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SENATE

{ REPORT
{ No. 920

TO ABOLISH THE SEVEN-YEAR REGAUGE OF DISTILLED SPIRITS

JANUARY 22 (calendar day, JANUARY 24), 1925.—Ordered to be printed

Mr. SMOOT, from the Committee on Finance, submitted the following

REPORT

[To accompany H. R. 9138]

The Committee on Finance, to whom was referred the bill (H. R. 9138) to authorize the discontinuance of the seven-year regauge of distilled spirits in bonded warehouses, and for other purposes, having considered the same, report it favorably, without amendment, and recommend that the bill do pass.

The purpose of this bill, and the favorable recommendations of the Treasury Department, as set forth in their letter of January 29, 1924, to Hon. William R. Green, chairman of the Ways and Means Committee of the House of Representatives, are contained in House Report No. 701, which is attached hereto and made a part of this report, as follows:

[House Report No. 701, Sixty-eighth Congress, first session]

The Committee on Ways and Means, to whom was referred the bill (H. R. 9138) to authorize the discontinuance of the seven-year regauge of distilled spirits in bonded warehouses, and for other purposes, having had the same under consideration, report it back to the House without amendment, and recommend that the bill do pass.

Under existing law distilled spirits in bond are gauged three times: (1) When they are entered into bond, (2) before they have reached the age of seven years, and (3) when they are released from bond. The object of this legislation is to remove the requirement for a regauge before the end of seven years, which has become unnecessary by reason of the national prohibition act and the concentration of these distilled spirits in Government warehouses. The bill also reduces the evaporation and leakage allowance for distilled spirits held in bond more than seven years, by making the allowance apply every six months instead of every four months. It will be observed that the maximum allowance is fixed and definite.

The tax on distilled spirits attaches as soon as they come into existence as such, under the provisions of section 3240 of the Revised Statutes. Section 3293 of the Revised Statutes provides that the tax shall be paid within eight years from the date of the production of the spirits or entry into the warehouse. In recognition

of the fact that spirits stored in bonded warehouses sustain certain bona fide losses, it is provided in section 50 of the act of August 27, 1894, as amended by the act of March 3, 1899, that, under certain conditions and with specific limitations, allowance may be made for losses from packages in bonded warehouses. These allowances are expressly scheduled in the act of August 27, 1894, as amended to cover the maximum "leakage and evaporation period" of 84 months.

Under the above statutes the bonded period exceeds the leakage period by one year, but no loss allowance is made for the time the spirits remain in bond after seven years. The law requires that in order to obtain the allowance authorized for the seven-year period the distiller shall, prior to the expiration of such period, file a request for the making of a regauge on which to base the allowance, otherwise the regauge and allowance can not be made.

The revenue act of 1918, section 600 (b), indefinitely extended the time within which spirits produced prior to September 6, 1917, for beverage purposes, may remain in bond, and provided additional leakage allowances for that class of spirits, but stipulated that all conditions imposed by section 50 of the act of August 27, 1894, must be met before the additional allowances may be made.

Thus, an anomalous situation was created. The request for a seven-year regauge must be made and the spirits regauged pursuant thereto, but it readily can be seen that under present conditions such a regauge is of little, if any, value, as a regauge must be made upon withdrawal for consumption. In fact, the reasons for the creation of this seven-year regauge passed with the enactment of the national prohibition act and section 600 (b) of the revenue act of 1918, for, as pointed out the bonded and leakage periods were both indefinitely extended as to distilled spirits produced prior to September 9, 1917.

There are in bonded warehouses in the United States approximately 150,000 barrels of distilled spirits which would require a regauge under the present law. Such regauging, at an approximate cost of 10 cents per barrel, would cost the Government about \$15,000. Furthermore, to regauge these spirits would work a hardship upon the Government, since a sufficient number of internal revenue gaugers are not available, and the appropriation for such services has been greatly curtailed. The requirement that the request for regauge must be made before the end of the seven-year period works a hardship on taxpayers in many individual cases. For example, where no request has been filed by the owner for a regauge, either through oversight or ignorance of the law, the tax must be paid on the original content of the package despite any loss which might have occurred by leakage and evaporation and without any fault on the part of the owner. The probability of such occurrences is made much greater by present conditions. Under the act of February 17, 1922, spirits are deposited in warehouse under bonds of the owners who, in a large number of cases, are totally unaware of the requirements of the internal revenue laws, and in many instances these owners do not know where the distilled spirits are concentrated. The same situation, somewhat aggravated, is encountered in the case of a seizure of a bonded warehouse, particularly if the seizure fails. In such cases the distiller or warehouseman usually concludes that the spirits being seized are under control of the Government and no need for the filing of a request for the seven-year regauge exists; then when the spirits are released for removal to concentration warehouses, as is often done, the actual owner is required to pay the tax on the original gauge although failure to file the request was no fault of his.

The following letter from the Secretary of the Treasury, dated January 29, 1924, explains the purposes of the bill in detail:

TREASURY DEPARTMENT,
Washington, January 29, 1924.

HON. WILLIAM R. GREEN,
Chairman Ways and Means Committee,
House of Representatives.

MY DEAR MR. GREEN: I have the honor to submit for your consideration, and in the event you deem it appropriate, a provision to be included in the proposed 1924 tax bill as an administrative provision, as follows:

"That upon withdrawal of distilled spirits from bond, in lieu of the allowance provided in section 600 (b) of the revenue act of 1918 an allowance of one proof gallon for loss by leakage or evaporation for each period of six months, or fraction thereof, in bond after seven years from the date of original gauge, shall hereafter be made in addition to, and under the conditions imposed by, section 50 of the act entitled 'An act to reduce taxation, etc.,' approved August 27, 1894, as to package of a capacity of not less than forty wine gallons: *Provided*, That any allowance for loss by leakage or evaporation under section 50 of the act approved

August 27, 1894, as amended, and the additional allowance herein provided, shall be made notwithstanding a regauge has not been made on request of the distiller prior to the expiration of eighty-four months from the date of original gauge: *And provided further*, That in cases where such regauge has heretofore been made it shall be disregarded in determining the allowance for losses upon withdrawal of any package of spirits from bond. This section shall not apply to packages of spirits withdrawn from bond prior to the date on which this act becomes effective."

Recent developments resulting from the concentration of bonded whiskies into a smaller number of warehouses make it desirable that the regauge of spirits within seven years be dispensed with. I am advised by the legal officers of the Internal Revenue Bureau that this can not be done without legislation.

Section 50 of the act of August 28, 1894, provides in part as follows:

"That the distiller of any distilled spirits deposited in any distillery warehouse, or special bonded warehouse, or in any general bonded warehouse established under the provisions of this act may, prior to the expiration of four years from the date of original gauge as to fruit brandy, or original entry as to all other spirit, file with the collector a notice giving a description of the packages containing the spirits, and request a regauge of the same, and thereupon the collector shall direct a gauger to regauge the spirits and to mark upon each such package the number of gauge or wine gallons and proof gallons therein contained. If upon such regauging it shall appear that there has been a loss of distilled spirits from any cask or package, without the fault or negligence of the distiller thereof, taxes shall be collected only on the quantity of distilled spirits contained in such cask or package at the time of the withdrawal thereof from the distillery warehouse or other bonded warehouse: *Provided, however*, That the allowance which shall be made for such loss of spirits as aforesaid shall not exceed * * *: *And further provided*, That in case such spirits shall remain in warehouse after the same have been regauged, the packages containing the spirits shall, at the time of withdrawal from warehouse and at such other times as the Commissioner of Internal Revenue may direct, be again regauged or inspected; and if found to contain a larger quantity than shown by the first regauge, the tax shall be collected and paid on the quantity contained in each such package, as shown by the original gauge: *And provided further*, That taxes shall be collected on the quantity contained in each cask or package as shown by the original gauge where the distiller does not request a regauge before the expiration of four years [extended to seven years by the act of March 3, 1899] from the date of original entry or gauge: *Provided also*, That the foregoing allowance of loss shall apply only to casks or packages of a capacity of forty or more wine gallons, and that the allowance for loss on casks or packages of less capacity than forty gallons shall not exceed one-half the amount allowed on said forty-gallon cask or package; but no allowance shall be made on casks or packages of less capacity than twenty gallons: *And provided further*, That the proof of such distilled spirits shall not in any case be computed at the time of withdrawal at less than one hundred per centum."

Section 2 of the act of March 3, 1899, amending the act of August 28, 1894, extended the leakage and evaporation period to 84 months.

Section 3248, Revised Statutes, provides that tax shall attach to the substance known as distilled spirits as soon as it is in existence as such. Under this section of law the tax was collected on the original contents of every package of spirits. In recognition of the fact that spirits stored in bonded warehouses inevitably sustain certain bona fide losses, it was eventually provided that under certain conditions and within specific limitations allowance might be made for losses from packages in bonded warehouses. These allowances are expressly scheduled in the act of August 28, 1894, as amended to cover a maximum "leakage and evaporation period" of 84 months.

It will be noted that the "bonded period" or the period during which spirits might remain in bond, prior to prohibition, exceeded the leakage period by one year. This came about through a compromise between the distillers and the Government. The bonded period was originally of only a few years' duration and the leakage period coincided therewith. The bonded period, at the instance of distillers, was later lengthened, as was the leakage period, but not to the same extent. It is obvious that the longer the period within which allowance for loss may be made the less the tax collected on the package will be. Congress, therefore, compromised by granting the eight-year bonded period, but at the same time provided that losses sustained during only seven years thereof might be allowed.

One of the conditions imposed precedent to allowances for losses sustained was that the distiller should, prior to the expiration of the seven-year period, file a request for a regauge on which to base the allowance. It has been repeatedly held by the legal officers of this department that this condition of the law is mandatory and that in the absence of such request no allowance whatever may be made.

With the coming of prohibition the situation was changed. The time within which spirits might remain in warehouse was automatically and indefinitely extended; in fact, it was compulsory that they remain until a legal withdrawal might be made under the new law. Hence, in equity, it was necessary that the leakage allowance be enlarged, and, in section 600 (b) of the revenue act of 1918, this was done; but the section stipulated that all conditions imposed by section 50 of the act of August 28, 1894, must be met before the additional allowance might be given.

This created an anomalous situation. The request for a seven-year regauge must be made and the spirits regauged pursuant thereto, but at present such a regauge is of little, if any, value. The reasons for its creation passed with the enactment of the national prohibition act, for, as pointed out, the bonded and leakage periods were both indefinitely extended ipso facto. Few internal revenue gaugers are now available and the appropriation for such service has been greatly curtailed. As a whole, I believe a continuance of the seven-year regauge will cost more than can be gained thereby.

Moreover, the rule that a request for regauge must be made before the end of the seven-year period works a hardship on taxpayers in many individual cases; as, for example, where, through ignorance or oversight, no request is filed tax must be paid on the original contents of the package, despite any loss which might have occurred. The probability of such occurrences is made much greater by present conditions. Under the concentration act of February 17, 1922, spirits are deposited in warehouses under bonds of owners, who in a large number of cases are totally unaware of the requirements of internal revenue law. The distillers, on whom the condition was originally imposed, do not know, generally, where the spirits are and would not concern themselves if they did, under the new arrangement.

The same situation, somewhat aggravated, is encountered in the case of a seizure of a bonded warehouse by the Government, particularly if the subject of the seizure is a general bonded warehouse. Spirits stored in general bonded warehouses are ordinarily owned by parties other than the distiller, and the distiller may not even know that spirits of his production are in existence; the owner, who may hold a power of attorney from the distiller authorizing the filing of internal-revenue papers, usually does not know a request for regauge is required, or it may be concluded by the party responsible that the spirits, being seized and under the control of the United States, no need for the filing of the requests exists. Still, where the seven-year period terminates during the seizure, and no request was filed, if the spirits are released, as is usually done, no loss allowance may be made.

The provisions of internal revenue law relating to this subject of seven-year regauge were harsh. They are, however, plain and mandatory. The Congress, in its wisdom, felt that such provisions were required for the protection of the revenues when the tax on liquors provided one of the major sources of revenues. Several new provisions of law in the past few years have afforded some relief in the matter of losses of distilled spirits from packages while in bond. The matter of the seven-year regauge, which is one of the most serious problems in that regard, must still be remedied. I, accordingly, have the honor to recommend that provision of law be made to afford this relief.

Sincerely yours

A. W. MELLON,
Secretary of the Treasury.

