices and faults common to most men. Taking away from one interest and giving to another is never going to bring that about.

We think our plan recognizes all those truths and many similar ones. That is why it works.

What are our suggestions, if any, for legislation? As a corporation we have no ax to grind. We need no incentives. Our profit sharing pays its own way. It is not an infant industry with us and needs no protective tariff. But on behalf of the workers themselves we do need some fair and just measures.

We clearly recognize the fact that what the Government is seeking in Federal security legislation is much more comprehensive than, and based on different considerations from, a profit-sharing plan, as we conceive it.

The Government plan protects all workers, good and bad, loyal or disloyal, whether their efforts are along a definite path, or shifting and sporadic.

We do not protect workers in their first 3 years of employment with us at all, nor do we carry on with members of our plan after they resign or are discharged.

Our interest is confined to employees of 3 years' standing or more, and only so long and to such an extent as they can and do respond to the incentive we offer, by continuous service with exceptional values.

Can these two ideas be reconciled? Can we confine Government activities to regulatory and emergency functions, leaving ordinary operation to industry, where it can be handled with far greater efficiency and economy and used as a stimulant and not as a palliative? It seems entirely possible to me and most desirable. I offer suggestions for legislation, not without appreciation of the difficulties involved but in the hope that the difficulties may be overcome by careful thought on the problems, especially if that thought is sincerely sympathetic to their solution.

SUGGESTIONS FOR LEGISLATION

A profit-sharing-plan commission to be established and maintained with power to approve or disapprove profit-sharing plans, found equivalent to or better than the existing Federal security plan, and to gather and transmit to all interested parties data and information on the working of existing plans, and suggestions as to possible improvements, and also to have such other powers as may be deemed necessary or advisable.

Under approved plans, Government to exempt payments to members at maturity from all income taxes. We have now a heavy income tax on all of the accumulations, except the part contributed by the employee, though these accumulations relieve Government of all old-age or disability expense. This tax is unsound.

Government to sell to approved plans, 5-percent Government bonds, nonassignable, due December 31 of any future year, as reasonably required, for maturities under the plan, and drawing interest only from December 31 of the year issued.

I might say here that Mr. Roeder was asked to go to Canada at the request of the Dominion Steel Co. of Canada, which adopted our plan word for word, and it took just two hours and a half, I believe—I will let him tell the story—for the Government of Canada to voluntarily provide a 4 percent compound security for the fund in the form of an annuity, compounded at 4 percent and payable at any time, cashable at any time in the amount he had in, plus the 4 percent compounded. In other words it was an annuity starting at 60 or 65. Joe can tell you about it—but the Government said that our plan was perfect and they would cooperate immediately by affording a security. We do not need that. We don't as a company need that because we are able to get 6-percent mortgages which we have substituted for the old 4½- or 5-percent municipal and State bonds that we used to have, and which have gone down so low that they are not a sound investment for us. We now have 6-percent mortgages. We take a new home and take a 40 to 50 percent mortgage.

And you will wonder how we can do that with the Government lending money at 4 and 4½ percent, but we do it because we have a separate trust company that will buy the second mortgage and will lend the money to a man up to 90 percent of what he wants, if his reputation is good, and will take the second mortgage. We charge him for that and make a good profit out of it. In that way we are able to do this, but we are in the business solely to enable us to get securities for the profit-sharing fund. In that way we have plenty of gilt-edge securities. We went through the depression without the loss of a dollar and the fund had a profit at the end of the depression on the securities, which it held which were at that time bonds—we had good bonds; the State of Iowa, for instance, were some of the bonds we had.

But it would be very advisable, it would answer the one really sensible criticism that I have seen, which is—an employer says, "I am not going to bother myself to find securities to invest this man's money in, and, heavens, if I should ever lose it I don't know what I would do." So the money the men pay in should be protected. We protect it as well as we can; we protect it by limiting it to certain securities approved by the State of Illinois for trust investment, but that isn't good enough. We would like to have a Government bond that we can invest in, but we can't have any 2-percent bonds; that is no good to us. We suggest this 5-percent bond, nonassignable, not good for any other purpose, with a maturity such as is needed; and to relieve all bookkeeping and all trouble, we ask for it only once a year, the 31st of December. If we want it in September, we will lose the interest up to December.

Senator VANDENBERG. I hope Government bonds are that good.

Mr. JOSLYN. Well, we have all got to take this inflation in the neck some day, anyway, so we might as well forget that.

When a profit-sharing plan is approved, the employer to be exempt from the Federal security tax, so long as the payments to the credit of a member equal or exceed payments required under the Federal Security Act in the case of such member, and on the further condition that if such member leaves his employ under the plan, or is discharged, there shall first be paid to the Federal Security authorities, out of his credit, an amount equal to that which would have accumulated with the Government, if no profit-sharing plan had existed.

In other words, we say, "We will take this man into our profit-sharing plan and we hope he is going to stay there until he is 60." If so, we have taken care of him all his life. If he doesn't, we recognize that the Federal Security plans are much wider than ours and we say, "All right; we will put you right where you would have been had you never been in our profit-sharing plan," and for that purpose we would have an additional reason for having Federal securities that we can turn over.

Now, that gives us a chance to handle the situation, to relieve the Government from it; but whenever our plan is not comprehensive enough, the man drops back into the Government plan and we place him there just where he would have been if he had never been in our plan. That is merely a thought; I don't know whether it is good for anything or not.

In addition to such provisions as our own or similar plans embody, I would suggest that a profit-sharing commission consider as a condition for approval of a plan a provision—and somebody will like this—that no salary in excess of $15,000 be paid to any officer of the employing company in any one year, if such excess operates to reduce the payments of the company to its profit-sharing plan, in that year, below an amount equal to the contributions of the members of the plan.

That doesn't prevent the company paying $500,000 if they want to, but it does say, "All right, if your officer is worth that much money, go ahead and pay it to him, but for the purposes of profit sharing we want you to pay as much as the profit sharers put in there, if you are going to do that," unless by reducing that to $15,000 there aren't any profits. Then that is all right. I think that will be popular with some people—not with others. Now, that is for a purpose. You might have a firm that was not sincere. They might put in a profit-sharing plan and then proceed to pay all the profits to their officers. Yes, they have the profit-sharing plan, and they will tell the workers, "Sure, if there were any profits we would divide them with you, but there aren't any."

And then there is another danger. I talked to some of our profit sharers in our Fort Wayne steel plant and I suggested that they ask me questions. One man said, "What salaries do the trustee and the members of the board draw?" I said, "Not a nickel." Well, that was fine, but they could in a fraudulent set-up.

As a further condition I suggest that the actual expense of operating the plan as charged the same shall not exceed $500 a year, or one-fourth of 1 percent, of the fund capital, whichever is the larger sum, any additional necessary expense to be assumed by the company. That means if there is a capital of $1,000,000, $2,500 could be charged. That is all that is necessary. The company might have to do something else, but that is all the accounting that is necessary, and they ought to be willing to do that. That limits it so that they can't fraudulently make a lot of expenses for the fund.

Also a condition that the company whose plan is under consideration must be paying its employees not less than the average wage in its industry for similar labor. That is absolutely fundamental. No plan is worth a nickel that doesn't have that.

I believe these are advisable safeguards against possible abuses.

If the 5-percent bond idea is not acceptable, then a Government annuity based on the employees' payments and possibly, optionally, part of the employers' payments, compounded yearly at 5 percent, with full returns to his estate on death before it becomes operative as the Canadian Government has already granted, except on a 4-percent basis.

That is pretty much what I have to say except that I would like to offer a few comments on some views expressed before your committee during hearings as reported in the California papers. The reports may be all wrong and if so I apologize in advance. I am commenting on the reports just as I read them.

People are usually afraid to talk about unions, but I am perfectly friendly with every union in the country, though I have but one small plant which is organized, by the C. I. O., but I am perfectly friendly with all of them.

Mr. Lewis, if correctly reported, condemns all profit sharing because there have been or may be instances in which it was used to hold down wages, and because it is paternalistic. Neither criticism has even the most remote application to our plan, either in its principles or its operation.

Twenty years ago we asserted that our plan and all others like it must be predicated on at least the going wage in the industry. You can't hold down wages that way. There is nothing paternalistic in a definite contract to share profits, provided the worker delivers values equal to his benefits, which we declare to be a necessity. We do not give him a nickel. Fair dealing and partnership cooperation and division is not paternalism.

I do not believe Mr. Lewis would include us or our plan in his criticism. Where there are unions in any of our industries we maintain union wages and conditions and add a share of the profits, last year 20 percent of the employees' earnings. We do not condemn unionism because it is sometimes abused. Where necessary, and properly applied, it has often been a sovereign remedy for desperate ills. But it can develop ills of its own. Power can always be misapplied, and the misapplication is no measure of its value.

The antagonism that has developed between employers and labor unions has grown out of the failure of both to recognize a partnership or any obligation to sustain the general good.

Its origin lay with the indifference of capital to the welfare of the worker, but that indifference is rapidly giving way, and if labor will forget the origin of the discord, and stop being indifferent to capital, a real partnership of interest is entirely possible. Otherwise, every blow is equally disastrous to the welfare of both.

In our little industrial enterprise we have been partners and we have risen to strength together.

Mr. Green seems not to condemn profit sharing outright, but to postpone it to the time when labor is managing the corporation. I am afraid when that time comes there may well be no profits to share. The idea that labor is qualified for everything is Utopian. Expert management will always be the product of special adaptability and long training, it will not spring full panoplied from the ranks of labor, or the official role of labor leaders. Each element should contribute to the corporate whole what it is best qualified to give, not jealously seek to dominate it.

I have enough confidence in the sincerity of purpose of both Mr. Lewis and Mr. Green to believe that they can both come to approve profit sharing plans when properly safeguarded from abuse.

Certainly they must realize that with all labor unionized, increasing wages will not have any value at all to the worker because his cost of living must rise as wages rise. The measure of his prosperity lies in what he can retain and accumulate after necessary expenditures, and there our plan fits into the picture.

I have one more imposition on your time.

Senator VANDENBERG. It is no imposition, Mr. Joslyn; this is amazingly interesting and constructive.

Mr. JOSLYN. And this is brought about by some of the reports of employers' attitudes here.

Many employers are opposed to profit sharing on the theory that high wages are the complete picture of the employees' services. I do not agree with that. Many desirable social benefits do not at all necessarily follow high wages. Often quite the contrary. And high wages in dollars may be low wages in purchasing power. There is no tendency toward partnership in high wages alone, disassociated from measures designed to have employees work with, instead of for, the management. There is no encouragement of thrift, of the attainment of an independent financial status, of provision for future contingencies, so disastrous if unprovided for. A moderately high wage, steadily maintained, is a desirable foundation, but far better things can be built upon it.

Other employers wish the state to let them alone, and they resent its interference in what they regard as their private affairs.

A thought occurred to me the other day which I noted down, and I would like to present it to such employers. I do not like interference any more than they do, but I do recognize the right, and even the duty to interfere. This argument may have some meaning to them if the far better one of mutual profit in cooperative endeavors does not.

Certain simple facts are easily forgotten in the complication of modern economics. It is well to repeat some of them. The individual, finding some task beyond his own powers, took a partner to accomplish it. The partnership developed into considerable groups; but as each partner was responsible for all acts of the others within the partnership purposes, serious objections arose to the danger that one partner might, and frequently did, wreck all the others.

Association of many in a common enterprise was eminently desirable as the only practical way to accomplish purposes too large for the individual. The problem was passed to the state, already existing as a legal fiction, an imaginary composite entity, to express and execute the will of the majority of the people. The state, in response to the demand, proceeded to make rules under which subsidiary, imaginary entities might be established, called corporations, with powers to act almost as complete as those of individuals, but with the vast advantage of limited liability.

The state, having been created for the good of the whole people, and having no other excuse for existence, at least in a democracy, could not create a subsidiary with any other purpose or continue to maintain it unless it served that purpose. Corporations, once established, grew and thrived on the advantages given them by the state. Often they became arrogant, forgetting entirely the purpose and the sole excuse for their existence, and for their special privileges, and the power and duty of the state to hold them within that purpose, attempting instead to establish their own independence.

Now, it seems fundamental that the people who have set up the state for their own good may limit or abolish it entirely if it does not accomplish that end, and in turn the state may and must do the same thing with the corporation if it departs from the essential purpose of the state, its conditional creator.

If this be granted, then any corporate action which is in opposition to the general good of the people as a whole, no matter how profitable to the stockholders, is—this is my legal training—ultra vires—outside the law, and justifies and even demands vigorous repressive action by the State, even to the point of destruction.

If corporate officers would keep before them the conditional and the somewhat precarious nature of corporate existence, there would be far less abuse of their power and far more desire to accept and encourage all practical measures designed to serve the common good. One of such measures undoubtedly is the profit-sharing idea, expressed in its most efficient form.

The idea is democratic in its tendency, broadening the base of the corporate purpose and so strengthening the whole structure just as democracy does the same thing for the State.

Now let's examine the corporation, a restricted and conditional partnership of many persons, the stockholders, operating with special privilege, on condition of maintaining the general good.

Of course, they want, first of all, adequate returns on the capital invested, and in proportion to the risk assumed, and if they could not expect it they would not invest. They elect a management to conduct the enterprise, a management interested primarily in adequate salaries, without which they would not function. The management now calls in labor, without which neither capital nor management are of any value, and the three elements establish a cooperative endeavor in which each is vitally necessary, but management and capital have generally, in the past, negotiated on much more equitable terms than labor was able to secure, leaving the cooperative arrangement top-heavy and unstable and far from its proper purpose of serving the general good.

This maladjustment naturally developed the labor union, with all its good and bad features, its power to benefit labor and its frequent abuse of that power to the ultimate injury of the laborer. But the unions did unquestionably smoke out many unfair situations and so brought them into the light where they could not be overlooked.

Had capital and management really understood the conditions of their corporate privileges, they would have been seeking and correcting inequities to justify their very existence, rather than waiting to be compelled to do so, and then they would have discovered that it was more profitable and would have grown enthusiastic in the process, and no outside measure would have been necessary.

Some corporate managements did take this course and made attempts at least in that direction. Too many did not. It was too often the thought that capital should get all it could squeeze out of the corporation and keep management and labor functioning, and a prime purpose of management was to get all they could out of labor and still keep it operating. That thought must be changed so that labor gets all it can and still keep capital and competent management functioning, because, after all, labor is the base of the structure, and by its very numbers it represents the general good far more than capital or management, and so, more vitally within the condition on which the corporation was created; furthermore, labor is generally less interested in the economic structure and nothing is more necessary to a vigorous democracy than independent citizens.

The emphasis in corporate relations should be on the welfare and the independence of the worker, but, of course, that emphasis must stop the moment it begins to discourage or destroy capital or good management, because that impairs the corporate operation and leads to its collapse, to the detriment of all its elements, especially labor, and does not serve the general good.

That is in substance what I have to say, and I am relying on my secretary, Mr. Roeder, to give you some facts. I have more or less given you theories, and I want him to give you the facts of operation.

Senator HERRING. Well, that is a very fine statement and we appreciate it, Mr. Joslyn.

Senator VANDENBERG. Have you a copy of the contract that is signed between you and the employee?

Mr. ROEDER. I believe it was in that envelope that I gave you.

Senator VANDENBERG. I think it would be well, Mr. Chairman, to have that reproduced in the record at this point.

Senator HERRING. If there is no objection, it will be copied into the record.

(The contract referred to is as follows:)

EMPLOYEES' SAVINGS AND PROFIT SHARING FUND

JOSLYN MFG. AND SUPPLY CO., CHICAGO

This amended agreement made as of the 31st Day of December 1936, by and between such employees of Joslyn Manufacturing and Supply Company as have heretofore accepted the terms of that certain agreement dated as of the first day of January 1919, and of the amended agreement as of January 1st, 1924, and the Amended Agreement as of July 1st, 1929, between said employees as parties of the first part and Joslyn Manufacturing and Supply Company, a corporation, party of the second part, and/or as shall hereafter accept the terms of this amended agreement in the manner hereinafter indicated, parties of the first part, Joslyn Manufacturing and Supply Company, a corporation organized and existing under and by virtue of the laws of the State of Illinois, and having its principal place of business in the City of Chicago, in said state (hereinafter sometimes termed the "Joslyn Co."), party of the second part, and M. L. Joslyn as trustee, party of the third part, WITNESSETH.

WHEREAS said Joslyn Co., being desirous of distributing among its old and tried employees, a certain portion of its net earnings, thereby stimulating in them a keener interest in its successful operation, and at the same time encouraging a spirit of economy and thrift which may stand as a protection against the vicissitudes of old age, did as of the first day January 1919, enter into that certain agreement with certain of its employees, reference to which said agreement is hereby made; and

WHEREAS it is the desire of all the parties to the said agreement of January 1, 1919, that the same shall be amended and that from and after the 31st day of December 1936, this amended agreement shall supersede said original agreement, dated January 1, 1919.

NOW, THEREFORE, in consideration of the mutual undertakings of the respective parties hereto, it is hereby agreed by and between the said parties as follows:

1. The fund hereby established shall be known and designated as the "Employees' Savings and Profit Sharing Fund of the Joslyn Manufacturing and Supply Company."

2. All officers and employees who have been in the employ of the Joslyn Co. for a continuous term of at least three (3) full calendar years, shall contribute to the fund as hereinafter specified. No employee who has not been in the employ of the Joslyn Co. for at least three (3) full calendar years continuously, may participate in the benefits of this agreement, but as and when any such employee shall have been in the employ of the Joslyn Co. for at least three (3) consecutive calendar years, his participation upon the basis therein stated shall be compulsory.

As evidence of their acceptance of the terms and provisions of this amended agreement, all employees of the party of the second part, who now, or shall hereafter, have been in such employ for a term of at least three (3) continuous calendar years, shall sign an agreement of acceptance hereof in substantially the following form:

Chicago, Ill., __________, .

The undersigned employee of Joslyn Manufacturing and Supply Company, in consideration of such employment and the undertakings of said Joslyn Manufacturing and Supply Company and of M. L. Joslyn as trustee, as set forth in the amended agreement hereinafter mentioned, hereby approves and accepts the terms and conditions of that certain amended agreement by and between the employees of said Joslyn Manufacturing and Supply Company, parties of the first part, Joslyn Manufacturing and Supply Company, party of the second part, and M. L. Joslyn as trustee, party of the third part, dated as of the 31st day of December, 1936 and establishing the Employees' Savings and Profit Sharing Fund of the Joslyn Manufacturing and Supply Company; and the undersigned hereby further agrees to be bound by the terms and conditions of said amended agreement and to contribute to said fund such an amount or amounts as he may from time to time indicate, or as in said amended agreement provided.

The undersigned further agrees that said amended agreement dated as of the 31st day of December, 1936, supersedes the original agreement between the employees of said Joslyn Manufacturing and Supply Company of the one part, and said Joslyn Manufacturing and Supply Company of the other part, dated as of the first day of January, 1919, and subsequent Amended Agreements of January 1st, 1924, and July 1st, 1929, relating to said Employees' Savings and Profit Sharing Fund of the Joslyn Manufacturing and Supply Company.

WITNESS MY HAND AND SEAL this..........day of.......... A. D. 19..

3. (a) Except as hereinafter otherwise provided, each officer or employee shall be obliged to contribute to said fund not less than two and one-half per cent (2½%), and may contribute not more than five per cent, (5%), of the amount of their respective salaries, payable in equal installments, to be deducted therefrom at the time of payment; provided, however, that with the consent of the trustee and the approval of the advisory committee, hereinafter mentioned, any such officer or employee may anticipate and make advance payment, not extending beyond the first day of January or July next ensuing as the case may be. No officer or employee shall be permitted to contribute more than two Hundred Dollars ($200.00) per annum, anything in this agreement to the contrary notwithstanding.

(b) The Joslyn Company, Party of the Second Part, agrees to pay over to said Fund, not less than ten percent (10%) of its total net operating earnings for each year, after all taxes, (subject to an option in Second Party to elect to further deduct from any such yearly payment any and all amounts it may legally be required to pay for such year to State or National Agencies for purposes similar to those of the Fund) but the amount paid hereunder to the Fund by Second Party for any year shall not exceed four times the amount paid into such Fund during such year by the Officers and Employees from their regular salary or wage accounts.

Said contribution by the party of the second part shall be based upon its net operating earnings available for dividends, as determined by the Directors of the Joslyn Co. after the payment of all operating expenses and commission, including taxes on the property, stocks or income of the Joslyn Co., and after any other deductions which the Directors may see fit to authorize for losses, bad or doubtful paper, creation of reserve or contingent funds, or for any other purpose. All such payment by said second party shall be made annually on or about February 1st of each year, as near as may be, based on the net operating earnings of the year ending on December 31st immediately preceding, provided, however, that in the event that in any yearly period ending on the 31st day of December, the operation of said Josyln Co. shall result in a loss, said party of the second part shall not be under any obligation to make any contribution whatsoever to this fund for any subsequent period, unless and until the loss or losses theretofore sustained shall have been made up and said Joslyn Co. completely reimbursed therefor.

4. All payments by employees shall be placed to the credit of the respective contributors upon the books of said fund and from time to time, as may be directed by the trustee by and with the approval of the advisory committee, hereinafter provided for, there shall be added thereto such contributors' pro rata share of any amount or amounts contributed by the party of the second part or received by way of income or profits. Similarly, there shall be deducted the pro rata share of any expenses incurred or loss sustained in the administration of the fund.

It is the intention that, except a[s] may be otherwise determined by the trustee, with the approval of the advisory committee, all contributions of the Joslyn Co. and all income, profits, etc., shall be prorated and credited annually as of December 31st; that the periodic contributions made by the Joslyn Co. from its profits shall be prorated and credited in proportion to their respective contributions to the employees contributing to the fund during the same period for which the Joslyn Co.'s contribution is made, and that any income or profits realized on the "Current Fund" shall be similarly prorated, but that any income or profits accruing or realized on the "Reserve Fund" during any such yearly period shall be prorated and credited to the respective employees upon the books of said fund at the end of such period in proportion to their respective interests in the "Reserve Fund," as the same shall have been determined by the trustee, with the approval of the advisory committee at the beginning of such period.

The books, forms, and methods of accounting shall be entirely in the hands of, and subject to, the supervision of the trustee and the advisory committee.

5. The Joslyn Co. hereby agrees that it will, simultaneously with the execution of this amended agreement, assign, transfer, and deliver to M. L. Joslyn, as trustee, all of the cash, securities, and other assets of whatever kind and character, which now comprise the Employees' Savings and Profit Sharing Fund of the Joslyn Manufacturing and Supply Company and which said Joslyn Co. is now holding under the terms of said original agreement dated as of the first day of January 1919, and will at the same time deliver to said trustee any and all books, contracts, papers, and memoranda of whatsoever kind and character which relate to said fund. Upon such assignment to the trustee herein named of the assets of said fund and the delivery to him of all said books, papers, contracts, and memoranda relating to said fund, said Joslyn Co. shall be, and hereby is, released and discharged from any and all liability arising from or growing out of the custody, management, control, and/or distribution of said fund under the terms of said original agreement of January 1, 1919.

The trustee agrees to hold, separate and distinct from all other assets, all of the invested assets of the fund created hereunder and under said original agreement, and that from time to time, as receivable, there shall be credited to the fund all income received therefrom, together with any profits resulting from the sale or sales of any such assets; similarly, there shall be deducted therefrom, time to time, all taxes, charges, or expenses necessarily incurred in the management or administration of the fund, together with any losses that may have been sustained with respect to said assets, either through sale or otherwise.

6. (a) The title to the fund shall rest absolutely in the party of the third part as trustee, and no part thereof or interest therein shall be grantable, transferable, or otherwise assignable, in whole or in part, either by the voluntary or involuntary act of the parties contributing thereto or by operation of law, and shall not be liable for or be taken for any debt, liability, or contract of any of the respective contributors, all right, title, and interest of said contributors having been by this amended agreement hereby absolutely transferred and assigned to said party of the third part as trustee.

(b) In the control, management, and distribution of said fund, the trustee shall be subject to and act only with the approval of an advisory committee, consisting of five (5) members (of which the trustee may be one), three (3) members of said advisory committee to be officers of the party of the second part, selected by its Board of Directors, and the remaining two (2) members to be employees, who shall be selected by a majority vote of the parties of the first part to this amended agreement. The members of the advisory committee shall serve for a term of three years from and after the date of their selection and shall receive no compensation for their services.

The advisory committee hereunder shall elect a chairman and a secretary from their own number and an actuary who may or may not be one of their own number, and may employ such clerical help as in their judgment may be necessary for the proper administration hereof. Said advisory committee may make such bylaws or rules, not inconsistent herewith, as they may deem desirable for the transaction of their business, and they shall not be personally liable with respect to any matter or thing done hereunder, unless they shall be guilty of willful negligence in the premises. Any action taken or approval given by a majority of the advisory committee shall be the action or approval of the committee.

Said trustee and the advisory committee shall treat the contributions of the parties of the first part and of the party of the second part as one fund for the purposes of investment and reinvestment, and shall have power to invest and reinvest the same and the proceeds therefrom or from any part thereof in railroad, public service corporation, Municipal or Government bonds, income-bearing stocks, mortgages or other securities (provided, however, that a portion of the fund not less than the total amount paid into it by the officers and employees and interests actually earned on same, shall always be kept invested in United States Government or State Bonds or other securities approved by the State of Illinois, at the time of investment, for investment of Trust Funds), and in the name of the trustee, to sell, collect, sue for, alter, or change the investment thereof, from time to time, as they shall deem best, and said trustee and advisory committee in the matter of investment and reinvestment shall not be limited in any wise by any laws of the State of Illinois or of the United States, now or hereafter in force, governing the investment of trust funds. No transfer, sale, or investment of or for any part of the fund hereby established may be made by the trustee except upon the approval of or in accordance with general rules adopted by a majority of the members of the advisory committee hereinbefore referred to, evidence by a certified copy of such resolutions or rules of said advisory committee, or by an order duly signed by a majority of the members of said advisory committee, and filed with the treasurer or cashier of the party of the second part.

In the custody, control, management, and distribution of said fund the trustee shall incur no personal liability, save for his own gross negligence or willful default.

7. The privilege of contributing to said fund shall apply only so long as the employee is in the active service of the Joslyn Company. As and when any such employee shall attain the age of sixty (60) years, he or she shall retire from the service of the Joslyn Co. unless for special reasons the Joslyn Co. may wish such employee to continue in its service and he or she shall consent thereto; provided, however, that any officer or employee who has been for three (3) continuous years in the active service of the party of the second part on the first day of January 1919, shall have the privilege of participating in said fund for at least twenty (20) years from that date (notwithstanding the fact that the retiring age of sixty (60) years may be exceeded), but only so long as said officer or employee shall remain in such active service.

8. (*a*) In the event of the voluntary resignation or the dismissal of an officer or employee, one of the parties of the first part, prior to the date of retirement, there shall be paid to him his pro rata share of the portion of the fund contributed by the officers and employees and all interest or profits accumulated on the same and one-half of his pro rata share of the portion of the fund contributed by the Joslyn Co. with interest or profits accumulated on the same, said payments to be made on the basis of the fund as then constituted and as determined by the trustee under the approval of the advisory committee. The remaining one-half of such officer's and employee's pro rata share of the portion of the fund contributed by the Joslyn Co., with interest or profits accumulated on the same, shall remain in the fund to be prorated among the other officer and employee contributors thereto.

(*b*) Upon the death of any officer or employee prior to retirement, there shall be paid to the estate of such officer or employee, or to such beneficiary as may have been designated by said officer or employee in the manner hereinafter provided, the pro rata share of the fund as constituted as of the date of the death of such officer or employee, all as evidenced by the books of account hereinbefore in this amended agreement referred to; provided, however, that payment to the estate or beneficiary of such a decedent at any time within six (6) months after proper proof of death of any officer or employee shall have been filed with the trustee hereunder, shall be considered to be full compliance with the terms of this amended agreement.

(*c*) Upon the termination of the services of any officer or employee by reason of the attainment of the age of retirement, or at any time after the attainment of such age, or at the discretion of the trustee, with the approval of the advisory committee, by reason of illness or physical incapacity, there shall be paid and delivered to such officer or employee his pro rata share of the Savings and Profit Sharing Fund as then constituted, all as evidenced by the books of account hereinbefore in this amended agreement referred to; or at the option of the trustee with the approval of the advisory committee in each individual case, and if, in their opinion, the purposes of this amended agreement will be more fully attained thereby, the payment of said pro rata share to such officer or employee as determined at the termination of his services, may be divided into eleven (11) equal parts and paid one part in cash and one part each year thereafter for ten (10) years, the deferred portions to be invested in the same high grade of securities as hereinbefore provided for the investment of the portion of the fund contributed by employees, and subject to the same provisions as to responsibility for gain or loss, and all gain or loss on each yearly portion to be added to or deducted from such portion.

(d) All distributions made to officers and employees under the terms of this amended agreement shall be in cash, provided, however, that at the option of such officer or employee, or beneficiary, as the case may be, or at the option of the Trustee, such distribution may be made in securities held by the Trustee and Advisory Committee, or partly in securities and partly in cash, as said Trustee, with the approval of the Advisory Committee, shall deem best.

9. Any officer or employee, a contributor hereunder, may designate as his or her beneficiary, in case of death, the person or persons to whom his or her share of the fund shall be paid, provided, however, that any such designation is approved by the trustee and advisory committee hereunder. Such designation shall be in such form as shall be determined by the trustee and advisory committee, and shall be filed with the trustee. Where such designation has been filed as herein provided distribution of the share of any such deceased officer or employee shall be made direct to such beneficiary, and payment to such beneficiary shall fully acquit and discharge the trustee and the members of the advisory committee from any and all liability on account thereof. The beneficiary or beneficiaries hereunder may from time to time be changed at the election of the officer or employee by the filing of a new designation in accordance with the rules adopted by the trustee and the advisory committee. In the event of the prior death of any such beneficiary the portion of the fund which would otherwise have been payable to such beneficiary shall be paid to the legal representative of such deceased officer or employee.

In the event no such designation of a beneficiary is filed hereunder as above provided, or in the event that any such designation shall not have been approved by the trustee and the advisory committee, then and in either such case the share of any such deceased officer or employee shall be paid his or her legal representatives.

10. No officer or employee shall be entitled to withdraw any part of his interest in said fund so long as he or she shall remain in the employ of said Joslyn Co., provided, however, that in the absolute discretion of the trustee and with the approval of the advisory committee a loan or loans may be made to such officer or employee in cases of necessity when circumstances warrant, but so long as any officer or employee is indebted to the fund he may not participate in the benefits of any contribution made by the party of the second part, and all contributions made during the continuance of such loan by such officer or employee, as hereinbefore provided, shall be used in the liquidation of the amount of his indebtedness to said fund and not to be used to increase his pro rata interest in said fund.

11. The trustee of said fund, together with the advisory committee, may from time to time formulate such rules and regulations for the management and distribution of the fund, not inconsistent with the provisions of this agreement, as may to them seem desirable.

12. In the event of the death, resignation, mental or physical incapacity of the trustee hereunder to act, then a successor trustee shall be named by the party of the second part, acting through its Board of Directors. Any such successor trustee so chosen shall thereupon become vested with all the rights and powers and shall perform the duties and shall be subject to the limitations of the trustee named in this amended agreement.

12-A. In the case where the Joslyn Mfg. & Supply Company owns 51% or more of the stock of another Company, then such other Company may file a request with the Joslyn Mfg. & Supply Company, that its employees be allowed to become members of the Joslyn Mfg. & Supply Company Savings and Profit Sharing Fund on the same basis as though actually employees of the Joslyn Mfg. & Supply Company, such other Company, however, to reimburse the Joslyn Mfg. & Supply Company for any contributions made by the Joslyn Mfg. & Supply Company to said Fund by reason of the Membership in such Fund of employees of such other Company, and on the approval of such a request by a majority of the Directors of the Joslyn Mfg. & Supply Co. and by the Trustee and a majority of the Advisory Committee of the Joslyn Mfg. & Supply Co. Savings and Profit Sharing Fund, then the Employees of such other company may become members of such Fund, with the same privileges and conditions as though employees of the Joslyn Mfg. & Supply Co., except as heretofore provided, and change of employment from one Company whose employees are members of the Fund to another Company whose employees are members of the Fund, shall not be deemed discontinuance of employment under the terms of the Fund, provided, however, that if at any time the ownership of Stock in such other Company by the Joslyn Mfg. & Supply Company becomes less than 51%, then the Fund Agreement as to employees of such other Company, may be discontinued on thirty days' notice, by vote of a majority of the Directors of the Joslyn Mfg. & Supply Co., or by the Trustee and a majority of the Advisory Committee of the Fund.

12-B. On and after December 31, 1936, when a Member of the Fund has concluded his first year of Membership, there shall be deducted from the amount of his credit in the Fund, the sum of $20.00, and in like manner when he has concluded his second year of Membership there shall be deducted from the amount of his credit in the Fund the sum of $15.00, and similarly on the conclusion of his third year $12.50, fourth year $10.00, fifth year $7.50, and finally at the conclusion of his sixth year of Membership the sum of $5.00, shall be deducted from the amount of his credit and these deductions, while from his general credit, shall, for all purposes of the Fund, be regarded as though deducted from the wage bonus and not from the amount contributed by the Member directly from his regular wages, which amount remains unimpaired. Such deductions shall be held, subject to the provisions hereof, in the General Fund, as a Reserve for Deaths and Total Disabilities during the second to seventh years of Membership, inclusive. In the event of the death of a member of the Fund during the second year of his Membership and while actually a Member of the Fund, there shall be added to the amount payable to his beneficiary the sum of $2,000.00, in like manner if death occurs in the third year of Membership there shall be added $1,500.00, if in the fourth year $1,250.00, if in the fifth year $1,000.00, if in the sixth year $750.00, if in the seventh year $500.00. Payments identical to those for deaths, as above provided, may be made from the Reserve for Deaths and Total Disabilities, to the Member, in case of Total Disability, entirely at the discretion of the Trustee and Advisory Committee in each case.

The additional payments hereinbefore provided for shall be paid from said Reserve for Deaths and Disabilities, during the second to seventh years of Membership, inclusive, except as herein otherwise provided. If the Reserve hereby created shall at any time or times be insufficient to pay maturing credits for which it is designed, then the Trustee, with the consent of the Advisory Comittee, may transfer to the Reserve Fund from the General Fund Credits of all Members who are in their second to seventh years of Membership, inclusive, by pro rata assessment, such sum or sums as will cover such deficiency or deficiencies. As and when Members hereafter complete seven years of Membership in the Fund, the Trustee, with the consent of the Advisory Committee, may, but in no event shall at any time be required to, transfer such pro rata portion of said Reserve (including earnings thereon) as the Trustee and Advisory Committee deem equitable, to the credit of such Members respectively in the General Fund.

13. This amended agreement may from time to time be further amended upon the recommendation of the Board of Directors of the party of the second part or its executive committee, subject to the approval of officers and employees representing not less than fifty-one per cent (51%) of the total amount contributed by such officers and employees for the period ending on the first day of January or July next preceding the date of said proposed amendment.

This amended agreement and the Savings and Profit Sharing plan hereby constituted may be discontinued at the end of any calendar year by the action of the Board of Directors of the party of the second part, upon giving six (6) months previous notice to that effect to the parties to this agreement.

14. The term "employee" as used in this agreement shall mean any employee or salaried officer of the party of the second part. The term "trustee" and/or "advisory committee" shall mean the trustee and/or advisory committee for the time being. Plural shall in all cases include the singular and the singular shall in all cases include the plural.

The term "pro rata share" shall be construed to mean the share of the fund to which any employee may be entitled hereunder as determined by the trustee and advisory committee after deducting the amount of any unpaid loans or advances made to such employee and the determination of the trustee and advisory committee shall be final.

The current contributions of the employees and the Joslyn Co. together with any income or profits accruing thereon during each current period of one year or otherwise shall for convenience be known as the "Current Fund" to distinguish the same from any moneys, investments, etc., held by the fund at the beginning of such current period and which for convenience shall be known as the "Reserve Fund."

15. This amended agreement shall be binding upon all employees who shall become parties hereto in the manner hereinbefore provided, their heirs and legal representatives, upon the Joslyn Co., its successors and assigns, and upon M. L. Joslyn as trustee, and his successor or successors in trust.

IN WITNESS WHEREOF, the parties of the first part shall from time to time execute and deliver to the party of the second part and the party of the third part their acceptance hereof in the form hereinbefore indicated, and the party of the second part has caused these presents to be executed in its name by its proper officers and its corporate seal to be hereto affixed, and the party of the third part, to indicate his acceptance of the terms hereof, has hereunto set his hand and seal, all this ---------- day of January A. D. 19--, but as of the first day of January A. D. 19--.

JOSLYN MANUFACTURING AND SUPPLY COMPANY,
By --,
President.

Attest:

------------------------------------,
Secretary.
------------------------------ [SEAL]
As Trustee.

Mr. JOSLYN. If there is no objection, I will keep the witness chair and let my secretary talk from there, and I will be available if there are any questions.

Senator HERRING. Yes.

STATEMENT OF JOSEPH A. ROEDER, ACTUARY, JOSLYN MANUFACTURING & SUPPLY CO., CHICAGO, ILL.

Mr. ROEDER. Victor Hugo once wrote that the misery of a child is interesting to its mother, the misery of a young man interesting to a woman, but the misery of an old man is interesting to nobody.

And I am afraid that that has held true for probably a hundred years until here some few months ago a Democratic Senate adopted a Republican resolution to select a committee to investigate profit sharing throughout the United States, and I am frank to say that I personally believe that your committee has done an exceptional piece of work. In fact, at that point I might say that today public attention is focused as it has never been before on employees' bonus payments and profit-sharing funds.

Although profit sharing has long been in existence, there still is little agreement as to what it really is. It covers many direct and indirect forms of compensation in addition to the regular wages. The distribution in itself, in the majority of cases, is usually made in cash. The serious objection to payments in cash, however, is that an employee usually does not save and by these extra cash payments he is very likely to establish an unwarranted and insecure standard of living.

We, in the Joslyn organization, subscribe to the belief that profit sharing covers a voluntary agreement by virtue of which an employee receives a share fixed beforehand—and that is all-important—fixed beforehand, in the profits of the company, and we further subscribe to the practice of establishing trusts for the receiving of such distribution for employees and the administering of that trust in such a way as to assure the safety of the principal to the employee, as well as a return sufficient to offer the proper incentive for that employee to save.

Mr. Joslyn has pointed out the various features of our plan. I have the good fortune, and have had for the past 10 years, of acting as actuary of that fund, and I have prepared here a 20-year record of the savings, company bonus, earnings, and the accumulation on that fund.

It comes within a very small percentage point of being absolutely correct. In fact, on the highest credit in the fund, which is approximately $40,000, these decimals, as far as I have carried them out, come within about 63 cents, on $40,000, of being correct.

(The table to which Mr. Roeder referred is as follows:)

Year	Member contribution in year	Company bonus in year	Interest earned in year	Total credit at end of year	Interest rate
					Percent
1919	$1	$4.00	Nil	$5.00	Nil
1920	1	4.00	$0.38	10.38	7.5716
1921	1	4.00	1.56	16.94	14.9958
1922	1	4.00	1.81	23.75	10.6645
1923	1	4.00	1.94	30.69	8.151
1924	1	4.00	2.10	37.79	6.8452
1925	1	4.00	2.89	45.68	7.6594
1926	1	4.00	4.36	55.04	9.5545
1927	1	4.00	4.82	64.86	8.7563
1928	1	4.00	5.75	75.61	8.8716
1929	1	4.00	7.72	88.33	10.2121
1930	1	1.31	7.27	97.91	8.2311
1931	1	Nil	7.35	106.26	7.5051
1932	1	Nil	5.87	113.13	5.5234
1933	1	Nil	3.28	117.41	2.8987
1934	1	.20	7.63	126.24	6.4968
1935	1	1.00	19.33	147.57	15.315
1936	1	2.00	14.77	165.34	10.011
1937	1	4.00	11.05	181.39	6.683
1938	1	3.00	11.79	197.18	[1] 6.50
Total for 20 years	20	55.51	121.67	197.18	8.12

[1] Estimated.

Mr. ROEDER. In 1919 Mr. Joslyn started this plan and a member saved $1 and the company contributed $4. Due to the fact that the payments came to us monthly and there was no chance of making investments, there is no interest paid in the first year. So at the end of the first year the man had $5 in the fund.

In the second year he contributes $1 and the company again gives him $4, and then they find that, from investments made from the inception of the fund, we average 7.57-percent interest on that fund to give a man an earning on his $5 the year before an interest credit of 38 cents, to make the total at the end of 2 years $10.38 even though in 2 years he had only contributed $2. In other words, after 2 years of membership in the fund, having saved but $2 of his money, he already had five times the amount.

Senator VANDENBERG. Mr. Roeder, how much of those net percentage earnings flow from lapses in the fund?

Mr. ROEDER. If I might add, I would like to wait until I finish here and I will bring that out. It varies, Senator.

Senator VANDENBERG. All right.

Mr. ROEDER. The contribution of four-for-one becomes almost monotonous. For 11 years Mr. Joslyn and his board of directors have contributed $4 for every $1 that the employee contributed, so that this 11-year picture reveals this: The member has saved $11, the company has put in $44, but the fund, which is the trust for the benefit of that employee, has credited him the vast sum of $88.33. In other words, the fund does as much probably for the employee as the company does in this great union of partnership between capital and labor.

There is the high point [indicating]. Then we hear:

"Don't sell America short." Commentators, newspaper editors, front page of the Hearst papers, "Don't sell America short." Stenographers, clerks, truck drivers—in the stock market at prices higher than America has ever seen them before.

Here comes the unexpected collapse.

Earning strength, even in the Joslyn organization, whose earnings for 11 consecutive years allowed them to pay 4 for 1, collapses. For the first time in 12 years, they must tell the worker that due to conditions beyond their control they can't give him 4 for 1 as they promised, but were only going to pay $1.31 for $1 contributed.

Mr. Joslyn. Just a minute, Joe, we didn't promise anything of the kind.

Mr. Roeder. No; we anticipated; we didn't promise.

So, for the first time in 12 years he practically gets a matched dollar, dollar for dollar, just a little better.

Now, let's see what the result was that year after the employee received the first shock that the bonus payment is not 4 for 1.

He saves a dollar, the company only gave him $1.31, but in that year the fund, his pot, earned for him $7.27, or the interest accumulation during this period was seven and one-fourth times better than the dollar that he contributed.

Now come the dark years of 1931, 1932, and 1933, in which there are no contributions. The company—I believe I am correct in saying—for the first time in its history lost money.

Mr. Joslyn. For the first time in 40 years.

Mr. Roeder. We lost money and had no profits to divide. The employee saves a dollar and the company doesn't do anything. He goes to the trustee and the trustee advises him in 1931 that the fund has earned $7.35 for him for every dollar in the pot. And so on through 1932 and 1933.

In March 1933, President Roosevelt closed the banks in America, I believe, after the failure of some 5,000 banks. In that year the fund's earnings were $3.28 for every dollar.

Now the clouds lift and on the industrial horizon the sun of profits starts to rise, and here we come in and we make a little money, and we pay them 20 cents for each dollar. The interest at that is still seven times what he saved in that year, and in 1935, a generally good year after all of these hard years, our earnings came to a point where the directors decided to clean up all back accumulation, and in that year we were able to match dollar for dollar and, because of the patience of that employee, the accumulations earned for him that year were $19.33 for every dollar that was to his credit, had he been in the fund since 1919.

Mr. Joslyn. During the worst of the depression our preferred stock passed its cumulative dividends, and when you come to 1935 they contain part of the deferred dividends.

Mr. Roeder. For every dollar saved here from 1919, the inception of the fund, up to 1935, the fund earned $19.33.

Senator Vandenberg. If the man started in the fund in 1930, let us say, he wouldn't have any of those incentives?

Mr. Roeder. We will show a little later a chart for a man entering the fund in 1930.

Mr. JOSLYN. His job was enough incentive at that time

Senator VANDENBERG. I hope so; but before I go entirely cuckoo over these figures, I wanted to straighten that out.

Mr. ROEDER. In 1936 we paid 2 for 1. The interest accumulation was quite heavy, $14.77.

Last year we returned to the 4-for-1 ratio, after 8 years, and the interest accumulation was $11.05.

I have pinned this onto the map because the 1938 results will not be determined until about January 10, 1939.

Mr. JOSYLN. We have determined it at $3.

Mr. ROEDER. At $3 for the parent company; yes.

So assuming we pay $3 for $1, the interest accumulation will be $11.79.

So the story goes that for all of those who have been in the fund since 1919, for every dollar per year that they have saved for 20 years, or a total of $20, the company has paid them $55.51, a ratio of 2.775, while the fund itself has earned for that man $121.67 in interest, or six times the amount he saved. This chart is made up for quick calculation.

Assuming that a man saves, on a $1,000 salary, $50, and say he got no increase, that his average was $50 a year, he would have 50 times $197.18. Well, he would have $10,000, roughly.

A man saving $100 each year, with full membership for 20 years, would have the grand sum of $19,718, or just a few dollars less than $20,000.

For the maximum, assuming a man worked for 20 years and got no increase and started at $4,000, and he average $200 in contributions per year, he would leave the fund, providing he was 60, with $39,436, or almost $40,000.

Some years ago we were quick to see that this fund in 20 years, assuming that the amount here was left in our preferred stock, and assuming again that the Joslyn organization could do in the next 20 years, what it has done in 39 years on its preferred stock, earned 6 percent return, and through some years they paid 7 percent, the fund would pay a man, per month, what he saved per year without dissipation of the principal. It would pay him per month what he saved per year without dissipation of the principal. For calculation purposes, he saves $200 per year. He would save, in 20 years, $4,000. He would have in 20 years $40,000—we only miss that by a little. Six percent on $40,000 would be $2,400 a year. Figuring 12 months to a year it would be $200 a month income. He saved $200 a year and the preferred stock would carry on after his death to his widow and, after her death, to their children, and so forth, without any dissipation.

You ask what safeguards you have on the preferred stock. We have earned in some years as high as $83 a share, and in other years $60 to $65. In other words, it is anywhere from 10 to 14 times the requirement and, I think in good financing, bankers tell you that anything that earns over 2¼ or 2½ times is a good investment.

Senator VANDENBERG. Your fund isn't invested in your preferred stock, is it?

Mr. ROEDER. It is; the portion that the member contributes is invested, as Mr. Joslyn told you, in Government, municipal, State bonds and/or in securities as approved by the State of Illinois for investment of trust funds under the State laws of Illinois.

Now when municipal bonds in through here [indicating] used to carry anywhere from a 4¾ to 5½-percent coupon, they are selling now on a 1.90 percent; 2.10 percent probably, with 3 percent as the top yield. They were attractive, but now we have shifted and we buy—we still have some bonds—gilt-edge 45- or 50-percent mortgages. This investment of bonus is put in preferred stock, the compound interest earned on the members' money is held in those Illinois investment approved trust funds as security. This [indicating] is in preferred stock, and the interest on this is permitted to be held in preferred stock.

Senator VANDENBERG. Could you find investments for the whole thing outside of your business and maintain any such ratios?

Mr. ROEDER. Outside of our business?

Senator VANDENBERG. Yes.

Mr. ROEDER. I think the average broker might be in a position to give you upwards of probably 200, I might say even 400 preferred stocks throughout the country that have a record equally as good as ours. Let me cite one of the largest motor manufacturers in Detroit. They have outstanding 1,845,000 shares of preferred stock at $100 par, $185,000,000, if that is a correct calculation. That would provide ample investment sources for the profit sharing in probably that particular industry. And so on. You will find that the great majority of the companies are so capitalized that they have a preferred stock and there is no harm in the employees owning this preferred stock.

I call particular attention to the interest earned. It is rather large. I have calculated it at 8.12 percent. Due to the fact that somebody might say it was interest earned over 20 years, but inasmuch as there is no interest earned up here, the average should probably be taken on 19 years, and if that was true then it would be 8.54 percent.

Now the Honorable Senator asked what percentage of the relinquishments comes in under this "Interest earned" column. I would say, Senator, that the earnings from relinquishments, as we call them, have varied from one-half of 1 percent in 1 year to as high as 3.1 percent in the highest year. It is what we call among our profit shares the "jack pot."

Senator VANDENBERG. Well, you have rediscovered compound interest [laughter], as well as profit sharing.

Mr. ROEDER. In other words, it goes to show just this. Without pointing the finger of criticism at any industry or any particular company, I say that we in the Joslyn organization have been trained that profit sharing means trusts for employees, the same security that the man at the head of the company would choose for his own investment, for his wife's investment, or probably his children's investments.

A man should not be permitted to be sold on the idea that profit sharing means a cash bonus.

One of the large industries in the United States paid out in one year $6,000,000 to 144,000 employees. That, in itself, seemed like a lot of money, $6,000,000.

But when the cashier got through preparing the dividend checks, it averaged $46 per worker. Now I ask you, with Christmas falling on Friday, Saturday, or Sunday, so that we have a 3-day holiday, which we had in 1936 and 1937 and will again have in 1938, because it falls on a Sunday, with three holidays over Christmas, and then probably the plant closed that week for inventory—but if they are open—another 3 days at New Years, with everybody imbibed with the Christmas spirit and the holiday spirit, I am going to ask you, how long do you think that $46 lasted in the pocket of any worker or what did it bring? They repeated the operation in 1937.

I have a chart here—I am sorry I can't post it—but if they did nothing more than to put this $6,000,000 in the preferred stock of this company at 5 percent, 146,000 employees in 20 years, the same as in our company, would have owned $185,000,000 of their preferred stock. It would have eliminated from their books 21,000 stockholders, and I don't see any harm in an employee owning the prior issue of any corporation for which he works. In other words, Mr. Joslyn has taken the money that he pays his employees, and he hasn't put it in the common stock of his company. He placed the employees' money ahead of his and gave them a prior issue on earnings and on liquidation in the event of default of the company.

Back in 1929 we were all drunk with the stock market pyramiding. In through this channel here, 1927, 1928, 1929, our larger industries thought they were doing something for their workers when they permitted them to buy into the common stock of the corporation. I point particularly to one of the large merchandising concerns in the United States, doing several hundred million dollars of business. They sold stock to their employees at $30 and the stock pyramided and went up, to $75, $100, went on up and made a high, in 1929, of $439⅞. I personally know the company, have intimate friends in the organization. When they had such profits they ran to their bankers and the bankers said, "439—John, don't begin to sell, it is going to go to $500, it is going to go to $600—hold on."

Mr. Brisbane, one of the best editorial writers America has ever known, broadcast throughout the Nation, "Don't sell America short—we have just begun the climb—capital had shown the worker the 7–11 on industrial dice—they taught them how to gamble."

And then the crash came, stocks tumbled. "Don't sell out, that is only a normal reaction, it only dropped from 439 to 390. It will come back to 400 and over."

It dropped to 300—"Oh, it will go back to 400."

And everybody waited for that comeback, which never came.

And then came the collapse of the entire structure, everything stopped. There was no industry, no labor, no employment, and whom did they blame? They said that poor Mr. Herbert Hoover was running the crap game, and I just say this, that it was our system of teaching employees to speculate—and I say personally and I believe Mr. Joslyn will bear me out—that an employee has no right in the common stock of a corporation, because no matter how strongly you control your own company, you cannot guarantee the price on the market and you can't guarantee where it will be in 1927, 1931, or 1937.

Now, let me show you what this man did. He started out here in 1919 and he estimates and says that for every $100 that you boys will save I will guarantee you $22,000 in 20 years.

Mr. JOSLYN. Not guarantee, Joe, you musn't use that word, estimate.

Mr. ROEDER. Well, we will estimate that you will have $22,000. He missed it by $2,300 in 20 years, or just a little bit more than $100 a year, and he took that ship through an inventory depression in 1921, the world's greatest depression in 1929, and in our own industry a third depression in the collapse of the Insull empire—we sell to utilities.

Now that is what you can do. You can really tell your employees to a certain extent that through trust deposits in a big trust, mutual agreement like we have here, that these things are almost apt to result.

But you take them through common stock and there is no man, no matter how large a company he operates or how small a company he operates, who can guarantee, over a period of 20 years, what his common stock will do.

Senator HERRING. What is the reason for having your employees work 3 years before they become a member of the fund?

Mr. ROEDER. I would like to have Mr. Joslyn answer that. I asked that question of him when I started.

Mr. JOSLYN. What is the reason that you court a girl quite a while before you ask her to marry you?

Senator HERRING. You are asking me?

Mr. JOSLYN. Or did—Senator?

We don't know whether we want this man with us permanently until we have tried him out, nor does he know whether he wants to hand us over 5 percent of his earnings all the rest of his life until he has tried us out.

Senator HERRING. After you decide at the end of 3 years, you do not date it back?

Mr. JOSLYN. Oh, no; but we did have a preparatory schedule for a great many years, and we still do it to some extent. We used to pay $4 to the profit sharers for $1, but we also paid, that is, we paid them 20 percent of their earnings, but we also paid a 1-year man 5 percent, a 2-year man 7½ percent, and a 3-year man 10 percent in cash. In other words, we educated him up to the point or the time when he would be willing to trust us, and get no more cash but contribute 5 percent of his own. It was a sort of school by which a man could feel that this year he is going to get 5 percent and he had better stay in next year because he will be getting a little more, and the next year he would be getting a little more, and he would feel that he was contributing to his record which would make him a profit sharer some day. We do that still, only in a different percentage. Last year we paid 2, 4, and 6 percent in cash, more as preparatory to the other thing than that we believe in the cash bonus.

Senator HERRING. Do you think your plan would work in industry generally?

Mr. JOSLYN. I think the best answer to that is that Mr. Roeder, with night work and a tremendous amount of preparation, has secured every bit of information on the 60 largest corporations in this country, and, to our surprise, we don't find one that it wouldn't work perfectly in, on their record for the last 10 years, and, surprisingly, we thought we were pretty good, but their percentage that they would have contributed would have averaged about the same as ours, and we thoroughly believe that if they had done that, there would not have been a murmur of labor trouble of any kind. We can't see how there could be, because we are so far from it ourselves that we can't understand it hardly.

Senator HERRING. There is a certain penalty upon employees if they leave before 60 years of age, is there?

Mr. JOSLYN. Absolutely, and that is the nub of the whole agreement. If we don't have a penalty, what happens? A man accumulates $5,000. A fly-by-night salesman comes around and says, "John, you have got $5,000 that you can go down there and draw. I have a gold mine out here that is going to be worth $100,000,000, and you can get a share in it that will make you rich for life."

He resigns, draws his $5,000.

That is why all these plans that permit a man to draw out the full amount are temptations to him all the time, and he loses his money and the whole thing is flat.

Senator VANDENBERG. How many companies are operating on the so-called Joslyn plan now?

Mr. JOSLYN. How many do you think, Joe?

Mr. ROEDER. I would say approximately 20.

The most interesting story is a story over the Canadian border line. They heard of the plan through the Toronto Star. Mr. Sherman, president of the Dominion Steel Foundries, wrote and asked for some data on the plan, and I sent to him what I delivered to you Senators today in the form of that envelope.

He read it over, we had some correspondence, and he invited me to come to Canada. He had 1,776 workers—and I took advantage of the magic figure.

Hamilton, Ontario, is the dominion in which Mr. Hepburn did the strong act of throwing the unions out. I said to the workers that 1776 in America—you know I was talking to a bunch of Canadians and Englishmen—meant liberty in America, and I talked with them that 1776 might mean liberty to the worker.

I talked with 100 keymen later, and we have a letter here from Mr. Sherman saying that unanimously the employees adopted the plan.

The Canadian Government was then called in, because you can't do anything in Canada for labor but what you are referred to the Department of Labor, and they sent a Mr. Weir down into the conference. We were not over two and a half hours, when Mr. Weir consented to issue for the profit-sharing fund of the Dominion Steel Foundries, or at least for that portion contributed by the employees, an annuity compounded at 4 percent a year. I am sorry I only have one copy and I would like to pass it to your attention. It won't take you very long to read it.

Under the Dominion plan, this employee dollar would go to buy compounded annuities at 4 percent, this portion here [indicating] would go into the preferred stock of the Dominion Steel Foundries, and then the interest item here [indicating] would only be the interest item on that portion of preferred stock carried. This portion [indicating] would be separate in the Canadian Government annuity form.

Now, the man might work and retire with a Canadian Government annuity of $42.62 per month. Now, he may get from the company enough credit to probably have $60 or $65, so he would get $102.82 guaranteed by the Canadian Government in annuities, which are strong in character, and by preferred stock in the Dominion Steel Foundries—and they have about the same ratio as we have, about one-tenth of preferred stock to their outstanding capital stock.

So there would be a guaranty of $102.82. It is true at his death this [indicating] would be dissipated if he took the fully liquidated annuity, but he has the choice of taking less and leaving a portion for his wife and family.

But certainly this portion [indicating] represented in the preferred stock, would continue after his death in his family, as the contract, as drawn, is verbatim with the Joslyn Manufacturing & Supply Co. contract. The only thing we did was install the Dominion Foundries name and where we have the State of Illinois securities requirements for investments of our members' contributions, they have the Government annuity.

Mr. JOSLYN. I would like to make the statement here that we haven't the slightest interest in the introduction of this plan by anybody. We have never asked anybody to put it in, and when we respond to requests we accept nothing, we pay our own expenses, and when we are asked we have gone and paid our own expenses and done what we could to show them what we do. We have no interest whatever in its increase.

Senator VANDENBERG. The plan is based on the integrity of preferred stock?

Mr. JOSLYN. Yes; to some extent. No; the man is getting a wonderful saving, a compound interest at 8½ percent, which is a pretty hard thing for anybody to get; even though the company was bankrupt, he would still get everything he put in with 8½ percent compound interest, because that is all in securities that the company hasn't anything to do with.

Senator VANDENBERG. He can't lose his own money?

Mr. JOSLYN. No. Furthermore, I am asking and contending that what we should have is this 5-percent Government bond, with the privilege of putting part of our own funds in there as well, of our own contributions, in there as well.

Senator VANDENBERG. Because certain stocks have been known to fail?

Mr. JOSLYN. And there is a limit to preferred stock—we can't go on issuing preferred stock forever for the profit-sharing plan.

Senator VANDENBERG. I think this schedule that has been used ought to be inserted in the record.

Senator HERRING. It will be inserted at the proper place.

Mr. ROEDER. May I tell you about some of the credits of some of the members of our fund?

We have a warehouseman who has never operated outside of the warehouse and shipping department who, in 19 years, saved $2,874. The company in that time gave him $8,676, and in 19 years the combined contribution by member and the company contribution in the form of a bonus earned $17,455. To give the man a total credit in 19 years of $29,106. His record for 1938 will be sufficiently large so that he will leave the fund—he is aged 60—on January 1, with $31,300.

During this period, using the $29,000 accumulation in the profit-sharing fund, he has earned in total salary $56,510. That was his total wage in 19 years. So that we did something for that worker when we saved 52 percent of his salary—I think it is about 52—in excess, anyway, of 50 percent of his salary, and there are very few men that save anywhere near that amount.

We have a girl worker who has been with us 18 years. The memorandum says that this employee's first week's pay was $7 per week.

Mr. JOSLYN. That wasn't 19 years ago, that was about 30 years ago.

Mr. ROEDER. Last year her wage was $2,520. In 18 years she saved $1,772. The company gave her $4,667. The interest amounted to $8,026——

Mr. JOSLYN (interposing). There is your compound interest again, Senator, it is a great thing.

Mr. ROEDER. The average yearly accumulation of contribution by the member, company bonus, and interest, is now $803.66. That is the average, and last year it was $2,520 that the young lady earned. So you can see the ratio between the accumulation per year and the salary. And that girl has $14,465 in the fund after 18 years of work in the main office of the Joslyn Manufacturing & Supply Co.

Now, you say that is well and good, those are beautiful accumulations and credits due to the fact that you have gone back 20 years and there is your help [indicating], four for one.

If you will bear with me, I will try to copy the figures of a man who went into the fund in the very dark years of the depression. He entered the fund in 1930. In 1931, 1932, 1933, 1934, 1935, and 1936 he enjoyed membership. During that period he gave $687.56. The company paid him $1,019.46, or approximately 1½ for 1, and even during the dark years that $687.56, plus the company bonus, earned $333.96.

You see the power of your interest during those worst years in the history of the United States.

So that man today has $2,040.98 to his credit, Senator, and he only contributed $687.56, and his membership was from 1930 on.

Senator HERRING. He went to work for you in 1927?

Mr. ROEDER. Yes. Now, no company would have had the courage to let him enter their fund knowing that conditions were as bad as they were in 1931. He entered the fund and he gets $1.31 for $1 on entering, not even encouraging, just a matched dollar. I can show you where your leading industries can do that.

In the next year he gets nothing, and the next year nothing, and the next year nothing. It makes him almost vulnerable to attack. Then he gets 20 cents for each dollar, still nothing to brag about.

But when the clouds lift and industry gets back, there is the picture [indicating].

Mr. JOSLYN. We never, during the depression, had one word of complaint from the men because we didn't have any profit to share then because they had received heavy sharing before. In other words, they are far better sports than the stockholders are.

Mr. ROEDER. Now, on that basis, say that at the end of 1936 there was $1,256 to the man's credit. We have our set rules, but this plan adopted by others is just as flexible as any ruler, you can bend it and adapt it to practically any corporate situation.

Assume that that man was an automobile worker in Detroit during the recent crisis when they couldn't agree whether anybody wanted to go to work or not, with 150,000 men overrunning the streets of Detroit.

The surrender value there was sufficiently large that they could have given him help and carried him. In giving him help they would have taken him off the streets, probably giving him work at 50 percent of capacity. He may have had say $28 a week, and they made him live on $24, and loaned him $10, look how long they could have carried him, and when the skies lift he could start to pay this back out of his contribution in the good years. His earnings would still go on on that $2,000 credit that I showed you.

Now, I say it is a buffer, it is something to fall back on. It helps carry your employees in the sick lean years.

Mr. Joslyn made the statement about the fund loaning money during the depression.

Mr. JOSLYN. They can carry themselves, we don't have to carry them.

Mr. ROEDER. That is right.

I have an intimate knowledge of this plan, living with these people. No profit sharer lost a home during the depression. I had the great satisfaction of walking in where a banker was going to take the man's home away, and say, "What does he owe, I will take it out of your hands, as you are not willing to carry him and we will take it over for him."

And we just bought the paper and transferred it. We not only had the homes, Senators, we had the man's credit in the fund as collateral, and when you help a man he is not going to run away from you.

Every one wondered how we could do it. I will show a case where a bank sold us a $13,000 mortgage for one of our workmen, and we got it for $9,000, and Mr. Joslyn will tell you that we did not make the $4,000 difference. We said, "Here you are (employee) we made it for you, take it."

If that is paternalism, I would like a lot more of it, and if we had a lot more of it, there would be less troublesome relationships between capital and labor today. There shouldn't be any difficulty between labor and capital today. The man who was a capitalist today was the worker of yesterday, and there are too many capitalists today who write their autobiographies about how they rose from bootblacks, and how they couldn't have risen to the top unless they demanded a lot for themselves. It was fair then because they were on the other side. A lot of them take a selfish position, and if they are on the top now they don't want that same demand by their workers.

There shouldn't be that difficulty. In other words, a man is entitled to benefit to the extent that his employer benefits. We are gradually getting away from the old rule of it being a privilege to work for a man.

We didn't come equipped to bring testimony as to some of the workers but the Wall Street Journal made a survey of the plant, unsolicited, and I read from some of the expressions of the members.

The man whom I showed you was going out with $31,300—Father Coughlin, during the Detroit difficulty, or just about the time it started, got wind of the Joslyn plan and telephoned, long distance to talk to this worker who had worked for us for 39 years. And here is what that worker said:

> Father Coughlin, of Detroit, asked me one time if I were sure of getting my money when I finished working for Joslyn, and I told him that I wished I was sure of going to heaven as I was of getting my money. Our boys here at the plant try to show their loyalty to the company by saving on materials and company property all they can. We all work together and save, so it makes a habit from youngest to the oldest worker. In the 39 years I have been here this practice of not wasting materials has saved the company thousands of dollars.

A man under him, who has never done anything but push a truck—the best job that he has had at that warehouse was to drive one of the Mercury electric trucks—has $12,000 to his credit after 15 years. He said:

> Profit sharing is great, for I would not have been able to save a dime myself.

The testimony of that girl I told you about with $14,465—they quote it as $15,000—after 18 years, this girl worker says:

> The profit-sharing plan gives me a complete feeling of security, for I know I will be taken care of when I stop working. I really try to work harder for the company because it has been so good to me. As long as I have been here I never have known an employee to leave due to discontent, and the only ones who left did so because of ill health or probably to get a better job—at least they thought so.

Another office worker said:

> We all feel we are a part of this company and have a direct ownership in it because of the profit-sharing plan. Everyone I know here is satisfied and expects to stay as long as permitted. There is a rare loyalty to the company and Mr. Joslyn because of the excellent treatment we all receive.

Those are statements solicited by the Wall Street Journal. There was no reason for the Wall Street Journal to enter the profit-sharing field. They never have done it in previous years.

You asked concerning the application of the fund to other industries. Am I boring you with figures, or would you rather I submit this?

Mr. JOSLYN. I think you should submit that, Joe, to them, and let them have it.

Senator VANDENBERG. Suppose you submit that to us; we would be very glad to have you do that.

You have made a marvelous contribution.

Senator HERRING. Yes, sir. Do you have anything additional you would like to submit, Mr. Joslyn?

Mr. JOSLYN. No, sir; I am open to any questions from you, Senator, or from anybody in the room, as far as that is concerned.

Senator HERRING. Thank you very much, Mr. Joslyn; we appreciate it very much.

Mr. Simonds, we must adjourn in 20 minutes, but we will be glad to hear you unless you will be here tomorrow.

Mr. SIMONDS. Anything you like, Senator. I have enjoyed very much Mr. Joslyn's testimony, and if you have any idea of passing any laws, if you will let Mr. Joslyn put out the plan, or at least give him the veto power, I think I will sign it on the dotted line. I don't know how well it would fit other industries, but I am sure it would fit mine.

Senator HERRING. Fine.

Mr. SIMONDS. I have had the greatest treat I have had in years to have Mr. Joslyn give his plan in detail. I wanted to ask Mr. Joslyn how much of the voting stock he owned.

Senator HERRING. How much of the voting stock in the company do you own, Mr. Joslyn?

Mr. JOSLYN. That is a very ticklish question, a good deal of it. I suppose I don't own so much now, because I managed to slip a good deal of it to my children to avoid the Government taxes, but my family I suppose own 70 percent of the common stock. So we will still go on with the profit-sharing plan.

Senator HERRING. Now, Mr. Simonds, will you proceed?

Senator VANDENBERG. Would Mr. Simonds rather go on in the morning when he would have more time?

Senator HERRING. It will be perfectly agreeable to us if you so desire.

Mr. SIMONDS. I don't think, Senator, that I have very much to contribute. Our outfit isn't a very big one, and you have had so many important witnesses here that I feel as though I could contribute all that would be of interest in that 20 minutes.

Senator HERRING. I notice from your letter that it isn't a very large firm—only $13,000,000.

Mr. SIMONDS. We have a capital of around $13,000,000 to $14,000,000, and about 2,500 employees.

Senator HERRING. Well, all right, you may proceed if you desire.

STATEMENT OF ALVAN T. SIMONDS, PRESIDENT, SIMONDS SAW & STEEL CO., FITCHBURG, MASS.

Mr. SIMONDS. Of course, we are quite old, being 106 years in business in the family, and, of course, we don't usually speak to competitors unless they have been in business 50 years. We wouldn't speak to a fellow like Joslyn at all.

But somebody invented the term "Economic Royalists"—I don't know who did that, but I have an idea. But anyway, since it was invented we rather like the name, because the business has been in the family for so long, and we are continuing it successfully, that we think that we are entitled to the premier title, if there should be one, compared with other concerns who haven't been able to weather the storm so many years.

Of course, as I understand Mr. Joslyn's plan, it is a sort of compulsory savings, I should say. It is paternalistic to that extent. That is the reason I asked how much stock he owned, because I should say that the plan entirely circulates around Mr. Joslyn's personality. But still it is a remarkably good record.

I have read all the profit sharing plans back for 100 years that I could put my hands on, and the general rule is that they don't work out any too well.

Senator HERRING. Well, of course, there must be a personality behind any of them, but the fact that 20 other companies are using this same plan successfully, would indicate that there are at least 20 others.

Mr. SIMONDS. As I said, I thoroughly enjoyed the hour and a half that I have been here, and I say if you have any better plan appearing before you I can't imagine it.

My business was in six different codes during the N. R. A. period, and we make saws and machine knives and files and hacksaws, and grinding wheels, and tool steel, and all of those are an outgrowth from nothing.

We run a paternalistic, autocratic family affair. Up until a few years ago my two brothers and myself didn't use to report profits at all, as being of no particular interest except to a few of the older men in the business who owned stock. We have profit sharing to the management group only, and that is entirely without plan, picking out the young men we like and either helping them to buy stock, giving them stock, or seeing that they own stock, and if they don't want stock we don't want them.

Most profit-sharing plans have the difficulty, in the first place, that there is no definite rule for *profits*; nobody can determine a profit. We keep one set of books for the Government, one for the Securities and Exchange Commission, and one for ourselves, and they are all different. So that anybody knows what the profit is I would like to have him tell me, because I don't; at least, I don't know it until 10 years afterward. So I should hate to have the men have to wait that long to get their share of the profits.

We have a pension system that is 35 years old and is still without rhyme or reason, purely in our judgment as to whether the man is entitled to a pension and how much it ought to be. The company, the stockholders, contribute 100 percent to that.

On our aid and benefit plan, which is for sickness and death, we have a plan by which it is voluntary for each man to contribute so much a month and the company contributes 20 percent on every 80 cents contributed for that. That is also 35 years old.

We were inclined to believe that we wouldn't care for Government supervision, Government-supervised profit-sharing laws, but if a fellow like Joslyn, with a remarkably good experience, should determine the major parts of that law and should have veto power over the parts that he didn't like, I am sure a great many industrialists would like to see it tried for 10 or 15 years to see whether it would work out or not.

Senator HERRING. There has been no suggestion from this committee of any law that would make profit sharing compulsory, as you understand, Mr. Simonds.

Mr. SIMONDS. I didn't understand that, because I didn't know what the committee was aiming at except that I supposed that you had a choice of the corporation to accept a profit-sharing plan under one form of taxation and not accept under another.

Senator HERRING. There has been some suggestion of incentive taxation, but there has never been any suggestion that we might even suggest such a law——

Mr. SIMONDS (interposing). I talked with my brother a little before I came down and he said, "Just one more law and we might as well quit entirely."

So we would like to have you take off about 75 percent of all the laws that have been put on the books in the last 6 years. I believe it would benefit the working man and all the community combined, but of course that is only asking what we want.

Senator HERRING. I hope that you have modified the opinion you expressed in your letter that you thought that we were wasting our time, this committee, since you have heard Mr. Joslyn's testimony. Don't you think we are really accomplishing something if we can place such information as that before the employers?

Mr. SIMONDS. Oh, as I said to you, Senator, I never enjoyed myself so much as I did hearing Mr. Joslyn, and to have the details of the plan set before me, because we are very socially minded in our business. In fact, I voted for Norman Thomas in 1932. [Laughter.]

But I should like to see an experienced man like Mr. Joslyn consulted if you think of writing any laws along this line.

Senator HERRING. Well, speaking for myself, if we recommend a law we will put his name right in as the dictator of the law, if we are going to make it compulsory.

Mr. SIMONDS. Speaking for yourself?

Senator HERRING. Speaking for myself; yes.

Mr. SIMONDS. I congratulate you, Senator. I don't think I have anything to add to the many important men that you have had here, very much larger in size.

I must say I don't look—unless the present bracket taxes are put out of business—I don't think it makes very much difference whether you have profit sharing or not because my principal business in life is to provide capital for the working man. It takes about $5,000 of capital for everybody that we have in our business and I shall no longer provide capital under my prospective inheritance tax and the other taxes that I have had to pay that are running two or three times my income. So that the working man will have to, in the future, provide his own income, his own capital, so far as I am concerned.

Senator HERRING. Well, that is being provided under the Joslyn system.

Mr. SIMONDS. Well, that is all right; I don't care how it is done, but I am sure that capital is needed in any industry, and I am sure that the capitalists and the laboring man must find a way to work. Usually harmoniously together. They are Siamese twins who cannot be separated in any way whatever, and any scheme that makes the cooperation better is a splendid scheme.

I am not going into the matter to any great extent, because I have nothing to offer except a general proposition, that I am very much interested in business or have been, but am being forced out by the inheritance tax situation which I have consumed six-sevenths of now, according to the statistics of the life-insurance companies, and I must provide—I am hoping that the next generation will not go in their shirt sleeves, having been three of them in the business, I hope that the royalty will continue in the blacksmith business we are in, and that they will be successful blacksmiths, and not necessarily in their shirt sleeves.

Senator HERRING. Have you any questions?

Senator VANDENBERG. No; I should think you would want to ask him a lot of questions. [Laughter.]

Senator HERRING. I might ask about some of these statements in his letter.

Senator VANDENBERG. I am very sympathetic with about 75 percent of your viewpoint.

Mr. SIMONDS. I am glad to find that in Washington, that is more than I expected to find when I came here.

Senator VANDENBERG. Well, there is a little more here now than there was a few weeks ago.

Senator HERRING. Well, unless you have something else to suggest, Mr. Simonds, I don't know of anything I wish to ask you. I would be glad to hear anything you have to say, though.

Mr. SIMONDS. Well, I don't think I can add anything toward profit sharing inasmuch as we haven't thought it was a very good thing except that it was arbitrarily controlled, and Mr. Joslyn has a very fine scheme of considerable duration. Of course, we don't consider 20 years much in our business, but then it is a period.

Senator HERRING. Thank you very much.

Senator VANDENBERG. Thank you.

Senator HERRING. We will now take a recess until 10 o'clock tomorrow morning.

(Whereupon, at 3:55 p. m., a recess was taken until the following day, Friday, December 9, 1938, at 10 a. m.)

SURVEY OF EXPERIENCES IN PROFIT SHARING AND POSSIBILITIES OF INCENTIVE TAXATION

FRIDAY, DECEMBER 9, 1938

United States Senate,
Subcommittee of the Committee on Finance,
Washington, D. C.

The committee met, pursuant to adjournment, at 10 o'clock a. m. in room 312, Senate Office Building, Senator Clyde L. Herring presiding.

Present: Senators Clyde L. Herring and Arthur H. Vandenberg.

Senator Herring. We will come to order. Mr. Fetzer, of the Peoples Drug Co.

STATEMENT OF M. B. FETZER, WASHINGTON, D. C.

Senator Herring. You are Mr. M. B. Fetzer?

Mr. Fetzer. Yes, sir.

Senator Herring. An employee of the Peoples Drug Co.?

Mr. Fetzer. Yes, sir.

Senator Herring. Your vice president was here the other day and told us about the operations of your company. We are glad to have you come in as an employee of the company and tell us, from your angle, what you think of it.

Mr. Fetzer. Thank you. Are there any particular questions?

Senator Herring. Just proceed in your own way.

Mr. Fetzer. Well, I have been with them 17 years. I am now manager of one of their larger stores. We are paid a very substantial salary, and also we work on a profit-sharing basis, taken from the net profits of our store operations; 3 percent of the net profits being taken and divided between the manager and his assistant, 75 and 25 percent, respectively.

The employees come under what we call a "wage-dividend basis" besides their salaries. That is 25 percent, 35 percent, and 50 percent. Over 6 months continuous service entitles them to 25 percent; to 2 years, 35 percent; and 2 years and over it is 50 percent of a month's salary.

Then we have a number of protections in our organization, such as life insurance, health and accident; we have hospitalization, and we have old-age retirement. The employee pays about 65 percent on the premium. With the exception of hospitalization—that is given to us absolutely free. They offer us 70 days of sickness, and $4 a day to pay for the hospital room. They give us $20 for anesthetics and X-rays.

Senator Herring. About what is your annual salary without the profit sharing, would you say?

Mr. Fetzer. You mean in dollars and cents?

Senator Herring. Yes.

Mr. FETZER. Mine runs around $3,800.

Senator HERRING. Without the profit sharing?

Mr. FETZER. Yes, sir.

Senator HERRING. That is as much as any of the other drug companies are paying for similar work that do not have profit sharing?

Mr. FETZER. I believe so, sir.

Senator HERRING. And in addition to that you get 75 percent of 3 percent of the profits of the stores that you mentioned?

Mr. FETZER. Yes, sir. We also get life insurance, that has a limitation to it. If you want me to go into detail, I can do so very easily.

Senator HERRING. No; that will not be necessary.

Mr. FETZER. The health and accident, of course, gives us two-thirds of our salary every week for 13 weeks. The assistant manager and manager draw full time at all times, they are not deducted. I believe that is also true for the executives. The old-age annuity calls for retirement at 65 years of age, 55 years of age optional.

Senator HERRING. You have had this profit-sharing plan for the full 10 years that you have been with the company?

Mr. FETZER. Yes, sir; the full 10 years since I have been with the company. I have been 17 years with the company. I have shared in the management end of it for 12 years.

We have the vacations, we have picnics and social functions. We have an educational program that I think is an outstanding thing of the country. We have a promotional department in our stores. We have a man who teaches new employees. The management also comes in and makes different talks on things they have in mind. Then outside of that we have an educational program that permits students to go to the George Washington University. We draw the prospective students from the various departments throughout our stores, through their application. Twelve boys are chosen to take entrance examinations to George Washington University, and out of that bunch would be five that pass. We furnish them with money and part-time work while they go to school, and after they are graduated they are not obligated to work for the company unless they see fit to do so. They have 10 years to pay the money back. There is little to pay back, because they get part-time pay while they go to school and it almost carries them.

Then we have another thing that I think has created quite a good feeling in our organization. When there happens to be a new-born baby coming along, this maternity kit goes to the home. That creates one of the best feelings that I think you can possibly have.

We have a credit union within our organization, where we can borrow or deposit money. They pay us dividends of 6 percent. They charge us 1 percent of the monthly loans up to $399, and one-half of 1 percent over that.

Senator HERRING. How many employees are in the store that you manage?

Mr. FETZER. One hundred and three.

Senator HERRING. What is the labor turn-over there?

Mr. FETZER. I have very little labor turn-over. In the food department is my heaviest turn-over. We have perhaps a 5-percent turnover due to employing many boys during school vacations.

Senator HERRING. A 5-percent turn-over?

Mr. FETZER. Yes, sir.

Senator HERRING. Do you have much loss from shortages or breakage?

Mr. FETZER. We have very few.

Senator HERRING. You have very few of those things?

Mr. FETZER. Yes.

Senator HERRING. I mean from your employees.

Mr. FETZER. We have a department in our warehouse that we call the obsolete department, and they furnish us cost credit on losses.

Senator HERRING. What I mean is the shortages of cash on the part of the employees.

Mr. FETZER. We have an overage and shortage fund. Each employee is allowed 25 cents a day.

Senator HERRING. I mean from dishonesty.

Mr. FETZER. I have had very little of that. I have had three cases in 4 years.

Senator HERRING. I am trying to get the effect of this policy on the honesty and efficiency of the employees.

Mr. FETZER. I misunderstood. I thought you meant merchandise breakage.

Senator HERRING. You think it helps in that respect?

Mr. FETZER. Oh, my Lord, yes, sir. We have had three cases in 4 years of actual theft when cash was involved.

Senator HERRING. So it is really a help in that direction?

Mr. FETZER. I'll tell you, when a man comes to our store he never wants to leave. We have had that impressed on us time after time. I have promoted over 200 boys and girls from our store into other stores of the organization; I trained them there; and if they leave our employ everyone of them wants to come back.

Senator HERRING. This policy you have been outlining, you think, has had much to do with that?

Mr. FETZER. I think it has all to do with it. They know their chances for promotion are 100 percent; they know they are going to be treated right; and they also know that they are getting a living wage.

Senator HERRING. I think that is very fine. Unless you have something else, Mr. Fetzer, we appreciate your coming over.

Mr. FETZER. I have outlined about what the operation of my store is.

Senator HERRING. Thank you very much.

Mr. FETZER. Yes, sir.

Senator HERRING. Mr. Shineman, treasurer of Beechnut Packing Co.

STATEMENT OF E. W. SHINEMAN, TREASURER, BEECH-NUT PACKING CO., CANAJOHARIE, N. Y.

Senator HERRING. Mr. Shineman, is Mr. Sharpe with you?

Mr. SHINEMAN. Yes, sir.

Senator HERRING. You have a profit-sharing plan, do you not, Mr. Shineman?

Mr. SHINEMAN. We call it the Beech-nut welfare plan.

Senator HERRING. Will you please tell us about it?

Mr. SHINEMAN. The plan was started in 1912. What I give you now will pertain merely to plant workers and office workers, and not to salesmen.

For a period of 3 years we stated our plan to our people in letter form. In 1915, we thought it would be a fine idea to give them something that was a little different than a letter. At that time we put out a certificate such as this [indicating], which embodies a plan practically the same as we offered in the letter the first 3 years.

This certificate provides four different things. In the first place, we give $3 per capita for each year of service around Christmas time. We give the employees for sickness, limited to 26 weeks, from 50 percent of his wages to 100 percent, depending on the length of service. For retirement and old age we give the employee 2 percent of the day wage for each year of service. For natural death while on the pay roll we give them insurance protection. That is, nothing for the first 3 years, and then starting at $250, up to $2,000, depending on the length of service.

Senator VANDENBERG. That is nothing for the first year?

Mr. SHINEMAN. Nothing for the first 3 years. When he touches 3 years he is insured for $250.

Senator VANDENBERG. Are you looking at the same thing I am?

Mr. SHINEMAN. I believe so.

Senator VANDENBERG. The first year is the only one which is exempted.

Mr. SHINEMAN. "One full year to 3 years, none."

Senator VANDENBERG. You are speaking about the third column, and I am speaking about the fourth column.

Mr. SHINEMAN. Yes; but is there not "none" at the top there?

Senator VANDENBERG. For just 1 year.

Mr. SHINEMAN. One to three years.

Senator VANDENBERG. Oh, yes.

Mr. SHINEMAN. The certificate which we issued in 1915, we followed until 1927. In 1927, we changed the certificate, not so far as figures are concerned, but so far as phraseology is concerned. The certificate which you hold there, on the back, says "series 1927." That is the certificate which we are operating under today. Now, the changes in this certificate—do you want me to read the certificate part? It is very short.

Senator HERRING. Yes; go ahead.

Mr. SHINEMAN. It reads as follows:

> This certifies that (employee) entered our employ in the year (blank) and may receive the benefits for continuous service while on our pay roll, which we hope but do not guarantee to provide as in the following schedule, providing legal liability is unsought by the employee, or his or her legal representative.

Senator VANDENBERG. What is the meaning of that final phrase?

Mr. SHINEMAN. You mean "providing legal liability?"

Senator VANDENBERG. Yes.

Mr. SHINEMAN. The fact is that we offer certain benefits to our employees. We feel, of course, that we should have the management of these offerings, and that is the reason that phrase has been put there.

Senator VANDENBERG. In other words, if the certificate is legally challenged at any point the holder has lost all rights under it?

Mr. SHINEMAN. Well, no one has ever yet forfeited his rights thereunder because of that phrase. We simply want it as a lever for ourselves, if anyone should contest. On the latter certificate, the one of 1927, you will note at the bottom of the "sickness" column there that we made a change, and it reads, "Payment is limited to 26 weeks in any 3-year period." The first certificate did not have the 3-year period limit.

Senator VANDENBERG. Why was the change made? Because of any adverse experience?

Mr. SHINEMAN. No; simply a matter of safety. We had gone along quite a while without any change; and while everything seemed quite satisfactcory, and it appeared that we should make it a little more plain to our people and define it in better terms.

Under the old age and retirement we have here, "Applicable upon retirement from service at age 70 or at the company's option under age 70." Now, under the next column there——

Senator VANDENBEG (interposing). Excuse me.

Mr. SHINEMAN. Yes, sir.

Senator VANDENBERG. The old age and retirement benefits do not start until 10 full years of service, is that right?

Mr. SHINEMAN. That is right. In other words, that would mean a person employed just before 60 would not be entitled to very much.

Under the heading, "For natural death occurring while on pay roll," we have something that was not on the original certificate.

In case employee is on retirement from service, the amount of insurance upon death is based on the length of active service and is subject to reduction by the amount paid while on retirement.

Senator VANDENBERG. I think the record should show what these figures are in each of these columns.

Mr. SHINEMAN. You mean the different years?

Senator VANDENBERG. Yes. I suggest that you leave a copy with the stenographer and that all four schedules be inserted in the record at this point.

(The matter referred to is as follows:)

Years of consecutive service	Annual cash distribution	For sickness caused by duties while in service	For old age and retirement from service	For natural death occurring while on pay roll
1 full year to 3 years.		50 percent of wages.	None	None.
3 full years to 5 years.	Basis: $3 per capita for each year of service to employees in active service.	do	do	$250.
5 full years to 10 years.	do	do	do	$500.
10 full years to 15 years.	do	75 percent of wages.	2 percent of the day wage for each year of service. Maximum payment $25 per week.	$750.
15 full years to 20 years.	do	do	do	$1,000.
20 full years to 25 years.	do	do	do	$1,250.
25 full years to 30 years.	do	do	do	$1,500.
30 full years to 35 years.	do	100 percent of wages.	do	$1,750.
35 full years and over.	do	do	do	$2,000.
Special conditions.	do	Payment is limited to 26 weeks in any 3-year period.	Applicable upon retirement from service at age 70 or at company option under age 70.	In case employee is on retirement from service the amount of insurance upon death is based on the length of active service and is subject to reduction by the amount paid while on retirement.

Mr. SHINEMAN. Then we have a provision in the 1927 certificate, which was not in the first certificate, "Employees who have attained the age of 50 years when first employed, or do not pass a satisfactory physical examination when employed, participate only in the 'annual cash distribution' and not in any of the other benefits above mentioned. In addition we reserve the right to withdraw or modify at any time the above schedule and supplementary statements and issue a new certificate in place thereof. Furthermore, this certificate supersedes all former certificates issued."

Senator VANDENBERG. This is a new clause in this particular certificate?

Mr. SHINEMAN. Yes, it is.

Senator VANDENBERG. Born of any necessity out of your experience?

Mr. SHINEMAN. No, sir; but we felt that we should define matters more clearly to our people.

Senator VANDENBERG. Does this indicate that each employee passes a physical examination prior to employment?

Mr. SHINEMAN. Of late we have each employee in the plant submit to physical examination by our company doctor.

Senator VANDENBERG. Is this compulsory?

Mr. SHINEMAN. Well, we ask them, and nobody has refused that I know of.

Senator VANDENBERG. I am simply trying to get into the record the complete theory upon which you operate. If an employee declined a physical examination might he still be employed and not receive a certificate?

Mr. SHINEMAN. Inasmuch as we have never had the occasion, I could not tell you.

Senator VANDENBERG. They always are perfectly willing to proceed under that rule?

Mr. SHINEMAN. So far as I know, everyone is perfectly willing to submit.

Senator VANDENBERG. How many employees have you under this plan?

Mr. SHINEMAN. We have a total of 2,800, including all. Under this plan there would be about 1,700 factory and office employees; in addition we have approximately 1,100 outside sales employees, and so forth, not classified under this specific certificate, but who participate in all benefits except the annual Christmas distribution of $3 for each year of service.

Senator VANDENBERG. How much does the whole thing cost the Beech-nut Packing Company per annum?

Mr. SHINEMAN. At the present time, we are paying, under this plan, $100,000 a year, about. In addition, we are reserving for accumulation at the present time about $150,000 additional per year.

Senator VANDENBERG. I do not quite understand that. You mean that is in reserve?

Mr. SHINEMAN. That is in a reserve fund to back the plan.

Senator VANDENBERG. In the event of any subsequent difficulty?

Mr. SHINEMAN. Yes. As an example, suppose we should some time substitute our plan for an insurance company, I think that we can operate our plan cheaper than we could to put it out with an insurance company, but the time might come when we would decide to put it out, and in that event we have at this time, to the close of last year, a reserve of $961,000 to back the plan.

Senator VANDENBERG. Is this reserve chargeable to operating expenses for the purpose of tax exemption?

Mr. SHINEMAN. No, sir.

Senator VANDENBERG. It should be, should it not?

Mr. SHINEMAN. Being as we operate the plan, any reserve that is not paid out is not deductible.

Senator VANDENBERG. Don't you think, as a matter of simple equity and as a matter of sound incentive to social service of this character, that the very least the Government could do would be to permit you tax exemption with respect to reserves of that character?

Mr. SHINEMAN. We are willing to abide by the Government's decision. We are willing to work with the Government, and the regulations do not permit this reserve as a tax deduction, and we do not deduct it for tax purposes.

Senator VANDENBERG. If the Government did say that such reserves were deductible, don't you think it would encourage the creation of such reserves?

Mr. SHINEMAN. It might.

Senator VANDENBERG. Is there any reason, in sound logic, why the exemption privilege should not apply just as much to an honest reserve as to any current expenditure for the same purpose?

Mr. SHINEMAN. I would think so.

Senator VANDENBERG. You would think they ought to be treated alike?

Mr. SHINEMAN. I would think so.

Senator VANDENBERG. Yes.

Mr. SHINEMAN. But if you will note the phraseology of the welfare certificate, we are hoping to provide. It is not absolutely definite, like a life-insurance certificate, but we are going to play with our people.

Senator VANDENBERG. Are these reserves irrevocably set aside, or are they still within the recapture reach for other purposes?

Mr. SHINEMAN. We have never yet used any of the funds, and I do not expect that we will. I might advise you that the offset to the reserve is not earmarked on the debit side.

Senator VANDENBERG. How is the reserve invested?

Mr. SHINEMAN. The reserve is not set up separately, but is in our own cash account, in our own investments, in our assets unallocated.

Senator VANDENBERG. What has been your experience under this whole activity? Do you conclude that it is advantageous to the company?

Mr. SHINEMAN. I firmly believe that it has been advantageous to the company, because we have had very little trouble with employees. Everything seems to be very harmonious.

Senator VANDENBERG. Does it reduce your turn-over?

Mr. SHINEMAN. I firmly believe it does, because of the fact that if a party leaves us he leaves the plan.

Senator VANDENBERG. At no point is there any employee contribution to the plan, is there?

Mr. SHINEMAN. There is not. May I follow now with the next step in relation to this certificate?

Senator VANDENBERG. Yes. First, may I ask you whether you know whether, if the reserve were placed in an irrevocable trust, that it would be tax deductible?

Mr. SHINEMAN. We have not discussed that matter—well, pardon me. May I have your question once more?

Senator VANDENBERG. If the trust were set up irrevocably, would it not be deductible currently from your tax return?

Mr. SHINEMAN. I am not prepared to say.

Mr. WALSH. Under section 23-P they are allowed the deduction, provided it is an irrevocable trust, at the rate of 10 percent for each of the first 10 years.

Senator VANDENBERG. Ten percent of what?

Mr. WALSH. The fund set up.

Senator HERRING. Ten percent of the fund set up?

Mr. WALSH. Yes.

Senator VANDENBERG. Go ahead with your own statement.

Mr. SHINEMAN. I would like to make this statement, in addition to the welfare certificate, as to some of the things that we do for our employees:

In 1936 we announced to all factory people, those that had been with us 1 full year would receive 1 week's vacation. We are now announcing in 1938 that beginning with 1939 all factory employees will enjoy a 2 weeks' paid vacation, providing they have been with the company for 2 full years. In addition to this, we have already announced to our people that we will pass out at the holiday season 1 week extra, limited to $50, providing the employee has been engaged prior to October 1 of this year. Also we are passing out 2 weeks' pay, limited to $100, to all employees engaged prior to July 1, this year.

Senator VANDENBERG. You said these certificates to the employees represented a cost of about $100,000 a year. I seem to have a statement before me for 1937 which would indicate that you paid out $273,000 on account of all of these benefits.

Mr. SHINEMAN. Yes; payments under the certificate plan in your first column there shows $97,000, and what I am telling you now, your 1 and 2 weeks' payment, is the second column, which I have just announced to you.

Senator VANDENBERG. So the grand total of benefits is $273,000 for 1937?

Mr. SHINEMAN. Well, I would leave the vacation part out. You notice I have added there paid vacations to employees who had never enjoyed paid vacations before.

Senator VANDENBERG. Yes.

Mr. SHINEMAN. I would leave that figure out and say $240,000 is the grand total.

Senator VANDENBERG. The interesting thing I wanted to bring out was the relationship that that figure bears to your final net income for the year, which seems to indicate, speaking roughly, that 9 percent of net earnings has gone into these benefits. Is that correct?

Mr. SHINEMAN. Nine percent are the cash benefits. On top of this we are reserving $150,000, approximately, that is in round figures, additional.

Senator VANDENBERG. Well, the payments are 9 percent, are they not?

Mr. SHINEMAN. That is right.

Senator VANDENBERG. How long have you been appropriating to the reserve?

Mr. SHINEMAN. Ever since 1913, gradually.

Senator HERRING. It would be helpful if you can give us an average case, an average employee, just about what he draws in salary and what he gets in his benefits.

Mr. SHINEMAN. Well, our oldest employee, as an example, will receive under the $3 per capita for years of service, $141 this year. That is for 47 years of employment. That party will also get his 2 weeks maximum of $100.

I would like to make this mention also, that we have employed in our office one man who is 81 years of age. We have one man employed in our plant who is 81 years of age. We consider that they are doing a fair task. Those parties, while they are not the highest type people, will draw out of this fund, one over $100 and one just under $100.

Senator VANDENBERG. Then, in addition, if any of these long-time employees are sick, they have the benefit of 100 percent of their wages up to 26 weeks?

Mr. SHINEMAN. Yes; in any 3-year period.

Senator VANDENBERG. In any 3-year period?

Mr. SHINEMAN. Yes.

Senator VANDENBERG. If they die they have the benefit of the $2,000 life insurance policy?

Mr. SHINEMAN. Yes, sir.

Senator HERRING. As to this average employee now, what, in addition, would he get?

Mr. SHINEMAN. The average employee?

Senator HERRING. The one you just mentioned.

Mr. SHINEMAN. Under both plans?

Senator HERRING. Yes; I was just wondering as to the relation of the benefits to the salary that he gets in the first instance.

Mr. SHINEMAN. That would have to be a guess. Your high man, as I gave you, would be about $240. The low girl would be around—well, of course, the newer employees engaged prior to July 1, 1938, would run down to $50 or $60.

Senator HERRING. Just give us a typical average of them all.

Mr. SHINEMAN. I think that would run well over $100.

Senator HERRING. And the base wage is equal at least to what is being paid in competitive plants?

Mr. SHINEMAN. Our starting wage in the plant is 44 cents an hour for women and 55 cents for men. In the office our starting wage is $14 for such as a high school girl and for a boy $16 per week, and as to others, it depends on their experience and depending on what kind of a job we have for them.

Senator VANDENBERG. Is there any collision between the benefits under your certificate and the benefits under the New Social Security Act?

Mr. SHINEMAN. I am just ready to give you that now.

Senator VANDENBERG. All right, go ahead.

Mr. SHINEMAN. On January 1, or in December, we issued a letter to be effective on January 1. The letter reads as follows:

> Effective January 1, 1938, provisions under the Welfare Certificate Plan for "Old Age and Retirement from Service" and for "Natural Death Occurring While on Pay Roll" are terminated except as to benefits accumulated and created under these categories to December 31, 1937, for individual employees, which benefits the company hopes but does not guarantee to provide in accordance with the terms of the certificates. Provisions for all other benefits, where applicable, continue upon the terms as stated in the welfare certificate.
>
> The foregoing change is occasioned by the benefits provided in and the expenses resulting from the Federal Social Security Act and various State unemployment insurance laws.

Dated December 20, 1937. At the time we put this letter out we asked our employees to sign a receipt and an acceptance for that change.

Senator VANDENBERG. Now, what is the status of the employee relatively under the Social Security Act to which he must now look for these last two series of benefits, and his status under your original certificate plan? Is he better off under the Social Security Act, or worse?

Mr. SHINEMAN. I would hesitate to say.

Senator VANDENBERG. Well, it is a mathematical calculation, is it not? I mean mathematically is he better off?

Mr. SHINEMAN. You know our people appreciate this certificate. I am on the employers' side, so I cannot talk for the employees, but I firmly believe that the employees would rather receive that protection under this certificate right here.

Senator HERRING. Would they get more money under this certificate than under the new plan?

Mr. SHINEMAN. I could not tell you that. It depends on the employees' years of service under here and the years under the other plan.

Senator VANDENBERG. Have you ever made a calculation under the same given premises, as to which plan would give the more benefits?

Mr. SHINEMAN. I would like to mention this, that under this welfare certificate many of our people already are getting the maximum, or would get the maximum under the old age and retirement. They have earned it already. We are not taking anything away from our people. Many of them have already earned their $1,500 insurance credit, and even the $1,750, and even some of them have earned the $2,000 credit. Nothing is being taken away from those people. They have the Social Security added, but the newer employee, he receives his protection under Social Security and not under here, excepting as to the $3 per capita for each year of service. Everybody gets it. Sickness—everybody is entitled to it. These certificates are no longer passed out. Those that have them, have them. Those that have not, do not receive them, but they fare just the same under the two of these headings, whether they have the certificate or not.

Senator VANDENBERG. Well, have you made any calculation as to whether the Social Security Act will cost your company more or less than the cost under the last two categories in the certificate?

Mr. SHINEMAN. Well, I estimate that we will pay under Social Security, that is the company, this year, about $180,000.

Senator VANDENBERG. As compared with what figure, if you can give it, for the last two categories under this certificate?

Mr. SHINEMAN. Well, the actual cost in dollars under this certificate now is $100,000 a year.

Senator VANDENBERG. So the change is going to cost the company approximately $80,000 more a year?

Mr. SHINEMAN. I am talking cash under here as against cash under Social Security; I am not talking reserve.

Senator VANDENBERG. Yes. Well, if I understand you correctly, the transition from the certificate to social security will cost your company more and produce less for your employees?

Mr. SHINEMAN. Well, of course, if you take the reserve and add that in, why it is probably 50-50.

Senator VANDENBERG. Why do you need a reserve if you are canceling the last two categories?

Mr. SHINEMAN. We are not canceling them, we are only arresting them as of a certain date. We still have the obligation here, and in many instances with our employees we go beyond the certificate. Then, too, the investment of the reserve is not earmarked and the fund does not receive any credit from the investment, and because of that we are still reserving, adding to our reserve. We are also adding to the reserve because of the fact that some day we might want to turn it to an insurance company.

Senator VANDENBERG. Well, speaking generally from the standpoint of the company and standpoint of the employee, would you think you both were better off under the Federal Social Security Act, insofar as that has amended the certificate, or worse off?

Mr. SHINEMAN. We were both happy before the Social Security went in.

Senator VANDENBERG. Well, I think I can interpret that answer.

Senator HERRING. Unfortunately, we have a lot of employers where the employees were not so happy, that do not have this system.

Senator VANDENBERG. Let me put it this way: If the Social Security Act had carried an exemption, as many of us believe it should have, for existing systems of equality or greater advantage to the employee, in your judgment your system would have been exempt?

Mr. SHINEMAN. What is your question again?

Senator VANDENBERG. If the Social Security Act had carried an exemption for private plans that produced an equivalent or better benefit to the employee, it is your judgment, is it not, that your plan would have been exempted?

Mr. SHINEMAN. Well, I do not know whether it would or whether it would not. It depends on what kind of a ruling would be made by your committee.

Senator VANDENBERG. I fully understand that, and that you would be at the mercy of the overlords down here who run the show, but on a basis of equity and logic, in your judgment your plan would have been exempted under that proviso, would it not?

Mr. SHINEMAN. I should hope that it would.

Senator HERRING. At least you think it should have been?

Mr. SHINEMAN. Yes, sir.

Senator VANDENBERG. All right. You are almost as cautious as the National Manufacturers Association.

Mr. SHINEMAN. In these days you have to be cautious.

Senator VANDENBERG. I suppose so.

Senator HERRING. Just proceed, Mr. Shineman, if you have anything else.

Mr. SHINEMAN. Well, I do not know that I have. That concludes the certificate information, unless you have some questions.

Senator HERRING. I do not think you gave me your estimate of the average salary of the average employee. Is it $1,000 a year, $1,500 a year, or what?

Mr. SHINEMAN. Now, you mean the plant employees?

Senator HERRING. Yes.

Mr. SHINEMAN. Well, I have given you the starting wage here. We feel that that is fair as compared with what other competitive concerns are paying.

Senator HERRING. I am only trying to get the comparison of the salary or base wage in your own plant and the salary or base wage which is the prevailing wage in similar industries, and then in addition the benefits which you give to the employees. I am trying to find out just about how much this plan means to each employee.

Mr. SHINEMAN. I would say of the factory workers, men and women together, the average might be somewhere around $24. That is the working people. It would run between $23 and $24, and that is a guess.

Senator HERRING. And the benefits are about $240 per year?

Mr. SHINEMAN. The benefits in cash are $240 for some of the long-service employees, but the average is less.

Senator HERRING. That is the relationship I was trying to get. Have you had any labor trouble?

Mr. SHINEMAN. We have had no labor trouble.

Senator HERRING. Are you employees organized at all?

Mr. SHINEMAN. In our Rochester plant the A. F. of L. approached our people about 2 years ago, and we were happy to allow the people to decide for themselves, and they had a meeting, and our people decided that they would prefer to have their own organization, the Beech-nut cooperative plan, in other words.

Senator HERRING. Under the present law it is wise to let them decide for themselves, is it not?

Mr. SHINEMAN. Yes, it is; but it is immaterial to us; we do not care; but they decided, I think, about 3 to 1 for the Beech-Nut cooperative plan.

Senator HERRING. These benefits, were they arrived at after any negotiation with the employees which might be termed collective bargaining?

Mr. SHINEMAN. You mean these benefits here that I mentioned?

Senator HERRING. Yes.

Mr. SHINEMAN. No, sir; it was absolutely voluntary on the part of the company.

Senator HERRING. Did you call them in for discussion as to what the employees might think about it?

Mr. SHINEMAN. No, sir; we did not. We just felt that we wanted reward for our employees to a further extent.

Senator HERRING. I ask that question because one or two witnesses have testified that they believe this profit sharing and these other benefits are all right if arrived at through collective bargaining. I just wanted to get your idea on that.

Mr. SHINEMAN. No, sir.

Senator HERRING. Unless you have something else to suggest, Mr. Shineman, I think that is about all.

Mr. SHINEMAN. I do not have another thing.

Senator HERRING. Thank you very much.

Mr. SHINEMAN. Thank you.

Senator HERRING. Mr. Sharpe.

STATEMENT OF GUY W. SHARPE, SECRETARY, BEECH-NUT PACKING CO., CANAJOHARIE, N. Y.

Senator HERRING. Mr. Sharpe, you are secretary of the Beech-nut Packing Co.?

Mr. SHARPE. Yes, sir.

Senator HERRING. You may proceed.

Mr. SHARPE. I do not know that I can add anything. I first want to discuss, while it is fresh in my mind, the situation at Rochester. There was no feeling on the part of the employees that the conditions under which they worked were unsatisfactory. It developed from something which the management did not know, and I assume they should have known, and that was the unfortunate assignment of a foreman who was not at all popular, and the workers felt the only way they could get rid of him was to organize. As soon as that situation was corrected, everything cleared up, and everything has been fine ever since.

On the question of the termination of the old-age benefits, in view of the social-security legislation, I think, and I am quite sure of this because I have talked with some of them, the employees very much regretted the necessity for that taking place. They were better satisfied under the profit-sharing plan, so-called. There is, however, one advantage that I think, in all fairness, we should mention, and that is that in the event that an employee severs his connection with us, the social-security old-age plan provides for him a stop gap, because he does not lose the benefit of his experience, if I understand it, and it is continuous with his subsequent employment. However, so far as our operation is concerned, I do not think there is any advantage to the employee. To comment very, very generally, and it is my own opinion and not the opinion of the company because it has not been discussed, I think for our company, perhaps, that the incentive plan would be a desirable one. I think this might include also other companies with a set-up similar to ours, but I do see one or two disadvantages that might affect our company. One is, it seems to me that the company that would receive the greatest benefit would be the company that paid an ordinarily low-wage scale, thus permitting themselves to expand and elaborate a profit-sharing plan to a greater degree.

Then, too, there are concerns that may have taken the position that they prefer to pay a high wage and do so in preference to some profit-sharing plan. They might feel that they are discriminated against. This is purely something outside of our own category. Our minds are pretty much open on the subject. We have not come to any conclusion as to whether or not it is a desirable thing.

I feel that profit sharing, wherever a company is able to establish some sort of a plan, is very desirable and should be encouraged, and I also have a conviction that most concerns, if they have made any study of it at all, if they are able to do it, will, whether there is an outside incentive or not, enter into some profit-sharing arrangement.

Senator HERRING. By "being able" you refer to their being able to pay for it or being able to devise a plan to pay these benefits?

Mr. SHARPE. That is true, because all companies do not operate on a really profitable basis. I think, however, that the relationship between an employer and his employees must be a happy one if the company is to succeed.

Senator HERRING. Don't you think your plan has aided you in being able to pay for it?

Mr. SHARPE. Oh, yes, sir. That is the point I tried to make. First of all, I do not think you can make a good product unless you have a satisfactory working condition for your employees. They must be happy and satisfied with the conditions under which they work, or you cannot produce a good product, or expect the maximum of efficiency.

Secondly, I think it is absolutely essential, in maintaining a satisfactory relationship between the employer and employee, that working conditions be pleasant, and the relationship be a pleasant one, and this plan, I think, is a means to that end in both cases.

Senator VANDENBERG. If I understand you correctly, you are saying that if an employer is in a position to use a profit-sharing plan there is an ample incentive in the benefits of the plan itself, ample incentive to the employer to encourage it and invite it?

Mr. SHARPE. I think so; yes; if he is thoroughly familiar with the results that come from a sound and well-devised plan.

Senator VANDENBERG. Yes.

Mr. SHARPE. Now, I do not, by that, want to say that I feel that is a sufficient incentive to encourage the thing. I do not know whether it is or not. It would be, I think, if they understood the relationship that it creates.

Senator HERRING. It is sufficient to the extent, though, that you would not want to do away with it in your business?

Mr. SHARPE. That is correct.

Senator VANDENBERG. Exactly.

Mr. SHARPE. And with reluctance, I might say, we froze the part that we did. We would have been much more pleased to have gone on with it.

I do not think I have anything else to add. Mr. Shineman covered our plan so thoroughly that I do not think I have anything more, unless you have some questions.

Senator HERRING. Thank you, Mr. Sharpe.

Mr. Schweikle.

STATEMENT OF EDWARD C. SCHWEIKLE, DETROIT, MICH.

Senator HERRING. We had Mr. Marsh, of the Hoskins Manufacturing Co., here the other day. Mr. Schweikle, you do not happen to be the man who presented the silver loving cup to Mr. Marsh?

Mr. SCHWEIKLE. I am not the man who started it, but I was quite surprised to see Mr. Marsh when he came out of his office. When he came out the first words were, "Well, I don't think it is a sit-down strike, but I don't know what it is." Of course, he was very much pleased.

Senator HERRING. Tell us your experience with the company.

Mr. SCHWEIKLE. I have been with Hoskins Manufacturing Co. 30 years almost, within a couple of months. I have enjoyed all the profit sharing they have had there, the wage rates or the bonus, or whatever they call it, and everyone there that gets it seems to think that it is just about the thing. It helps out in a good many ways.

I brought a little list with me, and if you don't mind listening to it, I will read it to you. This list includes myself. It starts from 1923. The first year it was $625.20; the next, $634.74; $980.15; $1,056.76; $766.18; $983.99; $1,211.73; $681.56; $229.80; and in 1932 nothing. Then it jumped up to $67.87; $287.57; $635.06; $898.40; and last year $940.21. That is a total of $9,998.20, since 1923, 15 years.

Senator HERRING. How much did you say?

Mr. SCHWEIKLE. $9,998.20.

Senator VANDENBERG. That is in addition to a wage that is equal to the going wage in your community at least; is that correct?

Mr. SCHWEIKLE. Yes, sir. The grand total for 15 years' service at Hoskins Manufacturing Co. was $40,594.11.

Senator VANDENBERG. I am interested specifically in the question I asked you. You received as good or better than the prevailing wage during all this time that you were receiving the bonuses?

Mr. SCHWEIKLE. During all this time; yes, sir. You can look over the wage rates, if you like.

Senator VANDENBERG. I am just interested in the general statement. I will take your word for it.

Mr. SCHWEIKLE. Well, it is all here. I asked the timekeeper for this, because I had nothing to go on. I did not think I would have to be telling it to anyone.

You take it with most of the fellows there, they all put it to good use. It gives a man a chance, working for wages, to buy a home. He does not have to work on a budget, you might say, budget out his money to get a few nickels here and there to try and get a start.

They have no labor trouble there and no unions at all, and, no matter what the bonus is, everybody seems to be more than satisfied.

Senator VANDENBERG. You are in the midst of an area which, to say the least, is rather persistently disturbed by labor trouble?

Mr. SCHWEIKLE. I'll say we are.

Senator VANDENBERG. Has the profit-sharing plan, in your judgment, anything to do with the Hoskins Manufacturing Co. immunity to these labor troubles?

Mr. SCHWEIKLE. Well, I think it has a good bit to do with it. Nobody talks union at our plant.

Senator VANDENBERG. Do you think that the statement of satisfaction with the plan that you are asserting would be the very general opinion of your fellow employees?

Mr. SCHWEIKLE. Yes, sir; I do. They all believe in it.

Senator HERRING. That is very fine. Do you have anything else that you wish to put into the record?

Mr. SCHWEIKLE. Well, I don't know. I can cite you a few instances around the shop there. For instance, one fellow there, an electrician, started in November, 2 years ago. Of course, the first year he got nothing. He was there a little over a month that year. The next year he thought possibly $15 or $20 would be his share. When they passed out the checks he got a check for $167, and, of course, it was very welcome.

Senator HERRING. And he was being paid the prevailing wage for an electrician to begin with?

Mr. SCHWEIKLE. Yes, sir.

Senator VANDENBERG. Does the company make a full statement to you to indicate why your wage is precisely what it is?

Mr. SCHWEIKLE. No; they do not make any statement to us at all.

Senator HERRING. You have access to the balance sheet and their profit and loss statement?

Mr. SCHWEIKLE. Well, for myself, I am a stockholder there, and, of course, I get a balance sheet of the business, but they do not pass it out through the shop to everyone.

Senator VANDENBERG. But a sufficient confidence has been established so that the announcement by the company is accepted in full good faith?

Mr. SCHWEIKLE. Yes, sir; everybody believes in it.

Senator HERRING. Those checks at the end of the year are pretty good evidence of it, are they not?

Mr. SCHWEIKLE. I will say they are. If a man has gotten behind with his doctor bills, or anything else, it gives him a chance to clean up. If he wants to buy an automobile, well, it gives him a chance to make a payment; with his wages the following year it will help him make the payments without having them come along the second of the next month and have them take it back.

Senator HERRING. Well, thank you very much, Mr. Schweikle. It was very helpful.

Mr. Aldrich.

STATEMENT OF C. B. ALDRICH, WASHINGTON, D. C.

Senator HERRING. You are a store manager?

Mr. ALDRICH. Yes, sir.

Senator HERRING. How many employees are there in your store?

Mr. ALDRICH. Thirty-five.

Senator HERRING. And you share in the profits, the 75 percent of the 3 percent?

Mr. ALDRICH. Yes, sir; that is right.

Senator HERRING. How long have you been with Peoples Drug Co.?

Mr. ALDRICH. Since 1920.

Senator HERRING. Tell us your impression of the system which the Peoples Drug Co. use, please?

Mr. ALDRICH. I think the system is good; that is, from the incentive standpoint. The bonus, of course, is something that we can depend upon, and then there are other things that the company does for the employees to create better relationships between the employees and the company, that keep the people happy. From the very beginning of the company they have aimed to establish a sort of a big family feeling among the employees and make them feel they are part of the organization rather than just an employee. For instance, even the newest employees are told that they in some instances will probably be the first and only contact with the public, even a soda-fountain man may be the only contact with the public representing the organization, and we want them to feel that the public shall be treated as the company would have them treated.

There are a number of things that seem possibly minor. One of them I would like to mention that has created a lot of good feeling is the little kit that is sent out to the family where there is a new baby.

Senator HERRING. Well, each man testifying for Peoples Drug Co. has mentioned that.

Mr. ALDRICH. Yes; we have a great many young people that haven't gotten to the place where they share in some of the other benefits. I think that is possibly the reason that this impresses them.

For instance, some of our plans are dependent upon the length of service, 6 months or more, or a year or more.

Another thing that I think is important. From the very beginning promotions in the organization have been made within the organization. It has been an incentive for a person to stick with the company and to do his best work, to turn in a good job, because he felt his efforts would be rewarded if he did turn in a good job.

Senator HERRING. As a store manager, you are getting as big a salary as any other drug-store manager, on the average, before you get the benefits?

Mr. ALDRICH. Yes, sir; that is right. That is, comparing it with other like organizations, I think it is a little above the average.

Another thing that I think creates good feeling is a record that is kept of each person's performance. We have a system in our organization where each employee has a personal performance card. Store managers and other people who are in charge of employees will make a report to the head office of little services other than those that are expected of the employees to the public or to the company, and those notices are made on his personal performance card, and his store manager, or he himself, has access to the files if he wants at any time to see his personal performance card.

Senator HERRING. Do you agree with the other store manager that was here this morning that this policy improves the general conditions, it creates loyalty, perhaps prevents some cash shortages, breakages, and other things that might occur?

Mr. ALDRICH. I think it does, because we explain to the employees that a piece of merchandise worth a dollar is the same as a dollar bill in the cash register, and we impress that upon them. If they see a valuable piece of merchandise lying around that is in a place where it would be apt to be broken or destroyed, or stolen, we impress upon them that they take care of it the same as they would the money that they take in over the counter.

Senator VANDENBERG. Well, speaking generally, the employees of the Peoples Drug Co. all feel as you do, probably, that it is a very satisfactory employee-employer relationship.

Mr. ALDRICH. Well, from my contacts with them, I would say they feel the same way. We have an outing each year where we have a chance to contact many more of the employees than we do in the ordinary conduct of business during the year, and we get a chance to talk with people not only in the other Washington stores but in some of the out-of-town stores, and they seem to have created, in the newer stores even, with newer employees, the feeling that they are working for a fine company and they are satisfied with their job. Of course, I feel it is more or less natural for some of the fellows that have been with the company for a number of years. The fact that they are still with the company indicates that they are satisfied, but when you hear it from people that have come into the organization, and have gotten that feeling in possibly 1 or 2 years, why, I feel it is general in the company.

Senator VANDENBERG. And as a store manager, where you are in a position to observe the net results, would you say that this profit-sharing plan is not only useful in its social advantages but that it also is actually good business for the company?

Mr. ALDRICH. I think so; yes, sir. As one instance, our food department, the soda fountain managers' share in the efficient operation of their soda fountain, and it gives them the incentive to turn in the best job from that standpoint, as well as wanting to hold his job and show that he is a good man.

Senator VANDENBERG. I suppose that is one of the major departments of your business?

Mr. ALDRICH. It is in a great many of our stores. In my particular store it is 20 percent, and in some it comes up to 50 percent and over.

Senator VANDENBERG. Your drug stores occasionally sell drugs, also?

Mr. ALDRICH. My store has about 60 percent so-called drug business. The down town locations, of course, are big food stores. We are about third or fourth in volume with our stores, and yet we have in what are classed as drugs, sundries, and toilet goods about 60 percent of our gross business.

Senator HERRING. Well, that is very helpful, Mr. Aldrich. If you have anything else you would like to put into the record we will be glad to have you do so.

Mr. ALDRICH. I think probably Mr. Fetzer covered the bonus, the insurance, the health and accident, and the annuity plan for you.

Senator HERRING. Yes; he did.

Mr. ALDRICH. I think that is all; thank you very much.

Senator HERRING. Thank you. Mr. Alfred P. Sloan, Jr. chairman of the board of General Motors Corporation, will be here at 1:30. So we will recess until 1:30.

(Whereupon, at 11:07 a. m. a recess was taken until 1:30 p. m. of the same day.)

AFTERNOON SESSION

(The hearing reconvened at 1:30 p. m., pursuant to the recess.)

Senator HERRING. Just proceed in your own way, Mr. Sloan.

STATEMENT OF ALFRED P. SLOAN, JR., CHAIRMAN, GENERAL MOTORS CORPORATION, NEW YORK, N. Y.

Mr. SLOAN. Mr. Chairman, I have prepared here a memorandum that I would like to leave with the committee, if I may, and that memorandum goes into the questions before your committee I think quite thoroughly, from an economic standpoint, as well as from an industrial standpoint.

Now, I think that some of these things are perhaps too involved for a public hearing, but if it is your pleasure I might go through the memorandum, the high spots, and then if there are any observations the committee might want to make or any questions I would be glad to answer them as best I can. Is that satisfactory, Mr. Chairman?

Senator HERRING. Fine.

Mr. SLOAN. All right.

Well, in the first place, I understand the questions before this committee are of profit sharing from the standpoint of, I would say, improving the economic and social position of the worker, and of developing better factory or management labor relations, and also what might be done in the way of tax incentives to increase the productivity of industry. That is the assumption that I make.

Senator HERRING. Yes.

Mr. SLOAN. Now, when it comes to the tax-incentive idea, I would like to deal for a moment with that from the standpoint of the principle involved.

It seems to me that the question divides itself into two parts—first, what might be done in the way of tax-incentive principle as applied to the general problems of industry; next, what might be done as applied to specific problems; that is, pick out one thing and see what can be done to encourage that.

It seems to me that the greatest opportunity for increasing the productivity of industry and stimulating business lies in the general application. For instance, I think we might well consider that the taxation on business and business incentive—by that I mean the corporate tax, the personal tax, and the capital-gains tax—have gotten beyond the point of return, profitable return, and that they are impeding the development of business. I really think that is true, and I think from what I have seen and heard that the reduction of the capital-gains tax made at the last session of Congress has really stimulated the transfer of capital from certain things to others. In other words, it injected into the capital market increased flexibility, which I think is very essential. Too much of our capital is frozen, and we must arrange the tax structure so that it flows with the least resistance from one thing to another, especially into the new things that offer an opportunity and must be encouraged if we are going to increase and stimulate employment.

So I think that those general items in the tax structure which involve business as a whole offer an opportunity. If they were lowered, for instance, I might call that enterprise taxation, in a sense. In General Motors, for instance, when we are sitting around the table wondering what prices we are going to make for the next year, as we do once a year, we don't try to figure out how high we might make the prices; we try to figure out how low we dare to make the prices and protect our position.

I might call that enterprise pricing. I think, if we had enterprise taxation and capitalized the law of increasing returns as we went down it would be a real help to business. I feel that the revenues of the Government would probably be increased and not decreased, and employment and the productivity of industry would be stimulated as well.

When it comes to the question of specific taxation from an incentive standpoint, I think it is very important that in whatever your committee recommends, and whatever is done by the Congress, you should be sure that you are right, because to the extent that you are right, of course you are doing a constructive thing, but to the extent that it is not economically sound or doesn't work out that way, you are superimposing your judgment over that of industrial management, and it is important that it should be right.

And then another thing it seems to me is important, is that whatever you recommend should be applicable along a broad front of enterprise. If it is applicable only to too narrow a front, you unbalance the economy and you perhaps upset competition. If it is on a very narrow front you step from the principle of incentive taxation to a subsidy, and that is the worst thing; certainly none of us want subsidies injected into the economy.

So, I think, to make a long story short, that in dealing with this question of specific application of the incentive principle to industry, it is impossible for anybody to say that it is right or it is wrong. I think you have to pick out the specific thing, and not only the specific thing but you have to consider the specific application of the specific thing in order to answer the question of whether it is in line with the general principles that ought to be considered in any tax incentive idea.

Now, when it comes to the question of profit sharing, I would make this observation, after having read the testimony before your committee, that there seems to be a good deal of confusion in definition of what constitutes profit sharing. Many things have been discussed here which are manifestly not profit sharing because they are carried on whether there are profits or not. Therefore, I would like to divide the subject of profit sharing into two parts.

One is profit sharing, true profit sharing, and the other is composed of things that might be, in a broad application of the term, considered profit sharing.

I would like to mention those, if I might, separately.

When it comes to profit sharing, true profit sharing, and by that I mean to establish the profits at the end of any period and take something away and divide it among the workers, it would seem to me that if we analyze American industry on a broad front we must definitely come to the conclusion that a very broad application of true profit sharing is impossible for the simple reason that there are not enough profits to go around.

For instance, if you take the 16 leading industrial organizations in their respective fields in the United States, each employing a capital of $100,000,000, or more most of them considerably in excess of that, you will find that their return on capital over the last 15 years has only been 8 percent. That represents a term of years to get an average.

Now, if we are going to have true profit sharing, it seems to me that we have to apply an equitable formula to the profits, whatever they may be. By an equitable formula for profit sharing I mean that as long as labor gets an economic wage, the highest possible wage to insure the greatest productivity, capital is entitled to some wage before the profit-sharing principle sets in, and if you apply that to the already small profits of American industry, over the business cycle, I think you will come to the conclusion that what is left is relatively unimportant and is only applicable to a relatively few cases of special instance.

I don't think that profit sharing as such in a large organization—I mean true profit sharing—would particularly increase efficiency; at least not in a highly mechanized industry like we have in the motor industry.

So I think that true profit sharing might better be left to the initiative of individual management, based upon the merits of each individual case, and determined without any particular application to the tax-incentive principle.

Of course, you are aware of the fact that the present tax structure permits the deduction of anything that goes to the workers, whether it is wages or anything else.

So I don't want you to think that I am taking a position exactly against true profit sharing, but I think its application is limited, and I think that—well, I will take that position now and then I will take up the other part of it—I think I can explain to you more in detail just what I mean.

There is another side to profit sharing which I think ought to be stressed, and I think Mr. Green, of the American Federation of Labor, made a somewhat similar statement before your committee, and that is this, that if you recommend and the Congress adopts some form of special incentive to encourage profit sharing, it seems to me it might well raise the question as to whether that did not give labor a proprietary right in the enterprise, due to the fact that the Government has taken that position. I don't say that would follow by law, but it might follow by implication. If we should get to the point where profit sharing was based upon a wage which was less than what I might call the truly economic wage—by which I mean the wage that produces the greatest productivity relative to price—then, of course, the equity would be there, and then the question would arise whether labor should not be involved in determining industry's managerial policies, and I think that that would be very objectionable and would be quite dangerous in what it might lead to.

I believe that whatever we do in industry, labor should have at all times the highest possible wage. I don't think we should develop anything that means that labor should take a subnormal wage at any time. I think the pay envelope should be the biggest that we can possibly make it all the time, and therefore I think that rather than take anything out of any particular unit of industry that might be given to the worker or superimpose upon the economic wage whatever might be taken out, even if it is a part of the profits that might be applicable in some cases in good years—I think ought to be devoted to insuring the economic stability of the worker.

I think the greatest problem today is to do those things that give the worker a continuity of income. I think small extra amounts in good years are not half as important as devoting our energies to the problem of stability.

Too often, even the way things are now, in good times or even in a limited period where employment is high, plenty of work, and income is high, the worker is likely to set his standard of living on that basis; and then, when he has reduced employment, or no employment at all, it causes a great deal of unhappiness and dissatisfaction. It is far better, I think, to do what we can in working toward stability.

Therefore, I think that the opportunities of profit sharing—I pass now from true profit sharing to other forms which I think might better be called benefit plans—is really the thing that industry should work toward with the objective of improving the economic and social position of the worker.

Now, there are many of those plans, and they are in various forms, such as investment plans, health-insurance plans; you are familiar with the general group of plans of that type.

We in General Motors have had down through the years a plan that we call the savings and investment plan, which was an organized scheme of saving in which the worker participated and the corporation participated. At the beginning of the depression, the big depression in 1930, our workers had with us over $100,000,000 that had been accumulated as a result of that organized saving, which was very, very helpful in carrying them through the bad years which were to follow.

And in the 19 years since that plan was put into operation we have paid back to the workers, our contribution and theirs together, $247,000,000, which you can see was really a scheme on a broad basis.

But then when the Securities and Social Security Acts were passed and we had very heavy burdens to carry, and due to other complications that arose, we discontinued that plan, and we have recently worked out a benefit plan with the objective of stabilizing the income of the worker, which we call the General Motors income security plan.

That plan has recently been announced. I will be glad to explain it to you if you would like to have me, Senator.

Senator HERRING. We would be very glad to have you do so.

Mr. SLOAN. All right.

The income security plan is not a profit-sharing plan, a true profit-sharing plan. It is of the benefit plan type. It provides for any year in which the plan is declared operative that any worker in the General Motors group of companies with five years or more seniority who was employed in December of the previous year is guaranteed a weekly income not less than 60 percent of his normal income. His normal or standard income is defined as his hourly rate for the standard 40-hour week.

Now, if, during any week in that year, due to the effect of the seasonal trend, which in the automobile industry is very irregular, or due to the effect of the business cycle, his income falls below 60 percent of normal, the corporation makes up the difference and he gets the 60 percent.

That, in reality, is a loan of a special type. I mean by "special type," that it carries no interest, and it is not returnable in money, it is returnable in work and only as work may be made available by the corporation in subsequent months.

In subsequent months any worker who has had advances—it is purely optional, he doesn't take advantage of them if he doesn't want to—when he has work that gives him an income in excess of 60 percent, he pays back to us half the difference between 60 percent and his earnings until the entire amount is liquidated.

We hear a good deal nowadays about the importance of a yearly wage or a yearly salary. A yearly wage or a yearly salary is hazardous to the business and it is somewhat hazardous to the worker, because it is apt to be predicated upon an hourly rate less than what the worker would normally get; and to the extent that there is no work, say a collapse of the economy such as we had a year ago, big business or any business that had an obligation of a yearly wage would have felt it very disastrously. During that period we dropped 45 to 55 percent of our business. And, of course, any situation of that kind must be reflected ultimately in higher cost of goods and services, which is undesirable.

But in our case in this plan that we are working on at the moment the worker gets the full productivity at his regular work. Over the years he gets whatever you might say is coming to him, and the sole purpose is to stabilize his income and normalize his standard of living, and to level off the peaks and the valleys.

In addition to that, naturally what is reflected in the economy, you might say, of a large group of workers, is also reflected in the economy of the community in which those workers live, and I have been very gratified, following the announcement of this plan, to receive endorsements from many communities in which we are important providers, pointing out the benefits that will result to those communities through this stabilization, for merchants and others, by giving the workers a more uniform income.

Therefore, the point I am trying to make is that it is my belief that what we can take out of the productivity of industry, without unduly affecting prices, should be used or can be used to the best advantage by injecting into the workers' scheme of things, greater stability. I think that that is the real benefit, the real purpose to which industry should direct its energies and its thoughts, and anything you might recommend that might be adopted to encourage that type of thing would, I believe, be a real contribution to the worker economically and from the standpoint of stabiliy, and would make a contribution, too, toward stabilizing the economy as a whole.

You are familiar, of course, with the facts, as I said, with respect to true profit sharing. These plans, whatever they may be, if they are in the worker's interest, are already deductible under the income tax. Anything you might do further in that particular, I would see really no objection to doing.

First, when it comes to the specific application of the tax incentive principle to industry's problems, I have already mentioned, in principle, that we must be careful that we are right. We haven't been any too successful in that at times.

And second, we must be sure that the application is along a broad front of enterprise, not along a limited front. We particularly must beware, for if it is applied on a very limited front, it becomes a subsidy.

Those are broadly the principles which I have outlined as being applicable.

Now the tax incentive principle, as applied to industry's specific problems, has not, as you know, been used very much in this country but it has been used in other industrial countries to some extent. Those specific applications have taken the form of encouraging new enterprises by giving a tax benefit. They have taken the form of reducing the cost of usage, with a view to promoting the manufacture or broadened use of the things that were being used, to stimulate productivity. They have been employed—well, we will say in very many different ways—in relation to industry, and have been very helpful.

I would like the privilege of submitting to the committee certain specific plans on that, if I may have it?

Senator HERRING. We would be glad to have them; yes.

Mr. SLOAN. There is one specific application which I would like to mention which I believe is illustrative of this general scheme of things, and perhaps the one, at least in my judgment, that offers the best opportunity. And I might express that by saying that it is encouraging the substitution of the new for the old. In other words, it is doing those things that will encourage scrapping old instruments of productivity of various kinds, and buying the new.

In support of that idea, I think it can be well said that today America's producing plant is obsolete. As a broad statement that can be made. For instance, there was a study made by a responsible authority in 1935. It showed at that time that 65 percent of the machinery in the metal working field was at that time 10 years old.

Well, during the last 10 years, we will say, 8 or 9 years anyway, or rather since the big depression set in, there has been an enormous acceleration in the development, the injection of advanced technology in the development of our instruments of production. It is really remarkable what has taken place.

Anything that might be done to encourage obsolescence—for instance, if industry when it destroys something and buys something new could have certain privileges in the way of encouraging that type of thing would really be a marvelous help, I believe, because you probably know that about 50 percent of industry's workers are concerned, are involved, in the production of durable goods, both durable capital goods and other types, as well as in the attendant services, such as the railroads that have to carry the merchandise incidental to such production.

And you probably know also that we have never had sustained prosperity unless we have had liberal employment in our capital goods industries. You often see it stated that the real measure of whether we are going to be prosperous is the status of our capital-goods industries.

Of course, employment in the capital-goods industries means that industry is developing, it is expanding, new things are coming, and that naturally reflects general business confidence. In other words, it reflects confidence in the fact that the capital so employed can be profitably employed over a term of years.

But, irrespective of that fact, I believe that if we could encourage industry to bring its producing plant up to date, that the economic result would be not only to create employment in our capital-goods industries—that is very important in itself—but the productivity of those who are producing consumer goods would be increased, it would result in our ability to produce those consumer goods at lower cost and hence sell them at lower prices. And the great problem before the economy today—and the only way we can maintain the wage scale, and increase wages—is to do those things that lower prices. It can't be done any other way because if we go to work and increase wages and it increases prices, nothing is gained. We can only gain by increased efficiency and greater productivity per man, by the employment of more capital so the man can earn more. That is the only way it can be done, and that is why anything that could be done in an administrative way or in adjusting the tax structure to stimulate the capital-goods industry would, in my judgment, be helpful.

I might make a couple of illustrations and then I will be finished.

I will take two illustrations in General Motors, in its scheme of things, because, of course, I know that picture.

We have developed in the past 3 or 4 years into a more intensive form than has ever been done before, the Diesel engine; and the Diesel engine, as we are now developing it, has quite a wide range of application. I will refer to one application, the Diesel electric locomotives, as applied to transportation by rail, and one specific application of that, the Diesel electric locomotive as used for switching purposes.

I only offer it is an illustration of what could be done by better instruments of production, thereby reducing the cost of goods and services, and stimulating business.

It is possible for a railroad today to buy a Diesel electric locomotive for switching purposes, and to pay for the locomotive, including the interest charges for carrying it, from the out-of-pocket savings within 6 years. Do I make myself clear?

You can see that there is a case where the benefits of this employment in the production of the Diesel electric locomotive, and in the services incidental to same, go to the railroads, the railroads can make a saving, and that saving could be effectuated through a lower cost of goods and services. At least the influence is there.

Now, another illustration. Take the motorcar business, for instance. Let's compare the car of 1929, if you will, with the car of 1937. The automobile of 1937, if produced in 1929, under the conditions then existing, would have cost possibly 25 percent more. In other words, the car itself is 25 percent better because it is bigger, wider, more luxurious, has more things on it, and all that sort of thing.

Due to the application of better instruments of production, the capitalization of technological progress in General Motors, we were able to give our customers in 1937 at the same price a car that was 25 percent better than the one we gave them in 1929. We were able at the same time to pay our workers $80,000,000 more for the same amount of work hours through increased wages, and to pay the Government $32,000,000 more in income taxes.

That is just an illustration of what can be accomplished in the way of better technology as applied to industry's problems.

That completes my story.

Senator VANDENBERG. Well, Mr. Sloan, your statement is most illuminating and most helpful.

If I understand you correctly you would favor the application of the incentive tax idea on a practical basis to the encouragement of replacements throughout American industry on a broad front; is that correct?

Mr. SLOAN. I certainly would.

Senator VANDENBERG. And you think that the application of incentive taxation to that purpose would produce not only an immediate expansion and immediate reemployment, but also a substantial economic advantage across a broad front?

Mr. SLOAN. Well, on that point, Senator, I would say without reservation that I can't emphasize my position on the second point too strongly.

On the first point of course I don't know how quickly that would take effect. It would certainly be an urge and would depend, as I said, upon the general attitude of mind toward the future of business by the investor, and the amount of capital that was available. I don't think in any of these things, Senator, we can take a position other than that it is a step in the right direction, the way in which we ought to go, and it is certainly that. It is the only way—I want to emphasize this—it is the only way we can raise wages without raising prices, and therefore have increased purchasing power; increased productivity per man—it can't be done any other way. And this thing that you mention is directed toward that objective.

Senator VANDENBERG. In other words, incentive taxation could be used effectively to increase productivity?

Mr. SLOAN. That is right.

Senator VANDENBERG. And you have said rather dramatically that American industry is practically obsolete in respect to its equipment today. Isn't it a fact that the estimates of the possibilities in dollars and cents of replacements of the character we have been discussing, that the possibilities are so enormous that it is almost fantastic to even set down a figure?

Mr. SLOAN. Yes; it is. If studies could be made, Senator, I think they would demonstrate that. Start from where we are now and if you assume a very small growth of the country and go back and see what has been done, and realize how much we have lost in the last 10 years, many of which have been years of low productivity and uncertainty, and therefore capital investments haven't been made, you will see that there is a real opportunity.

And don't forget that it isn't only the employment in those industries that we get, but we are taking a step toward lower cost of goods and services, and so often, Senator, when we are talking about our national economic problem, we talk about wages. If we would only, when we talk about wages, ask ourselves what is the effect of what we do on prices, because you can't talk about wages without talking about the things that wages will buy. There is a direct relation there, and that is all-important because it doesn't make any difference how you increase, how much you increase the wages of the workers, if prices go up accordingly, because money isn't worth anything except what you can exchange it for.

Senator VANDENBERG. I think that is a very courageous and forward-looking statement in respect to incentive taxation.

I want to revert, just for a moment, to the profit-sharing problem.

Mr. SLOAN. All right, Senator.

Senator VANDENBERG. You have undoubtedly made a correct division of the types.

Mr. SLOAN. Yes.

Senator VANDENBERG. We are considering, for the purpose of this inquiry, that any addition by way of benefits to a standard wage is in essence profit sharing.

Mr. SLOAN. Well, I don't know your definition. I have accepted that, Senator, except I have divided them into two categories, that is all.

Senator VANDENBERG. Now, on that basis, General Motors has been a profit sharer, has it not?

Mr. SLOAN. Yes; very importantly so, Senator.

Senator VANDENBERG. I notice an entry in the answer to our questionnaire, that over a 20-year period approximately 9½ percent of your net earnings have gone into employee benefit and welfare plans?

Mr. SLOAN. That would include, probably, executive bonuses, too, Senator. Yes; that is right.

Senator VANDENBERG. At one time recently you paid general bonuses, you haven't said anything about that. Will you state for the record what you did in that respect?

Mr. SLOAN. Yes; we did. At the end of two different years, Senator, we paid what you might call Christmas bonuses and we didn't think that they were particularly constructive, they weren't based upon anything, they were just paid out in the form, really, of a Christmas present, but I feel that—you see I don't want to take too much of your time——

Senator VANDENBERG (interposing). Go ahead.

Mr. SLOAN. In industry, in any unit of industry, take General Motors, if you pay the workers more than an economic wage, as I said before, it doesn't make any difference what form it may take, and if it isn't offset by increased productivity it is reflected in the price structure. And there is only a limited amount of leeway. If you start on the assumption, as I do, that the worker should have the biggest economic wage, you have got to be careful how much more you pay the worker or else you prejudice his income on an annual basis by less productivity, resulting from higher prices. Do I make myself clear?

Senator VANDENBERG. Yes.

Mr. SLOAN. In other words, it brings up another question: Too often a worker who gets perhaps an increase in an hourly wage thinks he has a better situation, but if that hourly wage means higher prices, he may have a less number of hours of work and his income may be less. So that when we take anything out of the productivity of any unit, in addition to an economic wage, you have got to be careful how much more you pay him, or else you prejudice his income on an annual basis by less productivity, resulting from higher prices. Do I make myself clear?

Senator VANDENBERG. Yes.

Mr. SLOAN. And I take the position that we can use it more effectively by promoting the stability of the worker's income and stability of his position, rather than by giving him a little more in times when business is good.

Now, do you get what I am trying to say?

Senator VANDENBEG. Yes.

Still, for the record, I would like to know what your big bonus payments were in the 2 years that you made the distribution.

Mr. SLOAN. I will have to submit that. I would say it was about $15,000,000, Senator; I think one was $10,000,000 and one was $5,000,-000, but I will submit that to you.

Senator VANDENBERG. Is there anything in this contemplation, which is the thing that I am coming to—in my view you correctly emphasize the importance of not charging unduly the cost of production lest it increase the selling price?

Mr. SLOAN. Yes.

Senator VANDENBERG. All right.

Mr. SLOAN. Pardon me, from the standpoint of the worker, himself, the maximum annual income comes through the greatest productivity.

Senator VANDENBERG. And to inspire the maximum employment?

Mr. SLOAN. That is what I mean; that is right.

Senator VANDENBERG. All right—now, when you pay a bonus such as you did, is it not charged against the cost of production, and is it not an element to a certain extent in increasing, rather than decreasing, the selling price?

Mr. SLOAN. It depends, Senator, upon how it was done. You are absolutely correct. The two bonuses that we gave, such as you specify, did not affect the price. But many of these benefit plans that are not truly profit sharing, do affect it. For instance, if a corporation, if a business, sets up a pension plan, it becomes part of what we call the cost of sales. Let me refer, if I may, to this income security plan that I have just described to you, which I believe is highly constructive. Whatever expense may come out of that will become a part of the cost of sales, and it will have an influence on selling prices. Now, I don't mean, Senator, that it will jump the price of the car, but I mean to say it will have an influence; it works in that general direction, because it goes into the cost, and selling prices are made on the basis of cost.

Senator VANDENBERG. All right; exactly. But if true profit sharing distributed this extra compensation in the form of a profit-sharing dividend, it would not increase the cost of production?

Mr. SLOAN. That is right, Senator.

Senator VANDENBERG. Therefore it has that advantage, even from your viewpoint, because it does not enhance the price?

Mr. SLOAN. That is right, anything that can be paid out, that is true profit sharing, but then, Senator, you get up to the point, if you do that on a broad scale, is—I am not talking about the specific application, Senator, but if you do it on a broad scale and it amounts to anything as a real effect on workers' income, then the question arises whether the profits of industry justify or make possible that type of thing and at the same time leave enough profits to retain the profit urge, which we must have to develop and expand industry's productivity.

Senator VANDENBERG. Well, we would agree with you, I am sure, Senator Herring and I, that there is no such thing as a universal application of a standard profit-sharing formula to business. The only thing we are trying to discover is whether there are not individual situations, and there seem to be some, in which profit sharing is the logical means to create this sense of partnership?

Mr. SLOAN. I have dealt with it along a broad scheme, not a specific scheme.

Senator VANDENBERG. Well, I think you have been very helpful.

Senator HERRING. Mr. Sloan, in your opinion, incentive taxation or compensatory tax benefits could be applied to plant expansion and to provide for obsolescence, but you doubt whether it would be beneficial as applied to encourage profit sharing?

Mr. SLOAN. Yes; that is my position.

Senator HERRING. That is the way I understood you.

On those advances which you provide under your new plan, is there any interest charged?

Mr. SLOAN. Is there any what?

Senator HERRING. Any interest charged?

Mr. SLOAN. None. I might tell you something about how that works out financially, if you would like it.

Senator HERRING. Yes.

Mr. SLOAN. As to cost of such a plan, in answer to the inquiry of the Senator from Michigan, I might say that in that State that cost would go into the tax structure and whatever it was would have influence, but it would be so small it would be inconsequential.

Now, that cost in our income-security plan comes about from two things, in two ways. First, if a worker to whom we made advances under the plan should die while he has work to return to us, you might say, that is a loss to us because that is not a liability against his estate.

Second, a worker who might have had advances, should he leave our employ—and he is free to leave—those advances are canceled.

So that the cost liability under the plan to the business which might adopt such a plan would be due to those causes.

Now, we don't know just what that will amount to in dollars, as applied to us. It will depend on so many circumstances that we would have to make so many assumptions that it would be very difficult, but from studies we have made we feel that it will not be unduly burdensome, and we feel it is so important to encourage, to promote the stability of income, and particularly, Senator, in our business where what we call the seasonal trend is very wide; and do what we may, and we have done everything about it, to level off the seasonal trend, and to regularize employment over the year, it is still a very difficult problem, and this particularly applies to a business of that type. But it also applies to—for instance, you take last year, in December of last year, when, without any warning, our business was more than cut in half. Now, if we had had the income-security plan we would have guaranteed all those workers that were with us for 5 years up to 60 percent of their standard income, and I should say that the workers that have service with us of from 2 to 5 years have also a benefit on a somewhat reduced scale——

Senator HERRING (interposing). In the distribution of those bonuses as between the executive staff and the workers' staff, was that in proportion, on a percentage?

Mr. SLOAN. You mean the one the Senator asked me about?

Senator HERRING. Yes.

Mr. SLOAN. No, sir; that was done on a basis of wage or income, it was done on a straight-across-the-board proposition, or practically so. If I recollect right the last year when the distribution was made it was about $10,000,000 and our workers, our hourly workers, received, I think it was, from $35 to $60 as a bonus at the end of the year.

Senator HERRING. Evidently you don't agree with a statement that was made here by one witness that one of our difficulties today is that we are too efficient. You are still contending for more efficiency?

Mr. SLOAN. Well, of course, Senator, that brings up an awful big question, about technological employment. Of course, I think you can say this, Senator, that technological progress must be capitalized through lower prices. If it isn't capitalized through lower prices then there is no doubt that technological employment, which is increased efficiency, does throw people out of work, but on the other hand it is more than justified by putting people back at work in larger quantities some other place. Now, sometimes there is a time lag there, and sometimes there is a dislocation. Perhaps a man loses his job in one place and perhaps he has to move to another. But that is the price of progress, Senator. You can't get these things for nothing. That is one of our troubles, we try to get too many things for nothing, and it can't be done. But technologically, the only way we have to increase productivity and to increase employment is to—we must be more efficient, we must give that back to the people in lower prices so they can have more things, or as I express it, more things for more people in more places—that is the objective, and it must be done by increased efficiency, and that is the reason why I am so strong for considering anything that will give us the instruments of a higher efficiency.

Senator HERRING. I think that is all, and I thank you very much.

Senator VANDENBERG. Thank you very much, Mr. Sloan. You have been very helpful indeed.

Senator HERRING. We will now recess until 10 o'clock Monday morning.

(Whereupon, at 2:25 p. m., a recess was taken until 10 o'clock Monday morning, December 12, 1938.)

SURVEY OF EXPERIENCES IN PROFIT SHARING AND POSSIBILITIES OF INCENTIVE TAXATION

MONDAY, DECEMBER 12, 1938

UNITED STATES SENATE,
SUBCOMMITTEE OF THE COMMITTEE ON FINANCE,
Washington, D. C.

The committee met, pursuant to adjournment, at 10 a. m. in room 312, Senate Office Building, Senator Clyde L. Herring presiding.

Present: Senators Clyde L. Herring and Arthur H. Vandenberg.

Senator HERRING. I hardly think it necessary to tell you who Mr. Parker is. He is the man upon whom we have relied so long in this room, and, as usual, I will keep still and let him tell us what we are trying to get at here.

Mr. PARKER. Thank you, Senator. Perhaps—I have here, a brief written statement which will probably take me 10 minutes; and if I should go ahead with that, if that is your pleasure, I think we could accomplish more in that way, and then you may ask me questions.

Senator HERRING. Certainly; proceed in your own way, Mr. Parker.

Mr. PARKER. I came here mainly to answer any question that I might be able to answer.

Senator VANDENBERG. Before you start, Mr. Parker, I think the record ought to show specifically that you were the agent of the Joint Congressional Committee on Taxation of the House and Senate for—how long?

Mr. PARKER. Twelve years.

Senator VANDENBERG. Yes; and that you left voluntarily, with the benediction of every Member of the House and Senate.

STATEMENT OF LOVELL H. PARKER, WASHINGTON, D. C.

Mr. PARKER. And I would like to also add that I am appearing here for myself; I am not interested in any client or anything like that in my appearance here.

Senator VANDENBERG. All right; go ahead.

Mr. PARKER. If I may be so privileged, I would like to confine myself to incentive taxation, because I have no specific knowledge about the profit-sharing plan; and even in respect to incentive taxation. I would like to confine myself to the method by which it might be applied.

Of course, everybody has a somewhat different definition of incentive taxation. I believe it has been suggested that the better way to speed up business is to reduce tax rates. That may be true, and in the long run tax receipts might be considerably increased by that method. But I don't think that would take place immediately. While we are facing a $4,000,000,000 deficit in this fiscal year and a public debt of $40,000,000,000 at the end of the year, it seems to me that tax reductions can only be allowed when they will result in increasing the national income. If we had a national income of $100,000,000,000 a year, instead of $65,000,000,000 a year, our tax troubles would be over.

The old theory was that tax laws should be designed for revenue purposes only, and most tax experts looked with horror at introducing anything in these laws which would create an incentive to do certain things. However, we have some instances under existing law where the principle of incentive taxation has been used.

For example, there can be little doubt but that discovery depletion and its successor, percentage depletion, have substantially stimulated the oil and mining business, and encouraged investments therein. Again, the allowance for charitable gifts up to 15 percent of an individual's net income, has stimulated gifts up to that point. There can be little doubt that if that percentage were decreased you would have less gifts, and if it were increased you would have more gifts.

Now, in the interest of brevity, I wish to come directly to the point of suggesting what I consider a safe and practical method by which certain additional incentives might be incorporated in the tax laws. This method is based on the proposition of maintaining the present level of taxation unless certain expenditures are made tending to increase employment, in which case the tax will be reduced and approach a certain minimum.

The method I suggest for your consideration may be briefly stated as follows:

1. Impose a normal tax.
2. Impose a surtax.
3. Impose a supertax.
4. Reduce present surtax rates, but compute normal and surtax on the net income as defined in the existing law.
5. Allow certain incentive deductions from net income in arriving at what may be called a supertax net income subject to a graduated supertax.
6. Adjust supertax rates so that if there are no incentive deductions the tax will be as great as under existing laws.

For example, take the man that makes $1,000,000 a year. Under existing law his tax is $679,000, and he has $321,000 left. Now, suppose you fix a normal and surtax rate so that the sum of these taxes will amount to $400,000. At this point he has $600,000 left. Now fix the supertax rates on the $600,000 so that his supertax would be $279,000, if he has no incentive deductions. On the other hand, if his incentive deductions equal $600,000 or more, he will only pay the minimum tax of $400,000. Of course, if his incentive deductions are somewhere between zero and $600,000, his total tax will be somewhere between $679,000 and $400,000.

That is just to give you the idea that you have a minimum tax of $400,000. That is, of course, up to Congress; they might want to make it $300,000 or $500,000, but you would have a minimum that would reasonably protect your revenue.

One purpose of this system is to provide for a certain minimum tax on net income computed as at present, and thus protect the revenue. The other purpose is, of course, to provide for a reasonable system of trying out incentive taxation.

Now, about these incentive deductions, what might be suggested for these in the case of individuals? First, I have been reliably informed that there are about 1,000,000 domestic servants and chauffeurs unemployed. One incentive deduction which might well be considered is for the wages and salaries paid which are not now allowed in computing net income. This deduction would be allowed, of course, only for the purpose of computing the supertax net income.

Now, suppose a man did save $5,000 in tax by spending $20,000 more for domestic servants. Certainly what the Government would lose in tax would be more than made up by a decrease in the relief rolls.

Second, since unemployment is probably the main factor in our present troubles, it might be well to consider the effect of a deduction for supertax purposes in an amount equal to the excess of the wages and salaries paid in the current year, whether or not deductible in computing income, over the wages and salaries paid in the prior taxable year.

Third, in order to increase expenditures for the construction of homes, factories, and buildings, and for the acquisition of machinery, the effect of a deduction which would allow these expenditures to reduce the supertax net income should be considered. If such a deduction stimulated these expenditures, it would tend to reduce the necessity for huge governmental building projects. In connection with such a deduction it is possible that the taxpayer should be given the option of taking one-half of the expenditures as a deduction in the current year and one-half in the succeeding year, or one-third, the principle being, instead of allowing depreciation for supertax purposes, you allow costs to be amortized over 2 or 3 years.

Fourth, a deduction in computing supertax net income equal to the amount of contributions to charitable, educational, scientific, and similar institutions, which is in excess of the 15-percent net income now allowed, and possibly even a deduction for direct gifts for the relief of individuals. It is probable that such a deduction would increase these charitable gifts and reduce the amount of the relief expenditures of the Government.

Now, let us see if there is anything unreasonable about these deductions. The first deduction was for wages and salaries paid and not now deductible. Personally, I cannot see why it is not as logical to deduct a servant's salary as it is to deduct taxes on your house or taxes on your theater tickets, which latter deductions are already allowed.

The second deduction suggested is more debatable. This was a deduction for increased pay roll. It is possible that some refinement should be made in this deduction by the use of averages; but, in any event, it is worth considering, because we certainly need more employment.

The third deduction, having to do with the construction or acquisition of depreciable property, is likewise controversial, but it has the same objective—increased employment.

The fourth deduction, for charitable gifts in excess of 15 percent of net income, already allowed, cannot be looked upon as a violation of our present income-tax principles, since such gifts are already allowed in part.

The principal advantage of this normal, surtax, and supertax plan would be to provide a fair minimum tax and yet give reasonable incentive to the expenditure of money, resulting in employment by giving deductions for supertax purposes only. In other words, the revenue of the Government would be protected and still a fair trial of a step toward incentive taxation could be made.

There would be another advantage to this supertax plan, which is not connected with incentive taxation. Certain equitable reliefs could be given which are now deemed too expensive. Under existing law a married man with a $10,000 salary, who pays $1,000 rent and $3,000 for food, clothing, and living expenses, pays a tax of $415, and he has $6,000 left with which to pay it. Another married man with a $10,000 salary, paying $1,000 rent the same as the first, $3,000 for food and clothing and other expenses as in the first case, $3,500 for college expenses of his 20-year-old son and 19-year-old daughter, and $2,500 in hospital and doctors' bills, also pays $415 in tax, although he has nothing left out of his salary with which to pay it.

This may be excusable in such a case now, the tax in lower brackets being so small; but suppose the tax in those lower brackets is raised, as so often has been advocated. For example, suppose our tax on a $10,000 salary, instead of being $415, was $1,645, as it is in England. Then it might be very much in accord with the principle of ability to pay to allow, at least for supertax purposes, a deduction for doctors' and hospital bills and some allowance for children over 18 who are attending school or college. As you know, allowance is already given for children under 18, therefore, under existing law this allowance is taken away just when the actual expenses are the greatest in the case of children being sent to school or college.

As far as corporations are concerned, a similar system might be employed with a minimum rate on the net income computed as at present, and a supertax rate to be applied to the supertax net income arrived at by deducting the incentive-tax allowances from the net income.

In conclusion, I believe there is nothing more important than the speeding up of all industry and the increase of the national income. It is possible that this can be done by direct legislation, lack of legislation, or repeal of legislation. If it can be done even by changes in the tax laws, it might be that the ends would justify the means.

That is all I am prepared to say, Mr. Chairman.

Senator HERRING. You haven't considered particularly the tax incentive to encourage profit sharing?

Mr. PARKER. I haven't considered that, Senator. What little study I have given to that subject caused me to only arrive at one preliminary conclusion, that it was hard to make any one system that would fit all kinds of industry. One system would be more applicable to one industry than another. But I know nothing about that, and I think my advice on that matter would not be useful.

Senator HERRING. Well, as usual, you have gone into the subject all right in a way that would challenge all of us.

We are now permitted to deduct, as far as profit sharing is concerned, any bonus that is arrived at in advance and definitely determined, are we not; that is, corporations are?

Mr. PARKER. Any bonuses are treated as compensation; that is right. Yes; that comes off.

I did make one point previously, that there are certain allowances already made in the law which I call incentive deductions which encourage people to do certain things, like making gifts.

Senator VANDENBERG. The point at which your formula chiefly differs from the existing practice is in your creation of the so-called supertax bracket: is it not?

Mr. PARKER. That is correct. Of course, that may look complicated. It isn't complicated. You just make one more computation. But the trouble with most of these tax reduction plans is, that when you first look at them on paper they appear to make such a tremendous difference in the revenue that you don't dare make that trial. Now, in connection with my plan you can limit the theoretical loss of revenue. But you should look at the proposition from a long-run viewpoint. Now, you might be able to figure that if we lose two or three hundred million the first year, that would be all right, but if you were facing the loss of a billion, that would be another matter. Under my plan you can adjust this proposition so as to give some incentive without taking very great chances. Your loss would be absolutely limited. Your gain would be more uncertain, but it might even make up the loss, and in the long run I am rather inclined to think it would substantially increase your revenue.

Take the rich man—I have no great brief for the millionaire—but here is a man that loses $1,000,000 this year. Now, he has got to make $1,000,000 in three successive years to get even—he doesn't even get even then, he is still out $34,000. So that the man with the capital that you want used in productive enterprises is being kept out of business. He just can't make money if he is investing in any business that has any chances or hazards to it, because he is bound to have losses, and therefore, he would have a much better chance at the race track—I mean if he didn't include his winnings in his income—he would have more chance to make money than he would in business.

Senator VANDENBERG. This is what I wanted to get at first, Mr. Parker, while you call this new category a supertax category, that might at first blush be misleading. It is merely a redivision of the existing tax collection, you are not proposing the assessment of a supertax which would be a tax on top of the existing tax?

Mr. PARKER. No, I am proposing to keep the tax at about the present level, but instead of dividing it into two parts, divide it into three.

Senator VANDENBERG. And the supertax is simply the third and final section of the tax as it now exists?

Mr. PARKER. That is right.

Senator VANDENBERG. And the purpose of the further division, as you indicate, is to leave a ceiling on the Federal revenue?

Mr. PARKER. That is right, it can't drop below a certain rate.

Senator VANDENBERG. Now, you have suggested that there might be some original loss in revenue to the Treasury as the result of these deductions, but that you would expect a logical result to be an increase in this national income which would more than take up the slack, is that right?

Mr. PARKER. That would be what I would expect.

Senator VANDENBERG. Well, why isn't it just as logical to proceed in that direction as it is to proceed by direct expenditures for the purpose of taking care of unemployment. It seems to me that this thing which, let us say we loosefully call "pump priming," takes money out of the Treasury for the purpose of encouraging employment. I am not speaking of it critically, I am just speaking of it analytically. It takes money out of the Treasury for the purpose of encouraging employment.

Incentive taxation, of the sort you discuss, merely stops, in the first instance, a certain portion of the money going into the Treasury. The net result to the Treasury is precisely the same. So that the final question solely is, do you create more employment in the American way by pump priming than by incentive taxation, and the justification for it seems quite obvious if the result of the incentive taxation is to increase the national income, because as I understand you, you feel that the only possible hope of balancing the Budget is through an increase in the national income—is that right?

Mr. PARKER. That is right.

Take that first deduction, about servants, that is a very heavy cost when you figure how much a man has to make in the higher brackets to pay that servant.

Supposing he lives in New York. He has to pay his 8 percent New York State tax and he has to pay his Federal tax. Say that he makes over $100,000—he is up in the 62-percent bracket. Well, we will say he pays a maximum total rate of 66 percent in Federal and State tax. Now, if he pays his servant $2,000, he has to make almost $6,000 to pay that servant's salary, when you figure the tax.

Senator VANDENBERG. You were very much more definite in analyzing your suggestions in respect to individual tax returns than you were in respect to the corporate tax returns. Would it be correct to say that your analogy in the corporate-tax field would mean that you would approve of the application of incentive taxation in the supertax bracket for plant expansion and plant replacements?

Mr. PARKER. I would have the same incentive deductions, and by the way, I may not have listed all that could be used. I have a few more that might be considered.

Only, in the case of the corporation, you wouldn't have to have this normal surtax and supertax, you would have a normal tax and a supertax and you would divide it into two parts in that case, because I don't think, in the case of a corporation, you have any need for graduation. With corporations the size of their net income isn't a good basis for a graduated tax because you can't tell how many stockholders are in it. A corporation may have a large net income but it may have a large number of stockholders, and graduated taxes on corporations' incomes become unfair unless they are based on some principle like excess profits or something like that.

So that this plan with respect to the corporation, what I had in mind, roughly, was to compute their net income as at present and pay a certain rate, 12½ percent, perhaps; on the supertax net income, after taking off these incentive deductions, perhaps 10 percent. Of course, that rate might be applied to zero, or it might be applied to part of their net income, according to the magnitude of the deductions.

Senator VANDENBERG. In your suggested deductions for corporations, would you specifically include in your suggestions allowance for plant expansion and plant replacements?

Mr. PARKER. Yes; I would. In fact, I think if you are going to apply this system you want to make it of general application. I think that is one trouble with the allowances you make to oil and mining businesses by way of percentage depletion. You stimulate that industry but you want to stimulate all industries at the same time.

Senator VANDENBERG. Have you any figures at all which indicate the extent to which the discovery depletion and so forth in the mining field did increase the activity?

Mr. PARKER. I thought of that, and I thought probably you would ask that question, but I didn't have time to assemble anything on it. I looked over the statistics roughly. Of course, it is pretty difficult to tell, on account of the depressions that we have been in and the state of other industries and their purchasing power, and so forth. The price of oil has been accommodated to the great production that has come about, and we have had some overproduction, but we wouldn't have had so much overproduction if we had had all industries stimulated. I will try to furnish you some figures on this point.

Senator VANDENBERG. You are convinced that it did operate to increase the productivity and thus to actually increase the income, though?

Mr. PARKER. That is right, and I know it stimulated investment in the oil business. A man got the chance to make more money and pay less taxes.

Senator VANDENBERG. Have you ever made any estimates on the amount of expenditure which might be made in this country by way of overtaking obsolescence in industrial institutions, if our entire industrial equipment were brought up to par again?

Mr. PARKER. No, sir; I have no accurate figures on that. I think you could arrive at some basis for making an estimate through the depreciation allowances to corporations. Depreciation allowances to corporations alone are a little less than $4,000,000,000 annually, and of course some of that is on buildings, but a great deal is also on machinery. So that you can tell that there was a very large investment in plant and in machinery. I don't know what that depreciation would run merely on machinery; it might run a billion and three-quarters, I would think, which would indicate an investment in machinery of perhaps $40,000,000,000.

Senator VANDENBERG. Well, that is a very interesting figure.

Mr. PARKER. I am just taking these out of my head, I may be rather inaccurate.

Senator VANDENBERG. Your head is the best source of that information that I know of in Washington.

Mr. Sloan made the statement Friday, rather dramatically, that the American industrial plant is virtually obsolete today, taken as a whole, because of the failure to keep it up to date. Well, I have heard estimates running all the way from 10 billion dollars up, as to the essential expenditures that ought to be made for the sake of simple efficiency in restoring the American industrial machine to a basis of decent productivity. Well, if the total investment is $40,000,000,000, taking your figure, and Mr. Sloan is remotely correct in suggesting that it is substantially obsolete, and estimate $10,000,000,000 as available for immediate expenditure under proper incentive, would not be out of line, would it?

Mr. PARKER. I don't think so, because of course some buildings are also obsolete and would have to be replaced in connection with the installation and modernization of the plants. The old buildings might not be adaptable to the heavy machinery, the floors might be wrong. Therefore, if you include what additional buildings are necessary, I think $10,000,000,000 to modernize our industries would probably be too conservative.

Senator VANDENBERG. Exactly.

Now, how are you ever going to reach this national income of $100,000,000,000, which you deem essential to an ultimately balanced budget; how are you going to reach it except that you do it through these precise fields of expenditure? Are not these the channels that we must pursue?

Mr. PARKER. The income is going to come about through a more rapid turn-over, which means a more rapid exchange. Everybody's standard of living goes up. There is more production and more exchange of that production. I have no panacea, Senator, for the whole thing, but it does seem to me, from my engineering experience, that this is a dynamic proposition. It is not a static one. The wheels have to go around and they have all got to go around together, in general, and everybody must produce more, thereby there will be an exchange for those articles that are produced.

Senator VANDENBERG. And, in your judgment, it is a practical thing to anticipate the stimulation of this increase to a reasonable degree of incentive taxation?

Mr. PARKER. I think it is well worth the trial.

Senator VANDENBERG. A suggestion has been made by some witnesses that corporations should be allowed to accumulate reserves in good years for the regularization of employment in bad years, and that those reserves ought to be entitled to some tax consideration. Would you have any comment to make on that?

Mr. PARKER. It is a little difficult to handle on account of getting a formula that would apply to all business. I think it ought to be studied. I haven't gone into it enough to know whether you could provide for a reasonable formula for such a reserve, and, of course, you might have to put certain safeguards around it. You would have to be careful not to open up loopholes to tax evasion.

Senator VANDENBERG. I think that is all I have to ask, Mr. Chairman. I am greatly indebted to Mr. Parker for his contribution. I think it is thoroughly constructive and forward looking.

Senator HERRING. It was suggested, Mr. Parker, that in connection with your general proposal we get your reaction as to whether or not you could obtain the same results as you hope to obtain by limiting the incentive deduction to a certain percentage of the net income.

Mr. PARKER. You mean abandon the surtax idea and limit this deduction to a certain percentage of the net income?

Senator HERRING. Yes; if you could obtain the same results.

Mr. PARKER. Well, it would be a very difficult thing. If you have a different percentage for each deduction, you would have all these percentages operating; however, if you lumped all the deductions together and set a percentage limit that would be practical, I believe the results, though, would be different than under my plan.

Senator HERRING. Well, if you have any other suggestions you wish to give us, we would like to have them. We appreciate very much having your advice.

Mr. PARKER. I have nothing else; I am glad to be here.

Senator VANDENBERG. I would like to ask you one more question, Mr. Parker.

When the Tax Research Institute of New York City testified the other day, they offered a specific proposed change in the revenue act, dealing with the particular thing you and I were discussing a few moments ago, namely, the importance of stimulating plant expansion and plant replacements. Evidently their suggestion also had in mind the necessity for protecting, to some degree, the existing Federal revenue. I would like to read to you—it is very brief—the proposed change which they suggest in section 23-A of the 1938 Revenue Act. They suggest it be amended to permit the deduction of—

> Fifty percent of any amount paid out for new buildings or for new machinery and equipment or for permanent improvements or betterments to be used in the taxpayer's trade or business, whether or not having the effect of increasing the value of any property or estate, and any amounts expended in restoring the property or making good the exhaustion thereof, whether or not allowance is or has been made, provided that the total of such amounts permitted to be deducted during a given taxable year for any and all of such purposes may not exceed 15 percent of the taxpayer's net income as computed without the benefit of this deduction.

Would that provide the essential revenue protection that you have in mind?

Mr. PARKER. That would provide protection. Of course, you have one little difficulty there. We already allow the corporation 5 percent as a deduction for charitable gifts—and it has got to be specified whether you are going to consider the net income after that charitable gifts deduction, because you would have the two percentages. You can do it, but suppose you wanted to give three or four more deductions—they propose one deduction, then you have all these different percentages and you are in more trouble. I think, unless you provide that the total of all these deductions shall not be more than 15 percent—and you could work it out that way—you would not gain in simplicity. This is the essential difference between the two plans: Under the one proposed by the Tax Research Institute you get no relief for spending for employment and plant expansion more than 30 percent of your net income, under my plan the relief increases until you have used all the net income you have left after payment of the minimum tax. Let me illustrate in the case of an individual. Under the 50-15-percent proposition, an individual having a net income of $1,000,000 who spent $300,000 for plant expansion would have his tax reduced from $679,000 to about $565,000. If he spent more than $300,000 his tax would not be further reduced. Under my plan if he spent $300,000 he would have his tax reduced from $679,000 to about $540,000 (not a far different result), but if he spent $600,000 instead of $300,000, his tax would be reduced to $400,000. My objection to the percentage limitation is that it will discourage instead of encourage expenditures beyond the point of that percentage. That is what happened in the case of the percentage limitation used in the allowance for charitable gifts.

Senator VANDENBERG. Well, it seems to me that your method of categories is preferable.

Senator HERRING. Thank you, Mr. Parker.

Judge Fletcher. Judge R. V. Fletcher, general counsel, Association of American Railroads.

Judge Fletcher is going to discuss profit sharing and incentive taxation in connection with the testimony we had the other day of Mr. Cherne.

STATEMENT OF JUDGE R. V. FLETCHER, GENERAL COUNSEL, ASSOCIATION OF AMERICAN RAILROADS, WASHINGTON D. C.

Mr. FLETCHER. My name is R. V. Fletcher; I am a lawyer. I live in Washington, and I am general counsel of the Association of American Railroads.

I think I should say perhaps that the Association of American Railroads is a voluntary association, and in its membership is comprised practically all of the class I railroads of the United States.

I think of those class I railroads something like 98½ percent of the mileage belongs to this association. A class I railroad, of course, is a railroad which under the classification of the Interstate Commerce Commission has a gross revenue of $1,000,000 or more per year. There is also an association which deals with the so-called short-line railroads, which is something separate and apart from the association with which I am identified. I think of the mileage of the railroads of the United States, of all classes, something like 95 percent belongs to the Association of American Railroads.

That association was organized and exists for the purpose of handling, cooperatively, all or any of the problems that come along in connection with railroad operation, railroad finance, railroad legislative proposals, and the like. It has various departments, and I happen to be in charge of what is known as the law department of that association, paying special attention to matters pending in Congress which are of interest to the railroads of the country.

I appear here in regard to Senate Resolution 215, not so much to discuss the profit-sharing features of that resolution, but another. I call attention, simply to make the record complete, to subsection (c) of the first section of the resolution, which reads:

> To the consideration of any other recommendations which may prove desirable in pursuit of the objectives—

And I refer back to one of the objectives mentioned in the resolution, which has to do with the grant of compensatory tax exemptions and tax rewards when profit sharing is voluntarily established.

I should be very glad, indeed, to give some information to the committee with respect to profit sharing except for the fact that the railroads have had no experience in profit-sharing enterprises and profit-sharing schemes; and indeed, in recent years, it is a matter of common knowledge that the revenues of the railroads have been so scanty that there were really no profits to share. But aside from that, I think the committee will understand that the railroad industry is a highly regulated industry whose rates are fixed by the Interstate Commerce Commission, and whose expenditures are determined very largely by the Interstate Commerce Commission, and by various other governmental agencies, particularly those that deal with wages and with working conditions, all of which are regulated in accordance with law.

So that it is very doubtful indeed if the Interstate Commerce Commission would permit rates to be put into effect on the railroads of the United States which would allow the accumulation of any amounts that might be shared with the employees in accordance with a profit-sharing scheme.

Theoretically the rates of the carriers are fixed in such a way as to give no more to the railroads than a fair return upon the value of their property. As a matter of fact, as I shall take the liberty of stating in a moment, the Interstate Commerce Commission has never been able to establish and approve rates which would give anything like a fair return upon the value of the property, and I have no doubt that the Commission would hold as a proper interpretation of the Interstate Commerce Act, under which it functions, that it would not be privileged, in the course of protecting the public interest, to allow any funds to accumulate to share with the employees beyond what would be necessary to pay operating expenses and taxes and something like a return upon the investment.

I think, gentlemen, that in considering profit-sharing plans, a distinction will have to be drawn between regulated industries, such as the railroads, and private industries, where they are free to fix their prices without Government interference as to the amount of the price.

And, in the third place, I don't think that railroad labor—I do not hold any brief for railroad labor, railroad employees—but my experience with them would indicate that they would probably not look with favor upon any established profit sharing. As I understand the policy of the leaders of union labor, they think that whatever amounts are left over and above such sums as are needed to sustain the industry, that their reward should come rather by an increase in the wage scales than by any profit-sharing plan. For those reasons I will ask the Committee to excuse me from expressing any views upon the subject of profit sharing as such.

But I understand, from what I have seen in the press, that perhaps this committee would permit me to say something on the question of tax incentives, which is one feature of the inquiry in which the railroads are tremendously interested.

Now, two serious problems confront the railroads at the present time, or perhaps I should say that there are many problems, but there are only two that I need mention, because I think they are matters of supreme importance.

In the first place, there is the great necessity for the reduction of debt on the railroads of the United States; and there is, in the second place, the greatest need for the expenditure of very large amounts of money in the rehabilitation of the plant. And to those two I would like to address myself.

I understand that the committee might not be interested so much in the question of debt reduction as they are in the question of plant expansion, and I can readily understand how that point of view might prevail, for the reason that a sum spent in debt reduction would probably not go immediately to the employment of the unemployed labor, or to the relief of the unemployment situation; whereas amounts spent in plant expansion, or in rehabilitation, which is probably a more accurate term to apply to it, would go to the improvement of the unemployment situation, and in a very substantial way, as I shall endeavor to point out.

On the subject of debt reduction, which I will refer to rather briefly, I call attention to the fact that as of January 1, 1937, the amount of the outstanding capitalization of the railroads of the United States was $18,319,000,000.

Of that $18,319,000,000, $11,250,000,000 is funded debt and $7,069,000,000 represents the par value of the outstanding capital stock.

Senator VANDENBERG. Before you leave that figure, Judge Fletcher, have you a comparable figure showing the market value of that capital stock as of that date?

Mr. FLETCHER. I haven't that figure before me, Senator. I would be very glad to supply it. It is a great deal less, of course.

Senator VANDENBERG. I think it would be a very significant figure.

Mr. FLETCHER. Of course, that varies from day to day.

Senator VANDENBERG. How about the bonded debt?

Mr. FLETCHER. The bonded debt of the railroads, if you talk about market value, is very much less than the par value. The par value is what I have given you of $11,250,000,000.

Now, the market value also fluctuates from day to day, but I could give you that figure as of any day that you would desire, and I should be glad to supply that in a letter to the committee if you should like to have it.

Senator VANDENBERG. Suppose you give it to us for the day comparable to the day when you made your other calculation.

Mr. FLETCHER. That would be easily done. This figure that I give you is of January 1, 1937, and the market value both of the stocks and bonds is less at the present time than it was then.

Senator VANDENBERG. Suppose we have both figures, then and now.

Mr. FLETCHER. I shall be glad to give it to you as of January 1, 1937, which is the date when I stated the par value of these securities, and I will give you the market value as of December 1, 1938.

ASSOCIATION OF AMERICAN RAILROADS,
Washington, D. C., December 14, 1938.

COMMITTEE ON FINANCE,
United States Senate, Washington, D. C.

GENTLEMEN: When I appeared on last Monday as a witness before the subcommittee conducting the hearings pursuant to Senate Resolution 215, I was requested by a member of the committee to furnish figures as to the market value of stocks and bonds as of certain dates. I stated that I would endeavor to supply the information through the medium of a letter.

Our statistics cover only the market value of railway bonds listed on the New York Stock Exchange. I undertook to give the figures as of January 1, 1937, and December 1, 1938. I am compelled, however, to request that I be allowed to substitute November 1, 1938, for December 1, 1938. I find that the figures are not available as late as December 1 of this year.

The market value of listed railway bonds on January 1, 1937, was $9,049,374,375. As of November 1, 1938, the market value of listed bonds was $6,083,140,000. It will be noted, therefore, that my estimate of 60 percent as representing the ratio of market value to par value was not very far wrong.

With respect to stocks, the market value of all railway stocks listed on the New York Stock Exchange as of January 1, 1937, was $4,498,551,725. As of November 1, 1938, the figure was $2,071,110,000.

Asked by a member of the committee to make a guess at the ratio of the market value of the stock to par value, I suggested 25 percent. The figure, however, turns out to be more nearly 37½ percent.

I shall be glad if this letter can be made a part of the record in this proceeding.

Very truly yours,

R. V. FLETCHER.

Senator VANDENBERG. Fine.

You wouldn't feel free to make a stab at that now?

Mr. FLETCHER. I can guess at it, and I don't know that my guess would be so very far off.

My opinion is that in the case of the funded debt, the market value at the present time is about 60 percent of the par value. In the case of the capital stock, the market value is more in the neighborhood of 25 percent of the par value.

Senator VANDENBERG. In other words, the $11,000,000,000 bonded debt was worth in the market value about $6,500,000,000?

Mr. FLETCHER. Yes, and the capital stock would be worth somewhere in the neighborhood of a little less than $2,000,000,000.

Senator VANDENBERG. Compared with a par of what?

Mr. FLETCHER. The par value of the stock is $7,069,000,000 as of January 1, 1937.

You will observe that taking this capitalization at par, and comparing the bonded debt with the capital stock, the bonds constitute about 60 percent of the entire capitalization, and the stock about 40 percent. That is true of the class I railroads, that ratio of 60 and 40 for the class I railroads. Taking the railroads as a whole, and basing my statement on a report recently made by Dr. Splawn, who is the chairman of the Interstate Commerce Commission, a very well informed and a very worthy gentleman indeed, he figured out that taking all of the railroads, the ratio of stock to bonds was about 55½ percent of bonds and about 44½ percent stock.

That is generally conceived to be a rather unwholesome situation, that the bonds should be 60 or even 55½ percent of the entire capitalization. Many people who have given some attention to this believe that the bonded indebtedness of the railroads should not be more than 50 percent of the entire capitalization.

I want to call your attention to the fact, however, that there may be something a little bit peculiar about railroad capitalization, that this 55½ percent, or in the case of the class I railroads, 60 percent, of the entire capitalization representing bonds, is money which has been borrowed and spent in plant expansion, in the construction of the plant. It doesn't represent accumulated deficits for which money has had to be borrowed. It represents really a part of the essential capital structure of the railroads.

Senator VANDENBERG. You mean you don't run the way the Government does?

Mr. FLETCHER. Well, I don't know about that, but I know that sometimes private industry has to borrow money to pay expenses. That isn't the case of the railroads. The truth about it is that railroads were originally built out of money derived from the sale of capital stock, and as those railroads expanded and extended and found it necessary to double and treble their plant, they were able in those days to borrow money so much cheaper than they could acquire money by the sale of capital stock. That is to say, if you had a fairly prosperous railroad that was paying 6-percent dividend, the owners of that stock did not feel like selling stock and admitting others into a 6-percent dividend-sharing program, when they could borrow money at about 3½ or 4 percent. It was considered to be sound financing for them to expand their property through the sale of bonds rather than through the sale of stock, and I think it is worth remembering that the average interest rate now upon the bonds which the railroads have outstanding is 4½ percent.

Well, in order to meet the interest on these outstanding bonds, the annual interest accruals for the year 1937 amounted to $448,344,204. I give you the exact figure for the year 1937, the latest year for which figures are available. That is the figure of interest accruals, that is the amount which the railroads would have to pay as interest upon their bonded debt if in fact all of them were paying the interest on their bonded debt. As a matter of fact, the interest payments for 1937 amounted to no more than $344,425,036. That is because about one-third of the mileage of the country is in the hands of the courts, undergoing reorganization, either through the medium of equity receiverships or through bankruptcy under section 77 of the bankruptcy law. So that one-third of the mileage of the country is relieved from the immediate duty of paying interest on their bonds.

Senator VANDENBERG. How much of that one-third is in class I railroads?

Mr. FLETCHER. I am speaking of class I railroads; I should have said that, I meant class I railroads—31 percent is now in the hands of the courts.

Senator VANDENBERG. How much of the other railroads is in the hands of the courts?

Mr. FLETCHER. I haven't that figure before me, Senator, but I think it runs about the same proportion. It is worth remembering that at the present time in the hands of the courts, under reorganization, are such important railroads as the Frisco, the Missouri Pacific, and the Chicago, Milwaukee & St. Paul, and the Chicago & Northwestern, and the Central of Georgia, and the Seaboard Air Line—and many others that I could mention.

And I might say in that connection, that many other railroads beyond those would have been probably in bankruptcy but for a very generous and liberal lending policy on the part of the Government of the United States through its lending agency, the Reconstruction Finance Corporation.

Senator VANDENBERG. Does that just postpone the time when they will go into the hands of receivers?

Mr. FLETCHER. Unless things improve; yes.

Two important railroads are now undertaking the very difficult task and the very interesting experiment of trying to get their capital structures reorganized by the voluntary action of creditors, without having to go through the long and expensive and tiresome machinery of reorganization under section 77. I refer to the Baltimore & Ohio and to the Lehigh Valley. It looks as if the Lehigh Valley were going to make the grade all right. I hope the Baltimore & Ohio will also. Their structure, of course, is much more complicated than that of the Lehigh Valley, because it is so much larger.

Now as I have said, sound financing would probably require that the funded debt should not be more than 50 percent of the entire capitalization. And that means, you see, that there should be a reduction of funded debt amounting to at least $4,000,000,000, which would bring this figure of $11,250,000,000 down to about $7,250,000,000 an amount equal to the par value of the capital stock outstanding.

Senator VANDENBERG. And that would also bring it down about to your estimate of the market value of the bonds?

Mr. FLETCHER. Yes; that is not far from it, Senator. I think that is a coincidence, but an interesting one.

Senator VANDENBERG. I think it is a very significant coincidence.

Mr. FLETCHER. I think it is.

Senator VANDENBERG. Because I have been tremendously intrigued by the idea that if the railroads were permitted to buy their own bonds instead of letting the speculator, and take advantage of the shrinkage without a tax on them, that they could rather painlessly reorganize their bonded structure through this very simple tax incentive. Are you going to discuss that?

Mr. FLETCHER. I had not had it in mind to discuss particularly that which was so clearly brought out at an earlier hearing by a gentleman who appeared before the committee, but it is a very interesting and practical point.

Senator HERRING. Do you think that is a practical suggestion, the one made by Mr. Cherne?

Mr. FLETCHER. I thought so. Of course the funds would have to be forthcoming by the railroads, but it seems to me that if the railroads could go into the market, using the illustration that I think was made before the committee, if they could buy bonds for 20 cents on the dollar, as some of them can be bought, without having the necessity for paying taxes on an 80-percent profit, it would be a very great incentive indeed to the purchase and retirement of these securities.

If we could reduce the funded debt by $4,000,000,000, assuming that 4½ percent is the average interest rate on the railroads' funded debt, you would thereby reduce their fixed charges, you see by $180,000,000, and that would be a very desirable thing indeed.

The Interstate Commerce Commission properly and wisely, as I think, is endeavoring to bring about a policy whereby there will be reserves set up by the railroads for the retirement of their bonds; and in the securities which they approve—because the Interstate Commerce Commission, you know, has to approve the issuance of all securities—in the orders which they make permitting the issuance of securities (sometimes those are refunding securities), they have very generally, in recent months or in recent years, provided that sinking funds shall be set up for the purpose of retiring those bonds and putting into effect a system of wholesome amortization of the funded railroad debt.

It has been commonly said that the ideal situation would be to retire these bonds, or to provide for future plant expansion by the sale of capital stock, but that is of course impossible at the present time because there is no market for the sale of capital stock except in the case of a very few railroads. In the case of those railroads that could sell their stock at a desirable figure, their funded debt rests upon them, not as a burden, no particular burden, and therefore there would be very little incentive to retire it. I refer to such roads, for instance, as the Norfolk & Western, the Chesapeake & Ohio, possibly the Pennsylvania, which are in a fairly good financial condition compared with some other railroads of the country.

And I know, Senators, no public opinion which is more pronounced, more unanimous, than the view that there should be some kind of a program set up for reduction of debt on the railroads. It goes to the point, of course, of having many people advocate, to use the common expression, that the railroads should be put through the wringer. Personally, I don't have much sympathy with that view, stated thus broadly and without exceptions, because if a railroad is insolvent and can't pay its debts, the court will put it through the wringer all right through the medium of bankruptcy, the Bankruptcy Act, and if the railroad is able to pay its debts, I know of no principle of law or of morals, for that matter, which would justify repudiating its obligations.

But I am quite sure that if some method could be found whereby moneys could be secured for the purpose of relieving the burden of debt that rests upon the railroads, it would go very far toward restoring its credit and rehabilitating the industry.

And that is all I had in mind to say, unless there is some question on the question of debt reduction.

Senator VANDENBERG. Before you leave it, I would like to recur once more to the suggestion we were previously discussing, because I would like to know what is wrong, if anything is wrong, with this notion that a railroad shouldn't be permitted to buy its own securities at their market value and take advantage of the saving without taxation on them. If the total debt reduction which the railroads require is already represented by the total market reduction in the value of railroad securities, doesn't it seem rather clear that there ought to be a relationship between the two in seeking a formula that you discuss, and would it not inevitably be to the advantage of the situation if the railroads were permitted to take in these securities without tax?

Mr. FLETCHER. Why, undoubtedly, Senator, I don't see how there can be any question about it. If there are other considerations of public interest that would permit it to be done.

Senator VANDENBERG. Doesn't every public interest trend in that direction?

Mr. FLETCHER. Well, it seems so to me. I have no thought of saying anything else except in commendation of such a suggestion, because as you well say, Senator, the market reflects the views of the investors as to what is now the amount of reduction there should be in debt, stating it in another way.

Senator VANDENBERG. But meanwhile there is this further consideration; let us assume that the Government, by some heroic contribution, makes it possible for railroads to be rehabilitated; the private speculator who bought these bonds at 20 cents on the dollar thereupon becomes the beneficiary of the Government's activity in cooperation with the railroads. Certainly it is to the interest of the Government which furnishes the cooperation that the railroads, backed by the Government's cooperation, should be the beneficiary instead of the speculator.

Mr. FLETCHER. I think so.

Now turning to what is my principal subject here, and about which I want to lay the greater emphasis, namely, the need of the railroads to spend money for their own rehabilitation, I would like to call attention to the needs of the railroads in the matter of equipment, both the amounts which they should spend for repairing their equipment and the amount which they should spend for new equipment.

I have before me a statement which was made up by our department of operation and maintenance, headed, as it is, by a very competent man—I may mention his name, Mr. Symes—submitted at one time in the course of a rate case to the Interstate Commerce Commission, and now revised so as to reflect present conditions. And with your permission I would like to put into the record a few figures, with some comment of my own, with respect to what that shows.

On November 1, 1938, which is a very recent date, the carriers owned 1,689,782 freight cars.

Of that amount, 234,926 cars were in bad order. That is too many cars in bad order for a wholesome condition. It is commonly believed that not more than 6 percent of the freight cars of the country should at any one time be in that condition which we call bad order; that is, not available for immediate use. And therefore, of that number of cars which I mention, the bad-order situation should be corrected to the point where the bad-order cars are not more than 6 percent of the ownership.

Senator VANDENBERG. By your figures then, over 12 percent——

Mr. FLETCHER (interposing). Yes; there are over 12 percent at the present time, and upon my figures and upon my theory, they should immediately put into good condition, or as soon as possible put into good condition, as many as 133,540 cars.

Senator VANDENBERG. Have you any estimate as to what it would cost to do that?

Mr. FLETCHER. That is what I was coming to next.

The average cost of repairs is estimated at $400 per car, and the total amount that should be expended, to reduce the bad-order situation down to where it wouldn't be greater than 6 percent of the entire ownership, would require the expenditure of $53,416,000. That is the situation as of November 1, 1938, so far as freight cars are concerned.

But I want to call attention to the fact that not only is there great need for the repair of these cars, but the railroads of the United States, if they are to perform their legitimate function, need at the present time to buy new cars in an amount which has been conservatively estimated at 100,000 new freight cars per year for the next 5 or 6 years. They ought to buy 100,000 new freight cars every year for the next 5 or 6 years.

"Well," someone will say, "how do you reach any such conclusion as that?" Well, one way to arrive at it is to examine what the railroads did do in a period of comparative prosperity, and I refer now to the period from 1923 to 1929, inclusive, a 7-year period. In that time, this table that I have before me shows that the average number of cars added annually during that 7 years was 114,832 cars. In that whole time from 1923 to 1929, while the amount varied in different years, being highest in the year 1923 and lowest in the year 1928, the average was 114,000 new cars every year, which the railroads added to take care of the traffic which was offered to them. Of course, you understand why it was so heavy in 1923. That was because the railroads had then only recently emerged from the Government-ownership period—Government-operation period, I should say—and railroad equipment was run down dreadfully when the railroads came out of the Government control. That is no reflection on the Government; they had to run those cars just as long as they could to handle the war traffic which was offered to them at that time, and with no time to stop and keep the cars in repair.

In the period from 1930 to 1935, the depression period, instead of buying 114,000 cars a year, they bought only 21,000 new cars a year, for lack of funds, and partly because, of course, traffic had fallen off. To show how responsive the railroads are to anything like an improvement in business, I call your attention to the fact that in 1936, when things were looking a little better, they bought 43,941 cars; and you remember that at the beginning of the year 1937, when the picture was much brighter, before the recession set in, they had already contracted for and did actually receive and pay for in 1937, 75,058 cars. Of course, if they could have stopped their orders after the recession began to be so marked and significant, along about August or September of 1937, it would have been a different story; but those orders had already been placed, and of course delivery was being made.

So I think it is clear that the railroads ought to buy 100,000 new freight cars for the next 5 or 6 years.

Senator VANDENBERG. You mean yer pear?

Mr. FLETCHER. Yes; annually. And that would cost about $300,000,000 a year to buy those 100,000 freight cars annually, so there is an expenditure of $300,000,000 annually for the replacement of freight cars.

And that means, too, if you continued to perform the railroad business in the type of equipment which they have now—and I would like to have permission if time permits to consider, with the committee, briefly, in a little while, the necessity for spending a great deal more money than that in buying a new-type freight car, lighter cars, cars that can be handled more economically than the present cars—but these figures are made upon the assumption that the classic type of freight car, so to speak, will be continued in use.

Let us look at the locomotive situation, which is interesting.

On the 1st day of July 1938—that is the latest date that I have the figures on that particular type of equipment—the carriers owned 43,119 locomotives. Of that number, 7,875 were awaiting repairs. Now, that is an unwholesome situation. That is a greater percentage of locomotives in bad order than should prevail if the railroad business is to be carried on as it should be. The best judgment is that the bad-order locomotives should not be more than 10 percent of their ownership. That means that 3,564 locomotives should immediately be put in good condition, so that the percentage of bad-order locomotives would not be in excess of 10 percent.

That will cost, on the basis of an expenditure of $7,000 per locomotive, which is conservative, about $25,000,000 to repair, put in good order, the locomotives necessary to produce a comfortable and wholesome situation in the matter of power.

Not only is there the necessity for repairing these locomotives, but it is well understood in the railroad industry that the railroads ought to buy 2,000 new locomotives per year for the next 5 or 6 years, which would involve an expenditure of $200,000,000.

Senator VANDENBERG. Per year?

Mr. FLETCHER. Per year.

The reason why we say that they ought to buy that number of locomotives is based largely, as in the case of cars, upon experience.

For the same years, 1923 to 1929, inclusive, for that 7-year period, the average number of new locomotives added per year was 2,075; and it is for that reason, among others, that it is believed that 2,000 new locomotives should be added annually for the next 5 or 6 years.

Senator VANDENBERG. Are you still dealing with class I railroads alone, or all railroads?

Mr. FLETCHER. I am still dealing with class I railroads alone.

From 1930 to 1935, inclusive, they added only, on the average, 174 new locomotives per year.

There were 2,000 new locomotives annually in the period from 1923 to 1929, 174 in the period from 1930 to 1935.

In 1936 they added 87 new locomotives. In 1937, for the same reasons that I mentioned awhile ago, because business looked pretty good at the first of the year, they added 373 locomotives.

So the best judgment is, 2,000 locomotives should be added each year for the next 5 or 6 years, with an annual expenditure for that purpose of $200,000,000.

Senator VANDENBERG. As you go along with these figures, Judge Fletcher, would there be any general percentage that could roughly be applied to project the figures over the entire railroad situation of the country?

Mr. FLETCHER. You mean including the small railroads as well?

Senator VANDENBERG. Yes.

Mr. FLETCHER. I think there would be very little difficulty about that. I do not happen to have that information because, as I said, we deal only directly with the class I railroads.

Senator VANDENBERG. Would you hazard a general percentage which we might apply to your figures to cover the country as a whole?

Mr. FLETCHER. Well, I think 10 percent added to it wouldn't be far wrong.

Not only do we have this need for the considerable expenditure for locomotives and freight cars but we have got to look at the railway track structure; that is to say, the condition of rails and ties and the ballast.

The railroads in the last 8 years, these being years of depression, have laid something less than 1,000,000 tons of new rail annually. It is believed that they ought to have expended, or at least they should begin now the expenditure of 2,000,000 tons annually for the next several years.

Again referring to experience, our tables show that in the period from 1923 to 1929, inclusive, the average per year of new rail was 1,977,000 tons, which is practically 2,000,000 tons. For that reason we say they ought to put in 2,000,000 tons of new rail annually for the next 5 or 6 years. That is only new rail. I do not encumber this record—I don't think it would hardly be desirable—by mentioning the amount of second-hand rail which has been laid in that time, because, generally speaking, that is rail which has been taken out of the main lines and put into less important lines. I am confining my observations to new rail.

In the 6 years from 1930 to 1935, they laid on the average, annually, instead of 2,000,000 tons of rail, only 751,000 tons of rail, due to the depression and the lack of revenue to pay for the new rail.

In 1936 they laid 921,000 tons, and in 1937 a little over 1,000,000 tons. But clearly, there is need for the expenditure of very considerable amounts of money in the laying of additional rail.

Now, to lay 2,000,000 tons annually of new rail would cost about $100,000,000.

Senator VANDENBERG. Is that the cost of the rail and the cost of laying it, together?

Mr. FLETCHER. That is the cost of the rail in place, as we call it; the cost of the rail and laying it, figuring it on the basis of $50 a ton.

Senator VANDENBERG. That would be $100,000,000 a year for the next 5 or 6 years?

Mr. FLETCHER. Yes; for the rail.

Now, $50 per ton—that figure is predicated upon the cost of something like $40 per ton for the original cost of the rail, plus $10 per ton for laying the rail.

There has been some advance in the price of rail recently.

Not only is there the necessity for this expenditure of money for rail, but we have got to consider the tie situation. In the 7-year period to which I have referred, the period of relative prosperity, the railroads laid annually, from 1923 to 1929, inclusive, 52,440,000 treated ties and 27,606,000 untreated ties. By a "treated tie" ordinarily we mean a creosoted tie. The tendency in recent years is, wherever it is possible, to lay down treated ties rather than untreated ties, because they have so much longer life.

Those figures have fallen, in the 6-year period of 1930 to 1935, inclusive, to 35,000,000 treated ties annually and 11,412,000 untreated ties annually. Again we find that in 1936 the number had increased, particularly in the case of the treated ties, that figure going up to 36,771,000 for 1936 and 38,074,000 for 1937, although there had been no increase in untreated ties, the state of the art being such that untreated ties were put in only in rather exceptional cases.

It is probable that due to the fact that treated ties have taken the place of untreated ties, and they have so much longer life than untreated ties, it would probably not be necessary to lay more than 60,000,000 ties annually for the next 5 or 6 years, but that would cost about $90,000,000, because the cost is about $1.50 to lay, put in place, a treated tie.

Senator VANDENBERG. That is $90,000,000 a year for 5 years?

Mr. FLETCHER. Yes; for the next, say, 5 years.

Now, ballast cannot be ignored. That is not as large an item as the others, but certainly it is a factor of additional expense in order to take care of deferred maintenance, so that there should be spent, say, $10,000,000 annually for the next 5 or 6 years, in repairs and restoring the ballast conditions of the railroads.

But that makes a total, if my arithmetic is not at fault, adding up all these items, of $775,000,000—repairs to cars, new cars, repairs to locomotives, new locomotives, new rails, new ties, ballast. I think it is a very conservative figure to say $600,000,000, making all allowance for possible error, and that figure of $600,000,000 has been used rather confidently by railroad spokesmen in recent months in public statements, as to the needs of the railroads for the next few years.

Senator VANDENBERG. In your inventory, Judge Fletcher, you said nothing about passenger cars?

Mr. FLETCHER. No; I have not; I have confined, so far, my statement to freight cars.

The passenger-car situation is undergoing changes so rapidly that it is a separate story altogether, and a very interesting one, and that brings me to mention one feature of this thing that I cannot state arithmetically or statistically but which nevertheless is one that ought to be considered.

At the present time, due largely to the scientific use of alloys of various kinds, it is possible, if the money were available, to discard the old type of freight car and put in its place cars made out of these light alloys, cars that are light in weight, in such a way as to reduce the total load which has to be drawn by a locomotive, and thereby add immensely to the efficiency of the railroads, and particularly to the economy of operation.

I don't know that this committee would be interested in the detail of just how those various alloys may be used, but they are compositions of iron and chromium, nickel, manganese, silicon, and molybdenum, and others—of greatly increased strength of material, but nevertheless they would lighten the weight probably 50 percent.

A few of those cars have been built, and they have been tried, and if you could substitute for the present wooden freight cars, cars made out of these alloys in accordance with recent inventions, you would lighten the load of the equipment, which is a very important part of the thing, so much that the tractive power of the locomotives would be tremendously increased, and as a result operating expenses would be much less than they are now.

That leads you to a consideration of the passenger-train situation, because there is a tendency, as you all know, in recent years, to substitute passenger cars of lighter weight for the passenger cars of the heavier weight, which so long prevailed, and that has resulted in a tremendous increase in the speed of passenger trains, and also added greatly to the comfort of passengers.

Now, just how much money would be involved, Mr. Chairman, in the substitution of the lighter-weight cars for the heavier cars, I am sure I couldn't give you a figure on, but it would be a tremendous improvement in railroad operation if funds were available for that purpose.

Senator VANDENBERG. How about the substitution of Diesel engines and the electrification of railroads?

Mr. FLETCHER. Of course, that is going on all over the country, the substitution of Diesel locomotives for steam locomotives. There is some difference of opinion among the experts as to the relative value and merit of those.

Electrification is going on on the Pennsylvania Railroad, perhaps, more strikingly than any other railroad I can think of at the present time. The capital cost of electrification is high. The operating expenses, however, are so much lower that it has been considered justified in many cases where the money could be found.

Obviously, the railroads are passing through a transition stage, and we need the lighter materials. Every effort should be made and every resource should be exhausted to reduce railroad operating expenses.

I think it might be interesting to remember that even without the substitution generally of the lighter equipment for the heavier equipment, the improvements in the art of railroading have been such that the speed of freight trains has been increased 50 percent in the last 20 years. Our figures show that if it had cost as much per unit of weight to move the tonnage of the railroads in the year 1937 as it did in 1921, the operating expenses of the railroads would have been $1,500,000,000 greater in 1937 than they really were. In other words, the present bad situation of the railroads would have been much worse if there hadn't been improvements in the direction of economy, in the use of fuel and things of that kind.

I have a table here which shows that. I don't intend to put a great deal of it into the record, but I think it is worth remembering that whereas in 1921, the freight-car-miles per train-mile were 37, that means that the average freight train had 37 cars in it; in 1937 that had risen to 46.6 cars. If you can haul, with 1 locomotive, a train of 46 cars, whereas in 1921, you had an average train of 37 cars, you have made a tremendous improvement in the matter of expense. That is attributable in part to more efficient power, and part to the cooperation of shippers in loading the cars more promptly, and a great deal of it is attributable to the fact that much of the movement of less-than-carload freight, which goes for short distances, has gone to the trucks. And therefore the railroads have been bulk carriers of freight to a greater extent than they were in 1921.

Senator HERRING. Do you have any figures as to the comparative cost of labor, per train-mile, as between 1921 and 1937?

Mr. FLETCHER. Yes, sir; I have a lot of that.

Senator HERRING. I wondered if this decreased cost could in any way be ascribed to a decreased cost of labor?

Mr. FLETCHER. Labor is higher per hour—it isn't higher per unit of traffic handled, Senator, because of the increase in the case of freight trains. I think the most significant figure I have to show on what economies have been brought about is that in freight service in 1921, you had to burn 162 pounds of coal for each thousand gross ton-miles that you operated on the railroad; that is to say, to move 1,000 tons 1 mile you had to burn 162 pounds of coal in 1921; whereas, due to improvements in the handling of fuel, fuel practices, the consumption of fuel, in 1937 it took only 117 pounds of coal to move 1,000 tons 1 mile. That is in freight service.

In passenger service, to move a passenger train a mile, the number of pounds of coal necessary per passenger-train car-mile was 17.7 in 1921, and it had dropped to 15.1 in 1937.

Taking those figures and applying them to the widely extended railroad service throughout the United States makes a tremendous amount of improvement in the matter of economy.

Gross ton-miles, locomotive and tender being excluded, gross ton-mile for freight trains, per train-hour, in 1921—it was 16,555 in 1921, and it had gone up to 30,349 in 1937.

I mention those economies. They may not have such a particular bearing on the question before you, but it does answer the criticism which is often made that the railroads have not been alert to adopt modern methods in the operation of their railroa...

I think they have made as much progress along that line as any other industry. Of course, it is not spectacular, Senators, the public doesn't see it; they are not offering a new locomotive for sale every year, with a lot of beautiful improvements and gadgets and the like, but the improvement has gone on there as shown by these rather dull figures that I produce.

Not only do we need to spend a good deal of money now to build new freight cars of lighter weight, but we need to gear our locomotives to the demands of industry in a very significant way. We are undergoing, as everybody knows—you know it better than I—a very great revolution in the way in which business is handled in this country. It is manifested in one significant, striking way, in the relocation of industry; that is to say, the relocation of manufacturing plants so as to be in smaller units and nearer the point of consumption, and thereby prevent the necessity for such long hauls and the payment of large transportation charges. You have to gear your railroad industry and every other form of transportation industry to the demands of the modern business, and that is going to require greater speed, and a greater number of locomotives, and locomotives frequently of a different type.

That is the reason why I lay emphasis upon the need of improving railroad credit so as to enable the railroads to tap sources of private capital to allow this rehabilitation to go on in a significant way.

Not only do we need this improvement, but we need to spend a great deal of money in the improvement in shop machinery. That is a subject that might lend itself to a discourse all by itself, but a good many people think that a large amount of money ought to be spent in shop machinery.

I dare say that if it were possible to secure the capital, in order that the railroads might function properly, they ought to spend $1,000,000,000 annually for the next few years. I mentioned the figure awhile ago of $775,000,000, or $600,000,000, dealing with cars and locomotives and rail and ties and ballast only, but if we were to go into a policy of replacing the present type of equipment with modern equipment, both cars and locomotives, and take into consideration the necessity for rebuilding the shops, I believe that it would be safe to say that $1,000,000,000 a year ought to be spent in the next 10 years for the railroads. They spent close to that, you know, in the years 1923 to 1929, in the way of improvements, and I think it is quite significant too, that while they did spend a large amount of money in that time, they did not issue new obligations for all of it either in the form of bonds or stocks. The amount of such issues was not more than one-third of their total addition to their capital account.

The rest of it was plowed back into the property and represents in a way a sacrifice on the part of the stockholders in the way of dividends to improve and rehabilitate the property.

That money wasn't wasted. If it had not been for that expenditure of large sums of money in the years 1921 to 1929, it wouldn't have been possible to bring about the economies that I mentioned awhile ago, because it was only by reducing grades, by enlarging yards, by buying new equipment of greater power, and new cars of greater capacity, that they were able to make this great improvement in the matter of fuel and other expenditure which reflected itself finally in the operating results of the railroads.

Suppose we could spend that amount of money for the next year, what would it mean to industry outside of the railroads? Well, it seems to me that you may assume in the manufacture of cars, the manufacture of locomotives, the manufacture of new shop machinery, rails, ties, 60 percent is labor cost. I don't know that I have any accurate figures on that, but I think that figure is too low. On the most conservative basis, 60 percent would be represented by labor costs, either direct cost of laying the material, or the cost of manufacturing back of the line, so to speak. I know that in the case of grade-crossing projects, we made some studies on that subject, and the labor cost amounted to 80 percent of the total cost; but say 60 percent, in order to be safe. Then you would assume that the average annual wage is $1,200.

Now, that may be too low. In the case of the railroads, railroad labor average cost is about $1,700; but taking it by and large, if it is $1,200, $100 a month, on the average, that would put 500,000 men to work if the railroads were to be permitted to spend the amount of money that I have stated, and I mentioned a while ago that it does not seem to be extravagant to speak of $1,000,000,000 a year, in view of the experience of the railroads in the period 1921 to 1930.

We have a distressing amount of unemployment in the railroad industry, just as much so as in any other industry. I have a little table here before me that shows how many men were employed in the railroad industry as far back as 1916, and how it stands now.

On November 15, 1938, which is the middle of the month—and the Interstate Commerce Commission makes it count as of the middle of the month—there was then on the pay rolls of the American class I railroads 960,776 men. In 1926, which was the high year of railroad activities since the war, there were 1,779,000 men employed. So that you see there has been a falling off, as between 1926 and 1938, of three-quarters of a million employed by the railroads.

The highest year that has ever been in railroad employment was in 1920, when there were 2,000,000 men employed, but that was a reflection of the Government-control period, when there was no necessity, you know, for meeting the expenses from the receipts of the railroads. The Treasury took care of the deficits, which ran about $1,000,000,000 a year, or something like that, during the period of Federal control.

So there is a distressing amount of unemployment undoubtedly in the railroad industry, and I certainly think it would be in the public interest to employ a greater number of men.

Senator HERRING. This rehabilitation program, in addition to those 500,000 men, would put quite a number of these 800,000 back to work, wouldn't it?

Mr. FLETCHER. Well, I would think so. From now on the particular question that you have before you, namely, the tax situation, maybe I would not be amiss to put into the record just how much taxes the railroads pay and how that is distributed. It will take me only a minute.

In 1937 the railroads of the United States—this is now the class I railroads again—paid altogether in taxes $325,665,000. That was a lower figure than they had paid in many previous years. The figures ran as high as $396,000,000, back in the relatively prosperous year of 1929. Most of us making railroad speeches, and so on, commonly say that they pay $1,000,000 a day in taxes, and under anything like normal conditions they certainly do.

Senator HERRING. That is all taxes, Federal and State?

Mr. FLETCHER. Yes; and I am talking about 1937 now.

Of that amount they paid $29,298,000 in social-security unemployment taxes to the States, and they paid $10,286,000 in social-security unemployment taxes to the Federal Government.

You understand how that law stands now. Ninety percent of it is supposed to be paid to the State and something like 10 percent to the Federal Government, the 10 percent to the Federal Government going largely to pay operating expenses of the Social Security machinery that operates and applies the act.

Now, from and after July 1, 1939, the unemployment taxes paid by the railroads will no longer be paid to the States because, by an act of Congress passed this year, at the last session of Congress, the whole matter of unemployment insurance taxes as far as railroads are concerned, is transferred to the Federal Government and the States will relieve the railroads from that tax. But to get the total amount of taxes you have to add those two figures together. It amounts to about $40,000,000,000.

The railroads in the year 1937 also paid $25,289,000 for their railroad pensions system, which has now been taken over by the Federal Government and is administered by the Government. That figure is not a normal figure. For 1936 the amount paid was $47,298,000. You may wonder why it is that between 1936 and 1937 the amount was reduced from $47,000,000 to $25,000,000. That was due to a certain readjustment which was made in the year 1937 in the accounts of the carriers, due to the fact that the first pension act, passed in 1935, was declared unconstitutional by the Supreme Court, and the amounts of money which had been paid under that, were refunded to the railroads by the Federal Government under a decree of the Court, and credit was given on that account. I think normally you could depend upon something like $50,000,000 being the tax bill of the railroads for this retirement system.

Outside of the Social Security unemployment tax, there was paid in 1937, to the States, $222,558,000. The income taxes, ordinary income taxes, paid to the Federal Government for that year, amounted to no more than $32,000,000, because of the fact that railroad operation had been so bad that there were not many railroads, not a great many railroads, that had any taxable income after making deductions for their expenses and their fixed charges. Their capital stock taxes were $4,824,000, and some certain miscellaneous items of small dimensions, such as taxes on liquors sold in dining cars, and club dues, and so on, made the total amount paid to the Federal Government $72,700,000.

I am not at all certain, gentlemen, that if tax incentives are to be applied to the railroads, that you could do anything about this railroad retirement tax. You see, that has got to be self-supporting. That is a tax upon the pay rolls to pay pensions to the railroad employees, and the amount required and the amount that will be expended, the amount that will be collected from the tax on the pay rolls, has been rather carefully worked out on an actuarial basis. But I do think, I don't know whether this is the time to make that statement or not, that the present unemployment tax as applicable to railroads, should take into consideration the merit principle, which has been so largely adopted by the States. I think that 41 States out of the total that we have in this Union have some kind of a merit-rating principle in their unemployment taxes, which means, translated into the simplest language that I can think of, that a man who has so handled his business as to have little or no unemployment, gets a credit for that fact so that he doesn't have to contribute, by taxes on his pay roll, to the benefit of the unfortunate employer who has so handled his business, either deliberately or through the accidents of fortune, as to have a great deal of unemployment in his particular business.

I don't know whether this committee could do anything about State taxes. It is the heaviest tax burden that rests upon the railroads at the present time, but I take it that the Congress should build for the future. If the railroads are to be rehabilitated and to be reinstated to a position where they will be able to earn enough to establish their credit, undoubtedly this figure of income taxes will go up very rapidly. As a matter of fact, they have paid income taxes in the past, ordinary income taxes, as high as $88,000,000 a year, that being the year 1929.

If this committee should see proper to present a report to Congress along the line of giving some credit on taxes, for the amounts which the railroads spend in the rehabilitation of their property, it certainly would have, I think, a wholesome effect upon the policy of the States in the matter of taxation of railroads, because there are instances, I venture to say, where it would seem that the policy of the States in connection with railroad taxes has been very short-sighted.

I don't want to mention the States, I don't think it would be proper, but there are States in the Union where, while consideration has been given to the losses that ordinary property has sustained and to their inability to meet a heavy tax burden, that same consideration has not been given to the railroads. Railroad property, you know, is pretty hard to escape taxation. It spreads out before the tax assessors in a very conspicuous way. There are their tracks, and there are engines, and there are their operations—and there is no way of having securities in your portfolio which the tax assessor never hears about.

I would like to ask that—I believe there has already been made a part of this record a very thoughtful memorandum submitted by Mr. F. J. Fell, of the Pennsylvania Railroad. I do not need to more than refer to it, but I do want to say a word, if I may, upon the special situation of the railroads in connection with what is left of the undistributed-profits tax. It is still on the statute books, it is still, I believe, the policy of a good many people in authority who cling to the principle of an undistributed-profits tax. We worked on that a good deal. I have had the privilege of making rather extended statements before the House Committee on Ways and Means, and the Senate Committee on Finance, with reference to the hardship of the undistributed-profits tax as applied to railroads, and I have a memorandum here that a committee of ours prepared for the use of the

Secretary of the Treasury on that subject, and I wonder if I might file that with the committee, rather than try to go into it in detail and take your time in trying to rehearse all the arguments therein set out?

Senator HERRING. It may be included in the record as an exhibit.

(The document referred to was received as an exhibit.)

Mr. FLETCHER. Briefly, it amounts to this: That there is a great necessity for reduction of debt, as I have tried to show, and there is great necessity for the expenditure of a very considerable amount of money in rehabilitation of the railroads. There is no way by which that money can be obtained, as far as I know, except by having some profits over and above the cost of operation.

It did seem to us, with special reference to that particular type of tax, that the public interest would be greatly improved or increased if it were possible for the railroads to apply those profits to those wholesome ends rather than to the payment of undistributed profits tax.

I think that is all that I have, Senators, unless there are questions.

Senator VANDENBERG. Well, as I understand your general conclusion, Judge Fletcher, you think that if the railroads return to solvent operation, the principle of incentive tax, as appropriately applied, would go a long ways toward releasing this tremendous buying power to take up this building necessity for replacement and expansion that the railroads are confronted with?

Mr. FLETCHER. I think there can be no serious doubt about it by anybody who looks into it. The railroad industry not only is a great industry so far as transportation is concerned, which is its principal function, but in normal times it spends $1,500,000,000 for materials and supplies.

Think what that means. I think if the railroads could have continued to buy as much material and supplies through the depression as they did before the depression, there would have been no necessity for such a tremendous expenditure of public funds for relief. They would have spent $1,000,000,000 a year more than they did.

Senator HERRING. Thanks very much, Judge Fletcher. That has been very helpful.

Senator VANDENBERG. Mr. Chairman, before we recess, I would like to refer, for the record, to the estimates which were made when Mr. Parker was on the stand about the deficiency of durable-goods production in the United States.

One of the leading economists of the country, whom I am not at liberty to identify at this moment, but shall later, and who is as reliable as anyone could be upon such a subject, finds that the deficiency of durable-goods production, estimated in present dollars, is in excess of $60,000,000,000, and he makes the very interesting comment that if this country is not to go down hill in the economic sense, but is merely to hold its own in a modest way, there are probably jobs for at least 7,000,000 more able-bodied workers of all types other than in agricultural pursuits than were on the averaged employed in the year 1938.

I am inserting that estimate in the record simply because it bears upon the possibilities of the results that might be encouraged through incentive taxation.

I should like also to present for the record a letter from P. W. Horner, chairman of the National Council of Independent Unions, dated December 7, 1938, whose headquarters are in Canton, Ohio. He refers to the fact that the labor spokesmen of the American Federation of Labor and the C. I. O. have been somewhat critical of profit sharing, and he asks that in behalf of his so-called National Council of Independent Unions, the records indicate that his membership is completely in favor of the principle of profit sharing. I will ask that this go into the record.

Senator HERRING. Without objection, it will be included in the record.

(The letter is as follows:)

NATIONAL COUNCIL OF INDEPENDENT UNIONS

DECEMBER 7, 1938.

Senator ARTHUR H. VANDENBERG,
Subcommittee on Profit Sharing of Senate Finance Committee, Senate Office Building, Washington, D. C.

DEAR SENATOR VANDENBERG: As chairman of the National Council of Independent Unions I would like to make known to your committee and to have incorporated in the record my views of the general idea of profit sharing by industry. It seems to me that the principle is sound. Any device which works to provide a more equitable division of the wealth created by industry is good. Any device which fosters harmony in industry, which lays emphasis upon those interests which are shared by the owners, the management and the employees, and which gives the workers an additional stake in the well-being of the business, is good. This is not to say that I endorse all profit-sharing plans. Nor do I mean to endorse this idea of penalty or incentive taxation. That seems to me discriminatory. But the basic idea of sharing the profits of industry with the workers, entirely apart from their normal wages, is good. Your committee is doing a real service in investigating the many plans now in operation, in bringing together in one place information which will throw light on those plans which have worked best, and in drawing attention to this method of improving the economic condition of the workers and placing the employer-employee relationship upon a sounder foundation.

The National Council of Independent Unions is devoted to the advancement of the workers themselves, rather than the advancement of the professional union leaders. Therefore, the National Council is not forced to take the narrow view that anything that is got for the workers by any action except union action is not good for them and should be opposed. The National Council of Independent Unions favors those things which improve the real condition of the workers and which promote harmony, prosperity, and jobs for all those engaged in industry.

I shall appreciate it if you will put this letter before your committee and incorporate it in the record.

Senator VANDENBERG. I also have a letter from Morris S. Tremaine, the State comptroller of the State of New York, who had expected to be a witness, but is unable to do so for personal reasons, in which Mr. Tremaine endorses the general principles of incentive taxation, and I ask that that letter go into the record.

Senator HERRING. Without objection, it will be included in the record.

(The letter is as follows:)

STATE OF NEW YORK,
DEPARTMENT OF AUDIT AND CONTROL,
Albany, December 9, 1938.

Hon. DONALD DESPAIN,
Room 317, Senate Office Building, Washington, D. C.

MY DEAR SIR: Referring to your telegram, I am very sorry that I cannot be available for the next 2 weeks—doctor's orders.

For the record, however, may I say that, in principle, I believe in incentive taxation as compared to punitive taxation.

It is my opinion that a great many of our present tax laws are punitive in nature and do tend to reduce the net money received by the Government.

There is only one real virtue and that is moderation, and tax bills that go to extremes or tax bills that retard business become dangerous and undoubtedly add to depression.

There seems to be much of merit in Mr. Hazelett's theory "incentive taxation," but it would have to be worked out by Washington experts. A man like Mr. Lovell Parker probably could adapt a good deal of the idea and it could be worked into the tax law gradually.

Of course, any revolutionary plan might create additional difficulty and cause too much of a shock.

The capital gains and loss tax, because of its extreme provisions, and because of the time of holding, unquestionably has done a great deal to retard trade. I do not believe that this tax has ever produced any net revenue, but the harm it has done has more than counterbalanced the money collected. To phrase it another way, it has retarded a great deal of business that would have paid revenues to the Government in far greater amount than the revenues actually collected under this tax. Therefore, I call it a punitive tax.

The extreme upper brackets of the income tax have tended to retard business and trading so that the net result of these high taxes is undoubtedly a drawback and hindrance to business and employment.

I feel sure this tax would produce more revenue if it were sharply modified.

All of which is respectfully submitted.

Yours very truly,

(Signed) M. S. Tremaine,
State Comptroller.

Senator Herring. We will recess until 1:30, and then hear Mr. Brown, chairman of the board of Socony-Vacuum Oil Co.

(Whereupon, at 12 noon a recess was taken until 1:30 p. m. of the same day.)

AFTERNOON SESSION

(The hearing was resumed at 1:30 p. m., pursuant to the recess.)

Senator Herring. Mr. John A. Brown, chairman of the board, Socony-Vacuum Oil Co., New York City.

As I understand it, you have an annuity system of some kind in your business. Please go ahead and tell us about your experience; give us the benefit of your advice.

STATEMENT OF JOHN A. BROWN, CHAIRMAN OF THE BOARD, SOCONY-VACUUM OIL CO., NEW YORK CITY, N. Y.

Mr. Brown. I hardly feel competent to give much advice, but I will be glad to explain what our annuity plan is, and something of our experience.

The question, as it came to me first, was in regard to profit sharing. In our view, any contribution from the earnings of a company that goes for the benefit of the members of the organization, above the regular wage scale, is a form of profit sharing. It may take a variety of forms.

In our own experience our company was incorporated in 1882 as the Standard Oil Co. of New York. It changed its name when it was combined with the Vacuum Oil Co., which was a similarly old company. So that the history of the personnel and the organization goes back quite a few years.

We have had a pension plan operating as far back as 1903, which was entirely a company-administered plan, paid for by the company and not placed in any way with insurance companies. We carried on in that way until the beginning of 1931, when there went into effect a more formal, definite type of plan, placed with the Metropolitan Life Insurance Co., and in our contract with them we made provision for funding the past service liability and carrying on in the future.

That plan is rather simple. It is a contractual plan, jointly financed by the company and the employees. A subscribing employee is eligible for normal retirement at 65 for men and 55 for women, or after 40 years of service, regardless of age.

The retirement annuity is based on 2 percent per each year of service, based on actual salary classification from year to year for service since the present plan was established, and for the past service on the basis of whatever their return was at the end of 1930 when this contractual plan went into effect.

The past service liability the company has paid for entirely. The current service, since this plan went into effect, is paid jointly, the employee contributing 3.6 percent of his salary classification, 3 percent for annuity and 0.6 percent for insurance, this being both an annuity and an insurance plan.

The company makes up the difference in the current cost which is on the average of about 4½ percent. There are various details in the plan for earlier retirements with reduced annuities, with company approval. An employee may retire on a discounted annuity at age 60 after 20 years of service, or at age 55 after 30 years of service.

We also have provision for joint and survivorship annuities where an annuitant may have a reduced payment during his life, with an annuity paid to his beneficiary or widow, for life, after his death.

The insurance feature of the plan is approximately a year's pay. It includes double indemnity in case of accidental death, total and permanent disability benefits, and benefits for dismemberments.

If an employee dies before reaching the retirement age, his beneficiary receives, in addition to the life insurance provided in the plan, a refund of all his contributions to the annuity plan. So that he doesn't lose what he has paid in, if he doesn't live to enjoy it.

If an employee leaves the company after 25 years' service, he is entitled to a paid-up, deferred annuity, payable as at his normal retirement date. That is based on both his and the company's contributions.

We have also a provision that in case of an employee dying after 20 years of service, that in addition to the ordinary insurance provided in the plan, there is an additional 2 years' wages or salary, which go to his beneficiary in addition to the other benefits, on the theory that after that many years of service, and before being able to enjoy the full fruits of the plan, something should be provided in there to take care of that kind of a situation.

I think that briefly is about all the features of the plan. We consider it a form of profit sharing.

The cost to the company, as we are going today, for the old plan that was self-administered and the past service funding which we do from year to year, and the current liability, brings us in the neighborhood of a cost of about $7,000,000 a year. That, on the basis of last year, would have been over 11 percent of our earnings. It will be a greater percent of our earnings this year because the earnings are going to be less.

Senator VANDENBERG. How does that figure compare with your distribution in dividends on stock?

Mr. BROWN. Our dividends on stock in 1937 were approximately $25,000,000. The cost of this plan was about $7,000,000.

Senator VANDENBERG. How many employees have you?

Mr. BROWN. About 35,000 in the United States.

Senator VANDENBERG. Does this plan cover them all?

Mr. BROWN. This is entirely a voluntary plan. It covers all who wish to participate.

Senator VANDENBERG. And that is how many?

Mr. BROWN. About 92 percent.

Senator HERRING. In 1937 it shows $6,747,000, or about 11.8 percent of the net profits?

Mr. BROWN. Approximately; yes; that is the figure. I was just quoting from my memory.

Senator HERRING. Unemployment-insurance and old-age payments were $2,168,000, or nearly 4 percent of the net profits.

Mr. BROWN. Yes.

Senator VANDENBERG. What is your experience as to the employee reaction? Do you consider that this is helpful in establishing loyalty and efficiency?

Mr. BROWN. We think that it is helpful; yes. To what degree one would find it difficult to say. The fact that 92 percent of the employees are in it, entirely voluntarily, contributing part of their pay to the plan, I think is fairly conclusive evidence that they like it and that it means something important to them.

Senator VANDENBERG. Probably neither they nor you would want to give it up?

Mr. BROWN. No, we would not want to give it up, and I am quite sure the employees would not.

Senator HERRING. There has never been any question, Mr. Brown, but what the base wage was as high as any other company is paying for similar service, before these special benefits were given to the employees?

Mr. BROWN. No plan, either our old plan or the present plan, has in any way had any bearing on the question of what a proper wage remuneration was. They go along on their own basis and own merits, and I believe they are at least as good as any in our industry.

Senator VANDENBERG. Didn't you inaugurate a new so-called 20-year survival plan in 1936, which is in addition to what you have reported to the committee?

Mr. BROWN. I think I referred to that when I was speaking. That is the plan whereby, after 20 years of service, there is an additional 2 years' salary or wage benefit provided, if a person does not live to enjoy the annuity.

Senator VANDENBERG. Have you any thought on the subject of incentive taxation in any of these connections, Mr. Brown?

Mr. BROWN. I perhaps got a little misunderstanding of what I was going to be asked to speak about. I was thinking of incentive taxation in respect to such things as encouraging profit-sharing plans. And on that, my mind naturally went to the thought that they might better be left to the different employers, and industries, to work out according to their own disposition and wishes of the stockholders and the character of their business, and its varied success.

Incentive taxation, in its broader phase, for the encouragement of employment, is quite another matter, and unemployment being our most serious problem, I would certainly not want to say that I would be opposed in principle to anything that could be devised to improve employment in private industry.

Senator VANDENBERG. Well, you have had a very large and broad business experience and responsibility, Mr. Brown; would it not appeal to your business sense that a series of tax exemptions or tax rewards for plant expansion, plant replacements, regularization of employment, and so forth, that such encouragements would be well calculated to stimulate these methods of essential attack upon unemployment?

Mr. BROWN. I think they undoubtedly would. It is a question of each particular industry trying to answer that question as to degree.

Senator VANDENBERG. Well, we quite concur in your thought that no standard formula of profit sharing, direct or indirect, can be dictated from one central point to the ramifying, complex business of this country, but incentive taxation, it seems to me, might be offered by way of option to the employer who voluntarily does participate in this sort of thing, without any necessity for attempting to standardize on a national formula.

Do you think that there is a great retardment during the last few years, in America, of plant maintenance, up to a degree of maximum efficiency in industry?

Mr. BROWN. I don't think I should take it upon myself to answer that question with respect to industries other than our own.

In our industry I don't think that that has been such an important factor because we have not suffered such a great decline in the volume of our business during these years. The oil industry has gone on with a moderate decline in its total volume, and a coming back of part of it in its main products. It has a constantly shifting source of supply. Competition is keen, technological improvements are on the way all the time, and companies have, perforce, been more or less obliged to keep going along on those things which they, of course, would not have been able to do if the volume had gone way off and they couldn't operate.

Senator HERRING. The transition from the use of coal to oil and Diesel engines, and so forth, has helped somewhat, has it not?

Mr. BROWN. The growth in volume of heating oil for household has been quite a feature of the past few years, but of course the consumption of gasoline, for example, has kept up in great volume and kept us going.

Senator VANDENBERG. Have you any figures showing how much has actually been paid out to employees under your annuity plan?

Mr. BROWN. How much has been actually paid out? I don't think, back through all the years, that I have any figures available. I think I have some figures here. The amount paid out by the company, part of which went to the insurance company for refunding past service liability, and part for current service, and part going out in pensions and insurance, in this experience of 7 years we have paid out some $58,000,000 in this plan; that is, the combination of plans.

Senator HERRING. Well, unless you have something else you would like to put into the record, or some suggestion you want to give, Mr. Brown, I think that is everything.

We appreciate your coming.

Senator VANDENBERG. Thank you very much, Mr. Brown, we are much obliged.

STATEMENT OF ALLEN W. RUCKER, PRESIDENT, THE EDDY-RUCKER-NICKELS CO., CAMBRIDGE, MASS.

Senator HERRING. Mr. Allen W. Rucker, economist, writer and author of Labor's Road to Plenty, of Cambridge, Mass.

Mr. RUCKER. How do you do, sir?

I am going to read to you gentlemen a prepared statement, but if you would like to ask any questions at any point, please do not hesitate to do so, and I don't think it will make any great difference in the context.

Senator VANDENBERG. I have heard it said that this new book of yours is the best thing on the subject in 20 years. Do you agree with that?

Mr. RUCKER. I would hesitate to do that, offhand. Perhaps modesty might prevent me. But possibly it is one of the few in which we are looking at the manufacturing economy as a unit rather than as a collection of parts, and I will ask you, when you listen to this particular statement and in asking your questions, to realize that we are taking a perspective or telescopic view rather than a microscopic view in this case.

Your committee, through its director of survey, extended me an invitation to appear here chiefly, I think, because our studies of the end-results of the operation of the manufacturing industry as a whole, offer some definite suggestions whereby government and individual business management may encourage an improvement in the relations between employer and employee, an increase in industrial production, a wider distribution of that production among wage earners and consumers.

These studies of what actually has happened in our economy are based wholly upon the records of the Biennial Census of Manufacturers, the Bureau of Labor Statistics, and the Income Tax Division of the Treasury Department, supplemented by audited reports of individual firms. As much of the data and all of the detailed study have been reported in a book, Labor's Road to Plenty, under the subtitle, "The Return of the American System of Productivity," I shall not particularize them here. The following summary will indicate their nature, and I shall be glad to answer questions which arise from this description of the conditions found and the employee compensation plan suggested by them, as that plan is currently being applied.

I should like to suggest to your committee that the seeds of industrial unrest were probably sown during the years 1923 to 1927. The harvest reaped in the past 5 years, 1933 to 1937, inclusive, justifies a brief summary because it points directly toward one basic industrial shortcoming which has not heretofore been given attention. In the past 5 years, according to the records of the Bureau of Labor Statistics, there have been something over 12,000 labor disputes and strikes; these disputes involved 6,469,331 employees and occasioned the loss of 96,005,400 man-days of work.

In from 55 percent to 65 percent of such disputes, the percentage varying somewhat from year to year, and in the case of from 65 percent to 75 percent of the employees concerned, the major issue was wages and hours of factory labor.

I do not think it farfetched to conclude that when such a high percentage of total disputes and total workers involved concerns the compensation problem there is very definite evidence that business management has not yet developed a fundamental principle of group compensation. And that neither labor leadership nor government has yet contributed anything material to such a development.

As yet, relatively few seem to appreciate that unless a constructive working principle of compensation is devised by industry generally the next depression almost certainly will see the Federal Government in full control of industry. It matters little that a Fascistic social control will serve only to do what it has done to nearly every important nation abroad, bring us to financial or social bankruptcy, or both. Unless business management can advance and establish a fundamental principle of labor relations which will win public support, that development seems almost inevitable. We have been tending in that direction since the Federal Reserve Board undertook in 1921 to stabilize the general price level and the Federal Government in the same period undertook the regulation of wage rates and working hours of railway employees. Ever since we have proceeded apace along the path leading to regulation of labor policies in all industries, each legislative move resulting in new failures that created new problems seemingly requiring new regulation and a new extension of Federal power. The resultant symptoms of large-scale unemployment, widespread labor disputes, and cessation of our long-term economic progress are all too plain in their meaning. The threat of a coming fascistic control of industry is a very real one.

I am convinced, in common with other observers, that the crux of this matter lies in the development of a rigid price economy born of an inflexible cost level arising in part from arbitrary determination of wage rates and working hours. And I think that growth of arbitrary practices is traceable to our failure to develop a fundamental principle of labor compensation which will make our capitalism intelligently democratic and our democracy intelligently capitalistic.

This absence of a fundamental principle of compensation appears to be due to a general failure to realize that labor's compensation involves both individual and group income. Our studies strongly suggest that satisfactory adjustment of compensation differences before they arise requires a dual and not a single-phased compensation plan, viz:

1. A method whereby individual skill and merit may be rewarded in proportion to individual skill and merit; and

2. An allied principle whereby factory labor as a group, that is collectively, may be assured a group income in keeping with its contribution to industrial income.

The first of these two requirements is well served by the differential wage rate, hourly, piece, or daily. Through this device, a machinist may be paid $1.50 an hour as contrasted to, say the 80 cents an hour paid a truck driver. The difference in the value of men on the same job, or different jobs, is thus expressed by a compensation differential. The differential wage rate is one of civilization's great inventions; it enables management to reward individuals according to their relative skill and merit and to do so without impairing the earnings of fellow-workers. Even though its application can still be improved, the principle of the differential wage rate takes first rank among industry's great accomplishments.

Any attempt, however, to use this remarkable device as a means of enlarging the total collective or group income of factory labor is almost certain to be disappointing or even disastrous in its results. A few brief illustrations:

Average hourly wage rates in industry increased 10 percent between 1923 and 1929; the total income of factory labor, yearly, with adjustments for the number of persons employed, increased about 5 percent; between 1929 and 1933, average hourly rates declined about 20 percent only, whereas annual income declined some 34 percent; between 1933 and 1937, average hourly wage rates were increased 41 percent whereas incomes rose only 21 percent in round figures.

This 15-year movement was accompanied by an increasing rate of decline in job opportunity in industry as a whole, suggesting that the rate of increase in wage rates was in excess of that justified by increased productivity—and probably that even the slight gains in the average income of employed workers were made at the expense of those disemployed.

Evidence that the wage-rate device cannot safely be used—through an arbitrary increase in the average level of rates—to expand the total income of factory labor, is strengthened by the fact that in individual instances coming under my observation, the result is equally as unfortunate:

In one firm, the 1936 average annual income of identical employees was $1,226.72; wage rates were then increased 15 percent for the year 1937; but annual incomes became only $12 higher, or $1,234.13, just short of 1 percent increase.

In a second firm, average annual incomes were $1,245 for 1936; in 1937, after a wage rate increase of 10 percent, average incomes were only $1,236, a shrinkage of $9, or about 1 percent.

Such misuse of the wage rate in an effort to enlarge annual incomes is often carried to ridiculous extremes, creating intense antagonism and distrust. For instance, repeatedly in 1937, we noted press reports of wage disputes settled by a 10 percent increase in rates and a reduction of hours from 48 to 40 per week. Without considering the effect on annual income, you will perceive at once that the 16 percent reduction in weekly hours requires a 20 percent increase in hourly rates, simply to maintain the weekly pay at the former level. The mere 10 percent increase in rates leaves the employee worse off than before; and he not unnaturally feels that he has been betrayed.

Senator VANDENBERG. And that calculation takes no account the increased cost of living and the decreased buying power of the dollar involved?

Mr. RUCKER. Not at all, Senator, that is purely in current dollars. It would require a 20-percent increase in wage rates to offset a 16-percent reduction in hours, and of course there are corresponding percentages for any other hours that might be used as an illustration.

Senator VANDENBERG. Then there is the added factor, is there not——

Mr. RUCKER (interposing). Without a doubt. I am going to have a little something to say on that score just shortly.

That such results are rather widespread is indicated by the facts previously cited, showing that average annual incomes of factory labor do not show increases proportionate to increases in wage rates and by the steady increase in wage disputes. That such results persist seems rather definite evidence that management, labor, and government have all been remiss in failing to develop a fundamental principle of group labor compensation, one which would determine more or less scientifically the proportionate economic share of industrial income due to factory labor collectively, just as the differential wage rate determines the relative compensation of individuals.

The cumulative consequences of the lack of such a principle are today everywhere visible; they are perhaps our most fertile source of distrust, suspicion, and unrest. Labor, led to expect a larger income from higher wage rates, and receiving in fact little more, and often less, naturally feels that its only recourse is a demand for still further increases. And any resistance is often construed as a desire on the part of management to defraud the wage earner. Management, on the other hand, realizes that even though increases in the level of wage rates do not appear in labor's income, they do appear in production costs and prices, making those costs relatively high and rigid; in consequence, as prices exceed the purchasing power of buyers and costs cannot promptly be adjusted to the ebb and flow of that purchasing power, the annual total of saleable production values tends to shrink. That means a reduction in the income of both labor and capital and consequent bitterness on both sides.

Senator VANDENBERG. And also reduces the national income for the year?

Mr. RUCKER. Correspondingly.

Here in those conditions is what our study shows to be a compelling demonstration of the unfortunate results of neglect to find a fundamental principle of group compensation.

The situation today in industry generally has become, as you know, one closely resembling two opposing camps, both peacefully inclined but deeply fearful of one another. Labor fears that management may arbitrarily reduce wage rates in times of stress or fail to raise them in times of prosperity; management fears that labor may arbitrarily demand rigid wage maintenance or wage-rate increases at just the time when market conditions require flexibility of costs and prices. Where either labor or management has the power to change wage rates without some economic "governor" automatically coming visibly into play, that power soon appears arbitrary by whomsoever exercised.

I do not think we can substantially improve industrial labor relations until we remove the question of wages and incomes from the influence of arbitrary changes at the hands of either employees or employers. And in that way remove the basis for fear of injustice to one party at the hands of the other. That means a fundamental principle of group compensation distinct from the principle of differential compensation for individuals.

Before going into this matter of group compensation more fully, I should like to say that I believe such a principle can and should be developed by management. As things now stand every change in wage rates made by management is too readily interpreted as a wage increase unwillingly conceded or a wage reduction unjustly enforced. For the want of a principle by which to make clear the economic fairness of wage changes management is accused and condemned for arbitrary practices; and, on the other hand, labor for want of just such a principle to justify its position, is as heartily condemned by management for the arbitrary demands which it makes. If management can advance a principle which will remove wage changes, and the total compensation of labor from the realm of arbitrary action, it will automatically remove the reason for much of the mutual fear and distrust now prevailing. And management can find such a principle and apply it quite readily.

From our studies of the end results of industrial operations, I do not feel that profit sharing as the term is usually defined will provide such means of group compensation, insofar as industry generally is concerned. There are, of course, exceptions among individual concerns. Our studies, however, point out more comprehensive principles. Before I can describe it and how it has been applied, I perhaps ought to say now why I feel that profit sharing is not an adequate solution insofar as the majority of employees and employers are concerned. The reasons are chiefly two, as they concern manufacturing industry:

1. The percentage of active manufacturing corporations actually earning a profit is far too low, and has been too low, to encourage confidence in the adequacy of profit sharing. It is not generally appreciated that in 1923 only 63.1 percent of active corporations earned any taxable profit whatever; by 1929 that percentage had fallen to 57.5 percent; in 1932 it was 16.3 percent; by 1933 it was 28.1 percent. Even in 1935 the percentage of profitable corporations to total active was only 41.4 percent, and in 1936 the profitable ones were fractionally over 49 percent of those active. It is evident that even in the best of times the number of wage earners who would share in profits would be limited.

The limitation would be greater than these figures suggest, inasmuch as less than 50 percent of those firms making a profit make more than $10,000 net annually.

2. The second deficiency of profit sharing, which our studies indicate, is that such a move might, in the aggregate, though there would be individual exceptions, actually operate to create new unemployment. Briefly, our studies show that total job opportunity in manufacturing year by year rises and falls with the number of going concerns, and these, in turn, with the number of profitable concerns; that is, with the chance to earn a profit. That fact appears to show that any further prospect of a drain upon net profits directly might well make many operations so unattractive to capital as to result in a severe shrinkage in the number of going concerns. The importance

of the number of going concerns to the relative plenty or scarcity of employment opportunity has never been appreciated. I think your committee should be apprised of the fact that the greater part of the loss of factory-employment opportunity between 1929 and 1933, and the failure of employment to recover, has been accompanied, if not caused by, the enormous shrinkage in the number of going concerns, and the failure of the subsequent recovery to restore the losses. For instance:

Between 1929 and 1933 the number of going concerns declined by 68,000, or 32.4 percent—the number of job opportunities by 2,800,000, or 31.2 percent.

If I may do so, I should like to emphasize that there has been virtually no change in the average number of jobs per going factory throughout the period 1923 to 1935, inclusive. The official records of the Bureau of the Census, Census of Manufacturers, shows the following average jobs given per going firm for pivotal years:

Jobs per going business:	
1923	44.8
1929	42.0
1933	42.5
1935	43.7

Of course, these figures must not be confused with total work per going business. Total work given is best measured by total man-hours of labor provided. In that there has, of course, been an enormous change. I can give the committee our data in this respect, if desired. But there is virtually no change in the average employment opportunity or jobs per going firm. Hence, the number of persons getting some work is seemingly closely related to the number of going businesses. That is why I think it is important that nothing be done to reduce the percentage probability of earning a profit in manufacturing; to do so may result in a shrinkage in the number of going concerns and total employment opportunity, or, as apparently occurred in the 1933–37 period, a failure of the number of going concerns to expand any faster than the chances of earning a profit, thereby limiting employment opportunity quite seriously.

For these two reasons, it may be that profit sharing generally will be unattractive to both labor and management; and if attempted on a broad scale, might conceivably be harmful to the interests of both.

Senator VANDENBERG. Before you leave that comment, returning to the bottom of the previous page, you say that it is important that nothing be done to reduce the percentage probability of earning a profit in manufacturing, inviting the inference that a profit-sharing plan would reduce the percentage probability of earning a profit.

Mr. RUCKER. I don't mean to give that inference at all, Senator. The difficulty, I imagine, would be that a good many people would suppose—I am speaking now of management—that if they must take some of their profits and pay them to labor as a part of profit sharing it would reduce the incentive to go into business. As you know, we have today all sorts of charges on profits, and an additional one might be harmful.

Senator VANDENBERG. I can fully understand your point expressed in that language, but I don't believe you mean that profit sharing would reduce the percentage probability of earning a profit.

Mr. RUCKER. I think you are quite right; I don't mean that, and the wording is certainly ambiguous at that point.

Senator HERRING. In addition to that, I note you say that therefore the situation in 1923 and 1924 was so and so. We have evidence here from one concern that in 1919, up to 1923, they were losing money and put in a profit-sharing plan, and they have been making better than a million dollars a year ever since. So possibly putting in profit sharing didn't have that effect on them.

Mr. RUCKER. I think if they have an incentive plan which might be termed profit sharing or otherwise—and I want to stress that later—but the incentive plan I am heartily in accord with. I am thinking of profits in the narrow accounting sense as the term is likely to be interpreted by management.

Senator HERRING. Then you have given some thought to profit sharing as a producer of profits; that it might rescue business?

Mr. RUCKER. As an incentive, yes, sir; and the difficulty has been that in applying it in such a way, and getting around some of the inhibitions perhaps that management and labor both have, I am going to give you a little bit later a somewhat broader principle which might not be subject to some of those limitations.

Senator HERRING. Fine.

Mr. RUCKER. On the other hand, our studies do indicate that there is a principle of group compensation which will enable labor collectively automatically to share in any expanding prosperity and be protected in any period of adversity. As far as we can judge, this principle is open to none of the objections which can be raised against sharing of net profits; and, equally or more important, it is not susceptible to arbitrary influence by either labor or management.

From our study of the end results of industrial operation, all of which studies have been based upon either the official records of the Bureau of the Census or the audited operating statements of individual firms, it appears that there is one factor which determines the aggregate yearly income of factory labor. That factor is the total sales value of factory processing as distinguishable from either product values or business profits. This total of processing sales values is definitely known for industry as a whole, and for separate industries: it is described by the Census of Manufactures as "value added to raw materials" by manufacturing process. It represents, as you know, total product sales values less the cost of raw materials, containers, purchased power, and supplies. It is, in other words, the sales value of factory productive effort added to the cost of raw materials.

Now, the remarkable fact unearthed by our study is that the percentage of yearly pay rolls to the total of values added by manufacture, that is to total productive sales values, tends to be relatively constant year after year. That percentage differs, of course, among the various industries and firms according to the nature of the product, productive efficiency, marketing customers, and local conditions. For the most part, though, there are exceptions. The percentage in successive years tends to fluctuate within narrow limits around a 5-year average. The result is that total pay rolls, that is the collective or group income of labor in each industry and firm, rises and falls almost directly with the yearly dollar total of productive sales values, regardless of the level of wage rates or corporate net earnings. Labor as a whole is literally paid proportionate to salable productive effort.

It is of interest, and a significant empirical fact, that this remarkable relationship is maintained for manufacturing industry as a whole at almost the same percentage for a long period of years. The national averages are informative and I give them:

All manufacturing industries

[Source: U. S. Census of Manufactures]

	Productive sales values, i. e. value added	Total factory pay rolls[1]	Percent pay rolls to productive values		Productive sales values, i. e. value added	Total factory pay rolls[1]	Percent pay rolls to productive values
	Billion	*Billion*			*Billion*	*Billion*	
1929	$31.89	$11.61	36.4	1933	$14.54	$5.26	36.2
1931	19.33	7.17	37.0	1935[2]	20.83	7.54	36.2

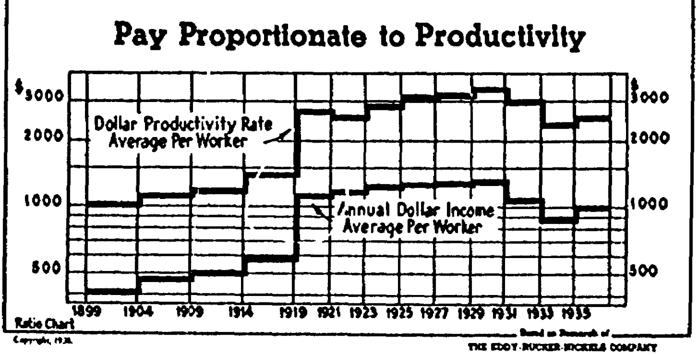
[1] Exclusive of compensation of supervisory, clerical, and executive employees.

[2] The raw data show a slightly different figure, due to the fact that in 1935 the census excluded "supplies" as one of deductions from product values. The figure in this table has been adjusted to make it comparable to preceding years when "supplies" were deducted from product values in computing value added by manufacture.

This rise and fall in the total income of labor with the rise and fall in total marketable productive values, has been the real fundamental factor determining the collective dollar income of labor. When we examine the record of separate industries, the identical result appears: total pay rolls tend to go up and down, more or less directly with total salable output values. And again, in examining the record of individual firms a similar result is apparent.

In brief, regardless of what anyone does, the total income of labor—exclusive of course of supervisory, clerical, and executive salaries—is only that permitted by total marketable output values.

To supplement the foregoing I am appending to this statement a chart showing average annual salable productive value per worker and income per worker for all manufacturing for the 35-year period 1899 to 1935, inclusive.



That chart is a ratio chart in order that the percentage changes may be shown, which wouldn't be possible with the straight arithmetical chart.

It is significant that in 1923, when wage rates were relatively low as compared to those now prevailing, and profit probabilities were relatively high, the aggregate dollar income of labor and the average annual income per wage earner were both higher than today. That is true, though now the situation is reversed and wage rates are relatively high and profit probabilities are relatively low. It is highly significant that the changes in labor's income are determined, seemingly entirely, by changes in the annual total or productive sales values.

This appears strongly to suggest that there is nothing economically arbitrary about the collective income of factory labor; it rises and falls in dollars quite constantly with the rise and fall of productive sales values, for industry as a whole and, for the most part, for individual firms.

Our studies thus point out that a nonarbitrary principle of group labor income can be developed and made to improve the relations between employer and employee by diminishing wage disputes. Specifically, perhaps the greatest single contribution which management might make today would be to take the initiative in doing two things:

1. Demonstrating to employees, forcefully and factually, that the total pay roll of the firm is dependent upon the yearly total of productive sales values, and hence that it is to the joint interest of employees and management to cooperate in making that total the highest possible.

2. And then give significance to the fact by guaranteeing employees that in return for full cooperation, they as a group will receive a fixed percentage of total productive sales values, the percentage being that determined by the preceding 5-year average of the individual firm.

Such a move would give every employee an immediate and direct interest not only in the profits of the firm but in the production of goods. An assured percentage share of production for labor as a group means an automatic increase in income with every dollar of increase in the firm's productive sales values, whether that increase arises from price inflation, expanding physical volume of sales, prevention of waste of materials, increased labor and machinery efficiency, or the reduction of "seconds" and "rejects" in the factory. Labor's interest becomes identical with that of management.

I can perhaps best illustrate the operation of the principle of group compensation by showing how it is applied in an actual case, that of a New England manufacturer.

In the instance in point, the firm's operating records showed the 5-year average of pay rolls to productive values to be 34.79 percent. This average represents the firm's experience over a business cycle, good times and bad alike. For convenience, the management has decided to pay an even 35 percent of productive sales values as labor's group income. Clerical, supervisory, and executive salaried employees are not included. In addition, the management has decided, though it is not necessary to the operation of the share of production plan, to pay an equalized weekly advance wage in order to even out the seasonal fluctuation in the income of its employees. The weekly advance wage is individually determined according to the job evaluation and the efficiency of each employee. In other words, the differential wage rate principle comes into play in determining the individual's compensation. The total of all weekly pay-roll disbursements is debited to a share of production ledger account.

This account is credited each month with 35 percent of the month's productive sales values; that is, the value added by manufacture to raw materials. Each $100,000 of such values produces a credit of $35,000 to the share of production fund. Employees will know each month how the fund stands. At the end of each 6 months' period, the fund is balanced and the excess over weekly wage disbursements is paid pro rata to qualified employees. Put another way, actual wages are adjusted each 6 months to bring the aggregate total up to 35 percent of the period's productive sales values.

Your committee will be quick to appreciate that each employee will have a direct personal interest in enlarging the total of productive sales values, an interest that can be translated into active personal effort. For instance:

Every hundred dollars saved by avoiding the waste of raw materials, containers, power, and supplies means an additional $35 for the share of production wage fund. Every reduction in losses due to factory damaged goods, "rejects" and "seconds," results in a credit of 35 percent of the saving to the fund. Any increase in the volume of sales directly has the same effect. Should prices be advanced to consumers, labor as a group is automatically advanced in income, and to exactly the same proportion. In any and every way by which the dollar total of productive sales values is enlarged, labor's group income is correspondingly enlarged. Increases in machine, process, or labor efficiency all react to labor's immediate benefit. The share of production principle thus gives labor a more concrete and direct interest in industry than might be possible under the more limited profit-sharing principle.

Senator VANDENBERG. In a broad sense, it is a profit-sharing principle?

Mr. RUCKER. Of course it is, because it operates whether or not there are profits, and of course it would come out of profits before there would be any available to the stockholders.

Senator VANDENBERG. Are you familiar with the Westinghouse plan?

Mr. RUCKER. Only partially, and not well enough to discuss it.

Senator VANDENBERG. It would seem that it contains something of the same principle, with a different index.

Mr. RUCKER. It approaches it; yes, sir. I believe that plan is geared to the price structure, is it not?

Senator VANDENBERG. It is geared to the net earnings.

Mr. RUCKER. In this particular application, as would be the case in all instances, labor's collective income is removed from the arbitrary determination of wage rates. Under this plan, the level of wage rates is comparatively unimportant so long as differentials are maintained. The wage-rate level can thus be allowed to flex up and down in order that unit production costs and prices may adjust themselves to the ebb and flow of consumer purchasing power.

It perhaps is unnecessary to summarize the economic and commercial advantages of this plan at greater length. If such a summary appears desirable for the committee's records, I suggest that the committee's record include the summary contained in pages 190–192 of Labor's Road to Plenty. Meanwhile, it is perhaps more pertinent to point out that the share of production plan offers for many firms, and perhaps most, the means of accomplishing two ends in which your committee is especially interested:

1. It establishes a nonarbitrary basis for determining the collective or group income of factory wage earners, which will automatically distribute the fruits of industrial effort to those who create them, according the fair economic share to each.

2. It removes the level of wage rates from the arbitrary realm of "rule of the thumb" compromise or coercion on the part of anyone. When labor collectively receives its economic share of productive sales values, it makes no difference what the level of wage rates is; dollar income proportionate to production is assured.

Under such an arrangement, I think it conservative to say that, with due study and education on the part of all concerned, it will speedily become appreciated that management is assuring employees by this plan that no changes in the level of wage rates will be made which will have the effect of causing the percentage of yearly pay rolls to productive sales values to become less than the preceding 5- or 7-year average for the concern, and that any changes necessitated will preserve the relative compensation differentials between individuals. And, in turn, labor is assuring management that it will make no demands for changes in the level of wage rates which will have the effect of raising the specified percentage share of productive values, or which might so affect costs and prices to the consumer as to cause a diminution of demand and a consequent shrinkage of productive values and employment.

With such mutual assurances, there is reason to believe that in time the wage-rate level will be eliminated as a major source of industrial disputes. The differential wage rate would simply be confined to its proper sphere of determining the relative compensation of individuals according to skill and merit. Industrial management would supplement the principle of individual compensation with a principle of group compensation, an assured percentage or share of production values regardless of business conditions.

There is reason to feel that by these twin principles of compensation we can remove the collective income of labor from both the arbitrary determination of the wage-rate level and the uncertainties of business profits. As I have previously said, our studies of what has actually happened in industry point out that the great deficiency now is the lack of a fundamental principle of group compensation. The share-of-production plan provides that principle.

With due appreciation for the time required for recognition of the need and the value of a principle of group compensation, and with full realization of the technical difficulties to be overcome in individual application, I nonetheless feel it conservative to say that the twin principles of group and individual compensation together will do much to make capitalism intelligently democratic and democracy intelligently capitalistic.

For many and perhaps the majority of the firms, this can bring about in time a rebirth of confidence between employee and employer, the stimulation of the productive effort of labor and the generation of new encouragement to management to go ahead once more in the American way.

Those things we must have if we are to avoid the coming of fascism in this country. We can have them by widely applying a fundamental principle of compensation that rewards labor collectively in proportion to its contribution to the general industrial output.

Adapted to individual enterprises and soundly presented by management to labor and the public, this principle offers the means of restoring to private business the confidence of employees and the freedom of initiative it must have if the American system is to continue.

That is all of that statement, sir.

Senator VANDENBERG. What would organized labor say to the share of production plan?

Mr. RUCKER. I should say that the C. I. O. and perhaps also the A. F. of L. would oppose it. Now, that, of course, is purely an opinion, Senator, and is not based on any information which I have.

Senator VANDENBERG. Have you given any thought to incentive taxation in connection with this theme? Is there any way that the tax power could be used to encourage this regularization of the relationship between capital and labor?

Mr. RUCKER. The thought which I have given to it does not enable me to think how, directly, it can be done. Undoubtedly there should be a connection, there is between all things in economy, but its direct connection isn't apparent, and I haven't studied it enough to know just where it would come in.

Senator VANDENBERG. Of course, even under your theory of sharing production, the final and fundamental thing is to increase the production?

Mr. RUCKER. That is right.

Senator VANDENBERG. And anything that increases the production encourages the validity and success of your plan?

Mr. RUCKER. Correct.

Senator VANDENBERG. Well, isn't it quite obvious that in the field of plant equipment and plant expansion there is great need for a very great increase in productivity?

Mr. RUCKER. Without any question, or in gross production as well.

Senator VANDENBERG. Yes; and why isn't it logical to contemplate that tax rewards, compensatory tax allowances, would stimulate that sort of productivity?

Mr. RUCKER. I think unquestionably that would be an encouragement to management in this respect. In a good many businesses—and particularly those just on the border line between profits or relatively minor profits—they must allow cash for the payment of taxes, and frequently that cash represents a very sizable reduction in the available liquid resources of the concern. Now, I can tell you of a good many instances when, as management counsel, as I am, I have been compelled to recommend that no expansion or moves in that direction be made, in order to conserve cash so that taxes might be met.

I can tell you that between income taxes, which are for so many concerns not particularly serious, but local taxes, real-estate taxes and the like, and Social Security taxes, that is a severe burden on the liquid resources of a concern. If you were to look over a group of balance sheets you would see that very few concerns, considering the aggregate, have sufficient cash to pay all of their outstanding current liabilities. The exception will, of course, but comparatively few of the rank and file will, and those are the people whom in the aggregate can contribute very materially to an expansion of production and productivity, if they are given an incentive in that direction.

THE EDDY-RUCKER-NICKELS CO.,
Cambridge, Mass., December 13, 1938.

HON. ARTHUR H. VANDENBERG,
Senate Office Building, Washington, D. C.

DEAR SENATOR VANDENBERG: May I supplement my testimony of yesterday with reference to tax incentives by these two suggestions?

First, it may prove feasible, and I believe it would prove most welcome to business, if under a new law corporations might set up a reserve account against which could be debited losses on inventories in the years in which they occur, with credit for inventory gains in the years in which such gains occur, the inventory gains to be free of taxation. It has been my experience over the past 15 years that the current level of profits is either unduly inflated by inventory gains due to rises in raw materials and the like and, conversely, in times of adversity unduly deflated by inventory losses. If a formula could be found for permitting corporations to throw such gains and losses into a special reserve account, which would be untaxed within a reasonable period of years; that is, the reserve account's net credit balance might rise to a certain proportion of total assets before a tax would apply on such additions to the account due to inventory gains, I think it would be constructive.

My second suggestion is that in allowances for depreciation it is now customary to deduct depreciation on plant equipment an equal percentage amount year by year. I believe that it would be useful to permit business to charge off depreciation at so much per unit of products. The effect of this would be to level off some of the peaks and valleys in the tax income of the Government and also to restrict the fluctuation of the profits of individual firms.

The second of these suggestions would be a definite incentive for corporations to increase the physical volume of output in each year, inasmuch as that would permit a larger deduction for depreciation. Many corporations, particularly in times of depression, might thus be encouraged to offer their products at lower prices than they otherwise might do simply because the larger volume would permit some price concession to be made up in depreciation deductions. Inasmuch as total man-hours of employment vary almost directly at any given level of efficiency with the physical units of production rather than their dollar value, the move would be constructive from that viewpoint.

I offer these suggestions in the hope that they may prove useful to your committee.

Let me thank you for the courteous and friendly hearing yesterday and to say again that I feel privileged to have had an opportunity to take a part in the splendid effort which your committee is making.

Cordially yours,

A. W. RUCKER.

Senator HERRING. I am still interested in your observation as to those 2 or 3 years when 64 percent of the corporations made no profits. We have had several witnesses here that went through that period when their competitors had no profits. These concerns happened to have had a profit-sharing plan and they didn't hesitate to state that they thought that one of the principal reasons why they continued and made profits was the fact that they had this loyal support of their employees, they had these efficiencies and economies which they thought were in no small part due to the fact that they had a profit-sharing system.

Mr. RUCKER. And I think they were probably right in that respect. I know of one concern particularly, in which a profit-sharing plan has been in operation since 1901, which makes it one of the oldest in the country so far as businesses now in existence are concerned. And they had, while some bad years, they feel that that has contributed a great deal to the stability, the good will, and the mutual confidence between themselves and their employees. They would tell you, I think if they were careful, that that had been a contribution to their profits, but not the sole cause.

Senator HERRING. I think that is true.

Mr. RUCKER. And that probably would be the case in other instances, I should say, from what I know of those things.

Senator HERRING. I think that is all, Mr. Rucker, unless you have something else you wish to put into the record.

Mr. RUCKER. No, sir; except that I wish to put into the record a copy of my book.

Senator HERRING. I wish you would tell me where I can buy a copy—I tried all over Chicago to get one.

Mr. RUCKER. I would be happy to send you a copy.

Senator HERRING. That is what I was leading up to. [Laughter.]

Mr. RUCKER. I will leave this copy for the record.

There is one other fact that possibly, on second thought, might be included in your record. That is the fact, a rather peculiar one in our economy, that the total of industrial pay rolls has steadily since 1921 maintained a 1-to-1 ratio with gross farm income. Now, as to which is the hen and which is the egg I am not prepared to say, but I want to call attention to that fact. We ran on it, I think, originally—but it doesn't matter—some years ago, and I waited for some time before basing any public predictions on what would be the outcome. But as far ago as in the fall of 1936, it was evident that we were going to have a decline in aggregate farm income. I tentatively, at the time, put the period as possibly 1937, and almost certainly 1938. I won't go into the reasoning back of it. And I predicted that factory pay rolls would come down to the same percentage and degree.

Of course, that is what has occurred. Now this is not from a matter of my ability as a prophet, and I disclaim any ability in that direction, but merely to point out that apparently those two fundamentals are tied together and they go up and down together.

Now, the significance of it is that our assumptions that we can expand the total dollar income of labor are simply assumptions. If that total is restricted or limited by some other economic factor, maybe farm income or it may be the factor which limits both, it means that we can raise wage rates to $2 an hour, if we wish, but the income will be no more.

Now, it apparently has worked that way. It is interesting to note that the relationship has persisted since 1849, though not always in the same ratio, but the changes in the ratio are very slow and comparatively minor from year to year. So apparently we cannot arbitrarily expand anyone's dollar income insofar as factory labor is concerned.

Senator HERRING. Have you found that labor income of the factory precedes farm income, or is it the other way? They follow each other, do they not?

Mr. RUCKER. They go so closely hand in glove that it would be hard to say whether there was a lag in one or the other, and which one would be behind. Of course, you realize that our division of periods into a calendar year is purely arbitrary, and we couldn't say that economic forces would adjust themselves at once to that sort of measuring. But say from 1921 down to 1935, if you total the cumulative total of both incomes, there is less than 5 percent difference between the two, and year after year the differences are very minor.

Senator HERRING. I was interested in your observation as to the action of the Federal Reserve Board in 1921, because that was very definite in the agricultural sections of the country.

Mr. RUCKER. Yes. Of course there was some sporadic attempt prior to that time. I think Governor Strong was primarily responsible for that policy, though I would hesitate to state that definitely.

Senator VANDENBERG. What conclusion is to be drawn from that experience?

Mr. RUCKER. In a few words I would say we have got to let values be determined by the market, and do nothing to clog the market.

Senator VANDENBERG. We can't run this show by rule from Washington?

Mr. RUCKER. Definitely not, Senator.

Senator HERRING. Thank you very much.

Mr. RUCKER. You have both been very patient and kind, and I thank you very much.

Senator HERRING. Tomorrow we have Mr. Teetor, of the Perfect Circle Co., Hagerstown, Ind.; Mr. Cooper, vice president of the American Telephone & Telegraph Co.; Mr. Morss, president of the Simplex Wire & Cable Co. of Cambridge, Mass.; Mr. Reading, vice president of Leeds & Northrup Co., Philadelphia; and employees of a number of companies who have asked to come down and make a statement in behalf of the systems that are employed in their factories or in the factories in which they work.

So we will recess until 10 tomorrow morning.

(Whereupon, at 2:35 p. m., the hearing was recessed until 10 a. m., Tuesday, December 13, 1938.)

SURVEY OF EXPERIENCES IN PROFIT SHARING AND POSSIBILITIES OF INCENTIVE TAXATION

TUESDAY, DECEMBER 13, 1938

United States Senate,
Subcommittee of the Committee on Finance,
Washington, D. C.

The committee met, pursuant to adjournment, at 10 a. m. in room 312, Senate Office Building, Senator Clyde L. Herring presiding.

Present: Senators Clyde L. Herring and Arthur H. Vandenberg.

Senator Herring. The committee will be in order. We will hear from Mr. Lothair Teetor, president of Perfect Circle Co., Hagerstown, Ind.

STATEMENT OF LOTHAIR TEETOR, PRESIDENT, PERFECT CIRCLE CO., HAGERSTOWN, IND.

Mr. Teetor. Inasmuch as our company is a rather small company and unknown, I thought perhaps it would be better to start out with a short history of the company.

The company which I represent is the Perfect Circle Co., of Hagerstown, Ind., manufacturers of piston rings, employing at the present time approximately 1,100 people, with plants in Hagerstown, New Castle, and Tipton, Ind.

The company was organized in 1895 by the Teetor family and Mr. Hartley, with paid-in capital of $2,500. No additional capital has been paid into the company since its organization—its growth and expansion being financed entirely from the profits of its operations. The company has changed its name several times, starting as the Railway Cycle Manufacturing Co., changing to Light Inspection Car Co., Teetor-Hartley Motor Co., Indiana Piston Ring Co., and the Perfect Circle Co., but always continuing under the management and virtual ownership of the Teetor family. During the company's history it has manufactured and sold various products, the most important of which have been small velocipedes for the use of inspectors and maintenance men of railroads, stationary gas and gasoline engines, air compressors, automobile and truck engines, piston rings and piston expanders. For the last 10 years piston rings and piston expanders have been practically the only products manufactured and sold by the company.

During the entire history of the company its relations with employees has been personal, informal, and friendly—a relationship which is undoubtedly characteristic of small-town industry. Wage rates have always compared favorably with the wages paid in the central Indiana manufacturing district. For many years the company has carried and paid for group life insurance of from $500 to $1,000 on each employee. Group accident and health insurance is also carried on all employees but is paid for by the employees. A credit union sponsored by the company but managed by employees has deposits of $65,000, representing savings of employees, and annually loans $110,000 to its members. One week vacation with pay has been given to employees for years. The personnel activities such as insurance, safety, credit union, personal consultation, recreation, and records are supervised by a personnel director and staff of five.

In 1935 the company encouraged the formation of employee council groups in all plants. The councils were formed and periodically had meetings with the management, at which meetings all subjects of interest to employees, including wage rates, hours, and working conditions were discussed. The council meetings contributed to the general welfare of employees; however, the management was disappointed at the general lack of interest of employees in the council meetings.

In the year 1936 the company instituted a plan of profit sharing and announced the plan to all employees. The plan was simple, definite, and, we believe, understandable. Briefly, it was this: The rate at which all employees were then being paid was established as a normal wage. A dividend rate of $2 per share per year was established as a normal return to stockholders for their investment. Whenever the company paid an extra dividend to stockholders, it paid to employees an amount equal to 75 percent of the extra dividend. The total sum paid to employees was apportioned among them according to wages received and length of service with the company. The oldest group received twice as much bonus, based on wages received, as the youngest group.

The plan apparently was well received by employees. We felt that we had started a plan about which there could be little controversy. If the company made abnormal profits and was able to distribute extra dividends, then the employees would receive three-fourths as much as the stockholders. The wage rate would be kept constant to discourage increased living standards that could not be maintained through unprofitable periods, and yet periodically employees would receive sizeable bonuses which could be used in making important purchases or invested in savings accounts or securities.

Three profit-sharing payments at 6-month intervals were made—each payment approximating 10 percent of the pay roll for the profit-sharing period—and then the plan was discontinued—discontinued in June 1937, after 18 months' experience.

Discontinuance of the plan was the result of a demand on the part of a majority of employees for higher wages. We had a sit-down strike in the New Castle plant. After an election conducted by the employees, a C. I. O. union became the bargaining agency in that plant. They demanded an increase in wage rate approximating the amount they had been receiving in profit-sharing bonuses. We granted their demands under condition that the profit-sharing plan would be withdrawn. The union accepted and the strike ended.

Employees' unions were then organized in the other plants and similar wage increases were made. In each case the profit-sharing plan was withdrawn, it being impractical to have profit sharing in one plant and not in another.

The natural question is, "Why did the employees reject our plan?" As we see it, there were two principal reasons. First, our labor controversies occurred at the height of the "hatred campaign." Strikes were the fashion, issues were confused, perspectives were distorted. Few manufacturers, regardless of past records of fair dealing, were viewed by their employees without suspicion. Second, the employees failed to recognize the fairness of the plan to both themselves and their employer. They felt that if they could get an increase in wages that would be in the pay envelopes every week, the element of probability which exists in any kind of profit-sharing system would be removed. Whether or not the company could make a sufficient profit to continue a normal return on capital invested seemed to be of little interest.

Yet, we still believe in the principle of profit sharing. We believe it is the only method of remuneration that can be made absolutely fair to both employee and employer. But we cannot reinstate profit sharing in our plants now. The wage rate is at high-profit levels in a low-profit period. Stockholders have earned less than a normal return, while employees have received a higher-than-normal wage. Profit sharing cannot work where such a condition exists. Stockholders will refuse to invest their money in business where wage rates are so high that dividends can be paid only in boom times, and at those times make a division with employees.

Profit sharing can exist only when there is a complete realization on the part of the employee that his hourly or weekly wage rate can never be at the top. He must depend upon the profits of his firm in periods of good business to raise his wage to maximum levels. This means embracing a new principle of remuneration. It means that the employer shall not be forced to pay the maximum wage for any given period; but rather, the employer and employee shall work out together a normal wage that can be maintained throughout good times and bad.

The principle of profit sharing is undoubtedly right, and in the years to come we hope that employers generally will be able and willing to adopt some kind of satisfactory plan. However, the plan or enforcement of a plan has no place in the legislation of this country. The idea and ideal for which we are striving requires education and must have time to grow, both in the minds of employees and employers. It might be possible to legislate employers into offering a plan acceptable to Government, but will employees accept at this time a new principle of remuneration which, of necessity, must contain the following fundamental tenets:

1. Payment of a normal wage for the community and industry which can be maintained over a reasonably long period of time.
2. Payment to stockholders of a normal return on invested capital—due account being taken for individual risk involved.
3. Acceptance of that percentage of excess profits that can be paid in cash after retention of sufficient profits for business expansion and financial security.

To treat the problem as a legislative matter would be to bring fresh turmoil to business, further hampering recovery and progress. We all must realize that both business progress and business reforms are a matter of growth, slow but absolutely sure, and there is no golden, legislative road to either.

Our company will probably adopt a profit-sharing plan again. We believe in the principle. But we want our own plan, according to our own ideas; and we will want it when we think we can have it, not when government thinks we should have it.

There is something, however, that government can do. Government can encourage the adoption of profit-sharing plans through the dissemination of educational literature on the subject. The printing and circulation to companies of the various profit-sharing plans now in use would be of very great help in assisting companies to work out their own plans in keeping with the conditions that prevail in their own individual businesses. Many companies today are successfully operating profit-sharing systems. In time, there will be many more.

And now, just a word about incentive taxation—whether in connection with profit-sharing legislation or any other kind. We believe that incentive taxation is a curse to any nation that adopts it as a principle. In our country, it is a hole in the dike of freedom which will ever wash larger. Once started, it is not improbable that laws and regulations of every kind and description might be passed, each bearing a tax penalty for noncompliance.

The undistributed-profits tax was our first great experiment in incentive taxation, and we can all see what a dismal failure that was. The shreds of that law are still hanging to the revenue act, and during the coming session of Congress we hope every vestige of the undistributed-profits tax law will be stricken forever from the acts of this country. Regulation of business by law is bad enough in most instances, but regulation of business by taxation is insufferable in a supposedly free nation. If a law is right, enforce it with enforcement officers. Let us not degenerate in our legislative character to the place where it is legal to violate the law if we pay the fine. Incentive taxation can never be a reward, for we would be rewarded with our own money. It is always a tax penalty—a penalty for noncompliance, a bribe to the Government to permit us to violate the law.

It has been suggested that a tax reward might be paid to those who use profits or surplus for capital investments. Such a incentive would undoubtedly encourage capital expenditures. However, we believe that actual expenditures as the result of such an incentive would be disappointing. Plant expansion, new machinery, increased inventories are usually the result of demand, not the cause.

Like the undistributed-profits tax, a tax reward for capital investment would be inequitable as between different firms. The large, well-financed firm could expand and receive a credit against taxes, whereas the less fortunate firm, through no fault that it could rectify, would be forced to pay the full tax rates. The reasoning behind the conception of incentive taxation is the recognition that all cannot or will not take advantage of the incentive. There might be justification for forcing the "will nots," but hardly justification for penalizing or withholding rewards from the "cannots." In other words, it might be all right to stimulate the fellow who can afford to be stimulated, but tough on the fellow who is not in a position to respond to the treatment.

If we need more laws to control business, let's pass laws that can and will be enforced. But let's levy taxes for revenue only.

Senator HERRING. There is one statement that you made, that the Government can encourage the adoption of profit-sharing plans through the dissemination of educational literature on the subject. I want to make clear that that is precisely what this survey is intending to do. There has been no suggestion of any compulsory or punitive taxation in connection with profit sharing.

Mr. TEETOR. I understood incentive taxation might be coupled with profit sharing.

Senator HERRING. There was some thought that that might be considered, but only as an incentive. Our whole purpose was to get together just the information, for the purpose, exactly as you said, to disseminate it, so that the manufacturers may know the successful plans that are being followed.

Mr. TEETOR. That undoubtedly would be of great assistance.

Senator VANDENBERG. When you say "Let's levy taxes for revenue only," you mean you would wipe out all protective tariffs?

Mr. TEETOR. No, sir.

Senator VANDENBERG. You do not mean that?

Mr. TEETOR. No; I do not mean that. In connection with business taxation, though, I did mean that.

Senator VANDENBERG. Well, the tariff is an incentive tax, is it not?

Mr. TEETOR. Every tax probably is an incentive tax of some kind; it carries an incentive with it; but I am speaking particularly of the incentive tax which would force business to do something that the Government wants it to do.

Senator VANDENBERG. Well, I think your general warning is very much worth while and, as far as I am concerned, I am glad to have it in the record, because a new subject of this nature which is in process of initial exploration can benefit just as much from opposition as it can from approval. I think, however, without arguing the matter with you, that you might find, upon further deliberation, that you would want to make other exceptions, along with the tariff, to your statement that we must confine our taxes solely to revenue purposes. I appreciate your candor in stating that you would exempt tariffs from this indictment.

Senator HERRING. I think that is everything, Mr. Teetor, unless you have something else you would like to place in the record.

Mr. TEETOR. No; I do not have anything else.

Senator HERRING. We appreciate very much your coming up. We are glad to have this contribution.

We will next hear from Mr. J. Arthur Gibson, vice president, Simplex Wire & Cable Co., Cambridge, Mass.

STATEMENT OF J. ARTHUR GIBSON, VICE PRESIDENT, SIMPLEX WIRE & CABLE CO., CAMBRIDGE, MASS.

Senator HERRING. Mr. Gibson, I received a letter from a man the other day who was interested in profit sharing, and it referred to the Simplex Wire & Cable Co. as being their ideal of profit sharing, stating that your experience went back, I think, to 1902.

Mr. GIBSON. Well, we paid profits the first time for the year 1901.

Senator HERRING. You might go ahead in your own way and tell us about your experiences.

Mr. GIBSON. I have not really prepared a brief, like the previous gentleman. If it meets with your approval, I might, roughly, read a brief that we wrote up some few years ago, which is essentially the present situation.

Senator HERRING. Just so we can get into the record your system and plan.

Mr. GIBSON. The reports of these various experiences encouraged us to make the experiment—that is, profit sharing—but we felt that our plan must differ, to a degree, from any we had heard of, and the scheme was developed in accordance with the following considerations. It was a doubtful experiment and was confined to our factory employees, leaving out clerks and salesmen in our main office.

Realizing that the result must be a question of judgment rather than definite figures, and wishing to be assisted in our judgment by the opinion of our two factory superintendents whom we had interested in the experiment, we increased their salaries instead of making them profit sharers, in order that their judgment might not be biased by their own interest. We expected the best results and wished particularly to benefit certain old and faithful employees, while from recent employees, and particularly those who were not likely to stay with us long, we expected very little, and we had very little interest in them, so that it seemed to us to be necessary to make a distinction, and this was accomplished by the requirement that no one should be eligible to benefit until he had been in our employ for at least 1 year.

On the principle that no partner has a right to any part of profits earned before he comes into the partnership, we decided that a profit sharer must be informed of this status and must work as such for the full year before he is entitled to any profits.

In order to provide ample time to make up the books of the company—that is, for any calendar year—and to determine the profits, we set the time of payment as March 1, or 2 months after the close of the year; that is, the calendar year. To further extend the time of service it was decided that no profit sharer should benefit who leaves our employ before the dividend date of March 1. To give our people the greatest stimulus it was necessary for the amount of their dividend to be absolutely dependent on the profits of our business for any given year, and that, as nearly as possible, the profits of each year should be separately determined, so that no man should either gain anything from the profits of the year before, nor lose anything from profits carried into the succeeding year when he may have left our employ.

At the outset we were confronted with the difficulty that, being a private corporation, wholly closed, we were absolutely unwilling to make any statement from which the amount of our profits could be determined, which would certainly be the result should we announce the percentage of our profits which we proposed to pay and later told what this percentage amounted to. To obviate this trouble we refrained from stating the percentage of the profits which we proposed to pay, saying simply that such percentage was fixed in advance although not published. At the beginning of the first year, in order to give our people some idea of the probable result, we advised them that the percentage, as fixed, was sufficient to justify the expectation that the dividend on their wages would be at least 5 percent—incidentally, to interject here, the first year's dividend was a little over

11, as I remember it—providing that the profits of that year were as large as those of the year preceding. In order that the administration of the profit sharing should be absolutely fair, we have, at the beginning of each year, posted a set of rules which we had been able to keep down to one typewritten page and had administered each year strictly according to rule. On January 1—that is, the first year—we assembled our entire force and carefully explained the profit-sharing scheme to them. Immediately afterward the preliminary list and the rules for that year were posted. While our people were evidently pleased that something good was coming to them, it looked rather a long way off and comparatively few seemed to really understand the scheme. A repetition of the address the following January still left the matter somewhat hazy in their minds; and the results for the first year, while visible, were not as great as had been hoped. The actual payment of the first dividend, March 1, had a great effect—that was after the second address, you will realize, perhaps—had a great effect, and ever since the results have been much more satisfactory than before.

Senator HERRING. Did you make a payment at that time on the first year's profit sharing?

Mr. GIBSON. We made a payment on the first year's profit sharing. Whereas we had tentatively told them we had hoped to pay the 5 percent on their wages, we paid 11.05 percent.

Senator HERRING. That probably had something to do with their having more interest in it the second year?

Mr. GIBSON. Yes; after they actually got it, 26 months after the time, or the plan, went into effect. Then follows, in this write-up the rules, which perhaps you may not care to have me read.

Senator HERRING. No; if you will just outline the working of the plan itself.

Mr. GIBSON. Well, quickly, without going through all of this reading, perhaps this will tell it as well as I can, and better.

The specific percent of the profits distributed among the employees under this plan is fixed 1 year in advance, and although this proportion is unknown to the rank and file of the profit sharers, it is communicated to the accounting department by the directors the first of the participating year; it is made, in other words, a contract between the directors of the company and the employees, although it is a blind contract, as you will see, as far as the employees are concerned, in that they cannot know just what the percentage of the company's profits is going into the profit-sharing fund. That percentage being settled, when the final results for any calendar year have been ascertained, whether large or small, the contribution, at the percentage agreed on, is put aside in a so-called profit-sharing fund, and that fund is divided in the exact proportion that each person's own wage or salary (the total remuneration for the year) bears to the total salaries, wages, and so forth, of all eligible profit sharers.

Senator HERRING. What is the basis for the determination of the percentage, the amount to be allowed, whether it is 10 percent or 11 percent?

Mr. GIBSON. Well, that grew, something like "Topsy." As it has been said here, it started off as a sort of experiment, and it was hoped and shaped up with the thought that we would at least be able to pay somewhere in the neighborhood of 10 percent. That is not quite what I have told you in this reading, but you do not always put forth your best foot first. If we told them we expected to pay them 5 percent and gave them 10, so much the better. If we had said 10, which we hoped to pay—I was not with the company at that time—and only paid 5, then it would be against us. Now, the original percentage was started knowing what the pay roll had been for the prior year and what the profits had been. We figured out that it would have to be a certain percent to realize a fund which, if distributed, would give them 10 percent. Do I make myself clear?

Senator HERRING. Yes.

What percent of the profits, on an average, is distributed as profit sharing?

Mr. GIBSON. I would rather not answer that.

Senator HERRING. How does it compare or contrast with the dividends paid, in total amount?

Mr. GIBSON. Well, of course, that is variable. I do not have any of the exact figures with me. Of course, it would be a smaller amount, and you would expect that.

Senator HERRING. It is not always a small amount. Some profit sharing exceeds the amount of dividends.

Mr. GIBSON. There have been years when no dividends have been paid from the company's business. You will remember, maybe, 1931 and 1932.

Senator HERRING. Yes; I remember.

Mr. GIBSON. There has been a profit-sharing fund in every year since 1901 down to the present time, with one exception.

Senator HERRING. Well, your base wage is at least the equal of the wage being paid by other concerns?

Mr. GIBSON. We feel that our wages are far in excess—we know they are in excess—of others in our line. That is not my end of the business, but I have a figure in mind of something like 60 cents an hour as being the minimum paid for wages.

Senator HERRING. Are your employees organized?

Mr. GIBSON. They are, at the present time.

Senator HERRING. Do they belong to organized labor?

Mr. GIBSON. No; it is an employee union, wholly unaffiliated.

Senator HERRING. Did you arrive at this percentage of profit sharing through any negotiation with the employees?

Mr. GIBSON. No, this was something that was sprung on them, for their own good. By the way, I might say that the percentage first established in 1901, was an experiment. It has since been increased; that is, the percentage of the profit sharers fund has been increased five times. Perhaps you will remember in the reading here I said they left out the superintendents. It was later thought best to bring them in; therefore, the percentage was increased somewhat to take them in; and then there were a couple of other increases, just to fatten up the fund. Later on the plan was extended to cover the administrative office and salesmen, and a year later to take in our branch offices, so that from 1914 on all the employees of the company, with the exception of the officers, were covered.

Senator HERRING. About how many employees have you, Mr. Gibson?

Mr. GIBSON. About 700.

Senator HERRING. Have you had any labor trouble?

Mr. GIBSON. Only incipient labor troubles, and we credit the fact that we have had no labor troubles to our profit-sharing plan.

Senator HERRING. Well, you had a show-down in 1937, I think, did you not?

Mr. GIBSON. In 1937 we had, as our questionnaire shows you, some trouble, which was from A. F. of L. organizers coming in. Briefly, the matter went before the National Labor Relations Board and came to a vote, and the A. F. of L. affiliates were in the minority. After that our employees got together and formed their own unaffiliated union, which is now in effect.

Senator HERRING. Is part of your profit sharing providing the employees with the balance sheet so as to show the net results of the operation of the company?

Mr. GIBSON. No. Being an entirely closed corporation and wholly a family affair, it is a relatively small corporation. It is a one-family affair, and it is our policy not to publish either gross business, profits or dividends.

Senator HERRING. In spite of that, you feel that your employees have a confidence that they are getting a fair share of the profits in accordance with the proposal?

Mr. GIBSON. They always have, so far as I know. Of course, there are exceptions to every rule. It might interest you to know that the profit-sharing dividends have ranged from a high of—well, it is not quite a fair figure to use, it is so far back—but it has been as high as 18.45 percent, down to 2 or 3 percent.

Senator HERRING. How much would you estimate the average flat wage of the average employee?

Mr. GIBSON. At what time?

Senator HERRING. Well, at any time.

Mr. GIBSON. These are profit sharers wholly of course?

Senator HERRING. Yes.

Mr. GIBSON. You understand that all of our employees are not eligible.

Senator HERRING. The only requirement is that they shall have been in your employ a year, is it not?

Mr. GIBSON. Well, that they shall have been in our employ at least 1 year prior to the participating year.

Senator HERRING. There is no other requirement?

Mr. GIBSON. That is all. Now, to answer the question as to the average yearly return for the profit sharers for the year 1937——

Senator HERRING (interposing). Yes.

Mr. GIBSON. And do not misunderstand me; this is the wage of all profit sharers.

Senator HERRING. Yes.

Mr. GIBSON. It would take in the salesmen, the administrative clerks, and the clock workers. I do not have the figure for clock workers alone. It is $1,600.99.

Senator HERRING. Then somebody got nearly $300 in profit sharing?

Mr. GIBSON. The average dividend for everybody, from office boy up to the fellow next to this director, was $132.02 plus.

Senator VANDENBERG. If I understand that, you deduct social-security taxes from the profit-sharing dividends?

Mr. GIBSON. The social-security taxes are applicable to this remuneration under the law. The company pays its tax, under the old-age payments, of 1 percent, and that is $1.32, and that would result in $1.32 deduction, and likewise the company pays its $1.32.

Senator VANDENBERG. That is what I am getting at. You do not deduct the company's share?

Mr. GIBSON. Absolutely not.

Senator VANDENBERG. The statement in your pamphlet is a bit ambiguous on the subject. I thought it ought to be cleared up.

Senator HERRING. Does it say anything about that?

Senator VANDENBERG. Yes; it says the social-security taxes will be deducted from profit-sharing dividends. That should be broad enough to include everything. I notice you have a profit-sharing committee elected by the employees.

Mr. GIBSON. Yes.

Senator VANDENBERG. What is the function of that committee?

Mr. GIBSON. The only function of that committee is, it meets three or four times a year to clear up any border-line cases. When a person leaves our employ he is automatically out of the profit-sharing scheme, whether we discharge him or whether he leaves. That is clear in the rules. Now, there is a provision—I think you will find it there; I do not have the copy myself—there is a provision as to the requirement in case of a 6 weeks' lay-off—I am just mentioning a hypothetical case——

Senator VANDENBERG (interposing). Yes.

Mr. GIBSON. Now, for instance, suppose this fellow was intended to be laid off for 6 weeks and still continues as a profit sharer, we might take him back, well, on the fifth day of the last week, and employ him for 2 or 3 days, and lay him off again. Now, suppose he did not get back until 1 day after 6 weeks, some of the employees, might feel that he ought to still be a profit sharer. It is their fund. If they vote that, due to some error of the foreman in not getting that man back on the last day of the 6 weeks, but if they find it went the other way, if they vote he is still eligible, we agree. It is their fund, in other words, and they are voting their own money away, to some small extent.

Senator VANDENBERG. The committee has no right of consultation with respect to the amount of the profit sharing?

Mr. GIBSON. No. It is only these border-line, hair-splitting cases that might come up in administering the plan.

Senator HERRING. Do you have anything else you would like to put into the record, Mr. Gibson?

Mr. GIBSON. Why, there is nothing that I would wish to put in, unless you have some more questions. There is just the one point. You asked in your questionnaire for ideas, plans, and so forth, for a compensatory scheme of taxation.

Senator HERRING. Some incentive taxation, compensatory tax benefits.

Mr. GIBSON. Yes. The quick reaction is that we are somewhat against that, although we do not have any very strong feeling. If you did not come up to the yardstick that your law might lay down—if for some reason, in a bad year, a year of heavy expenses, and so forth, the plan did not allow us to come up to your yardstick—well, there would be a penalty, of course, and that would be an objection.

Senator HERRING. What is your labor turn-over? Do you think it is affected by your profit-sharing plan?

Mr. GIBSON. We are morally sure that it has in years past, and even now, with the incipient labor trouble that we had last year, we are absolutely sure that it has kept our people with us.

Senator HERRING. You are convinced it is good business?

Mr. GIBSON. Oh, yes. Another thought that has been wandering around in our minds for a year—last year was a good year, 1937, and this year is going to be bad, and if there would have been some way of, we will say, just to illustrate—I want to say this has been discussed this year—but to illustrate my point, if instead of the percentage that we did give, knowing it was a good year, certainly going toward the end of the year, if we could have doubled that, if the directors could have doubled that percentage and withheld the doubling for a bad year or sort of spread it out, we would have liked to have done it, but we would have penalized ourselves. We could not have taken it on our income-tax return as a deduction from taxable income; we could not have done that; and of course we would have paid—to have held it back—we could have paid undistributed-profits taxes on the reserve.

Senator VANDENBERG. Then what you are saying is that you would favor tax exemptions for a reserve set-up?

Mr. GIBSON. Irrevocable reserves. We could agree, in our minds, to set up irrevocable reserves for our employees, if you would let us.

Senator HERRING. A common observation from employers who are not interested in profit sharing is that it would probably work all right when there are profits, but what would you do if there are losses? Now, you have had that experience. How would it affect your business?

Mr. GIBSON. Well, of course, they do go down when you do not get it, and they go up when you do get it. I do not have the average for the years through 1937, but in this brief here I remember there was an average figure for certain years. I do not want to take your time, but I thought it was averaged. It is something like 12½ percent there for a matter of 12 years. Now, if those had been with us for some considerable time, they knowing they are going to get that average percentage approximately, and knowing how much they are working during the year, they know in advance what the percentage is going to be; they strike it closer than the bookkeepers.

Senator HERRING. And really you had labor trouble when you had the fixed profit sharers in 1937, and you did not have any labor trouble in 1931 and 1932?

Mr. GIBSON. The answer is "no" to your question.

Senator HERRING. You did not have it in 1931?

Mr. GIBSON. Well, you see, Senator, as against some of the depression years, relatively, it was not the biggest year, by any manner of means, although, I should say, incidentally, the biggest year of our labor troubles, such as ours were, started way back in the spring of 1937. Now, our profits, of course, were not known until March this year; and when they were known, if I may say it—although a lot of our old-timers were death against this, oh, the outside proposition of unionizing our people—when the profit sharing was given out and the percentage was known—incidentally, it was a month's pay, roughly—more flew away from the A. F. of L., I imagine, if you want to put it that way, or the outside domination than ever before. Incidentally, I am wondering how far I am to go. I had really no brief. I expected to be asked questions. Every year the profit sharers themselves have given the officers of the company a banquet. They got up this banquet, a big entertainment, a dinner, and so forth, and lo and behold, we did not have to pay for our tickets.

Senator HERRING. You have had 37 years of experience in this, and I was trying to get your answer to the objection which was made that it will work when a profit sharer has profits and when you do not have profits it will not work.

Mr. GIBSON. You can see that is not so. You cannot say it has militated against the plan as a whole, over 4 or 5 years. One swallow does not make a summer, nor does 1 bad year work against the plan.

Senator HERRING. Your men went along with you in 1931 and 1932, when you had no profit sharing?

Mr. GIBSON. Oh, yes. Perhaps they could not get jobs elsewhere and they were glad to stay with us. I do not know offhand what the reason was.

Senator HERRING. And it would affect other plants equally, that had profit sharing, if they went through a period of that kind?

Mr. GIBSON. Oh, yes.

Senator HERRING. All right, Mr. Gibson; thank you very much.

We will next hear from Mr. C. P. Cooper, vice president, American Telephone & Telegraph Co., New York.

STATEMENT OF C. P. COOPER, VICE PRESIDENT, AMERICAN TELEPHONE & TELEGRAPH CO., NEW YORK

Senator HERRING. Just go right ahead. You have a statement there, haven't you, Mr. Cooper?

Mr. COOPER. Yes; I have. It is not long. If I may, I would like to read it.

Senator HERRING. Certainly.

Mr. COOPER. I appreciate the opportunity to appear before this committee in response to your invitation to state the general policies of the Bell System applicable to employee relations and to describe briefly the methods followed in carrying out these policies.

We believe firmly in paying good wages and in providing good working conditions—first, because we consider that efficient workers are entitled to them; and, second, because it is good business to do these things. This policy is not new but has been in effect for a long period of years. It was reiterated by Mr. Gifford in his annual report to stockholders for 1933, where he said:

> This country is entitled, in good times and bad, to the best possible telephone service at the lowest possible cost. The success of the American Telephone & Telegraph Co. and its associated companies must be measured by that standard and depends on giving at all times, day and night, dependable, accurate, and speedy telephone service, constantly improved and extended in scope by research and invention, at a cost to the users as low as efficient operation can make it, consistent with fair treatment of employees and such return to the stockholders as will insure the financial safety of the enterprise.

This does not mean that our companies do nothing more for the employees than to pay good wages and provide good working conditions. On the contrary, we have long endeavored to aid them in meeting the vicissitudes of life and have helped them to save for themselves against the rainy day.

At the beginning of this year the average annual earnings of our employees was 17 percent higher than in 1929, due to higher wages, a more experienced force, and lower proportion of employees in training. Hours of work have been reduced from 48 and 44 per week to 40, and wages have been increased. Substantially all employees are now receiving as much or more pay for 40 hours per week as they formerly received for the longer week. Vacations with pay are given to all employees. They also receive pay for holidays. Vocational and supervisory training is provided to develop knowledge and skill for effective performance, thus helping the employee to increase his usefulness and prepare for advancement. It is the general policy and practice of the companies to make promotions and fill supervisory positions from within the organization.

Most workers strive to earn enough to live in comfort, educate their children, provide for emergencies, such as sickness and accident, and to care for old age. To assist the employees in mitigating the common hazards of sickness, accident, disability, superannuation, and death our companies established in 1913, more than 25 years ago, a plan for pensions, and sickness, disability, and death benefits. The plan is noncontributory. Next to good wages and favorable working conditions, nothing in our employment is valued more highly by the employees nor contributes more to the giving of good telephone service than the benefit and pension plan.

The sickness and disability benefits aid in stabilizing employee income, and the death benefits aid the dependents in necessary adjustment of living arrangements. The provision for pensions permits the retirement of all employees who have been long in the business and have reached an advanced age.

Expenditures under this plan are charged directly to expenses on a pay-as-you-go basis, except for pensions. Pensions are provided for in advance by accruing on an actuarial basis through current expenses and payment to pension trust funds from which pensions are paid. On September 30 these trust funds—each company has, of course, its own separate fund—aggregated $185,866,000.

In addition to the payments made regularly for benefits under the plan, special payments are made in case of need or emergency. Many of the companies maintain medical departments to aid employees in prevention of sickness and promotion of health. These departments have sponsored first-aid training courses for men and health courses for women. Seventy-five thousand employees, mostly men, have completed first-aid training courses; and 60,000, mostly women, hold certificates of completed health courses. Both courses were prepared in cooperation with the American Red Cross. They have helped the system to establish an enviable record of accident prevention and have contributed to the good health of the personnel. The public has benefited directly from the first-aid training through considerable emergency assistance by telephone men to victims of accidents.

The expenses of Bell System companies for all of these activities and benefits, exclusive of social-security taxes and not including payments for vacations and holidays, are annually about $25,000,000, or about 6 percent of the pay roll. Social-security taxes are $13,-800,000 or an additional 3 percent of the pay roll.

We believe in helping employees to provide for themselves according to their individual ability and need and have established thrift programs for voluntary use by them through pay-roll deductions. Under these plans 17,000 employees are buying United States savings bonds, 63,000 are paying premiums regularly on their life insurance, and 60,000 are making deposits of savings regularly in savings banks or credit unions. Of course, these figures represent only a part of the picture. Many are home owners and many others have savings accounts, insurance, and investments which they have accumulated directly rather than through pay-roll deductions.

About 65,000 employees of the Bell System companies are now stockholders in the American Telephone & Telegraph Co. and hold approximately 820,000 shares of stock, an average of 12½ shares each.

Over the years, there has been constant improvement in income, better working conditions, and shorter hours for telephone employees. The public has received more and better service for its money. Telephone workers generally are keenly interested in the success of the business and not only appreciate the importance of good service, but have a sincere desire to do the best job they can for the public. It is impossible to determine the extent to which this spirit of service has been strengthened by the system's plans for greater employee security and peace of mind or by the workers' voluntary participation in plans for their self-protection and advancement. Certainly both management and employees would be most reluctant to risk the impairment of this spirit of service through any withdrawal or curtailment of this program.

We do not believe that profit sharing beyond that herein stated is applicable to our business. It is the policy of the system that earnings over and above those required to provide good wages, favorable working conditions, and such returns to investors as will insure financial safety should be shared with our customers. We believe firmly that this is the only sound policy for us—a regulated business—to follow for the long pull; and, of course, there is no justification for acting other than for the long pull.

I do not want to be understood as advocating the abolition of profit sharing in those cases where it has been found satisfactory and helpful to both employees and the employer. My view is that for industry as a whole, profit sharing as a national policy would not be helpful. It would not tend to smooth out the peaks and valleys of booms and depressions but would tend to exaggerate them. Our national policy should be aimed at smoothing things out.

Similarly, it is my belief that the principle of "incentive taxation" is unsound as a national policy. All taxes are restrictive, but they must be levied to provide for the expenses of government. I believe that to influence the course of business by either penalties or incentives so far as taxes are concerned is unwise.

Senator VANDENBERG. Is this benefit plan a standard practice throughout all of your subsidiaries?

Mr. COOPER. Yes. They all have adopted the same plan.

Senator VANDENBERG. And are the costs charged against the subsidiaries?

Mr. COOPER. The costs of the plan?

Senator VANDENBERG. Each company bears its own costs?

Mr. COOPER. That is what I mean.

Senator VANDENBERG. Now, the rates, of course, are regulated by State authorities?

Mr. COOPER. Both State and Federal commissions.

Senator VANDENBERG. Have you ever found these regulating authorities quarreling with you for any money taken out of gross income and devoted to social service and benefits of this character?

Mr. COOPER. We have had a few cases where commissions have disallowed, in rate proceedings, part of the expenditures that have been made under our benefit plan.

Senator VANDENBERG. How often has that happened? Let me put it a little differently. Would you say that was the normal standard attitude of regulatory bodies?

Mr. COOPER. No; it is the exception rather than the rule.

Senator VANDENBERG. That is what I am getting at. Ordinarily public authorities that regulate your rates accept your benefit and pension payments as appropriate operating-cost deductions.

Mr. COOPER. Yes; they do. There have been apparently few cases where those expenditures have been questioned and where they have been disallowed in rate proceedings.

Senator VANDENBERG. Has the question ever gone to court?

Mr. COOPER. Yes; I am filing for the information of the subcommittee a list prepared by our legal department of court and commission cases involving Bell System companies in which the matter of pension expenses was under consideration. This list, of course, does not include the many rate cases in which such expenses were not expressly at issue and were allowed without comment:

COURT AND COMMISSION CASES—PENSION EXPENSES

COURT CASES

Chesapeake and Potomac Telephone Company v. *Public Utilities Commission* (62 Wash. Law. Rep. 486). (Supreme Court, District of Columbia, 1934.)

State of Minnesota v. *Tri-state Telephone and Telegraph Company* (District Court, Ramsay County; Minnesota, 1937). (Now pending on appeal before the Supreme Court of Minnesota.)

Wisconsin Telephone Company v. *Public Service Commission of Wisconsin* (Circuit Court for Dane County; Wisconsin, 1938.) (Now pending on appeal before the Supreme Court of Wisconsin.)

COMMISSION CASES

Re Mountain States Telephone and Telegraph Company (P. U. R. 1917B 198, 249–253, 296–297; Colorado 1917).

Re Chesapeake and Potomac Telephone Company (P. U. R. 1920F 49, 92; Virginia 1920).

Re Mountain States Telephone and Telegraph Company (4 Utah, P. S. C. 21; 1921).

Re New York Telephone Company (P. U. R. 1923B, 545, 624, 681–686; New York 1923).

Re New England Telephone and Telegraph Company (P. U. R. 1925E, 739, 754; Massachusetts 1925).

Re Chesapeake and Potomac Telephone Company (P. U. R. 1926E 481; Virginia 1926).

In Re Uniform System of Accounts (191 Commission Leaflet 429; I. C. C. 1927).
City of Columbia v. *Southern Bell Telephone and Telegraph Company* (42 Ann. Rep., Ga. R. C. 233; Georgia 1914).
Re Southwestern Telephone and Telegraph Company (Missouri Commission, June 1915).
Re Chesapeake and Potomac Telephone Company (P. U. R. 1932E, 193, 200–201 (District of Columbia 1932); 4 P. U. R. (N. S.) 346, 355–356 (District of Columbia 1934); Reversed 62 Wash. Law. Rep. 486).
Re Michigan Bell Telephone Company (10 P. U. R. (N. S.) 149, 211–212; Michigan 1935).
Re Michigan Bell Telephone Company (1936 Opinions and Orders of Michigan Public Utilities Commission, 402).
Re Wisconsin Telephone Company (Wisconsin Commission, 4 cases consolidated) P. U. R. 1932D, 173, 183–190; 4 Wis. P. S. C. Rep. 201 (1933); 6 P. U. R. (N. S.) 389, 402–403, 410 (1934); 13 P. U. R. (N. S.) 224, 253–256 (1936).
These orders are reviewed in *Wisconsin Telephone Co.* v. *Public Service Commission* (Wisconsin Circuit Court Dane County 1938).

Senator HERRING. Thank you very much, Mr. Cooper. I have nothing else. Unless you have something else, there is nothing that we want to inquire about, except as to Mr. Gifford's health.

Mr. COOPER. He is getting along very nicely. He gets back to work a few hours each day, but the doctor is still keeping him rather quiet.

Senator HERRING. Give him my regards. He happens to be a cousin of Mrs. Herring.

Mr. COOPER. I will be glad to do that.

Senator HERRING. We will next hear from C. S. Redding.

STATEMENT OF C. S. REDDING, VICE PRESIDENT, LEEDS & NORTHRUP CO., PHILADELPHIA, PA.

Senator HERRING. Mr. Redding, you have a bonus plan, I think, have you not?

Mr. REDDING. Yes; we have.

Senator HERRING. Would you tell us about it?

Mr. REDDING. I am sorry Mr. Leeds has not been able to come down to present this matter, because he is an authority on this very thing, having been interested in industrial relations for a good many years. I think I can speak for him, but in presenting some of these plans, I would like to read very largely from some of his statements, because they are considered statements, and I can save time, probably, by reading from them.

I would be glad to put in a little bit of Mr. Leeds' philosophy, if I may. It is taken from a paper appearing in Forbes Magazine, November 1, 1931. At that time they said:

The Leeds & Northrup Co. manufactures electrical measuring instruments and apparatus for temperature measurement and control. It was started in 1899 with 25 employees, and now has something over 1,000, an unusually large proportion of whom are engaged in sales, outside service, research, engineering, inspection, and office work. Instruments of precision can be successfully produced only by trained workers whose skill is the result of years of experience, and owing to the difficulty of replacement, it is important to maintain the sort of industrial relations which will conserve such a working force once it has been assembled and trained.

Our plan, which has been gradually evolved and put into practice during the past 25 years, has at all its stages been in full sympathy with the Forbes principle that "Although based upon the profit motive, business exists for man and not man for business." We have sought to build a durable institution which should be profitable to all who have a part in it and serviceable to those who use its product. Justice to all concerned seems the soundest guiding principle; and of the various definitions of justice, I have found most useful this which Durant attributes to Plato: "Each man shall receive the equivalent of what he produces and shall perform the function for which he is best fit. A just man is a man in just the right place, doing his best, and giving the full equivalent of what he receives." As we conceive them, human relations involve the entire personnel from the executive officers to the latest apprentice; they must be something more than the means which management and ownership use to maintain morale and efficiency among workers. A business organization should be a unified group of people banded together to earn a living for its members, seeking to do justice among all of them and to the rest of the world. A considerable element of democracy must enter in—not democracy in our political sense, with one vote for each, but, as I suggested some years ago, a democracy which aims to secure equality of opportunity—not equality of power or equality of reward, but an equal chance for each to rise to that level of reward and power for which he is qualified. These few words must suffice to indicate the conditions under which we work and the guiding thread of industrial philosophy on which the diverse elements of our plan are strung.

Ownership and control are of primary importance because the destiny of the organization rests with them. Our company is a corporation but with unusual provisions in regard to the ownership and rights of shareholders, which aim to keep control in the hands of those who are experienced, competent, and in full sympathy with the company's policies. There are three classes of shares—employees' shares, converted shares, and investment shares.

Employees' shares have full voting rights, may be held by employees of the company only, and receive all of the profits, after the limited preferred dividend is paid on converted and investment shares. The provision that these shares which exercise the control and receive the profits shall be held only by employees is made because, if held by outsiders, control might be in the hands of those who, through lack of knowledge and contact with the business, might not be best fitted to exercise it, and because profits going to absentee owners might leave the more active managers on the job with a feeling that an injustice had been done them, resulting in a let down in their loyalty and efficiency.

While employees' shares may be held by employees only, they may not be held by any and all employees who happen to be able and willing to buy them. The shareholders elect annually a board of trustees who have the responsibility of determining which employees may buy shares and how many, but this selection can be made only from employees who have been with the company 5 years and who have salaries of $1,500 or over. Employees' shares are sold for cash only. There is no provision for their purchase from the company on an installment plan, although considerable purchases have in recent years been arranged through private loans with the stock as collateral. The bonus plan, to be described later, has provided many with the means of making stock purchases. The value of employees' shares is determined annually for trading purposes by a formula and is based on a weighted average of their earnings for the past 5 years, greater weight being given to recent years. Employee shareholders who leave the company may either sell their shares at the formula value to other approved employees, or may have the total value of their holdings determined by the formula and used to purchase converted shares, which have a par value of $100 and an 8 percent preferred dividend. These may be called at any time by the trustees and sold to employees as such, or reconverted into employees' shares. They may be bought and sold like ordinary stocks.

Investment shares are like converted shares except that they have a prior claim on earnings and assets, are sold for cash only, and their issue is limited.

One of the objects of the trusteeship was to distribute the holdings to a large number of employees. In 1915 I held all of the employees' shares, and there was only one other holder of investment shares. Today my holding of employees' shares has been reduced to approximately 54 percent of the total. There are 60 other holders of employees' shares, holding a total of 4,452 shares. There are 63 investment shareholders holding 1,563 shares and 132 converted shareholders holding 10,210 shares.

Another object was to provide a fair means, which would not cause controversy, for converting and retiring the holdings of men who retired from the company. Since 1924, men who have left the company have had the employees' shares which they at that time owned converted to 2,999 converted shares, worth $299,900, and these shares have now all been called and taken by present employees. In addition, approximately $100,000 worth of converted shares which had belonged to me have been called and sold to employees.

The hope that our stock-participation plan might be sufficiently attractive to good men to prevent them from leaving us and setting up competing enterprises or engaging with competing houses has also been realized. None of our employees, who have been with us long enough to become holders of employees' shares have become dissatisfied and left us to go with competitive firms or to set up such organizations of their own.

The plan also provides, in the investment and converted shares, a relatively safe fixed dividend form of stock which can be properly bought as an investment by those employees whose business experience and outside circumstances do not justify their taking the employees' share. The investment and converted shares yield a good return while at the same time such stock ownership gives the employees who purchase these shares a sense of "belonging" and increases their interest in the company's welfare.

The bonus plan was inaugurated some 9 years ago. Under it we set aside each year, when earnings permit, a certain portion of them, called the bonus fund, which is divided among a group of major and minor executives called the bonus group. The group has gradually grown until it now numbers 91. The members are arranged in subgroups. The share of bonus varies with the different groups, those in the upper group getting much more than those in the lower. The ratio between the smallest and largest bonuses is of the order of 1 to 100. In good years, bonuses may be 15 or 20 percent of salaries for those in the lowest group, and two or three times salaries for those at the top. This arrangement is an attempt to carry out the idea in Plato's definition of justice—that each man shall receive the equivalent of what he produces; it is an attempt to give managers their just share of the fruits of the enterprise they manage.

When there are profits left over after fair wages and salaries have been paid, other ordinary expenses have been met, and invested capital has received compensation properly related to its cost and risk, it is a reasonable assumption that management has contributed the something extra that has brought about these profits, and therefore has in justice a considerable claim to them. The range in the amount of bonus is a recognition of the fact that it is the major executives who, through their determination of policy and procedure, chiefly influence profits. This has been discussed more than once in the group and is cheerfully accepted as fair.

The relatively large number included in the bonus group is due to a realization that management resides not alone in the ranks of the higher executives, and is part of a deliberate effort to cultivate it as far down in the ranks as possible. In many cases, the subordinate executives not only transmit and enforce policies, but also have a share in making them. These subexecutives are appreciably more than the mere channels through which the high command executes its purpose.

The bonus group exercises the chief influence in determining what new members shall be brought into it and shifts of rank of those that are in. Each year the group makes recommendations to the management on both of these points which have, with a few exceptions, been approved as made. The recommendations have several times included demotions as well as promotions. It might be thought that the group would feel that the introduction of new members would simply decrease the share of bonus for those already in, and so become exclusive. This has not been the case. They know that the introduction of new members will not ipso facto increase the fund, but they also realize that management originally formed the bonus group in the belief that by distributing to its members a share of the profits, it would not only be doing what is fair, but would also so stimulate their interest and enthusiasm that the share of profits that would be left for owners would not be diminished. In the same way, the members of the group feel that additions of the right people will not decrease their bonus.

For our organization the bonus plan has worked well. Shortly after it was put in operation, the group, without suggestion from the management, arranged to have monthly meetings, which have been continued. They are held once a month in the evening, away from the plant, and at the members' expense. There is a dinner, followed by papers and discussion of plant problems, and then by recreation, generally bowling. The meetings have two good results: First and most important is the "get together" on something other than the everyday business basis—an arrangement by which the men get to know each other as a group of good fellows engaged in a common enterprise. The mutual understanding and respect so engendered have made it much easier to iron out internal plant misunderstandings and difficulties; second, real progress has been made in these meetings in dealing with specific problems that have to do with better operation.

This much space has been given to the arrangements for the relatively small number of those in the management and ownership groups, because it is these who make the organization what it is. By making justice the basis of arrangements with them we appeal to and cultivate their own sense of justice so that they tend to make it the standard for all dealings with other employees and the public.

The cooperative association is an organization of the entire personnel. It was formed in 1919, when under wartime stimulus our numbers had grown so that the personal contacts of earlier times were no longer possible. Its formation was a deliberate democratic procedure, discussed first in a small group of foremen, then in a larger group of all the older employees. It was decided that everyone in the company should be a member, and that we would not, as is done in some cases, organize the bench workers and those of similar grade separately. One of the primary objects of the association was to effect a unified group, and to organize the manual workers as such and pit them against the management would not tend to do that. The association functions through a council, whose members are elected annually and represent various divisions of the organization. The name cooperative is descriptive of its functions in two directions: First, among the employees for a wide variety of activities in which they can be mutually helpful, such as athletics, entertainments, education, mutual-benefit societies, etc.; and, second, in working with the management on business matters in which the employees have a direct interest, such as the good order, convenience, and comfort of grounds and buildings, hours of work, vacations, overtime pay, regulations safeguarding discharge, and wages. In connection with the first group of subjects the council has full power. In connection with the second the management leans heavily on it for consultation and advice. The work of the council is regarded as a legitimate function of business, so its meetings are held on company time and its secretarial and other expenses paid by the company. Recently it has had a full-time executive secretary, chosen by it, but paid by the company.

The following brief synopsis of the work of some of its important committees indicates, inadequately, the range and extent of its activities:

Permanent committee on wages: This is a standing committee which, in cooperation with the management, has worked out the system that we are now using for a review, once in 3 months, of the rate of pay of all hourly workers and of a large part of the clerical force. It has satisfactorily handled many minor problems relating to wages and hours of work.

Lunchroom committee: This committee concerns itself with the conduct of our cafeteria and makes recommendations in regard to food and service.

Reception and entertainment committee: A committee which welcomes newcomers and helps to make them acquainted with the plant. It has managed a large number of dances, receptions, and other entertainments, which have been very successful.

Dispensary committee: This has done much to interpret the nursing and dispensary needs of the employees.

General improvement committee: This is a permanent and very useful committee. It regularly makes plant inspections, comments on the cleanliness and general order of the various departments, and suggests improvement.

Finance committee: This deals with council's finances, which it has recently put on a budget basis.

Committee in charge of athletics: This has a fine record of accomplishments in tennis, baseball, bowling, and other sports, to which our well-filled trophy case bears testimony.

Music: Glee and mandolin clubs have an excellent record in instrumental and vocal music, including performances to large audiences outside of the company, and broadcasts.

Appeal board: In 1921 an appeal board was set up, the members of which are appointed annually by council. Any employee who is discharged and feels that he has not had proper consideration may appeal to this board. It reviews the case and submits its findings to the management. Although comparatively few cases have been referred to it, the influence of this board has been greater than its activity. The character and success of its work may be illustrated by the cases of two men who were discharged for "beating" the time clock. One was an older man, who arranged with a comparatively young one to punch the clock for him when he was late. The board found that the discharges were justified, but recommended that the young man should not be discharged because it believed that he was not fundamentally inclined to do wrong, and that with the lesson of the incident he would not do so again. The recommendation of the board was approved by the management, and he was retained with the company. Several years later the older man again applied for employment. The management, having some doubt as to the advisability of taking him back, referred the case to the appeal board, which, after going into his record and interviewing him, recommended that he be reemployed, the feeling being that he had learned his lesson and would not again commit such an offense. This recommendation was also accepted, and both men have continued to be satisfactory employees.

It seems to me improbable that cases of this character could be dealt with equally satisfactorily in any other way. Experience shows that the appeal board can be depended on to deal with strict justice and will not favor workers who are discharged for good reasons. It makes the workers feel that their interests are in safe hands of their own appointing, and in cases like those of the two men described, it makes it possible for the company to deal more leniently than it could without such an agency, because without the work of the appeal board there would be a danger that leniency would be mistaken for slackness. The appeal board is also an influence in making foremen and others who wish to lay off men for cause very careful to be sure that they have good grounds for doing so.

Educational plan committee: This committee presented a plan for helping employees who were endeavoring to improve their education out of working hours. It was cordially accepted by the management, because its own earlier efforts in this direction, through classes in mathematics, shop practice, etc., had not worked out satisfactorily. The council committee supervises the employees' educational efforts, and the company pays one-half of the cost of evening courses, correspondence courses, etc., for such employees as the committee certifies to have done satisfactory work. This plan was put into effect in 1928, and since then employees have received such compensation amounting in total to $4,257.

Time study committee: This committee was appointed at the suggestion of the management, because we want to make sure that nothing that is unreasonable or unfair to the workers shall be introduced as a result of time and motion study. The committee has made helpful suggestions, and as a result of its work and the general plant attitude of cordial approval of time study, it is expected that we will be able to introduce it in such a way that it will be advantageous both to the company and to the workers.

Cooperation with other employee organizations: In 1927 a plan was inaugurated for annual meeting with representatives of the cooperative associations of three other companies—the Dennison Manufacturing Co., William Filene's Sons, and the Dutchess Bleachery. This was done with the thought that such an association as ours does not have the advantage of broad contacts, and in that particular it is at some possible disadvantage compared with members of trade-unions or with members of employers' organizations which exchange experiences. There have been a few interchanges of meetings, and the thinking of our council has been stimulated by them, but due to the depression, and at the request of one of the other companies, this exchange has been discontinued for the present.

An early experience gave significant evidence of the usefulness and competence of council. Soon after its organization, council appointed a minimum wage and overtime pay committee (since superseded by the permanent committee on wages), and that committee was asked to consider a request, received from a large number of the workers, that the standard number of hours per week be changed from the 48 which we were then working to 44. This was during the war and was an indirect proposal for increasing the rate of pay by increasing overtime. We were actually working about 54 hours per week, and no one thought of working less. Horizontal wage increases were in order in those days, and another one was about due. The management felt that under normal conditions a standard 44-hour week would be satisfactory, and the request was accordingly granted. The armistice was signed shortly afterward, and we received telegrams from numerous Government departments instructing us to stop all overtime work on their orders, and many of them gave instructions that work should be stopped entirely. These orders constituted most of the business in the shop, and consequently we had to cut down at once to the 44-hour week, which made a very severe reduction in the total week's wages. The management asked council for an expression of opinion as to what should be done about it, and in a few days the recommendation was made that (1) 10 percent of our force should be dispensed with, partly because so large a force would not be needed, and partly because at least that much of the force was not well adapted to our work; (2) that the shop work not over 44 hours per week; (3) that the workers who remained with us have their rate of pay increased 10 percent, a partial compensation for the reduced number of hours. We were much pleased with these recommendations, promptly put them into effect, and found that they met the situation satisfactorily.

However, the record of the cooperative association is not one of unmixed success. Its earlier years of accomplishment were followed by an unsatisfactory period. This was in the depression of 1921–22. Our management, preoccupied with difficult business situations, acted more summarily than it should have done in wage reductions, lay-off, etc. Council, jealous of its prerogatives, which it felt had been infringed, became sulky and inactive and lost standing with the people. From this experience we learned that we must not expect to get consultation and advice from council unless we continuously have a receptive attitude toward it and always treat it with the respect which it deserves. When compliance to its recommendations or requests is not considered advisable, the reasons must be made clear and the whole subject thoroughly canvassed by joint committees which will earnestly seek a mutually satisfactory adjustment. Guided by this experience, council and management have since achieved a good degree of mutual understanding, which has resulted in years of harmonious cooperation on many problems—some of them quite important.

The entire history of the cooperative association reveals an impressive record of accomplishment. Other devices, such as highly developed personnel department, might have been employed for the same ends, but I believe that no plan less democratic would have been equally successful or would have resulted in an organization that is so well knit together and permeated by good will as is ours.

Security and status for workers, which will allow reasonable peace of mind and self-respect without destroying incentive and sapping morale, are two desiderata which our industrial system does not provide as fully as would be desirable. The devices now to be described aim to do this.

Not only in such times as these does the threat of unemployment prey on the workers' peace of mind. To mitigate this element of insecurity, our plan for unemployment benefits was inaugurated.

When the 1921 depression struck the country, we were caught with large inventories and were forced to make a considerable reduction in personnel. Conversations with some of our people dismissed then showed how serious a crisis we were bringing into their lives. The social harm that comes from sudden interruption of employment became very clear.

In 1923, we inaugurated an unemployment benefit fund, with an initial deposit of $5,000, and arranged to contribute to the fund 2 percent of each pay roll until the total should equal twice the largest pay roll of any week in the previous 12 months. It was estimated that such a fund, when fully accumulated, would be adequate to pay what we thought were suitable retiring allowances to as many as were likely to be laid off or have their working time reduced. We placed the fund with a trust company under a trust agreement for this particular purpose, so that it would not be subject to the hazards of the business.

Realizing that unemployment compensation was at best only a palliative and not nearly so desirable as continuous work, we also adopted measures to stabilize employment. When business is brisk we increase our working hours, paying time and a half for overtime. When work slackens we drop back to the standard week. This procedure avoids the necessity of taking on, during peak periods, employees whom we should have to lay off later, and in the overtime pay we share prosperity with our employees. During slack periods we manufacture for stock, insofar as there is sufficiently stable demand for certain items to justify this practice. We also carry on research to develop new apparatus and new uses for present products, on a scale that is large in proportion to the size of our business.

We invited council to assume chief responsibility for the management and disbursement of the unemployment benefit fund, explaining that the benefits would be paid only up to the amount of the fund as accumulated, and that we undertook no obligation beyond that. The council willingly assented and decided upon the following working agreement for administering the fund:

Control of the fund is vested in a committee of five members, of whom three are appointed by the council and two by management.

Only employees whose annual compensation is $2,600 or less will be eligible for unemployment benefits.

Unemployment benefits are to be at the rate of 75 percent of wages for those having dependents and 50 percent for those without dependents.

Unemployment benefits are to be paid to those discharged, laid off, or working less than the regular 44-hour week. Those discharged for cause do not benefit from the fund, but may contest such discharge before the appeal board.

Duration of benefit payments is regulated by length of service and ranges from 3 weeks for 3 months' service to 26 weeks for those who have served 5 years. In general, each year of service adds 5 weeks of compensation.

Those who work on a reduced schedule are compensated for the time lost in the same proportion as those who lose full time.

Benefits cease if the recipient gets another job, but may be reinstated if he loses or leaves that job and has not yet received all payments due him.

By January 1930, contributions of $68,000 by the company, with interest accumulations, brought the fund up to $82,000, the required maximum. Prior to 1930, demands on it had been small. Since then separation allowances have been paid to 168 people and 502 have received compensation on account of part time. Under the rules, $41,775 has been paid, and an additional $8,600 will be necessary if the prosent rate of part-time operation continues. With allowance for interest, not much more than half the fund will be needed to meet demands so far incurred, leaving nearly $40,000 to be used for further reductions in force or working hours, which it now seems will be necessary. Of the employees eligible for benefits, 36 percent who were completely laid off found new jobs before their benefits ceased (a good record under existing conditions), while 55 percent did not succeed in obtaining employment before their benefits ran out. The remainder, about 9 percent did not apply for benefits.

The council keeps in touch with those whose benefit payments have expired and who have not yet found other work, and provision is being made for them through loans or gifts from a separate fund created by those who have been fortunate enough to remain on full pay. Only 18 applications for such loans have been received, and these were for small amounts each week. There will probably be more applications if the depression continues unabated for many months. We intend to keep in close touch with all who are on part time or are entirely separated from the company, and when the depression is over, a review and analysis of our experience may suggest certain desirable amendments to our plan.

Old age without income is another threat of insecurity that preys on the minds of workers of advancing years. At the request of council this subject was taken up in 1926, and a joint committee, on which council members predominated, worked on it assiduously for many months, finally reporting a plan of old-age retirement allowances, which was approved and put into operation in 1927. Under this plan the company purchases from the Metropolitan Life Insurance Co. and keeps paid up, policies for all employees of 5 years' service and over, which, on retirement of men at 70 years of age and of women at 65, will give an annual income of 1 percent of their total salary during service. If employees elect to cooperate by paying 4 percent of salary, the company doubles its contribution. Thus, a nonparticipating employee with 40 years of service and an average salary of $1,500 would have received a total of $60,000 and get $600 per year for the rest of his life. If he had participated, he would receive double this amount from the company's contributions and something like half as much more than his own—a total of about $1,800. When the plan was inaugurated, the company paid up all the amounts for its employees of 5 years' standing necessary to bring the insurance up to date, and did this on the 2-percent basis.

This plan is not a bar to the employment of older men because the pension cost to the company depends on the total wages paid during employment. Such men who work with the company only a few years before retirement will naturally receive smaller pensions than those who retire on equal wages, but have worked a longer period. Experience with this plan has been quite limited. Only one man is receiving a pension. It is hoped that many can be kept on the pay roll beyond the specified retirement age because it is believed that generally people will be happier with regular employment than retired with little to do. It has been found that few of the younger men and women take advantage of the contributory feature, although it would be much to their advantage to do so. The problems of old age are too remote to interest them. Those who leave the company before retirement age may at their option have any money that they have paid in refunded or get the equivalent in an annuity policy.

Sick benefits, life insurance, and loans: A sick-benefit association, originally organized in 1917 by the employees, has had a successful and useful career. Its funds are accumulated from dues and from them it pays sick benefits and makes loans to members. With the cooperation of the company, it provides group life insurance for its members, which pays at death $500 for those of less than 1 year of service and larger amounts for longer service up to a maximum of $1,500 for 10 years. About 80 percent of the employees are members.

Wages: Wages are perhaps the most fundamental element of right relations in industry. The general policy of wage payments was worked out with the council's committee on wages. We have as yet no piece-rate payments, but careful cost records are kept on each job and compared with standards. Each worker is reviewed once in 3 months, and those whose cost records justify it are promoted. An extensive study of the adequacy of wages paid to meet living requirements has recently been made and indicates that for the great majority they are safely above the health and decency standard cost of living.

Among minor agencies through which it is aimed to administer to the workers' comfort and self-respect may be mentioned well lighted and comfortable work places, well-appointed toilet and wash rooms, and comfortable rest rooms. Workers paid on the hourly basis are given vacations and holidays with pay as their length of service increases; those of 9½ years' service are paid during two weeks' vacation and for eight regular plant holidays.

Much effort is made to carry out that part of Plato's definition which calls for a man to be in just the right place, doing the work for which he is most fit, difficult as it is, particularly in a growing and changing organization. Every encouragement is given to employees to qualify themselves for advancement, and so far as possible higher positions are filled by promotion from within, so that we may keep open the opportunity for each to rise to that level of power and reward for which he is qualified.

The Forbes announcement calls for a showing of economic and other advantages to the company accruing from its employee plans. I am perhaps too close to the scene to appraise these. Our company has achieved a good measure of success, but so have many others who have no such plans. I believe, nevertheless, that part at least of that success can be ascribed directly to the loyal and intelligent cooperation of our entire personnel, which is one of the fruits of these plans. I believe that we have an unusual esprit de corps throughout the organization and that difficult and complicated work can be and continuously is being carried on with unusually little strain on the higher executives.

Now, our bonus system is an evolution. It started with a small group and 2 years ago was extended to include practically the entire plant, and if you are interested in a detailed story of that scheme I can again possibly give it by quoting from another paper of Mr. Leeds.

Senator HERRING. We might possibly put that in as an exhibit, unless you can sketch it briefly to us.

Mr. REDDING. You already have a copy of the paper. It was a paper presented to the Seventh International Management Congress in 1938. This bonus plan started many years ago—during 1910—and it was confined to a very few of the upper executives of the company, maybe four or five. The original plan, as is commonly done, was based on individual effort. Two of us in the sales department had one type of bonus plan, the man in charge of manufacture another based on savings in costs, and so forth.

That worked fairly well for a while, and it was modified from time to time, but during the war days, when there was a pressing demand for instruments, the business grew very rapidly, and those bonuses grew out of all reasonable proportion from what anyone conceived

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them to be worth; they grew out of reason. The plan was then changed. It was at that time that the idea of group incentive came in as against the individual incentive. The later plans have all been based upon a common pool in which participants share, the measure of that pool being the gross profit to which all by their combined efforts are supposed to contribute.

Senator HERRING. All the employees there?

Mr. REDDING. All sharing in the benefits of the plan are supposed to be working toward increasing the gross profits of the company as against working for their own individual bonus, without respect to what the other fellow gets. It is entirely a credit and cooperative plan whereby everybody is working toward the same end; that is, increasing the gross profits of the company.

That plan was, until about 1923, confined to comparatively few, those in the upper group of the organization, known as the executive committee, but about that time it was decided by that group that it had been so effective in that group that perhaps we might get more results by spreading the group out, and that was done, including the number of executives down the line, and that has expanded until at the latest report I think we had 105 altogether in that preliminary bonus group. I call it a preliminary bonus group because it had not yet come to the extent of going down into the entire organization. That group was made up, roughly, half and half between the sales department and the inside department, as we call it, the manufacturing department. That group of people is divided generally into two groups, the sales group and manufacturing group.

I want to deal for a while on the manufacturing group, because it is the one with which I am closely affiliated. That manufacturing group, right from its inception, practically, has been divided into subgroups. People have held their position in those groups, depending upon the position they held for their ability, and so forth, and the participation of individuals in the general bonus fund is based upon their position in these subgroups, and the higher up in the subgrouping you find yourself the greater your participation in the general bonus fund, on the basis that the higher up in that group you go the more your responsibilities are and the more you are entitled to share in this extra compensation.

It is very interesting to note that right at the very beginning of that inside bonus group—I use that term because it is the one I am familiar with—that group of people decided, entirely on their initiative and at their own expense, to get together once a month in a meeting nearby, in a club, for final discussion of company affairs. That has continued from that day to this, and it is interesting to note that during 5 years of the big depression, when there were no bonuses in sight those meetings kept going just as regularly and just as effectively as they had been going on during the time when the bonuses had been paid.

That, I think, covers in general the general bonus plan. Now, 2 years ago, and I think this would have happened sooner if it had not been for the big depression, because in the 5 years there was not anything to distribute; in 1936 it was decided to extend this bonus plan throughout the whole plant. Of course, there was a time of 9 months, or something like that, before a new employee could participate, but that scheme has now been extended throughout the whole plant, and everyone, when there is any bonus fund, receives a bonus at the end of the fiscal year. We believe that that is the only proper way for us to do it, to distribute it more even to the profits that are earned. Of course, you cannot share losses. We wait until the end of the fiscal year, and, if there are any profits sufficient to pay the bonuses, they are paid, and they are paid through the whole plant.

Senator HERRING. The amount is determined upon the result for the year?

Mr. REDDING. Yes. I should have said awhile ago that the amount is determined by the gross profits less a fixed return on the equivalent of preferred stock, and less a 6 percent return on the latest value of the equivalent of common shares and after Federal and State income taxes. The remainder is divided between the stockholders and the bonus fund.

Senator HERRING. On the average, how does the bonus compare in comparison with the dividend?

Mr. REDDING. In some years the bonuses have exceeded the dividend. You might say, roughly, it is at least equal to the dividend. Of course, the dividend fluctuates, but the dividend is more fluctuating than the bonus, because we set up each year a fixed bonus plan that carries through, whereas the dividends are at the mercy, or at the discretion, of the board of directors from quarter to quarter.

Senator HERRING. As I understand it, you have had this system for the higher executives for a number of years, but for the entire employees really only for 2 years?

Mr. REDDING. That has only been effective really for a year and a half. It was completed and put into effect in December 1936. Our fiscal year ends May 31, so that the first payment of that fund was only a half year's payment. The 1936–37 fiscal year happened to be a relatively good year. There were bonuses paid, and in substantial amounts. The following year was less profitable, and the bonus has decreased, without any complaint of any kind whatever from the people, and this year it appears as though there would not be any bonus.

I might also add that during those 5 years, when no bonuses were paid, I cannot recall a single instance, in connection with the 105 people who were then participating, of complaint or dissatisfaction because the bonus was not there.

Senator HERRING. Because they were not paid?

Mr. REDDING. Because they were not paid.

Senator HERRING. How many employees do you have altogether?

Mr. REDDING. We have now about 940. Our maximum has been about 1,150, I think.

Senator HERRING. Are they organized in any way?

Mr. REDDING. They are organized into their own independent union.

Senator HERRING. You have had no labor trouble?

Mr. REDDING. We have had no labor trouble whatever.

Senator HERRING. Do you think the bonus plan helps in that connection?

Mr. REDDING. With respect to the bonus plan applying to the entire plant, I think it is a little too early to say anything about that yet, but it is one of a great number of things done through a period of years. I have no doubt but that it helps, but as to how much it helps, you cannot tell after only a year's experience.

Senator HERRING. You extended it throughout the entire pay roll, because, in your experience with the executives, you found it paid to have everybody interested in the profit?

Mr. REDDING. We found it paid to have everybody interested in the profit. What we were really interested in, as Mr. Leeds said in that paper, where you need a particular type of people it is of interest to have a continuity of organization, so as to keep a highly qualified group, and it would have the same effect throughout the plant.

Senator HERRING. The amount of the bonus is in no way arrived at through negotiation with the employees, is it?

Mr. REDDING. No; that is one thing we do not do negotiate with employees, although the formation of this last plant wide large bonus group, was discussed with the employees. I do not think the amount of the fund was ever discussed with them. That is a matter for the executives and for the board of directors to decide.

Senator HERRING. I mentioned that, because one or two witnesses indicated they thought profit sharing would be all right if the amount was arrived at through collective bargaining or negotiation with those benefited.

Mr. REDDING. As I said a moment ago, our general bonus fund was set up on a very definite formula, and we assured the people—that is, this new group—that their bonus fund would bear a very definite relation to this other scheme, so that the whole scheme all the way through is subject to a very definite formula, which is the same general formula used from year to year, but which has to be modified in detail from year to year, because every year we have different taxes that have to be reviewed before we arrive at the fund.

There is another thing I would like to put in as a matter of information. Ever since these bonus funds were started, at the end of the third month of the fiscal year and each month thereafter, every participant excluding those in the recent plant wide group, is given a graph from which he can determine his bonus if conditions for the entire year remain the same as the average for the elapsed time. Of course, at the beginning of the fiscal year that figure is very unreliable, but as you approach the end of the year it becomes more and more reliable, so that a man is able to predetermine pretty well what his bonus is going to be as he approaches the end of the year.

That same thing is general in a slightly different form applies with respect to the larger group which was later admitted. There is a notice posted on the bulletin board every month giving a figure which, combined with a particpant's length of service which he or she knows, enables the individual's expected bonus to be determined with the same reservation with regard to the accuracy of the figures in the early months of the year. There has been a little difficulty in getting that across to the people, because at least one person that I have heard of thought when that notice was posted at the end of the month that the money was set aside for that purpose, and it took a little time for them to realize that that figure changes from month to month, as the business conditions change, and it might not be the same at the end of the year as it was at the time it was posted.

Senator HERRING. Unless you have something else that you would like to get into the record, Mr. Redding, I think that is all.

Mr. REDDING. Would you give Mr. Schultz an opportunity to say a few words?

STATEMENT OF D. H. SCHULTZ, LEEDS & NORTHRUP CO., PHILADELPHIA, PA.

Mr. SCHULTZ. Probably you would be interested in a statement as to the relation between the bonus and wages. It has always been our policy, that before bonuses are considered wages should be at least comparable with those in the community, and comparable with those in similar industries throughout the country. Our wage policy may be of interest. Each employee's rate is considered at quarterly intervals, so that no one is forgotten in reference to his activities. Each rate is reviewed by a wages committee, on which his immediate superiors sit.

Recently we have gone to a great deal of time and study in order to define and evaluate positions. In other words, we classify the job, place the man in the job, then notify him how he is classified, what his position is, and the rates that apply. So we have always felt that an employee is entitled to a fair wage before any thought of profit sharing enters in.

While there is the belief, that every employee can contribute something toward the profits of the company—considering the rank and file—it is more particularly a question of sharing prosperity than one of rewarding them for direct contributions to profits.

As to membership in the preliminary group, Mr. Redding mentioned, you will be interested in knowing, that there are qualifications that an entrant must meet, and in his questionnaire he must fill out his whole history. His sponsor has to show that the applicant's position and his work really permit him to make a contribution toward the company's profits. He has got to pay his way definitely in this first group. That is the practice that has always been maintained. Where the man stands in the group, as a matter of fact, is determined not by the company but by the remainder of the fellows in the group.

Mr. REDDING. I would like to enlarge on that point a little bit, because it is a thing I should have touched on. Mr. Schultz has covered it in general. While the executive committee of the company retains the final say as to who participates in these bonus funds, that applies to the upper group and not the lower group, because that is more or less automatic, and it depends on the relative position of the people in the group. A committee of five from the bonus group is appointed every year, and it calls a meeting, at which the executives are not invited, and that group makes a careful examination of that whole plan which Mr. Schultz refers to, and makes a recommendation as to the new entrants into the group, but they may, from their own, pay their own way; that is, by contributing a better effort.

Senator HERRING. That is the bonus group of about 100?

Mr. REDDING. This is the inside group of 50. The salesmen come on more or less automatically. They make recommendations as to shifts up and down or out. Those recommendations are made to the executive committee, and in 9 cases out of 10 are wholly accepted by the executive committee, and are made the order of the day.

Excuse me for interrupting you, Mr. Schultz.

Mr. SCHULTZ. That is perfectly all right. I have just one more point that I would like to make. The company has entertained representation from its employees for many years through what most companies would call a works council, where the employees are represented, that these things, such as the profit sharing and employee welfare plans are not the result of something which has been handed down, as emanating from management, but rather something which has grown up either spontaneously by cooperative effort or, as in many cases, insisted upon by the employees. It has been done through their collective bargaining arrangements. That has been done aside from any union formation. Even the profit-sharing plan was designed by the employees, except for the amount of the share of the profits which they should receive. The distribution of it is entirely up to the employee, and is based on service on the one hand and normal wages on the other.

Senator HERRING. Thank you, Mr. Redding; and thank you, Mr. Schultz.

We will next hear from Mr. Frederick E. Macy, of the Collins Manufacturing Co.

STATEMENT OF FREDERICK E. MACY, A. M. COLLINS MANUFACTURING CO., PHILADELPHIA, PA.

Senator HERRING. Mr. Macy, we do not seem to have a schedule here. Do you have a profit-sharing plan, or a bonus plan?

Mr. MACY. We are establishing, as of the 1st of January, a bonus or profit-sharing plan which we feel—that is, the directors and I feel—will be very satisfactory.

Senator HERRING. What is the A. M. Collins Manufacturing Co.?

Mr. MACY. The A. M. Collins Manufacturing Co. makes very high-grade papers, mostly for advertising purposes, and also another line that is used for shipping tags, and so on.

Senator HERRING. How many employees do you have, approximately?

Mr. MACY. We have about 125. It is a very old company. The workers are more or less artisans; they are a little different than the common-labor type. Our average is, I think, about 25 or 30 years with the plant.

I was put in there to manage the plant about 2 years ago, and I feel, and always have felt, that the worker is entitled to some share of the profits of the organization, but the cost of supervision of the workers and the mistakes they make is what costs us money; that is where we take our losses; and what I have endeavored to work out and get by the directors was a plan which would reflect the cost of their mistakes.

So we have established our even point, where we make money or lose money; we have established a figure somewhat above that, and, contingent upon our shipping beyond that point each month, we will pay the men 5-percent bonus. Then it is on a graduated scale upwards. So that for each 10 percent in additional shipments during the month we give them an additional 2½-percent bonus.

Senator HERRING. Above their wages?

Mr. MACY. Above their wages. We feel that will adequately impress itself upon the men, and it will be accepted in a good spirit throughout the whole plant—everybody will share in it. It does not matter whether he is the wash-up man, the man on the cutting machines, or anyone else, they will all share in it, and, therefore, we feel it will make each worker not only watch his own work but watch the work of the other departments, and if one department falls down it will certainly be open to criticism to the other departments that they are continually making mistakes.

Senator HERRING. Your men are largely skilled?

Mr. MACY. Yes, sir.

Senator HERRING. Do they belong to a union?

Mr. MACY. No; we have no union, we never have had, and I do not believe that they would care to join. They are very well satisfied. I found our help was more interested in a continuous and steady employment than they were in a little extra wages, in a little higher rate, and what I tried to do all the way through the last 2 years, the trying years, was to spread the work out. Our main problem was continuous employment this year. I do not think they had more than 1 or 2 days off during the month all the way through.

Senator HERRING. Your wage base is equal, though, to the union scale?

Mr. MACY. Yes, we are on a comparable basis with any other plant in our territory. We are very conscious of the fact that our men are on the average older, they have reached almost the age limit, and for that reason they are constantly worried about being thrown out of work; and we try to see that they are taken care of, and personally, in my own hiring, I prefer men over 45, or quite a young chap. We are always trying to break men in, to teach them a particular trade which requires a rather high degree of skill.

Senator HERRING. Your plan is a cash bonus that is paid, and it does not provide for any security in the future?

Mr. MACY. It is paid absolutely on the cash basis.

There is another point I brought up with your committee through Mr. Despain here, in which he was rather interested, and that was the question of incentive taxation to increase employment. I have received considerable comment on it from people around, and especially from Mr. Despain and some of the committee. I would like to read it to you. It will not take more than a minute.

Senator HERRING. All right.

Mr. MACY. Any man charged with the responsibility of managing a business during the last few years cannot fail to be moved by the plight of the help he has been compelled to lay off or discharge. Competition, improvements in processes, the search for lower costs, poor business, all have helped to swell the stream of workers leaving the plant for the last time.

Today we have the awful specter of 13 million or more unemployed, and the realization that even were business good, we shall never be able to employ them all again.

For years the search in management has been for labor saving; i. e., labor-eliminating machinery. This has resulted in the building of new continuous packaging and machining devices, all designed to give lower costs and cut down the number of men employed in a mill. The more successful the machine or process, the keener the search for improvements or combinations of these machines. Even the farmer has been favored with new equipment, combines, and so forth.

Less progressive companies who have tried to get along with outmoded equipment have found themselves unable to compete with up-to-date competitors. With the advent of the New Deal in 1932 and and the stream of legislation on labor, working conditions, and new tax laws the situation is becoming steadily worse. The attitude of labor, with its demand for shorter hours and higher pay, has also contributed a great deal to make a bad situation worse. The mill manager or business employer, and the unemployed, have a great deal in common if they only realized it. There is a vicious circle around them. The manager, hampered by steadily rising costs and taxes, puts in new machinery to eliminate some labor; men are laid off whom the Government has to help with unemployed insurance and relief and, therefore, the taxes on the manufacturing plant are raised, added to which there are additional families with diminished purchasing power to buy the products of the factory.

Nothing that the Government has done so far has had any tendency to counteract this condition. There must be a solution. Here is my suggestion:

No businessman is going to hire extra help unless it is profitable to him. Let's make it profitable to him. Suppose we pass a law that from his net taxable income he be allowed to deduct $5,000 for each employee on his pay roll during the full year over and above the average for the last 5 years. Wouldn't this fix the mind of a manager on the savings to be obtained by employing extra help? If a plant estimates it will have a net taxable of $50,000, it could eliminate its corporation tax entirely by employing 10 extra men for a full year. Its corporation tax would probably be around $20,000, so that by paying, say, $15,000 for extra help, $5,000 could be saved. The Government would be helped, too, for the cost of relief and administering relief for 10 unemployed must run close to $12,000 for a year, especially the men that are heads of families. There is another angle to this idea. The men who would be hired first would probably be used for odd jobs and nonessential work around a plant, and we all know that the unskilled laborer and the man over 45 form a large portion of the unemployed surplus.

The problem of administering such a law would not be difficult; factory and business pay rolls are available to check with Social Security information. The relief administration would be available to help with a far happier job.

Possibly the exemption would have to be lowered or raised slightly in the cases of larger establishments. The principle remains the same, and should also be applied to farmers operating on a large scale, for we also have unemployed agricultural workers.

Unless something really drastic is done to turn businessmen's minds toward employing men in their establishments, there is little hope for the unskilled and less for the middle aged. My suggestion comes after observing trends in manufacturing plants over a number of years. As a plant executive, I have seen many good men laid off or jobs eliminated entirely during recent years. Something should be done about it. No relief—no self-respecting man wants relief. With a law such as I suggest, the old custom of hiring apprentices could be revived. All managers know of the scarcity of skilled help and how few young men are being trained to trades today. The trade-unions could help with a better attitude on this question. Eventually they would have a larger membership of men who would owe their better standard of living to a more enlightened stand on the part of Government, management, and labor. What do you think?

I worked this out originally for E. P. Mathewson, who was head of Anaconda Copper and the International Nickel Corporation, and since then I have taken it up with a large number of my friends in industry, and I have had very little criticism. I also put it up to our banks, and I was surprised to find that they would not criticize it severely.

Senator HERRING. You make the statement that no employer would employ additional men unless he could make a profit from them?

Mr. MACY. Certainly.

Senator HERRING. That is, of course, true. I was wondering what effect your plan would have upon the man who could not employ additional men because of the conditions of his business. He could not get the benefit, whereas the man who was more prosperous and who was better able to pay the tax would be able to employ more men, and therefore it seems he would be relieved of the tax. It would seem that you would penalize the man who needs it most.

Mr. MACY. As we pick up the unemployed, do not we produce better conditions in the country?

Senator HERRING. I hope so.

Mr. MACY. Certainly. The average man who is on relief today does not like to be on relief; he wants a job.

Senator HERRING. That is true.

Mr. MACY. If we can pick them up and make them profitable to them, so much better for all. In my own case, on the basis of my own estimate, I can pick up for the next year 10 or 15 men. I would use them around the plant in various ways; I would keep them busy, and it would be good business for me to do it.

Senator HERRING. I am not quarreling with that suggestion, but the thing that puzzles me is, perhaps, the benefit that would go to the man who needs it least.

Mr. MACY. Well, most plants are either operating at a profit or hoping to operate at a profit. The question that was brought up to me rather forcibly was the question of the sacrifice of income that the Government would take, but my plan provides that they have got to be employed a full year before they can take this amount from their taxable income, so the load would be taken off the Government a full year before they would lose the income.

Senator HERRING. Do you have anything else you would like to put in?

Mr. MACY. No, sir.

Senator HERRING. Thank you very much, Mr. Macy.

We have tomorrow morning at 10 o'clock Mr. McNear, a railroad president, whose bonus plan is making money, and he is not borrowing money from the R. F. C., so it ought to be quite interesting. We will recess until 10 o'clock tomorrow morning.

(Whereupon, at 11:45 a. m., a recess was taken until the following day, Wednesday, December 14, 1938, at 10 a. m.)

SURVEY OF EXPERIENCES IN PROFIT SHARING AND POSSIBILITIES OF INCENTIVE TAXATION

WEDNESDAY, DECEMBER 14, 1938

UNITED STATES SENATE,
SUBCOMMITTEE OF THE COMMITTEE ON FINANCE,
Washington, D. C.

The committee met, pursuant to adjournment, at 10 a. m., in room 312, Senate Office Building, Senator Clyde L. Herring presiding.

Present: Senators Clyde L. Herring and Arthur H. Vandenberg.

Senator HERRING. The committee will be in order. We will hear this morning from Mr. George P. McNear, Jr., president of Toledo, Peoria & Western Railroad.

STATEMENT OF GEORGE P. McNEAR, JR., PRESIDENT, TOLEDO, PEORIA & WESTERN RAILROAD

Senator HERRING. Mr. McNear, you might give us information as to the location of the railroad, the mileage, number of employees, and so forth.

Mr. McNEAR. The Toledo, Peoria & Western Railroad is located practically entirely in the State of Illinois, running east and west across Illinois through Peoria. The mileage owned is approximately 230, and the mileage operated is 239. It is a small railroad and a small business.

Senator HERRING. And how many employees do you have, approximately?

Mr. McNEAR. About 600. We run from 600 to 700 employees.

Senator HERRING. How long have you operated the railroad?

Mr. McNEAR. I have operated the railroad since the summer of 1926. At that time the predecessor company, the Toledo, Peoria & Western Railway Co., was in receivership and was sold at a foreclosure sale. The old company had been in receivership since July 1917. It had been owned largely by the Pennsylvania and Burlington Railroad companies, who had bought into this old company in 1893.

Senator HERRING. The stock is pretty closely held?

Mr. McNEAR. Now?

Senator HERRING. The present ownership.

Mr. McNEAR. Oh, yes, sir. The stock is held indirectly by me and by a New York bank; there is a small amount held by the bank.

Senator HERRING. There is a small indebtedness?

Mr. McNEAR. Yes. We have a total funded debt of about $1,600,000 in first-mortgage bonds.

Senator HERRING. None from the R. F. C.?

Mr. McNEAR. No; we have never borrowed any money from the R. F. C., or any other governmental agency, and have only borrowed from banks twice in the period from 1927 down to date, and those two loans were for comparatively small amounts and for about 45 days.

Senator HERRING. Well, your situation is unique in that you seem to be operating at a profit and you have a bonus plan, which is a little unusual in a regulated industry. Just tell us about your whole operation, will you please?

Mr. McNEAR. As I have just mentioned, this is a small railroad. When we arranged our original financing and tried to sell our first-mortgage 6-percent bonds that we put out in 1927 we had great difficulty. The average investor would say that a road like ours was a pretty risky investment, particularly with the kind of a past it had, and so we adopted the policy that we had to operate at a profit, and we have done that right along. Our whole policy is, we must run our own business and operate at a profit.

Senator HERRING. It is largely a freight railroad, is it?

Mr. McNEAR. Yes. In the old days a large proportion of T. P. & W. revenues came from passenger business, but since the advent of the private automobile, the passenger business disappeared, and we now do practically entirely a freight business. Our business is made up, to a large extent, of what we call overhead traffic. The T. P. & W. lies in between the eastern and western lines, and we serve as a little intermediate line connecting the large east and west lines. We have a certain amount of local business that we originate and terminate as well.

Senator HERRING. Well, you pay each year a dividend on the outstanding obligations, the bonds and stocks?

Mr. McNEAR. We have always earned the interest on our bonds. We started out with $1,000,000 of first-mortgage 6's, and then we got permission to issue a half million additional 6's, and then, in 1937, the early part of 1937, we refunded the first-mortgage 6's with first-mortgage 4's. We have always paid our interest. Beginning in 1936 we started paying dividends on our capital stock. Up to that time there had been no dividends paid. All of the surplus earnings were put back into the property. The reason why we started to pay dividends in 1936 was because of the tax on undistributed profits.

I might say in this connection, if it is of any interest, that this little railroad has been built up in the manner that it has largely through the reinvestment of surplus earnings. As I have mentioned, we could not sell securities in the early years; we had to get along on what we made.

I might point out, in passing, that I do not believe a job like this, if it is worth anything, could be done today under existing laws. You see, the financing of this purchase, in the first place, had to be done through a bank loan. At the time of the sale the decree provided that the purchaser had to put down 5 percent of his bid to have his bid accepted. My bid at the sale was $1,300,000, and 5 percent of that figure took all of the money that I had and could borrow at the moment. In order to have the sale confirmed, it took 5 percent more, and I borrowed that money from my father. So at the moment that left the 90 percent to be raised at the end of 4 months, which period we were able to obtain to meet the balance due. The only way that money could be raised was by a bank loan. The bank who loaned us the money naturally did not want to get into the limelight at that time, so it was necessary to form a personal holding company. The way things are going now I do not believe that personal holding companies are very popular, but that is the only way we could do the job. Of course, now we are trying to find some way of getting rid of these holding companies without paying an excessive tax, and I guess we will have to work it out sometime. I mean, with the kind of a feeling that is in vogue now against personal holding companies, it would make it, as I say, almost impossible to do this kind of a job now. If it had not been done, a large portion of this railroad would have been abandoned, because at the time of the sale there was no bid for the entire property except the one that I had made. The railroads that had owned the T. P. & W. said in open court that they might bid for portions of the railroad but not for it as an entirety. It had been offered in 1925 as an entirety, and there was no bid.

Senator HERRING. How much would you estimate the total amount of profits were plowed back into the property before the undistributed-profits tax compelled you to change that policy?

Mr. MCNEAR. At the end of 1936 our surplus account was approximately $1,600,000. That had all been accumulated in 10 years. In the year 1936 we had a net income of $273,000, and we paid a dividend of $75.000, and, of course, had to pay a very substantial tax. We had to pay a tax of $61,000 on the net income that we left in the business, however, it did not seem to me that we ought to jeopardize the working capital of the company merely to save the tax, so we declared out only about one-third of our net income and paid the tax on what was left.

Senator VANDENBERG. What was your gross income?

Mr. MCNEAR. Our gross revenues, you mean?

Senator VANDENBERG. Yes.

Mr. MCNEAR. In the year 1936 our total revenues were $2,424,000.

Senator VANDENBERG. How did it happen you could run in black ink when every other railroad is running in red ink? Have you got a secret of some sort that you would like to cut loose of?

Mr. MCNEAR. As I say, Senator, we insisted on running our own business and running it at a profit.

Senator VANDENBERG. How can you do that in the railroad business? I am sure every railroad would like to find that out.

Mr. MCNEAR. I really think that you can do it if you want to.

Senator VANDENBERG. Are not you under the same restrictions with the I. C. C. that other railroads are?

Mr. MCNEAR. Yes, sir.

Senator VANDENBERG. And do not you deal with brotherhoods the same as other railroads do?

Mr. MCNEAR. Not quite to the same extent; no, sir. In 1929 there was a strike on our railroad due to the fact, as these brotherhood leaders told me, that they wanted to get the shop crafts back on the different railroads. You remember at the time of the shopmen's strike in 1922 a great many railroads were relieved of the burdens that had been imposed upon them by these different shop-craft organizations under the A. F. of L. I was told by one of these labor leaders that the Big Four brotherhoods wanted to get a certain man appointed as Secretary of Labor, and that to obtain A. F. of L. support for that objective the idea was for the Big Four brotherhoods to help get the A. F. of L. shop crafts back on the railroads. And so these operating brotherhoods were endeavoring to use such influence as they could with the railroads to bring that about. They said they had accomplished that purpose on one or two other railroads, and came down to our railroad in 1929 and said we were going to have to begin to do business with these A. F. of L. unions. We told these brotherhoods that we were perfectly willing to talk to them about matters that pertained to them, but not about something else. The upshot of the whole matter was, they decided to call a strike. The theory of that strike, as it was also explained to me by these brotherhood officials, was that their theory now was to have concerted movement strikes on one railroad and just put that railroad out of business. They figured that inasmuch as the shopmen's strike, and those other strikes where there was a Nation-wide movement—did not succeed, they now were going to have the concerted movement on one railroad and put that railroad out of business, and then they would not have much difficulty. But we managed to get along, and since that time we have not dealt with any of these national labor organizations except the Brotherhood of Locomotive Engineers.

The engineers had a contract with us and did not go out on strike, but all the others did. So, after that, the employees on our own railroad formed their own associations. We do not have any control over what those associations do. They are just as hard to deal with at times as some national organization might be, but they are the organizations with which we deal at the present time.

Senator VANDENBERG. You pay the same wage rate as if you were under one of the national organizations?

Mr. McNEAR. No; we did not grant the increases that were made in 1937, in the fall of 1937. Up to that time we were fairly closely in line, but when that national committee was formed to negotiate in behalf of a great many railroads we did not give it our power of attorney. After the decision was reached with respect to the nonoperating brotherhoods, you will perhaps recall that some of the railroads immediately proceeded to lay off a lot of men; and so when our people asked for a corresponding increase our management said, "Would you like to have what happened on these other railroads?" And they said, "No." So we did not make any increase and did not cut down on our employment.

Senator HERRING. Did you have a bonus plan then, Mr. McNear?

Mr. McNEAR. Yes.

Senator HERRING. How long have you had it?

Mr. McNEAR. Of course, I would not say it is a definite bonus plan. Shortly before Christmas in 1936 we gave additional compensation amounting to 1 week's average earnings, based upon the first 10 months of the year, to our people. We did it again in 1937.

To continue, if I may, about our wage rates, when the operating brotherhoods' increase came out in the early part of October, we were approached by the men in those organizations wanting a corresponding increase, and our people told them that they would be glad to consider it if the employees in those organizations would make themselves worth more. By that I mean that there would be some changes in the rules in working conditions. Incidentally, I think that is the most important subject that anybody could get into, would be the rules and working conditions on the railroads. At any rate nothing was done about changes in our rules and working conditions so we did not make the increases made by the others and since that time we have not made the same payments. On the other hand, when the notice came out this year for a 15 percent reduction in pay, we did not serve any notice for reductions.

Senator HERRING. Well, do you think that by keeping all the men at work, and this little bonus which really brought them up to about the same wage as they were being paid on other railroads, that that prevented trouble?

Mr. McNEAR. Well, I do not know what you mean by "trouble." I think that is a relative term. In other words, I think that a man could, or a group of people could, be made to be dissatisfied, no matter how much they were getting. If you have people around who are bent upon making trouble, I think you will find yourself in trouble no matter what you do.

Senator HERRING. Well, I referred to their demand for the same pay that other roads were paying.

Mr. McNEAR. Well, of course, there is a little difference in our railroad, and that is this: Our average compensation per employee per annum is not so bad. According to the Interstate Commerce Commission statistics for the year 1936 class I railroads, of which we are one—

Senator HERRING (interposing). You are one of the class I railroads?

Mr. McNEAR. Yes; we are, our revenues being over $1,000,000. That is the dividing line. We are just over the line. In average annual compensation paid per employee, we stood sixty-third out of a list of 126. Our compensation per employee per annum for 1936, according to the Interstate Commerce Commission figures was $1,682.

Senator HERRING. That applies to all employees?

Mr. McNEAR. Yes, sir.

Senator HERRING. That takes in all employees?

Mr. McNEAR. All employees; yes, sir.

Now that amount exceeded the average compensation per employee per annum paid by such railroads as the Missouri Pacific, the Milwaukee, the Delaware, Lackawanna & Western, the Norfolk & Western, the Louisville & Nashville, the Illinois Terminal, the Reading Co., and many others. In other words, what we endeavored to do was to permit our people to work and not restrict the hours that they can work.

Senator HERRING. Were you paying time and a half overtime?

Mr. McNEAR. Oh, yes. We have the basic day, the 100-mile basic day, and time and a half for overtime, and all that. The only thing is that our basic rate in train-and-engine service is not as high as it is on some of the other railroads, but we do not restrict the number of miles or the number of hours that a train or engine man can work in a month.

Senator HERRING. I see.

Mr. McNEAR. Of course, you take in our shop organizations, I guess our shopmen get just about as much as the shopmen on the other roads do, and I think our clerks and people in those capacities get about the same.

There is another thing we have always done. We have never reduced the wages of the unorganized employees in order to pay increases to what you might call the highly organized groups. We go on the theory that everybody is entitled to consideration whether they are highly organized or not. We have so much to go around, and it seems to us that the employer who does not have anybody speaking for him is entitled to just as much consideration as someone who has some grand lodge officer to come in and talk for him.

Senator VANDENBERG. How much does the week's bonus cost you?

Mr. McNEAR. About $16,000.

Senator HERRING. Are your rolling stock and locomotives up in condition?

Mr. McNEAR. Well, I would say that they were. In our line of business we do not have a great deal of need for a lot of freight cars, because so much of our business is an overhead business that is received from our connections. It would not pay us to have our own freight cars. If we did, we would find that we did not have them in times of great shortage, and in times when there was not any great demand for cars we would just find them setting around doing nothing.

Our locomotives are in pretty fair shape. We bought six new locomotives in the early part of 1937, of the most modern design, and they cost us about a half million dollars. We bought them on open account from the American Locomotive Co. and finished paying for them this year.

Senator HERRING. Judge Fletcher mentioned that equipment on all railroads is far below standard, and many hundreds of millions of dollars would be necessary to rehabilitate the equipment. That is why I asked you the question. You have been able to keep your equipment up and still pay the interest on your bonds and dividends, and a little more?

Mr. McNEAR. I do not believe there is any question but that the railroad plant of the country as a whole has become deteriorated. There are things that we would do in the way of putting in heavier rail and making greater expenditures for curve and grade reductions and other maintenance work and improvement work if we felt we had a little more confidence. Of course, in this particular year we have been using what funds we could to pay off the debt on the locomotives. We try to pay our bills.

Senator VANDENBERG. Were you in the railroad business before you bought this line?

Mr. McNEAR. No, sir; I was in the investment-banking business in New York.

Senator VANDENBERG. Well, they railroaded quite a few things, speaking generally and not personally.

Mr. McNEAR. No; I had no experience in operating a railroad before the foreclosure sale in 1926.

Senator HERRING. Do you think that accounts for your success?

Mr. McNEAR. No; I would not say so. I think that the engineering training that I got while I was in college, and before the war, and the financial training that I got in Wall Street, was of great value to me in running this railroad, but, as I said before, the fundamental policy that we have had right from the start was that we had to operate for a profit. There was nobody who was going to give us a lift; we just had to make it on our own.

Senator HERRING. No rich uncles?

Mr. MCNEAR. No, sir.

Senator VANDENBERG. Including Uncle Sam.

Mr. MCNEAR. You may remember in that connection, the Government had a program for buying a lot of rail—I think it was in 1933—and they wanted to know if we would buy a lot of rail, and I said, "All right, we will buy that rail." That was, I think, on the basis that you could get a 10-year loan with interest waived the first year. I think that was 4-percent money, so, with the interest waived for the first year, that made the average interest charge of 3.6 percent. I said we would buy. I did not recall how many thousand tons we would buy; provided there were no strings attached, but by the time we saw the contract that was prepared by the R. F. C., or some other organization down there, it had so many provisions in it that I figured we did not want to get tied up with anything of that kind.

Senator HERRING. From your experience, what do you think the Government could do best to help the railways?

Mr. MCNEAR. Oh, I think the first thing to do is to leave them alone. Tell them they cannot get any more money, and perhaps change the foreclosure procedure. You now have a new type of reorganization law. So far there has been no railroad reorganized under it. Maybe they will get to that point some day, but it seems to me that the security holders, whose securities are in default, ought to be able to step in and take charge and clean up, and clean up promptly—get started on a reorganized basis.

Senator VANDENBERG. Well, in that same connection, what would you say to the suggestion that the railroads be permitted to buy in their own securities at deflated market values without having to pay any capital-gains tax or income tax on the increment, so as to accomplish a more painless readjustment of the capital structure?

Mr. MCNEAR. Well, of course, anybody would like to save on taxes.

Senator VANDENBERG. Well, why should not a railroad be permitted to take advantage of low market values on its own securities in a time of stress?

Mr. MCNEAR. Where would the money come from to buy the securities at these low prices?

Senator VANDENBERG. Let us consider the use of R. F. C. loans for some such purpose as that rather than for a more nebulous or uncertain purpose.

Mr. MCNEAR. Well, of course, really, I just wonder——

Senator VANDENBERG (interposing). Of course, I realize I have collided with your idea now that no one should borrow anything anywhere at any time.

Mr. MCNEAR. Well, I believe in the old system of private enterprise. I believe in private banking instead of Government banking. I believe that the way you are going to get along is through private enterprise, through private initiative, letting the individual do the business rather than letting the Government compete with everybody.

Senator VANDENBERG. But when in Rome you have to eat Roman candles, and here we are. [Laughter.]

Mr. McNEAR. Well now, take a specific case. Somebody, let us say, has some first-mortgage bonds of a railroad, selling around 11 cents on the dollar. As I understand it, your proposal is that the R. F. C. would come along and buy up those bonds. Well, in the first place they would not be sold at that price very long, there would not be very many at that price.

Senator VANDENBERG. That is right.

Mr. McNEAR. In the second place I just wonder whether it is fair, from the standpoint of the owner, the person who bought those bonds in perfectly good faith. You might find the person who bought the bonds bought them for 100 cents on the dollar.

Senator VANDENBERG. He probably did.

Mr. McNEAR. Now it seems to me that those people who bought those securities in perfectly good faith, and perhaps the issuance of the securities was approved by the Interstate Commerce Commission, it seems to me that those security holders should have a better chance to reorganize the property and take it over and make what they can make out of it.

Senator HERRING. I am wondering if they would not profit more by a program of this kind, where there was a market and where their bonds would go up, so they really would get more than they will get if they continue the same policy they have now.

Mr. McNEAR. I have not thought this thing through. Suppose the R. F. C. bought these bonds, let us say they started in to buy at 10 or 11, before they bought very many of them they would be running the market up and maybe before they bought 25 percent of the issue the market price would be practically up to par, because everybody would know that the R. F. C. would be buying the bonds.

Senator HERRING. That would help the original owner then, would it not?

Mr. McNEAR. Well, it would not help the man who sold at 11 cents on the dollar.

Senator VANDENBERG. No, but let us take the man who does sell at 11 cents on the dollar, in the first place he does not have to sell, there is not any compulsion about this except as he confronts compulsion in his own situation. He sells at 11 cents on the dollar and some speculating investor puts 11 cents on the dollar into it. Subsequently, through Government aid of one sort or another, the railroad is rehabilitated and the speculator gets the benefit of the increment.

Senator HERRING. As it is today.

Senator VANDENBERG. Yes. Now, why could not the railroad get the benefit of that increment, inasmuch as we are assuming that this is a public obligation to straighten things out?

Mr. McNEAR. I see. You are going on the premise that these railroad bonds that are in default are owned by people who bought them from the original investors on a speculative basis?

Senator VANDENBERG. I am going on the theory solely that when bonds are offered for sale voluntarily at a low figure and somebody is going to buy them, that the railroad ought to have the same right to buy them as the investor, the private speculating investor, plus the right not to be taxed for the increased increment when they take them into their capital structure and be permitted to reduce their capital structure accordingly. They might not reduce it 5 percent in the course of the year. I am not talking about buying the whole bonded structure. They might not reduce it over 5 percent a year, but that would be a 5-percent advantage, and they would be 5 percent better off at the end of the year in their capital structure, which is more than they would be under any other system.

Mr. McNEAR. I think perhaps there is a lot of merit in that. I just have not had an opportunity to think the thing through, to see where we would wind up. I am just wondering if the R. F. C. buys these bonds would the R. F. C. then turn them over to the railroad to retire?

Senator VANDENBERG. I am talking about the railroad buying them.

Mr. McNEAR. The railroad buying them?

Senator VANDENBERG. Yes.

Mr. McNEAR. With its own funds?

Senator VANDENBERG. Yes.

Mr. McNEAR. Oh, that would be fine; yes.

Senator VANDENBERG. All right.

Mr. McNEAR. Of course, then you are merely giving the railroads a little concession on their taxes.

Senator VANDENBERG. We are giving them an incentive to reduce their bonded structure by this painless method.

Mr. McNEAR. Yes, sir. Of course, I think there is another thing, if you want to help the railroads in connection with taxation, and that is to provide some way that they can take greater allowances for depreciation. We are having a time of it now with the Internal Revenue Department, because we are taking, and have taken for some years, depreciation on our way and structures. They tell us that is not customary on railroads, but it seems to me, with a plant that admittedly is becoming obsolete, that you certainly ought to be able to take depreciation, and at a generous rate.

Senator VANDENBERG. Well, now, suppose a new and more generous rate of depreciation were permitted in the tax law, would that be calculated to stimulate replacements?

Mr. McNEAR. I should think so, because the railroads would then—take in our own case, we have a fairly substantial amount. The amount of our accrued depreciation on road accounts as of October 31, 1938, is $388,000. That is against an investment in total road and equipment of $3,483,000.

Senator VANDENBERG. You mean that the $388,000 figure is the one that is being disputed?

Mr. McNEAR. Yes, sir. The Internal Revenue people first took the position that all of that was earnings, it was all earnings, but recently it seems to me they have sort of swung around to the theory that we might be entitled to some depreciation, but at very low rates. We go on the theory, as I have just mentioned, that the railroad plant, particularly with new changes, which are coming along so fast, that there certainly ought to be generous allowances for depreciation, particularly to cover the item of obsolescence. Then the funds, you see, that are set up in the depreciation reserve would be used for maintenance and replacements.

Senator VANDENBERG. Exactly.

Mr. McNEAR. Then there is another thing. When you set up those amounts and charge them into expenses, you have less net earnings shown for interest and distribution, and therefore you are not able to show perhaps as good a relation of earnings to interest charges, and therefore you are not in a position to put out quite so many bonds.

Senator VANDENBERG. The thing I am particularly interested in is whether or not the allowance of a reasonably liberal depreciation for obsolescence, and so forth, would not definitely be an incentive toward replacements?

Mr. MCNEAR. I think it would absolutely; yes, sir; very definitely so.

Senator VANDENBERG. And replacements will be a broad contribution to the general economy of the country.

Mr. MCNEAR. Yes. For example, with these new locomotives that we bought, we wanted to give them a 20-year life. Now I think that most anybody would agree that after a locomotive is 20 years old it has become obsolete. Look at these locomotives that are running around now, that are 20 years old, they are certainly due for replacement. However they will still run, they are not entirely worn out. You can keep a locomotive going for 50 years maybe, but it is not up-to-date. The new locomotives have features in them that will give you considerable economy. Well, we could not get a 20-year life. I think the Commission told us we would have to use a 25-year life, and I think the Internal Revenue people told us we had to use a 30-year life.

Senator VANDENBERG. Now how do you succeed in running your own business the way you want to when you run into mandates of that character?

Mr. MCNEAR. Well, I don't know. We may have to go to bat with the Internal Revenue people before we get through with it. The first thing they said was that these way and structure depreciation charges were all earnings. We have not acceded to their views as yet. We hope we will make an agreement with them.

Senator HERRING. You have not applied to the Commission for a general increase in rates?

Mr. MCNEAR. No, sir; we have not applied for the increase in 1938, or whenever that request was made, for the reason that we had not increased our wages, and for the further reason that we did not have an increase in rates was in our best interest. It seemed to us an increase in rates would merely drive traffic away and increase the sphere of operations of our truck competitors. We would prefer to go on the theory of large volume and low rates and low expenses. You know, when you make some comparisons, going back to pre-war periods, and take the price of corn and the price of hogs pre-war and what they are now, and see how that situation compares with the big increases in railroad wages and railroad freight rates, and some other things, there is quite a disparity.

Senator HERRING. Well, that is a strange doctrine from a railroad president, is it not?

Senator VANDENBERG. It is a strange railroad.

Mr. MCNEAR. Yes; it is. Of course, this is a little bit of a one-horse railroad and maybe these things that I am talking about would not work on some other railroad. I do not know about that. All we are trying to do is to run our own business.

Senator VANDENBERG. Well, I hope they let you keep on doing it. There is a little more hope of that than there was.

Mr. McNEAR. So it would seem; yes, sir. I think, from the standpoint of all concerned, if we had lower freight rates and lower expenses and larger volume, we would have just as good if not better profits, and we would have more employment and everything would be in better shape.

Senator VANDENBERG. How would the employee profit from that equation?

Mr. McNEAR. Well, of course I go more on the theory of purchasing power than high wages. If we get the high wages, it does not necessarily mean that you can buy an awful lot with them.

Senator VANDENBERG. That is fairly correct.

Mr. McNEAR. This may be getting way outside the field of this inquiry, perhaps, but since we have made all of our costs and expenses go up in this country, I do not see how we are going to do much in foreign trade in competition with other countries.

Senator VANDENBERG. And then we pare all our operations down at the same time and wonder why everything goes up the chimney.

Mr. McNEAR. Well, you take these farmers in our country; they used to ship a lot of hogs in our country to a big packer in Indianapolis; that packer had a big export trade, which he does not have any more.

Senator HERRING. All the time that the railroad was operated by the receiver, before you took it over, they did not earn operating expenses, did they?

Mr. McNEAR. No; they were operating at a pretty large deficit.

Senator HERRING. And since you acquired control you have made your interest charges each year, have you not, and paid operating costs?

Mr. McNEAR. If you are interested in the figures, I can give them, beginning with 1928, showing the relationship of times fixed charges earned; that is the relationship between income available for fixed charges and the total fixed charges, which include the interest on funded debt, interest on unfunded debt, and amortization of discounts on funded debt, those three items constituting the total fixed charges.

In 1928 the fixed charges were earned 4.3 times, in 1929 they were earned 4.04 times, in 1930 they were earned 3.33 times, in 1931 they were earned 1.73 times, and in 1932 they were earned 1.14 times. I might mention that in 1932 we realized that we had not spent as much money for maintenance as we should have spent, so we included in the item of maintenance accounts a charge of $100,000 to cover deferred expenditures for renewal of ties and for equipment repairs. In other words, this figure of 1.14 times charges earned was after we included in our expenses this item of $100,000, which was set aside but not spent. In other words, we did not think it would be a fair representation of the facts to include this $100,000 in earnings because we did not maintain the property in 1932 as we should.

In 1933 the relationship was 2.58, in 1934 was 2.39, in 1935 2.64, in 1936 3.7, and in 1937 about 3.5.

Senator HERRING. Being a connecting line, you do not have many point of origin revenues, do you, which is usually the larger revenue?

Mr. McNEAR. No. Our percentage of traffic originated on our railroad is about 25 percent.

Senator HERRING. Did your increased revenue come partly through better rate divisions on interstate traffic?

Mr. McNEAR. We have had no particular change in our divisions. The divisions on our railroad are the same now, substantially, as they were at the time of the foreclosure sale.

Senator HERRING. Well, as I understand it, there is a point-of-origin rate that is much more per mile than is paid on merely a connecting line receiving through traffic.

Mr. McNEAR. Yes; I think that is generally true.

Senator HERRING. You do not have much of that? Yours is largely connecting-line business, is it not?

Mr. McNEAR. Yes, sir. Our revenue per ton-mile, if you are interested in that, which gives effect to that feature, was 0.0122 in 1937. That compares fairly well, I think, with the other railroads in our territory.

Senator HERRING. Well, this is most interesting and helpful, Mr. McNear. If you have anything else you think you should put into the record, we would be glad to have you do so.

Mr. McNEAR. I am really not entirely informed as to just what the Senators have in mind.

Senator VANDENBERG. They have a lot more in mind than they did before you arrived; I can assure you of that.

Mr. McNEAR. Well, if you are looking into the whole railroad situation with the idea of improving its net earnings——

Senator VANDENBERG (interposing). No.

Mr. McNEAR. You are not interested from that angle?

Senator VANDENBERG. We are interested primarily in knowing how the tax power can be used to contribute rationally and effectively and practically to railroad rehabilitation and to the general economic rehabilitation of the country.

Mr. McNEAR. If you are talking about taxes, then I would ask: Why is it that the railroads must pay so much more for the social-security benefits than industry generally?

Senator VANDENBERG. Senator Herring will answer that.

Senator HERRING. Because of the additional risk, I guess.

Mr. McNEAR. Now, there is quite a difference between what the railroads have to pay under the Carriers' Taxing Act and what the industries have to pay under the Social Security Act. Now, if there would be some way of giving the railroads some relief in that direction, it would be very nice.

Senator HERRING. Well, that is another measure that was passed before I got down here.

Senator VANDENBERG. You almost did not get here in time.

Senator HERRING. I think this makes a rather happy ending to the 3 weeks of these hearings.

Mr. McNEAR. If I may leave one thought with you, sir, and that is this: I would not bear down too hard on these personal or so-called family holding companies that are organized for the purpose of trying to do a constructive job. Sometimes you have got to have them.

Senator HERRING. You do not think a family group should be penalized because they have been enterprising and energetic and have gone ahead and built up something?

Mr. McNEAR. No; I think you should encourage what is referred to as venture capital.

Senator HERRING. That is right.

Mr. MCNEAR. I think in a great many instances you have to handle a thing like that through some sort of a family or personal holding company. A bank or some other source of wealth which loans money on a thing like that may not want to be known in the situation. Perhaps some of the banks have bad reputations down here, but I think there are many of these financial institutions that have done and are doing an awful lot of good. I can readily understand why a financial institution might be looked at in a bad light, and I do not see why they would want to become known, but they might say, "Well, this looks like an opportunity; let us take a chance." Maybe you are going to go on the theory that those people should not do that, but if that had not been done half of this railroad would have been abandoned and a great many people thrown out of work.

Senator VANDENBERG. If that had not been done, there would not be any railroads to begin with.

Mr. MCNEAR. No, sir. I say, give the fellow a chance who is going to try and do something.

Senator VANDENBERG. You realize that is horse-and-buggy stuff, don't you?

Mr. MCNEAR. Yes, sir; and our country got to be a pretty good kind of a place to live in under that form of procedure.

Senator VANDENBERG. I thought so.

Mr. MCNEAR. I do not know that we have gone ahead a whole lot since those ideas have been changed around.

Senator VANDENBERG. I am very glad you came down, my friend. It has been very refreshing.

Mr. MCNEAR. Thank you.

Senator HERRING. Thank you, Mr. McNear.

Mr. DESPAIN. If it please the committee, on behalf of the staff I would like to request permission to add later, because it is now in the course of compilation and analysis, certain data which I believe is appropriate for the record and which might correct some erroneous impressions. Our mail at the present time is reflecting the thought that not enough employees have expressed themselves on the subjects before this committee. Our staff is now engaged in quite an extensive questionnaire poll through more than 100 industrial institutions, in the employee group there, obtaining their sentiment for or against profit sharing. It has not been easy for employees, who are under many handicaps, to come here, although your committee has been more than desirous to receive them and welcome them if they wanted to come, and, therefore we are going out to the employees and getting reactions as to their attitude for or against profit sharing and if profit sharing is adopted their opinions as to the amount of participation, their expressions as to form and structure of plans for profit sharing which will create the widest satisfaction. The analysis of this employee sentiment will, I think, be very interesting and pertinent to the record in a summarized form.

Another impression which seems to us is a little too prevalent is that every individual business or institution must have a different form of profit sharing. While neither the committee nor the staff makes any claim that a standardized form or formula of profit sharing can be applied generally to all industry, I think the attitude is a little too narrow that no formula can be applied with any reasonably wide application. We are now utilizing a selected formula which is a combination of two principles adopted from two companies where they have proven to be effective as to both angles, and we are superimposing that formula, for analysis purposes, on more than 60 of the largest industrial institutions in the United States, in 10 major industries, and it shows its practical adaptability to their present financial structures and operations. So, with the permission of your committee, we will add certain summarizations of these facts to the record of these hearings.

Senator HERRING. The formal hearing is closed, but the staff is to continue with its survey and its work in connection with the final report, which we hope to have finished early in the next session.

Before concluding these hearings I should like to express my appreciation to the members of the staff, and to Senator Vandenberg especially, for his helpfulness throughout. I am deeply grateful for the very fine cooperation which I have received not only from Senators Johnson and Vandenberg, but from all of the persons who have participated in the various phases of the work of this survey and the hearings.

The committee was charged with the duty of making [reading]:

> A complete study of * * * existing profit-sharing systems between employers and employees * * * in the United States * * * with a view to the preparation of an authentic record of experience * * * and to consider what favorable contribution, if any, may be made in the encouragement of profit sharing by the Federal Government, including the grant of compensatory tax exemptions and tax rewards when profit sharing is voluntarily established, and to consider any other recommendations which may prove desirable in pursuit of these objectives

The inspiration behind the resolution adopted authorizing this survey was the belief on the part of the author and the Members of the United States Senate that the time had come to undertake an investigation of those principles and that experience consonant with the American system of government and industry.

In our research we have constantly sought a solution to three of the most vital problems confronting the American people, namely, industrial unrest, unemployment, and protracted loss of normal national income.

As a result of this survey two important observations are to be made: First, it is apparent that a great many employers have, over a long period of years, recognized the value of the services rendered by their employees; that they have made a very real effort to reward those services by an equitable division of the fruits of industry by voluntarily establishing some form of profit sharing or extra compensation plan. The sum devoted to this extra remuneration over and above the contractual wage often has amounted to as much as 12 or 15 percent of the net income, and in some instances the division has been on the basis of 50 percent, and compared favorably with the amounts paid by management to stockholders in dividends.

The friendly relations existing between these employers and their employees indicate that in such a program as profit sharing is the seed of industrial peace, and that if liberally adopted in those industries to which profit sharing would be adaptable, the American people would soon be freed from the burden of strife, strikes, and lock-outs, which have beset our industrial life over the period of the past several years.

The second important fact is the willingness of employers to cooperate with the Government in finding a solution to our common problems. This enormous reservoir of good will, which barely has been tapped as a result of this survey, may be called upon to aid in the restoration of prosperity and industrial peace. It is the belief of the members of this committee that the progress made thus far is but an indication of what can be accomplished, with government, employer, worker, and public adopting a friendly attitude toward one another and with a sincere determination on the part of all to find a solution to our national problems.

Throughout this investigation I frequently have been impressed with the patriotic motives underlying this survey and the earnest spirit which actuates all who have been connected with the enterprise.

The spirit which has thus come into being will, I believe, grow in strength and in importance with the convening of the new Congress. As a result of this survey and our final report, inspiration will be found for renewed efforts on the part of government to bring about a complete and a harmonious understanding among employers, workers, and the people of the Nation, to the end that we may find rational means for solving the problems of labor unrest, unemployment, and reduced national income. The cooperation of all citizens is invited in this common task.

If there is nothing else we are adjourned.

(Whereupon, at 11:05 a. m., the hearing was adjourned.)

(Subsequently, the chairman ordered the following memorandum submitted by Mr. Elisha M. Friedman, of New York City, printed in the record. Mr. Friedman's contribution was received after the close of the public hearings.)

MEMORANDUM ON PROFIT SHARING, STABILITY, AND DEMOCRACY OR PROFIT SHARING A CHECK ON CYCLICAL FLUCTUATIONS AND STATE CAPITALISM

[Statement submitted by Elisha M. Friedman, New York City]

I. Introduction

Profit sharing has reached the stage of legislative inquiry. In England in the eighties and in the United States in 1937 the organization of unskilled workers into trade-unions was followed by labor crises. The economic waste and political unrest resulting from sit-down strikes led to a search for remedies. Profit sharing arose as an antedote to labor warfare in England then and to sit-down strikes in the United States now. History repeats itself.

The testimony before the Senate committee has concerned itself largely with the narrower aspect of profit sharing—attaining peaceful labor relations. But profit sharing has larger implications. Its wide extension should help to smooth out the fluctuations in the business cycle and thus check the inroads of the State on private business enterprise during depressions. By reducing such inroads, it should check the advance of state capitalism, which has been sweeping contagiously over the world and which has found its highest expression in Russia, Germany, and Italy. These two theses, economic and political, are to be demonstrated.

II. Violent Fluctuations in Business Cycles

From May 1937 to May 1938 the Federal Reserve Board index of production had probably the most violent decline on record—from 118 to 76. From May

1938 to December 1938, it had the most violent rise on record, but one—from 76 to 102. The speed of the advance has been the subject of comment by economists, journalists, and Government officials. During this period wages per hour were the highest in American history. Yet labor leaders and public officials advocated wage rigidity as a solution for the depression. They offered as an excuse that high purchasing power was thus maintained. Whose high purchasing power? The general community? Or the favored group?

(A) CAUSES OF 1937–38 SLUMP

What are the facts?

(*a*) The Government's statistics and charts tell a different story. Real wages in 1936 and 1937 rose substantially above 1929, but national income was substantially lower. Who made good the difference? The groups with fixed incomes—the salaried classes, Government employees, teachers, pensioners, and beneficiaries of life-insurance policies, and bondholders, generally. Entrepreneurs and stockholders suffered a decline in income. The unemployed lost their entire income.

(*b*) Again wages in selected industries since the N. R. A. in 1934 rose sharply above the cost of living. Who paid the difference?

(*c*) Wages increased faster than employment. Those fortunate enough to be employed enjoyed an increase in wages at the expense of the rest of the community. The ratio of pay rolls to employment rose to a new high record in the spring of 1937, in some industries, as steel.

(*d*) Building wages rose much faster than rents which depend on tenants' wages. Therefore construction was delayed.

(*e*) Wages were raised first by the N. R. A., then as a result of the too rapid unionization of labor. Output was decreased by shortening hours and by actual restriction through "slow-downs." At the peak of the cycle in the spring of 1937 there were unemployed 13 percent of the working population, a figure three times as high as any previous peak.

To obtain "grass roots recovery," the stream of national income was diverted to a small area of organized and politically powerful workmen, thereby afflicting other areas of workers with economic drought. At the peak of the recent recovery, December 1936, when the Federal Reserve index of production was 121, there were over 8.3 million unemployed. In September 1929 when the Federal Reserve index was 121, there were only 600,000 unemployed. How much of current unemployment is ascribable to regidities in cost, chiefly wages?

(B) THEORIES OF BUSINESS CYCLES

There are many theories of the cause of business cycles. One group of causes has certain elements in common, namely, disequilibrium in income and purchasing power to the several groups in society and resulting inability to buy the goods produced. Herein lies the significance of profit-sharing. It makes wages vary with profits, or selling prices. It stabilizes profits, industrial production, employment, and consumer purchasing power.

To the writer, the physiological conception of equilibrium seems the most satisfactory explanation of the business cycle. The human organism functions within very narrow ranges of temperature, atmospheric pressure, blood count, concentration of salt and sugar in the blood, and so forth. The organism, when pushed off normal, automatically sets in motion a train of compensating forces to push it back again to normal. Any wide variation that cannot be corrected results in sickness. In economic society not only is such automatic compensation absent, but the forces tend to aggravate the disequilibrium until panics result. Economists call it a vicious spiral. Instead of flexible and compensating factors, economic society is filled with rigidities. Since wages constitute the largest factor in production costs, one may say that rigid wages are an important cause of fluctuations in production and employment. For example, when union wages remain rigid and nonunion wages fall, the nonunion workers cannot consume the products of union labor. When laborers' wages are raised and salaries of clerks are not, the white-collar class suffers a shrinkage in purchasing power. When industrial wages remain rigid and farm income falls, the farmers cannot buy the products of the factories. To these old or accidental unbalancing factors in economic society are needlessly added new and politically inspired rigidities.

Under theoretically ideal conditions production and employment could be maintained at a high and constant level if all the factors fluctuated proportionately.

If when selling prices fall all costs could be reduced proportionately, production could be maintained, because at lower wages employment could be maintained and consumer purchasing power could therefore remain high enough to take off the market all the goods produced. However, if wages and other costs are rigid when selling prices fall, profits turn to losses and threaten bankruptcy, thus compelling the entrepreneur to liquidate, to retrench, and to discharge workers.

Some items have by custom become rigid, such as rents and interest. In fact, the whole system of life insurance is built up on a promise to pay the beneficiary a fixed number of dollars. Life insurance in force in the United States amounted to over $100,000,000,000 in 1936 (Statistical Abstract, 1937, p. 277). The payments on life-insurance policies in the United States fluctuated between $2,500,000,000 and $3,000,000,000 per annum in recent years. The insurance companies offer a fixed return and therefore proceed to seek a fixed income. The insurance policyholder, relying on the insurance company's promise, expects the American economy to make good. The rest of economic society, however, bears the increased burden of fluctuation. The guaranty to the insured is borne by the groups receiving the rest of the national income.

The need for flexibility, even of interest charges, is evident when bankrupt companies emerge from reorganization. Often the new company issues income bonds paying interest only if earned, a contingent charge and therefore a flexible cost item. Other similar flexible forms of interest are found in participating bonds, where the minimum interest charges can be carried under all circumstances and a flexible portion added when profits justify. Similarly in convertible bonds the charge disappears when profits are high enough to convert the bond into stock. Flexibility of interest charges is necessary in any economy or any corporation seeking stability. Again, landlords' rent, another fixed charge, caused much difficulty in the last depression. The necessities of the crisis resulted in the invention of the flexible rent. Tenants, particularly chain stores, which operate on a very thin margin of profit, devised a scheme whereby after a low minimum fixed rental is paid a flexible supplement was added, depending on the volume of sales or the volume of profits. These examples, resulting from crises and collapse, illustrate the need for flexible costs to avoid violent fluctuations in earnings and in production of a corporation or an economic society.

(C) RIGID HOURLY RATES VERSUS FULL EMPLOYMENT

In a dynamic economy there must be some shock absorber. If all the elements were flexible, adjustment would be easy. But usually when selling prices begin to decline and the entrepreneur, in order to stave off bankruptcy, desires to reduce his costs proportionately, Government officials and union leaders resist such necessary adjustment. They fight reductions in hourly rates. Employers thereupon must seek flexibility elsewhere. They discharge men. Something must yield. If wage rates are constant, volume of employment shrinks. Thereupon the Government steps in a second time with relief proposals to repair the damage which it caused. It "makes" work and pays relief wages, which are lower than discharged skilled workers had been receiving. In other words, the result originally sought by private employers is accomplished in another way by the State. The workers' wages are cut—with this important difference—that in public work there is the stigma of charity, whereas in private employment a reduced wage is regarded as a temporary sacrifice. The Government had not made good on its promise to keep up workers' wages. The rigidities won't work. Elasticity still persists, but at what an expense? Government Budget deficits, lowered morale of the workers, and a breach in the organization and working staffs of corporations. In reality the Government, by dictating wage policies, assumes the function of business management but dodges the responsibility for the results. It attempts to fix wages and then lets the management work as to the outcome. Power flees from responsibility. Irresponsible power leads to social mismanagement.

In an organic society something must be flexible. Volume of sales increase or decrease as selling prices per unit falls or rises. Witness bargain sales. Volume of employment tends to increase or decrease as wage rate per unit of production falls or rises. Witness the automobile. In the field of finance the currency, which was regarded as fixed before 1931, snapped because price levels had become too rigid either through monopolistic practices or rigid union-wage rates. For example, England had to abandon the gold basis when she was unable to reduce wages directly. By depreciating the currency she did so indirectly. If a variable item is made constant, the old constant item snaps; its goes overboard, as did the gold standard in England or democracy in Germany. Economic society requires flexibility. Increasing the rigidities increases the violence of booms and depressions. Political unrest results. The labor leaders in democratic Germany and Italy tried to maintain rigidity in hourly rates, lost out, and acquired another rigidity, *gleichschaltung*—totalitarianism, a rigid economy of prices and a rigid policy on imports, censorship, and concentration camps. Then the standard of living becomes the flexible element. The Soviet economists forecast that the fluctuations of capitalist society will become increasingly violent until it finally collapses, like a whirling dervish.

The thesis of economic flexibility and equilibrium gives a new significance to profit sharing. To keep up wages when selling prices shrink is bad arithmetic. Wages and other costs can only come out of selling prices. Costs may not exceed the sales price. If the shock absorbers and tires are taken off an automobile, the shock is transferred to the vertebra and to the cranium of the rider. That is just about what has been happening to society with its flexible factors eliminated.

Biology affords an analogy. Our rigid economy represents a low order of evolution. In winter the frog and the fish experience a decline in body temperature. Because they have no automatic mechanism for heat compensation, they become apathetic in winter and scarcely function. In this respect they are something like our lowly evolved economic society. But the bird or the rabbit in cold weather remains active, because it has automatic devices for maintaining a constant temperature. The cold-blooded animals lack a compensating mechanism; they function like the business cycle. The warm-blooded animals have compensating mechanisms and serve as a pattern of how some future stable economic society might function. Our economy often suffers from a vicious spiral—a self-aggravating disequilibrium. Our physiology has a self-corrective mechanism. When it fails, we become ill. Illness in the human body is due to failure to compensate, as the physiologists call it. Economic and social distress is likewise due to failure to compensate.

To justify rigidity of wage rates, a fallacy known as purchasing-power theory has been evolved by "crackpot" economists and by union leaders. They say keep up wages in order to maintain purchasing power, but only for the particular favored union group on whose good will the salary and prestige of the spokesman depends. As for the rest of the community, nonunionized labor, the salaried classes, and the men whose unemployment was caused by wage rigidities, they suffer. They have no spokesman—no friend at the court. Eventually even the supposed beneficiaries suffer. Economic society, including even organized labor, is a victim of the fiction or lie that high rigid wages make for prosperity. High wages are a symptom of prosperity. They are not a cause. During the 5 years of recovery from 1933 to 1937 there was practically no residential building. Theoretically hourly wage rates were high, but annual wages were low. A $16-a-day plasterer could not build dwellings for a $16-a-week clerk. There was no basis or possibility for exchange of a day's work between them.

The policy of creating purchasing power through budget deficits tends to hide, and therefore to perpetuate, existing maladjustments. It is a soft and lazy way. It avoids the necessary corrections. It can only end in inflation. It deters savings. It checks adjustment. It penalizes the taking of risk.

(D) POLITICAL ASPECTS OF ECONOMIC RIGIDITIES

Obviously regidities prevent private capitalism or private enterprise from functioning smoothly. These rigidities, whether fostered by Government or by trade-union leaders, discredit the present economy. Private capitalism is now in the dilemma of a puppy that has been locked up in the house and then is beaten and kicked out for soiling the floor.

III. CAUSE OF ECONOMIC INSTABILITY

Economic rigidity is a cause of economic instability. This thesis becomes obvious whether we consider the United States as a single business, or whether we consider a decade record of some major corporation, or whether we consider the analogy of stock speculation on a thin equity.

(A) IF THE UNITED STATES WERE A SINGLE CORPORATION

If the United States were a single corporation, the national-income account compiled by the Department of Commerce would give statistical evidence of the thesis that rigid wages and resulting risk of bankruptcy exaggerate cyclical fluctuations.

The national income paid out was as follows:

[In millions of dollars]

	1929	1932	1936
National income	78,174	48,487	62,056
Total compensation of employees	51,204	31,013	41,250
Wages in selected industries [1]	16,852	6,796	11,369
Work relief wages	....	....	2,205
Dividends	5,969	2,749	4,573

[1] Mining, manufacturing, construction, transportation; in this group not only were corporate earnings wiped out, but large deficits were incurred.

PERCENTAGE OF 1929

	1929	1932	1936
Total income paid out	100.0	62.0	79.4
Total compensation of employees	100.0	60.6	80.6
Wages in selected industries	100.0	40.3	67.5
Dividends	100.0	46.1	76.5

PERCENTAGE DISTRIBUTION BY TYPE OF PAYMENT

	1929	1932	1936
Total income paid out	100.0	100.0	100.0
Total compensation of employees	65.5	64.0	66.5
Work relief wages (included in total compensation)	0.0	0.0	3.3
Dividends	7.6	[1] 5.7	7.4

National income paid out, 1929 to 1936, tables Nos. 3, p. 16 and 4, p. 18.

[1] 4.9 percent in 1933.

What is the significance of these figures? As individual corporations show deficits, they cut expenses. If wages had yielded so as to avoid the threat of bankruptcy, the volume of employment could have been better maintained and with it the volume of national purchasing power. The national income account of the United States shows statistically the reason for labor's distress, for work relief, and for Budget deficits. Declining earnings cause declining employment. Business dare not operate at a loss.

(B) A DECADE OF CORPORATE BOOKKEEPING

The thin margin of profit on which the national economy works is well illustrated in a few typical industries.

For example, for the 10 years 1928 to 1937, the Great Atlantic & Pacific Tea Co. showed a very low ratio of net income to total sales. The average was 2.30 percent. The highest ratio was 2.95 percent in 1931, and the lowest was 1.04 percent in 1937. Armour & Co., in the same period, showed an average of 0.25 percent, a high of 1.20 percent in 1934, and a low of —3.13 percent (deficit) in 1931. It is this thin margin which determines whether business shall function and whether workers shall be employed. Yet there is in the United States, under capitalism, an abundance and variety of goods available for the choice of the consumer. Contrast this with the scarcity of merchandise in the Mostorg, the great, almost empty, store in Moscow, where goods are unavailable, where consumers wait in queues and often are rationed as to amount. Yet the price of good service under private ownership is an insignificant profit.

Similarly the 9-year record of operations from 1929 to 1937, published by Westinghouse Electric & Manufacturing Co., shows the following account:

	Amount	Percent
Total sales	$1,262,000,000	100.0
Cost of materials and supplies	491,000,000	38.9
Renewal of plant and equipment	58,000,000	3.6
Taxes	42,000,000	3.4
Total uncontrollable disbursements	591,000,000	46.9
Balance for wages, dividends, and expansion	669,000,000	53.1
Wages and salaries and employees' annuities and insurance	604,000,000	47.9
Balance for stockholders and expansion of plant	65,000,000	5.2

The annual average earnings for the common stock on an average investment in plant and equipment of $191,000,000 was 3.62 percent.

The United States Steel Corporation published the following computation for the 10 years from 1928 to 1937:

	Amount	Percent
Total sales	$6,950,000,000	100.0
Materials and services purchased	2,496,000,000	35.9
Taxes	467,000,000	6.7
Depreciation and depletion	518,000,000	7.5
Total uncontrollable expenses	3,481,000,000	50.1
Balance	3,469,000,000	49.9
Wages and salaries	2,928,000,000	42.1
Balance	541,000,000	7.8
Interest and preferred dividends	334,000,000	4.8
Balance for stockholders and expansion of plant	207,000,000	3.0
Common dividends	220,000,000	3.2
Deficit after common dividends	−13,000,000	−.2

The earnings available for the common, or $207,000,000, were equivalent to 1.37 per cent per annum on the average net worth of $1,513,807,000.

Obviously, any business can run only if it is profitable. This applies alike to privately owned plants in the United States or State-owned plants in Russia or Germany. Under no system can the workers be paid more than the selling price provides. When all the items of cost become rigid and the entire shock absorber is the thin margin of profit for the investor, then employment and production must fluctuate violently. Even if the United States Steel Corporation and Westinghouse Electric & Manufacturing Co. were expropriated, and even if capital received no return, wages would be limited to the figure left after paying for raw materials, replacement, and taxes. The workers operating the plant themselves would thus have to limit the wages paid. However, in the event of expropriation no new capital would be forthcoming for expansion or risk in new ventures. And if private capital is to continue to function as the mainspring of our economy, and if the business fluctuations are to be lessened, a profit-sharing scheme between wages and capital would be highly desirable.

An accountant analyzing the income account and balance sheet of the major corporations could make a factual diagnosis of our economic ills better than an economist working on theoretical grounds. For depressions, such an accountant would prescribe flexible production costs, including wages, rather than the rigid wages advocated by doctrinaire economists.

(C) OUR ECONOMY OPERATES ON A THIN MARGIN

The experience of the Securities and Exchange Commission affords a helpful analogy. The raising of margin requirements was a stabilizing factor. Before the Security Exchange Commission legislation, 10-point margins caused violent short-term fluctuations in the stock market. On the old way of figuring margins the bookkeeping was as follows:

Market price of the stock	120
Loan or rigid portion	100
Equity or flexible portion	20

The margin then was figured as the percentage of equity to loan.

An 8 percent decline in the market price, or 10 points, cut the equity or margin in half and compelled the speculator to sell. A high percentage of loan, the rigid factor, caused instability.

What was the nature of the Securities and Exchange Commission reform? The flexible factor or the equity was increased. The rigid factor or the loan percentage was decreased. Under the new method of figuring margins under the Securities and Exchange Commission the bookkeeping was revised as follows:

Market value of the stock	100
Loan or rigid portion	60
Equity or flexible portion	40

The margin is now figured as the percentage of equity to market value.

Under the new rules, an 8-percent fluctuation in the market price leaves the account unaffected. For this reason the stock market has had fewer quick-turn fluctuations since the Securities and Exchange Commission law went into effect. If the administration extended this principle from the stock exchange to the whole economy, a similar quick-turn stabilizing effect could be produced. As it is, the entire national economy is speculating on about a 6-percent margin, namely the percentage of dividends to the total income paid out. Since the other factors are practically all rigid, it seems that a small fluctuation in selling prices of merchandise creates the same violent disturbance in our national economy that a small fluctuation in market price of shares did in the stock market in the pre S. E. C. days.

(D) POLITICAL CONSEQUENCES OF ECONOMIC INSTABILITY

Can any economic system stand the strain of the violent fluctuations of the past few years? The cyclical instability of economic society has many grave consequences. The workers, even the employed, develop a sense of economic insecurity. Therefore, there is a search for political relief. And we have sought it. Unemployment relief by the Government causes burdens on the Budget, unsound state ventures into private enterprise and a movement toward state capitalism. Everywhere governments are moving at top speed to unknown destinations. As was widely said, "No man is in such a hurry as he who does not know where to go." Our economy must yield a little, or else the state steps in to overcome the evil effects of rigidities. Thereupon the economic responsibilities of the state increase.

Democracy has not two alternatives, as is so superficially believed. The Communists of the left and the Fascist-Nazis of the right are identical. There is only one alternative. Either we retain our individual initiative and private economy or we move ahead toward state capitalism. For the difference between Communists and Fascist-Nazis are differences only in language. It is the same panacea—spoken in a different accent.

All three leaders—Russian, German, and Italian—reflect the saying of Bismarck, "Any fool can rule by force. It takes a wise man to rule by reason." Paraphrasing it in economic terms, one may also say that "Any fool can run a business at a loss, to be recouped out of taxes. It takes a wise man to make a profit on his sales."

IV. Remedies for Economic Instability

The cure flows from the diagnosis. The diagnosis is that rigidities cause disequilibrium. The remedy therefore should be to substitute flexibility for rigidity. Theoretically the business cycle could be smoothed out. Of course in actual practice it is impossible to get all the elements of the economy to adjust for the fluctuation in one element, such as selling price.

(A) FLEXIBILITY OF COSTS

Some elements of cost are rigid, such as rent, interest, and most taxes, other than those on profit and income. However, these rigid factors are a small percentage of the total cost. In percentages of the national income paid out (National Income, 1920–36, p. 18), total compensation of employees ranged between 64 and 66.5 percent in the 8 years from 1929 to 1936. Dividends fluctuated from 4.9 to 8 percent. Obviously the reduction in the total compensation of employees was the effect of the reduction of earnings. In other words, from about 5 to 8 percent of the national income—namely, dividends or earnings—determine the volume of employment and in turn national purchasing power. How important is it, therefore, to develop a wage and dividend policy which will insure high employment and high national purchasing power!

Occasionally by agreement the workers will accept a wage reduction as an emergency. For example, one of the large mail-order houses in the autumn of 1937 offered a furniture factory a substantial order, to be sold at a price which would move a considerable volume of the merchandise. The factory owner assembled his workers, reported the offer of an order at a lower price, and agreed to forego profit if they would temporarily reduce their wages. They did so and they were employed for about 8 weeks. Here is an example of the "discovery of the obvious." Self-interested parties befog this simple truth. Again, in the building industry, wages are nominally maintained at the rigid rate, but to make the rigid rate work there is a "kick-back" or rebate in wage to the contractor. The rigid wage rate in this case is a fiction or a lie. The actual rate is flexible. The Amalgamated Clothing Workers, enjoying statesmanlike leadership, has from time to time agreed on wage reductions in order to keep its members employed.

How would a flexible wage smooth the business cycle? When profits are high, labor would receive more, the investors would receive less, and therefore there would be less tendency to overexpand. Violent peaks of the business cycle would thus be replaced by a smoother curve. When profits fall, labor would receive less and the investors would likewise receive less, but would avoid a deficit. Therefore, there would be less incentive to lay off labor. Therefore the volume of employment would remain high. Therefore there would be high-wage income and high consumer purchasing power, and more ability to take off the market the goods produced. So much for the cyclical aspects.

From the political aspect there would be less unemployment relief; smaller Budget deficits, damaging the fiscal standing of the Government and banking structure; fever Public Works projects, interfering with private enterprise; less obligation on the State to intervene for the unemployed, and therefore less state ownership and control.

The consequences may be contrasted under a flexible or profit-sharing wage and under a rigid wage. In the latter case the union leader succeeds in having wages raised in a boom. The wage increase is then passed on to the selling price. Other consumers, particularly the nonunion group, can then buy less of the goods. The rise is therefore self-defeating. This applies particularly to the building, automobile, and steel industries, in which rapidly rising wage rates early in 1937 broke the recovery. On the other hand, by a flexible or profit-sharing wage, incentive are given to increase efficiency or to raise wages per man without adding to the cost per unit. Therefore the selling price is not raised; it might even be reduced. In this event the rest of the workers should be able to buy more of the goods. Though wages per worker rise, wage costs per unit fall. Of course, the workers sharing in the profits have also an increase in their own purchasing power. Profit-sharing improves the condition of the workers both within and without the industry, more than does a fixed and rigid increase in wages.

(B) PROFIT-SHARING AND GOVERNMENT POLICY

The Government has already in its regulation of the stock exchange increased the flexible factors (equity) and decreased the rigid factors (collateral loan). In an address before the National Association of Securities Commissioners at Kansas City, September 22, 1938, Commissioner Jerome N. Frank, of the Securities and Exchange Commission, extended the concept of flexibility to capital structures of corporations and advocated greater use of common stock, a flexible security, as against bonds, a rigid security bearing fixed interest. He also advocated diminishing legal rigidities, even when bonds are used. Undoubtedly such a flexible financial structure constitutes the test of good financial policy. The United States Steel Corporation, which in 1929 exchanged $370,000,000 of bonds for common stock, avoided possible bankruptcy in the deflation of 1932. By analogy, therefore, a flexible wage structure should constitute good labor policy.

(C) FLEXIBLE ACCOUNTING

Profit sharing could also help in making the rest of the accounts more flexible. Reserves for depreciation, bad debts, and contingencies could be larger in good years and smaller in poor years, thus obviating the need for reducing employment. Again, profit sharing could be used to increase the reserves for unemployment, old-age pensions, dismissal bonuses, all of which would benefit the workers in the long run.

(D) FOREIGN EXPERIENCE

Profit sharing is not new. It has been done before. In fact the foreigners had a good word for it almost 100 years ago. In France in 1840 Leclaire was a contracting house painter with about 70 employees. He calculated that by sharing profits the workmen would economize in material and be more resourceful in applying themselves. The psychological motivation was sound. The worker, instead of being driven, pulled for the company. Leclaire's slogan for his workers seemed to be "Be not dumb driven cattle, be a hero in the strife." He could afford to pay them a substantial part of the increased profits and still have much left for himself. Then, as now, the plan was suspected by the workers. In fact, he was accused of trying to reduce wages. The plan worked well with a small group. In 1870 when a Socialist charged that Leclaire's firm was merely "a group of little masters who made profits out of others," Leclaire extended profit sharing to all his employees, even those who had been working only 1 day. The profit-sharing payments, as a percentage of wages, over a long period of years averaged 17 to 20 percent. Leclaire subsequently retired from business with a fortune which he said was far greater than he could have accumulated without profit sharing, and his workers benefited greatly.

In England the profit-sharing idea also had a long record. In 1889 a movement like our Congress of Industrial Organizations rose rapidly. Unskilled workers were being organized into trade unions hoping to gain the advantages that the skilled workers obtained. When a large body of unskilled labor suddenly sensed their power over the community, a critical situation developed. "The men seemed to have gotten the idea they could obtain anything they asked for. One of them was reported to have said, 'If we had asked for gold watches, he would have given them to us'" (Williams, Aneurin, Copartnership and Profit Sharing, N. Y., Holt, 1913, p. 75). The South Metropolitan Gas Co., which had a profit-sharing plan for the officials of the company and the foreman of the plant, decided in 1889 to extend it to all the workers. The result was a sliding scale of gas rates, of wages, and of dividends. The consumer the worker, and the investor enjoyed the advantages of a flexible scheme. If the company reduced the price of gas to the consumer, it could pay an additional dividend, if earned, and pay the workers a wage dividend in addition. The workers were encouraged to leave their wage bonuses on deposit, on which interest was paid at higher than the market rate. The men, however, were completely free to withdraw bonuses in cash or to invest them in the company. Worker ownership was encouraged so that eventually the workers owned a good part of the outstanding stock of the company. Furthermore, of the 10 directors, 7 were elected by the general shareholders, 2 by the shareholders who were manual laborers, and 1 by the shareholders who were on the office staff. The basic wage rate was the prevailing standard in the industry. The bonus was a supplement. There was ultimately no objection to union membership. The experience of the South Metropolitan Gas Co. extended to a large part of the gas industry in England, excepting the municipally owned gas works. Of all the companies which adopted it, only one, a small plant, ever abandoned it. The British experience was, under the urging of Louis D. Brandeis in 1905, adopted in the gas works in Boston.

(E) EARLY AMERICAN PRECEDENTS

Mr. Nelson arose from the ranks of labor and became the head of his own company. Profit sharing was fairly liberal. Mr. Nelson said there was "most perfect satisfaction on both sides and utter unity of feeling. * * * Beyond any question, the system is right and judicious, whether regarded from a moral or purely commercial standpoint." Recent Senate testimony reveals numerous other profit-sharing plans covering diverse industries and size of corporations. True profit sharing, however, should furnish a genuine increase in wages to workers. It is not profit sharing merely to give the workers the right to buy stock on the installment plan, as in the case of some American companies. The benefits in increased efficiency are too remote. The risks to the worker are too great. United States Steel Corporation common stock sold up to 261 in 1929 and declined to 21 in 1932. Such a decline completely obliterated any advantages of profit sharing to the workers. In fact it subjected most of them to serious losses which they could ill afford. Again, profit sharing, confirmed to a few of the top officials, as in some American corporations, does improve the company's operations but it has no significance for the general economy in smoothing fluctuations of the business cycle or in lessening the pressure for the extension of State capitalism.

V. Opposition to Profit Sharing

(A) Union Opposition

One hundred years ago when Leclaire attempted to introduce it, profit sharing was criticized by labor in France as an attempt to reduce wages. In 1923–25 the British Trade Union Congress rejected copartnership and profit sharing as a device to mislead workers and prevent trade-union solidarity. The union leaders' opposition is due to the fear that harmony of interest between employer and employee would tend to the abandonment of unions, to an aversion to strike and to lessening the importance of labor union leaders, whose function depends on a conflict of interests. There are many companies with long experience in profit sharing where none of these fears have proven justified. In fact under a scheme of profit sharing, intelligent union leadership finds greater scope for activity, for interest in the management and for the development of labor-saving devices and practices. The recent Steel Workers Organizing Committee pamphlet urging workers to apply scientific management to increase output per man is a token of a new spirit. The opposition of union leaders indicates a lack of fundamental understanding. Profit sharing should develop a new and a high type of labor leader—the economic statesman—which our increasingly complicated economic life requires and should enable intelligent laborers to rise to managerial ranks.

(B) Workers' Opposition

It is said that the workers object because the participations are small. A profit-sharing participation equal to 5 percent of the year's wage is equivalent to a Christmas bonus or less than the workers may obtain in one successful strike. However, a year-end bonus is a gift, but profit sharing becomes a worker's right. In Leclaire's profit-sharing plan the worker received 17 to 20 percent of the yearly wage. In many companies the workers have independent accountants auditing the books before the final sums are determined. Furthermore, a successful strike may be expensive, a Pyrrhic victory. Profit sharing insures continuity of employment and a resulting higher annual wage. Early plans of profit sharing were often ended by strikes, but there are records of several decades of successful operation of such plants without any labor disturbance.

(C) Employers' Opposition

Employers oppose profit sharing on various grounds. Some say that the worker requires stable wages. However, reread in terms of society this means that workers require rigid wages. This thesis cannot be true because rigid wages cause violent fluctuations in employment. For the worker as well as for the investor, half a loaf is better than no bread.

Universal, free, and compulsory education and universal suffrage grew out of the industrial revolution, and mass production and the trend from the farm to the city. In turn, universal education and universal suffrage are modifying the system which gave them birth. The masses are taught what to want and with the vote are proceeding to take it. Recognition of this simple fact should make the intelligent thinker on social problems open-minded. Since change is inevitable, is it not wiser to control its gradual development rather than to check it and create social crises?

(D) POLITICAL IMPLICATIONS OF LABOR OPPOSITION TO PROFIT SHARING

The opponents of profit sharing should weigh the evils of State ownership and control. The labor opponents should remember that the Government often pays very low wages, as in the post office. Employees in State plants generally have not the right to strike. The opportunities for promotion are fewer in Government-owned plants, where political pull rather than individual efficiency is the consideration. Last but not least, State capitalism has destroyed labor unions in several countries.

(E) POLITICAL IMPLICATIONS OF EMPLOYERS' OPPOSITION

Many large businessmen are now turning to the Government, almost like the unemployed laborer looking for relief and aid. Such a tendency can result only in the gradual decay of the system of private enterprise. The end of the road is known. Other nations have traveled it. If the employers would avoid State control, they should not simultaneously oppose profit-sharing for it will afford at least a temporary stay and a transition stage, even if State capitalism should, as is unlikely, prove to be the ultimate goal. It need not be so. A system of profit-sharing would give all the benefits of private enterprise and many of the benefits that are claimed for State capitalism. As for the public officials, they themselves are reluctant to force the extension of State control, if only for the lack of an adequate personnel.

VI. Profit-Sharing and Reconciliation of Conflicting Claims

(A) COOPERATION VERSUS ANTAGONISM

At present private enterprise is run on the basis that every group takes as much and gives as little as possible. Such a system is essentially based on antagonism. Interests now conflict. Labor wishes high wages. Capital wishes a high return. The management wishes large compensation. The consumer wishes lower prices. The State wishes higher taxes. At present these conflicts are resulting in perpetual maladjustments. If one substitutes for internal competition between these groups the cooperation of worker, owner, and management for the common end, the consumer must benefit and the State should have stable tax receipts and less expenditure for relief. In profit-sharing the latent but dynamic factor of mutual aid and cooperation becomes active. Instead of quarreling about how to divide a small pie, there is concerted effort to increase the size of the pie. Some new balance should arise. If labor is represented in the management, it will have an opportunity to protect the small investor against concentrated and arbitrary large blocks of stockholders or against fraudulent managements. Labor directors should constitute an additional protection for the small stockholder and additional warranty for the ethical conduct of corporate affairs. A sympathetic attitude between management and labor should develop. The workers should become more efficient. Private capitalism in our own country could adopt some of the spirit of cooperation and copartnership which has been carried to such a high degree in Denmark and Sweden, countries noted for their economic and political stability.

(B) THE EDUCATION OF THE WORKERS

Bookkeeping is the alphabet of business. Profit-sharing teaches the worker the elements of bookkeeping. Would the rank and file of workers in the steel and railroad industries, under a policy of profit-sharing, have voted for retaining peak wages during a period of violent contraction of business? A system of profit-sharing would train the worker not merely in the elements of accounting but in the problems of management and administration. An independent audit by the accountants for the labor unions would be a great factor for peace in times of conflict between management and men. The 10-year record cited above, of the United States Steel Corporation and Westinghouse Electric & Manufacturing Co. shows how the workers are already getting the great bulk of the receipts from sales of the corporations. The workers through their education in simple bookkeeping, could be cured of the idea that wages can be increased without limit, or independently of gross corporate income. They would then participate with the management in increasing the net sums available for distribution between capital and labor. Indeed arithmetic would become in a new sense the mother of safety—economic safety as well as political safety.

VII. Political Alternatives and Future Trends

(A) PRIVATE ENTERPRISE OR STATE CAPITALISM

Aside from the economic or cyclical factors, profit-sharing has political implications.

There is a great struggle in the world today between two compet'ng systems. The system of capitalism or private profit by individual initiative on the one hand, and the system of State ownership and State control on the other. Great Birtain and America and the democracies generally, particularly the Scandinavian countries, are functioning under the system of private enterprise. Russia, Germany, and Italy have State capitalism in various forms. This difference in policy may be a difference in psychology. In private enterprise the individual tries to solve the problem locally by cooperation within an industry. The government remains the servant. Under State capitalism, private enterprise steps aside and the government attempts to solve the problem centrally and becomes the master. In the former case the citizen supports the government; in the latter case the government tries to support the citizen. In the former case, administration is decentralized and supple. In the latter case it is rigid and centralized in a bureaucracy. In the former case the standards of living are high; in the latter case the standards of living are low.

If we avoid those wage practices which cause violent fluctuations in the economy. with the resulting national economic instability and insecurity for the individual, and the turning toward government for relief, we can continue to function under our system of private enterprise. Certainly not until State capitalism has proven more workable, more efficient, a better provider of goods and of a high standard of living somewhere in the world, would it seem desirable to abandon the existing economic mechanism which has served the masses so well and to substitute State capitalism for it.

Yet in the United States there has been a great rush to the public ownership of utilities. The result has been to extend State capitalism, thus drying up the sources of private risk-capital which could have furnished jobs to millions now idle. If we had applied the British scheme of a three-fold partnership of capital, labor, and the consumer in a flexible plan of profit-sharing and rate reduction, we might have averted the current crisis in the utility industry. Consumers' rates would have gone down automatically on a sliding scale. Capital would have been attracted into the industry. Wages, including the profit-sharing bonus, would be higher. The State has no special advantages over private enterprise in the operation of utilities. In England the municipal gas works suffered some of the worst strikes. They also do not have any profit sharing. Even before the war the tendency toward State ownership and State management—what the French call étatism—had already produced its own antidote, namely, revolutionary syndicalism, whose leader before the war was Georges Sorel. However, profit sharing and copartnership can offer the worker and society the best that syndicalism had to offer, without its violence and its antagonism to the State.

(B) TOWARD INDUSTRIAL DEMOCRACY

Not merely the United States but the entire world is in a critical stage in political and economic evolution. State management and control is manifested in the Communist-Fascist-Nazi countries and is everywhere on the uptrend. It is a new and untried field, of doubtful efficiency and not satisfying the ideals of individualism. The system of private enterprise has the manifest advantages of flexibility and opportunities for individual effort. Profit sharing between capital and labor, with labor represented on the board, opens possibilities of an evolution along new lines. It would provide the basis for that gradual growth which is essential if we are to avoid the revolutionary violence which has attended the emergence of State capitalism elsewhere. The elements for such a development are all here; in each industry a few large corporations with Nation-wide markets and Nation-wide employers of labor. It needs but the breath of a new spirit to make it possible for them to evolve slowly in the general direction of industrial democracy. If the monopoly investigation seeks to break up these large corporations into small units, it will only succeed in turning back the hands of the clock—a sort of nostalgia for a day long past. If our economic evolution is to go forward, profit sharing and copartnership would seem to afford a prudent, practical next step in a gradual economic evolution.

VIII. Economic Statesmanship

A. No one knows or can see very far ahead into the future, not even the statesmen who are creating that future. Would it not seem the part of prudence to provide alternate methods of economic evolution and then to test each program and institution by its results? The system of private ownership and wage service has to its credit the technical achievements and dynamic advances in the standard of living during the past century. No age and no system has produced even faintly comparable results. In the Communist-Fascist-Nazi world, state socialism is developing. Its characteristics are compulsion and political pressures—a system slow and unadaptable and lacking in initiative. In the middle ground there could evolve private ownership with voluntary cooperation in the great corporations. Instead of wage service, there might be some form of profit sharing and a sense of participation in the industry, free from political pressures of state capitalism. Initiative would remain alive. High adaptability would continue. If the trend abroad toward state capitalism continues and if in the democratic countries profit sharing and cooperation develop, there could then be a test indeed as to which method produces the best goods at the lowest prices and affords the highest standards of living for the workers in the industry.

The history of economic man has been first slavery, then serfdom, then indentured servants, and more recently wage payment for service. Decades ago profit sharing as a free partnership and cooperation between labor and capital rose. It began with the religious background of Robert Owen, St. Simon, and the Christian Socialists. As it developed, it proved to be essentially practical and sound. State capitalism seems to be a reversion to semi-serfdom.

Berle and Means in "The Modern Corporation and Private Property," say that "business practice is increasingly assuming the aspect of economic statesmanship," and the Berle Memorandum on Monopolies, of August 1938, lays down these tests for economic organization:

1. Does it provide an adequate supply of goods?
2. Does it provide a maximum number of people with an opportunity to make a living?
3. Does it accomplish this process with due regard for labor and self-development of the individual?

Against these tests Mr. Berle cites:

1. The claim of the consumer for the product.
2. The claim of labor not merely for an hourly rate but for an annual income, permanent jobs, sick relief, and pensions.
3. The claim of capital for a return sufficient to induce the investment of capital.
4. The claim of management for pay not only but also for prestige.

By all of these tests profit-sharing seems the superior method of economic organization. All these claims can be best met by a form of organization in which capital, labor, and management cooperate voluntarily. Critics of the corporation and of modern society charge and cite concentration of wealth and power in great economic aggregations, absentee ownership, the separation of ownership and management, the separation of ownership and labor. A scheme of profit sharing would give the worker a sense of ownership in the plant to the extent that he participates in the profits. It would give labor a sense of management through its representation on the board. It would reconcile many of the conflicting interests whose maladjustment has created some of the political and social problems of the day. It would synthesize the three elements, labor, ownership, and management, in a way that characterized the simple economy of hand production and craftsmanship.

IX. Recommendation

The study of profit sharing by the Senate committee should be extended to its broader aspects. The witnesses should include some of the best economists of the country who have studied the problems of labor and cyclical fluctuations and some of the political scientists who have been studying trends toward state capitalism throughout the world. A commission on profit-sharing, somewhat similar to the recent Commission on Labor Relationships Abroad might well go to Europe to study the successful experience over many decades in the several countries abroad.