

627-6

REVENUE ACT OF 1940

HEARINGS

BEFORE THE

COMMITTEE ON FINANCE UNITED STATES SENATE

SEVENTY-SIXTH CONGRESS

THIRD SESSION

ON

H. R. 10039

AN ACT TO PROVIDE FOR THE EXPENSES OF NATIONAL
PREPAREDNESS BY RAISING REVENUE AND
ISSUING BONDS, TO PROVIDE A METHOD
FOR PAYING FOR SUCH BONDS,
AND FOR OTHER PURPOSES

JUNE 12, 13, AND 14, 1940

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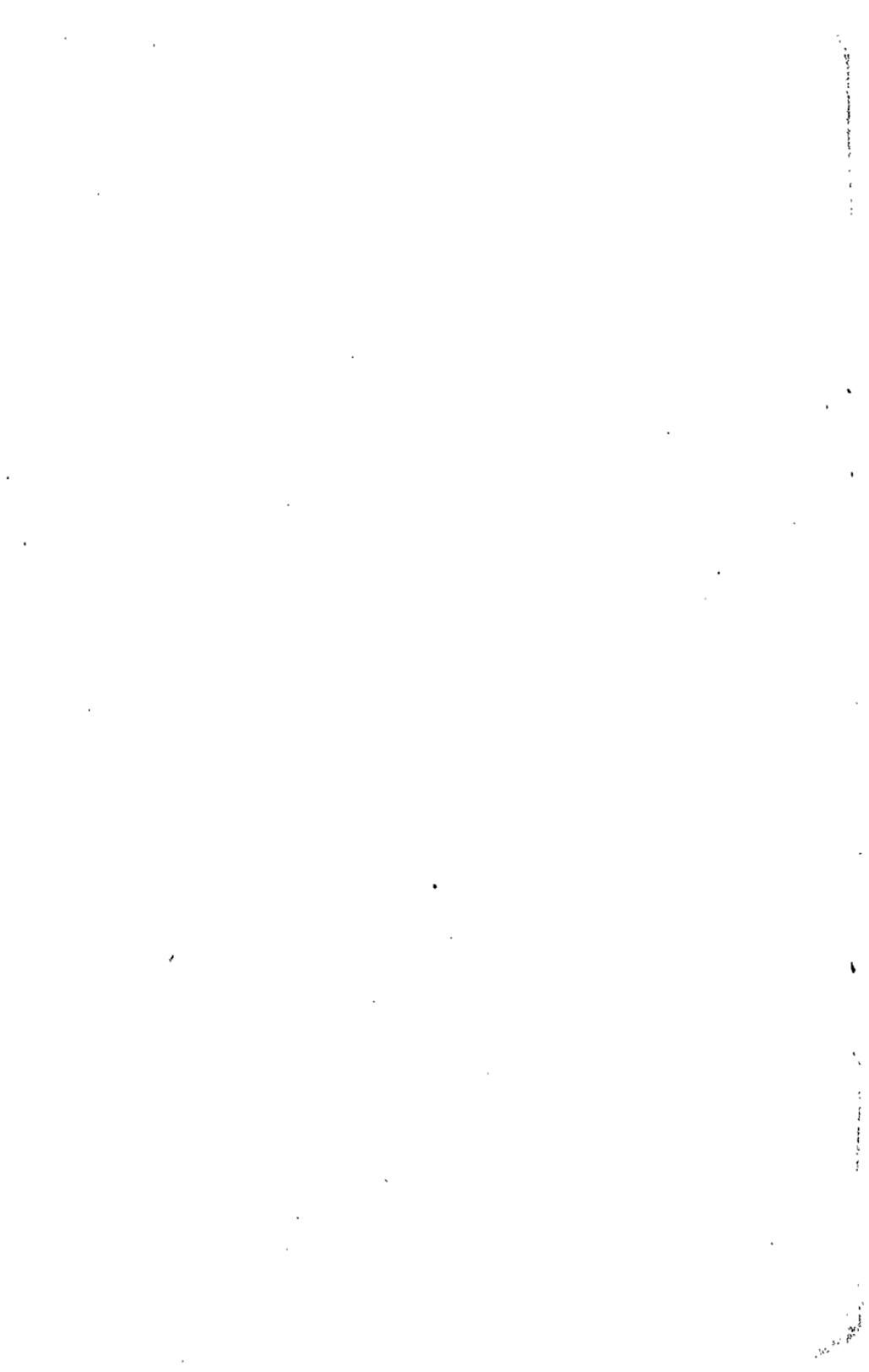
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REVENUE ACT OF 1940

WEDNESDAY, JUNE 12, 1940

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

The committee met, pursuant to call, at 10 a. m., in room 312, Senate Office Building, Senator Pat Harrison (chairman) presiding.

The CHAIRMAN. The committee will be in order.

We have met this morning for the purpose of considering H. R. 10039, the Revenue Act of 1940, which passed the House of Representatives last night.

The CHAIRMAN. We have the Secretary of the Treasury before us and other representatives of the Treasury Department. Mr. Secretary, the committee desires to hear any statement or explanation you desire to make concerning H. R. 10039.

You may proceed.

STATEMENTS OF HON. HENRY MORGENTHAU, JR., SECRETARY OF THE TREASURY; HON. DANIEL W. BELL, UNDER SECRETARY OF THE TREASURY; AND HON. JOHN L. SULLIVAN, ASSISTANT SECRETARY OF THE TREASURY

Secretary MORGENTHAU. Mr. Chairman, I am here today to give my support to the pending bill for increasing the revenue of the Government and raising the limit of the public debt to meet urgent needs of national preparedness.

Since the members of this committee are thoroughly acquainted with the fiscal situation, I will do no more than review it briefly.

The President in his Budget message of January 3, 1940, estimated that expenditures for the fiscal year 1941 would exceed normal receipts by \$2,876,000,000. He anticipated that recovery of excess capital funds from Government corporations would yield \$700,000,000, and he recommended that \$460,000,000 additional taxes be imposed to cover emergency defense expenditures. This left an estimated deficit of \$1,716,000,000 to be financed by borrowing.

Events since that time have made it urgently necessary to increase expenditures for national preparedness far beyond the amounts included in the 1941 Budget. It is estimated that, on the basis of appropriation bills which have passed and those which are now pending in Congress, expenditures for the fiscal year 1941 will exceed by \$4,350,000,000 the revenues so far provided.

The borrowing power remaining under the existing debt limit was, on May 31, 1940, \$1,950,000,000, and it is estimated that by June 30, 1940, the unused borrowing power will have shrunk to \$1,700,000,000.

In the light of the proposed additional expenditures for national preparedness, it is anticipated that, unless the Congress acts to relieve the situation, the Treasury's authority to borrow will be completely exhausted by the end of January 1941 and the working balance of the Treasury will be too low for safety. Such a situation calls for prompt action by this Congress.

The Treasury working balance is now approximately \$1,200,000,000. It would be undesirable to permit it to fall much below this level. Reduction of the balance would yield no significant saving in interest cost. When viewed from the standpoint of the insurance and financial security which a large Treasury balance affords, the interest cost of the Treasury bills issued to maintain the balance is small—at current rates it amounts to only \$130,000 a year. The maintenance of a substantial balance is distinctly in the interests of economy and financial strength because it gives to the Treasury the flexibility in the timing of the issue of securities desirable at all times and particularly needed in times such as these.

The financing of the increase of Federal expenditures for national preparedness requires provision for additional taxes, or a decrease in other expenditures, or an increase in the national debt beyond the present statutory limit. In my judgment all three steps are required.

This bill provides for raising additional revenue of \$729,000,000 for the fiscal year 1941 and approximately \$1,000,000,000 yearly thereafter.

The public is willing and ready to accept the additional burdens necessary to support adequate national defense.

It is important not only to increase revenue with which to help finance our preparedness program, but also to cut expenditures wherever feasible. However, I disapprove of random reductions in appropriations which are likely to enforce premature curtailment of expenditures for relief, retardation of the necessary execution of public works, or impairment of essential administrative services.

The enlarged preparedness program will increase employment but its effect will not be immediate. There will inevitably be a lag of some months. To take men off work-relief rolls before the preparedness program has its effect on employment would hamper rather than help our purpose of mobilizing a great national effort to strengthen our defenses.

I am also opposed to placing a disproportionate part of the cost of our national-defense program upon Federal employees by reducing their salaries. Along with the rest of the people of this country they will make an increased tax contribution in accordance with their ability to pay. The new taxes will apply equally to them as to other individuals. Many Government employees, too, are already making extra contributions in the form of added hours of work without pay.

I strongly favor the passage of legislation to raise emergency revenue for purposes of national preparedness in the amounts provided in this bill as well as the provisions of the bill raising the limit of the public debt.

Members of the Treasury staff are here and are prepared to discuss technical details with you.

Thank you.

The CHAIRMAN. Thank you very much, Mr. Secretary.

Senator BYRD. I would like to ask Mr. Morgenthau what are the estimated expenditures for the fiscal year beginning July 1?

Secretary MORGENTHAU. Could Mr. Bell answer that, Mr. Chairman?

The CHAIRMAN. All right, Mr. Bell.

Mr. BELL. The estimated expenditures for the fiscal year 1941 are \$10,000,000,000, and that includes contemplated expenditures from all appropriation estimates which have recently been submitted to the Congress by the President, but it does not include the \$320,000,000 added yesterday by the House to the Army bill.

Senator BYRD. For the purpose of clarification, just let us take the original Budget submitted in January. What additions do you estimate, and for what purposes, to that figure of \$8,400,000,000?

Mr. BELL. Do you want the details of the increase?

Senator BYRD. Well, along general lines, how much for national defense, how much for additional relief, and so forth?

Mr. BELL. \$1,300,000,000 approximately for national defense and about \$300,000,000 additional for relief. I am assuming there that advantage might be taken, under the provisions of the relief bill, to spend the billion dollars in 8 months.

Senator BYRD. In other words, you admit, then, that the total expenditures will only be a billion dollars more than contemplated in January?

Mr. BELL. No, sir; they are about a billion six hundred million dollars more than contemplated in the January budget for the fiscal year 1941.

Senator BYRD. How much more do you intend to spend for the national defense for the coming year than has been spent up to the present time?

Mr. BELL. \$1,300,000,000 more in 1941 than was contemplated last January when the Budget was submitted. \$1,600,000,000 under the heading of "Emergency".

Senator BYRD. We saw announcements in the newspapers of billions and billions for national defense. That is not going to be spent this coming year?

Mr. BELL. Not all of it. It will be under contract and will run heavily the last 6 months of the fiscal year 1941, and heavier in the first 6 months of fiscal year 1942.

Senator BYRD. You think this is a safe estimate of the total of \$10,000,000,000, in view of these continued appropriations for national defense that come to us practically every day?

Mr. BELL. I think that is a fair estimate. Possibly the Army and Navy people would give you an estimate a little higher for national defense expenditures, but we tried to make it as fair as we could, based on our previous experience with similar estimates.

Senator BYRD. This \$1,600,000,000 additional for national defense will be distributed approximately how? How much for the Navy and how much for the Army?

Mr. BELL. Are you talking about the whole 3 billion or the emergency, Senator?

Senator BYRD. I am more interested in the emergency. If you can give both figures, very well.

Mr. BELL. I think I will have to put that in the record. It will take some little time to figure it out.

Senator BYRD. Give us the total, then, of the two.
Mr. BELL. I will have to figure that out too.
(The information requested is as follows:)

National defense estimated expenditures for fiscal year 1941

(In millions of dollars)

	War Department	Navy Department	Total
On basis of estimates included in 1941 Budget	804	1,041	1,835
On basis of supplemental estimates contained in the President's messages of May 10 and June 3, 1940	755	500	1,315
Total	1,559	1,541	3,250

Senator BYRD. Assuming that the total expenditures are 10 billion and we have an increase of taxation and the revenue will be 5½ billion—

Mr. BELL. The revenue will be \$5,652,000,000. That is exclusive of social-security taxes.

Senator BYRD. That makes a deficit of 4½ billion.

Mr. BELL. \$4,349,000,000 net.

Senator BYRD. Then if this revenue bill is passed, the deficit will be something about \$3,000,000,000?

Mr. BELL. No, only \$729,000,000 additional revenue is estimated for the fiscal year 1941, leaving a deficit of about \$3,600,000,000.

Senator BYRD. \$500,000,000 will be obtained from a reduction of expenditures, and that would reduce it to 2½ billion?

Mr. BELL. I do not think it would go quite that far. Four billion three hundred million is the estimated deficit, take off \$700,000,000 representing additional revenue to be received in 1941 under this bill would give you a deficit of \$3,600,000,000 and then take off \$500,000,000 for savings would give you about \$3,100,000,000.

Senator BYRD. \$700,000,000 is increased taxes?

Mr. BELL. Yes.

Senator BYRD. Would it not be 1 billion increased taxes?

Mr. BELL. Not in 1941, Senator Byrd. Only about \$700,000,000 in 1941. The billion dollars is based on the full year's receipts.

Senator BYRD. Four billion three hundred million and \$700,000,000 from that would be \$3,600,000,000.

Mr. BELL. That is right.

Senator JOHNSON: That is \$729,000,000.

Senator BYRD. The deficit, then, would be approximately 3 billion in the event the expenditures were reduced \$500,000,000.

Mr. BELL. That is right.

Senator BARKLEY. When you speak of the additional \$300,000,000 for relief, based on the expenditure of this billion in the bill now under consideration within 8 months, you take into consideration that in the Budget in January, as I recall, the total expenditure appropriated for relief for the 12 months' period was a billion?

Mr. BELL. That is right, approximately a billion.

Senator BARKLEY: A little more than a billion. So that if the billion we are appropriating is expended in 8 months and the Congress would appropriate for the remaining 4 months at the same rate, it would take more than \$300,000,000 to make up that difference, would it not?

Mr. BELL. It would on that basis, but the 8 months practically takes you through the whole winter and we have estimated that it would be less in the last 4 months than it would be in the previous 4 months.

Senator BARKLEY. So that your estimate is that \$300,000,000 would cover it for the last 4 months of the fiscal year?

Mr. BELL. Yes, sir; and again I am assuming that the national-defense expenditures will be heavy in those last 4 months, much heavier than in the previous 8 months.

Senator BARKLEY. Are you assuming also that there will be some lessening of unemployment due to the increased Budget expenditures for national defense?

Mr. BELL. I think that the \$300,000,000 takes that into consideration.

Senator KING. There are so many uncertain factors, are there not, that it is impossible to predict with any degree of certainty just what the deficit will be and what the expenditures will be for national defense and relief and for other purposes?

Mr. BELL. We have made our estimates on the basis of the submissions by the President to Congress up-to-date, and the best we can do is estimate them; yes, sir.

Senator BARKLEY. One other question I overlooked.

In your estimate of the amount to be actually spent during the fiscal year 1941, you stated that much more than that would be contracted for, obligations entered into. If the contract should be more speedily executed than is now estimated, the amount of actual expenditures in the fiscal year would correspondingly increase, would it?

Mr. BELL. That is right; yes, sir.

Senator GEORGE. Mr. Bell, may I ask this: You do not contemplate by this bill, as passed by the House, the raising of the debt limit for ordinary expenditures, do you?

Mr. BELL. No, sir; the \$4,000,000,000 increase is for national defense.

Senator GEORGE. So that the debt limit will remain as now fixed in law?

Mr. BELL. \$45,000,000,000.

Senator GEORGE. Approximately \$45,000,000,000?

Mr. BELL. Exactly \$45,000,000,000; it is fixed at not to exceed \$45,000,000,000 face amount of obligations outstanding at any one time.

Senator GEORGE. Well, I understand, but we had quite a discussion here before as to whether or not it wasn't something above that—but \$45,000,000,000. So that you are proposing to increase the debt limit by \$4,000,000,000, but that increase is exclusively for the purpose of financing national defense?

Mr. BELL. Yes, sir; that is right.

Senator GEORGE. And could not be used for the financing of any of the ordinary expenditures of Government?

Mr. BELL. No, sir.

Senator GEORGE. That is correct, is it?

Mr. BELL. Yes, sir; that is correct.

Senator KING. Pardon me, will the expenditures be so labeled that you can allocate to the \$45,000,000,000 certain expenditures and allocate to a category above that the expenditures for national defense?

Mr. BELL. In our financial statements we do classify expenditures in such a way that we can tell what goes for national defense. What will happen is this, we probably will meet the first expenditures for national defense out of the general fund, and then we will have to reimburse the general fund from the proceeds of national defense notes sold under this authority. I don't think you can tie them in day by day exactly, and for that reason we will have to have some flexibility.

Senator GEORGE. That is contemplated here?

Mr. BELL. Yes.

Senator CLARK. How do you define national defense, Mr. Bell? We have every sort of scheme under the earth that comes under that. What is the Treasury definition of "national defense"?

Mr. BELL. We classify all of our expenditures on the basis of symbols allotted to various disbursing officers and there is a series of symbols allotted to disbursements under the War and Navy.

Senator CLARK. In other words, you limit national-defense expenditures to expenditures by the War and Navy Departments?

Mr. BELL. Yes.

Senator CLARK. For instance, we have got a lot of schemes in here for building roads and setting up civilian airports and the Florida Canal, and nearly everything you can think of, proposed under the guise of national defense. You don't so classify those things as national defense in keeping your accounts?

Mr. BELL. Not at the present time.

Senator VANDENBERG. Do you include in the 4,000,000,000 that portion of the Budget which heretofore has ordinarily maintained the Army and the Navy?

Mr. BELL. Yes, sir; they are national-defense expenditures.

Senator VANDENBERG. So you take the entire Army and Navy expense, a portion of which has been heretofore a part of the regular Budget, over into your special budget?

Mr. BELL. That part which is applicable to the military branch of the War and Navy, I don't mean flood control and rivers and harbors—that is another classification.

Senator VANDENBERG. After you have done that, leaving your debt limit of \$45,000,000,000 in respect to what you would call the non-defense expenditures, how long will it take you to reach the \$45,000,000,000 in this other category?

Mr. BELL. You mean on the present basis?

Senator VANDENBERG. Present and prospective.

Mr. BELL. The present Budget estimates that I just gave you—I don't know that I quite understand your question, Senator Vandenberg. You mean assuming that we use the \$4,000,000,000 for financing national-defense expenditures?

Senator VANDENBERG. Yes; I want to know where we stand entirely aside from national defense in respect to your program?

Mr. BELL. If we use the \$4,000,000,000 during 1941 to finance national-defense expenditures, we will end the fiscal year 1941 with approximately \$1,100,000,000 of borrowing power under the \$45,000,000,000 limitation.

Senator VANDENBERG. That is the figure I wanted.

What happens under this program, let us say, in 1942? Suppose we have another big additional defense program in 1942, is it contemplated that that in turn is to be set aside in this special budget?

Mr. BELL. Well, we can operate under the \$4,000,000,000 until it is exhausted, and when that is exhausted Congress will have to take some other action, either increasing that special debt limit or providing additional taxes.

Senator VANDENBERG. Of course, this \$4,000,000,000 contemplates a 1-year series of appropriations. Obviously there will be other appropriations during the 5-years in which these bonds are to be retired, and what I am trying to find out is whether, under your scheme, if we have to have additional appropriations in the following fiscal year, we must then find some additional new taxes to allocate to these special bonds for that purpose?

Mr. BELL. We must find some means of financing those additional appropriations, either through public debt issues or additional taxes.

Senator VANDENBERG. I am afraid I don't make myself clear. You are setting up a financial program which runs over a period of 5 years to pay for a 1-year series of appropriations, is that correct?

Mr. BELL. Well, that is approximately correct, we contemplate about \$3,250,000,000 in national defense notes during the fiscal year 1941 out of the \$4,000,000,000. It may be larger than that, as Senator Barkley has suggested, if the program is speeded up, but whenever the \$4,000,000,000 is exhausted, then some other means will have to be provided, and the taxes levied under Title II of this bill, will be set aside to retire whatever is issued under that \$4,000,000,000 limitation, and will be available for nothing else.

Senator VANDENBERG. So long as you are running on a deficit basis in the general operations of the Government, isn't it more or less of a fiction to talk about any special allocation of taxes to any special purpose?

Mr. BELL. I think setting aside special funds and earmarking them like this, is nothing more than a restriction on the Treasury, but we are used to operating under restrictions, and I take it that that is what Congress wants, and we can operate under it.

Senator VANDENBERG. It is just a matter of comfortable book-keeping?

Mr. BELL. It would be easier for us if the restrictions weren't there, Senator. I wouldn't say it was "comfortable bookkeeping."

Senator VANDENBERG. I would like to ask the Secretary a question, if I may.

In connection with this bond program, do you know of any plan to end a free market in the purchase and sale of United States bonds, any plan either in the Treasury or in the Federal Reserve System, which is being developed for the purpose of concentrating the purchase and sale of United States bonds in the Reserve banks so that the free market is terminated?

Secretary MORGENTHAU. That is a new one to me.

Senator VANDENBERG. You know nothing about it?

Secretary MORGENTHAU. It is the first time I have ever heard about it, but that doesn't mean that somebody may not be working at it, but not in the Treasury.

Senator VANDENBERG. I realize that there is a limitation upon your information as well as mine.

[Laughter.]

Senator TOWNSEND. May I ask a question?

The Secretary said in his statement that on June 30 the borrowing power will have shrunk to \$1,700,000,000?

Mr. BELL. Yes, sir.

Senator TOWNSEND. Now your estimate is that our income will be \$10,000,000,000?

Mr. BELL. No; our expenditures will be \$10,000,000,000.

Senator TOWNSEND. And our income will be \$5,650,000,000, which will leave a deficit of approximately \$4,350,000,000, and with the extra taxes of \$720,000,000, we will still have a deficit of \$3,521,000,000. How are you going to finance that deficit on \$1,700,000,000?

Mr. BELL. That is what this bill is for.

Senator VANDENBERG. No; this bill contemplates—the money that this bill contemplates is to be spent for war materials.

Mr. BELL. You realize that the \$4,350,000,000 deficit includes \$3,250,000,000 of national defense expenditures, so your deficit on the other account is only \$1,100,000,000.

Senator VANDENBERG. Then you figure you will have \$600,000,000 left at the end of this year, of your borrowing power, is that right?

Mr. BELL. It works out about \$1,100,000,000, Senator Vandenberg, because we are assuming in our estimates that we are going to get back from the Governmental corporations and credit agencies the \$700,000,000 capital funds referred to in the President's Budget message of last January.

Senator BARKLEY. Let me ask you, Mr. Bell, the Secretary in his statement said that if nothing is done in the way of raising revenues or increasing the debt limit, the borrowing power of the Treasury will expire, will be exhausted, next February. Now, assuming that the entire \$4,000,000,000 of increase in the debt limit be devoted to the new requirements for national defense, and assuming that for ordinary purposes the borrowing power would be exhausted the first of next February, and inasmuch as the original recommendation was for an increase of \$3,000,000,000 in the debt limit, and the House has made it \$4,000,000,000, why wouldn't it be wise to make it \$5,000,000,000 while we are at it, so that when the borrowing power of the Treasury next February has been exhausted for ordinary purposes they will at least have \$1,000,000,000 more of a borrowing backlog. What is your reaction to that?

Mr. BELL. You are talking about increasing it from \$45,000,000,000 to \$46,000,000,000?

Senator BARKLEY. I am talking about increasing it from \$45,000,000,000 to \$50,000,000,000. You are increasing it here to \$49,000,000,000, 4 billion of which is for defense purposes, and if you run out of borrowing power next February for ordinary purposes you will either have to quit borrowing or we will have to raise your limit then. Why not do it now?

Senator VANDERBERG. The scheme isn't quite as frank as you present.

Senator BARKLEY. I am trying to look as Magnus Johnson said about agriculture, "Take the bull by the tail and look the future straight in the face." [Laughter.]

Senator VANDENBERG. That is exactly what you have done. Now we are getting down to business. [Laughter.]

The CHAIRMAN. Are there any other questions?

Senator BARKLEY. I would like to get an answer to that one. I mean, if we are going to run out of borrowing power for ordinary purposes the 1st of next February, why not face it frankly now, and at least increase the borrowing power another \$1,000,000,000 to take care of that situation?

Mr. BELL. I would like to answer it this way, Senator. First, that it is entirely a matter for Congress to act upon, but we will have enough borrowing authority under the \$45,000,000,000 limitation if you give us this \$4,000,000,000 for national-defense obligations, to get through the fiscal year 1941.

Senator BARKLEY. That will take you up to July 1?

Mr. BELL. July 1 of next year.

If we have another sizeable deficit in 1942, and I don't think we can foretell the future, we certainly will have to have an increase in the regular debt limit at that time.

Senator VANDENBERG. What would be the difference between a straight increase of the debt limit to \$49,000,000,000, or in pursuing this detour?

Mr. BELL. The net effect would be the same, and it would give the Treasury more flexibility if you would make it a straight increase to \$49,000,000,000.

Senator JOHNSON. In this bill, in increasing the debt limit, you not only increase the debt limit but you set up a sinking fund to retire that extra debt limit?

Mr. BELL. That is right.

Senator JOHNSON. Then it is not the same, there is no sinking fund for retiring the regular debt limit.

Mr. BELL. There is a sinking fund, Senator, for the regular debt, but of course as long as you run a deficit in excess of the annual sinking fund, then it does not decrease the debt.

Senator JOHNSON. But this sinking fund would be positive?

Mr. BELL. That is right, there is a special earmarking of funds for this particular purpose here, and there is that difference.

Senator BYRD. The statutory debt payments have been set aside for some time?

Mr. BELL. They have been accumulated and now amount to about \$2,200,000,000.

Senator VANDENBERG. In transferring the regular expense of the Army and Navy establishment in the regular Budget to your special budget, what is the amount of that transfer, do you have that figure? In other words, what have you taken out of the regular Budget and put into this special budget?

Mr. BELL. We haven't set up two budgets, but we will regard approximately \$3,250,000,000 of expenditures in 1941 as coming under the \$4,000,000,000 limitation. There are not two budgets.

Senator VANDENBERG. I don't think I have made my question clear. We had items in the regular Budget for the maintenance and appropriations of the Regular Army and Navy. You have now taken those out of the regular Budget and put them into your calculations, or whatever you want to call them, under this special fund. That is correct, isn't it?

Mr. BELL. Yes.

Senator VANDENBERG. Now what is that item?

Mr. BELL. There was \$1,635,000,000 in the Budget as it was submitted to you last January, representing the regular annual expenditures for national defense but there was set out in that Budget, as you recall, supplemental items which were labeled "emergency national defense expenditures," in the amount of \$300,000,000. This made total national defense expenditures in the January Budget of \$1,935,000,000. Since that time the President has submitted two messages, one on May 16 and one on May 31, under which we estimate if those appropriations are made there will be spent \$1,315,000,000, or a total of \$1,615,000,000 in 1941 as emergency expenditures for national defense or total national-defense expenditures of \$3,250,000,000.

Senator BYRD. Mr. Bell, I would like to ask this. As I understand the proposition we have two bookkeeping systems, two budgets and two deficits. Now what will be the deficit in the operating expenses of the Government; in other words, how much would be the deficit next year after eliminating the expenditures for national defense in that particular budget or particular branch of the Treasury, or whatever you might call it?

Mr. BELL. I don't admit that we are going to have two budgets, and I don't admit that we are going to have two bookkeeping systems, nor two deficits.

Senator BYRD. You certainly are going to have two deficits, are you not?

Mr. BELL. No, sir; one deficit, but of the deficit amounting to \$4,349,000,000—\$3,250,000,000 of it will represent expenditures on account of national defense, and \$1,099,000,000 of it will represent all other Government departments and agencies.

Senator BYRD. But you are recognizing national defense as a separate expenditure, separated from the other expenditures, because you are authorizing an increase in the debt only to be used for national defense. Now that being the case, what will be the deficit in the operating expenses of the Government, eliminating the national-defense expenditures?

Mr. BELL. \$1,099,000,000.

Senator BYRD. And what will be the deficit in the national defense?

Mr. BELL. \$3,250,000,000.

Senator BYRD. So we have got deficits in both branches; we are not collecting enough money to pay the operating expense?

Mr. BELL. There will not be two deficits, Senator Byrd, there will be one Budget and one deficit.

Senator BYRD. I know there is only one Treasury to pay this all out of, but you have got two systems of bookkeeping, one is for national defense, which you are segregating and separating from the ordinary expenses of the Government, and the other is for the other expenses, and all I want to know is, what is the aggregate of the two deficits? Is it true that we are not now collecting enough revenue to pay the ordinary expenses of Government, eliminating the national-defense expenditures?

Mr. BELL. That is right, by \$1,000,000,000.

Senator CONNALLY. Mr. Bell, may I ask you a question?

All this money that is owed by the Government, it is all Treasury obligations?

Mr. BELL. Yes, sir.

Senator CONNALLY. They are all for national purposes?

Mr. BELL. Yes, sir.

Senator CONNALLY. All the taxes you collect are Government taxes?

Mr. BELL. Yes.

Senator CONNALLY. What difference does it make which pocket you put it in, why shouldn't we go ahead and raise this debt limit and put on all the taxes the people will stand, and let the bookkeeping take care of itself? Isn't it a restriction on your freedom to try to create artificially a little pocket over here that you are going to put certain taxes in? I don't see any sense in it. It is all Government money and Government obligations, every dollar we get in is Government taxes; why shouldn't we proceed that way? I am for your program. I am going to vote for it, but I don't see any sense in having a "now you see it and now you don't" system. Let's put it on and treat it like we have always treated it.

Mr. BELL. It is a restriction on us, Senator Connally, as now proposed.

Senator CONNALLY. Isn't any Government or any business that self-imposes a restriction on its own freedom hurtful in the long run?

Senator KING. I think if we had more restrictions it might be wise in some instances.

Mr. BELL. We are used to operating under restrictions.

Senator CONNALLY. You don't like them, do you?

Mr. BELL. No, we don't like them, but—

Senator BYRD. This was a suggestion of the Treasury Department.

Mr. BELL. It was an arrangement worked out with the leaders of the House and the Senate.

Senator CLARK. This thing you suggest has one great outstanding merit of showing conclusively how far short we are of raising money by taxation to pay the ordinary expenses of the Government, exclusive of national defense.

Mr. BELL. It separates it to that extent.

Senator CLARK. A man can tell we are falling far short of paying the ordinary expenses of Government, leaving entirely aside anything chargeable to national defense?

Mr. BELL. It shows that; yes, sir.

Senator VANDENBERG. Well, the Secretary's statement says that we are raising the public debt to meet urgent needs of national preparedness. You would have had to raise the limit of the public debt anyway, without regard to national preparedness?

Mr. BELL. In due course, but not right away.

Senator VANDENBERG. Well, in due course would have been 12 months, wouldn't it?

Mr. BELL. Yes, sir; unless the next Congress raised taxes to meet the over-all expenditures of the Government.

Senator KING. Where do you draw the line between the ordinary expenses for the Army and the Navy, which are, of course, military expenses, and expenses for the maintenance of the peace of our country, and the expenses which you say are to be incurred by reason of national defense; where do the ordinary expenses for military and naval affairs end, and where do national-defense expenses begin, under your program here?

Mr. BELL. We take all the expenditures for military purposes made by the Army and Navy and classify them as national-defense expenditures.

Senator KING. Then each year we have been spending, for several years, more than \$1,000,000,000 for the Army and Navy, and now, instead of treating those as ordinary expenses, as we have been doing, you transfer them over to national defense?

Mr. BELL. They have always been labeled "national defense."

Senator KING. But they were the ordinary expenses, weren't they?

Mr. BELL. Yes, sir; they were, and they are still under the caption of "Ordinary expenses." We don't classify expenditures as "ordinary expenditures" and "extraordinary expenditures." They have always been classified as "national defense" and under this bill you are merely going to provide a means of financing national-defense expenditures separate and distinct from the expenditures of other departments and agencies.

Senator KING. But in a sense you are minimizing the expenses of the Government, or at least for national defense, or rather you are minimizing the ordinary expenses which we would have for the Army and Navy by transferring them over to the national defense and labeling them "National defense," and including them in the taxes which are to be raised, and in the extension of the bond limit?

Mr. BELL. They have always been labeled "National defense", and our financial statements, have set out very clearly what they are.

Senator KING. Well, when you have submitted your budget at the beginning of each year during the past 4 or 5 or 6 years, you have had so much for the Army and so much for the Navy. Those were ordinary expenses, weren't they?

Mr. BELL. Yes; they are regular expenditures, if that is what you want to call them.

Senator KING. Now they are irregular in the sense that you are transferring them to national defense?

Mr. BELL. I wouldn't call them irregular.

Senator BYRD. The Budget itself denominates them as ordinary expenses up to this time.

I would like to ask this question: At the end of the year, after you have spent \$3,250,000,000, or whatever it is, for national defense, you would have practically exhausted this additional \$4,000,000,000 of borrowing power, and you have dedicated \$1,000,000,000 worth of taxes to that for 4 years?

Mr. BELL. Five years, as I understand.

Senator BYRD. What has the Treasury in mind, what are the other taxes it will dedicate for an additional \$4,000,000,000 for national defense at the end of this year?

Mr. BELL. It is a matter for the Congress to determine when it appropriates the money next year.

Senator BYRD. In other words, we must look forward to another dedication and still have an unbalanced Budget over that period for the ordinary expenses of the Government?

Mr. BELL. That I can't answer at this time.

Senator BYRD. You are establishing the principle that all national defense expenditures should have dedicated taxes that are collected over a period of 5 years, but the money is spent in 1 year. Suppose you continue that for 4 or 5 years, it will be a terrific accumulation of dedicated taxes?

Mr. BELL. I am afraid it will if it goes on at the rate of \$3,000,000,000 a year.

Senator BYRD. What is the necessity of doing that? I can't see any reason for separating these. Why separate two systems of book-keeping, why confuse the people by separating that? I agree with Senator Connally that I don't desire to put any restrictions on the Government, but I want to see the utmost economy in the ordinary expenses, and let us meet these defense expenditures without restrictions.

Senator GEORGE. May I suggest to the Senators from Virginia and Texas that the people of this country might not be willing to increase the debt limit for ordinary expenses of the Government, but they might be willing to increase them very rapidly for national defense.

Senator BYRD. If they are not willing to do it, let them reduce the expenditures, or raise taxes, they have got to be met one way or the other. It is all the same debt limit, it is all the same obligation upon the United States Government.

Senator GEORGE. The Secretary makes this statement:

This bill provides for raising additional revenue of \$720,000,000 for the fiscal year 1941 and approximately \$1,000,000,000 yearly thereafter.

How much of that amount of \$720,000,000 is raised from other than excise taxes?

Secretary MORGENTHAU. Senator George, would it be agreeable if Mr. Sullivan would give an answer to that question?

Senator GEORGE. Surely.

Mr. SULLIVAN. Of that sum—\$185,000,000 would be raised from corporation and individual income taxes.

Senator GEORGE. \$185,000,000?

Mr. SULLIVAN. Yes; that would also include a minor item of \$3,000,000 on cigarette papers and tubes.

Senator GEORGE. So that all we get out of this bill is \$185,000,000 that you wouldn't get out of the mere increases made in the bill on the excise taxes?

Mr. SULLIVAN. No; that is not strictly true, Senator. The \$185,000,000 is the permanent increases in the rates. In addition to that, there is a supertax of 10 percent imposed on corporation and individual income taxes, capital stock and excess-profits taxes, estate taxes and gift taxes. That list is as follows:

An increase of \$62,000,000 for corporation income taxes, the supertax; \$74,000,000 for the supertax on individual income taxes; \$11,900,000 for the increase or supertax on capital stock and excess profits taxes; \$2,500,000, the supertax on the estate taxes; and \$1,500,000, the supertax on gift taxes.

Senator GEORGE. Well now, otherwise you would get two instalments, you estimate March 15 and June 15, under this bill on those taxes?

Mr. SULLIVAN. That is right, sir.

Senator GEORGE. So that if we passed a tax bill by March 15 of next year, providing these or additional taxes, we would really lose nothing except the special excise taxes?

Mr. SULLIVAN. Yes; that is correct.

Senator GEORGE. So that if we dealt with the excise taxes only at the present time, and remained in session, or went on immediately into the consideration of the tax bill, realistically, we would have lost nothing at all, would we?

Mr. SULLIVAN. Well, you would have lost the increase in estate taxes which becomes effective on the passage of the bill; you would have lost the increase on gift taxes, which becomes effective on the passage of the bill; you would also have lost the increase in the capital stock and excess profits taxes, for which returns will be made next month.

Senator GEORGE. They become effective from the passage of the bill, that increase will become effective?

Mr. SULLIVAN. I think the return is made July 30, sir.

Senator TOWNSEND. What would that amount to?

Mr. SULLIVAN. On the capital stock and excess-profits taxes, sir, the increase is estimated at \$11,900,000.

Senator KING. The greater part of the increase, then, that you expect to derive from this bill flows from excise taxes upon many of the commodities of life?

Mr. SULLIVAN. Well, estimating a full year's return, sir, under the pending bill we would expect additional revenue of \$1,003,000,000. Of this amount \$325,000,000 would come from the permanent increases in the corporate and individual income taxes, and in addition to that, the supertaxes on the corporations would be \$135,000,000; the supertax on the individual income taxes would be \$123,000,000; on the capital stock and excess-profits taxes, \$12,300,000; the estate taxes, \$29,000,000; and the gift taxes, \$3,000,000.

Senator KING. Do any of these taxes imposed by this bill expire at the end of 5 years, or are they continuous?

Mr. SULLIVAN. The super tax that is imposed does expire in 5 years.

Senator KING. But all these excise taxes continue?

Mr. SULLIVAN. No, the excise taxes were to have ended in a year, and because a supertax has been imposed upon them for 5 years, it was necessary to continue their operation for 4 years beyond the present expiration date, next June.

Senator KING. Do you earmark the taxes that are derived from excises and from these various sources of income, so that in the event that we should revise our entire tax bill a year from now, or 2 years from now, we would be inhibited from invading the fields that are covered by this bill, or would we not be compelled in a general tax bill to tax those sources of income which today are practically, under this bill, theoretically, at least, earmarked?

Mr. SULLIVAN. I have not yet foreseen any restrictions that would be placed upon you, Senator. You must realize that we do not earmark those taxes that are imposed by Title I, and for this reason: In that Title the exemptions, the personal exemptions are lowered and the rates, the surtax rates, are increased. To take any one return and to find out how much additional revenue we derive from that particular return because the personal exemptions have been reduced and the surtax rate has been increased, would involve at least as much work as auditing the return in itself.

Senator GEORGE. Don't you think it would be a disadvantage in the sale of a bond, and would create some felling among the people that there was a discrimination, if some bonds have earmarked taxes for their payment, and others do not? If you do earmark various sources of income, and say that the income derived from those sources shall be limited to the payment of bonds which are issued now under this bill, don't you think that that would be a disadvantage?

Mr. SULLIVAN. I would prefer to defer on that question to Mr. Bell.

Senator GEORGE. Well, it seems to me, if I may say so—and I won't state it in an interrogative form—that if we impose taxes and earmark taxes, say, so much on tobacco, so much on liquor, that is earmarked for 5 years to pay this indebtedness, then we have a general tax bill next year, and we want to increase taxes materially, two or three or four billions, as we may have to, it would seem to me that if you earmark certain sources of revenue to meet the bonds that we now issue, you would be met with a moral obligation to relieve those commodities of taxes in the future.

Mr. SULLIVAN. That might be so, sir; there would be less revenue out of which to discharge the obligations, the other obligations.

Senator BYRD. You think there is a moral obligation to continue these particular taxes for 5 years to amortize these particular bonds?

Mr. SULLIVAN. If these bonds were issued with that understanding, I should think these might be moral obligations to raise sufficient taxes to retire these securities, but not necessarily by these specific taxes.

Senator BYRD. Will they be issued, that is what the public has been told, will they be issued with that legal understanding?

Mr. SULLIVAN. I understand that from the statements made in the hearings, that the public would be justified in believing that they were to be issued that way, and I believe they would be issued with that understanding.

Senator BYRD. That is, these taxes would be frozen, if not legally at least morally, so that they could not be disturbed by Congress?

Mr. SULLIVAN. The total might be fixed.

Senator CONNALLY. They could be disturbed by an increase?

Mr. SULLIVAN. Yes.

Senator BYRD. Suppose you increase them to the point of diminishing returns, then the revenue wouldn't be forthcoming to pay the bonds?

Mr. SULLIVAN. That is a problem we always face.

Senator VANDENBERG. When have we earmarked special sources of revenue for special bond payments before?

Mr. BELL. Senator Vandenberg, we have earmarked all of the principal repayments coming in from foreign governments on account of cash advances made to them during the World War, and we applied the amounts so received to the retirement of our public debt, as a part of the 9-billion-dollar reduction that was made between 1920 and 1929.

Senator VANDENBERG. You are not talking about an earmarking which goes against the public debt as a whole, are you?

Mr. BELL. That is right.

Senator VANDENBERG. I am asking you when, if ever, we have taken a portion of the public debt and given it a special revenue; that is a sort of a South American system, as I view it. [Laughter.]

Mr. BELL. I don't recall that we have ever earmarked taxes for any special part of the public debt.

Senator KING. Didn't we earmark some of the taxes levied in 1917 or 1918 on corporation income for public debt, to meet public debt?

Mr. BELL. There was some earmarking of revenue in 1917, Senator King.

Senator KING. That is my recollection.

Mr. BELL. But I am not sure—

Senator HERRING. That is a common practice among the States and always has been—that isn't a South American practice, that is a practice of the American States.

Senator VANDENBERG. It is also a South American practice.

Senator HERRING. I hope they have learned it from us.

Mr. BELL. I am informed that the act earmarking tax receipts passed in the spring of 1917, was repealed in the fall of 1917, and was never in operation.

Senator VANDENBERG. I didn't hear an answer to the question which I thought Senator King submitted, as to whether or not the allocation of special revenues to special bonds would affect adversely the value of other bonds in the public eye?

Mr. BELL. I don't think it will, Senator Vandenberg; in my opinion, these obligations will be issued on the full faith and credit of the United States Government, and will be sold on that basis. In that respect they will be no different from all other public debt issues. I feel the holders will look to the United States Government, and to it only, for their payment.

Senator LA FOLLETTE. In other words, if I understand your answer correctly, Mr. Bell, you don't think that the special arrangements which are set up here for this series of 5-year defense bonds, will have anything to do with making them more attractive to American purchasers?

Mr. BELL. I think they may be more attractive only because they are short-term obligations.

Senator LA FOLLETTE. No; I meant because you are setting aside, you are dedicating 5 years of taxes to their retirement, and do you think that will have any effect on their sale?

Mr. BELL. No; I don't think so; I think they will be sold on the faith and credit of our Government and that is what the investor is interested in.

Senator LA FOLLETTE. The reason I ask that is that you may be confronted with a situation here in the next session of Congress where you will have to issue more bonds of this same type, and assume now, for the sake of argument, that it might be difficult to find additional taxes to set up the same type of scheme that you have got in this bill, for the retirement of this particular set of bonds; do you think an alteration in that policy would adversely affect the sale of bonds?

Secretary MORGENTHAU. There have been a number of questions here, and if I may I shall try to answer them, stating, if I may, the position of the administration on this program, and how we arrived at it.

The CHAIRMAN. Go ahead, Mr. Secretary.

Secretary MORGENTHAU. After all, I believe that every member of this committee has voted, as far as I know, for this national defense program, and the Secretary of the Treasury is faced with the problem of financing this program. It was perfectly obvious that we had to increase the debt limit, and we ought to increase the taxes and make all strata of American society contribute toward meeting these expenditures, and make them conscious of the fact that we are entering into this very tremendous program of national defense.

Now there are a number of ways of doing it, and I have learned, after 7 years here, that you arrive at decisions through compromise.

Now the easiest way, I take it, would have been to increase the debt limit from \$45,000,000,000 to \$50,000,000,000, but I don't think I am disclosing any secret when I say that I was led to believe that the increasing of the debt limit from \$45,000,000,000 to \$50,000,000,000 would have been a rather difficult procedure.

At the same time, if I had asked 3 weeks ago for an increase of \$1,000,000,000 in taxes, I think I would have been laughed out of Washington.

Senator KING. I would have commended you.

Secretary MORGENTHAU. Well, you would have been among the minority, Senator King.

The fact remains that we have got this serious situation. Congress, if I may say so, has acted magnificently in this emergency and has certainly gone as far as anybody could expect, or ask them to, as far as appropriating the money needed for the Army and Navy. I believe, if you don't mind my saying, that they have done a magnificent job.

Now the job falls on me to keep the Government's credit sound, and in consultation with the leaders of the Senate and the House, correctly of the party to which I belong, we arrived at this program which we felt would be acceptable to Congress and very acceptable to the people of the United States.

Now I don't say it is the best program in the world, but I do say it accomplishes the thing which is of the utmost importance at this time, and that is to finance this national defense program.

Senator VANDENBERG. Does it keep the Government solvent, Mr. Secretary?

Secretary MORGENTHAU. I believe it will, Senator. As I say, I don't believe it is the best program in the world, but it is the best that we in the Treasury were able to arrange, with advice and counsel of the gentlemen from the Senate and from the House.

Now, that is an honest statement, and I trust a very frank statement. There may be better plans but this is the best one under these very difficult times that we have been able to work out.

Senator BYRD. Mr. Secretary, is it your opinion that we are under a moral obligation not to reduce any of these taxes that are dedicated for national defense for 5 years in advance?

Secretary MORGENTHAU. Senator Byrd, I believe that myself or my successor is obligated to raise \$800,000,000 to retire these bonds each year over the next 5 years.

Senator BYRD. I mean, do you have to raise it in the particular way devised in this bill? Of course, you have got to raise money sooner or later to pay the deficit in ordinary expenses.

Secretary MORGENTHAU. I would say that myself or my successor, unless it is written in the bill otherwise, is obligated to raise \$800,000,000 a year.

Senator BYRD. You know, at the end of this year, we are going to spend still more money for national defense; this is just the beginning, we are told that this national defense is going to cost \$20,000,000,000 before it is completed.

Secretary MORGENTHAU. If it does we will have to think up methods to finance such a program and we will have to go further than this bill contemplates. If you are correct that we are going to spend \$20,000,000,000, and I don't know, because 6 weeks ago no one

thought of going this far—but what I am saying is, if we have to raise \$20,000,000,000, then we are going to have to go to tax methods a great deal more severe than are incorporated here.

Senator BYRD. I am not in any way trying to hamper you or restrict you, but I want to know whether Congress is at liberty, in your judgment, under moral obligations that some may think it has, to reduce or change this particular schedule of taxation which is dedicated for 5 years for the payment of this national-defense item which will be spent in 1 year?

Secretary MORGENTHAU. What I feel is this, that if this bill passes in its present form, the Secretary of the Treasury will sell \$4,000,000,000 worth of these notes to the public, and that the public has the right to expect that \$800,000,000 a year will be raised and set aside in a special fund to retire them over the 5-year period.

Senator BYRD. You don't think it will be confined to these particular levies?

Secretary MORGENTHAU. I wouldn't so interpret that.

Senator BYRD. When you have them increased a year from now, when you have to issue \$4,000,000,000 more of national defense bonds, then you would have another set of dedicated taxes, is that true? Is that your plan? We may as well view the situation as a whole. It is certainly going to cost \$10,000,000,000 for national defense, because the American people are going to demand a greater national defense, regardless of the outcome of the European war, than we have had in the past. So why not look forward to the future as well as to the present? There is only a certain amount of taxes that we can raise by imposing a horizontal increase of 10 percent, which is not the scientific way to do it, and we all realize that.

Secretary MORGENTHAU. May I answer you?

Senator BYRD. Yes.

Secretary MORGENTHAU. If the Congress votes another large amount of money for national defense next year, certainly a program will have to be worked out to finance it, and whatever tax revenues are decided upon they will have to be superimposed on top of revenues provided by these taxes.

Senator BYRD. Well, that is true, of course, in certain instances. There may be some taxes in this bill that reduce the returns.

Secretary MORGENTHAU. That is perfectly possible.

Senator BYRD. Now I want to know from you, and I am not trying to embarrass you at all, whether you feel that by putting through this bill, the hands of Congress would be tied in revising the tax structure during the next session?

Secretary MORGENTHAU. My answer to you is "No"; but I believe you are morally obligated to provide \$800,000,000 taxes to take care of these bonds.

Senator BYRD. This will not interfere, in your judgment, with the revision of the taxes on a scientific basis?

Secretary MORGENTHAU. No.

Senator GERRY. Then, Mr. Secretary, what advantage would you get by setting off these particular taxes for the sale of the bonds if you in effect can pay them out of any general funds? What is the special advantage of setting aside this sum if there is no moral obligation to pay?

Secretary MORGENTHAU. If I said that, and I don't think I did, may I explain it? What I am trying to say is this: In the first place it has never been, in my mind or the minds of any of you gentlemen that I have talked to, that by earmarking these taxes we are going to give these bonds a certain advantage over some other bonds. That was never in my mind. As a matter of fact, I think they might be less advantageous because, if the Congress leaves it discretionary with me, as it is now, I propose to issue these notes subject to all Federal taxes including the normal taxes. So that they will be less advantageous than existing notes outstanding which are fully tax exempt.

Senator KING. I think we ought to give you that authority, I think that is wise. I think that if you attempt to earmark them, and let the public believe that they have got a certain excise tax to guarantee them, it will interfere with the imposition of taxes.

Secretary MORGENTHAU. If it is left discretionary with me, these \$4,000,000,000 of notes will be subject to all taxes.

Senator BYRD. There is nothing in the body of the bond that indicates that they are different in security from other bonds issued by the Government?

Secretary MORGENTHAU. No; but to repeat, I believe that if this bill passes, the Congress of the United States is obligated to set aside \$800,000,000 of taxes a year, into a special fund until these \$4,000,000,000 worth of notes are retired.

Senator GERRY. Then what special advantage is there in that, it is a bond like any other Government bond, and all you are doing is setting aside a certain amount of money which you have got to pay anyway?

Secretary MORGENTHAU. Senator, there is no advantage; all Government obligations are issued on the full faith and credit of the Government; in fact, these notes might be less advantageous because they are going to be subject to all Federal taxes. The American people will know that here are \$4,000,000,000 worth of obligations which will pay for the national-defense program, and that they are being taxed \$800,000,000 a year for 5 years, to pay them off.

Senator BYRD. I think you are right, Mr. Secretary, if this was the total expenditure for national defense, but this is just the beginning, and that is the weakness of the whole proposition.

Secretary MORGENTHAU. It may be also a strength, because if this works, and next year Congress decides to vote additional amounts for national defense, it can do it the same way or it can do it the way we have done heretofore.

Senator BYRD. We all recognize, I think, and I think you do, Mr. Secretary, the need of scientific revision of our complete tax system. That being the case, wouldn't it be better to put this supertax on for 1 year, and let the Congress work out some scientific plan? It certainly isn't scientific to impose an arbitrary increase in each item of taxation.

Secretary MORGENTHAU. Senator Byrd, I am in complete sympathy with you, that we need a scientific revision of our tax system. I have said that over and over again, and we have had the material in the Treasury for years, but we have not had the opportunity to accomplish a cold-blooded, disinterested, scientific examination of the tax system, not only of the Federal Government but of the State and municipal governments.

Senator BYRD. Isn't this the time now to do it, in view of the fact that the people of America have to make this sacrifice?

Secretary MORGENTHAU. If you gentlemen want to stay here—

Senator BYRD. I am willing to stay here. I think it is a grave mistake to make this an increase for 5 years, facing the necessity, the imperative necessity, of a complete revision of the tax system, and I was wondering if the Treasury would agree to impose this supertax for a period of 1 year instead of 5 years? If we could write that provision in, write it into the bill, making it for 1 year with the understanding that the complete tax system would be revised.

As a matter of fact, I think \$1,000,000,000 is chicken feed, we ought to raise two or three billion dollars additional taxes, and we have to raise it if we are going to have a solvent Government.

Senator KING. Mr. Secretary, I am in entire sympathy with the statement which you have made recently, to wit, that the bonds which you issue now will be paid out of the general fund. I am not quite clear, though, that that view is in harmony—and that is what I think it ought to be—with the declaration found in section 301 of title III of the act of the bill under consideration, where it reads:

The Secretary of the Treasury shall, as soon as practicable after the end of each quarter, determine the additional amount of taxes collected attributable to the increases in taxes made, and to the floor stocks taxes imposed, by the amendments to the Internal Revenue Code in title II of this act (not including the amount of taxes attributable solely to section 209 and not including any amount collected under section 1700 (a) (1) of the Internal Revenue Code attributable to a basic admission charge of more than 40 cents), and the amounts so determined shall be set aside as a special fund which shall be available only for the retirement of any of the obligations issued pursuant to the authority contained in section 21 (b) of the Second Liberty Bond Act, as amended.

It seems to me that you are, by this language—and I don't approve of it, I think it ought to be eliminated—enmarking these funds and setting them aside as a special fund available only for the meeting of the obligations of the bonds which are issued under this act, and I think that that will create the impression that there is a special fund to pay these bonds, where there is no special fund but only the general fund to cover the general bonds which may be issued, and that will lead to a discrimination between bonds and stocks, and people who buy the bonds will say, "I have a better bond, a special fund bond, and you have got only a general fund bond."

Mr. SULLIVAN. I believe that is a fair statement, sir, though the bonds will be equally good.

Senator CONNALLY. Suppose the Senate and the Congress should decide to go right on here with a general tax bill at this time; is the Treasury ready with its data and studies for us to do that?

Secretary MORGENTHAU. Yes, sir.

Senator CONNALLY. You are ready right now?

Secretary MORGENTHAU. I don't say right at this minute.

Senator CONNALLY. I don't mean by 1 o'clock, but I mean if we should continue this session of Congress—I think it is an awfully good time when you have got an operation to perform to perform it while the patient is willing, and the country or the patient is willing now, and as far as I am concerned, I am willing to continue right on if the Treasury has got the studies and everything for this revision of tax bill; pass this if you want to, and come along with the tax bill.

Secretary MORGENTHAU. If we are not ready, somebody is going to get fired, and it may be me.

Senator CONNALLY. We are not interested in that, but we are interested in the fact of whether you are able, ready, and willing?

Secretary MORGENTHAU. Yes.

Senator TOWNSEND. Mr. Secretary, you still have \$2,000,000,000 in your stabilization fund, do you not?

Secretary MORGENTHAU. Yes, sir.

Senator TOWNSEND. Did you, in working out this plan, take into consideration, or did you consider the advisability of using your stabilization fund?

Secretary MORGENTHAU. We considered it and I felt—I made this statement before and I am glad to make it here again—that the stabilization fund is there, as I said before in the House, as a nest egg belonging to the American public against that day when possibly a grave national emergency will come, and I strongly believe and strongly urge that the stabilization fund should remain intact until such a time as we may need it. I think it would be a great mistake to touch it, now.

Senator JOHNSON. Well, you look forward to a greater emergency, then, than we have today?

Secretary MORGENTHAU. I live and learn, and each day the situation changes so radically and one just doesn't know when a situation may arise when we may be very glad that we have got the stabilization fund to use. Both the President's and my policy is not to use it, we couldn't spend it without coming to Congress to get the authority anyway. I have said before, and I repeat now, that I would not spend it for any purposes without coming to you gentlemen, explaining what I wanted it for and getting your approval either formally or informally.

Senator TOWNSEND. You have only, up to date, spent \$200,000,000?

Secretary MORGENTHAU. We haven't spent a dollar that we haven't gotten back and more too.

Senator TOWNSEND. You haven't spent any?

Secretary MORGENTHAU. I have got \$2,000,000,000, and we must have \$20,000,000 over that. I mean we still have more than the original amount set aside.

Mr. BELL. \$2,019,000,000.

Senator VANDENBERG. I want to get one figure straight in my mind, dealing with the general question of solvency and your general responsibility for the Treasury as a whole. My understanding is that this bill will raise \$729,000,000 estimated for the next fiscal year?

Secretary MORGENTHAU. That is right.

Senator VANDENBERG. And that the regular deficit for the next fiscal year, without respect to this national preparedness, is \$1,716,000,000?

Mr. BELL. No; \$1,100,000,000.

Senator VANDENBERG. That is after you have taken the Army and Navy out, isn't it?

Mr. BELL. I thought you said without respect to national defense.

Senator VANDENBERG. No; I am talking about the original Budget, the estimate, according to the Secretary, was \$1,716,000,000.

Mr. BELL. The original deficit was \$2,876,000,000, and the President, in setting up a means of financing it, asked for \$460,000,000 of additional taxes and \$700,000,000 return of capital funds from corporations and credit agencies, bringing it down to a net deficit to be financed through public debt issues of about \$1,700,000,000.

Senator VANDENBERG. So this new tax bill only actually raises for the next fiscal year considerably less than half of the regular ordinary deficit of the Government?

Secretary MORGENTHAU. Your mathematics are correct.

Senator BYRD. About one-fourth.

Senator VANDENBERG. I mean after they got all through.

Senator BYRD. It is ridiculous to take out the peacetime expenditures of the Army and Navy; that is just camouflage.

Senator KING. I wouldn't use that term. I would say, however that it is not quite proper to lift those peacetime liabilities of the Army and Navy out of the general expenses and put them into the category of the national defense. They are a part of the ordinary expenditures of the Government and ought to be so recognized, and the national-defense program ought not to call those peacetime appropriations for military purposes as a part of the national-defense program now. However, it is a question of bookkeeping.

Senator BROWN. I have been particularly interested in a question Senator CONNALLY asked you about revision. You anticipated, when you submitted these recommendations to the committees of Congress, that there would be a further tax revision in January and February of the coming year, at the next session of Congress, did you not?

Secretary MORGENTHAU. I have every reason to believe so.

Senator BROWN. That there should be?

Secretary MORGENTHAU. Yes.

Senator BROWN. And any revision that we then make would, of course, be effective as to the income taxes that are payable March 15 and each quarter thereafter in 1941?

Secretary MORGENTHAU. Yes.

Senator BROWN. I take it, then, that the attitude of the administration is, as expressed by you, that you prefer the passage of this tax bill now, with plain notice to the country that in January and February we expect a further revision of the tax laws?

Secretary MORGENTHAU. Yes; and if somebody could give me that resolution that was passed in the House I would read it.

The CHAIRMAN. Here is the report of the committee, as I understand it.

STUDIES OF EXCESS-PROFITS TAXES AND SPECIAL AMORTIZATION

During the executive sessions, there have been discussed proposals to provide special amortization for national defense industries and to provide for the imposition of excess-profits taxes. These two measures—each in itself requiring a complicated and exhaustive legislative project—must be considered together. It is the desire of this committee, which is favorably reporting a bill which will enable a larger proportion of our citizens to participate in the responsibility of providing an adequate national defense than has ever been the case before, that there shall not be an opportunity for the creation of new war millionaires or the further substantial enrichment of already wealthy persons because of the rearmament program. Accordingly we have instructed our technical assistants and the appropriate Treasury officials to accelerate their work in these two fields so that bills will be prepared for submission not later than the opening of the next session of Congress, which if passed by the Congress may become retroactive and apply to income earned during the calendar year of 1940, or may become effective upon any other date which Congress, in the light of information it then possesses, may deem advisable.

Senator BROWN. Is that the resolution you had in mind?

Secretary MORGENTHAU. That is the resolution I had in mind. That was the resolution that I was authorized by the President to say

was not only acceptable, but pleasing to him, and he made the same statement, I understand, at his own press conference yesterday.

Senator BROWN. Well, I am in sympathy with the resolution and I think it is a good thing that it was said, but I don't think it should be interpreted to mean that either the Treasury Department or the House and Senate committees should confine themselves to those particular taxes, because there are many other avenues of revenue open that could be considered. For instance, as the members of the committee well know, I have long been interested in the question of taxing State and municipal bonds and permitting the taxation of Federal and State bonds to the fullest extent, and cutting out all tax exempt features. I think that should be considered.

Senator CLARK. In that connection, if the Senator will permit me, and it seems to me to be very applicable to this pronouncement, to say that on the tax bill last year the Senator knows that I had prepared, and as a matter of fact was on the point of offering an amendment to the tax bill on the very subject which the Senator from Michigan is now mentioning, and the representatives of the Ways and Means Committee came over and said, "Please don't do that this year, it will delay the consideration of this bill; it will delay adjournment; and the Ways and Means Committee is now preparing studies and will have a bill in before the end of this session."

That session ended and this session is about to end, and the bill has never come over, and it seems to me we cannot afford to postpone legislation on that promise of the Ways and Means Committee.

Senator BROWN. I joined in the effort to prevent the bond tax from being imposed in the last revenue bill, and I may say I will again join in that effort if I am reasonably well assured that that will be considered in a tax bill which will be submitted in January or February of next year, but I don't think we should confine ourselves to that tax but should consider other revenues, also.

There are many other revenues. I have discussed a manufacturer's sales tax, and I understand that has been considered by the informal committee that presented this bill, and I think it should be included in any study. But my main point is this, I was much interested, as I said earlier, in the answer to the question asked by Senator Connally, and I thought possibly, in view of what has been said, that your answer might be revised to some extent, and I submit that to you now.

Do you not think, Mr. Secretary, that the Treasury would be in a better position after having had the experience of the operation of this tax bill, particularly with respect to the excise part of it, to advise the Congress after 3 or 4 or 6 months, as to the new taxes which should be considered in January and February?

Secretary MORGENTHAU. I don't think there is any question about that, I don't think it is in conflict with what Senator Connally asked me.

Senator BROWN. I take it, then, that the recommendation of the Treasury Department is that we pass this bill with an assurance to the country that the entire subject will be fully gone into by your experts between now and January, and that you will submit additional recommendations for taxes at that time?

Secretary MORGENTHAU. I would be very glad—

Senator BYRD. If that is the case, then why do you want to make this a 5-year tax bill?

Secretary MORGENTHAU. In order to finance this \$4,000,000,000 of national-defense program.

Senator BYRD. Everybody knows it has got to be financed, there is no question about that. You could put an amendment on the bill saying that we recognize the obligation, but why continue these specific taxes for five years if you are looking forward to a general revision in January?

Secretary MORGENTHAU. As I tried to explain earlier, 3 weeks ago if I had come here before you gentlemen and asked you to raise the debt limit \$5,000,000,000. I would not have had the remotest chance of your approval. If I had asked for \$1,000,000,000 increase in taxes, I doubt whether I would have gotten that.

Senator BYRD. Frankly, Mr. Secretary, I have been opposing an increase in debt so we can curb this extravagance which is rampant in every branch of our executive departments today.

Secretary MORGENTHAU. That doesn't take care of the situation, Senator Byrd, at this moment at all. If I understand your position, all you have been recommending is that we cut \$500,000,000.

Senator BYRD. Do you favor that; do you favor reducing the non-defense expenditures \$500,000,000? I have read your statement which I understand is more or less in opposition to that reduction.

Secretary MORGENTHAU. Oh, no; but I am not in favor of making a flat percentage reduction in all expenditures.

Senator BYRD. Would you favor reducing the nondefense expenditures \$1,000,000,000?

Secretary MORGENTHAU. Would I favor it?

Senator BYRD. Reducing the nondefense expenditures \$1,000,000,000?

Secretary MORGENTHAU. Your program, as I understand it, up to now has been to cut expenses by \$500,000,000?

Senator BYRD. Nondefense expenses.

Secretary MORGENTHAU. If we did that, and did nothing about raising new taxes, or did nothing about raising the debt limit, the Treasury would not be in a sound fiscal position.

Senator BYRD. I at the same time advocated an increase of taxation. Do me the honor of reading my remarks in the Senate. That was a two-barreled proposition. One was to reduce the nondefense expenditures and the other was to increase taxes. As you seem to intimate that this is a very small amount to reduce the nondefense appropriations, do you favor reducing them above \$500,000,000?

Secretary MORGENTHAU. I am in favor of reducing Government expenditures and have been ever since I have been Secretary of the Treasury, wherever feasible or proper.

Senator BROWN. Might I say that Congress is responsible for those expenditures and not the Treasury Department. We have made these appropriations and the President is way ahead of us through his veto of the rivers and harbors bill. He took a big slice out of us through his veto of that, and I am glad he did.

Senator BYRD. The Secretary opposed certain reductions, in the written statement that he read this morning. The Secretary of the Treasury must have some responsibility or he would not have gone out of his way to oppose reductions to the bill proposed.

Secretary MORGENTHAU. I am here today recommending a plan which I believe is feasible, which I believe will work, and which will

take care of the present situation as it exists today, and it seems to me, as I say after consulting with Senators and Congressmen, that it is the best that we can get out of the present situation. No tax bill, no appropriation bill that I have ever seen, is perfect, but this is the best that I felt we could get, and I think it is a good bill.

Senator GERRY. Did I understand from the resolution that Senator Harrison read, that the recommendation was to pass this bill, and then in January have retroactive taxes passed?

The CHAIRMAN. Proceed, Mr. Secretary.

Secretary MORGENTHAU. I want to get the exact language. It says here,

* * * which if passed by the Congress may become retroactive and apply to income earned during the calendar year of 1940.

Senator GERRY. What I wanted to know was whether you thought it was wise to have those taxes retroactive, or whether it wouldn't be better to consider them now so that the people would know what the taxes were going to be. That is one thing I had in mind on the tax problem, treating it realistically now.

Secretary MORGENTHAU. If the Congress of the United States wants to stay here, I have got to be here anyway this summer, and I would be delighted to work with you gentlemen if you wish me to. I am at your disposal and so is everybody else in the Treasury Department.

Senator GERRY. I don't think that is answering my question.

Secretary MORGENTHAU. That is the best answer I can give you.

Senator CONNALLY. Senator Brown asked you something about your answer to the question which I propounded at an earlier date. Now if we pass this bill now, and then revise the whole tax structure in January, these taxes in this bill, of course, will be superseded; I mean by that that they will all be incorporated, either incorporated or eliminated, in the new bill, isn't that true? We won't have two bills, we will revamp the whole program, and we will absorb what we are doing now into the general tax bill, won't we?

Secretary MORGENTHAU. You could do it that way.

Senator CONNALLY. That would be the sensible way to do it, if you are going to revamp the whole thing you would naturally take this bill into consideration and integrate it with whatever bill we are going to pass in January?

Secretary MORGENTHAU. Granted.

Senator CONNALLY. My question to you a while ago was—if Congress should so decide, is the Treasury prepared with all these studies and data that you have been making, to go right on now, pass this bill, and right on the heels of it, instead of January, now, revamp and renovate and mothproof all the old tax laws and get an entirely new tax system? Are you ready to proceed if we are?

Secretary MORGENTHAU. We are ready tomorrow.

Senator CONNALLY. Of course Senator Brown asked you if you wouldn't, by waiting until January, have some more experience. All of the experience you would get would be out of these excise taxes because the income taxes would not be payable until March 15 anyway; isn't that true?

Secretary MORGENTHAU. Yes.

Senator CONNALLY. Haven't you got a world of experience in excise taxes already in the Treasury?

Secretary MORGENTHAU. Yes.

Senator CONNALLY. Haven't you got a lot of war taxes that we had during the war and know what happened to them?

Secretary MORGENTHAU. Yes; and we have made a study, Senator Connally, of these war taxes in every country in the world, and we have sent missions to England and other places several years ago.

Senator CONNALLY. You have got all of that?

Secretary MORGENTHAU. It is all in the Treasury.

Senator CONNALLY. So far as I am concerned it seems to me that if the Congress wants to we are just about as well-equipped now to pass this bill, and go right ahead with a general tax bill, as we would be in January.

Senator BROWN. My point is, will we gain anything by it?

Senator CONNALLY. We will gain in public attitude. They are all ready to pay taxes now, and they will think that this is all you are going to put on, and then next January when you pass a new bill they will snort and raise the devil.

Senator GUFFEY. How soon can you have an intelligent balance sheet of the United States Government prepared, a list of assets and liabilities? We know the liabilities. Has anybody ever prepared a list of the assets of the United States Government?

Secretary MORGENTHAU. We have got one right now that I will be glad to give to you.

Senator GUFFEY. I will be glad to see it.

Senator BROWN. I would like to ask concerning this last section of the bill, referring to section 21 of the Second Liberty Bond Act. Do you propose to make these maturities 5 years, or is there any restriction on you as to maturity?

Secretary MORGENTHAU. Can Mr. Bell answer that?

Senator BROWN. Certainly.

Mr. BELL. Those sections referred to in section 202 of this bill refer back to the Second Liberty Bond Act, which authorize the Secretary of the Treasury to issue treasury bills and Treasury certificates of indebtedness, having a maturity of not to exceed 1 year; and to issue Treasury notes, having a maturity of 1 to 5 years. So that anything we issue under this \$4,000,000,000 limitation will fall in that category.

Senator BROWN. Do you think that is an undue restriction upon you, Mr. Bell? It seems to me that it is; that you might do much better if you were not restricted in that fashion?

Mr. BELL. If you are going to confine it to this particular type of obligation it is not a restriction in that sense, it is a restriction to confine the \$4,000,000,000 to that character of obligations. If it were under the \$45,000,000,000, and the \$45,000,000,000 were increased by \$5,000,000,000, without this restriction, then we could issue bonds as well as the short-term securities—

Senator BROWN (interposing). Then I take it that you have three classifications: notes, bills, and bonds, and that under section 302 you are just going to issue the first two, you are not going to issue any bonds?

Mr. BELL. No, sir.

Senator BROWN. That will be a long-term obligation?

Mr. BELL. That is right.

Senator BROWN. Do you think your interest rate will be as favorable?

Mr. BELL. The interest rates on short term securities of this character would be more favorable than a rate on a long term bond. The only disadvantage is, that it piles up your debt within a relatively short period.

Senator BROWN. Well, I personally favor granting full discretion to the Treasury Department in that respect, rather than a restriction.

Mr. BELL. This is a restriction, but we can operate under it all right if this is what the Congress wishes.

Senator VANDENBERG. I would like to ask what excise taxes are not increased?

Mr. SULLIVAN. I would be happy to answer that. There are two classes of excise taxes that are not increased. The first group are the regulatory taxes and the second group are the import-excise taxes.

In the first group of regulatory taxes the tax was not increased on: Adulterated butter and processed or renovated butter; bituminous coal; cotton futures; filled cheese; firearms and machine guns under the National Firearms Act and under the Federal Firearms Act; marihuana; opium; oleomargarine; white phosphorous matches; tax on circulation of banks other than national banks; licenses for certain dealers; and sugar.

That refers to dealers in marihuana, opium, oleomargarine, filled cheese, and what not.

The list of items on which the import-excise taxes are not increased is: Fish, animal and vegetable oils; coal; copper; lumber; petroleum and products; coconut oil, palm oil and palm-kernel oil.

Those are the only excises which have not been increased under the pending bill.

Senator VANDENBERG. And on what theory were those omitted?

Mr. SULLIVAN. Those were omitted on the theory that neither of these was originally passed as a revenue raising measure, that they were intended to regulate or discourage certain processes and certain materials.

Senator VANDENBERG. I think that is a fair discrimination.

Mr. SULLIVAN. I am reminded that I have omitted one other excise tax which didn't happen to be on the list. There was a tax on telephones and telegrams which has been omitted, and the reason that that was omitted is that an additional 10 percent would bring the toll charge into pennies and there is no provision on a pay booth for paying that extra tax, and for that reason it was omitted.

Chewing tobacco was eliminated from the excise taxes in the deliberations in the House.

Secretary MORGENTHAU. Senator, could I amplify my reply to Senator Brown, knowing his particular interest in this subject?

The CHAIRMAN. Yes.

Secretary MORGENTHAU. I want to indicate clearly the Treasury's position with respect to repeal of tax exemption affecting interest on all public securities. I am opposed to any action modifying contractual obligations exempting from taxation interest on outstanding Federal securities.

Senator BROWN. No retroactive taxes?

Secretary MORGENTHAU. No. The Treasury is in favor of a repeal of those statutes granting exemption of interests on all future public security issues, Federal, State, municipal, and local, including the

obligations to be issued under this act. However, if the tax exemption affecting future State, municipal, and local issues is not repealed at this time, the Treasury wishes to reserve the discretion it now enjoys under the Second Liberty Bond Act, and it will make the interest on the notes to be issued under this act subject to Federal taxes.

Senator BROWN. I am very glad to have that statement because I am in complete agreement with it.

Senator KING. That is to say, if I understand you, Mr. Secretary, that you have the discretion now to impose taxes, if I may use that expression, upon State issues?

Secretary MORGENTHAU. No.

Senator CLARK. I may say, Mr. Secretary, that there was an amendment precisely along that line that I was prepared to offer last year, and on the promise of the House Ways and Means Committee that they would present a bill of that character at the end of the year I didn't present it.

Secretary MORGENTHAU. On these new securities, if I have the discretion I want to make them fully taxable.

Senator CONNALLY. So you can't sell them so easily?

Senator BROWN. Because it is the just way to do it.

Secretary MORGENTHAU. To make this thing fair all around I don't think we should increase the taxes \$1,000,000,000 and then give the people who lend the money a special privilege through tax exemption.

Senator BROWN. But this bill makes it discretionary with you on the issue of these short-term securities?

Secretary MORGENTHAU. That is right.

Senator VANDENBERG. What would be the difference in the cost of money to you?

Secretary MORGENTHAU. I can't tell, it might cost a little more.

Senator VANDENBERG. Have you made any estimates, roughly?

Secretary MORGENTHAU. Oh, it would be a trifle.

Senator BROWN. Well, I may say that a general summary of the testimony before our committee last February was that it would probably be around a quarter of 1 percent, higher cost to the Federal Government.

The CHAIRMAN. Are there any other questions? [No response.]

Anything further, Mr. Secretary?

Secretary MORGENTHAU. Nothing.

The CHAIRMAN. Mr. Sullivan?

Mr. SULLIVAN. Do you wish a statement from me? I can make it as short or as long as you want.

Senator CONNALLY. Is it the purpose of this committee to meet this afternoon?

The CHAIRMAN. I had hoped we could meet at 2 o'clock.

(Off the record discussion.)

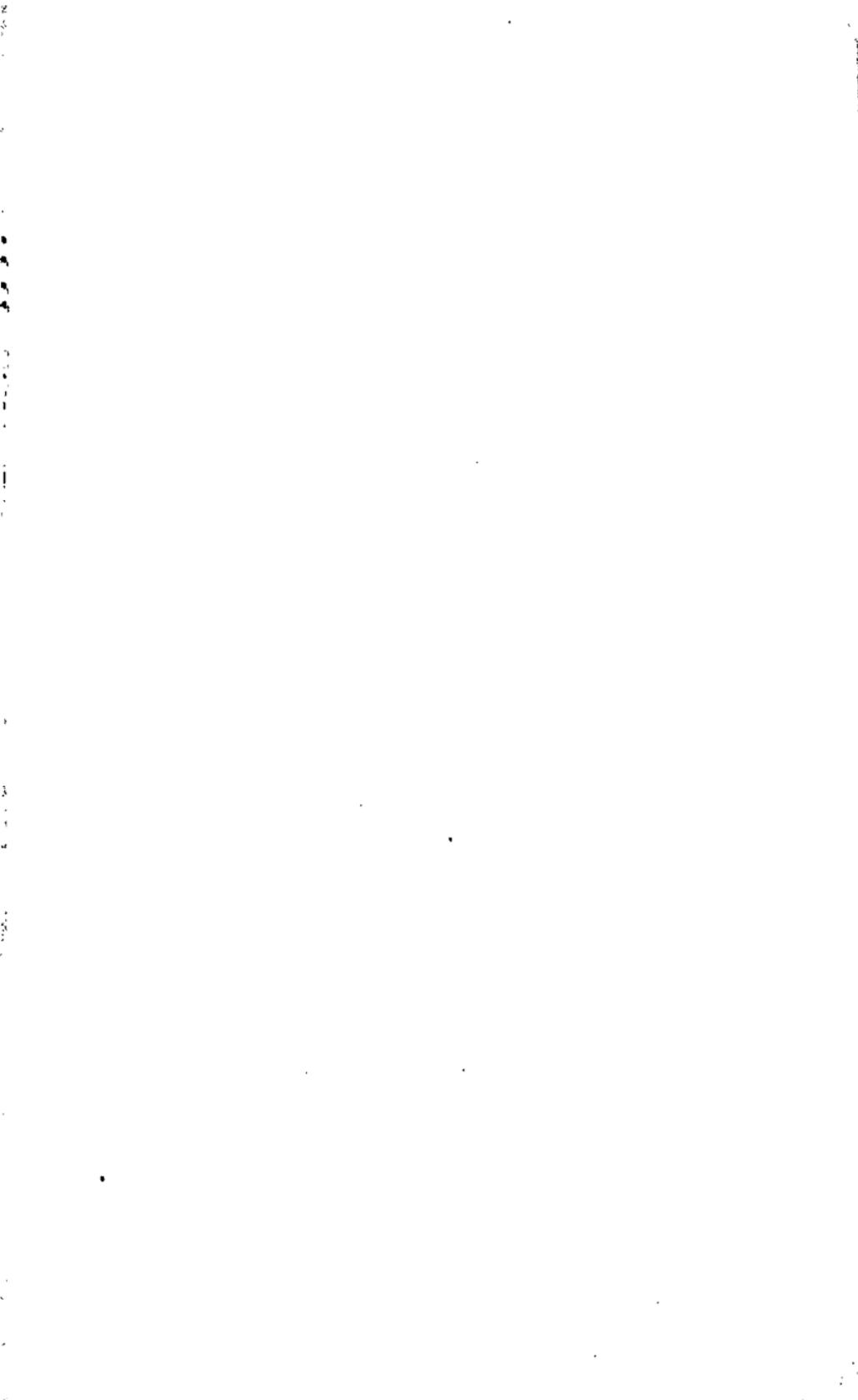
It might not be necessary to meet this afternoon, but I think that while we are here Mr. Sullivan, who has been participating actively in connection with this bill and who represents the Treasury, should be heard. As one member of the committee I am anxious to get along as expeditiously as possible. If the committee wishes to postpone it—all right, but if some people want to adjourn by the 22d, we can't do it if we are going to hold this bill up and go into every detail of the

tax problem. We have got to decide whether we are going to have hearings or not. There are some gentlemen who want to be heard. We never have considered a tax bill yet where there weren't some people who wanted to be heard on taxes, and we have got to decide that question.

Mr. SULLIVAN. I have no pride of authorship in this paper, and I would be very happy to dispense with reading it and go right into questions, if you want to.

The CHAIRMAN. Suppose we have an executive session so that we can lay out a program of what we intend to do.

(Whereupon, at 11:50 a. m., the hearing was adjourned, the committee went into executive session, and thereafter the public hearing was recessed until 10 a. m., Thursday, June 13, 1940.)



REVENUE ACT OF 1940

THURSDAY, JUNE 13, 1940

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

The committee met, pursuant to recess, at 10 a. m., in room 312, Senate Office Building, Senator Pat Harrison (chairman) presiding.

The CHAIRMAN. The committee will come to order.

Mr. Sullivan, will you proceed with your statement?

STATEMENT OF HON. JOHN L. SULLIVAN, ASSISTANT SECRETARY OF THE TREASURY

Mr. SULLIVAN. Mr. Chairman, and gentlemen; the Treasury Department believes that the bill before you satisfactorily meets the tests that should be applied in determining the merits of a tax measure. It will produce substantial additional revenue, it should involve no serious administrative difficulties, and it distributes the tax burden among all elements of the population in a fair and reasonable manner.

The bill imposes no new types of taxes but rather increases the rates of existing taxes and lowers present exemptions from tax. Some of these increases under the bill are to become a permanent part of the revenue system and others are to be operative only for a period of 5 years. It is estimated that the yearly additional revenue to be secured from the bill before you is \$1,004,000,000. Those provisions that are to become a permanent part of the revenue system will produce approximately \$325,000,000 yearly additional revenue and the temporary increases account for the balance of \$679,000,000.

Title I of the bill contains those provisions which make permanent changes in the Internal Revenue Code. Four significant changes in the income tax are made by this title. The first is the lowering of the personal exemptions from the present \$1,000 in the case of a single individual and \$2,500 in the case of married persons to \$800 and \$2,000 respectively. The lowering of the base occasioned by the bill will add some 2,190,000 new taxpayers to the internal revenue rolls and will account for about \$75,000,000 of additional revenue each year.

The CHAIRMAN. There was a good deal of discussion, as I understand, as to married persons, that exemptions be lowered to \$1,800, and I noted the bill places it at \$2,000. How much more revenue will be raised under your estimate, if we made it \$1,800 instead of the \$2,000?

Mr. SULLIVAN. We can compute that on the present surtax schedule and I will give you that answer.

The CHAIRMAN. Can you give us any idea about what it would be? I had an idea that it would be about \$28,000,000.

Mr. SULLIVAN. I don't think you are very far off.

Senator CONNALLY. Is there any proposal to cut the dependency exemption? They get \$400 a child now, don't they?

Mr. SULLIVAN. That is not changed.

Senator CONNALLY. Do they get \$400 for every child?

Mr. SULLIVAN. That is right.

Senator CONNALLY. Suppose they had 10 children?

Mr. SULLIVAN. That is \$4,000.

Senator GUFFEY. They are entitled to it.

Senator CONNALLY. How do you know? [Laughter.]

The CHAIRMAN. I am informed that it would be about \$35,000,000; is that right?

Mr. SULLIVAN. Somewhere between \$25,000,000 and \$35,000,000.

The CHAIRMAN. How would the Treasury feel, if the committee should desire, that instead of making it \$2,000 as an exemption, to start at \$1,800 for married persons?

Mr. SULLIVAN. We are agreeable to whatever is the pleasure of the Congress.

The CHAIRMAN. All right, proceed.

Mr. SULLIVAN (continuing). Of this \$75,000,000, \$14,000,000 will be the amount of additional revenue obtained from the new taxpayers and the remaining \$61,000,000, is the additional amount that will be obtained from those taxpayers who already are paying tax under existing law.

Now, if the suggestion that was just made is adopted, that the personal exemption should be further decreased from \$2,000 to \$1,800, that \$75,000,000 is the figure to which the additional \$28,000,000 or \$30,000,000 would be added.

Senator TOWNSEND. It wouldn't be added to the \$14,000,000, it would be added to the \$61,000,000?

Mr. SULLIVAN. There would be something added to the \$14,000,000, but some two-thirds of the increase probably would come from those taxpayers who are already on the rolls, because you see the effect of lowering the personal exemption is that it takes the amount by which that exemption is lowered and at present it is being lowered \$500, and at \$1,800 it would be lowered \$700, and it puts it at the top bracket, so that that additional \$700 would be taxed at the higher surtax bracket applicable to that person's net income.

Senator TOWNSEND. Could you, in making up the figures, state just how much would be added to the \$61,000,000 and how much to the \$14,000,000?

Mr. SULLIVAN. Yes; we could, sir, and we will do that.

Senator CONNALLY. In making these estimates have you made any estimate of any increase by reason of the fact that 1,000,000 or so that heretofore have not filed returns and consequently haven't paid any taxes, might by the mere reason of the filing of the returns—you might get some money that you had been entitled to all the time—

Mr. SULLIVAN (interposing). You are now referring to those people who are in the employ of the States and counties and municipalities?

Senator CONNALLY. No; I am talking about anybody. You require now, as I understand, in this bill, that a great many people

that have never had to file returns have got to file them whether they have got any income taxes or not?

Mr. SULLIVAN. Yes; and our estimate on that is 8,000,000 rather than 1,000,000.

Senator CONNALLY. Certainly you will get money there, some money, because there are a great many people that had they been filing all this time would have been paying taxes, but they didn't think they were taxable. You estimate that that will pick up \$8,000,000?

Mr. SULLIVAN. No; we say that there will be 8,000,000 individuals who have never been required to file income-tax returns, or who have never filed them, who will file them.

Senator CONNALLY. Have you made any estimate of the pick-up on that?

Mr. SULLIVAN. Yes, sir; we prefer to call that a guess, because this is a field in which we have had no experience, our guess is extremely rough, and it is that it will run between \$25,000,000 and \$45,000,000.

Senator GERRY. How much do you figure it is going to cost you to collect this money, to check up on these—

Mr. SULLIVAN (interposing). In just handling these 8,000,000 returns?

Senator GERRY. No; you will have to make checks to see that the returns are being filed.

Mr. SULLIVAN. We figure roughly \$8,000,000; to handle a return upon which a tax is paid averages \$1.56; to handle a return upon which a tax was not paid averages about 50 cents, and we figure that it will come to just about \$8,000,000.

Senator VANDENBERG. Under your figures, Mr. Sullivan, if there are 2,190,000 new taxpayers, and they pay only \$14,000,000, then the new taxpayers are going to pay about an average of \$7 apiece; is that right?

Mr. SULLIVAN. I think that is probably so.

Senator VANDENBERG. Well, we are not putting very much of a burden on them, are we?

Mr. SULLIVAN. Well, everything is relative, you understand that under this act, sir, a single individual who is earning \$15.40 a week will be obliged to make a return.

Senator TOWNSEND. What surprises me most about the figures is that the amount is so small—\$14,000,000, and what we are getting—

Senator VANDENBERG (interposing). Well, \$7 a year is about 15 cents a week. All I am saying is that I don't think they have got much kick against this bill.

Mr. SULLIVAN. We haven't had any evidence of complaints, and as a matter of fact there have been coming into the Treasury the most amazing series of telegrams and letters enclosing contributions toward a national defense fund. Some checks have been coming in as high as \$500, and many contributions of 10 cents.

The CHAIRMAN. Let me ask you this. I have a letter from a gentleman from Miami, Fla., whose judgment I respect. What is your reaction on this suggestion? I have heard the same suggestion made in the Senate cloak room, notably by our friend, Senator Tydings, of Maryland.

Sometimes a good thought comes from the outside. I was talking to an internal revenue man today who is a good friend of mine, and he gave me this

thought. If it should work out, I will send you his name so he can be given the credit. This chap says that there are approximately 6,000,000 tax returns annually. He advocates that as about 40 percent of these 6,000,000 returns are not taxable, an extra \$5 tax be placed on all tax returns, and an extra \$10 on all nontaxable returns. This will not hurt anyone, and would net the Government \$40,000,000.

Then he says that he thinks it is a good idea. What is your reaction?

Mr. SULLIVAN. Of course, the question immediately coming to my mind is whether or not such a proposal is constitutional. It is in the nature of a limited poll tax, a direct tax which is apportioned not among the States, but I imagine it is contemplated that it would be apportioned as to gross income of the various people who are obliged to file. There isn't any doubt but what it would raise revenue.

Senator KING. Would it be unconstitutional from your hasty examination of the matter? To say that all persons shall file an income-tax return within a certain time, and that with it there should be a tax imposed of \$1 or \$5 or any sum that might be indicated?

Mr. SULLIVAN. Well, I don't know, I think perhaps you have in mind that many people are obliged to pay a certain tax for a certain privilege. This is a little bit different from that, Senator King, I think, because here is a law that will require a person with a certain gross income to file a return and if they don't do it, they will be subject to certain penalties. So that whatever filing fee they are paying is not voluntary in exchange for a privilege, as for example a privilege to fish or to hunt or whatever it may be.

I don't know, sir, I have some doubt about that.

Senator KING. Well, I would have some doubt—obviously that is along the line of the suggestion made in this letter.

Senator BROWN. I have been thinking along that same line as suggested. I think that from the legal standpoint you could put it in a little different way. Suppose we applied it only to these 2,190,000—as I recall the number—new taxpayers; and to save them from what I know to be a fear on their part when they are making out a Federal income tax return—they just don't like the trouble of making it out—make the rate so that there would be a flat \$5 for any taxable income to any person below the \$2,000, the \$2,500 or the \$1,500 limit; in other words, make it a flat figure.

Mr. SULLIVAN. I think we are trying to accomplish the same thing by indirection.

Senator BROWN. Possibly, but I think that would be legal. You don't have to make your rates absolutely uniform.

Mr. SULLIVAN. Correct, sir.

Senator BROWN. A fellow with a \$11,000 income is taxed perhaps at a very different rate if he is in the surtax bracket, low down—

Mr. SULLIVAN (interposing). No "perhaps"; he is.

Senator BROWN. Then if he is in the surtax bracket higher up. So within that classification it seems to me that you could take the suggestion I make and apply it.

Mr. SULLIVAN. You mean that rather than have a graduated rate up to a certain point it would be a flat rate?

Senator BROWN. Just a flat \$5 tax.

Mr. SULLIVAN. I think I would want to consider that before I gave you an answer, sir.

Senator BROWN. I am just thinking of the trouble to these 2,000,000 new taxpayers, and I don't think they mind paying the \$5 tax half as much as they mind making out a complicated income tax return. It is complicated to them, and I want to save them that trouble.

Senator VANDENBERG. That would eliminate all the necessity of checking the return.

Senator BROWN. That is exactly right.

Mr. SULLIVAN. I don't think that is quite true, Senator Vandenberg, I think you would have to check the returns to see that they were correct in their assumption that they did come within that rate.

Senator BROWN. That would be a very simple check.

Senator VANDENBERG. It would minimize the work.

Mr. SULLIVAN. It would, very much.

Senator BROWN. How much did you tell Senator Gerry it cost to check the additional returns?

Mr. SULLIVAN. We estimate it will cost \$8,000,000 to check the 8,000,000 additional tax returns.

Senator BROWN. And you would get \$14,000,000?

Mr. SULLIVAN. No; we would get in addition to the \$14,000,000, we anticipate that we will take into our collections the people who should have been filing in the past but who haven't filed, and that those additional people will give us an additional revenue somewhere between \$25,000,000 and \$45,000,000. You see here is the difficulty under the present system, Senator. John Jones has a gross income of \$1,500. He knows he doesn't have to pay an income tax unless he has a net income of \$1,000, under the present law, and he says, "Now, let's see, I paid so much to the church, so much to the Y. M. C. A., and I had incidental expenses on my car, going to and from my job; I am sure it takes it down below the \$1,000, and I am not going to bother to file a return."

But we have taken samples of those persons and required them to file returns and we find that it hasn't amounted to \$500, that maybe it amounted to \$200 or \$225. And it is from that group that we expect that this additional \$25,000,000 to \$45,000,000 will be collected.

The CHAIRMAN. All right, you may proceed.

Mr. SULLIVAN (continuing). This bill does not change the existing \$400 credit for dependents nor the earned income credit.

The second significant amendment to the income-tax law contained in title I is the increase in the surtax rates. Although this increase affects all taxpayers having surtax net incomes in excess of \$6,000, the increases are heaviest on the lower and middle ranges of the schedule—from \$6,000 to \$100,000.

Tables have been prepared comparing the tax burden on net incomes of selected sizes under existing law with that under the surtax schedule proposed by the bill.

The increase in surtax rates effected by title I of the bill is estimated to yield an additional \$177,000,000 annually. In other words, the total increase in individual income taxes resulting from lowering the base and increasing the surtaxes totals some \$252,000,000 per year. That figure is arrived at by adding to the \$177,000,000 here, the other \$75,000,000.

The third major amendment contained in title I of the bill is an increase of 1 percent in the tax rate in every bracket of the corporation

income tax. For example, the 18-percent rate now provided for corporations having a net income in excess of \$25,000 is raised to 19 percent. With respect to corporations having a net income of \$25,000 or less, the present law provides for a tax of 12½ percent on the first \$5,000 of net income, 14 percent on the next \$15,000, and 16 percent on the last \$5,000. These rates have been increased to 13½ percent, 15 percent, and 17 percent, respectively. The additional revenue raised by the new corporate tax rates is estimated at \$70,000,000 a year.

The fourth important change in title I of the bill is a provision which calls for the filing of income-tax returns by all single individuals who have a gross income of \$800 and by married persons with gross incomes of \$2,000. By eliminating the net income test as the basis for the requirement of filing returns and by lowering the \$5,000 gross income test to \$800 in the case of single persons and \$2,000 in the case of married persons, the bill will add some 8,000,000 returns to the some 7,500,000 individual returns now filed annually. The present net income test for the filing of a return makes each person in effect his own auditor in determining what are the proper deductions to take from gross income. It is believed that today many persons fail to file returns on the assumption that their net income is insufficient whereas actually they are liable for the filing of a return and the payment of a tax. That is the matter I referred to. Although the addition of 8,000,000 returns will result in increased administrative burden and additional expense, it is anticipated that the revenue which will be collected as the result of this change will be in excess of the additional cost of \$8,000,000. Since it is almost impossible to estimate the increase of revenue from this source with any accuracy, the estimates of the annual additional yield from the bill do not include any increase in revenue from this source.

In other words, the \$25,000,000 to \$45,000,000 we were discussing, Senator Gerry, is not included in \$1,004,000,000 that is anticipated as additional yield from the bill that is now pending before you.

The changes made by title I apply to incomes for the taxable year 1940 and subsequent years.

Title II of the bill contains those increases in the existing tax rates which are of a temporary nature, their duration generally being limited to 5 years. The pattern of this title is to provide a 10-percent increase in the rates of most internal-revenue taxes. In a few instances the increase is greater than 10 percent and in other instances no increase has been made—and that refers, Senator Vandenberg, to the import-excise and the regulatory excise taxes you referred to yesterday, and to that tax I should have added the tax on rectifiers which was eliminated from the original bill in the House.

Senator BARKLEY. Since you have mentioned that rectifiers' tax, it is the judgment of the Treasury, as indicated by the bill prepared by the subcommittee of the House, that inasmuch as the tax on straight liquor is increased from \$2.25 to \$3 a gallon, there ought to be a corresponding increase in rectifiers' tax in order to adjust the difference in cost of production with the tax?

Mr. SULLIVAN. That is true, that was the opinion of the Treasury Department and of the Alcohol Tax Unit of the Internal Revenue Bureau.

As already stated, it is estimated that \$679,000,000 additional revenue will be derived annually from the increases provided in this title.

The CHAIRMAN. What were the reasons advanced why there was not a differential on the rectifiers' tax and the tax on straight liquor?

Mr. SULLIVAN. There was a good deal of discussion on that, and they seemed to feel that inasmuch as the rectifiers had to use, at least in part, tax-paid liquor on which this additional tax would be paid, that the rate should not be raised as to them.

Senator BARKLEY. While we are discussing that subject, I would like to state that the reason for the differential of 30 cents, as it now exists, grows out of the fact that straight whisky will be taxed \$3 a gallon, and costs about 90 cents a gallon to produce, including storage in bonded warehouses and so forth.

Rectified whisky is about one-fourth straight whisky plus three-fourths raw or pure alcohol, which costs 16 cents a gallon to produce; and while it does pay the \$3 tax when you mix the three-fourths part with the one-fourth part, raw alcohol and straight whisky, you bring about a combined cost of production that is considerably less than the cost of producing the straight whisky plus the tax, isn't that true?

Mr. SULLIVAN. That is correct, the three-quarters that you refer to may have been made yesterday or the day before, and there is no storage charge.

Senator BARKLEY. There is no storage charge or aging charge, it is just a plain straight cost of production which I understand is about 16 cents a gallon.

Senator KING. Mr. Sullivan, coming to the item of \$679,000,000, what part of that results from the excise taxes, and what part from the 10 percent increase?

Mr. SULLIVAN. That is the last sentence which I read?

Senator KING. Yes.

Mr. SULLIVAN. The total raised under title II, Senator King, for a full year, is \$678,000,000.

Senator KING. \$679,000,000 you have in your report.

Mr. SULLIVAN. It is \$678,000,000. In my statement I am using approximate figures. Now, of that \$679,000,000, \$135,000,000 comes from increase in corporate income taxes; \$123,000,000 comes from increase in individual income taxes; \$12,000,000 comes from increase in capital stock and excess-profit taxes; \$29,000,000 comes from increase in estate taxes; and \$3,000,000 from increase in gift taxes.

The rest are increases in excise taxes and the direct answer to your question is that subtracting these, the amount that is raised from the increase in excise taxes is \$376,200,000.

Senator KING. That would be the tax on the excise taxes?

Mr. SULLIVAN. Yes; and that excludes the gift and estate taxes as well as the capital stock and excess-profits taxes.

Senator KING. I assume that you weighed the question as to whether that was a fair adjustment, or whether you had imposed upon the excises too much or too little, measured by the increase that is imposed upon the other factors here which gives a total of \$679,000,000?

Mr. SULLIVAN. Yes; we recognize that a large amount is being raised from increase in excises and that a large proportion of those increases will be paid by people in the lower brackets. I am new at this game; there isn't anybody in this room who hasn't had a great deal more experience in tax matters than I have, but frankly the one

thing that I have learned is that there isn't any amount of cleverness or facility of phrase, or legal legerdemain that is going to raise revenue without taking money away from somebody. This just is about the best we have been able to devise in the time we have been working on it, Senator.

Senator BROWN. Have you ever used this term "supertax" before in the tax law?

Mr. TARLEAU (Thomas Tarleau, legislative counsel of the Treasury). The British have a term somewhat similar.

Senator BROWN. I was just wondering what evil genius in the Department devised that term?

Mr. SULLIVAN. I guess you are looking at him, Senator.

Senator BROWN. I don't like it. Why don't you make it easier for the taxpayer and not remind him by that phraseology that he is paying a supertax, but call it a national-defense tax.

Senator BARKLEY. Why give it a nickname any way, why not call it a tax?

Mr. SULLIVAN. I think the reason for that, Senator Barkley, is that this particular tax expires in 5 years, whereas the other changes you are making remain on the books. I think it should have some distinctive title.

Senator BROWN. We could call it the defense tax just as well, to remind the taxpayer what good his money is doing, rather than the fact that we are taking a large amount of money out of his pocket.

Mr. SULLIVAN. Isn't all of this money raised under this bill for defense purposes?

Senator BROWN. Then call it that, but why call it supertax? That reminds the taxpayer that we are soaking him pretty hard.

Senator VANDENBERG. If we don't say anything about it in the campaign, would it be all right? [Laughter.]

Senator BROWN. I would be a little bit disturbed about the Democratic Party putting on a "supertax."

The CHAIRMAN. The first time I ever heard of "supertax" was when it was employed by a distinguished Senator from your State, Senator Couzens.

Senator BARKLEY. It might be a defense tax and still not be super.

Senator BROWN. Let his successor denominate it by a little more enticing term.

Senator KING. Well, the word "super" now connotes many things. We apply it to ships of the air and ships of the sea.

Senator CONNALLY. A tax by any other name is just as burdensome.

Senator BROWN. But it doesn't smell as bad.

Senator KING. We might call it an esthetic tax.

Senator BROWN. Defense tax is what it ought to be called.

Senator VANDENBERG. You might call it "bottom of the barrel" tax.

Mr. SULLIVAN (continuing). Individual and corporate income taxes, beginning with incomes for the taxable year 1940, have been increased 10 percent. This 10 percent increase in the amount of tax is to be computed upon the tax payable under the permanent increases in rates effected by title I. The bill contains a special provision designed to alleviate the severity of this increase in the case of taxpayers in the very high surtax brackets, who under title I would pay more than 50 percent of their incomes in Federal income taxes. Under this special provision, the 10 percent increase will in no case result in a

levy of more than 10 percent of the income remaining to an individual taxpayer after payment of his title I Federal income tax liability. It is estimated that the 10 percent increase in individual and corporate income taxes will yield \$258,000,000 annually.

The excess-profits tax, the capital-stock tax and the estate and gift taxes are all increased 10 percent. The increase in the excess-profits tax is effective for any taxable year ending after June 30, 1940, and before July 1, 1945. The capital-stock tax is increased for the year ending June 30, 1940, and for the 4 succeeding years thereafter. The increase in the estate tax is made effective with respect to decedents dying after the enactment of the bill and before the expiration of 5 years thereafter. The increase in the gift tax is applicable to the calendar year 1940 and subsequent calendar years up to and including 1945. With respect to the calendar year 1940, the increase in effect is applied to gifts made after the enactment of the bill.

As stated above, most of the Federal excise taxes are increased 10 percent, effective July 1, 1940. Since many of these taxes were due to expire in 1941, this 10 percent increase necessitates an extension of such taxes to 1945, and this extension is provided for in the bill. The 10 percent rate of increase, however, has been departed from in some instances, either for reasons of revenue or of administrative necessity. The principal exceptions are the increases in the taxes on alcoholic beverages, tobacco products, and gasoline. The tax on distilled spirits generally has been increased from \$2.25 to \$3 per gallon and that on brandy from \$2 to \$2.75, an increase of 33½ percent and 37½ percent, respectively. The tax on beer and other fermented malt liquors has been increased from \$5 to \$6 a barrel, a 20 percent increase, and the tax on wines has been increased proportionately. Floor stocks taxes are imposed upon distilled spirits and malt liquors held on July 1, 1940.

Senator BROWN. Can you translate those figures into valuation? What percentage of increase is it on a valuation basis?

Mr. SULLIVAN. On a barrel of beer?

Senator BROWN. On a barrel of beer or a gallon of liquor.

Mr. SULLIVAN. Not on the basis of the tax but on the basis of the sales price.

Senator BROWN. For instance, how much is beer a barrel, how much does it cost?

Senator KING. There are 31 gallons in a barrel.

Mr. SULLIVAN. About \$15 a barrel, that would be an increase of one-fifteenth.

On cigarettes it is an increase of 1 cent a pack.

The floor stocks tax on malt liquors, beer, is not applicable to retailers. The floor stocks tax on distilled spirits is applicable to retailers, but only where the stock held by a retailer amounts to more than 100 wine gallons.

Senator KING. I have a communication which says that the Government has made no distinction between the tax on beer containing less than 3.2 percent alcohol and beer containing over 3.2 percent alcohol.

Mr. SULLIVAN. That is correct.

Senator KING. And the writer states that he feels some distinction should be made. He emphasizes the point that there ought to be a distinction made, that if it is more than 3.2, it ought to pay a greater tax than if it is less than 3.2.

Mr. SULLIVAN. Does he say why, sir?

Senator KING. No; but he feels that the tax should be higher on 3.2, or rather over 3.2 percent than on less than 3.2 percent.

Mr. SULLIVAN. I think that the variation is not great.

Mr. BERKSHIRE (Stewart Berkshire, Deputy Commissioner of Internal Revenue): If you take the alcohol content of a barrel of beer you will find that the tax on the beer is less per proof gallon than the tax that you have on spirits.

Senator KING. Less than on wine?

Mr. BERKSHIRE. No, sir.

Senator KING. Would not there be some reason—and it appeals to a prohibitionist, that is, those who don't believe in an excessive use of alcohol, to encourage a lower alcoholic content than to encourage a higher alcoholic content?

Mr. BERKSHIRE. As far as that is applied to beer, there is very little variation, in the alcoholic content of beer.

Senator CONNALLY. The Senator is making the point that the heavier beer is taxed no heavier, that is, the higher alcoholic content of beer is taxed no heavier than the lighter beer. You are taxing it all at practically the same rate.

Mr. BERKSHIRE. That is right.

Senator CONNALLY. That is all right, it suits me. You are really after the money instead of the beer, anyway, aren't you?

Mr. SULLIVAN. That is right, sir.

The CHAIRMAN. The Buck bill, H. R. 9117, has come over from the House for our consideration and action, and if we are to take action on that bill, we ought to do so before we report this tax bill, so that the appropriate change can be made in this bill. Isn't that right?

Mr. BERKSHIRE. Yes, sir.

Mr. SULLIVAN. Under the Buck bill, the collection of revenue will be increased.

The CHAIRMAN. Yes; I understand \$3,000,000, and so the Treasury is for that bill?

Mr. SULLIVAN. That is right, and for reasons other than the increase in revenue.

Senator CONNALLY. Does this bill carry any taxes on so-called soft drinks like Coca-Cola?

Mr. SULLIVAN. No, sir; it does not.

Senator CONNALLY. Why shouldn't it?

Mr. SULLIVAN. Barkis is willing.

Senator KING. I have been told that the Coca-Cola business is very profitable.

Mr. SULLIVAN. Our estimate, on 1 cent a bottle, is an additional revenue of \$76,000,000 a year.

Senator BARKLEY. On soft drinks?

Mr. SULLIVAN. That is right.

Senator BARKLEY. At 1 cent a bottle?

Mr. SULLIVAN. Yes, sir.

Senator GEORGE. You are not interfering with the basic rate on any of these taxes, you are simply adding the 10 percent or some arbitrary percent where 10 percent cannot be practically collected?

Mr. SULLIVAN. That is correct.

The CHAIRMAN. Let me ask you a question, Mr. Sullivan. I have a memorandum here with reference to this increased tax on liquors. The following amendment is suggested:

except for use in the extraction, manufacture, and preservation of medicinal preparations.

We have had that question before us many times before. Did the House give consideration to that question?

Mr. SULLIVAN. That was discussed briefly in the subcommittee, sir, and not thereafter referred to. We feel very unhappy about that for this reason. A similar exemption in favor of otherwise taxable liquor for medicinal purposes, pharmaceutical purposes and for foods, flavoring extracts and what not, was in the law during prohibition, and there were 43,000 permittees who were withdrawing liquor for those purposes.

We estimate that if the exemption were to be made now it would amount to about 50,000 permittees. There would be an additional administrative cost to the revenue bill in excess of \$1,000,000 and we would lose about \$6,000,000 tax on the liquor.

Now, in the case of a prescription, the increased cost in the preparation of the average prescription, according to the best information I have been able to get, because of the increase in the tax on the alcohol contained in that prescription is about a half of a cent a prescription.

The CHAIRMAN. So the Treasury opposed that?

Mr. SULLIVAN. Yes.

The CHAIRMAN. Largely on account of the administrative difficulties and costs?

Mr. SULLIVAN. That is right, where it is going to cost the average person who buys a prescription an additional one-half cent per prescription, we rather question whether that justifies costing the Treasury in excess of \$7,000,000 a year.

Senator KING. Mr. Sullivan, I had a communication which stated as follows:

I note in the proposed bill there is no reference to tax on soft drinks nor a tax on carbonic gas which goes into soft drinks. In the World War a tax was placed upon these beverages and I see no reason why competing as they do with various other products they should not bear some of the necessary burden of the present defense program.

Was that matter considered by the Treasury Department?

Mr. SULLIVAN. Yes; I think you will recall that this particular measure includes no new types of tax that are not at the present time on the books. The revenue that is raised under this bill is raised rather by an increase in the tax rate on those things that are now taxed.

Senator VANDENBERG. They are just confined to super taxes?

Mr. SULLIVAN. That, plus the increase in the permanent rate, sir.

Senator BARKLEY. Let me ask you, is that a very scientific way to approach this proposition, to tax more those that are already taxed, and leave untaxed those that are now untaxed?

Mr. SULLIVAN. I was merely trying to explain that.

Senator BARKLEY. For instance, you have got no tax here on soft drinks which you say would raise about \$76,000,000 a year.

Mr. SULLIVAN. Yes, sir.

Senator BARKLEY. You have increased the tax on tobacco products which is the only product in the United States that still bears a World War tax rate.

Mr. SULLIVAN. That is right.

Senator BARKLEY. And 4 years ago was raising one-eighth of the entire revenue of the United States.

Mr. SULLIVAN. That is right.

Senator BARKLEY. You add \$76,000,000 to the more than \$500,000,000 already being raised on tobacco products, and leave soft drinks, which is equally a luxury with tobacco, if either is a luxury—maybe both of them are a necessity to some people—but as a matter of fairness why add \$76,000,000 to that product which is already, or was until 2 or 3 years ago, paying one-eighth of the entire expense of the Government, and leave completely untaxed these soft drinks which could bear probably a 1-cent tax per bottle and raise the same amount of money?

I am not pleading for tobacco simply because I come from a tobacco State, but I happen to know that it is the only product that still bears the World War tax rates, they have never been reduced at all, and while everything else was reduced it was kept at that rate.

Now, if you have got to collect that \$76,000,000 extra from the tobacco products, which in the long run is taken out of the grower of tobacco, because those who buy these products claim they can't pay so much for it because of the tax, and what they make out of it, if you have got to add \$76,000,000 to the tobacco producers, which in my judgment is the effect of this, why can't you raise another \$76,000,000 by this tax?

Mr. SULLIVAN. We can, sir, and the Treasury does not object to such a tax.

Senator BARKLEY. What would you think of that sort of a tax and substitute it for the \$76,000,000 you are adding for tobacco?

Mr. SULLIVAN. I don't know as I want to pick and choose. We would welcome the addition of another \$76,000,000.

Senator BARKLEY. You have already picked and chosen by adding this additional tax to tobacco, and not taxing these others.

Mr. SULLIVAN. Perhaps there has been picking and choosing, but I don't know as that has been the picking and choosing—

Senator GEORGE (interposing). Congress has done the picking and choosing, Congress has simply retained certain taxes, and this proposal is to increase those taxes in order to get immediate revenue.

Senator BARKLEY. That is true, but that in itself is not very good justification for only picking those that have been chosen heretofore.

Mr. SULLIVAN. We are quite willing to accept your suggestion, sir.

Senator GEORGE. There are many things that we could tax, there is no doubt about that.

Senator BARKLEY. Maybe we ought to do it.

Senator BAILEY. I wish to suggest that the tobacco farmers are losing about one-third of their market on account of this war. The export tobacco from my State is fully 50 percent of the total production. It is not likely to be anything this year so far as I can see. Of 175,000,000 pounds bought last fall for export under Government loans, only 1,000,000 pounds have been carried across the Atlantic. France has quit buying the burley, England has quit buying the bright, or the cigarette tobacco.

Senator BARKLEY. And everybody has quit buying the dark.

Senator BAILEY. You are adding this to the highest tax burden in America, the only old World War tax. I am only saying that this tax ought to be considered in light of the fact that the tobacco pro-

ducers in this country stand to lose from 30 to 50 percent of their market this year. Now, if they lose it over here besides, it is my judgment that the money you raise, every dollar of it, will have to go for relief. You will gain nothing whatever for national defense.

Senator KING. And the Government will stand to lose many of those loans which it has made to the tobacco growers because of their inability to sell their product.

Senator BAILEY. Yes.

Senator KING. So there will be a double burden upon the Government.

Senator BAILEY. There will be a loss in revenue to the Government if you cut down the consumption.

I would like to have the Treasury Department, in making its recommendations, look into this situation. I am just calling your attention to the fact that this policy is calculated to ruin the tobacco farmers of North Carolina, who number about 300,000. It will ruin the tobacco farmers in South Carolina and in Georgia and in Alabama and in Florida, and in Kentucky and Tennessee.

Senator GUFFEY. And in Pennsylvania.

Senator BAILEY. And in Pennsylvania.

I would like the Treasury to think about that.

I am going to vote for the bill, I know I have got to, I don't care what sort of bill you put out, I am going to vote for it, but I should say we ought not to put up a bill that destroys our own people. That is not national defense.

Mr. SULLIVAN. That is quite true.

Senator BARKLEY. I feel the same way about it, I realize that the taxes you are increasing affect my State very largely and very effectively, both on liquor and tobacco, and if it weren't for that gold we have got buried down there, I don't know how we would get along with paying these extra taxes. We may have to draw a little on that.

Senator Bailey has mentioned the bright and the burley which England and France have quit buying. The dark tobacco, which is produced almost exclusively in west Kentucky, 85 percent of it was sold in the foreign market, and practically all of that is gone, they have got no market for it anywhere. I am thinking about what the effect is going to be on the man down at the bottom, and of course I am not going to oppose these taxes, I mean I am for the taxes, I want to raise the revenue, but I do feel that it is proper to call attention to the great disproportion part of these increases which will be borne by limited localities in the United States, especially on these products that I have mentioned.

The CHAIRMAN. All right, proceed, Mr. Sullivan.

Mr. SULLIVAN. For the sake of the record, I have the exact figures on the proposal to exempt liquor for medicinal and food purposes. I told you I thought it would be around \$1,000,000 for additional administrative expense. Our estimate is \$1,124,300. The amount we would lose in tax is \$6,000,000, so that would result in a total loss to us of \$7,124,300.

The rates of these floor stocks taxes are equal to the difference between the present rates of tax and the increased rates provided in title II of the bill—75 cents per gallon in the case of distilled spirits and \$1 per barrel in the case of malt liquors. The increase in the taxes on alcoholic beverages, exclusive of the floor stocks tax, is estimated to yield \$125,000,000 annually.

The tax on cigarettes has been raised from \$3 to \$3.50 per thousand, an increase of 16½ percent. The rates on other tobacco products have been increased in the same proportion. Chewing tobacco has been exempted from this increase, because of the constantly diminishing use of this product and the small amount of revenue involved. A floor stocks tax has likewise been imposed on tobacco products, applicable to those held by manufacturers and wholesalers on July 1, 1940, at a rate equal to the difference between the existing tax rate and the new rate under title II. The increase in the taxes on tobacco products, exclusive of the floor stocks tax, are estimated to yield \$76,000,000 annually. The floor stocks taxes on alcoholic beverages and tobacco products are together estimated to yield \$26,000,000 for the fiscal year 1941.

Senator CONNALLY. You exempt retailers from the floor stocks tax on 100 gallons of liquor, don't you?

Mr. SULLIVAN. A hundred wine gallons, yes, sir.

Senator CONNALLY. Suppose we didn't exempt them from that, why should we exempt them, how much would that give?

Dr. O'DONNELL. (Dr. Al F. O'Donnell, Assistant Director of Research and Statistics, Treasury Department). I think Mr. Berkshire might better answer that, Senator.

Mr. BERKSHIRE. The average return in 1938 showed that each retailer had 40 gallons; in round numbers there were 250,000.

Senator CONNALLY. Well, if he is going to be exempt, he will buy a lot in anticipation of this tax.

Mr. BERKSHIRE. They didn't do it before.

Senator CONNALLY. How much tax would we save if we didn't exempt them?

Mr. BERKSHIRE. You would want to multiply 40 gallons by 250,000 and that would be the gallons which we would collect the 75 cents on.

Mr. SULLIVAN. That would be \$7,500,000, Senator.

Senator CONNALLY. What would it cost—the expense be high to get that \$7,500,000?

Mr. BERKSHIRE. No, sir; we would get that without additional cost.

Senator CONNALLY. Why shouldn't we get that \$7,500,000?

Mr. BERKSHIRE. That is all right. The exemption wasn't in the Treasury bill.

Senator KING. That would be regarded as a new tax along the lines that you have differentiated the new taxes and simply adding to—

Mr. SULLIVAN (interposing). I think that whenever they had the floor stocks tax before, there was some exemption, it was 250 gallons in the last floor stocks tax on liquors. This is reducing that exemption from 250 to 100.

Senator CONNALLY. On the report on page 21, the last line, it says, "an exemption of 100 wine gallons is accorded to retail dealers."

I don't see any reason why the retailers should be exempt from that increased tax of 7,500,000. If you don't put it on, he will probably stock up and buy himself an extra quart before this tax goes into effect. I think we ought to strike that exemption myself.

Mr. SULLIVAN. The point that Deputy Commissioner Berkshire was making was that although in the 1938 act there was an exemption of 250 gallons, the trade did not avail itself of that opportunity

to stock up, and when the returns came in, instead of having up to the full exemption of 250, the amount of liquor the average concern had on hand was only 40 gallons.

Senator CONNALLY. But suppose you don't buy another drop, you get 7,500,000 on what he has on hand?

Mr. SULLIVAN. Yes, sir. If each one only had an average of 40 gallons on hand, as they did the last time, we would get 7,500,000.

Senator CONNALLY. That is a pretty good percentage.

Mr. SULLIVAN. Yes, sir.

Senator CONNALLY. And no expense to collect it?

Mr. SULLIVAN. We have got to go through the motions.

Senator LA FOLLETTE. Isn't that same thing true with regard to the tobacco floor stocks tax if you exempt the retailer?

Mr. SULLIVAN. Yes, we will lose some revenue there, sir.

Senator LA FOLLETTE. And wouldn't you create an unfair competitive situation in that larger retailers will be able to stock up between now and the 1st of July, and the smaller dealer will not be able to do so?

Mr. SULLIVAN. To a degree, sir, that is true, and the reason it isn't true to a greater degree is that there is a limit upon the length of time they can keep them, and have them fresh.

Senator LA FOLLETTE. That is true, but why should we create that unfair situation?

Mr. SULLIVAN. We have no objection to the imposition of a floor stocks tax on retailers, but we would remind you that the last time we had it, we had something over 800,000 returns, and I can get you the figures—

Senator LA FOLLETTE (interposing). Suppose you put some ceiling on it, gave them some amount that you would permit them to have without imposing a tax?

Mr. SULLIVAN. That is right. Well, we will then save some of the revenue and we will have almost all the additional administrative expense. I have those figures but I am sorry I haven't them on the tips of my fingers.

Senator DAVIS. What is the total amount of revenue coming in from the sale of cigars?

Dr. O'DONNELL. We collected \$12,400,000 in taxes on large cigars in 1939.

Senator DAVIS. What will this additional tax that you have on cigars raise?

Dr. O'DONNELL. It will raise that amount by approximately one-sixth.

Senator DAVIS. One-sixth of that amount?

Isn't it difficult now to sell cigars, and putting this additional tax on, wouldn't that decrease the revenue rather than increase it?

Dr. O'DONNELL. It can't possibly decrease the revenue unless the decreased consumption is much more than proportionate to the increase in tax since the tax is only a fractional portion of the sales price.

Senator DAVIS. It will decrease the sales?

Dr. O'DONNELL. Yes; as regards to what you would have sold if you had not increased the tax; that is true.

Mr. SULLIVAN. I can give you those figures, Senator La Follette. The additional revenue we would receive by imposing a floor-stocks

tax on tobacco with retailers would be \$4,500,000. We would expect something in the vicinity of 900,000 returns and it would cost us about \$2,500,000 to collect the \$4,500,000.

Senator LA FOLLETTE. You would have a net gain?

Mr. SULLIVAN. Yes; of \$2,000,000.

Now, if you allow an exemption of \$10, \$20, or whatever you would decide upon, there would still be the same administrative expense, but the collections would be that much less.

Senator KING. It seems to me that your expenses for collection are tremendously high. It costs \$2,500,000 there. You have your machinery all set up and it would seem to me that an additional expense of collection should be very small.

Mr. SULLIVAN. Well, this is hardly over \$2 a return; that means a collector has to go to every little retail store, Senator King. I don't think you would find that high. We can give you a complete breakdown of that. You see, we don't know when we get a return whether it is correct; we have got to just go and check up on that.

The CHAIRMAN. Proceed.

Mr. SULLIVAN (continuing). The tax on gasoline has been increased from 1 to 1½ cents per gallon and the increase is estimated to yield \$112,000,000 annually.

Senator BARKLEY. Let me ask you about that gasoline tax.

Mr. SULLIVAN. Yes, sir.

Senator BARKLEY. Isn't it very inconvenient to collect any multiple of a half a cent by tax? Suppose a man goes up to a gasoline station to buy 5 gallons of gasoline. The tax is 7½ cents. Now, the gasoline salesman can't change a cent into a half, and he couldn't collect the 7½ cents, but he would probably collect, and maybe 10, I don't know, but he would collect 8 anyhow because he couldn't give the man a half a cent in change.

Wouldn't it be better really to make that tax another cent, instead of half a cent, and you would raise \$56,000,000 more?

Mr. SULLIVAN. Excuse me, you would raise \$112,000,000 more.

Senator BARKLEY. That is right, it would double this amount with a 1 cent tax and raise \$224,000,000.

Mr. SULLIVAN. That is right.

Senator BARKLEY. My information is that practically all the States levy a gasoline tax in multiples of a cent. There may be some that have a half a cent, but not many as I understand it.

Mr. SULLIVAN. That is right, sir.

Senator BARKLEY. I don't see how it is going to be practicable to collect a tax of 1½ cents. If you could be sure that everybody would buy 10 gallons or 20, where the tax would be 15 cents or 30 cents, it would be easy to see how the change could be made, but in this multiple of half a cent, wouldn't the taxpayer pay more money inevitably that would never get into the Treasury?

Mr. SULLIVAN. He may in some instances, but the number who buy odd numbers of gallons is not necessarily great. There is an increasing vogue of going up to a filling station and not saying, "Give me so many gallons," but "Give me \$1.50 worth of gasoline," or "Give me \$2 worth of gasoline."

Senator BARKLEY. That would make it even more difficult to figure on a 1½ cent basis.

Mr. SULLIVAN. We now have the same difficulty in the trade because although the tax is in even numbers, you see some stations that advertise gasoline at 15½ cents a gallon, and they are creating that problem for themselves. There would be some difficulty.

Senator BARKLEY. Is this tax collected at the retail station or is it collected wholesale from the manufacturer?

Mr. SULLIVAN. From the refiner.

Senator GEORGE. Your Federal tax is a producer's tax?

Mr. SULLIVAN. That is right.

Senator GEORGE. It is levied on the producers?

Mr. SULLIVAN. At the refinery.

Senator GEORGE. Of course, the retailer passes it all on, if he can?

Senator BARKLEY. He will pass it all on, there is no doubt about that.

Senator GEORGE. That is the trouble, but so far as the Federal Government is concerned, it is a tax on the producer.

Mr. SULLIVAN. That is right. You think that in many instances the filling station will get the advantage of that half a cent?

Senator BARKLEY. It is possible for that to happen, and I am wondering whether it wouldn't be better, and not very burdensome, to make that tax 2 cents, and not 1½?

Senator KING. During the N. R. A. we had the half a cent, and I was wondering if any of your assistants can tell us how it worked when, under the N. R. A., we had to collect the tax?

Mr. SULLIVAN. Deputy Commissioner Bliss of the Miscellaneous Tax Unit, Bureau of Internal Revenue.

Mr. BLISS. There was no difficulty in collecting it at all as far as the Federal Government was concerned.

Senator KING. How did it affect the consumer, the automobile man when he was buying it, would he pay a cent instead of a half a cent?

Mr. BLISS. I wouldn't know.

Senator CONNALLY. Under the present set-up you collect the tax from the refiner?

Mr. BLISS. Yes, sir.

Senator CONNALLY. Now, when the filling station man sells that gas does he collect any of that tax?

Mr. BLISS. We don't look to him, we look to the producer.

Senator CONNALLY. I am talking about what is the fact.

Mr. BLISS. I imagine that he passes it on.

Senator CONNALLY. He pays that when he buys the gasoline, he pays the refiner 5 cents or 3 cents a gallon.

Senator GUFFEY. Plus the tax.

Senator CONNALLY. That is all right.

Senator GUFFEY. Why should he collect the tax twice?

Senator CONNALLY. I don't want him to.

Senator GUFFEY. He doesn't pass it on—

Senator CONNALLY. I am talking about the Federal tax because it is paid by the refiner, and the State tax is directly, or rather frequently paid by the consumer when he buys the gas. You see a sign up there "tax"—does that include both the Federal and the State tax?

Mr. SULLIVAN. I think in most cases it does include both.

Senator CONNALLY. Then he remits that to the refiner, I suppose, as part of his cost?

The CHAIRMAN. Some States provide that in the sale of the product to the ultimate purchaser, that there shall be maintained a schedule of how much taxes are to be paid.

Mr. SULLIVAN. Yes.

The CHAIRMAN. You don't know how many States have that law; do you?

Mr. BLISS. Practically all of them.

Senator CAPPER. I would like to ask you a question, if I may. My mail this morning is filled with propoganda on this tax question, and among other communications I find one from the American Taxpayers Association, with headquarters in the Munsey Building, Washington, and it encloses a carefully prepared circular, Statement of Associations' Position on Present National Policies, and this paragraph, which interested me, says:

A reduction in tax rates—

Note the statement, "reduction in tax rates"—

particularly on income will increase tax revenue. Past experience and the official records of the United States Treasury Department prove this.

I am wondering if there is anything in the records of the Treasury Department that would bear out any such contention as found in this statement?

Mr. SULLIVAN. I don't know, there may be. I rather think that is a fervent hope rather than a statistically proved statement, but I would want to check that for you before I gave you a statement for the record.

Senator KING. The law of diminishing returns might not apply there.

Mr. SULLIVAN. That is right, Senator.

Senator BARKLEY. Well, if a reduced rate would make a man pay more taxes, he wouldn't be advocating a reduced rate very enthusiastically.

Mr. SULLIVAN. I think there is something else behind this. I think the thought that the Senator read was that if the tax rates were lower, that would cause encouragement to venture capital, and there would be a lower tax rate on a larger volume of business. There is a relationship between cause and effect there which I am not prepared to accept, and upon which I don't think we could gamble in this particular period.

Senator KING. It is assumed if we had \$100,000,000,000 of national income, that we would get larger returns than if we had \$50,000,000,000 with higher taxes?

Mr. SULLIVAN. That is right, sir, that is right and the catch is in the assumption.

In increasing by more than 10 percent the rates on these three commodities—alcoholic liquors, tobacco products, and gasoline—this bill singles out commodities which throughout the world are considered specially suited for the imposition of fairly high excise taxes. The rates imposed upon these commodities in almost every other nation in the world are very much higher than the rates provided in this bill.

Senator VANDENBERG. When you are comparing gasoline taxes with foreign gasoline taxes, you have got to add all of the State taxes also to make a fair comparison.

Mr. SULLIVAN. I think that is true also.

Senator VANDENBERG. There is only one tax abroad on gasoline.

Mr. SULLIVAN. That is right in some places, yes, and in other places, no. But even taking that into consideration the total tax, both State and Federal, paid here is far less than I think you will find you pay for it anywhere abroad.

Senator VANDENBERG. Isn't there something to be said for the theory of leaving a few things for the States to tax?

Mr. SULLIVAN. Yes; and I think if I recall correctly yesterday Secretary Morgenthau spoke of the hope that some time the Federal and State taxing authorities would be able to iron out their differences on that subject.

Senator KING. They may tax the dead, that is about all the State can do.

Senator VANDENBERG. Gasoline is so essentially a source of State income that I think that fact ought to have consideration—some consideration in the degree of added burdens that we add in Washington.

Mr. SULLIVAN. I think that is quite true, sir.

In the case of certain excises a flat increase of 10 percent of the existing rate would not be administratively feasible for this reason: For example, the rates of tax of 2, 4, and 5 cents on transfers of capital stock have been increased to 3, 5, and 6 cents, respectively. Furthermore instead of raising the rate of the admissions tax, it was deemed more feasible from an administrative point of view to decrease the exemption from 40 cents to 30 cents. For practical reasons no increase was imposed with respect to the tax on telephone and telegraph messages. Such an exclusion was deemed necessary inasmuch as there was no way in which a person wishing to make a toll call from a pay station could pay the extra pennies of tax which a 10-percent increase would require.

Senator TOWNSEND. Have you an estimate there of what the amount would be in revenue when you change the exemption from 40 cents to 30 cents?

Mr. SULLIVAN. Yes, sir; \$25,000,000.

The CHAIRMAN. The suggestion has been made, Mr. Sullivan, that if we put a small tax on all admissions from 9 cents up and then lift the tax as the admissions go higher in price, then we would get \$60,000,000 from the amusement people, the motion-picture group, and that there was considerable unanimity of opinion in that industry that it could be done. Have you given any thought to that suggestion.

Mr. SULLIVAN. The only estimate I have, sir, was when it was at one time considered to reduce the exemption from 40 cents to 20 cents, and our estimate on the increased revenue, because of that exemption, was \$60,000,000. As I understand it, the suggestion you have just made would further reduce that another 10 cents. Now, I don't know how much that would increase the revenue, but I would expect it to be fairly substantially in excess of the \$60,000,000 you mention, because our figures indicate that by reducing it only to 20 cents, we would get an additional \$60,000,000. That, of course includes the \$25,000,000 that is in the estimate I just gave you, Senator Townsend.

Dr. O'DONNELL. The motion picture industry now has gross theater admissions of about \$1,000,000,000 a year. From the best information we can get that represents about three-fourths of all the admis-

sions, including admissions to baseball games, football games, prize fights, circuses, race tracks, and so on. I should very strongly suspect that if you lowered the exemption to 9 cents you would very nearly make all admissions subject to the tax, unless you made, as you did when you had a previous tax of this kind, a 10 cent exemption in the case of amusement parks and their special attractions. If I remember correctly, there was some sort of an exemption for children's admissions. Nevertheless with an exemption of only 9 cents and a tax of 1 cent on each 10 cents or fraction thereof above this exemption, I think that you would collect a tax on almost all of the admissions to amusements.

The CHAIRMAN. I wish you would look into that, please.

Senator TOWNSEND. What do you estimate that would be?

Dr. O'DONNELL. I estimate that we would collect about \$125,000,000, making some allowance for exempt admissions and considering that the effective rate of tax on taxable admissions is in excess of 10 percent. That estimate includes, of course, the present admission tax receipts of about \$19,000,000 and indicates an increase of some \$106,000,000.

Senator CONNALLY. Your assumption is on the basis of continuing the same tax down to 10 percent, but Senator Harrison's idea was to tax the lower ones a smaller rate, tax them 1 cent, say, from 10 cents to 20 cents, and 2 cents from 20 cents to 30, and then the regular 10 percent above that.

Mr. SULLIVAN. Could we have those rates, Senator Harrison, and we will give it to you?

Senator GEORGE. I have here, Mr. Sullivan, suggested rates of 1 cent on all admissions say up to 25 cents.

The CHAIRMAN. That is from 10 cents to 25?

Senator GEORGE. 2 cents from 26 cents to 49; and above 50 cents, 10 percent. They claim that that will produce about \$60,000,000, and I had figured on it somewhat, and there is a good deal of merit, maybe not in these specific levies, but in the thought of differentiating. I was advised that the Ways and Means Committee didn't go into that because they didn't affect the basic rate.

Mr. SULLIVAN. Did I understand that in one of those brackets you would reduce the rate that is contemplated in this bill?

Senator GEORGE. Yes; from 26 to 49 cents, admissions running from 26 to 49 cents would only pay a rate of 2 cents. That is less than we pay now.

Mr. SULLIVAN. I think for the Treasury, sir, that I would have to oppose that. I am afraid that we may be getting into an industry fight here. I am not sufficiently familiar with the theater business to know.

Senator GEORGE. I said that the rates possibly might need readjustment, but I was discouraged from presenting it on the theory that the Ways and Means Committee had built up the bill and that if we go into these rates and try to make those readjustments of course then you have got all kinds of industry questions involved, but I will be glad to leave these with you and you can study them out, because in January we will probably have it in hand any way.

Senator KING. I am told, Mr. Sullivan, that there are only about 146 theaters in the United States whose charges are 50 cents or above that, a very limited number.

Mr. SULLIVAN. One hundred and forty-six?

Senator KING. That is my recollection, I may be in error.

Mr. SULLIVAN. Frankly I don't know, but it sounds rather low.

Senator KING. I am told that in Kentucky they have the rates that were read by Senator George.

Senator GEORGE. Yes; those are the Kentucky rates.

Senator KING. And it works very satisfactorily there to all parties, and the revenue is very satisfactory and it meets the wishes of the people generally.

Senator GEORGE. It occurred to me that it would be best to defer consideration of this schedule until we are rewriting more or less the whole tax bill, in harmony with the present bill. I would be loathe to go into matters of that kind that may affect very vitally the industry, without some little opportunity for the industry to be heard on it. That is the theory that I would go on.

Senator KING. Well, if the industry approved a modification and the public generally, and the revenue to the Treasury was greater, then it would seem to me we could approach it with a good deal of sympathy.

Mr. SULLIVAN. I think we could. The rates of certain excise taxes are not increased at all by the bill, a list of which I gave to Senator Vandenberg yesterday morning.

Among these are the regulatory taxes—for example those on oleo-margarine, bituminous coal, narcotics, white phosphorous matches, and certain types of firearms. These taxes are imposed not for the purpose of raising revenue but to regulate certain businesses or discourage certain activities. Likewise, those internal revenue taxes have been excluded which are in effect import duties imposed for protection rather than for revenue—for example, the import excises on fish, animal, and vegetable oils, petroleum products, coal, lumber, and copper, and the processing tax on coconut oil. Similarly the bill does not affect the sugar tax since the rates of this tax are adjusted to an integrated program of agricultural benefits and quotas. The bill also makes no change in the taxes levied under the Social Security program since these taxes are imposed for a special purpose.

Senator VANDENBERG. Mr. Sullivan, on the first page where you have estimated the yearly additional revenue at \$1,004,000,000, that isn't for the next fiscal year, is it?

Mr. SULLIVAN. No, sir; the estimate for the fiscal year of 1941 is \$729,000,000. The reason that is less than the estimate for a full year thereafter is that we will only get two of the four income tax payments within that particular period.

Senator LA FOLLETTE. How much money will come into the Treasury by the first of January?

Mr. SULLIVAN. By the first of January?

Senator LA FOLLETTE. Yes.

Dr. O'DONNELL. If you will defer the question for just a minute, I think I can find that for you.

Senator KING. Do you mean from this date now?

Senator LA FOLLETTE. If we pass this bill, how much actual dollars will we get in?

Senator TOWNSEND. While you are looking that up, are there any practical difficulties involved in segregating the revenues provided for under this bill which are to be earmarked for the retirement of the defense obligations provided for in this bill?

Mr. SULLIVAN. It will involve a good deal of figuring, sir. You will notice that the increases that come from the permanent increase in surtax rates are not included in the amount that is to be earmarked. The reason for that is that we just can't figure it. We take the 10 percent supertax and earmark that. In the case of the increased tax on stock transfers, which was increased from 2, 3, and 5, to 3, 4, and 6, we have got to do a little guessing on that, I think.

Senator TOWNSEND. What do you think that would cost, have you an estimate of the cost?

Mr. SULLIVAN. I will get that for you, sir.

Senator VANDENBERG. Suppose you restored the tax on sugar that used to be collected a few years ago, how much more would we get?

Mr. SULLIVAN. The tax on sugar?

Senator VANDENBERG. Yes; I am talking about the sugar tariff.

Mr. SULLIVAN. We collected \$65,000,000, you are referring to the processing tax on sugar?

Senator VANDENBERG. I am talking about the reduction in the tariff on sugar.

Mr. SULLIVAN. I don't know about that, sir.

The CHAIRMAN. Are you through with your statement?

Mr. SULLIVAN. I am, sir.

Senator LA FOLLETTE. Can you answer my question on how many actual dollars will come into the Treasury by the first of January before we start revising the rates that are in this bill?

Mr. SULLIVAN. Yes; we are getting that information for you.

Dr. O'DONNELL. Senator La Follette I do have a monthly distribution of the increased income from this proposed legislation but I don't have it on a cumulative basis. I will have to add it up.

In July we expect an increased revenue of \$21,457,000; in August, \$59,647,000; September, \$34,591,000; October \$36,945,000; November, \$34,522,000; and December, \$32,564,000—making a total of \$219,726,000.

Senator VANDENBERG. About \$220,000,000?

Dr. O'DONNELL. Yes, sir.

The CHAIRMAN. Are there any further questions of Mr. Sullivan? (No response.)

The CHAIRMAN. Thank you, Mr. Sullivan.

We will now hear Mr. Fayette B. Dow. Mr. Dow represents the National Petroleum Association and other groups interested in petroleum and related products. I understand you want to be heard briefly, Mr. Dow?

Mr. Dow. Yes, sir.

STATEMENT OF FAYETTE B. DOW, APPEARING ON BEHALF OF THE AMERICAN PETROLEUM INDUSTRIES COMMITTEE, THE NATIONAL PETROLEUM ASSOCIATION, THE MID-CONTINENT OIL & GAS ASSOCIATION, THE WESTERN PETROLEUM REFINERS ASSOCIATION, THE PENNSYLVANIA GRADE CRUDE OIL ASSOCIATION, AND THE INDEPENDENT PETROLEUM ASSOCIATION OF AMERICA

Mr. Dow. Mr. Chairman, and gentlemen of the committee, my name is Fayette B. Dow. I represent the American Petroleum Industries Committee, and a group of petroleum-trade associations which

are named in my prepared statement. I ask leave to file, without reading it, a very brief statement with relation to this bill.

We do not oppose at this time any of the increases which are embodied in the bill. We do ask, however, that one change be made, and that is that a provision be inserted which will make it clear that none of the excise taxes here proposed shall be considered as fixed for the period of the 5-year term.

You will recall that the question was asked Secretary Morgenthau yesterday as to whether he regarded personally any of these taxes to be fixed taxes for the 5-year period, and he said that he did not. He said that he regarded the bill as an obligation on the part of the Federal Government to raise \$1,000,000,000-plus, with which to retire the special securities which are to be issued. We think that that question is not free from doubt and should be definitely covered in the bill when finally approved by the committee.

Senator KING. May I interrupt you? I think he stated, and I hope I am not misinterpreting his statement, that if persons bought these bonds under the assumption that certain of these excise taxes were earmarked to pay those bonds, there might be a moral obligation to make provision by setting aside in the Treasury Department sufficient to meet the obligation, but as I understood him, after all it was an obligation of the Government and it would be quite immaterial so far as the final results were concerned, whether they were earmarked or whether they were not, because the bonds which are issued would have the guaranty of the Government behind them.

Mr. Dow. I think that that is substantially what he said. This bill does require the Treasury to set aside as an especially earmarked fund, the return from certain of the taxes, namely in those in title II, and that includes the excise taxes which are here levied and under the terms of the bill for a 5-year period. Now, I think that it would be very simple to make it certain in the tax bill that Congress has not bound itself with respect to any of these excise taxes for that period.

Senator BARKLEY. Well, Congress can't bind any future Congress. Congress might come along next year and repeal all these taxes. What is the use of putting it in the law if we are levying taxes for 5 years, and we may not mean it?

Mr. Dow. Well, if it is perfectly clear and what is said before the committee would make it clear—

Senator CONNALLY (interposing). The law is going to be what is written on the books, and not what somebody says, and on the other hand these taxes are apt to be permanent. They talk of 5 years, but they are probably going to be for 25 years. There is nothing that would lead me to believe that we are going to take them off after 5 years, and we are probably going to put on more porous plaster after this one. I would rather strike out the 5 years and just put them on, and when we get ready to take them off, take them off.

Mr. Dow. Personally, I agree with that, but my point is this: We regard this bill as a temporary tax measure which is necessarily enacted without the opportunity to entirely review the whole tax structure, and we look forward within a reasonable time to a revision of the whole tax structure, and at that time we will want to come before this committee when, I think, numerous other commodities than those which are now taxed in this bill, will be taxed, and then to say that the taxes on these special commodities shall have a fair and equitable relation to all of the taxes which will then be levied.

Now, that may involve the reduction here and there of some of these taxes which are embodied in this bill.

Senator BARKLEY. We all anticipate that probably next January, certainly at the next session, we have got to consider the whole tax structure and Congress isn't bound to freeze these taxes for 5 years if in that general revision it should find it necessary to readjust them. I think that there might be some moral obligation that we shall not reduce the aggregate amount of money collected for the purpose of retiring these bonds that are to be issued, but when we get into the whole tax structure, I think Congress will be perfectly free without saying so in this law, to deal with the whole subject.

Mr. Dow. I am inclined to think that that is sound; I want to be sure that it is; there is some difference of opinion.

Senator LA FOLLETTE. Even if you could get such a statement written into the law, I don't think, in view of the past history of excise taxes, that you could get very much comfort from such a statement, because one of the evils of this type of taxation is that once it gets into the structure it doesn't come out.

Now, we have been extending these excise taxes at the tail end of sessions, when they expire, under a rush and hurry, ever since they have been put on, and while I can understand your desire in view of the fact that you do not now have an opportunity which I think you and everybody else should have, to have a thoroughgoing study, and attack made upon this whole tax problem, I do want to say that I don't think you could sleep any better nights if Congress wrote it in, because the history is that these taxes get on and stay, and that is the reason I am "agin 'em."

Mr. Dow. Well, I can share that view and I want to say, Senator, that this prepared statement very briefly sets forth the present tax burden which is assessed upon the highway users of the country.

Briefly now, there is collected by the States \$1,228,000,000 in gasoline taxes, and registration fees. Another \$328,000,000 is now collected under present rates by the Federal Government on gasoline and other petroleum products and on automotive equipment.

Then here is added, under this bill, another conservatively estimated \$126,000,000.

So you get a situation where, under present levies, State and Federal, you have \$1,558,000,000 already collected, and this additional amount gets you close to \$1,700,000,000.

Now, we say we are not here to oppose the taxation, but we do say that the levy is already a very substantial one, and that when you come to review the entire tax structure at the next session, we will be prepared then to come into the questions—to go into the question of whether it is proper to handpick a relatively few articles for very high taxes, or whether it may not be sounder to deal with the income taxes and the general commodity level in a broader way. That is substantially what I want to say.

The CHAIRMAN. We understand your position, substantially, and that statement will be incorporated in the record.

(The statement is as follows:)

STATEMENT OF FAYETTE B. DOW BEFORE THE FINANCE COMMITTEE OF THE UNITED STATES SENATE ON THE REVENUE ACT OF 1940

My name is Fayette B. Dow. I am appearing before this committee today in behalf of the American Petroleum Industries Committee, the National Petroleum Association, the Mid-Continent Oil & Gas Association, the Western Petroleum

Refiners Association, the Pennsylvania Grade Crude Oil Association, and the Independent Petroleum Association of America.

We are not here to make any statement in opposition to any of the taxes which have been proposed in H. R. 10039.

On the contrary, we recognize that the Federal taxes must be promptly and substantially increased. We believe that the American people understand the necessity for military preparedness and are ready to meet the tax obligations which such a program will necessarily impose.

There are, however, certain considerations which we think should be brought to the attention of your committee, and I am making this statement for that purpose.

First, The tax bill now under discussion is drawn in a new form and contains provisions which are new to our revenue laws in that they undertake to earmark certain tax receipts for a period of 5 years, to be set aside as a special fund, which is to be available only for the retirement of United States obligations designated as "national-defense series." Tax receipts to be so set aside are "the additional amount of taxes collected attributable to the increases of taxes made * * * in title II of this act" with certain exceptions. Title II designates certain taxes, including the excise taxes named in chapter 9A as supertaxes for 5 years. For example, H. R. 10039, commencing on page 17, line 23, provides as follows:

"SEC. 1650. SUPER-TAX FOR FIVE YEARS.

"In lieu of the rates of tax specified in such of the sections of this title as are set forth in the following table, the rates applicable with respect to the period after June 30, 1940, and before July 1, 1945, shall be the rates set forth under the heading 'Super-tax Rate'":

Then follow certain supertax rates, including the following:

Section	Description of tax	Old rate	Super-tax rate
3400 (1)	Tires	2½ cents	2½ cents.
3400 (2)	Tubes	4 cents	4½ cents.
3403 (a)	Automobile truck chassis, etc.	3 percent	3½ percent.
3403 (b)	Automobiles, etc.	3 percent	3½ percent.
3403 (c)	Parts	2 percent	2½ percent.
3412	Gasoline	1 cent	1½ cents.
3413	Lubricating oils	4 cents	4½ cents.
3460 (a), (1), (2), and (3)	Transportation of oil	4 percent	4½ percent.

The question arises as to whether the excise taxes so levied are fixed for a period of 5 years so that they cannot be reduced in the general revision of all of the Federal tax schedules which is contemplated in the near future.

At the hearing before the Senate Finance Committee on June 12, Secretary Morgenthau was asked the question whether he regarded these earmarked, or special funds, taxes to be fixed for a period of 5 years. His reply, in substance, was that he did not so regard them. He said that he regarded the tax bill as a commitment to raise \$1,000,000,000 plus per year, as earmarked or special funds, for a period of 5 years, but that the manner in which the special fund might be raised would be for Congress to determine, and redetermine, if it should so desire, within that period.

We think that this understanding upon the part of the Secretary of the Treasury should be clearly stated in the tax act which is now under discussion. If this is not done, and Government obligations of the national-defense series are issued under the authority of the act, a contention might be made that the taxes provided in the Revenue Act of 1940 could not be reduced, even though it should be found necessary to reconsider and revise the Federal tax laws in their entirety. The bill now under discussion proposes to levy increased excise taxes on certain commodities.

It might be considered wise by Congress, for illustration, to enact in a future revenue bill a general manufacturers' excise tax. If so, it would undoubtedly be desirable to reconsider the existing excise taxes, and those which it is now proposed to increase, and to place excise taxes on these commodities which would be properly and equitably related to a general excise tax on all manufactured articles. Certainly this Congress should not undertake to bind the action of a future Congress by enacting at this time a level of excise taxes which would be fixed, as a minimum, for a period of 5 years.

We, therefore, request that a clear statement should be added to H. R. 10039 to the effect that none of the excise taxes provided for shall be considered as fixed and unchangeable during the 5-year period.

This leads logically to the second phase of the subject which we think should be called to the committee's attention.

Second. Among the most essential commodities now subject to Federal excise taxation are gasoline and lubricating oils. It is important to note that the percentage of increase in the tax proposed in H. R. 10039 on gasoline is the largest percentage increase on any commodity subject to Federal excise taxation.

It will be of interest to note the percentage increases in taxes proposed on various commodities.

50-percent increase is proposed on gasoline.

37½-percent increase is proposed on brandy.

33¼-percent increase is proposed on distilled spirits, imported wines, cabarets, roof gardens, and insurance policies.

25-percent increase is proposed on transfer of bonds and on automobiles.

20-percent increase is proposed on distilled wines, sparkling wines and fortification of wines.

16¾-percent increase is proposed on other automobiles.

12½-percent increase is proposed on lubricating oils, transportation of oil by pipe line, and inner tubes.

11½-percent increase is proposed on electrical energy.

11-percent increase is proposed on tires.

10-percent increase is proposed on box seats, sales outside of box office, club dues, corporate securities, passage tickets, safe-deposit boxes, pistols and revolvers, firearms, wholesalers in liquor, retailers in liquor, brewers, wholesalers in malt liquors, retailers in malt liquors, rectifiers, stills, toilet preparations, radios, mechanical refrigerators, conveyances and playing cards.

The proposed increase in excise taxes on gasoline, lubricating oil, automobiles, etc., specifically referred to above, will provide conservatively \$126,000,000 in the fiscal year ended June 30, 1941.

These taxes will be added to the heavy burden now placed upon petroleum and automotive products.

State taxes on motor fuel and highway vehicles in the last 20 years have been tremendously increased.

In 1919 the car-owning public paid \$1,022,514 in State gasoline taxes and \$64,697,256 in registration fees. By 1939 State gasoline taxes alone yielded \$816,000,000 while State registration fees provided an additional \$412,494,000.

To this total of \$1,228,494,000 from State levies in 1939, must be added \$328,000,000 in Federal levies on petroleum products and automotive equipment under present tax rates.

To this State and Federal total of \$1,556,494,000 it is now proposed in H. R. 10039 to add \$126,000,000. The result will be a total State and Federal tax burden of \$1,682,494,000 borne by users of the highways.

This added revenue has been made bearable largely because the retail price of gasoline was reduced from 29.74 cents per gallon (excluding tax) in 1920 to 13.17 cents (excluding tax) in 1940.

Meantime, the simple average State and Federal gasoline-tax rate climbed to 5.44 cents per gallon and the proposed increase in the Federal levy will lift the average to nearly 6 cents, or a tax rate of 45 percent upon the retail price of an essential commodity used by almost every American family.

Lubricating oil, another absolute necessity, is now taxed at rates ranging from 25 percent to 100 percent of the wholesale price.

These taxes will be borne by the 30,000,000 motor-vehicle owners, most of whom use their cars largely in the business of making a livelihood, and who earn from \$25 to \$30 per week. Two out of three of them have never owned a new car. They are customers of the used-car lot, and they are the same people who will bear the brunt of the majority of other taxes which are levied in this bill.

Third. Whatever any critic may say of our deplorable lack of military preparedness, at the present time, there is one respect in which we are prepared.

We have the finest systems of improved roads in the world.

The war in Europe has shown the tremendous part played by the mobility and speed of tanks, power-drawn artillery and armored cars, motorcycles, and supply trucks. The trench warfare of two decades ago seems to be obsolete—modern warfare is a warfare of movement, and for movement good roads are indispensable.

At least it must be said that the billions of dollars which have been provided by the highway users in the last 20 years for road building and road repairs have not left it necessary for our armies to build roads over which to transport the mechanized equipment which the new taxes are intended to provide.

It follows that in considering present taxes and future taxes for military preparedness there must be credited to the highway users the contributions which they already have made to the national defense.

Nevertheless, this statement is not made in opposition to the proposed tax increases. The critical need for greater Federal revenues is apparent to all, and there is no disposition in the part of those for whom this statement is made to make objection to the imposition of higher taxes. Nor do we wish to overemphasize the fact that the Federal gasoline and lubricating-oil taxes originally imposed as "emergency" taxes in 1932, for the general revenues, were intended to expire in 1 year. The need for prompt action is also recognized, and there is no desire to ask for the delay which would be necessary in order to work out a more equitable basis of taxation. But it has seemed both fair and informative to point out the burden of special taxes which are now levied, for we understand that a complete revision of the whole range of Federal taxation may be expected in the near future. When that problem is taken up, the facts here briefly stated, and other facts equally pertinent, will be presented for the further and more deliberate consideration of this committee.

Respectfully submitted.

FAYETTE B. DOW.

JUNE 13, 1940.

Senator CONNALLY. I want to ask Mr. Berkshire a question along this line.

Mr. Berkshire, is there any reason why industrial alcohol shouldn't pay some tax? You have to regulate it and fiddle with it and spend a lot of money for that purpose and it doesn't bear any tax. Gasoline pays a tax; potable alcohol pays a tax. Why shouldn't this so-called industrial alcohol, out of which they make perfume and face lotions and all that sort of thing for beauty parlors, why shouldn't that pay some tax?

Mr. BERKSHIRE. That is an economic question.

Senator CONNALLY. Is there any administrative reason why they shouldn't?

Mr. BERKSHIRE. No.

Senator CONNALLY. There is no administrative reason?

Mr. BERKSHIRE. No.

Senator CONNALLY. You could collect it just as easily as you regulate it.

Mr. BERKSHIRE. Yes, sir.

Senator CONNALLY. Without any additional expense?

Mr. BERKSHIRE. Yes, sir.

Senator CONNALLY. How many gallons are consumed in the United States; do you know, annually?

Mr. BERKSHIRE. I can get that information for you exactly, and I will give it to you.

Senator CONNALLY. And suggest along with that, a rate.

Mr. BERKSHIRE. Yes.

(The following data was furnished by Mr. Berkshire:)

Ethyl alcohol¹ withdrawn for denaturation, and completely denatured alcohol and specially denatured alcohol produced, fiscal years 1937, 1938, 1939, and first ten months of fiscal year 1940

Fiscal year ended June 30	Ethyl alcohol withdrawn for denaturation ¹	Completely denatured alcohol produced	Specially denatured alcohol produced	Total produced
	<i>Proof gallons</i>		<i>Wine gallons</i>	
1937.....	181,034,322	22,118,378	80,084,281	102,202,659
1938.....	165,848,246	25,598,717	69,008,024	94,607,741
1939.....	177,330,888	17,170,433	83,581,077	100,740,510
First 10 months of 1940.....	189,026,471	14,057,002	92,960,930	107,017,932

¹ Includes rum and other spirits produced at distilleries for denaturation.

The CHAIRMAN. Thank you, Mr. Dow.

Mr. BERKSHIRE, let me divert just a moment to another subject and if possible get the committee to act on it at this time. Have you before you the so-called Buck bill, H. R. 9117, that has passed the House?

Mr. BERKSHIRE. Yes, sir.

The CHAIRMAN. I understand that it is recommended by the Treasury. It has got to be settled, I think, before this tax bill is acted on. Will you explain the bill, briefly.

Mr. BERKSHIRE. Yes, sir.

The CHAIRMAN. And the reasons for the Treasury supporting it.

Mr. BERKSHIRE. I might say that something like a year ago, representatives of the wine industry called on me with the idea of having a law passed eliminating tax on brandy used for purposes of fortification of wines.

That tax is now 10 cents a gallon. They wanted to eliminate that tax and move it over on the finished product, that is on the wine that this brandy is used in fortifying.

The tax, the 10-cent tax, if you transferred it over to the wine, amounted to something like 3½ cents a gallon on the finished wine.

We told them at that time that we didn't believe that we were interested in dealing in half cents and if they were interested in taking the brandy tax off and then increasing the sweet-wine tax to the extent of 5 cents a gallon, that the Treasury Department would approve their proposal.

Senator LA FOLLETTE. What advantage do they see in eliminating the tax on the brandy used for fortification, and putting it onto the wine itself?

Mr. BERKSHIRE. Well, Senator, it has been a troublesome thing to the industry and to the Bureau in administering it. At present, this tax is assessed, it is collectible in 18 months, and we find in the meantime the wine maker has disposed of the wine and the money too, and we look to the bonding company many times for this tax at the end of the 18-month period.

It has caused us trouble and it has caused some of the wine people to become financially involved, and it has generally disrupted the wine market. I think that is their interest.

Senator CONNALLY. How will this rectify it if you put it on the wine instead of the brandy?

Mr. BERKSHIRE. We at the present collect a wine tax on the wine as it moves out of the warehouse, but then we collect the 10 cents tax on the brandy 18 months later.

Senator CONNALLY. Why shouldn't you collect it all at the same time?

Mr. BERKSHIRE. That is what this does.

Senator CONNALLY. But you take the tax off the brandy?

Mr. BERKSHIRE. Yes; and add it on to the wine, and we will get that along with the wine tax which we are collecting now.

Senator CONNALLY. It won't be a loss of tax?

Mr. BERKSHIRE. We gain a cent and a half every gallon.

The CHAIRMAN. What do you estimate the gain?

Mr. BERKSHIRE. A cent and a half a gallon, I believe it will run—

The CHAIRMAN (interposing). About \$3,000,000?

Mr. BERKSHIRE. No; I think it is only \$1,000,000, or less than \$1,000,000; it is less than \$1,000,000 a year.

The CHAIRMAN. There is no division in the industry and there is no objection on the part of the Treasury?

Mr. BERKSHIRE. We think it is a good bill; that is right.

Senator CONNALLY. Does this tax bill increase the tax on wine, this tax bill?

Mr. BERKSHIRE. Yes, sir; and that will be an increase in addition to the increase proposed in the Buck bill.

I think that was Senator Harrison's idea in getting H. R. 9117 out of the way, changing the base rates on the wine before the supertax rates go on.

Senator CONNALLY. Does this affect apple juice and apple cider?

Mr. BERKSHIRE. It will affect only those manufacturers of apple wine who use brandy in fortifying that wine.

The CHAIRMAN. Without objection, the committee will report this bill favorably, and I will ask Senator George to make the report. It ought to be passed before this tax bill passes so that whatever taxes are added to it will appear in the pending tax bill.

Senator BARKLEY. May I ask Mr. Berkshire, while he is here on the stand, about the rectifiers tax? This bill increases the tax on straight whisky from \$2.25 a gallon to \$3 a gallon.

Mr. BERKSHIRE. Yes, sir.

Senator BARKLEY. It does not increase the tax on the rectified product which, as I understand it, is about one-fourth straight whisky and three-fourths fresh and possibly raw alcohol. And this 30-cent tax per gallon which is the law now was put in there to make an effort to adjust the difference between the cost of production plus the tax on straight whisky and the rectified whisky?

Mr. BERKSHIRE. That is my understanding.

Senator BARKLEY. And if you increase the tax on the straight whisky from \$2.25 to \$3, as I understand the Treasury recommended, and the alcohol tax unit of the Internal Revenue Bureau recommended that there be an increase in the tax on rectified, and that was contained in the House bill as written by the House committee—will you explain that to the committee so we can get it clearly, and what the facts are.

Mr. BERKSHIRE. Well, the Treasury Department thought that there should be a corresponding increase in the rectification tax which is now, as you know, 30 cents a proof gallon.

We feel that the increase is necessary, aside from the revenue-producing angle, in order to better equalize the production costs of the two commodities. If 30 cents was a proper equalizing tax at the time that it went on, on account of the increased cost in producing straight whisky, today, as against the time that the 30-cent tax went on, the 30-cent differential doesn't do the job, and we think that certainly 40 cents is a moderate increase.

Senator GUFFEY. How much did you recommend?

Mr. BERKSHIRE. 40 cents.

Senator GUFFEY. From 30 to 70?

Mr. BERKSHIRE. 30 to 40.

Senator BARKLEY. Is that really sufficient?

Mr. BERKSHIRE. Well, the best information that we were able to get, Senator, is that that does not yet equalize the cost of producing the two products.

Senator BARKLEY. They are competitive articles.

Mr. BERKSHIRE. They are competitive articles; yes, sir.

Senator BARKLEY. And where you levy a \$3 per gallon tax on straight whisky, that means that about \$3.90 a gallon is what it costs, including the cost of production, storage, aging, and so forth.

Mr. BERKSHIRE. Approximately.

Senator BARKLEY. Approximately \$3.90 a gallon before it gets out of the warehouse and starts into the trade?

Mr. BERKSHIRE. Yes, sir.

Senator BARKLEY. Whereas the cost of producing a gallon of alcohol is much less because they don't have to store it, they may pour it into good whisky tomorrow, after it is made today, and produce the rectified product.

Mr. BERKSHIRE. Yes.

Senator BARKLEY. And because of the lack of necessity for storage, aging, and other things, the cost of producing a gallon of that alcohol is about 16 cents.

Mr. BERKSHIRE. A proof gallon.

Senator BARKLEY. Yes. So that you have got three-quarters of the contents of a gallon of rectified whisky representing a 16-cents-a-gallon rate production cost, whereas the entire contents of a gallon of straight whisky is on the 90-cent basis.

Mr. BERKSHIRE. Yes, sir; 80 to 90.

Senator BARKLEY. So that this 40-cent rate which you recommend, which is only an increase of 10 cents a gallon, certainly is the minimum that would be required to adjust the difference in the cost of production.

Mr. BERKSHIRE. Well, if the figures that the Senator has mentioned are the correct ones, and I think they are substantially so, the 40 cents doesn't equalize; that is apparent.

Senator GUFFEY. Why not make it 50? It would improve the quality of the whisky.

The CHAIRMAN. I have had a memorandum handed to me, and I want to ask you about it. It reads as follows:

Any attempt to impose an increase in the rectification tax which is now 30 cents per proof gallon would constitute unwarranted discrimination. It is not generally understood that a rectifier or blender pays the same excise tax as any other member of the industry. To increase the rectification tax by 10 cents would mean that the liquor taxes are being increased 75 cents per gallon for some people and 85 cents per gallon for others, which is manifestly unfair. The rectification tax as it is at present, as it at present exists, is discriminatory. It contains another discrimination in that mixtures of 4-year old spirits produced below 190 proof, are exempt from the tax, while mixtures of 4-year old spirits produced above 190 proof, are not exempt. There could be no justification for increasing the discrimination by increasing the tax.

What is your reaction to that argument?

Mr. BERKSHIRE. I don't think that is sound, Senator.

The CHAIRMAN. You don't agree with it?

Mr. BERKSHIRE. No, sir. If 30 cents was right, and has been right all of the time, 40 cents or 50 cents would be right now if the corresponding costs of production have changed to that extent, if I make myself clear.

Senator BARKLEY. There seems to be some confusion as to the difference between "blended" and "rectified" whisky. If I understand it, blended whisky is where you take two straight whiskies and mix them, is that right?

Mr. BERKSHIRE. That is one form of blend, although the term "blended whisky" applies also to whiskies which are a blend of straight whisky and neutral spirits or alcohol.

Senator BARKLEY. What is the difference between a blender and a rectifier?

Mr. BERKSHIRE. None, it is used indiscriminately.

Senator GUFFEY. Don't you think the word "adulterated" would be better than the word "rectified"? [Laughter.]

The CHAIRMAN. It is nearly 12 o'clock, gentlemen. There are several witnesses who are present and are anxious to be heard. Is Mr. Garcia here?

Mr. GARCIA. Yes.

The CHAIRMAN. Mr. Garcia wants to make a brief statement, and I think file a statement, as a part of the record, is that right, Mr. Garcia?

Mr. GARCIA. Correct, sir.

STATEMENT OF ALVARO M. GARCIA, PRESIDENT, CIGAR MANUFACTURERS ASSOCIATION OF AMERICA, INC.

Mr. GARCIA. My name is Alvaro M. Garcia. I am a member of the firm of Garcia & Vega, of Tampa, Fla., and I am president of the Cigar Manufacturers Association of America.

Senator CONNALLY. Are you connected with the Perfecto Garcia people, or the other group?

Mr. GARCIA. Garcia & Vega.

Senator CONNALLY. Do you make the Garcia and Vega cigars?

Mr. GARCIA. That is correct.

Senator CONNALLY. A good cigar.

Mr. GARCIA. Thank you.

Senator CONNALLY. They are a little too high, but they are awfully good cigars.

Mr. GARCIA. Thank you, sir.

Our association of cigar manufacturers realize fully the need for revenue in order to finance the cost of national preparedness.

At the same time, the current trends and the problems of our cigar industry present a situation which we feel it is our duty to lay before this committee on behalf of the industry as a whole, and on this question of the proposed tax.

A comprehensive brief has already been submitted by our association, which the association has prepared through our general counsel, and I would ask permission to make it a part of the record.

The CHAIRMAN. All right, it may be made a part of the record.

(The statement is as follows:)

This memorandum is submitted with respect to the increase in cigar taxes proposed in section 2004 of H. R. 9960.

Our members realize fully the urgent need for increased revenue at this time in order to finance the cost of national preparedness. Undoubtedly it is the desire of those who are charged with the responsibility of levying new taxes to distribute the necessary burden equitably among those who must bear the expense of the program. Perhaps in the necessity for immediate action, however, some industries are being asked to bear a disproportionate share of this cost. This memorandum is intended to point out current trends and problems in the cigar industry which are such that the imposition of the percentage of increased tax proposed would result in irreparable injury. The heavy and inequitable burden which it

would cast upon the already declining cigar industry will be best understood when the following factors are considered:

- (1) The present status of the industry;
- (2) The internal-revenue taxes presently derived from cigars and the estimated increase in taxes under H. R. 9966;
- (3) The inability of the cigar industry to pass on such increase;
- (4) The inability of the cigar industry to absorb increase;
- (5) The contrast between the cigar and cigarette industries;
- (6) The effect of proposed increase on manufacturers, workers, and farmers.

(1) THE PRESENT STATUS OF THE INDUSTRY

For approximately 15 years, the American cigar manufacturing industry has been struggling to adjust itself to new trends in consumer demand. In 1920 the industry produced 8,000,000,000 cigars; but by 1937 only 5,300,000,000 were produced in spite of the country's considerable increase in population. By 1939 production, rising 200,000,000, was still less than 69 percent of that in 1920. In 1921, there were 4,078 factories producing \$5,000 worth of cigars or more and they employed 112,000 workers. In 1937 there were only 693 such factories and they employed approximately 56,000 workers, half as many as 16 years previously.

As striking as the decline in production is the shift in price level. Class C cigars (retailing at more than 8 cents to 15 cents) constituted almost 40 percent of total production in 1920. By 1937 they fell to 10.18 percent. In the same period class A cigars (5 cents or less) rose from 30 percent to about 88 percent of total production. Within class A equally significant changes are evident. From a survey made by the Cigar Manufacturers Association of America, of 1937 production of these cigars, it appears that not over 60 percent sold at 5 cents each and that the remainder sold for the most part at two for 5 cents.

The combination of these trends is clearly reflected in the value of the industry's product, which fell from \$371,000,000 in 1921 to \$312,000,000 in 1929 and to \$168,000,000 in 1937. Since the consumption in 1939 was only slightly in excess of that in 1937 and was marked by an increased shift to class A cigars, the value of last year's product was approximately the same.

In an effort to restore or at least to freeze a shrinking market, the industry has been compelled in recent years to offer a vastly improved product in the lowest price ranges. In the early years of the depression, manufacturers were forced to reduce many prominent brands from 10 to 5 cents and from 5 cents to 2 for 5 cents. It has nevertheless been necessary substantially to maintain the quality of the original product in order to meet competition from other smoking commodities.

While the price of the industry's product has sharply declined it has been burdened at the same time with a substantial increase in labor as well as raw material costs. Prior to the enactment of the Fair Labor Standards Act of 1938, 27 percent of the cigar factory workers earned less than the 30 cents per hour now required by that statute. In 1938 the Cigar Manufacturers' Association retained a firm of public accountants to conduct a survey of wages and hours in the cigar manufacturing industry in relation to the Fair Labor Standards Act. This survey revealed that even without any minimum wage 53 percent of cigar manufacturers were operating at a loss and that at the 30-cents-per-hour rate now demanded under the act, 65 percent of cigar manufacturers would operate at a loss.

As a result of the above-mentioned factors, class A cigars, although dominating in total production, have been produced upon a narrowing margin of profit which makes it exceedingly difficult for them to bear any further taxes at this time.

The production of cigars in revenue classifications B, C, D, and E has labored under similar burdens. As to these cigars, informed opinion in the industry has frequently been to the effect that unless they can regain some of the ground which they have lost to class A cigars or at least maintain their present share of total production, the entire cigar industry will necessarily continue to decline. This opinion is based upon the fact that smoking is a fashion habit and that approved smoking styles are set by those individuals in upper economic brackets. In the past, such persons have shown a preference for higher priced cigars and when more of such cigars are sold the smoking level of the entire industry will be lifted.

(2) THE INTERNAL REVENUE TAXES PRESENTLY DERIVED FROM CIGARS AND THE ESTIMATED INCREASE IN TAXES UNDER H. R. 9966

The table set forth below indicates as to each of the revenue classifications of cigars the 1939 consumption, internal revenue taxes paid, approximate percentage of total cigar taxes paid, and the estimated increase under H. R. 9966.

Class of cigars and present rate	Number of cigars consumed in 1939	1939 taxes	Approximate percent of total cigar taxes in 1939	Estimated increase in taxes under H. R. 9966
			<i>Percent</i>	
A (\$2 per M).....	4,042,744,000	\$9,887,550	77	\$1,847,026
B (\$3 per M).....	42,785,000	127,797	1	21,306
C (\$5 per M).....	483,916,000	2,420,186	18½	403,364
D (\$10.50 per M).....	35,030,000	377,333	3	62,889
E (\$13.50 per M).....	4,582,000	61,870	½	10,312
Total.....	5,500,966,000	12,874,742	100	2,145,790

While an increased revenue of \$2,145,790 would be obtained under the new rates if 1940 consumption equaled that of 1939, it is likely in view of the factors set forth in this memorandum that under those rates production would drop substantially and total revenue decrease accordingly.

As for the increase in rates under H. R. 9966, it is particularly significant to note that an unprecedentedly high rate would be imposed upon class D and E cigars. The maximum rates previously imposed, set during the World War under the Revenue Act of 1917, were respectively \$12 and \$15 per thousand, as compared with the \$12.25 and \$15.75 levies which would now be imposed. In view of the influence of these classes of cigars in raising the general level of the industry, as indicated above, these increases would be particularly unfortunate.

(3) INABILITY OF CIGAR INDUSTRY TO PASS ON INCREASE

The experience of the cigar industry has demonstrated repeatedly that it is impossible to pass on to cigar smokers in the form of an odd increased price any increase in manufacturing costs through taxes or otherwise. Cigars are traditionally sold in price multiples of 5 cents, and sales have fallen off sharply whenever it was attempted to charge an odd price, such as 6 cents or 7 cents.

Considerable testimony on this point has been given by the industry at hearings before the United States Department of Agriculture and in hearings at the time of the adoption of the N. R. A. code for the cigar industry. Answers obtained to a questionnaire circulated among retailers during the National Recovery Act period strikingly confirmed this fact. When it is borne in mind that about 90 percent of the industry's product today is in class A cigars, where the increase in price would have to be from 5 cents or 2 for 5 cents to 6 cents or to 3 cents each, respectively, it is evident that the increase in tax could not be passed on.

(4) INABILITY OF CIGAR INDUSTRY TO ABSORB INCREASE

As shown above a study of the cigar-manufacturing industry as recently as 1938 discloses that without any minimum wage requirements 53 percent of cigar manufacturers would operate at a loss and that under the 30-cent minimum wage requirements now effective under the Fair Labor Standards Act 65 percent of manufacturers are operating at a loss. It is clear that these manufacturers, who continue in business in the hope of eventually more favorable operations, would be altogether unable to pay further cigar taxes.

(5) CONTRAST BETWEEN CIGAR AND CIGARETTE INDUSTRIES

It cannot be too strongly emphasized that the cigarette and cigar industries fall into altogether different categories. This fact has been repeatedly recognized by State and Federal authorities. For instance, shortly after the enactment of the Fair Labor Standards Act of 1938 a conference was held with the Wage and Hour Administrator to determine whether, when industry committees were appointed in the tobacco field, a separate committee should be appointed for the cigar industry. It was agreed by the Administrator that this course would be pursued. Under the National Recovery Act, similarly, codes of fair competition were set up separately for the cigar industry.

While the cigar industry has steadily declined ever since 1921, the cigarette industry has increasingly prospered throughout the same period. The volume of cigar production attained its highest point in 1920. In the cigarette industry, on the other hand, there has been a constant increase in production which reached its peak in 1939.

It is well known, moreover, that the production of cigarettes is centered in the hands of a few very large manufacturers who have mechanized their methods to

a very considerable degree. The cigar industry on the other hand consists of hundreds of substantial manufacturers, small and large, many of whom employ hand cigar makers in whole or in part and only few of whom have mechanized their production to an extent comparable with that attained by the cigarette industry.

It is interesting to note in this connection that while the value of the cigar industry's product in 1937 (the last year for which United States Census of Manufactures figures are available) was approximately 17½ percent of the value of the cigarettes produced that year, nevertheless, the cigar industry employed 55,879 wage earners or approximately twice as many as the 26,149 wage earners employed in manufacturing cigarettes.

Although, as shown above, cigar manufacturers are unable to charge an odd price for their product, it is common knowledge that the cigarette industry labors under no such disability, and that packages of cigarettes have sold and do sell at such odd prices as 16 cents, 17 cents, and 18 cents. The cigarette industry will therefore have no difficulty in passing on the increased taxes imposed upon it by H. R. 9966, and for that reason its situation is in no way comparable with that of the cigar industry.

Apparently the 16½ percent increase in the cigarette tax was motivated by the thought that the tax per package of 20 cigarettes would thus be increased from 6 cents to 7 cents. The advantages of such increase from an administrative and mathematical standpoint are apparent. No such considerations apply, however, in the case of cigars, and as shown above, the industry cannot, like the cigarette industry, either absorb or pass on the increased tax. There would therefore appear to be no reason for imposing the same 16½ percent increase on cigars as on cigarettes solely because they are both tobacco products.

The cigar industry should be considered solely in the light of its own peculiar conditions and trends.

(6) EFFECT OF PROPOSED INCREASE

(a) *Manufacturers.*—As has been shown the proposed increase in cigar taxes will heavily burden the cigar manufacturers of America, more than half of whom are already operating at a loss. Many firms will be forced out of business and those who continue to produce cigars may be compelled against their will to lessen the quality of their product. Such action would necessarily operate to reduce the good will of the individual manufacturer and still further decrease the total demand for cigars.

(b) *Workers.*—Such effects upon the cigar industry would naturally be detrimental to the approximately 56,000 wage earners and the thousands of wholesale and retail employees who are dependent upon it. In addition those manufacturers who employ hand cigar makers in whole or in part, and who are already especially burdened by the requirements of the Wages and Hours Act, may be compelled either to go out of business or to resort to mechanization or increased mechanization of their plants so as to offset the increase in taxes by a reduction in labor costs. This course would necessarily result in the unemployment of a substantial number of cigar workers.

(c) *Farmers.*—The repercussions of the proposed tax increase upon the American farmer are evident. Cigar filler, binder, and wrapper tobacco is grown in the United States in Connecticut, Florida, Georgia, Indiana, Massachusetts, Minnesota, New York, Ohio, Pennsylvania, and Wisconsin. The decrease in the consumption of cigars which the proposed taxes are likely to cause would inevitably decrease demand for the tobacco grown by farmers in these States. In order to continue in business, moreover, many manufacturers would be compelled to seek economies by paying a lower price for tobacco used by them in cigars.

CONCLUSION

In view of the factors existing in the cigar industry which have been briefly summarized in this memorandum, it is respectfully requested that the proposed 16½ percent increase in cigar taxes contained in H. R. 9966 be revised so that the burden to be assumed will be fair and equitable.

Respectfully submitted.

CIGAR MANUFACTURERS ASSOCIATION OF AMERICA, INC.
By ALVARO M. GARCIA, *President.*

Mr. GARCIA. At this time, in order not to take up any more time than is absolutely necessary, I will attempt to emphasize the salient points of the contentions of the cigar manufacturers in their opposition to the proposed increase in tax on cigars.

1. The cigar industry is declining at an alarming rate. In 1929 the total volume was \$312,000,000. In 1937 that volume had decreased to \$168,000,000.

2. The tremendous shift in the price classification as indicated by the fact that at the present time over 88 percent of the total cigars produced are made for sale at 5 cents or less.

Of that 88 percent over 50 percent, and well over 50 percent, are sold at less than 5 cents. This leaves less than 12 percent of all the production today for retail at more than 5 cents.

This situation has been brought about by a combination of conditions but narrowed down it is a result of the efforts of the manufacturers to hold the cigar smoking market and to produce cigars to meet depressing conditions and the pocketbook of the country.

3. In revenue to our Government, the cigar industry paid in 1929 the amount of \$22,500,000; in 1937 the revenue was \$13,247,000. In 1938, the revenue was \$12,751,000.

Senator TOWNSEND. Was that on the same basis of taxation, as you go over these years?

Mr. GARCIA. Yes.

In 1939, the fiscal year, the tax was \$12,800,000.

The total proposed increase to the United States Government from the proposed tax amounts to about \$2,000,000.

From these figures it is very apparent that the law of diminishing returns has been operative in the cigar business for many years, and it is our contention that any further tax must reduce the Government's share of this partnership.

4. The proposed increased tax would promote more and more concentration of the cigar industry in the hands of fewer and fewer manufacturers. In 1929 there were reported 8,378 factories in the United States. In 1937 there were 4,853 factories.

The proposed increase in tax would, beyond question, be absorbed by a very few large units. Our industry, like other industries, has a few large units who, through conditions, are able to operate at a profit and they would absorb this tax. Certainly there are no more than 10 firms in these large units who would be able to absorb this tax. This would continue in force the standards of prices and sizes which competitors would be unable to compete against and still remain in business to support their factories.

With about 90 percent of all of the production selling at 5 cents or less, it can be readily understood how serious the absorption of a very small increase in taxation would be. Smaller units in a great preponderance would be forced to close. This is particularly intensified in the manufacturers who still employ hand work.

5. Our cigar industry should not be considered with the cigarette industry. A cigarette tax may be passed on in an industry that is not declining; while cigar volume is only about 17½ percent of the total cigarette volume, as the cigar industry employs 55,000 in its factories as against 26,000 in the cigarette factories.

6. From a survey which our association made through certified accountants, we estimate that the profits in the entire industry for the year 1937 do not exceed \$5,500,000. That \$5,500,000 can be well estimated to have remained in the hands of—or 80 percent of those profits have remained in the hands of six or seven firms.

The internal revenue tax—allow me to repeat—for that period, amounted to \$13,247,000.

7. Your bill under discussion has eliminated from increased tax, chewing tobacco, due to the declining consumption. The eliminated proposed revenue is about, I am advised, \$1,500,000 as against \$2,000,000 proposed on cigars.

In the opinion of our association, representing about 80 percent of the production of this country, this bill, the proposed tax, rather, would not accomplish its purpose. It will have no other effect than to hurt the industry, the farmers and the workers, and concentrate the industry more and more into the hands of a few, without any benefit to the Government.

Senator CLARK. Mr. Garcia, I noticed that this bill has a tax on manufacturers' floor stocks, but not on retail floor stocks. Do you know any reason why that distinction should be made?

Mr. GARCIA. As my personal opinion, I would imagine—

Senator CLARK (interposing). You are familiar with the trade, that is the reason that I ask you. I understand that that is not particularly within the line of your testimony, but isn't it a fact that the imposition of manufacturers floor tax and the relief of retailers from a tax on floor stocks will have the effect of greatly enhancing such retailers as the big chain stores, at the expense of the smaller retailers?

Mr. GARCIA. That would probably be so.

Senator CLARK. In other words, they can lay in a bigger stock before the act goes into effect?

Mr. GARCIA. That would probably be so.

The CHAIRMAN. All right, Mr. Garcia, thank you very much.

The committee will recess until 2 o'clock and will meet in the District of Columbia committee room in the Capitol.

(Recess at 12 o'clock noon).

AFTERNOON SESSION

(The hearing was resumed at 2 p. m.).

The CHAIRMAN. The committee will be in order.

Gentlemen, for your information I have received a letter from Mr. Wesley A. Sturges, executive director of the Distilled Spirits Institute, Inc., addressed to Chairman Doughton of the House Ways and Means Committee and myself, [reading] as follows:

The members of the Distilled Spirits Institute have directed me to inform you that they will make no objection to the increase of taxes on distilled spirits and brandy contained in H. R. 9966 which is designed to aid in financing national preparedness.

The members of the Institute hope that the proposed increases in the rate of the Federal tax on distilled spirits from \$2.25 per gallon to \$3 per gallon and on brandy from \$2 per gallon to \$2.75 per gallon will contribute their full share of the additional yearly revenue of \$85,000,000 which the Government seeks to realize from alcoholic beverages.

• We respectfully urge, however, that these increases in the Federal rate of tax involve certain hazards of which the Congress should take cognizance.

Most of the States superimpose a system of taxation like that of the Federal Government. There is the ever-present disposition to increase the rates in the

States. It is the consensus of judgment of the members of the Distilled Spirits Institute that the proposed increases in the Federal rates will bring the combined State and Federal levies to such a point that any further increases would put into operation the law of diminishing returns and impoverish both Federal and State revenues to be derived from the alcoholic beverage industry. As is well known, these revenues have exceeded \$5,000,000,000 since repeal.

We further ask that the Congress shall not be unmindful of the ever-threatening competitor of the legal industry, namely, the bootlegger. To the extent that our taxes are increased, the margin of profit for the bootlegger is made more attractive. The granting of additional funds for law enforcement should be given consideration, we believe, to insure the public revenue.

That concludes Mr. Sturges' letter.

The CHAIRMAN. Is Mr. Lanier present?

Mr. LANIER. Yes; I am here.

The CHAIRMAN. You are from Greenville, N. C., and interested in tobacco?

Mr. LANIER. Yes, sir.

Senator BAILEY. Mr. Lanier, Mr. Chairman, is a farmer and a lawyer and he was formerly connected with the Department of Agriculture here at Washington as head of the tobacco division, and knows a great deal about the whole tobacco business, and he comes from Greenville which is in the very heart of the tobacco section of our State.

The CHAIRMAN. All right, Mr. Lanier, make your argument as brief as you can.

STATEMENT OF J. C. LANIER, GREENVILLE, N. C.

Mr. LANIER. Mr. Chairman, as the Senator from North Carolina has said, my name is J. C. Lanier. I live in the little country town of Greenville, N. C., in the county that produces more tobacco than any county in the world.

I am a tobacco producer, I am also a lawyer, but for the most part my work is now producing flue-cured tobacco.

I was tobacco expert in the triple A for a year, 1933 and 1934. I might say that I am now a rising State senator from Pitt County. I say that to justify the statement that I think I speak for the tobacco farmers of my county and my section.

I am not up here, Mr. Chairman, to oppose the taxes generally for defense. I am in favor of adequate defense as far as this Nation can possibly afford. I will say that I was in the last war as a second lieutenant in a line infantry regiment, a Regular Army outfit, and I know what the cost of unpreparedness is. I know the lives that we lost because we were not prepared, and I want it understood that I am 100 percent in favor of the efforts being made now to prepare this country for what may come.

We tobacco farmers are not opposed to taxes. What I am here to try to show you gentlemen is the inequity of adding at this time to the burden of the tobacco growers. We are the first casualties of this war, the first American casualties.

Speaking of flue-cured tobacco and other types, Kentucky dark, it is an export crop. Two-thirds of flue-cured tobacco is exported and a great part of other types of tobacco that I won't go into.

We have lost our markets. We have lost, from 350,000,000 pounds of an export outlet, down to about 70,000,000 pounds.

Senator CLARK. What is that figure again?

Mr. LANIER. 350,000,000 that was exported to countries that are now at war, and we now have only about 70,000,000 pounds.

Last year the Government had to go down and buy approximately 200,000,000 pounds of flue-cured tobacco because we had no market; and this year, unless the Government does the same thing, we will have no market again.

My point is that our consumption has been most materially restricted.

Senator CLARK. You won't have any market as long as the British-Turkish agreement remains in effect?

Mr. LANIER. Plus Denmark, Sweden, Norway—all of those countries were good customers of ours and they are all gone now. The only hope we have is an increased consumption in the Americas, and that means principally in this country of ours.

Now, this tax, as levied under this proposed bill, will further restrict the consumption of our crop instead of giving us help. It will absolutely curtail the only chance we have got to recoup in any measure the markets that we have lost on account of the war.

I would not say that except for the facts, in regard to this tax, that our tobacco is already tremendously taxed. For every \$200, at 20 cents a pound, that I get out of an acre of tobacco, 1,000 pounds, the Government gets nearly \$1,000 already.

Senator KING. How much?

Mr. LANIER. Nearly \$1,000 off of every acre of my tobacco—\$1.13 a pound for what goes into cigarettes, and that is what we principally raise.

We are already tremendously taxed. I understand from the figures that tobacco taxes last year, the fiscal year, yielded around \$600,000,000 to the Government. No other farm commodity is taxed except maybe the corn that goes into corn liquor. But we have already carried this full wartime tax on tobacco that never has been reduced. In fact, it was increased in 1919 to where now we carry this burden of \$1.13 a pound on tobacco used in cigarettes, and it is not fair to us.

Senator CONNALLY. Let me ask you this: What does the farmer ordinarily get per pound for that same tobacco?

Mr. LANIER. Over a 5-year period, the last 5 years, from 20 to 22 cents a pound.

Senator CONNALLY. And the Government gets \$1.13 in tax?

Mr. LANIER. Yes, sir; under the existing set-up now. And I say it isn't fair to compare this country, its rate of tobacco taxes, with other countries like England, because England has no tobacco farmers to take care of, and it is analogous to say that we, taxing Scotch whisky, is the same as England taxing our tobacco because we don't produce any Scotch whisky and England, except in a few colonies, does not produce any of our tobacco.

We are faced down our way and in Kentucky and Virginia and South Carolina, and Georgia, and Florida, and all of these States, with a desperate situation under this present set-up.

And now, under this bill, to add an additional tax of 16½ percent on cigarettes, and under an item that will increase the tax on the common grades of tobacco, which are our export types and which do not have a market in this country, will amount to in some cases over 50 percent of the present tax on that tobacco.

Now, we farmers have to sell all of it to get the gross amount of dollars per acre to try to make a profit, and if we can't sell this low-grade tobacco, then of course we lose that much.

Under this paragraph there about cigarette papers, that will add to the pound tax on that kind of tobacco from 18 cents up to 21 cents under the tax, and then taxing every book of cigarette papers seven-twelfths of a cent will add from 5 to 8 cents a pound to the cost of that tobacco to the man who uses it.

Senator KING. That is only for the purpose of helping the man who makes these tubes?

Mr. LANIER. Yes; I have never seen one of those tubes, I don't know what they are.

Senator KING. I have seen them, and of course that is the disadvantage of it as I understand to those who produce tobacco—

Mr. LANIER. Yes, sir.

If this tax on papers goes on, the manufacturers will cut just so much tobacco out of the can of tobacco if they have to pay this seven-twelfths of a cent on every leaflet that goes with an ounce of tobacco, because it is sold usually in an ounce package. They will just sell a smaller package because no consumer is going to use or pay for a booklet of cigarette papers that has been given to him over all of these years.

That was done to increase the use of tobacco and as we sell less, the farmers have a less market for their crop.

To me—and I have studied this tobacco thing for years—the answer to our problem has never been a restriction of production. That is like giving a man a shot of morphine. The only answer, as I see it, is a larger market, an increased consumption, and that is what we are trying to do in this country, and in the other Americas, South America, and all over the world.

This tax bill will hit exactly what we are trying to do, it will further restrict our markets and will be the final straw on our back.

I certainly hope that this committee, in looking at it in all fairness with respect to other crops, with respect to other methods or means of taxation, will consider the fact that we, the tobacco growers, are already bearing a very high and, as I think, a disproportionate part of the taxes that are already being raised.

I am not a tax expert, but take chewing gum, soft drinks, and to be ridiculous, straw hats, or anything—but we are carrying our burden now, we are carrying a full wartime burden and we have already been cut down because of this war 50 percent in the possible outlets that we can get for our crop, and we would hope that this committee will see that and will at least not further add to the burdens and put a number of us in bankruptcy and on relief.

I thank you.

Senator BAILEY. Mr. Chairman, before Mr. Lanier takes his seat I would like him to disclose to the committee how extensive this matter affects the people of North Carolina.

There are fully 70 counties in our State out of the 100 counties in which tobacco is produced, is that not correct?

Mr. LANIER. Yes, sir.

Senator BAILEY. Do you know how many tobacco farmers there are in the State?

Mr. LANIER. Approximately around 100,000.

Senator BAILEY. And that means from 400,000 to 500,000 in the primary activities?

Mr. LANIER. Yes, sir; that depend primarily upon tobacco as a means of living. We have gone away from the cotton.

Senator BAILEY. The income of the farmers in North Carolina from tobacco is equal to the income from all other sources put together, is it not?

Mr. LANIER. I would say so.

Senator BAILEY. The total income is about \$230,000,000 and the income from tobacco has been from \$100,000,000 to \$120,000,000.

Mr. LANIER. Yes, sir.

Senator BAILEY. Now, we have lost our foreign market and if you add this new burden to that prostration, what will be the effect upon the 100,000 farmers of North Carolina and upon that whole state as a commonwealth? I would like you to disclose that.

Mr. LANIER. Senator, back in 1932, when tobacco had dropped to a 12-cent level, with a larger production we were all bankrupt. I want to say that we have a greater stake to me in the amount of tobacco that we sell than we have in any pound price that we get. We have got to have sufficient production to keep these people working. It is not at all safe or sound to just say that we get 30 cents a pound for what tobacco we raise, if we only have a very little quantity of tobacco, because the less tobacco we produced the more people that will be out of work down our way, not talking from my standpoint now, but from the standpoint of the tenant farmers, if you will.

Senator BAILEY. We do produce from 500,000,000 to 800,000,000 pounds a year in North Carolina, do we not?

Mr. LANIER. No, sir; that is the total bright tobacco.

Senator BAILEY. What is the North Carolina production?

Mr. LANIER. It averages around 400 to 450 million pounds per year.

Senator BAILEY. Now, disclose the facts also as to South Carolina and Georgia, Alabama, Florida, Tennessee, Kentucky, and Virginia.

Mr. LANIER. South Carolina raised around 80,000,000 pounds of flue-cured tobacco; Georgia raised between 80 and 100 million pounds—these are approximate figures; Virginia about 75,000,000 pounds; and Florida from 10 to 15 million. Kentucky, the burley crop, which includes Kentucky and Tennessee, with some tobacco in the adjacent States, Indiana and Ohio, but not much—was in round figures from 400,000,000 to 450,000,000 pounds of burley tobacco.

Senator BAILEY. In addition, North Carolina produces some burley?

Mr. LANIER. In addition, North Carolina produces some burley.

Senator BAILEY. In about 19 counties in the mountain section.

Mr. LANIER. Yes, and I might say it affects the burley people equally, although they do not export their tobacco, because flue-cured tobacco and burley tobacco are directly competitive, and every time we sell a pound of tobacco, which burley formerly sold, it displaces that much burley tobacco. If one is lower, they use more of that, and less of the other in the mixture.

Senator BAILEY. One more point. The Federal Government has imposed upon our farmers a curtailment program under the allotment system. What will be the effect on the average farmer who has an allotment of say from 2 to 4 acres, if his price goes all to pieces under the impact of this loss of market, plus this new tax?

Mr. LANIER. Senator, it can be proven mathematically, by figures, that under this restrictive acreage that you speak of, a 4-acre tobacco farmer at any price under 15 cents cannot possibly make a living.

Senator BAILEY. Well, the restricted acreage was put on with the assurance that we would get 20 cents, isn't that right?

Mr. LANIER. I do not recall that assurance.

Senator BAILEY. Well, it was a general assurance, nobody gave a guaranty.

Mr. LANIER. A parity price; yes.

Senator BAILEY. Now, if they don't get that, you have destroyed your whole program, but in destroying it, you have destroyed those farmers?

Mr. LANIER. That is right.

Senator BAILEY. If you destroy 100,000 farmers of North Carolina, you come very near destroying that Commonwealth for the time being, do you not?

Mr. LANIER. That is right.

Senator BAILEY. Now, Mr. Chairman, we got through the depression and called on the Government for less than practically any State in the Union, less per capita, but if this thing goes on we are going to call on this Government for a great deal more money than anybody will estimate that this tax will raise. That is the situation. You are not going to get any money out of this to buy any arms or pay any debts.

Senator GEORGE. Did the Government loan any money on flue-cured tobacco last year?

Mr. LANIER. Yes.

Senator GEORGE. What was the loan?

Mr. LANIER. The Government entered into an arrangement with the Imperial Tobacco Co. which is strictly an exporting concern, and some independents—some independent leaf-tobacco dealers—under the terms of which the Commodity Credit Corporation furnished the money for these companies to buy approximately 200,000,000 pounds of this tobacco under an option that they may take this tobacco at that option at any time before July 1941, at the price at which it was bought; but if they do not exercise the option, then the tobacco belongs to the Commodity Credit Corporation.

Senator BAILEY. That tobacco is still in this country.

Mr. LANIER. As the Senator said this morning, out of between 180,000,000 pounds and 200,000,000 pounds bought under that arrangement, less than 1,000,000 pounds of it has gone abroad; the rest of it is still in this country to overhang the market until it is disposed of in some way or other.

Senator GEORGE. With a new crop coming on in August and September.

Mr. LANIER. The new crop, yes; the estimate is now around 700,000,000. The domestic buyers will not take in excess of 300,000,000, which leaves 400,000,000 more pounds, with no buyers except speculators hoping to sell it abroad at some time.

Senator GEORGE. May I add here, Mr. Chairman, that there are some 30 counties in Georgia that raise tobacco, produce a great deal of tobacco; in round figures, 90,000,000 to 100,000,000 under the allotment, and, of course, in Georgia also, as in Carolina, we have substantially as bad a situation so far as the foreign market for cotton is concerned, and many of our tobacco farmers are also cotton pro-

ducers, and the only hope that we have for a market for cotton is substantially the loan that is put upon cotton this fall by the Government.

Of course, that is no tax—there is no tax on cotton, but nevertheless they happen to be in the same boat. The foreign market for these two main crops is simply out of the picture for the time being.

Senator KING. Do you know how much the Government has advanced by way of loans to the tobacco farmers, and to the exporters?

Mr. LANIER. They haven't advanced any to the farmers in the flue-cured area at all. They advanced approximately \$40,000,000 to these companies to buy this tobacco with last year.

Senator BAILEY. I think what the Senator has in mind is the Federal land bank operations.

Mr. LANIER. I don't know what they have loaned on the crop.

Senator KING. What I had in mind was if your industry is practically destroyed, the result to the Federal Government would be what? How much would the Federal Government be compelled to pay to meet the obligations of farmers and others who have borrowed from the Government upon their crops, those that were in esse and those that were in futurum?

Mr. LANIER. I want to say that I operate four farms and they have all got mortgages on them.

Senator JOHNSON. How much taxes were paid on this 180,000,000 pounds of tobacco that the Government purchased?

Mr. LANIER. There were no taxes paid on that, Senator.

Senator JOHNSON. No taxes on that at all?

Mr. LANIER. No; the tax is as it goes into manufacture.

Senator JOHNSON. That is what I thought.

Mr. LANIER. This is merely stored now in warehouses subject to the option of these exporting concerns.

Senator JOHNSON. And no taxes will be paid on it if it is finally exported?

Mr. LANIER. None whatever.

The CHAIRMAN. There has been some question raised by some Congressmen in the Ways and Means Committee as to a differential in the tax on cigarettes. Does that affect the farmers at all?

Mr. LANIER. I do not think that—in other words, I would be against any change in that set-up. I think it has not hurt the farmers the way it is now.

Senator KING. It would hurt the farmers if some plan were adopted which would restrict the use of cigarette papers or tubes?

Mr. LANIER. Yes, sir.

Senator KING. So that anything that would restrict or utilize these tubes and restrict the use of the paper would, of course, diminish the quantity of tobacco consumed and therefore diminish the quantity of tobacco which is purchased from the farmers and the repercussion would be that the farmer after all would have to pay?

Mr. LANIER. Yes; and another thing, people don't usually know about this, but I think you gentlemen should know this. Approximately a half of all the tobacco that is put in a cigarette is wasted. Now, if you put that in a pipe, it is all smoked up, but where you roll a cigarette or where you buy one of these cigarettes, one-third, I would say, of the tobacco goes into the cuspidors and the ashtrays.

So if you drive these people away from rolling their own cigarettes because they have got to buy the paper, and let them buy a corn cob

pipe for a nickel, you have right there destroyed a market for our tobacco of considerable quantity.

Senator CLARK. You mean because you don't waste so much tobacco in filling a pipe as you do in rolling a cigarette.

Mr. LANIER. That is right.

The CHAIRMAN. You don't think you favor a differential in the cigarette?

Mr. LANIER. No, sir.

The CHAIRMAN. As to the length of the cigarette, and so on?

Mr. LANIER. No, sir.

The CHAIRMAN. And the price?

Mr. LANIER. No, sir.

The CHAIRMAN. Thank you very much, Mr. Lanier.

Senator KING. I wonder if Senator Bailey had any further questions to ask this very intelligent witness?

Senator BAILEY. No; I think not. If necessary, I will talk to the committee. If the differential matter comes up, I would like to make a showing, but I am hoping that that will not be presented.

The CHAIRMAN. Is Mr. Jones in the audience?

Mr. JONES. Yes.

The CHAIRMAN. We will hear you briefly, Mr. Jones.

Mr. Jones is representing the National Association of Retail Druggists.

STATEMENT OF ROWLAND JONES, JR., WASHINGTON, D. C., REPRESENTING THE NATIONAL ASSOCIATION OF RETAIL DRUGGISTS

Mr. JONES. Mr. Chairman, I could probably conserve the time of the committee if I were permitted to read a very short prepared statement.

The CHAIRMAN. Go ahead.

Mr. JONES. My name is Rowland Jones, Jr. I am the Washington representative of the National Association of Retail Druggists, an organization of independent retail druggists of some 27,000 members.

Mr. Chairman and gentlemen of the committee, it is difficult in the extreme in this emergency to appear before you with any criticism of the pending tax measure, realizing its extreme importance at this time; but I would be remiss in my duty if I did not bring to the attention of this committee one situation which is of the utmost gravity to my people.

The retail druggists of the Nation stand ready as always to bear their fair share of the inevitable tax burden that faces every citizen.

Standing alone, I think it is safe to say that no Member of the Congress would seriously propose, in any emergency, an increase in the excise tax upon a chemical raw material, which is the most important component used in the preparation of drug and medicinal products, but in effect that is exactly what will happen unless a change is made in the pending bill.

Section 213 of the pending measure increases the excise tax on distilled spirits generally from \$2.25 to \$3 per proof gallon. This increase would bring the tax on pure ethyl alcohol used for nonbeverage medicinal purposes to approximately \$6 per wine gallon, a tax which is

seven or eight times the cost of the alcohol itself. We have contended for several years before the Congress and before Treasury officials, that it is inequitable to fail to recognize the need for the establishment of a differential for tax purposes between distilled spirits for beverage use and pure ethyl alcohol for nonbeverage medicinal purposes.

A basis for such a differential is found in section 3105 of the Internal Revenue Code, which provides that the Commissioner of Internal Revenue is directed—

from time to time to issue regulations * * * which may be necessary, advisable, or proper to secure the revenue, to prevent diversion of the alcohol to illegal uses, and to place the nonbeverage alcohol industry and other industries using alcohol as a chemical raw material or for other lawful purposes upon the highest possible plane of scientific and commercial efficiency consistent with the interests of the Government, and which shall insure ample supplies of such alcohol and promote its use in scientific research and the development of fuels, dyes, and other lawful products.

That is the language of the statute that is in the Internal Revenue Code.

In other words, some years ago the Congress recognized that ethyl alcohol for nonbeverage purposes was in a class apart from purely beverage alcohol. It is our thought that it is not the intention of the Congress to seek to derive additional revenue from drugs and medicines. Many of them are from necessity expensive and a large quantity of them, of course, go to relief organizations in the various States.

As I have said before, the 27,000 members of this association are ready and willing to contribute their full share to the increased revenue needs involved in our vitally necessary national defense, but they feel strongly that medicinal products should not be utilized as a source of increased revenue when all of the equities of the situation are considered.

While I realize the necessity for haste in the drafting and passage of the present emergency tax bill, I feel that I must bring to the attention of the committee the inequities involved in subjecting the chemical raw material ethyl alcohol used in nonbeverage, bona fide medicinal products to the same heavy taxes imposed upon distilled spirits for beverage use. I think that all will agree that the fundamental basis for the heavy taxes on distilled spirits for beverage use is the unquestioned luxury classification of such products. There can be no question that, standing alone, this Government would consider even for a moment the assessment of these heavy taxes on this most important general constituent of products that are essential in the prevention, alleviation, and cure of disease. The high cost of medical care is an acute problem to which the Federal Government has already given a great deal of study and in which it has had the cooperation of the professional groups involved.

I have pointed out the fact that during the last World War, in the emergency created thereby, the tax on distilled spirits for beverage purposes reached the high figure of \$6.40 per proof-gallon, while the same tax on pure ethyl alcohol for nonbeverage medicinal purposes was allowed to remain at \$2.20 per proof-gallon. Even at these latter figures and considering the emergency at that time, this tax, amounting to almost double the figure per wine-gallon, was an extremely heavy one in the light of the use of the alcohol involved. By this action during the first World War the Federal Government established

a precedent for the setting up of a differential in the tax between distilled spirits for beverage and for nonbeverage medicinal purposes. If such a differential was sound at that time, it would seem to be sound today, and the arguments in favor of it are even stronger in the light of the large number of our citizens who are dependent upon relief expenditures and relief agencies.

The only argument that we have ever heard advanced in opposition to such a differential is that it would involve additional administrative problems for the Treasury.

It is a fact that the Treasury has had complete and rather extended experience with the permit system for nonbeverage medicinal alcohol and at this time the permit system is in existence for tax-free alcohol for use by hospitals and research institutions. During the prohibition era, the retail druggists had the privilege of withdrawing alcohol for nonbeverage uses on such a permit system.

As we have indicated to the Treasury, the members of this association are ready to accept such regulations as the Treasury would feel would protect the revenue of the Government by preventing the diversion of the lower taxed alcohol into beverage channels. Based on the experience of the past, we are certain that if such a differential is set up under such a permit system the diversion of such lower taxed alcohol into illegal uses would be infinitesimal for all practical purposes.

Senator KING. Were there any evasions so far as you discovered under the old law?

Mr. JONES. Very very few. Our record in regard to alcohol compares with our record in the handling of narcotics, of which we have the exclusive handling.

The total of the pure ethyl alcohol that was withdrawn tax paid in 1939 amounted to only some four and a half million gallons. Not all of this alcohol by any means went into medicinal uses, but it is impossible to break down the available statistics to determine the amount of alcohol that such a differential would involve. It is my opinion, however, in the light of experience, that the total would not be in excess of 1,000,000 gallons.

Might I say at that point that the retail druggist was allowed to withdraw 60 gallons of alcohol a year. Very few of them even approached the withdrawal of that figure.

I hope that this committee will see fit to eliminate nonbeverage medicinal alcohol as a source of increased excise tax revenue, at least as long as other sources remain available. We submit that the retail druggist is one of the Government's best tax collectors. We hope that the Congress will not insist that he collect additional taxes from those whom he serves in the interest of the public health.

Senator KING. Is there an increasing demand for the nonbeverage alcohol? I assume there would be with the increase in population.

Mr. JONES. Yes; I think prescriptions, for instance, in this country are increasing; 250,000,000 were filled last year as close as we can figure from a survey that has been made.

The CHAIRMAN. Thank you very much.

Is Dr. Kelly here now?

Dr. KELLY. Yes.

The CHAIRMAN. All right, we will hear you briefly.

Dr. Kelly represents the American Pharmaceutical Association.

STATEMENT OF DR. E. F. KELLY, REPRESENTING THE AMERICAN PHARMACEUTICAL ASSOCIATION, WASHINGTON, D. C.

Dr. KELLY. I am representing, Mr. Chairman, the American Pharmaceutical Association.

The CHAIRMAN. Is your statement relating to the same matter we have just heard?

Dr. KELLY. Yes, sir; and I was just going to say, Mr. Chairman, that to save your time, I have gone over Mr. Jones' statement, and I want to record our association as being in accord with his statement.

Senator KING. Do you have any written statement prepared?

Dr. KELLY. No; but if I find it necessary to do so, I would like the privilege of submitting one later. I can do that right away.

Senator KING. Could you submit it by tomorrow?

Dr. KELLY. Yes, sir.

Senator KING. I suggest that if he submits it by tomorrow morning that it go into the record.

The CHAIRMAN. Yes; it will be incorporated in the record, if it is submitted tomorrow. I understand you are in accord with the statement submitted by Mr. Jones?

Dr. KELLY. Yes; but I haven't talked over this matter fully with Mr. Jones, as fully as I would like to, and if it is necessary to submit a statement, I would like the privilege of doing so tomorrow.

The CHAIRMAN. You may have that privilege.

Is Mr. Kolodny in the room?

Mr. KOLODNY. Yes.

STATEMENT OF JOSEPH KOLODNY, EXECUTIVE SECRETARY, NATIONAL ASSOCIATION OF TOBACCO DISTRIBUTORS, NEW YORK

Mr. KOLODNY. Mr. Chairman, and gentlemen, I am secretary of the National Association of Tobacco Distributors whose membership consists of more than 2,000 wholesale tobacconists catering to more than 800,000 retail tobacco outlets.

It is our intention to submit a brief in substantiation of our case. Hence, I will merely make a brief statement at present.

Should the provisions of section 2005 of the tax statute under consideration, exempting retail tobacco stocks, become law as written, it will be disastrous to both the wholesale and retail tobacconists.

The manufacturer of tobacco products sells directly to (a) the wholesalers, (b) chain stores, (c) certain large retailers.

The vast number of small retail outlets, of whom there are—as stated—approximately 800,000, procure their requirements from the wholesale tobacconists. These small merchants have neither the capital nor adequate facilities nor a credit standing which would enable them to stock up a substantial amount of merchandise prior to the date when the law becomes effective. The chain store, however, as well as the large retailer—and former experiences serve as a precedent for our contention—will avail themselves of the fact that retail floor stocks are wholly exempt from the new tax imposts to “load up” a quantity of merchandise which would enable them to “reap a harvest” for many, many weeks at the Government's expense. As you doubtless realize, cigarettes and kindred products do not rapidly deteriorate or become unsalable.

Coupled with these difficulties is also the fact that the Government will be deprived of an appreciable amount of additional taxes, and as good American citizens we know that the Government is in dire need— at present—of every added dollar of income.

While at first sight the amount of tax to be derived from a change in this provision might appear to be small, nevertheless it must not be overlooked that the additional revenue to be attained by the proposed levy will certainly amount to at least \$84,000,000 for the current year so that if retail stocks represent even as low as a 15-day supply, more than \$3,500,000 in revenue on cigarettes alone will be lost to the Government.

Senator KING. Mr. Sullivan, is the statement of the witness, and I am not questioning it at all, but merely for my own information, is the statement of the witness substantially accurate—about \$80,000,000 did you state?

Mr. KOLODNY. Yes; I think the Treasury Department stated this morning that it was \$76,000,000.

Mr. SULLIVAN. That is on the entire additional tobacco stocks. On the floor-stocks tax, my testimony this morning was that if there were no exemptions on floor-stocks tax of retail dealers, we would collect an additional 4½ million dollars at an expense of 2½ million dollars.

Senator KING. But the aggregate tax on tobacco was \$80,000,000?

Mr. SULLIVAN. \$75,000,000.

Senator CLARK. I am sorry, I wasn't there during your testimony this morning, Mr. Sullivan. In what way would you lose revenue by putting a tax on retail floor stocks?

Mr. SULLIVAN. We wouldn't.

Senator CLARK. I understood you would gain 4½ million dollars with an offset of 2½ million.

Mr. SULLIVAN. The \$2,500,000 is what it would cost us to administer the returns on the floor-stocks tax. There would be about 900,000 returns which we would have to handle.

Senator CLARK. In other words, then, you are simply recommending that a tax on floor stocks be not imposed because of the administrative costs being out of proportion to the money received?

Mr. SULLIVAN. No; we would receive a net profit on the transaction of \$2,000,000, Senator Clark. It was discussed in the committee this morning, the advisability of considering a partial exemption and requiring a floor-stocks tax on those retailers having over \$10 or \$20. In that event the number of returns we would receive would be far less. Our collections would be less, and we would have to make about the same investigation; the administrative costs would be about the same.

Senator KING. Excuse me for interrupting you, Mr. Kolodny.

Mr. KOLODNY. That is all right. Realizing the hardships that will inevitably arise, we suggest that the provision be rewritten as follows:

Floor Stocks Tax: (a) Upon all the articles (except chewing tobacco) subject to tax under subsections (a), (b), or (c) of section 2000 which on July 1, 1940, are held by any person for sale, there shall be levied, assessed, collected and paid a floor-stocks tax at a rate equal to the increase in rate of tax made applicable to such articles by section 2004; except that in the case of retail stocks where the amount of tax due aggregates \$10 or less, then no tax need be paid.

In urging this revision, we wish to emphasize that established precedent in the tax statutes of 1917 and those subsequent to it have

invariably extended the tax imposts to retail as well as other floor stocks.

Referring again to the impending tax loss to the Government of several millions of dollars, the following factors will contribute. There are—in the United States—in a vast number of chain stores and large retail outlets that would “load up” a large amount of merchandise prior to July 1. The saving to these firms—and the loss to the Government—at the rate of 50 cents per thousand on cigarettes will reach a fabulous sum. By obliging all firms whose tax liability exceeds \$10 to pay the tax on all floor stocks—as recommended—would serve a double purpose: (a) The yield to the Government will be appreciable, (b) instead of loading up excess inventories, these firms will handle only normal stocks and thus commence replenishing their stocks promptly after July 1.

Senator CLARK. In view of the statement of the Assistant Secretary of the Treasury that to make an exemption below \$10—\$10 or less—would diminish the amount of revenue to be raised by the tax, without appreciably diminishing the administrative cost, is there any reason for making an exemption of \$10?

Mr. KOLODNY. The only reason we suggested a \$10 exemption is solely to reduce the cost of collecting to a minimum, and secondly, that in the income tax bureau they also employ a method by which a man whose amount of earnings does not reach the requisite taxes required does not have to file any returns.

Mr. SULLIVAN. I have asked for an estimate, Senator Clark, on Mr. Kolodny's proposal. I had a wire from this gentleman yesterday in which he sets forth the proposal he submitted to the committee today and Captain Bliss, the Deputy Commissioner in charge of miscellaneous taxes, who will be charged with the administration of this, says that in his opinion that if there is a \$10 exemption on floor stocks taxes for retailers having no more than \$10 on hand, we would collect about \$2,500,000 in floor stocks taxes, and it would cost us about \$2,500,000 to collect that.

Mr. KOLODNY. Regarding the retailers—we state that that should apply where the amount of tax due aggregates \$10 or less.

Senator CLARK. Where the tax is \$10 or less.

Mr. SULLIVAN. I see.

The CHAIRMAN. Thank you very much.

Senator KING. Mr. Chairman, I suggest, because I have been quite impressed with the figures submitted by this gentleman, that Mr. Sullivan or the representatives of the Treasury Department if they care to, submit to us a brief statement in writing on this matter to be put in the record.

Mr. SULLIVAN. We will be very glad to do so.

Senator CLARK. If I understand the proposition, Mr. Kolodny, it is this: That the exemption of retail floor stocks from a tax gives a tremendous competitive advantage to such organizations as chain stores or department stores or the very large retailers who have the facilities and the money and the credit for laying in very large stocks of reserve before the tax goes into effect, which they can later use to great competitive advantage against the smaller retailers who either don't have the credit to do that or ought not to exercise the credit if they could get it?

Mr. KOLODNY. You state my case even better than I did.

Senator HERRING. And that applies to all floor taxes, too, Senator.

Senator CLARK. I think so, too.

The CHAIRMAN. All right; thank you, Mr. Kolodny.

Is Senator Chandler in the audience?

(No response.)

The CHAIRMAN. Are there any other witnesses who desire to be heard now?

(No response.)

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

(Whereupon, at 2:40 p. m. a recess was taken until the following day, Friday, June 14, 1940, at 10 a. m.)

REVENUE ACT OF 1940

FRIDAY, JUNE 14, 1940

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

The committee met, pursuant to recess., at 10 a. m. in room 312, Senate Office Building Senator Pat Harrison (chairman) presiding.

The CHAIRMAN. The committee will come to order. Is Senator Chandler in the room?

Senator CHANDLER. Yes, sir.

The CHAIRMAN. Senator, we tried to get you yesterday, so that you might appear during the afternoon but we could not reach you before we recessed. I understand that you want to present two matters in connection with this bill.

Senator CHANDLER. Yes.

STATEMENT OF HON. A. B. CHANDLER, UNITED STATES SENATOR FROM THE STATE OF KENTUCKY

Senator CHANDLER. Mr. Chairman and gentlemen of the committee, I desire to speak briefly to the committee with respect to two of the most important products of the Commonwealth of Kentucky, burley and bourbon—burley tobacco and bourbon whisky.

I am quite certain that the views of the people of my State have been well explained to the committee by my colleague Senator Barkley, who is a member of this committee, but I would like to take a few minutes of the committee's time to direct your attention to House Resolution 10039 amending section 2000 (d) of the Internal Revenue Code to provide for the taxation at seven-twelfths of 1 cent per booklet of cigarette paper of not more than 25 leaves, which booklets are not now subject to tax.

The purpose of not taxing cigarette papers in booklets of 25 or less was stated by the Senate Finance Committee to be as follows: "This is to permit the free distribution of such books with packages of tobacco."

Now, the result of the proposed change in the law, that is, the result of placing this new tax on cigarette paper, is to increase the tax burden on the consumer of roll-your-own tobacco from the present tax at the rate of 18 cents per pound, to a tax amounting, with the 3-cent increase in tax on tobacco, to from 30 cents to 35 cents per pound, or an increase from 66% percent to 99% percent.

Mr. Chairman, I would like to call your attention to the fact that there were 2,100,000,000 nontax paid booklets used last year. This is estimated to be sufficient to provide for 43,000,000,000 cigarettes. There were consumed from 125,000,000 to 250,000,000 pounds of

tobacco in this form. With the increase in tax from the new proposal, the price of the 5-cent package will go to 6 cents and the price of the 10-cent package will go to 11 cents, or the size of the packages will be reduced to—will be reduced one-eighth to one-fourth ounce per package. It is estimated that this loss will result in a decrease in consumption of 20 percent. The loss in revenue at 21 cents per pound on the smoking tobacco resulting from such decrease will equal from \$4,000,000 to \$7,000,000 and will exceed any possible collection which may result from the new tax on cigarette papers.

I don't believe it was the intention of the committee in either the House or the Senate, to tax these cigarette papers, and I wish very much that the committee would reconsider this tax. I would like to have permission to file the whole of this paper which I have not read completely, in the record.

The CHAIRMAN. That may be incorporated.
(Same is as follows:)

MEMORANDUM RE PROPOSAL TO TAX SMALL CIGARETTE BOOKLETS WHICH ARE NOT NOW SUBJECT TO TAX

H. R. 10039 amends section 2000 (d) of the Internal Revenue Code to provide for the taxation at seven-twelfths of 1 cent per booklet of cigarette-paper booklets of not more than 25 leaves, which booklets are now not subject to tax.

The purpose of not taxing cigarette papers in booklets of 25 or less was stated by the Senate Finance Committee to be as follows:

"This is to permit the free distribution of such books with packages of tobacco."

RESULTS OF THE PROPOSED CHANGE IN THE LAW

The result of placing this new tax on cigarette papers is to increase the tax burden on the consumer of roll-your-own tobacco from the present tax at the rate of 18 cents per pound to a tax amounting, with the 3-cent increase in tax on tobacco, to from 30 to 35 cents per pound, or an increase of from 66 $\frac{2}{3}$ to 94 $\frac{1}{2}$ percent.

Roll-your-own smoking tobacco is used by the poorest class of tobacco consumers. The booklets subject to the present new tax are universally given away by tobacco manufacturers to promote the consumption of this form of tobacco. These packages are for the most part sold in 5- and 10-cent packages with free cigarette paper. The increase in tax is arrived at as follows:

Tax:	Cents
21.3 $\frac{3}{4}$ -ounce packages equal 1 pound.....	21.0
21.3 booklets at $\frac{1}{2}$ cents per booklet.....	12.3
Total.....	33.3
Present tax.....	18.0
Increase, 85 percent or.....	15.3
With tobacco in 1-ounce packages:	
16 1-ounce packages equals 1 pound.....	21.0
16 booklets at $\frac{1}{2}$ cents per booklet.....	9.3
Total.....	30.3
Present tax.....	18.0
Increase 68 percent or.....	12.3

The proposed increase in tax on tobacco is supposed to be only 16 $\frac{2}{3}$ percent—yet in the case of the roll-your-own smoker, the poorest class—H. R. 10039 results in an increase of more than 66 $\frac{2}{3}$ percent.

There were 2,100,000,000 non-tax-paid booklets used last year. This is estimated to be sufficient to provide for 43,000,000,000 cigarettes. There were consumed from 125,000,000 to 250,000,000 pounds of tobacco in this form. With the increase in tax from the new proposal the price of the 5-cent package will go

to 6 cents and the price of the 10-cent will go to 11 cents, or the size of the packages will be reduced to one-eighth to one-fourth once per package. It is estimated that this will result in a decrease in consumption of 20 percent. The loss in revenue at 21 cents per pound on the smoking tobacco resulting from such decrease will equal from \$4,000,000 to \$7,000,000 and will exceed any possible collection which may result from the new tax on cigarette papers.

The CHAIRMAN. Well, the House put this provision in.

Senator CHANDLER. I understand that.

Senator KING. You would like it eliminated?

Senator CHANDLER. Yes.

Senator BAILEY. Does that relate just to cigarette papers?

Senator CHANDLER. Yes, sir.

Senator BAILEY. I am going to make a motion to strike that out.

Senator CHANDLER. Thank you, very much.

Senator BAILEY. I am satisfied that it is a big mistake.

Senator CHANDLER. I think so, too.

The wartime tax on tobacco, as is well known to all of you, is still continued and our people are very much alarmed. All the people in the tobacco producing States think that while they are willing to pay taxes to promote the national defense, in fact they are anxious to do it because they are anxious to have the country prepared, they do not think that tobacco ought to bear quite as severe a burden as it seems that it is proposed to have it bear under the circumstances.

And I hope the Senate Committee on Finance will give consideration to not placing such a heavy burden on the tobacco farmers of our section of the country which will be reflected in adverse tobacco prices next year, and result in more efforts on the part of the Congress to try to stabilize again the agricultural industry of our country.

I would like to speak just a minute with respect to another industry of our State which is going to be severely hurt if something is not done by this committee.

Generally speaking, rectifying consists of blending or mixing of distilled spirits. The prime rectified product in the distilled spirits industry is blended whisky. Blended whisky is a mixture—according to the definitions I find it—of straight whisky, alcohol, commonly known as neutral spirits, and flavoring and coloring ingredients.

There are also what are known as blends of trade whiskies which I will discuss briefly also herein.

At the present time the law imposes a tax of \$2.25 per proof-gallon on distilled spirits. This is applicable both to the whisky and to the alcohol which goes into the blend, as well as to the straight whisky sold as such.

The law in addition at the present time imposes the tax of 30 cents per proof-gallon on rectification, that is to say, on blended whisky. The 30-cent tax is not only a revenue producer, but was enacted primarily to equalize costs of blended whisky and straight whisky, so that the former would not have an economic advantage in the markets of the latter.

As evidence of the economic philosophy under which the 30-cent rectifying tax was imposed, I would like to call attention to the fact that blends of straight whisky, consisting of two or more whiskies each 4 years old, reduced in proof not below 90 percent, to which coloring and flavoring are not added, are not subject to the tax.

I would like to further call attention to the fact that gin, made by redistillation or in a rectifying house, at substantially the same cost of

production as gin made by distillation in the distillery, is not subject to tax.

Thus Congress did not impose the tax on these two rectified products which were of substantially the same cost as the unrectified product.

The Kentucky straight whiskies now 4 years of age and those which will become 4 years of age within the next year or two cost the average distiller when placed in the warehouse for aging 50 cents per proof-gallon. The cost to the distillery in carrying this whisky averages about 10.8 cents per gallon per year. The average 4-year-old whisky on the market is, in fact, about 52 months old. Thus a gallon of 4-year-old Kentucky straight whisky costs the distiller approximately 96 or 97 cents.

The blends on the average consist of 25 percent whisky and 75 percent alcohol or neutral spirits, and thus the whisky ingredient in a gallon of blended whisky costs 24.2 cents and the three-fourths gallon of alcohol costs, to produce, about 12 cents, so that the gallon of blended whisky costs approximately 36 cents.

Now the difference between 36 cents and 96 cents is apparent. The difference in cost, therefore, is approximately 60 cents per gallon. With a 30-cent tax on rectification, the blended whisky has a cost of 30 cents per proof-gallon less than the straight whisky.

There are now nearly 500,000,000 gallons of straight whisky stored in the internal revenue bonded warehouses of the country in which a tremendous capital investment has been made. Some 45 to 50 percent of this whisky is stored in Kentucky. Assuming that the increase in tax on distilled spirits is raised from \$2.25 to \$3 per gallon, it will to some extent diminish consumption, and it is obvious that withdrawals of the 500,000,000 gallons of bonds whiskies will be slowed up to the point where the distillers may have difficulty in meeting their obligations.

In addition to that normal slow-up, the blended whisky due to the tax structure is put in a position to take away any of the present straight whisky market.

From the above it will be noted that the rectifying tax should be raised, as I have stated here, to 60 cents per proof-gallon, although if you could see in your good judgment that it should be raised 40 or 50 cents in order to equalize the opportunities between the blended and the straight whisky, there would be no objection; but unless the 30-cent tax is materially increased to something approximating 60 cents per gallon, those with their capital invested in the tremendous stocks of straight whisky now in the country may find themselves—and I say, gentlemen, that they not only may but I think they actually will—find themselves in a difficult financial position.

This is particularly true of the smaller Kentucky distillers, many of whom will have difficulty in meeting their financial obligations if there is any material diminution in the rate of sale of their products.

My colleague is here now.

I mentioned at the outset that I knew he would advocate this strongly to the membership of the committee. I think it ought to be equalized, I am not seeking to burden unduly the industry that calls itself a blended whisky industry, but certainly they should not be placed in a position that would result, if not corrected, in an unfair advantage, and to the disadvantage of the straight, old-fashioned, hundred proof, aged-in-the-wood, pure old Kentucky whisky.

Senator BARKLEY. I will say that I have called the committee's attention two or three times, and again yesterday, to this. It seems to me that there can't be any question about the justice of this contention. If there was any reason for the 30-cent tax in the beginning, in order that there might be an adjustment of costs between the \$2.25 tax on straight whisky, certainly the increase from \$2.25 to \$3 a gallon justifies the increase in tax on rectified whisky.

They are competitive, and the more tax you put on one, and the less on the other, the more difficult it is for the higher taxed product to compete with the lower taxed product.

Mr. Chairman, thank you very much. That is all I have to say and I certainly appreciate your consideration, and the consideration of this committee.

Senator BARKLEY. Mr. Chairman, may I ask my colleague if he intended to make any reference to this other matter that has been brought to our attention, the tax on cigarette papers?

Senator CHANDLER. I already made reference to that before you came in, Senator.

Senator BARKLEY. All right.

Senator BARKLEY. Mr. Chairman, we had scheduled yesterday for hearing Mr. E. Winslow, the president of the North Carolina Farm Bureau. I have a wire from him this morning, addressed to the clerk of the committee, stating that it is impossible for him to be here and stating that Mr. B. B. Sugg is appearing in his stead, and I hope that you can hear him briefly.

The CHAIRMAN. All right, Mr. Sugg.

STATEMENT OF B. B. SUGG, GREENVILLE, N. C., REPRESENTING THE NORTH CAROLINA FARM BUREAU

The CHAIRMAN. I hope you will be as brief as you can, as we want to close this morning.

Mr. Sugg. I realize that.

Mr. Winslow, who was to be here yesterday, had a destructive hail on 80 acres of his tobacco, and he couldn't get here, and he asked me yesterday if I would come, and I couldn't get here before now.

I would like to call attention, Senator, that last September 8 the British buyers were withdrawn from our markets in North Carolina, and they were suddenly withdrawn and that resulted in the immediate closing of our tobacco markets in North Carolina, and South Carolina, and the markets were postponed in Virginia because of the exchange and war conditions over in the other countries, and it immediately placed the tobacco growers in the most disastrous condition they have been in, even including the period of 1931 and 1932.

Our markets were immediately closed, we came here to Washington, had a conference with the agricultural officials here, and also our various representatives in Congress and in the Senate, and through the agreement that we had the Government itself has purchased 175,000,000 pounds of flue-cured tobacco. That tobacco is now in storage with an option, held by the Imperial and other British purchasers, with certainly very little prospect at the moment of this tobacco being exported to Great Britain and other foreign countries.

Of course, we all are familiar with what has taken place in the last few weeks with reference to the exporting of tobacco to Belgium and Denmark and other countries, besides Great Britain. Our tobacco averaged last year, according to the official report that I

have in my pocket, just published by the Government here, a fraction over 14 cents. That does not permit any profit to be had by the tobacco growers.

Now, the point that I am making with respect to this tax of \$3 to \$3.50 a pound, is that it is apparent to us that a further increase in this tax on tobacco which I understand is probably estimated at from \$75,000,000 to maybe \$85,000,000, or \$90,000,000 increase, an additional increase, coupled with the fact that we received last year, the Government received, \$565,000,000 in tax, and necessitating of course, the increase in the price per pack of cigarettes, which is now 6 cents per pack, will have a tendency instead of raising revenue, to decrease revenue to the Government because it will drive people who smoke cigarettes—and it is doing that—from the cigarette to the roll-your-own or the pipe tobacco, where the Government only receives about 18 cents tax.

In addition to that it is bound to have a disastrous effect on our tobacco growers, because this increase in the tax will, if it does, and we believe it will, decrease the consumption of cigarettes, then it decreases the demand for the production of our tobacco.

With a 14-cent average price already, and with the prospects of shipping our tobacco this morning even darker than they ever have been before, if this tax is put on and we have the proposition of the decreased consumption of cigarette tobacco, it will certainly have a further disastrous effect on the tobacco growers who produce it, and I am speaking here on this occasion in behalf of the tobacco growers.

We realize it more keenly now than ever before, and I believe that you do because our export market, and probably more than 50 percent of our tobacco is exported to Great Britain; the Imperial Tobacco Co. alone buys one-third of our tobacco and pays one-half the number of dollars—and with the situation as we have it, with the tobacco growers now facing the absolute necessity of producing it at hardly the cost of production, it would have a strong tendency to increase our relief rolls by many thousands of people in North Carolina, Virginia, and other sections where we grow this tobacco.

And I say this, I believe that you will agree that the present tax of \$3 per 1,000 on cigarettes is already too high. The old war tax, if I recall, was \$1.50 and then raised to \$2 and is now \$3, and was put on during the last war, and that tax has never been removed—and in the condition that the tobacco farmers now are, Senator Bailey, in our State, and I would say almost in their present palsied condition, an additional tax on tobacco, as indicated in what I have just said with respect to the curtailment of the consumption of flue-cured tobacco, reflecting in the curtailed production of the farmer and some of that cost, is bound to be absorbed by the tobacco growers and with the present price of a fraction over 14 cents, it cannot be absorbed without injury to the growers.

I think that you further will agree that our tobacco farmers and our tobacco people, have certainly been patriotic, they have been patriotic all these years with this present tax on their product, and a further tax on their product would certainly curtail the production which would hurt the thousands and thousands of growers, and then will not produce the revenue that the Government thinks it will produce.

Senator KING. Heavy as the tax may be upon the producer, it is much heavier upon the smoker, isn't it?

Mr. SUGG. Yes. I imagine that the tax on the cigarettes will be increased. That will be reflected on the consumer, and the minute that he quits smoking one cigarette on which you get three-tenths of a cent every time one cigarette is smoked—

Senator KING (interposing). But the cigarette manufacturer pays a very heavy tax.

Mr. SUGG. The cigarette manufacturer?

Senator KING. Yes.

Mr. SUGG. The tax, as I pointed out, last year was \$565,000,000 on manufactured tobacco in the United States, collected from the consumer.

Senator KING. For my own information—I ought to know this—is that tobacco which the Government has made a loan upon, has the tax been paid upon it?

Mr. SUGG. No, sir. I am glad that you asked me that. That tobacco is being held now on the borders of Virginia and in the coastal cities. The Imperial Tobacco Co. has an option on that and the Imperial Tobacco Co. does not pay any tax on cigarettes in this country because they do not manufacture any cigarettes here.

Senator KING. As I understand, there is a tax upon tobacco, and what I am asking is whether or not that tobacco which the Government has a loan upon, whether the tax has been paid upon that.

Mr. SUGG. No; because that tobacco is for export purposes and this country does not tax, of course, export tobacco manufactured in a foreign country.

In closing, Senator, I will say this, that our growers just feel like a further tax on them will restrict the production of their tobacco, will restrict the consumption of the cigarettes, and the purpose that we are seeking, to raise revenue. It will decrease revenue, Senator.

Senator BAILEY. Mr. Sugg, I want to call attention to this, through you, that with the additional tax on cigarettes, the Government gets 6 cents a pack?

Mr. SUGG. At the present.

Senator BAILEY. Yes; at the present, but there are 29 State that levy additional taxes, 1 State levying as high as 5 cents a package.

Mr. SUGG. Yes, sir.

Senator BAILEY. And that is more than half of the States?

Mr. SUGG. Yes.

Senator BAILEY. And the whole thing is calculated now, you have reached the point where you may destroy the whole industry, not only the farmer but the source of the Federal revenue. That is true, isn't it?

Mr. SUGG. That is exactly true.

Senator BAILEY. Now the other question I want for the record. The carry-over of this bright tobacco and of the other tobaccos in this country, is very great now, isn't it?

Mr. SUGG. The greatest we have ever had.

Senator BAILEY. Can you give me the exact figure?

Mr. SUGG. Yes; I have it right here. These are the official Government figures just published on June 10 of this year.

Probable United States stocks, 1940 (this is flue-cured only, now), 1,425,000,000 pounds, 50 percent above any previous record.

May I just quote one other thing? In closing I will just read this from the Government bulletin, dated June 10:

With a large 1939 crop and the effects of the war on export markets, flue-cured tobacco growers are facing a serious market situation, worse than the situation from 1930 to 1932.

when thousands and thousands of our growers lost their farms and homes as well as their businesses.

Senator BAILEY. And tens of thousands were thrown on Federal relief?

Mr. SUGG. Yes; and I happen to be on the relief board myself in our section, and we are having constantly additional tobacco growers applying for relief.

The CHAIRMAN. Thank you very much. Mr. Alvord.

Mr. Alvord, you are the only one appearing for the Chamber of Commerce?

Mr. ALVORD. Yes, sir.

The CHAIRMAN. You have 15 minutes.

Mr. ALVORD. Yes, sir.

The CHAIRMAN. We have several witnesses here and I trust that you can close in 15 minutes.

Mr. ALVORD. I will do my very best.

**STATEMENT OF ELLSWORTH C. ALVORD, REPRESENTING THE
COMMITTEE ON FEDERAL FINANCE, CHAMBER OF COMMERCE
OF THE UNITED STATES, WASHINGTON, D. C.**

Mr. ALVORD. Mr. Chairman and gentlemen: I am sure that it is not necessary for me to assure each of you that I am not here to oppose increased revenue for national defense, nor am I here to oppose an increase in the statutory debt limit for national defense.

With respect to those two items I can be very brief, and, I trust, specific.

Every penny of additional revenues should be devoted to national defense, and to no other purpose. Every dollar increase in your statutory debt limit should be used solely for financing national defense and no other purpose. The bill pending before you does not comply with either of those two standards.

Title I, proposing to increase revenues about \$325,000,000—the so-called permanent increases—is not devoted to national defense. Nor is the sinking fund increase limited exclusively to national defense.

If some temporary stopgap is necessary, as I think it is, I would suggest that the Congress impose those taxes, designed to raise as much revenue as you gentlemen think you can raise, which cannot be made retroactive (such as additional excise taxes). Impose those immediately for a period of a year, and then get down just as promptly as you can to solve what seems to me to be a much larger, more important, more tremendous problem.

All of your increases in income taxes can be made retroactive, and a sound revision of your revenue system enacted any time before the 15th of next March will collect just as much revenue as if it were enacted now.

Senator CONNALLY. Wouldn't it be fairer to business to let them know it now, that we are going to collect it on 1940, so that they could, the rest of the year, arrange their business, rather than wait until next March and then make it retroactive?

Mr. ALVORD. It would certainly be more fair, but you have frequently imposed taxes after the close of the taxable year.

Senator CONNALLY. I know we have, and I know we can do it.

Mr. ALVORD. I think it would be more fair if you would impose taxes on a fair basis, even if made retroactive.

Senator BARKLEY. Did I understand you at the outset to indicate that the position of the United States Chamber of Commerce was that in this bill we ought neither to raise revenues for general purposes or increase the public debt?

Mr. ALVORD. For general purposes; yes.

Senator BARKLEY. What are you going to do about the debt?

Mr. ALVORD. I think that the Congress—and I will discuss that in just a minute, if I may—but I will answer you generally. I think that the Congress is going to find itself confronted with the absolute necessity of eliminating all nonessential expenditures, and if you do that I think you can live within your income.

Senator BARKLEY. Is Congress to determine what is or is not a non-essential, or is the United States Chamber of Commerce?

Mr. ALVORD. The Congress of the United States, sir, and I have advocated that the Congress do that, and I have a plan under which I think the Congress will do that.

Senator BARKLEY. All right.

Mr. ALVORD. It seems to me that a national-defense program is divisible into four separate but closely interrelated and integrated problems. One is the acquisition of adequate military and naval forces, adequately equipped and adequately manned.

Second, is maximum industrial capacity in order to sustain your national-defense program.

Third is the preservation, the protection, and encouragement of private enterprise, not so closely connected with national defense. Someone must pay your national-defense costs, and they will come primarily out of the activities in my third category.

Objective four is a sound fiscal system designed to bring about adequate military and naval forces, designed to permit the acquisition and maintenance of maximum industrial capacity for national defense purposes; and designed to encourage and protect and permit the continuation of private enterprise, both during the period which I might call the period of armed peace, and the period, which I trust we will see soon, of post-war activity.

With respect to the national-defense program, I think that Congress should insist that very soon someone tell you what the cost estimates are. Even though they are only estimates, let us have minimum and maximum estimates as to the total cost, first, of acquiring an adequate military and naval force; second, as to the cost of maintaining that adequate military and naval force; third, the probable length of time for such expenditures.

With those elements, then the Congress can really sit down seriously and consider methods of financing.

Now, I don't think that you are going to conclude that you can finance that program through taxation. To me it simply cannot be done. Certainly it cannot be done if you are going to permit private enterprise to play a part either in objective two or in objective three. But one outstanding fact which always forces me to the conclusion that you have to borrow money in very substantial amounts to finance an adequate national-defense program, is that if you take 100 percent

of the net income of corporations in the country, every corporation in the country, and if you take 100 percent of all the incomes of the country over \$10,000, you still wouldn't have enough money to finance your program.

Senator KING. The national-defense program, if you will pardon just an interruption—and I am sorry to divert you—will depend, will it not, to some degree, upon the conditions in Europe? If Hitler and his associate now, dominate Europe, and destroy France and Great Britain, and seek intrusion into the Western Hemisphere, our national program then would be a little different from what it would have been if we had drawn a national program 2 or 3 or 4 or 5 months ago?

Mr. ALVORD. That, of course, is true, sir. I naturally have my own ideas on it. But I, as a citizen of the United States, am perfectly willing to rely upon the judgment of the Congress in determining what that national-defense program should be.

The only thing I ask, as a citizen, is that you make that determination.

With respect to my first recommendation I find myself, very happily, in a very distinguished group. I want to endorse a proposal which has been suggested twice by the Secretary of the Treasury of the United States, and which has been advocated by the very able statesman who is the chairman of your committee.

I would change it just a little. I think there should be established for both the House of Representatives and the Senate, a special budget committee charged with preparing the financial program to carry out the objectives which I have enumerated. That committee would be an ex officio committee in each House, consisting of those gentlemen charged with raising revenues, and those gentlemen charged with spending money.

Let them decide upon the financial program, of our Government, what is going to be required, what can be eliminated.

Then I would suggest, secondly, that you sit down as soon as you can and prepare what I would call a permanent, long range tax system, one which, let me say, is designed to remain in force for a period of 10 years, and which will produce the maximum possible revenues for your Government consistent with your other political and economic policies. Your tax system, gentlemen, I don't need to tell you, must be coordinated with your other policies.

My best guess is that over a period of 10 years the average revenue which you can get under that system will not be far from \$7,000,000,000 annually. I have always said heretofore that it was \$6,500,000,000 but I have boosted it a half a billion because of the spurt of war activity.

The budget committee will then be faced with the job of determining how the excess of its planned expenditures will be financed. The best start on it would be to pass a concurrent resolution, in both the House and the Senate, fixing a ceiling upon the total expenditures. Whether that ceiling is \$10,000,000,000 or \$15,000,000,000 or \$20,000,000,000, I am not concerned, so far as the first or second session of the Congress is concerned. Eventually the Congress will be governed by what they can raise by taxation and by what they can borrow.

I just throw out one more thought, trying to keep within the chairman's 15-minute period. You gentlemen realize fully that there

are only four ways in which the expenses of your Government can be paid. One is by taxation; the second is by borrowing within your capacity to repay; the third is by confiscation, and the fourth is by repudiation.

Now, I still have enough confidence in the Congress to have a pretty good idea which of those methods the Congress will follow. I would be very happy to answer your questions.

Thank you very much.

Senator CONNALLY. Who suggested that Congress was not going to raise this money by taxation or bonds, and who suggested that we talk about repudiation? Nobody has suggested that, have they?

Mr. ALVORD. Senator, the time is going to come——

Senator CONNALLY (interposing). I am not talking about the time that is coming, I am talking about now. You are talking about repudiation, nobody is going to repudiate the Federal debt. Have you heard anything like that?

Mr. ALVORD. I am merely throwing out the very real probability that if you don't put your Government on a sound financial basis——

Senator CONNALLY (interposing). We are trying to put it on a sound financial basis, but every time we do, a lot of you fellows come up here and say "You musn't tax this" and "You musn't tax that," and you lecture us a lot. We are trying to raise this money by taxation and borrowing.

Mr. ALVORD. You have never heard me oppose a sound tax system.

Senator BARKLEY. Do you think that Congress ought now to sit down and revamp the whole tax structure before it passes this particular bill?

Mr. ALVORD. I don't think you can do it now, Senator. My suggestion was that you pass those taxes which cannot be made retroactive, and work your additional income taxes, your additional forms of revenue into what I would call your permanent revenue system, and you can do that any time between now and the 15th of next March.

Senator CONNALLY. We can't win this war with wind. If we could, we would have won it before. You fellows that are for strong national defense and protection, you are all right until it comes to tax, and then you want to squall and tax somebody else. I am in favor of taxing you all.

Mr. ALVORD. Senator, you wouldn't impose a system which would attempt to get more than the maximum revenues?

Senator CONNALLY. I have heard that old talk about the diminishing returns for a long time, and every time we pass a tax bill if it didn't increase the returns you wouldn't be up here hollering.

Mr. ALVORD. I would be very happy to have you look at the figures on diminishing returns.

Senator CONNALLY. I would be very glad to do that, but I don't see that we gain much by a lecture on philosophies. We have got to have money and have it now.

Mr. ALVORD. I quite agree with you, and I would get that amount now which you cannot get later, and then really sit down and do the rest of the job.

Senator CONNALLY. We are going to revamp it all in January, and we are going to jerk you out of your boots and you might as well get ready for it. I am in favor of revamping the whole thing in January and paying some of these debts.

Senator KING. As far as I am concerned, I would make the taxes now, instead of \$1,004,000,000, I would have it \$1,500,000,000, or \$2,000,000,000 because we will have greater difficulty in increasing the taxes which will be necessary to meet our obligations next January, than we have now.

Mr. ALVORD. I will sum it up by telling you to take every penny of increased taxes and use it for national defense and nothing else.

Pursuant to the permission of the chairman, I am appending hereto a statement submitted on behalf of the chamber's committee on Federal finance, and an outline of my remarks before the annual meeting of the Chamber of Commerce of the United States, May 1, 1940, primarily to make available to the committee certain statistics which I have compiled and which are appended thereto.

A TAX PROGRAM FOR NATIONAL DEFENSE¹

Taxes for the national defense are accepted by businessmen as essential. An increase in debt limit, solely for defense expenditures, is also required. We believe, however, that additional taxes or an increase in the debt limit for other purposes than national defense should be opposed.

POSITION WITH RESPECT TO THE BILL

(1) For national defense purposes the statutory debt limit should be increased by the amount necessary to finance the requirements for the fiscal year 1941.

(2) The situation requires the imposition of additional taxes; they should remain in force for only 1 taxable year in order that there may be opportunity for the development of a well-planned revision of the tax laws. A complete revision of the tax structure (on a better basis than the bill passed by the House) is most essential, in order that the needed revenues may be better obtained and that there may be equity among taxpayers and between the revenue opportunities of the State and the Federal Governments. The 1-year taxes to be added now should take the form of a flat percentage increase in the present income-tax rates, and possibly some increase of other rates. These temporary taxes should be supplanted, before their expiration, and as quickly as possible, by the comprehensive revision of the whole structure.

(3) Preparations should begin at once for the formulation of a Federal fiscal program dealing with taxes, expenditures, and debt. The revenue program should be suitable for the Government to follow for a period of years. If Congress remains in session, its appropriate committees should give immediate attention to the development of such a program. If Congress adjourns, there should be requirement for studies to be undertaken by the Joint Committee on Internal Revenue Taxation, the Treasury Department, and the Bureau of the Budget for prompt action next session.

(4) There should be added to the tax bill a definite requirement for reduction of nondefense expenditures, in an amount not less than the additional annual revenue proposed to be raised by it.

FINANCING A NATIONAL-DEFENSE PROGRAM

The vital need is for a long-range coordinated national-defense program.

Proper methods of financing the cost to be borne by the Government are essential elements of a defense program if confiscation of capital, inflation, and eventual repudiation are to be avoided. There must be prudent use of the taxing power, and the use of the borrowing power must be kept within limits permitting ultimate repayment.

We believe that there are proper methods of financing defense costs under which (a) we can acquire and maintain adequate military and naval forces, adequately equipped; (b) we can acquire and maintain maximum industrial productive capacity, including plant, equipment, and trained personnel essential for national-defense purposes; and (c) we can conserve, promote, and strengthen private enterprise not directly employed in national defense, but essential to the

¹ Statement of Ellsworth C. Alvord, chairman of the committee on Federal finance, presented June 14, 1940, to the Committee on Finance of the United States Senate, at the hearings on the revenue bill of 1940.

preservation of private economy and employment, particularly during the period of armed peace or post-war readjustment.

So far as is possible there should be early decisions with respect to the estimated cost of the Military Establishment it is necessary to build, the annual maintenance cost of that Establishment, the probable period of time over which the expenditures can be spread, the means of assuring efficiency and economy in making the expenditures, and the preservation of facilities needed for times of peace.

In the interest of maximum industrial productive capacity there should be decisions in favor of developing necessary expansion under private control and direction rather than under Government financing or ownership. To that end there should be relaxation of any undue Government restraints upon private financing and the tax measure should interfere as little as possible with the flow of private capital into industrial expansion. Any use of Government funds in aid of industrial expansion should be restricted to the most emergent situations after a clear showing of private inability to provide the financing.

ESSENTIALS OF A SOUND FINANCING PROGRAM

Any defense program can be financed from taxation and controlled borrowings, but there must be regard to three essential factors:

- (1) The importance of an increase in business and individual net incomes in order to provide a larger base upon which the major taxes are levied.
- (2) The method of obtaining maximum Government revenues without causing a shrinkage of the income base.
- (3) The best manner of rigorously restricting nondefense expenditures and of providing an effective control by Congress over the volume of expenditures from year to year.

These requisites should be recognized in order that there may be no resort to confiscation or inflation.

A PERMANENT FISCAL PROGRAM

On several occasions, the chamber committee on Federal finance has recommended, and outlined in detail, the following program:

- (1) A general revision of the tax system, for the purpose of writing a stable, equitable, and reasonably permanent tax law, designed to remain in force over a period of years, and calculated to produce the maximum revenue over that period.
- (2) An effective congressional control of expenditures, through the creation of congressional budget committees with power to propose a concurrent resolution for the consideration of the Congress, fixing maximum aggregate expenditures for each fiscal year.

The necessity for such a long-range program has not been diminished by the defense emergency. It has increased in proportion to the need for additional revenue. We still firmly believe that such a program offers the only possible solution of our fiscal problems, and that it should be undertaken as early as possible.

SOLVING THE TAX PROBLEM²

There is a solution for the tax problem. But the solution rests with you. A navigator doesn't pick the place of destination nor the ports of intermediate call. But he knows storm areas, and he sees storm signals. He knows the rocks upon which others have been wrecked. This same sea has been sailed before.

The beginning of the new decade is probably a particularly opportune time for us to determine our position, the distance we have come, and the variation from the course we have chosen—and possibly to recheck our destination and rechart our course. Astronomy is more reliable than astrology.

I shall summarize a few of the more important problems confronting us, the proclaimed objectives, and a brief summary of the more important facts, from which you may determine our present position. Sufficient statistical data, in support of the facts, will be found in a series of attached tables.

² An outline of remarks by Ellsworth C. Alvord before the annual meeting of the Chamber of Commerce of the United States, May 1, 1940.

IDLE MEN

The objective.

- (1) Private employment is the only sound solution for unemployment.
- (2) Temporary assistance is necessary and must be provided—and we are told that we should prepare for permanent assistance.

The facts.

- (1) No progress has been made—there are still 9,500,000 unemployed (see table 1).
- (2) The extraordinary business activity of last fall (the Federal Reserve Board index was at the all-time high of 128 in December—see table 2) increased employment by about 1,000,000.
- (3) The investment of about \$8,000 is required to produce work for one man; and possibly \$25,000,000,000 of new capital will be required to put our entire employable labor surplus to work.
- (4) The Federal Government has spent \$17,000,000,000 in providing temporary assistance, and untold billions in fruitless experiments.
- (5) Substantial sums intended for relief have been wasted and used for political purposes.

IDLE FUNDS

The objective.

The flow of private funds into private enterprise must be resumed.

The facts.

- (1) \$8,000,000,000 to \$10,000,000,000 should flow annually into capital construction—i. e., into expansion, additions, betterments, and replacements of plant and equipment.
- (2) From 1919 to 1930 there was an annual average of about \$3,400,000,000 in new corporate financing (see table 3).
- (3) In 1939, new corporate financing (exclusive of refundings) amounted to \$369,000,000 (see table 3).
- (4) Despite the tremendous reservoir of idle funds, new opportunities for private investment under present conditions are unattractive.
- (5) A small enterprise is unable to obtain necessary funds for expansion and improvement, and few larger enterprises are seeking new funds.
- (6) The investment of private funds is normally governed by three factors, none of which is present today: (a) Protection of principal; (b) liquidity; (c) a return commensurate with the risk.
- (7) At the present time, a business enterprise must possess the probability of an average annual net profit of more than 20 percent upon its investment in order to compete with tax-exempt securities in the hands of stockholders.
- (8) Undistributed corporate funds available for capital construction are rapidly being depleted—corporations distributed about \$17,000,000,000 more during the last decade than their aggregate net income available for dividends.
- (9) Excess bank reserves, which amounted to less than \$1,000,000,000 in 1934, swelled to \$6,000,000,000 in April 1940 (see table 4).

SOCIAL SECURITY

The objective.

Security from the fears of the future, from poverty, unemployment, sickness, old age—for our families, our friends, our neighbors, for everyone.

The facts.

- (1) The value of the social security offered by the Government depends upon its ability to meet its promised payments when they become due.
- (2) Substantially all the net proceeds of our social-security taxes are being used to meet current Government expenses.
- (3) Old-age assistance and retirement pay promised by the Government should not deprive us of the opportunity of providing security for ourselves and our families through private savings (in the form of investments, trust funds, savings accounts, insurance and annuity contracts, and private retirement compensation plans and pensions).
- (4) The financial security of every one of us is rapidly being impaired and jeopardized (see table 5). The following statement by the Federal Advisory Council of the Federal Reserve System (in a report dated June 6, 1939), with respect to the existing "easy money" policy, is significant:
"It has become evident during the past 2 or 3 years that the cumulative effect of the policy in question [the 'easy money' policy] is profoundly and adversely

affecting that large group of industrious and thrifty persons who are, by virtue of their character and habits, the backbone of the country's social and economic structure. Steadily they have seen the returns on their accumulated savings decrease as savings institutions, faced with constantly diminishing earnings, have been forced, step by step, to decrease the rate of interest paid on savings deposits. Steadily, year by year, they are meeting increased discouragement in their attempts, through the purchase of life insurance, to provide for their own old age and for the protection of their families, as the cost of insurance slowly mounts and as the dividends payable on policies steadily diminish. Schools, colleges, churches, hospitals, and educational and charitable institutions of all sorts see the returns on their accumulated endowments constantly lessening, the salaries of their staff members reduced, and their promotions delayed, services to students, patients, and dependents curtailed, and more and more of the functions which are normally and most efficiently performed by private or semiprivate agencies necessarily taken over by public boards at the expense of the taxpayers unless essential social needs are to be neglected."

(5) Private savings (invested in legal investments for trust funds) earned in 1939 only 46 percent of what they earned in 1936.

(6) High-grade security offerings on the public markets are rapidly dwindling, in part by reason of private placements.

(7) Ten years ago savings of \$20,000 would have provided our families, upon our death, with an annual income of \$1,000. Approximately twice that sum is required today.

(8) By reason of decreased net earnings, lack of liquidity, and potential tax liabilities, the net value of investments has decreased at least 50 percent.

(9) Regular employment is better security than unemployment insurance.

NATIONAL DEFENSE

The objective.

An adequate national defense to assure security from our enemies.

The facts.

(1) Our aggregate expenditures for national defense from 1931 to 1940 were \$8,500,000,000; for 1941, they will exceed \$2,500,000,000 (see table 6).

(2) In 1934 our expenditures were less than \$500,000,000. The estimate for 1941 is \$2,700,000,000.

(3) For the next several years, our defense expenditures will undoubtedly exceed \$2,000,000,000 annually, and may double or treble that amount.

(4) The direct financial cost of our participation in the World War was about \$40,000,000,000.

(5) It is reported that the current financial cost to the present participants in the war abroad is more than double that of the World War.

(6) A strong Treasury is the keystone of an adequate national-defense program

LABOR

The objective.

(1) Continuity of employment.

(2) Opportunities for promotion and advancement.

(3) Reasonable wages, hours of work, and working conditions.

(4) Retirement and disability compensation.

The facts.

(1) Total wages and salaries paid in 1939 were less by one-sixth than the payments in 1929.

(2) In the year following the enactment of the Wagner Act, there were more strikes than in any of the 15 preceding years. In 1937, there were more strikes, and more man-days of idleness by reason of strikes, than in any previous year of American history (see table 7).

(3) Opportunities for promotion and advancement are increased as private enterprise expands.

(4) Wages are payable only out of production.

(5) Net profit is the incentive which keeps an employer in business.

YOUTH

The objective.

The preservation of the opportunities of youth—to obtain an adequate education and training, to choose their work, to work for themselves or for others, and to advance.

The facts.

- (1) The individual ability to meet the cost of education and training has been impaired.
- (2) Employment opportunities are seriously restricted.
- (3) The difficulties of beginning and continuing an individual enterprise are constantly increasing.
- (4) Although temporary Government assistance has been useful as a stopgap, an adequate solution depends upon private enterprise.
- (5) We are passing on to the youth of today and tomorrow the burden of a stupendous and increasing public debt.

NATIONAL INCOME

The objective.

- (1) A national income of \$100,000,000,000.
- (2) A corresponding increase in business *net* income—an objective hitherto seemingly disregarded.

The facts.

- (1) The highest national income was about \$80,000,000,000 in 1929 (see table 2).
- (2) Our national income last year was about \$69,000,000,000.
- (3) National income can be increased only by stimulated production.
- (4) Pay rolls increase as national income increases.
- (5) Corporate net incomes have suffered a severe shrinkage in the last decade, and have not recovered as national income has increased (see table 2).
(For example, in 1937 the production index was 110 as compared with 111 in 1928, but corporate net income was \$6,900,000,000 as compared with \$10,000,000,000 in 1928. In 1936 and 1939 corporate net income approximated \$6,500,000,000 as compared with \$9,000,000,000 in 1927, although all 3 years averaged 105-106 in industrial production.)
- (6) From this small income base, business enterprises are expected to pay increased costs, heavily increased taxes, and earn sufficient profits to justify the investment of private funds.

GOVERNMENT EXPERIMENTS

The foregoing is a very brief summary of some of the important problems confronting us. Neither the summary nor the outlined facts are intended to be complete, but they are sufficient to point out the course we are traveling and the distance we have come.

Assuming that there are no undisclosed principles in the background, your Government has experimented with two conflicting theories: (a) Restriction of the production of income by discouraging private enterprise, private investment, and private employment, directly and indirectly, in order to promote certain social objectives and reforms; and (b) the stimulation of consumer purchasing power through Government spending and subsidies, in order to increase consumer demand and hence the production of income.

A statement of the two theories should be an adequate refutation of them. But if my outline of facts is reasonably accurate, a complete failure of both should be admitted. It is reported that attempts to impose further restrictions upon the production of income have been abandoned—and we can hope that the report means permanent abandonment. However, the spending policy is still vigorously advocated. Accordingly, some further discussion seems necessary.

THE SPENDING POLICY

The theory of "recovery through public spending" has had a thorough test in the last decade. The "net contributions to purchasing power" (or deficits, in ordinary language) have been tremendous, and prolonged over a period of years (see table 8).

The continued popularity of the spending theory among Government financial advisers seems to rest primarily on the fact that the 1937-38 "recession" followed rather closely upon a reduction of the Federal deficit from \$4,900,000,000 in 1936 to \$1,400,000,000 in 1938. This recession, therefore, has been attributed to a too-rapid curtailment of expenditures. Actually, if one examines the figures, it appears that two-thirds of the reduction in the deficit at that time was due to an increase in tax receipts, and only one-third to curtailment of expenditure. The logical conclusion would seem to be that a too-rapid rise in the tax burden rather than a too-rapid drop in expenditures was responsible for the ensuing

decline. Moreover, the only expenditure substantially reduced from 1936 to 1938 was the soldiers' bonus, a nonrecurring item—leading me to conclude that we should avoid inflationary hypodermics, which wear off rapidly and leave serious after effects. Finally, I think it should be noted that consumer purchases fell off last, and not first, among the economic indices in the 1937 recession. Loss of consumer purchasing power was evidently a result, not the cause, of decreased business activity.

SUMMARY OF FISCAL FACTS

Briefly, we face today the following financial situation (see tables 8 and 9):

Expenditures and deficits.

- (1) Gross Federal expenditures for the decade 1931-40 of \$71,000,000,000.
- (2) Expenditures for the current fiscal year aggregating \$9,700,000,000, and (assuming that the Congress appropriates no more than the current Budget estimates) expenditures for the next fiscal year of \$9,100,000,000.
- (3) An expenditure of approximately \$1,000,000,000 this year to run the ordinary departments and agencies of the Federal Government—an increase of 69 percent since 1934 (see table 10).
- (4) An average deficit for each year of the decade of \$3,000,000,000.
- (5) An estimated deficit for the current fiscal year of \$4,000,000,000, and for the next fiscal year of \$3,000,000,000.
- (6) We cannot continue forever to finance deficits—and we ought not to, even if we could.

The Federal debt.

- (1) An increase in the debt from \$16,800,000,000 in 1931 to \$43,200,000,000 on June 30, 1940.
- (2) A debt which in a few months will exceed the present statutory limit of \$45,000,000,000.
- (3) An interest charge on the debt of \$1,100,000,000, increasing annually.

Federal revenues.

- (1) We have had nine new tax laws during the last 8 years (although the Revenue Acts of 1938 and 1939 were reversals in part of prior policies).
- (2) Our present annual yield is below \$6,000,000,000.
- (3) Our existing tax rates are far above the point of maximum productivity.
- (4) We shall need the maximum possible revenues during the next 10 years.
- (5) There is no revenue system which will average \$10,000,000,000 or \$9,000,000,000, or \$8,000,000,000 annually, during the next 10 years.
- (6) Increased revenues must be found primarily in increased national income—new taxes or increased rates will be nonproductive.

SUMMARY OF CONCLUSIONS

- (1) Private enterprise offers the only possible permanent solution—it should be given a chance.
- (2) If we are going to stimulate employment, we must stimulate private investment.
- (3) If we are going to increase national income, we must stimulate production.
- (4) If we are going to enlarge consumer purchasing power, we must first encourage greater business activity.
- (5) A healthy and enduring recovery cannot be achieved without the combined forces of private enterprise, private investment, and private employment.
- (6) The choice lies between private enterprise and complete regimentation—private enterprise cannot succeed half regimented and half free.
- (7) Our fiscal policies must conform to the foregoing conclusions.

RECOMMENDATIONS

Upon the basis of these conclusions I submit the following for your consideration:

- (1) *Reasonably permanent revenue system.*—I recommend the adoption of a reasonably permanent tax system, designed to remain in force over a period of years. "Emergency" levies and annual tinkering with the tax laws should be avoided. We should adopt a stable, equitable revenue system, imposing reasonably certain tax liabilities, at rates designed to promote business activity and expansion and thus to produce maximum revenues over a period of 10 years. The Chamber's Committee on Federal Finance has published specific and detailed

recommendations to this end. The Treasury and the Congress made substantial progress toward such a system in the 1938 and 1939 Revenue Acts. Encouraging gains in business activity followed each of these acts. This work should be continued and completed.

(2) *Congressional control over expenditures.*—I recommend the adoption of a direct and more effective control by the Congress over the Executive Budget, in order to keep expenditures within necessary limits. The proposal by Senator Harrison for a Joint Congressional Budget Committee is a promising step in this direction. Separate committees for the House and Senate would, I believe, be more effective. The Budget Committee for the House might be composed primarily of the ranking members of the Committee on Ways and Means (which originates revenue measures) and the Committee on Appropriations, with either the Speaker or the majority leader as chairman. The Budget Committee for the Senate would be similarly constituted.

These committees should consider from the point of view of fiscal policy the expenditure program of the Government for the ensuing year. Each would review promptly the Executive Budget, the estimated revenues and expenditures, and the methods of financing any proposed deficit.

The Budget Committee of the House should then, by concurrent resolution, recommend the maximum figure for expenditures for the ensuing year. The House after full debate on this proposal, should vote to fix a "ceiling" on expenditures. The resolution would then go through similar procedure in the Senate. The Committee on Appropriations should not report out any appropriation bill until the concurrent resolution is adopted. After its adoption the appropriation bills should be required to conform to the total amount fixed in the resolution.

(3) *Statutory debt limit.*—Our aggregate expenditures, for a year or two, at least, will probably exceed our revenues. In such event, whether or not temporary expedients are resorted to, our statutory debt limit must be increased. The Budget Committee of the House of Representatives, after the adoption of the concurrent resolution fixing the ceiling upon expenditures, should then report out a joint resolution granting authority to the Treasury to borrow the specified portion of the proposed deficit which is to be financed by borrowing; and no appropriation bill should be considered until after the enactment of the joint resolution. Thus, attention of the public will twice be directed to the financial policies of the Federal Government. A flexible and effective control of the expenditure "ceiling" and of our public debt should result.

(4) *Executive controls.*—The Director of the Budget, with an adequate staff of experts, should be given more effective, businesslike controls over all the expenditures of the executive agencies, in order to promote efficiency and economy in Government.

TABLE 1.—Unemployment

1920.....	558,000	1930.....	3,809,000
1921.....	4,754,000	1931.....	8,113,000
1922.....	2,917,000	1932.....	12,478,000
1923.....	749,000	1933.....	12,744,000
1924.....	2,034,000	1934.....	10,400,000
1925.....	817,000	1935.....	9,522,000
1926.....	464,000	1936.....	7,599,000
1927.....	1,620,000	1937.....	6,372,000
1928.....	1,857,000	1938.....	10,099,000
1929.....	429,000	1939 (avg. for last 9 mo.)....	9,360,000

Source: National Industrial Conference Board study "Conference Board Studies in Enterprise and Social Progress."

TABLE 2.—Business indices

	Industrial production index ¹	Factory pay rolls index ²	Corporate net income ³	Federal income taxes ⁴	National income ⁵
1926.....	108	104	\$9,673,000,000	\$1,230,000,000	\$72,800,000,000
1927.....	103	102	8,982,000,000	1,131,000,000	73,400,000,000
1928.....	111	102	10,618,000,000	1,184,000,000	78,800,000,000
1929.....	111	109	11,064,000,000	1,103,000,000	79,800,000,000
1930.....	99	89	6,429,000,000	712,000,000	73,000,000,000
1931.....	81	67	3,433,000,000	399,000,000	62,000,000,000
1932.....	64	46	2,133,000,000	288,000,000	49,800,000,000
1933.....	78	49	2,086,000,000	423,000,000	47,000,000,000
1934.....	79	63	4,275,000,000	606,000,000	52,400,000,000
1935.....	90	71	6,165,000,000	735,000,000	55,100,000,000
1936.....	105	82	6,761,000,000	1,191,000,000	62,800,000,000
1937.....	110	98	6,914,000,000	1,276,000,000	69,300,000,000
1938.....	86	78	4,200,000,000	793,000,000	64,000,000,000
1939.....	105	91	{ 6,700,000,000	{ 1,000,000,000	{ 69,000,000,000
December.....	128	104	{ 6,900,000,000	{ 1,100,000,000	
1940					
January.....	110	98			
February.....	109	98			
March.....	104	98			
April.....	† 102				

¹ Federal Reserve Board index. 1923-25 average = 100.² Bureau of Labor Statistics index. 1923-25 average = 100.³ Corporations reporting net income only.⁴ Statistics of Income.⁵ Department of Commerce, National Income Paid Out.[†] Estimated.[‡] Preliminary.

TABLE 3.—New capital flotations

[Domestic corporate securities only.¹ Governments, refunding, and all foreign securities excluded]

12-year period through 1930:	Years since 1930:		
1919.....	\$2,246,385,636	1931.....	\$1,546,564,173
1920.....	2,563,340,731	1932.....	324,161,625
1921.....	1,700,739,851	1933.....	159,495,280
1922.....	2,211,512,707	1934.....	159,447,749
1923.....	2,635,374,555	1935.....	401,569,958
1924.....	3,029,035,764	1936.....	1,179,025,299
1925.....	3,604,488,597	1937.....	1,224,663,213
1926.....	3,682,846,010	1938.....	867,836,450
1927.....	4,481,893,941	1939.....	369,249,537
1928.....	4,559,374,596		
1929.....	5,779,833,093	Annual average.....	690,716,682
1930.....	4,250,344,697		
Annual average.....	3,395,430,848		

¹ Excluding investment trusts.

Source: Commercial and Financial Chronicle.

TABLE 4.—Excess member-bank reserve balances

[End of calendar-year balances]

1920.....		1931.....	-\$33,000,000
1921.....	\$99,000,000	1932.....	576,000,000
1922.....		1933.....	859,000,000
1923.....	14,000,000	1934.....	1,814,000,000
1924.....	59,000,000	1935.....	2,844,000,000
1925.....	-44,000,000	1936.....	1,984,000,000
1926.....	-56,000,000	1937.....	1,212,000,000
1927.....	63,000,000	1938.....	3,226,000,000
1928.....	-41,000,000	1939.....	5,011,000,000
1929.....	-73,000,000	1940, Apr. 17.....	6,048,000,000
1930.....	96,000,000		

Source: 1920-37, Annual Report of Board of Governors of Federal Reserve System, 1938-40, Federal Reserve Bulletins, February and May 1940.

TABLE 5.—Interest rates, 1929, 1934, and 1939

(Annual averages; percent per annum)

	1929	1934	1939
Open-market short-term rates:			
Prime commercial paper (4 to 6 months).....	5.85	1.02	0.50
U. S. Treasury bills (new issue).....	4.42	.26	.02
U. S. Treasury notes (3 to 5 years).....		2.12	.50
High-grade bond yields:			
U. S. Treasury.....	3.60	3.12	2.36
Municipal.....	4.27	4.03	2.76
Corporate (Moody's Aaa).....	4.73	4.00	3.01
Bank loan rates:			
Commercial loans of city banks:			
New York City.....	5.76	2.45	2.07
7 other northern and eastern cities.....	5.52	3.71	2.87
11 southern and western cities.....	5.93	4.32	3.51
Loans of country national banks:			
Northern and Eastern States.....	6.1	5.5	5.2
Southern and Western States.....	7.1	6.5	6.2
Lower-grade corporate bond yields (Moody's Baa):			
Industrial.....	6.02	5.15	4.25
Railroad.....	5.93	6.33	6.14
Public utility.....	5.76	7.49	4.50
Farm loan rates:¹			
Short- and intermediate-term:			
Production credit associations.....		5.00	4.50
Banks for cooperatives.....		3.00	1.50
Commodity Credit Corporation.....		4.50	4.00
Mortgages:		4.00	3.00
Federal land banks.....	{ 5.50 }	4.50	3.50
Federal Farm Mortgage Corporation.....	{ 6.00 }	5.00	4.00
Large life insurance companies ²	5.63	5.26	4.65
Urban real estate mortgage rates:³			
Home Owners' Loan Corporation (home mortgages).....		5.00	4.50
Insured by Federal Housing Administration (home mortgages).....			4.50
Large life insurance companies ⁴	5.69	5.50	4.50

¹ Average yield on 3 to 6 month Treasury certificates.² Figure for 1938. For banks, available data indicate little change in 1939.³ Interest rates in effect at end of year.⁴ Hearings before the Temporary National Economic Committee (76th Cong., 3d sess.), pt. 10-A, Feb. 12, 1940. Average contract rate on new mortgages after deduction of any payments out of interest for commissions for acquisition of mortgages; for farm mortgages as reported by 12 companies, and for urban real estate mortgages, by 24 companies.⁵ Figure for 1932, earlier figures not available.⁶ Maximum rate, excluding insurance premium of 1/2 of 1 percent.

Source: Federal Reserve Bulletin, May 1940, p. 389.

TABLE 6.—Actual and estimated expenditures

	National defense	Agriculture ¹	Relief ²
1931.....	\$667,000,000		
1932.....	664,000,000		
1933.....	633,000,000		\$20,000,000
1934.....	494,000,000	\$868,000,000	1,833,000,000
1935.....	663,000,000	958,000,000	2,383,000,000
1936.....	880,000,000	840,000,000	2,372,000,000
1937.....	895,000,000	660,000,000	2,527,000,000
1938.....	880,000,000	712,000,000	1,996,000,000
1939.....	1,140,000,000	1,043,000,000	2,573,000,000
1940.....	1,519,000,000	1,316,000,000	1,817,000,000
1941.....	2,736,000,000	954,000,000	1,488,000,000
Total.....	11,271,000,000	7,349,000,000	17,349,000,000

¹ Includes Agricultural Adjustment Program, Commodity Credit Corporation, Farm Tenant Act, Federal Farm Mortgage Corporation, Federal land banks, Farm Security Administration, Farm Credit Administration, Resettlement Administration, drought relief.² Includes Works Projects Administration, Civilian Conservation Corps, direct relief, and supplemental items.

Source: President's Budget Messages, 1930-41. National defense, 1941, revised on basis of emergency defense message of May 16, 1940. Relief and agriculture, 1941, revised on basis of congressional appropriations and tentative allotments by Bureau of the Budget.

TABLE 7.—*Strikes in the United States, 1920-39*

	Strikes	Workers involved ¹	Man-days idle		Strikes	Workers involved ¹	Man-days idle
1920.....	3,411	1,463,054	(?)	1930.....	637	182,075	3,316,808
1921.....	2,386	1,099,247	(?)	1931.....	810	341,817	6,893,244
1922.....	1,112	1,612,562	(?)	1932.....	841	324,210	10,802,033
1923.....	1,553	765,584	(?)	1933.....	1,695	1,168,272	16,872,128
1924.....	1,249	654,641	(?)	1934.....	1,856	1,466,695	19,561,949
1925.....	1,331	428,416	(?)	1935.....	2,014	1,117,213	15,456,337
1926.....	1,635	329,562	(?)	1936.....	2,172	788,648	13,991,936
1927.....	707	329,939	26,218,628	1937.....	4,740	1,860,621	28,424,837
1928.....	604	314,210	12,631,863	1938.....	2,772	698,376	9,148,273
1929.....	921	288,572	5,351,540	1939 ²	2,560	1,200,060	18,000,000

¹ The number of workers involved in strikes in 1926 is known for only a portion of the total. However, the missing information is for the smaller disputes and it is believed that the total here given is fairly accurate.

² No information available.

³ 1939 estimates preliminary; subject to revision.

Source: Bureau of Labor Statistics, Analysis of Strikes in 1938, p. 3.

TABLE 8.—*Federal receipts and expenditures, 1931-41*

Fiscal year	Total receipts	Total expenditures	Gross deficits
1931.....	\$3,189,638,632	\$4,091,597,712	\$901,959,080
1932.....	2,005,725,437	4,947,776,888	2,942,051,451
1933.....	2,079,696,742	4,325,149,722	2,245,452,980
1934.....	3,115,554,050	6,370,947,347	3,255,393,297
1935.....	3,800,467,202	7,583,433,562	3,782,966,360
1936.....	4,115,956,615	9,068,885,572	4,952,928,957
1937.....	5,293,840,237	8,546,379,956	3,252,539,719
1938.....	6,241,661,227	7,691,267,108	1,449,605,881
1939.....	5,667,823,626	9,268,358,031	3,600,534,405
1940.....	8,703,795,000	9,738,608,641	4,032,813,641
1941 ¹	9,150,700,000	9,120,991,570	2,976,231,570
Total.....	47,864,918,768	80,787,396,109	\$33,392,477,341

¹ Estimated; President's Budget Message, Jan. 3, 1940. For purposes of comparison, figures include net transfers to old-age reserve account.

² Deficit will be reduced by the return of an estimated \$700,000,000 from the surplus funds of Government corporations.

Source: Annual Report of the Secretary of the Treasury, 1939.

TABLE 9.—*Federal debt, 1931-41*

	Gross Federal debt	Per capita		Gross Federal debt	Per capita
June 30—			June 30—		
1931.....	\$16,801,000,000	\$135.37	1937.....	\$36,427,000,000	\$261.82
1932.....	19,487,000,000	155.93	1938.....	37,187,000,000	285.43
1933.....	22,539,000,000	179.21	1939.....	40,445,000,000	308.34
1934.....	27,058,000,000	213.65	1940 ¹	43,222,000,000	332.48
1935.....	28,701,000,000	225.07	1941 ¹	\$44,938,000,000	345.68
1936.....	33,545,000,000	261.20			

¹ Estimated, President's Budget Message, Jan. 3, 1940.

² Assumes that \$460,000,000 will be raised in new taxes prior to June 30, 1941.

Source: Annual Report of the Secretary of the Treasury, 1939.

TABLE 10.—*Ordinary Government expenditures*

	1934	1939	1940	Percent increase, 1940 over 1934
I. Legislative, judicial, executive.....	18.0	33.9	35.4	+97
II. Civil departments and agencies:				
Department of Agriculture.....	58.4	192.0	187.9	+222
Department of Commerce.....	17.9	19.9	37.5	+109
Department of Interior.....	48.9	136.8	102.8	+110
Department of Justice.....	31.6	37.1	43.9	+39
Department of Labor.....	10.8	15.5	19.8	+81
Department of State.....	11.1	16.8	20.7	+86
Treasury Department.....	184.0	159.5	166.4	-10
All departments and agencies.....	568.2	915.7	993.5	+69
III. General public works.....	497.6	505.1	687.7	+38
IV. Interest on public debt.....	756.6	940.5	1,050.0	+39

¹ Excludes loans and grants to States, municipalities, and railroads, and Public Works Administration administrative expense; includes Tennessee Valley Authority, public highways, river and harbor work, flood control, reclamation, and public buildings.

Source: President's Budget messages, 1930 and 1941.

The CHAIRMAN. Thank you very much, Mr. Alvord. Senator Thomas?

STATEMENT OF HON. ELMER THOMAS, UNITED STATES SENATOR FROM THE STATE OF OKLAHOMA

Senator THOMAS. I had not seen this bill until this morning. I do not know whether the amendment that I have in mind would be in order.

For years we have been producing asphalt, rock asphalt, in my State. It has not been heretofore considered in tax legislation. I desire to submit for the record a proposed amendment, placing rock asphalt and sand asphalt on the same status as sulfur, and accord asphalt the same treatment in tax legislation. I will submit the amendment for the record, and shall submit a statement justifying the proposed amendment.

(Proposed amendment and statement in support thereof are as follows:)

The amendment proposes a change in the text of section 114 of the Revenue Act of 1936.

The exact change is as follows:

In the second line of paragraph (2) of subdivision (b) of section 114—

First. Change the wording in parenthesis to read as follows: "(other than metal, coal, sulphur, rock asphalt, or sand asphalt mines)."

Second. In line 4 of paragraph (4) of subsection (b) of section 114, after the word "sulphur" add a comma and insert "rock asphalt and sand asphalt."

The effect of the amendment, if agreed to, would give mines producing rock asphalt and sand asphalt the same status in our tax laws as is now accorded to mines producing sulphur.

I am not advised of the number or location of asphalt producing mines; however, in my State of Oklahoma we do have deposits producing asphalt which is used for highway and street construction. These asphalt deposits are located at various depths underground; hence, they have to be discovered the same as petroleum and when once discovered they have to be mined something after the plan by which coal is produced. Like oil, when an asphalt deposit is discovered it is impossible to ascertain the amount of such deposits; hence, the hazard in drilling for asphalt is comparable to the hazard in drilling for oil.

The present law deals with depletion and fixes the percentage allowable for deduction. Because of the lack of time I shall not go into this phase of the matter. I know very few deposits of asphalt; hence, the amount of tax involved

in this amendment is very small, but to the persons engaged in the asphalt-producing business the depletion allowance is a most important item.

I am asking the committee to consider amending the existing law by the insertion of the words "rock asphalt and sand asphalt" in section 114, as indicated, so that this mineral may have the same status in our tax system as sulphur.

The CHAIRMAN. Mr. Carroad?

STATEMENT OF KENNETH CARROAD, ACTING CHAIRMAN AND SECRETARY, NATIONAL TAX COMMITTEE, THE NATIONAL LAWYERS GUILD, NEW YORK CITY, N. Y.

Mr. CARROAD. After hearing the comments of Mr. Alvord, I think I have a much more cheerful presentation for you.

I think our guild would recommend more taxes, and we will try to confine ourselves to the merits of some of these additional tax proposals.

I do think the real issue before Congress is not so much whether we have more revenue and less indebtedness, or more indebtedness and less revenue, as it is to get the greatest possible amount of revenue from those who are best able to pay it. In other words, the real issue is not only who pays the tax, but who absorbs this tax, and upon whom does the burden fall?

We would like to propose three plans.

One is a munitions tax, the other is an abnormal profits tax, and the third is the elimination of exemptions on Government securities, both State and Federal.

There isn't much need to discuss the third proposal, because I am sure all of you are familiar with it. The new 5-billion-dollar bond issue ought to be made taxable by Senate amendments.

But we would like to take up a discussion first of the munitions tax, and then the abnormal profits tax.

Senator BARKLEY. Is it "abnormal" applying to the tax or the profits?

Mr. CARROAD. Well, sir, I think under the proposal possibly it will be applicable to both.

By "abnormal profits" incidentally, we have in mind the excess profits over a so-called normal profit, which is sometimes referred to as a war tax, but since we are not in war yet, and I trust we won't be, we have used the expression "abnormal profits" to distinguish it from the type of tax that might be necessary if this country actually went into war.

Senator HERRING. I should like to ask the witness this: Is this National Lawyers Guild, the guild that all these reputable lawyers are resigning from?

Mr. CARROAD. Yes, sir.

Senator HERRING. Is that the one you represent?

Mr. CARROAD. Yes, sir.

I might say that possibly directly after my presentation—

The CHAIRMAN (interposing). I don't think that you meant all the reputable lawyers were resigning from it?

Mr. CARROAD. Well, I had better take that back. I think some reputable lawyers have resigned from it, possibly with good cause, and possibly not, I don't know.

I may state parenthetically that after the work on my tax committee is completed—and I think we have good tax proposals—I probably will resign as well. [Laughter.]

However, I should like to make clear that good sound tax proposals from those of us who are tax lawyers in the guild have nothing to do with the social implications and all the other programs that we hear so much about today as coming from the guild.

The CHAIRMAN. Let's have your proposals.

Mr. CARROD. Let's take first the munitions tax. It would seem to me that the country could save a great deal of money in its defense program by eliminating the excess profits on munitions, and a very simple proposal would be an extension of the Vinson Act and the Vinson-Trammell Act. In other words, I think we should have a tax that would take away all the profits in excess of 10 or 12 percent on everything which is denominated munitions or armament or essential defense needs.

I should also like to suggest that the determination of what is an essential defense need, or what constitutes munitions, should possibly be made through the President; that is through the Executive, but with the advice of the present Advisory Defense Commission. In other words, if our Advisory Defense Commission feels that uniforms, for example, or bullets, or cannon, are an essential defense need, then that type of material would be subject to a 100-percent tax in excess of 10 percent of the net profit. In other words, this is nothing more than an extension of the Vinson Act or the Vinson-Trammell Act to all defense needs.

I think we would see from such a proposal, two advantages. One is, it would be a lot cheaper for this Government to arm itself and arm itself adequately to defend itself. Also, it would be wholly unfair to the great bulk of this country and the taxpayers in it, if a group such as the munitions makers—and I don't want to sound jingoistic—I think we all understand that there are groups of industries who are concerned with war and war manufacture, that they should carry an equitable part of our entire tax load, and I should imagine that under normal circumstances a 10-percent net profit would be a decent return for those industries.

I should like now to go to the abnormal-profits tax proposal.

I think all of us appreciate the need for revenue. I have no doubt that this committee and the House Ways and Means Committee has been belabored with much talk about putting a tax burden on the ultimate consumer and having the poor people pay all the taxes while the rich people are paying very little of the increased taxes.

Of course, today with excise taxes being increased under the present House proposal, there is no doubt that a great portion of that tax burden, no matter who *actually* pays it, will fall on the ultimate consumer. There is no doubt, too, that such a little tax, like the tax on transfer of bonds and stocks will fall wholly on the rich.

However, there is one group which should carry part of this load, and that is those people who are profiting from war activity. I should like to make clear that by "war activity" I don't mean munitions manufacturers. I mean possibly those who indirectly supply them and those who benefit from increased industrial activity, and the like.

The proposal itself would seem to me to be equitable because it would help to take additional taxes from those who are best able to pay, in order to compensate for those industries who have suffered from the war activity.

Now we have heard from the tobacco trade and from the fruit people and from the cotton trade, from our exporters, that is, people who export goods out of this country—All those people have suffered. A great many of my own clients who are importers have suffered from the war. If you put on only a supertax, you are making those people pay approximately 10 percent more tax, which is perfectly fair. But you are making other people pay only 10 percent additional tax who have gotten a direct or an indirect benefit from all this war activity.

So it is rather hard to see why those who benefit should not pay this abnormal-profits tax.

Now the proposal we have in mind would be comparatively simple to administer.

In the first place, it was our thought not to have the tax on individuals or on partnerships, on the ground that the heavy surtaxes already take care of that problem. There isn't any point in putting in more tax there.

We also thought we would like to exempt corporations whose net income is less than \$25,000, possibly \$20,000. That would eliminate hundreds of thousands of corporations who have such little income that it would hardly be worth the expense of collection and auditing those returns. I say that partially from my own experience in the Bureau several years ago, and from my work representing private clients today. Sometimes the expense of collection isn't worth the revenue that you get.

We also had in mind that in order to try to satisfy conflicting theories we would use a combination of the average annual earnings theory that you gentlemen probably have heard so much about, and the invested capital theory. In other words, in the last World War we had a tax that was generally based on invested capital, and that tax was limited to various percentages of the return which you got.

It was our thought that this tax would have as a minimum, a 6-percent return on invested capital, and as a maximum, a 9-percent return on invested capital, so that if you got more than 9 percent of invested capital back as a net income, you would have to pay this abnormal-profits tax in addition to your corporate normal tax.

Now I should like to explain where the 6 percent comes in, because there I think is the nub of the whole problem.

It would seem that tax should include a base for average annual earnings. For example, if we took the years 1935 through 1938, you would have 4 years which are both good and bad for most industries in general. As I understand it, 1935 wasn't a very good year; 1936 and 1937 were pretty good years; 1938 was a good year and a bad year, depending upon certain inventory problems for many industries, such as the cotton industry and other types of industries that are affected by the fall in commodity prices, or were affected by the fall of commodity prices in 1937, which took effect in 1938—well, getting back to those 4 years as a base, if you would average out those profits, that average annual earnings would become the base for your tax.

So if, over 4 years' time, you had a net average income of \$2,000,000, then that would become your base.

Now if your average annual earnings of \$2,000,000 was in excess of 9 percent of your invested capital, then you would be limited to 9 percent. But if it were more than 6 percent, you would be allowed to use the average annual earning; at the same time no corporation would have to use less than 6 percent.

I should like to make one qualification of that. I think we all know, too, that there are certain industries which are particularly affected by an overcapitalization problem, such as the steels, the railroads, and the utilities. While it isn't the place here in 15 minutes to take up all of these complex problems to which some of the lawyers in the committee have given 9 months—we have been sitting on this thing now for 9 months—I do feel that that could be handled as a matter of detail at some future time.

But in essence the proposal is, I think, rather simple.

I would also suggest that the rates of tax be graduated; in other words, in effect it would be a tying up of surtaxes to the increase in income over the normal tax. There is no need for elaboration on that point.

I should like to add one more point. Many of the members of the committee were much worried about the problem of those corporations where capital is not a material income-producing factor. Of course, it is perfectly plain that if you have a selling agency, a selling corporation, or a corporation that sells only services, such as a management corporation, they have no invested capital. Consequently this problem as to a minimum of 6 percent and a maximum of 9 percent on invested capital must necessarily be limited to those corporations where capital is a material income-producing factor.

I should also like to cover a great weakness which possibly might become a loophole, and that is the question of corporations who are newly formed; for example, if you have a low capital structure and you think you may make a lot of money, you might start a brand new corporation. It was our thought that the law would provide that the maximum return on capital would be 6 percent for a new corporation. That would close the loophole of trying to take an old group of corporations and permit them to use a new corporate entity as an escape from the tax.

I should also like to refer very briefly to special problems which only need mention here. Of course a great many corporations have gone through 77B, through the wringer, through bankruptcy, through technical reorganization, and as a result, for net income-tax purposes, for ordinary tax purposes, their invested capital may be far below, its true net worth, or the true appraised value of the corporation. It was our suggestion, to overcome those problems by the establishment of a "relief and hardship" committee; in other words, to include a section in the law for "relief and hardship" cases, and to have an independent committee, named by the President, probably including tax men and other people who are competent in industrial matters; to determine these cases. It was the consensus of opinion among our own committee that it would probably be unfortunate to let the Treasury Department pick the entire "relief and hardship" committee. My own experience, for example, with the United States Processing Tax Board of Review, with the Unjust Enrichment Tax section, the Processing Tax Refund Division and other divisions of that type—seemed to indicate that the Treasury doesn't construe relief and hardship in the broad, equitable sense, but in rather a narrow, technical sense.

I don't believe that it would be sound to permit such interpretations to creep into an abnormal or a war-profits tax, because those technical definitions for tax purposes or for ordinary common-law purposes, have no place in a system which is intended as a temporary tax, and

which is intended to be an equitable tax; in other words, this isn't going to be a permanent tax measure, and I think it ought to be administered not so much leniently as *equitably*.

There will be a great many problems that come up, and I should imagine that that relief and hardship committee should be absolutely independent in its own judgment.

I should like to cover a few more points, and then I am done.

I think all of you know, too, another problem comes up over the exclusion of capital losses. We have today what some of us consider a very liberal capital-gains-and-loss provision; in other words, you are permitted to offset your capital losses against current income. It would seem to me that the capital losses should not be considered in determining your abnormal-profits income, because it would be too ready a loophole to sell out obsolete plants and other capital assets at losses in order to reduce your income temporarily for a few years' time.

Likewise, the definition of "invested capital" may be a difficult administrative problem. We also have to consider the special treatment of depreciation where the rate of production has been accelerated. Many plants have changed from a one-shift system to a three-shift system.

It is also expedient to consider the right to file "consolidated returns" for the special purposes of the abnormal-profits tax and yet to deny such privilege for normal corporate tax purposes. The abolition or revision of our capital-stock tax and affiliated excess-profits tax might also be necessary, in view of the abnormal-profits tax proposed.

Senator BAILEY. This gentleman seems to be a very excellent gentleman, and well informed, but we have a definite bill here, and he is talking about general tax theory. Would it not be well for you to appear before us next January when we get ready to write the bill, rather than to discuss tax theory now? We have no time to go into that.

Mr. CARROD. That is perfectly true.

The question comes up about one point on which I do agree with Mr. Alford and Secretary Morgenthau. After all, the bill next year is going to create a question of uncertainty for an entire year's time. I don't really believe that it is fair to impose upon corporate taxpayers and other taxpayers such uncertainty for an entire year's time. It would seem to me that if Congress is going to sit for the rest of the summer, that these proposals should be taken up now. In other words, we are suggesting that if you *must have* a supertax, if you *must have* excise taxes, if you *must have* these taxes imposed upon the great bulk of the people, then it is only fair to put this munitions tax upon those who make munitions and essential defense needs, and also an abnormal or a war-profits tax upon those corporations who are benefiting from the war.

I agree with you fully, if the bill were passed next year, that no great harm would be done with respect to abnormal profits. But certainly with respect to munitions it would seem to me to be a disaster if our Congress did not pass a munitions tax, extended in the same fashion that the Vinson Act and the Vinson-Trammel Act is phrased today. We are ordering our materials now, we can't wait until January to pass such a law in an attempt to recapture those taxes. First of all, you may lose a great deal of the revenue, and, secondly, it is

going to be hard to levy a confiscatory tax—because it is only a 100-percent tax—8 or 10 or 12 months later.

The abolition or revision of our capital-stock tax and affiliated excess-profits tax might also be necessary in view of the abnormal-profits tax proposed.

I agree with some of the members of the committee who stated that the public seems to be willing to take up tax matters now. It would be advisable to take up these matters at this time, although I should also suggest that it may not sit well with the bulk of the people to enact taxes which are a burden upon the bulk of the people, the excise taxes, gasoline, tobacco, all the other taxes—I don't have to enumerate them—and then to have only a promise from the committee—and I trust the promise, it isn't a question of the validity of the promise—but to have a promise from this committee and a promise from the House Ways and Means Committee, that next year they will try to rectify this gap or loophole by hitting those people who are profiting from the war.

It would seem to us that as much revenue as can be obtained from these new taxes, supertaxes, munitions taxes, our abnormal-profits tax, and the like, should not be limited to defense needs. In other words, if this war situation in Europe were to end suddenly, frankly, I am in complete disagreement with Mr. Alvord who spoke here a few minutes ago. It seems to me that such taxes could equitably be used for the social needs of the country without regard to whether they are expended for defense funds.

However, I do think they ought first to be earmarked for defense funds and the surplus thereafter to be used for the general welfare of the country.

Thank you very much.

The CHAIRMAN. If you desire to send a brief down it will be given proper consideration, in connection with this whole subject.

Mr. CARROD. Thank you very much, I may do that.

The CHAIRMAN. The next witness is Mr. Seidman, of the New York Board of Trade.

STATEMENT OF M. L. SEIDMAN, CHAIRMAN, FEDERAL TAX COMMITTEE OF THE NEW YORK BOARD OF TRADE, NEW YORK CITY

Mr. SEIDMAN. The New York Board of Trade is in full accord with the purposes of this bill. We believe that our first line of defense is a sound economy. For that reason, this bill is commendable in a number of important respects.

To begin with, it recognizes a principle we have frequently stressed before this honorable body, namely, that to make our income taxes produce much greater revenue than at present, we must do so through a broadening of the tax base. The bill also gives evidence of a recognition that our top income-tax brackets have reached the point of diminishing returns; hence cannot be increased in the same proportion as on income in the lower brackets.

Finally, this bill recognizes, at least to a partial extent, that expenditures of a nature so extraordinary as those with which we are now confronted, having been made from borrowed money, must be specifically tied in with a self-liquidating debt arrangement, so that the taxes paying for them will stop automatically when the debt is paid.

These are all principles for which business has been contending as necessary in any sound tax economy. To the extent that they are recognized in this bill, therefore, we think you are definitely headed in the right direction. It does seem to us, however, that this bill should extend each of these principles much beyond what is now proposed, with beneficial effect upon our economy and upon the results for which this bill is intended.

Take the matter of broadening the income-tax base. The aim should be to bring in as many new taxpayers as possible and to increase the revenue from that large number of persons who, while filing tax returns in the past, have had to pay little or next to nothing in tax.

Nearly all of us pay indirect Federal taxes, even if none is paid directly. This same bill that is now before you increases substantially many of these indirect taxes. They are, to a large extent, hidden taxes paid by the great mass of people in their cost of living, without knowing that they are in fact paying taxes.

We have on numerous past occasions stressed before you the desirability of eliminating these hidden taxes in the interest of a sound national economy. We believe that the emphasis placed on hidden taxes in recent years has been an important element in the skyrocketing of our national debt.

I know that direct taxes are said to be politically unpalatable, particularly in an election year. But it is the exception that proves the rule. I am convinced that the present state of mind of our people is such that they are anxious to do their direct part in meeting our national emergency. Here, therefore, is a rare opportunity to do what most of us agree cannot much longer be postponed—a real broadening of the income tax base.

The CHAIRMAN. How much further would you go than what is proposed in this House bill?

Mr. SEIDMAN. I cover that in my memorandum.

The CHAIRMAN. All right.

Mr. SEIDMAN. Considered from that point of view, this bill does not scratch the surface of the possibilities. Exemptions should be materially lowered, the normal tax should be increased, and the surtax increase should start much below the \$6,000 point now proposed.

Senator CONNALLY. How much ought it to be lowered?

Mr. SEIDMAN. I would take the \$800 exemption to the single individual as the basis for the exemption.

Senator CONNALLY. That is what we have taken.

Mr. SEIDMAN. Now a married man who has a wife should be given credit for a dependent—\$400, the same as any other dependent. So that a married person with two children would get a \$2,000 exemption. A married person with no children would have a \$1,200 exemption.

That is where the real national income lies and there also lies the basis for a sound national tax economy. As an offset to these tax increases, the hidden taxes should not be further increased at this time, and should ultimately be largely eliminated. That is one end of the problem.

On the other end of the income tax scale, we know that tax rates go up as high as 79 percent. To this most States add a State income tax, sometimes reaching as high as an additional 15 percent.

Senator GEORGE. I think we only caught but one taxpayer in the 79 percent bracket, didn't we?

Mr. SEIDMAN. I can readily understand why you can't catch them, you have got the door of tax exemption wide open, tax-exempt securities.

Senator CONNALLY. There was testimony before our committee some 2 or 3 years ago that there was only 2½ percent of the tax-exempts in the hands of people who paid those higher bracket taxes.

Mr. SEIDMAN. That may be so, that was some years ago. There is more inducement these days to go into tax-exempts.

Senator KING. Isn't that in part due to the low rate of interest paid by the banks and because of the lack of invitation or lack of encouragement to go into new business or expand the existing business?

Mr. SEIDMAN. Undoubtedly so, those are all elements.

As a result, income beyond a certain point has in the past been almost completely confiscated, and under the proposed increases will be more completely confiscated.

Now, I'll grant you this is not the time to quarrel about confiscation of income, and I don't believe anyone subject to these tax rates will be heard to complain, especially if they can escape through the open door of the tax-exempt security. I only want to point out that we have found, by past experience, that such a tax arrangement unfortunately stalls our entire economy. There is certainly a point in the taxing of income beyond which free enterprise and the profit system simply will not function. If, therefore, we are going to see through this national-defense program under our free-enterprise system, we must find exactly where that point is and stop progressive tax rates right there. It is our conviction that that point has long been passed in our income-tax rate structure.

We accordingly suggest that you limit the proposed increases to such cases where, under the present law, income is not already taxed, say, 50 percent. This, it seems to us, should be done in the Government's self-interest, if for no other reason, since greater revenue is bound to be the ultimate result.

As to earmarking revenues under this bill, we note that while the bill is intended to raise about a billion dollars, only 650 millions of it is to be applied to debt liquidation. The remaining 350 millions would, therefore, go into the general fund and be available for ordinary Government expenditure purposes.

We are firmly convinced that additional taxes at this time can only be justified by national defense needs and that, therefore, every single dollar of additional taxes raised under this bill should be earmarked for that purpose.

Senator CONNALLY. Before this emergency arose, weren't you all advocating balancing the Budget mighty strong?

Mr. SEIDMAN. We believe the Budget ought to be balanced without additional taxes.

Senator CONNALLY. How are you going to do that? You ought to run for Congress, that is where you belong, over in the House.

Mr. SEIDMAN. Well, it would be nothing to look forward to this summer. I think you are going to have a hot time of it.

Senator CONNALLY. Talking about balancing the Budget without raising any taxes when we have a \$45,000,000,000 debt—of course we are going to have to balance the Budget sometime, and I have understood that the chamber of commerce that you represent, and have been for years here representing, has always hollered about balancing the

Budget. Now you say that except for defense there is not another dollar of tax justified.

I think we have got to raise taxes whether we have got an emergency or not. I think we have got to raise taxes whether we prepare to defend ourselves or not. You don't think so?

Mr. SEIDMAN. I believe, Senator Connally, that if the Government showed a determination to reduce expenditures, the people of this country would be only too happy to bear a heavier burden of taxation, but there is no use, the more you raise taxes, you spend just twice as much.

Senator CONNALLY. Oh, no.

Senator BARKLEY. Won't you come back here in January and give us an idea of what expenses we can reduce? We will give you an opportunity then.

Senator CONNALLY. We will cut out those underpasses in New York, under the Hudson River, that we financed, and cut out a lot of the W. P. A. for New York City, that gets more capita than any State in the Union. Cut that all out and that will help. But you are not going to be down here advocating anything like that, of course.

Mr. SEIDMAN. I can only say that 7 or 8 years ago our national expenditures were about one-third of what they are today, and we still got along pretty well, and there does seem that there ought to be some way of preventing these Federal expenditures from skyrocketing.

Under this tax bill, all of us will have to tighten our belts. I believe, therefore, that business is justified in asking that the civil departments of our Government should do likewise.

Some of this vast increase is admittedly due to expenditures brought on by the depression. But, we are about to spend billions of dollars on a defense program, perhaps several times the 5 billions now contemplated. While such expenditures are a mighty poor basis for a business boom, they at least ought to have the effect of alleviating our unemployment problem and to that extent make unnecessary some of the present huge expenditures in that direction. We ought to be able to find a formula or a method whereby further increase in our taxes and in our debt should be definitely linked up with a decrease in our nondefense Federal expenditures. Whatever that formula is, this bill should provide for it. In that way, perhaps, we may hope to approach financial sanity at some future time.

Admittedly, we have before us a rakeshift, hurriedly drawn tax measure and no time may be available for refinements if Congress is to adjourn shortly. Yet, there is nothing in any of the proposals that I have here made which cannot be quickly written into this tax bill.

I cannot help but feel, however, that this bill falls woefully short of our present needs. I question the wisdom of postponing to the next Congress a complete revision of our revenue structure. That is a job, as you know, which has been shifted from Congress to Congress. Always it is admitted that this job needs to be done, but always it is too late to do it in the session about to close. It would appear that the Treasury has already made an ample study of the subject and that it is ready and willing to see this matter through if Congress is willing to do so. If this job could be done now, much would be gained and business would know where it is at.

Industry can try to adjust itself to oppressive taxation, but it has found it impossible to adjust itself to uncertainties. We all know that

in spite of the 5-year plan which this tax bill ostensibly embodies, important changes will soon again have to be made. Everyone who is for this bill admits that it is a temporary stopgap and a makeshift. What the coming changes will be, nobody can say. In addition, business has been put on notice that the next Congress will be asked to enact an excess-profits tax to be imposed retroactively on 1940 transactions.

Senator BAILEY. Mr. Chairman, has this gentleman's time expired?

The CHAIRMAN. He is about through.

Senator BAILEY. I wanted to move that he file his paper.

Senator KING. I am very much interested in his suggestions, many of them are very wise, and I sympathize with them.

The CHAIRMAN. Proceed.

Mr. SEIDMAN. How can business adjust itself and function under such uncertainty? Is not this bound to slow up our defense program? Would it not therefore be wiser for Congress to give its immediate attention to a more permanent revision of our tax structure?

Perhaps you gentlemen know best. If you should conclude that it is not feasible or practical at this time to go beyond the presently proposed changes, then I would like to say to you gentlemen that at least this bill should carry a provision for an interim study and an assured, comprehensive tax revision by the next Congress.

This, we suggest, should take the form of the creation of a representative commission charged with the duty of a careful study of this entire subject, including the coordination of Government revenues with Government expenditures. In this regard, I direct your attention to Joint Resolution 483 introduced by Congressman Celler on March 5, 1940, which calls for the establishment of a tax commission for the broad purposes we have in mind. This bill has the approval of the New York Board of Trade, the American Institute of Accountants, and other business and professional bodies. I am here submitting a copy of it and respectfully request that it be made part of this record.

(The joint resolution referred to is as follows:)

[H. J. Res. 483, 76th Cong., 3d sess.]

JOINT RESOLUTION Establishing a Federal Tax Commission, and for other purposes

Resolved by the Senate and House of Representatives of the United States of America in Congress assembled, That it is hereby declared to be the policy of Congress—

(1) To establish a stable, more permanent Federal tax structure, so as to avoid frequent changes in tax laws and minimize the adverse effect of changes in tax laws on individual initiative, investment, and employment;

(2) To raise the necessary revenue for the support of the Government in the most equitable manner, giving due regard to the principle of ability to pay, benefit derived, the welfare of the Nation and its citizens, and the undesirability of hidden or indirect taxes;

(3) To simplify the Federal tax system, including the forms of taxation, the statement of the law, and the methods of administration;

(4) To alleviate hardships and inequities in the application and administration of the internal-revenue laws;

(5) To coordinate the Federal tax system with those of the State and local governments to the end that double taxation may be minimized and overlapping or needless cost of administration reduced;

(6) To equalize taxation and prevent tax evasion and avoidance; and

(7) To make such other changes as will improve the Federal internal-revenue system.

SEC. 2. There is hereby established a Federal Tax Commission (hereinafter referred to as the "Commission"), to be composed of eight members, as follows:

(1) One member who is an officer or employee of the Treasury Department to be chosen by the Secretary of the Treasury;

(2) Seven members (none of whom holds any office in the Government of the United States or is engaged in the activities of any political party) to be chosen by the President, by and with the advice and consent of the Senate, one of whom shall be representative of agriculture, one of labor, one of individual taxpayers and consumers, one of industry and finance, one of lawyers, one of certified public accountants, and one of economists.

SEC. 3. It shall be the duty of the Commission—

(1) To make such investigations as it may deem necessary or advisable in order to carry out the purposes of this joint resolution;

(2) To publish from time to time, for public examination and analysis, as it deems desirable and appropriate, proposed measures for carrying out the policy of Congress herein expressed; and

(3) To report to the Congress from time to time, and in any event not later than January 3, 1943, the results of its investigations, together with such recommendations as it may have to make.

SEC. 4. (a) The Commission shall meet and organize as soon as practicable after at least a majority of the members have been chosen, and shall elect a chairman and a vice chairman from among its members, and shall have power to appoint and fix the compensation of a secretary and such experts and clerical, stenographic, and other assistants as it deems advisable. A vacancy in the Commission shall not affect the power of the remaining members to execute the functions of the Commission, and shall be filled in the same manner as the original selection.

(b) The Commission is authorized to hold hearings and to sit and act at such places and times, to require by subpoena or otherwise the attendance of such witnesses and the production of such books, papers, and documents, to administer such oaths, to take such testimony, to have such printing and binding done, and to make such expenditures, as it deems advisable. The cost of stenographic services in reporting such hearings shall not be in excess of 25 cents per hundred words. Subpenas for witnesses shall be issued under the signature of the chairman or vice chairman.

(c) The Commission is authorized to utilize the services, information, facilities, and personnel of the departments and agencies in the executive branch of the Government, of the Joint Congressional Committee on Internal Revenue Taxation, and of the office of the Legislative Counsel.

(d) The Commission shall have the same right to obtain data and to inspect returns as the Committee on Ways and Means of the House of Representatives or the Committee on Finance of the Senate, and to submit any relevant or useful information thus obtained to the Congress.

(e) The members of the Commission shall serve without compensation for such service, but they shall be reimbursed for travel, subsistence, and other necessary expenses incurred by them in the performance of the duties vested in the Commission.

(f) There is hereby authorized to be appropriated so much as may be necessary to carry out the purposes of this joint resolution. Amounts appropriated for the expenses of the Commission shall be disbursed by the Division of Disbursement, Treasury Department, upon vouchers approved by the chairman or vice chairman.

(g) All authority conferred by this joint resolution shall terminate on the expiration of three years from the enactment of this joint resolution.

Senator CONNALLY. Your board drew that bill, didn't it?

Mr. SEIDMAN. No, sir.

Senator CONNALLY. And gave it to Mr. Celler to introduce?

Mr. SEIDMAN. No, sir; our board had nothing to do with the drawing of the bill. We are responsible for some of the recommendations in the bill.

Senator CONNALLY. I don't mean that you wrote it out on the typewriter, but I mean that you drafted the provisions of it, that is all.

The CHAIRMAN. All right; thank you, Mr. Seidman.

There are two Congressmen who wanted to appear briefly, as I understand.

We will first hear from Congressman Cooley, of North Carolina.

**STATEMENT OF HON. HAROLD D. COOLEY, A REPRESENTATIVE
IN CONGRESS FROM THE STATE OF NORTH CAROLINA**

Mr. COOLEY. Mr. Chairman, members of the committee, I shall neither burden the record nor bore this committee with a detailed discussion of the plight of our American tobacco farmers. I am, however, happy to have this opportunity to appeal to this committee, as to a court of last resort, in behalf of those who live and labor and earn their livelihoods upon the tobacco farms of the Nation.

Many great crimes may be committed in the name of national defense, but there is certainly nothing in the present emergency which justifies the offense which is about to be committed against our tobacco farmers. The tobacco farmers of our Nation were the very first to be sacrificed upon the altars of world peace. They were the first to feel the ill effects of the present war in Europe. When war broke out in Europe last fall the British buyers withdrew from our markets, and as a result of their withdrawal our markets were closed and all business in the tobacco-growing areas was paralyzed and at a standstill. Until last year approximately 60 percent of our flue-cured tobacco crop was annually exported. As a result of the war we have lost our foreign trade, and our tobacco farmers are now on relief. But for the relief which was given to us last fall by the Federal Government, we would have faced bankruptcy and distress. When the British buyers withdrew from the markets and our markets were closed, intimidated, and coerced by a cruel situation and by circumstances over which they had no control, our farmers agreed to reduce the production of flue-cured tobacco from nearly 1,200,000,000, which was grown in 1939, to 600,000,000, which they will produce in 1940—a sacrifice of 50 percent of their production.

Upon the farmers agreeing to curtail production, the Commodity Credit Corporation made an arrangement with the British companies, under which the British buyers returned to the market and purchased their normal requirements. The British companies purchased and the Commodity Credit Corporation paid for approximately \$40,000,000 worth of tobacco. The British companies now have an option upon the 175,000,000 pounds of tobacco which was purchased under the business agreement, but apparently they will not exercise the option. This tobacco is still hanging over our market. We now have a 350,000,000-pound surplus of flue-cured tobacco; we have cut our crop by 50 percent; a British embargo has been imposed upon American tobacco; we have lost our foreign market, and the future is dismal and distressing.

We have nothing left but our domestic market, and now in the name of national defense we are told that even the domestic market must be further impaired and burdened by an additional tax, which is unjust, unfair, unreasonable, unwarranted, and intolerable.

No man can truthfully say that the entire burden of this tax is borne by the consumer, and I shall not be foolish enough to suggest that its entire burden is borne by the farmer, but I do know, and this committee and this Congress knows, that an additional tax will not increase consumption but, on the other hand, is calculated to decrease consumption and restrict our marketing of tobacco. If you would lift the entire tobacco tax no American tobacco farmer would ever again extend his hand and ask for charity and relief at the hands of his Government. Every right-thinking man will agree that if the tax

burden is lifted consumption will increase and prosperity will return to the tobacco farms of the Nation.

This in itself is convincing and conclusive evidence that the burden is largely borne by the farmers. On the other hand, if you double the tax, any intelligent person knows that consumption will be decreased and by the same token the additional tax proposed in the pending bill will be reflected in the price received by the farmer when he offers his crop for sale on the warehouse floor.

Oh, yes, I know we are told that tobacco is an evil luxury, but even if it is a luxury, why not tax the 10,000 other luxuries used and enjoyed by our people before dealing the death blow to our tobacco farmers. Tobacco may be a luxury to the consumer but it is a necessity to those whose livelihoods depend upon its production.

I appreciate the fact that "The power to tax is the power to destroy" and that is just about what this tobacco tax is doing to the tobacco farmers.

How in the name of high heaven can it be justified. About the only excuse that can be given is that it is the easy and the lazy way to raise revenue. Just let me give you these figures: The American consumer pays \$1,750,000,000 annually for tobacco; the Government collected last year in excess of \$580,000,000 in tax; the tobacco farmers received a gross income of only \$175,000,000 with which to pay for the cultivating and housing of the crop and for a thousand and one other things which they have to buy. No wonder there is a "Tobacco Road" on every tobacco farm in the Nation.

Now is the time to do something about the tragic treatment of those who till and toil on our tobacco farms.

What a ridiculous picture all of this presents. One agency of the Government putting up millions to save our people from bankruptcy and despair, and here in this bill is a proposition which contemplates putting an additional burden of \$87,000,000 upon the backs and brows of the self-same people. Sixteen cents per pound additional tax upon a commodity which sold on the market last year for 15 cents per pound. The 16 cents per pound additional is to be added to the \$1 per pound which is now being collected, making a total of \$1.16 per pound on a commodity which sells at public auction to the highest bidder for only 15 cents per pound.

Senator KING. The Government would lose that—would it not?—because it would make those who owe it less able to meet their obligations, so indirectly the Government would have to pay it.

Mr. COOLEY. I think you are entirely correct—

The CHAIRMAN (interposing). We don't want to cut you off, Congressman, but we have given more time, in these short hearings, to the tobacco interests, and the various questions presented by it, than anyone else. We have got some gentlemen here who are from a distance, and we are going to close these hearings this morning. So I hope you will be brief.

Mr. COOLEY. I will be brief, and in half a minute will finish.

The tobacco farmers of North Carolina and the others for whom I speak are patriotic, loyal American citizens, and they are perfectly willing to bear their fair share of the tax burden of the Nation. In defense of this Republic and its ancient institutions they will offer themselves and their sons and farms and their future fortunes, but

they should not be expected to bear in silence this unfair burden which is about to be imposed upon them.

I urge this committee in their behalf and in the name of justice to lift this burden from their backs and to look elsewhere for the needed revenue.

Senator KING. Did you make an appeal to the Ways and Means Committee of the House?

Mr. COOLEY. We made an earnest appeal.

Senator KING. They turned you down?

Mr. COOLEY. Yes; and we went then before the Rules Committee and asked for an open rule which would permit the House to express its own views with regard to this tax, and we came out with a "gag rule" which would not permit us to offer any amendment to the bill.

Senator KING. Theoretically, the House is supposed to be more responsive to the demands of the people than the Senate, but you have come down to the Senate?

Mr. COOLEY. Yes; and we hope you will relieve us.

I would like permission to file for the record a statement by Congressman Burch, of Virginia, which he prepared.

The CHAIRMAN. It may be inserted in the record.

(The statement is as follows:)

STATEMENT OF HON. T. G. BURCH, REPRESENTATIVE IN CONGRESS FROM THE FIFTH CONGRESSIONAL DISTRICT OF VIRGINIA, BEFORE THE FINANCE COMMITTEE OF THE UNITED STATES SENATE ON JUNE 14, 1940

Mr. Chairman, members of the committee; I fully realize the necessity of raising additional revenue to provide for the expenses of national preparedness and defense. Nevertheless, my intimate knowledge of the sad plight of the tobacco growers impels me to oppose the section of the pending bill which provides for an increase in the tax on cigarettes and tobacco products.

The present heavy excise taxes on manufactured tobacco and tobacco products tend to burden and depress the industry and have an ill effect on that large portion of our population engaged in the production of tobacco. In the flue-cured area alone—a portion of which I have the honor to represent—more than 300,000 farm families are dependent upon the proceeds of their tobacco crops for a living. The crop produced in the year 1939 netted the growers not quite 15 cents per pound. This bill will levy an additional tax of 16½ cents per pound—a figure in excess of the price the farmer received for his product in 1939.

Tobacco has been heavily taxed for many years and is the only agricultural commodity—with the exception of oleomargarine—upon which an excise tax is levied. Tobacco taxes have poured billions of dollars into the Federal Treasury. In the fiscal year ended June 30, 1939, the revenue from this source amounted to \$580,159,206—twice the sum paid to the farmers who labored to produce the crop. In the depression years from 1929 to 1933 the revenue derived from tobacco each year was approximately, \$400,000,000. In 1930 it was as high as \$450,000,000.

A subcommittee of the House Ways and Means Committee conducted extensive hearings in the year 1934 on the subject to tobacco taxes. There was complete accord among all witnesses—growers, consumers, and manufacturers—that the taxes on tobacco are outrageously high.

The tax on cigarettes prior to the World War was \$1.25 per thousand cigarettes, which, translated to a pack of 20, meant 2½ cents per pack. The tax was increased twice during the World War. On October 17, 1917, it was increased to \$1.65 per thousand, or about 3½ cents per pack. On November 2, 1917, the tax was further increased to \$2.05 per thousand, which was a little more than 4 cents per pack. This was the maximum war rate, and was in effect until February 25, 1919, after the ratification of the eighteenth amendment, when it was increased to \$3 per thousand, or 6 cents per package of 20 cigarettes. The ratification of the eighteenth amendment was declared on January 29, 1919. The tax rate has remained unchanged from that date to this.

The pre-war tax on chewing and smoking tobacco was 8 cents per pound. On October 4, 1917, it was increased to 10½ cents per pound and to 13 cents per

pound on November 2, 1917. On February 25, 1919, the rate was increased to 18 cents per pound—the present rate.

An increase in the tax on tobacco will most assuredly result in greatly decreased consumption which will more than offset the additional revenue this measure seeks to provide from this particular source.

The tobacco that is used in the manufacture of cigarettes is of the flue-cured and burley types. Such types comprise the great bulk of production. The proposed increase in tax on cigarettes will be reflected in the growers' prices and his meager income will be further diminished. If not absorbed by the cigarette manufacturers in reduced prices to the grower for his product, it will be passed on to the consumers and result in greatly curtailed consumption.

The future of the tobacco farmer is uncertain. Our export trade in tobacco is seriously crippled by the international situation. Foreign markets are practically closed to us because of the wars in Europe and Asia. England has declared a virtual embargo on shipments of American tobacco and is importing tobacco from her colonies and from Turkey and Greece. Prior to the present conflicts abroad we have enjoyed a healthy export trade in tobacco, but unfortunately that trade is lost to us and it is extremely doubtful that it will be regained for a long time.

Our types of tobacco are being cultivated to a greater extent each year from seed exported from the United States. We should avoid any step that will result in decreased domestic consumption of tobacco at this time when the tobacco farmers' outlook is so dismal.

I most earnestly urge this committee to eliminate the proposed increase in the rate of tax on tobacco and tobacco products.

The CHAIRMAN. Thank you, Mr. Cooley.

We will now hear from Representative Virgil Chapman, from Kentucky.

STATEMENT OF HON. VIRGIL CHAPMAN, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF KENTUCKY

Mr. CHAPMAN. I shall be just as brief as I can. I have been designated by all of the nine Kentucky Members of the House to represent the delegation here in opposition to the proposed increase of 50 cents per thousand on cigarettes.

Approximately 400,000 farmers grow tobacco on approximately 2,000,000 acres of land in this country; the production of tobacco is the hardest work known to farm life; tobacco impoverishes the soil more than any other farm product produced in the United States; a tax on tobacco is the next thing to, and very near to, a tax on the land itself.

Any increase must be paid by either reducing the price paid by the manufacturer to the farmers for leaf tobacco, by passing the increase to the consumer, or both. Passing the increase to the consumer would result in diminishing consumption of cigarettes, with the same resulting loss to the farmer in the prices received for tobacco. This is A B C economics. With the highly competitive nature of the cigarette trade the manufacturers know that they cannot increase the price of tobacco without diminishing consumption.

It is estimated conservatively that the grower, in compensation for his labor, interest on his investment, deterioration of his barns, expense of fertilizer, hiring additional labor and impoverishment of his soil, receives approximately a hundred dollars net per acre for his tobacco crop; the manufacturer receives approximately \$300 for an acre of tobacco, and the Government takes in taxes approximately \$1,000. The total Federal tax is \$550,000,000 annually, to which a tobacco tax in 21 States has added another \$90,000,000 every year.

It is well known that the leading popular brands of cigarettes are made from the finer grades of tobacco. The cigarettes of the so-

called 10-cent class are manufactured from the medium grades of tobacco. The independent concerns, many of them small, which make the latter grade of cigarettes, operate on a narrow margin of profit and well-informed students of this subject believe that the proposed increase in this tax will force many of the small independent manufacturers out of business.

We know that the farmer does not receive a fair price for his choice grades of tobacco used in the more expensive cigarettes. His crop average has been helped a great deal by the purchase of medium grades by the manufacturers of the cheaper cigarettes. By destroying the market for the medium grades of tobacco, which we believe this increase would do, the crop average of every producer of cigarette tobacco would be lowered to a figure well below the cost of producing the crop.

In 1910 the tax on cigarettes was fixed at \$1.25 per thousand which was equivalent to 2½ cents per package. On October 4, 1917, on account of the World War, it was increased to \$1.65 per thousand, amounting to 3¼ cents per package. Twenty-nine days later the war tax on cigarettes was again increased to \$2.05 per thousand, which amounted to a fraction over 4 cents per package. Statements were made that after the emergency passed these extraordinary wartime increases would be repealed. No reduction has ever been made.

Then came the advent of prohibition and, to take the place of revenue that had formerly been collected on alcoholic liquors, the tax on cigarettes was increased to \$3 per thousand, equivalent to 6 cents per package. Prohibition was repealed and liquors pay hundreds of millions of dollars annually into the Federal treasury, but the emergency war tax and the emergency prohibition tax still stand as they were enacted in those emergencies. This is the only war tax that has never been reduced. It is the only tax of any kind on a farm product except the tax on oleomargarine, which was levied for the express purpose of protecting other agricultural products.

Now it is proposed to increase this tax from \$3 to \$3.50 per thousand, or \$1.16½ per pound, equivalent to 7 cents per package on cigarettes. The average popular brands sell in the stores of Washington at the rate of two for a quarter. This proposed increase would mean that 7 cents out of every 12½ cents paid for a package of cigarettes would be collected as a Federal sales tax. It has been said that this is a luxury tax. It is no luxury to the 400,000 growers who spend nearly a year in producing and selling a crop of tobacco and in that production extract more fertility from the soil than in producing anything else that grows.

Suppose a man smokes one package of cigarettes a day. That means a sales tax of \$21.90 annually on his cigarettes. If two members of the family smoke they pay an annual sales tax on their cigarettes amounting to \$43.80. If the cigarette is a luxury it is the poor man's luxury that brings solace and comfort to the toiler in the fields and the workers in the mines and mills and shops.

If we concede that the entire tax would be passed by the manufacturer to the consumer we must recognize that the additional tax would unquestionably diminish consumption. The per capita consumption of cigarettes in the 21 States that have a State cigarette tax in addition to the Federal tax is 1,025 per annum while the per capita consumption of cigarettes throughout the 48 States as a whole amounts to 1,325 cigarettes in a year. Every time the imposition of

this additional tax decreases consumption by one package it will be necessary to sell seven additional packages to make up for the loss of revenue to the Federal Government resulting from the diminution in consumption by one package. Every time this additional tax causes one man to begin "rolling his own" or smoking a pipe, which I believe it will cause countless thousands to do, we will have to find seven new customers to begin smoking cigarettes in his place if we are to avoid a loss in Federal revenue.

Many economists who have studied this subject long and carefully and are thoroughly conversant with all its phases are strongly of the opinion that this increase would bring us to the point of diminishing return in revenue from this source. Let us be careful, lest we kill the goose that lays the golden egg.

Mr. James C. Stone, of Lexington, Ky., in my congressional district, and the largest tobacco market in the world, out of his long experience as a grower, warehouseman, buyer, and manager of the largest tobacco cooperative ever formed, testified before a congressional committee while he was chairman of the Federal Farm Board that in his opinion if the tax were reduced from \$3 to \$1.50 per thousand cigarette consumption would be increased so greatly that it would not only bring prosperity to the producers of the crop but would bring into the Federal coffers a much larger amount in revenue.

Except for the present tax of 6 cents per package on cigarettes the 10-cent cigarettes would sell for 4 cents per package and the 12½-cent cigarettes for 6½ cents per package. The increase of sales would be so great that tobacco growers would have no need to ask for any form of benefit payments from their Government but would enjoy prosperity in the good old American way as individualists attending to their own business and selling the product of their toil and their soil at a price governed by the fundamental economic law of supply and demand.

In the principal tobacco producing areas in this country the prosperity of practically every citizen—banker, merchant, lawyer, editor, insurance agent, butcher, baker, and candlestick maker—depends in large measure on the prosperity of the producers of tobacco.

The CHAIRMAN. All right, Congressman, thank you.

Mr. BRECKMAN, I understand you are appearing for Mr. Hanson?

Mr. BRECKMAN. Yes.

STATEMENT OF FRED BRECKMAN, REPRESENTING THE NATIONAL GRANGE AND THE ASSOCIATION OF SOUTHERN COMMISSIONERS OF AGRICULTURE

Mr. BRECKMAN. Mr. Chairman, the National Grange and the Southern Commissioners of Agriculture filed a brief with the committee expressing doubt regarding the wisdom of the proposed super-tax on tobacco, particularly as it will affect the farmer or the tobacco grower.

As one of the witnesses, Mr. Cooley, said a little while ago, tobacco may be regarded as a luxury to those who use it, but it is not a luxury to the men that produce it.

Now, this is a rather technical and complicated subject, and we tried to cover it in the brief we filed with the committee, but if the committee is willing to hear somebody summarize this brief, we have here Dr. Francis J. Clare, who is an agricultural economist.

The CHAIRMAN. I think we have already heard more on this subject than on any other, Mr. Breckman, and the committee will certainly take up the brief as you have filed it.

Mr. BRECKMAN. Well, we want to make it very clear. Of course, the tobacco growers, along with every other group in the United States, are in favor of paying their just share of national defense, but we do doubt the wisdom of imposing that supertax because of the effect that it is going to have on the tobacco growers who have already lost the major portion of their export market; and we believe that in the end the Government will have to put many of those farmers on relief if this additional tax is imposed. We know that Congress doesn't want to do anything that would be unfair and unreasonable like that.

Senator HERRING. Do you know of any agricultural product that hasn't lost its foreign market?

Mr. BRECKMAN. Oh, yes; but I don't believe there is any other product that at one blow lost fully 50 percent of its export market.

*Senator HERRING. I think you have oversold your proposition.

The CHAIRMAN. All right; thank you, Mr. Breckman.

(The brief referred to by Mr. Breckman is as follows:)

ARGUMENT AND BRIEF SUBMITTED BY THE NATIONAL GRANGE COOPERATING WITH THE ASSOCIATION SOUTHERN COMMISSIONERS OF AGRICULTURE SETTING FORTH THE ECONOMIC FACTUAL REASONS, T.A.F., AND OTHER DATA SHOWING WHY THE PROPOSED INCREASES IN TOBACCO TAXES PROVIDED FOR IN H. R. 10039 SHOULD NOT BE ENACTED INTO LAW

These are indeed tragic times. Today on the continents of Europe and Asia a modern civilization is battling for its very existence. Airplanes roar out of their hangars. They drone high in the blue of the heavens. The whistle of death wrapped up in aerial bombs is dropped from their bowels and out of the clouds, to scatter death and destruction over the cities of foreign lands. Men are dying by the thousands.

While touching every heartstring in America the horrors of this strife bring a fuller realization of the happiness found in our own historic American way of life. It has, however, driven home to one and all the necessity of preparing to defend our heritage with every possible resource at our command.

Americans of every political faith and religious creed loathe war and love peace. It is in recognition of the high sense of an outraged humanity being experienced by our people, that both our President and our Congress, in reflecting the national will, are now doing all possible to achieve that defense. They aim not alone to give succor to the needy, but to exert every effort to preserve our peace, and, at the same time, protect us from the consequences which might easily flow out of a peace. Especially a peace made in Europe, imposed upon a vanquished continent, by the weight of armies, navies, and aircraft, if that be the result of Germanic victory in the total war now raging.

We have seen the specter of other peace-loving nations suffer complete extinction at the hands of brute force in the last few months. We know full well that their "love of peace" did not spare them from the slaughter of virtual annihilation. They possessed but limited resources. These resources were coveted by the brute forces of the aggressor. We, on the other hand, possess unlimited resources which even at this moment are being hunted and sought out in other lands by the identical brute forces of conquest, aggression, and greed.

We have an almost unlimited bounty of goods and riches. These are coveted by other nations. Moreover, and more treasured, we have a way of life and a cherished heritage of freedom, inherent in our liberty-loving people. That love stands in the way of those whose ambitions are to develop a totalitarian world. These heritages, freedom and resources, we long since made high resolve to defend. It is because of these things that we must build our national defenses so strong that the most foolhardy of so-called dictator nations would not dare to risk attack upon us.

Not alone do we possess the resources essential to make either defensive or offensive wars, but we have the innate skill and the will with which to prosecute war or peace without fear of failure.

You gentlemen of the Senate Finance Committee are the representatives of our people, chosen by them at the ballot box. It is you to whom we delegated the powers to provide the necessary organizations and accoutrements for our national defense in peace and in war.

Of primary importance to our Nation is the problem of national finance in the matter of our national defense. It is to the task of making proper provision for that finance which you gentlemen, in your capacity as members of the Senate Finance Committee, are now devoting your able and constructive thoughts. It is with reference to the financing of our national-defense program that we, as representatives of American agriculture, now address you.

In addressing you, gentlemen of the Senate Finance Committee, we wish to express our recognition of the problems confronting your committee in this great national crisis.

We realize full well the need for prompt action and dispatch in the handling of the finances of the national-defense program. We approved the fiscal policy adopted, which looks to increased taxation in order to provide revenues to meet additional expenditures and thus preclude greater expansion of the deficit in financing our national affairs.

The undersigned representatives of American agriculture are in this instance addressing you with reference to H. R. 10039 which is a bill to provide for the expenses of national preparedness by raising revenue and issuing bonds to provide a method for paying for such bonds and for other purposes.

They are in this instance addressing you specifically with reference to the proposal made in H. R. 10039 to increase the taxation already imposed upon tobacco and tobacco products.

As representatives of American agriculture we feel it is unnecessary to elaborate upon the willingness of American agriculturists to bear their just share and proportionate part of any and all tax burdens. We feel it necessary however, to point out to the Senate Committee on Finance, the fact that the Federal Government is today collecting taxes on tobacco totaling many times the sum received by the American tobacco producers, for the entire tobacco crop of the Nation.

We realize full well the necessity of raising additional revenue to provide for the expenses of national preparedness and defense. But, in view of the present conditions of the tobacco farmers we are here giving expression to our objection to that portion of the pending bill, H. R. 10039, which seeks to increase the tax on cigarettes and other tobacco products.

For many years agricultural and tax economists have been convinced that the heavy excise taxes imposed upon manufactured tobacco and tobacco products, have tended to burden and suppress the industry and thus result in far-reaching ill effect upon that large number of our population engaged in the production of tobacco.

In the "Flue-cured Belt" alone, over 300,000 farm families are growing tobacco. The last crop netted the growers not quite 16 cents per pound. H. R. 10039 proposes an additional tax of 16½ cents per pound, which in the total revenue it proposes to provide, is in excess of the price the farmer received for his product in the current crop year.

The present proposal to increase the overburdening taxes now imposed against tobacco is being advanced in the face of the fact that for several years past the tobacco producers have interested themselves in an effort to obtain a reduction in the current rates of taxes imposed by the Federal Government.

The efforts recently put forth have been unsuccessful however, due, in a large measure, to the continuing annual deficits in the Federal Treasury and the annual recurring need throughout the entire past decade, for increased governmental revenues to meet expenditures consequent to the depression. These revenues comprehend both the cost of relief and the national recovery program.

The American tobacco farmers are not unmindful of the fact that it has been necessary for their Representatives in Congress to exploit every possible well-paying source of revenue to meet the cost of past emergencies and for that reason alone, they have not vigorously pursued efforts to reduce existent taxes in recent years, onerous as these have proven themselves to be.

Now, however, a national-defense emergency is flowing out of the developments in the European war. They now find that instead of achieving the long-sought and much-needed relief from overburdening taxation, that a proposal is being advanced to actually increase the cigarette and other tobacco taxes.

As representatives of American agriculture, the undersigned definitely feel that tobacco is already overtaxed in a measure out of all proportion to other commodities. They would also point out to the Senate Finance Committee that the present cigarette tax rate, a result of the World War financing, has in nowise been abated, although that crisis has long since passed.

They would also point out that while commodities other than tobacco have been relieved of much of the extra tax burden imposed during the World War, the war tobacco taxes still remain.

While tobacco may be classed and taxed as a luxury, it is no luxury to its producers. The industry, apart from its producers, provides a livelihood for hundreds of thousands of growers, warehousemen, buyers, industrial workers, and salesmen.

Increased Federal taxes, if superimposed now, could easily and most seriously cripple this industry in its industrial, as well as agricultural employment. Tobacco farmers are already hard hit by the loss of their historically held and acquired foreign markets as a consequence of the Second World War.

Discussing the Federal tax problems and the misfortunes that would befall American Agriculture and industry if Federal taxes were not equitable and kept well within bounds, President Roosevelt once declared: "Taxes are paid in the sweat of every man who labors because they are a burden on production and if excessive * * * are reflected in idle factories or in tax-sold farms * * *"

The undersigned, speaking in behalf of the tobacco farmers, would advise the Senate Finance Committee that this class of agriculture first is willing to pay its part of all taxation that its Representatives to Congress might find necessary for the support of their Government. We would not be fair to our farmers, however, if we did not say that researches support the fact that tobacco is already paying far more than a fair share of taxation into the Federal Treasury.

In order to exhibit that fact more clearly, may we take this opportunity of advising that last year the national average price paid for tobacco was slightly under 16 cents a pound and in lieu of the fact that it takes less than 3 pounds of tobacco to make a thousand cigarettes that existent taxes are equivalent to a tax of \$1 a pound on cigarette tobacco or more than 600 percent of the value of the tobacco itself.

May we now point out that the 50-cent increase per thousand cigarettes proposed at present, is an increase in taxation equivalent to 16 cents a pound on the tobacco. This proposed increase is itself a tax of more than the price received by the grower for this, the product of his soil and toil.

May we now take the further opportunity of pointing out that inasmuch as one-half of the flue-cured cigarette tobacco is exported that 50 percent of the tobacco crop domestically consumed is at the present time carrying a tax burden of nearly seven times as much as the farmer receives for his entire tobacco crop, and that the proposed increase of 50 cents per thousand would make the "tax crop" eight times the value of the tobacco crop itself.

The question might easily be asked, if this tax is increased who is going to pay it? Your petitioners would here point out that about 90 percent of the tobacco consumed in this country is purchased by not more than one-half dozen large manufacturers who process and market the crop. This practically constitutes the sole market for this great American agricultural product.

The heat, light, rent, power, interest, postage, telephone, telegraph, depreciation, taxes, salaries, wages, insurance, and interest on bonded indebtedness of the manufacturers and processors are all fixed charges. Their freight and other charges for transportation are predetermined and fixed.

As it is with the manufacturers of tobacco products, so it is with the distributors and retail dealers. Consumer purchasing power is limited if not fixed. If prices are increased they can buy less smokes and the sales would fall off.

Common sense dictates, that if, in the opinion of the "big six" their profits would be decreased, if attempt were made to pass increased taxes on to the ultimate consumer that by way of decreased consumption, the tax would be taken out of the price at which the tobacco is bought.

Evidence has already been offered the Committee on Ways and Means that when a man changes his smoking to pipe tobacco instead of cigarettes, that he will only pay 21 cents a pound tax on the pipe tobacco, instead of the \$1.16 a pound collected on the cigarette tobacco. This raises the question as to whether or not the Government would, in the last analysis, derive any increased income whatever by the increase proposed in H. R. 10039.

If on the other hand the buyers of tobacco pass the tax on and decreased consumption follows, the farmer loses. If they determine not to pass the tax on, for fear of decreased consumption due the fact that their "charges are fixed," they would either have to take the surtax out of their profits or out of the price paid to the producer. It would follow, therefore, that in either event the tobacco farmer would absorb a large percentage of the supertax.

It is necessary to advise you that the tobacco producers last year, under "production control" decreased their production, and in spite of so doing were

compelled to sell their crop at less than 16 cents a pound. Now that our producers are faced with the prospect of losing 60 percent of their normal income from sales in this crop year, due the loss of foreign markets, our tobacco farmers will cultivate their meager crops in the coming season not knowing how they are going to pay the costs and earn a living. For these reasons, if no other, they should now be insured against excessive burden of increased taxation on this year's crop of tobacco.

Nothing could be more expressive nor more truly disclose the enormity of the tax paid on American tobacco and covered into the Federal Treasury than the information conveyed to the Ways and Means Committee in the statement made by the Honorable William H. May, commissioner of agriculture, State of Kentucky, who recently appeared before that committee.

In order to exhibit the overburden of the present taxes collected on tobacco, an agricultural commodity which, in its last analysis, represents the labor product of the soil and toil of its producers, we here present a few facts and figures as to values, costs, income, production, and taxation pertinent to the subject and the wisdom, sagacity, or equity of increasing the present taxes as proposed under H. R. 10039.

The following data are specifically applicable to the State of Kentucky, which State with its hundreds of thousands of producers of American tobacco is representative of similar producers and factual conditions which obtain in tobacco-producing areas throughout the United States:

I. The average annual production of tobacco in Kentucky is in the round sum of 1,000 pounds per acre.

II. The average price received for all types of Kentucky tobacco in the crop year just closed was 15½ cents per pound or an average of \$150 per acre.

III. The average Kentucky tobacco farmer, under the quota system applicable to this commodity, planted and harvested 4 acres of tobacco.

IV. Under the present rate of taxation alone the Federal Government collects \$1 a pound, or \$1,000 tax on the tobacco produced on every single acre of land. The proposed increase in tobacco taxes contemplated in the bill H. R. 9966 would raise the amount to the sum of \$1,167 per acre of tobacco.

V. Thus it "follows" that while a tobacco farmer cropping under production control but 4 acres of tobacco land would receive the sum of \$626 for his tobacco crop, while the Federal Government, exclusive of other taxing agencies, would harvest a "tax crop" of \$4,668 in the marketing and sale of the product of that farmers' brain and brawn, soil and toil.

VI. With an average value of \$23, which represents the value per acre of the land upon which tobacco is produced in Kentucky, the amount of "the tax harvest" garnered from the tobacco cropped off 1 acre of Kentucky land is at the present time 52 times the value of the land upon which the "tax crop" was produced.

Your petitioners would here submit the further fact that while the tobacco producers received but \$85 per hogshead for the tobacco crop in the year just closed, that under our present system of marketing and taxing coupled with our national tobacco economy, our farmers, who are themselves large users of manufactured tobacco, are compelled to buy their own commodity back in the shape of cigarettes and other tobacco products at a price of about \$1,302 per hogshead, of which sum more than \$1,000 is represented by Federal taxes. While but a bare \$217 is the value added by all charges necessary to processing and distribution, the processing charges alone are nearly three times the value of the agricultural product itself.

While there are no data available at this particular moment showing the amount of manufactured tobacco consumed by American agriculturalists, may we now point out to the members of the Senate Finance Committee just how onerous, and at the same time how palpably unfair, is this proposed increase in the tax placed upon the growers of American cigar, cigarette, and chewing tobacco, and point out further how viciously the present system of taxation upon tobacco actually plays both ends against the middle; the tobacco farmers on one end, let us say, of an average agricultural county, against the wheat farmers producing wheat on the other end of the same county. Or in a broader sense, the American tobacco grower as pitted against the American wheat grower.

Following is a table showing the amount of tobacco that was used in 1937 in the United States in producing the cigars and cigarettes, together with the Federal taxes imposed upon various types of tobacco manufacture and sale.¹

Amount of tobacco per 1,000 cigarettes manufactured (pounds).....	2.85
Amount of tobacco per 1,000 cigars manufactured (pounds).....	24.85

¹ Authority U. S. Bureau of Internal Revenue.

	<i>Federal tax</i>
Nationally advertised brands (per 1,000).....	\$8. 00
Special large-size ciga re ttes (per 1,000).....	7. 20
Chewing, smoking tobacco, and snuff (per pound).....	. 18
Cigars selling up to 5 cents (per 100).....	2. 00
Cigars selling from 5 cents to 8 cents (per 100).....	3. 00
Cigars selling from 8 cents to 15 cents (per 100).....	5. 00
Cigars selling from 15 cents to 20 cents (per 100).....	10. 50
Cigars selling at more than 20 cents (per 100).....	13. 50

From the foregoing it will be deduced that it requires slightly less than 3 pounds of tobacco to make 1,000 cigarettes or the equivalent of 50 packages of "the standard brands."

With tobacco selling at 16 cents per pound the grower would receive the sum of 48 cents for all the tobacco in 50 packages, or less than 1 cent (forty-eight fiftieths of a cent) for the tobacco in 1 package of cigarettes.

With wheat selling on the farm at 75 cents a bushel and with cigarettes retailing at 15 cents a package, it would mean that when a wheat grower wanted to buy cigarettes he would have to take all the money that he received for a bushel of wheat in order to procure five packages of the "standard" brands, or seven and one-half packages of the "10-cent" brands of cigarettes.

In case he purchased the 15-cent brands he would in reality be trading a bushel of wheat for less than 5 cents worth of tobacco, and in case he purchased the 10-cent brands he would be giving his wheat for slightly more than 6 cents worth of tobacco, after it had been manufactured and wrapped.

Let us now look further into that transaction, and analyze the same to see just how it would affect a wheat farmer, say, in the State of Kentucky, where, in addition to the 6 cents Federal tax imposed, the State of Kentucky imposes a further tax of 1 cent on the 10-cent brands and a tax of 2 cents on brands selling above 10 cents. This makes for a total tax of 7 cents on the 10-cent brands and an 8-cent tax on the standard brands.

This actually means that a Kentucky wheat grower, when purchasing 15-cent brands of cigarettes today, has to pay the Federal Government 30 cents and the Kentucky State government 10 cents, or a total of 40 cents for the privilege of swapping a bushel of wheat for 5 cents worth of Kentucky grown tobacco.

If he smoked a "10-cent brand of cigarette," the sales of which are very high in rural districts, he is now compelled to pay the Federal and State Governments 52½ cents for the privilege of swapping the wheat which he produced on his own land and in the sweat of his brow for less than 6 cents worth of Kentucky-grown cigarette tobacco, after it had been manufactured, even though he, himself, had produced the tobacco in a field next to his wheat.

In support of the arguments herein being made, that our tobacco farmers are, even now, in dire straits, let us now call to the stand noted farm leaders in order to obtain their views. First let us learn what the Honorable Henry A. Wallace, Secretary of Agriculture, has to say about the present plight of the tobacco growers.

In discussing the problem of American agriculture with reference to the present problem of defense in a national broadcast Tuesday, June 4, 1940, Secretary Wallace declared:

"The immediate necessity of preparedness means that we must move as fast as we can to utilize our idle men, idle money, and idle factories in the production of guns, munitions, airplanes, tanks, and ships. We don't know yet how much the total cost will be."

"We must make sure that the farmers and the unemployed are not made victims of the war's interferences with world trade! * * *"

"In any event such export crops as cotton and flue-cured tobacco are almost certain to be in real trouble."

Let us now call upon the Forsyth County Pomona Grange and learn the attitude of this, America's oldest farm organization, as expressed in a news item appearing in the Winston-Salem (N. C.) Journal, June 6, 1940. Following is the news item:

"GRANGE FIGHTS PROPOSED RISE IN TOBACCO TAX

"The Forsyth County Pomona Grange is strongly opposed to the proposal presented in Congress to raise the Federal tax on tobacco. This opposition was expressed in a message dispatched yesterday to R. L. Doughton, chairman of the House Ways and Means Committee, by the legislative committee of the Forsyth Pomona Grange."

The message signed by G. G. Tucker, a member of the legislative committee, was as follows:

"The Forsyth County Grange protests the proposed additional tax on tobacco. Our tobacco farmers are now facing disaster. The loss of the export trade and the additional tax literally means ruin for the tobacco farmer, as this tax would be passed on down to him. He could not escape it. Why destroy any one industry when the tax could be spread over all and be no serious burden to any? Tobacco now carries the heaviest tax burden we know of."

The committee also sent a message to A. D. (Lon) Folger, Representative to Congress from the Fifth District, North Carolina, urging that the proposed tax increase be declined. This message was as follows:

"The Forsyth County Grange protests the additional tax proposed on tobacco, knowing it will eventually rest on the farmer who is now burdened to the limit since the loss of the export trade. We solicit your aid. The proposed tax is expected to be of widespread significance, especially in this center of the flue-cured tobacco industry, in view of the international events which have now completely eliminated the export tobacco trade.

"A referendum, which will be conducted among local tobacco farmers around July 25, will propose an acreage reduction of at least 10 percent, according to plans now being worked out in the office of G. C. Flinn, Federal Director of the East Central Division of the Agricultural Adjustment Administration, which includes North Carolina, South Carolina, Virginia, West Virginia, Tennessee, and Kentucky. This will involve the entire tobacco growing area, flue-cured and burley.

"One of the proposals to raise \$3,000,000,000 in special defense taxes during the next 5 years is to increase the cigarette levy from \$3 to \$3.50 a thousand.

It is estimated this will add approximately \$77,000,000 a year to the more than \$450,000,000 collected annually from the \$3 tax; a tidy contribution to the Federal Treasury from a single commodity."

What follows are copies of telegrams sent to the Representatives in Congress, among them the Honorable Robert L. Doughton, chairman of the Ways and Means Committee, in protest against the proposed increase in tobacco taxes.

Hon. R. L. DOUGHTON,

*Chairman, House Ways and Means Committee,
Washington, D. C.:*

Forsyth County Grange protests the proposed additional tax on tobacco. Our tobacco farmers now facing disaster. The loss of export trade and additional tax literally means ruin for the tobacco farmer as this tax would be passed on to him. He could not escape it. Why destroy any one industry when tax could be spread out over all and be no serious burden to any. Tobacco now carries the heaviest tax burden we know of.

G. G. TUCKER,
Member, Pomona Grange Legislature Committee.

WINSTON-SALEM, N. C., May 31, 1940.

Hon. A. D. FOLGER,

House of Representatives, Washington, D. C.:

Forsyth County Grange protests the additional tax proposed on tobacco knowing that it will eventually rest on the farmer who is now burdened to the limit since the loss of the export trade. We solicit your aid.

G. G. TUCKER,
Member, Pomona Grange Legislative Committee.

Mr. Virgil Steed, who recently appeared before the Ways and Means Committee submitted the following telegram sent to him by the executive secretary of the Kentucky Farm Bureau. The Farm Bureau wired:

"Tobacco is only commodity on which World War rates were not reduced after first conflict. This farm commodity now bearing more than its share tax burden even under present conditions.

"Rates should not be raised but should be lowered when present emergency passes.

"Small average allotments and low total income of tobacco producers already critical. Tobacco farmers need increased benefit payments instead of increased tobacco taxes. Hope entire Kentucky congressional delegation will join Virgil Chapman in opposing vicious abuse in tobacco taxation.

"BEN KILGORE,
Executive Secretary, Kentucky Farm Bureau Federation."

Let us now hear from the Honorable W. Kerr Scott, commissioner of agriculture, State of North Carolina, who under date of June 8, wired the secretary of the association, Southern Commissioners of Agriculture as follows:

RALEIGH, N. C.

C. C. HANSON,

*Secretary, Association Southern Commissioners of Agriculture,
Washington, D. C.:*

Tobacco now being taxed far in excess of most other commodities and to further increase the taxes would be an injustice to the farmer if he should be penalized through a reduction in process paid for the raw leaf.

Prospects for the sale of the 1940 tobacco crop are none too bright at present. Export outlook gloomy. No assurances that additional taxes will not have to be paid by the growers.

While I am in complete sympathy with every effort being made to secure necessary national defense, I do not believe that this requires that tobacco be taxed out of proportion to other commodities and products.

As you know, agriculture is one of the most essential of "first-line" defenses and our farmers one of the most patriotic groups in the Nation. Despite every remedial measure they are even now receiving comparatively little for their labors.

Be assured that the farmers of North Carolina do not object to paying their proportionate share of taxes, and I feel with them that it is obviously unfair to penalize their incomes out of proportion to other groups.

As North Carolina's commissioner of agriculture, I respectfully ask that you lend your every help to prevent the further taxation of tobacco.

W. KERR SCOTT,
Commissioner of Agriculture.

In order to the more clearly reveal to the Senate Finance Committee the basic causes for the opposition herein expressed to an increase in this tax, we respectfully would call directly the committee's attention to the following:

In spite of the curtailed production program adopted under the Agricultural Adjustment Act, in an effort to maintain a fair level of price they are now actually faced with a total loss of their export trade—in this connection we would also call the committee's attention to the fact that in 1938 and the years prior thereto, approximately 60 percent of the flue-cured tobacco produced in America was exported.

As a result of the war and the fiscal policies adopted by the British Government, in 1939 British buyers withdrew entirely from our markets. We would have you know with us that were it not for this assistance rendered to our tobacco farmers by the Commodity Credit Corporation, that total bankruptcy would have enveloped the tobacco-producing areas in the past crop year.

It becomes more evident daily that with a 50-percent curtailment of production and the further loss of foreign trade, it is perfectly plain to see that the tobacco farmers of America are now again faced with disaster. Confronted with existent conditions, it is our well-grounded fear that the laying of any additional tax whether upon this commodity at this time is bound to have a detrimental effect upon our tobacco farmers and, in our opinion, might even result in less total revenue to the Treasury.

It is not illogical to believe that the burden of the tax is visited heavily upon our tobacco farmers. Production naturally depends upon demand and this question in turn upon consumption. For instance, let us assume that the entire tax should be eliminated—it is only natural to assume that consumption would greatly increase. On the other hand, however, should the tax be doubled, it would be equally true that consumption would be greatly decreased. It is an undisputed fact that a commodity can be taxed out of existence and inasmuch as the power to tax is the power to destroy, we urge the Senate Committee on Finance not to further increase the tax burden on the commodity tobacco in any manufactured stage inasmuch as upon its production depends the livelihood of a large cross section of our low income agricultural producers.

The tobacco industry at this very time is so depressed that the growers of flue-cured tobacco are even now faced with the necessity of curtailing their production from the 1,100,000,000 pounds produced in 1939 to a mere 600,000,000 pounds in the crop year of 1940.

Our flue-cured tobacco farmers have the land and equipment and are capable of producing a crop of flue-cured tobacco far in excess of the 1,100,000,000 pounds which they produced in 1939.

The present consumption of cigarettes is in the approximate amount of 175,000,000,000 annually. The present tax rate on cigarettes of \$3 per 1,000

would return \$525,000,000 to the Federal Treasury. On the other hand, the gross farm income from tobacco used in these 175,000,000,000 cigarettes, amounted to but one-fifth of the revenue covered into the Federal Treasury.

Assuming that consumption of cigarettes continues at the present level, after the proposed increase in taxation was made effective, an additional \$87,500,000 of revenue would be derived from the increase in the tax rate. Ponder well on this one fact. The increase in revenue under H. R. 10039 alone would be equal to about 80 percent of the total farm income now derived from all the tobacco now used in cigarettes in the country.

Not the least among the deterrent reasons for not increasing the present levy is the matter of the 10-cent cigarette. It is reported that from 20 to 25 percent of all the cigarettes consumed in this country retail at 10 cents a package. An increase in the tax of 1 cent per package would necessarily mean that the manufacturers of the 10-cent cigarettes would have to close the production of such brands or else increase the price of such brands.

It is a well-known fact that the gross margin (excluding tax) received by manufacturers from the sale of 10-cent cigarettes is about 1½ cents per package and that a reduction of this margin to ½ cent per package would likely make the manufacture of the 10-cent brands prohibitive, unless the retail price could be increased.

The total elimination or even a reduction in the production of 10-cent cigarettes would destroy the existent competition which our farmers now enjoy for certain grades of tobacco, to the detriment of a large class of our tobacco growers, whose soil and climate are not susceptible of producing a thin leaf cigarette or even chewing tobacco.

Shifts from both the 10-cent cigarettes and other priced cigarette brands to other forms of tobacco products would unquestionably have a great influence upon the revenue derived from tobacco. It is most significant to note that the consumption of a pound of tobacco (farmer's weight) in the form of cigarettes yields the Treasury \$1 in taxes while the consumption of a pound of tobacco (farmer's weight) smoked in pipes or hand-rolled cigarettes would yield the Federal Treasury slightly less than 20 cents per pound. It would therefore follow that if the use of a pound of cigarette tobacco was shifted from cigarettes to pipe smoking or to use in making hand-rolled cigarettes, the Treasury would lose about 80 cents in revenue.

That the present Federal tax of tobacco has been found to be and adjudged exorbitant, is supported by the records of the hearing held in 1934 by the Committee on Ways and Means, presided over at that time by the Honorable Fred Vinson of Kentucky.

These hearings were exhaustive. Statements were made, not only by representatives of agriculture but by representatives of producers and processors and consumers of tobacco.

At the conclusion of the hearings on June 4, 1934, the committee reported in part as follows:

"It can be truly said that from the evidence of all witnesses for the growers, the consumers, and the manufacturers, there was complete accord that the taxes on tobacco are outrageously high."

That the farmer is now paying his fair share of Federal tax is shown by the following:

The pre-war tax on cigarettes was \$1.25 per thousand cigarettes. This, translated into a package of 20, meant 2½ cents per pack. This tax rate was increased twice during the World War.

On October 4, 1917, it was increased to \$1.65 per thousand cigarettes, or about 3½ cents per pack. Then, in less than a month thereafter, and on November 2, 1917, it was increased to \$2.05 per thousand cigarettes. This was a tax of a little more than 4 cents per package of 20.

This, the maximum war rate—was in effect until February. This again was subsequently increased to \$3 per thousand, or 6 cents per pack, which rate has remained unchanged and is in effect today.

Now, as to other grades, the pre-war tax on chewing and smoking tobacco was 8 cents per pound.

On October 4, 1917, this was increased to 10½ cents per pound and again on November 2, 1917, it was increased to 13 cents per pound. After the World War and on February 25, 1919, it was increased to the present rate of 18 cents per pound.

The tobacco producers are not themselves unmindful of the present emergency, and it is that knowledge that they direct the attention of the members of the Senate Finance Committee to the fact that they have already expressed their

willingness to carry their share of the cost of this national emergency. They do, however, now point out that their product is at present carrying the wartime rate imposed in order to discharge the cost of the first World War, and that as tobacco growers, as well as citizens, they feel that this crop should not be subjected to an added burden of the cost for national defense at this time.

As representatives of American agriculture we inherently feel that an increase on the tax of any grades of tobacco at this time will most assuredly result not only in the abatement of one or more classes of cigarettes produced, but by virtue of the result of decreased consumption this would probably more than offset any additional revenue which the Federal Government might hope to realize from the proposed increase in the rate of tax.

Let us here and now submit the fact that when the tax on plug and twist tobacco was 8 cents per pound, the consumption was approximately 180,000,000 pounds per year. That with each succeeding raise in the rate of taxation the consumption declined and that by the time the tax was finally established at 18 cents, the industry had suffered a loss of more than 125,000,000 pounds decline in its annual sales and the tobacco growers lost that much of their market of this class of product.

It is reported with credence, although specific supporting data are not available, that there exists a certain class of smokers who will pay 10 cents to get 20 "tailor made" cigarettes of a better quality and shape than they can make themselves, but, that they, this class of smokers, will not pay 13 or 14 cents for "tailor made." Ten cents for cigarettes is their limit as to price. For a package of cigarettes they will not pay any more.

There is on the market a little machine no larger than a bar of laundry soap called the Roll Your Own. The manufacturer of this machine sells the cigarette papers with the tobacco. Countless thousands of these machines are in use. The machine has but few movable parts and is highly efficient and is kept in repair free of charge.

The cigarettes produced by this machine are perfect in shape, tightly rolled, burn evenly, and are altogether sightly. A few minutes in the evening and a man can make his next day's supply of smokes. The tobacco and papers necessary to make 20 cigarettes by this process costs but 5 cents.

It is conservatively estimated that from 40 to 50 billion "roll your own" cigarettes are annually produced in this country by that class of smokers.

Further estimate has been made that if and when the tax was raised on the 10-cent cigarette, that the production of "roll your own," as well as hand-rolled cigarettes will increase at a rapid rate.

If that premise be true, and the tax on the "tailor made" is now increased, unquestionably more men will take to rolling their own instead of smoking "tailor made" cigarettes. In that event, it is to be remembered that the Government will only derive 1 cent in revenue as contrasted with the present revenue of 6 cents.

Moreover, when you raise the Federal cigarette tax on the 10-cent cigarette, on which priced package you get the same Federal tax as you do on the Big Four—the Camels, Chesterfields, Luckies, and Old Golds—the increase in consumption of "roll your own" will take place and cause a diminution in the consumption of the "Big Four tailor made," which sell at a higher cost and this change in the smoking habits will again cause a decrease of the revenues covered into the Federal Treasury, from the current normal consumption taxed at the present rate of taxes.

We representatives of organized agriculture who are presenting this argument and brief are particularly desirous of pointing out and emphasizing the fact that not alone is the American tobacco grower now suffering from the imposition of overburdening Federal taxes upon tobacco, but as will be pointed out in this document, a majority of the States have of late been more and more availing themselves of this proven and established, comparably easy and inexpensive method of raising revenues for their State treasuries by imposing additional tobacco taxes on the tobacco consumed in their respective States. Excise and stamp taxes imposed by the State governments are now in some instances 50 percent of the levy imposed by the Federal Government.

Moreover and in addition to Federal and State excise taxes certain municipalities now impose direct sales taxes by way of increasing their municipal revenues through the sale of cigarette and tobacco tax stamps. These, like the internal revenue stamp, are affixed to each package of cigarettes, box of cigars, or other tobacco container, on tobacco vended and consumed in their States.

All of these so-called stamp taxes, Federal, State, and municipal, are levied in addition to the regular annual license fees charged the dealers in tobacco. In many instances, State, county, and city license fees are collected. That these license fees are themselves piled one on top of the other is made evident by the fact that in certain States there is charged—

- I. A license fee to all distributors.
- II. An additional license fee charged to wholesalers.
- III. A still further additional license fee charged all retailers.
- IV. And a still further license is required if the cigarettes are sold from vehicles.

Following are presented in brief the codes of some of the many States showing the various excise taxes and license fees charged on cigarettes. These are presented, together with a table, showing the amounts collected and the percent of total State revenue derived from tobacco taxation.

NEW YORK STATE

A State tax is imposed on cigarettes at the rate of 1 cent for each 10 cigarettes or fraction thereof. This is equivalent to a 2-cent tax on a package of 20 cigarettes. The tax is paid by means of stamps purchased from the tax commission. The tax may also be paid by using metering machines if the commission so prescribes.

NEW YORK CITY, N. Y.

A city tax is levied upon every sale of cigarettes at retail at the rate of 1 cent for every 20 cigarettes or fraction thereof (ch. 41, Administrative Code is amended by local Law No. 100).

OHIO

Page —, General Code, S. 5894-1 et sequitur, as amended. An excise tax of 1 cent per each 10 or fractional part thereof is levied on sales of cigarettes within the State by consumers (S. 5894-2 as amended by Laws 1935-36, first special session, H. B. No. 695 and Laws 1939, H. B. No. 2, S. B. No. 102 2).

Wholesalers pay \$100 and retailers \$25 to county treasurer for annual license (5894-5).

OKLAHOMA

Laws 1939. H. B. No. 234.

An excise tax is levied upon the sale or consumption of cigarettes within the State of Oklahoma, subsequent to May 31, 1939, at the following rates (sec. 2).

	<i>Cents</i>
Package of 10 or less.....	1½
Package of 20.....	3
Package of 50.....	7½

The following annual licenses are required: Manufacturers and wholesalers \$25; retailers, \$10; distributing agents, \$100; permits to sell from vehicles, \$10 (sec. 4).

PENNSYLVANIA

Pendon's Statutes, title 72 as extended by act of May 4, 1939, Laws 1939, No. 44.

Until May 31, 1941, excise tax is imposed upon all sales of cigarettes by dealers in Pennsylvania at the rate of 2 cents per package of 20 cigarettes (3157). Wholesalers and retailers pay an annual license fee of \$1 to the department of internal revenue (3156). This tax is in lieu of the mercantile license tax (3162).

TEXAS

Vernon's Ann. Stat. 7047-1 as amended.

A tax is imposed on all cigarettes used or otherwise disposed of in Texas at the following rates:

	<i>Per M</i>
Weighing not more than 3 pounds per M.....	\$1. 50
Weighing more than 3 pounds per M.....	3. 60

Every person engaged in the sale or use of cigarettes must pay a license fee to the comptroller of public accounts at the following rates (art. 7047 c-1, 4, as amended by Laws 1936. H. B. No. 8, art. 3 3):

Type of permit:	Annual fee
Distributing agents.....	\$100
Distributors.....	25
Wholesale dealers.....	15
Retail dealers.....	5
Solicitors for sale.....	1

WASHINGTON

Laws 1935, chapter 180, as amended.

A tax is levied on the sale, use, consumption, handling or distribution of cigarettes in Washington, and is to be paid by the first person performing any of such acts by attaching tax stamps, purchased from the State tax commission to each package. The tax rate is one-tenth of 1 cent for each cigarette, except that when the selling price is more than 1 cent per cigarette, the rate is 20 percent of the selling price (82 as amended by Laws 1939, ch. 225). Each person subject to the tax pays a license fee of \$1 (187 as amended by Laws 1937, ch. 227).

The following table shows the percent of total State revenue derived from taxes and other imposts on tobacco imposed by certain States in addition to the taxes imposed by the Federal Government:

Tobacco taxes, by States

State	Yield	Percent of total	State	Yield	Percent of total
Alabama.....	\$2,077,760	7.03	Montana.....	\$20,200	0.14
Arizona.....	44,610	.30	North Dakota.....	454,003	3.78
Arkansas.....	1,456,538	6.25	Ohio.....	8,175,524	4.29
Connecticut.....	1,843,243	4.43	Oklahoma.....	2,100,057	3.45
Georgia.....	2,421,410	5.91	Pennsylvania.....	11,201,132	4.00
Iowa.....	1,714,572	2.69	South Dakota.....	581,442	4.04
Kansas.....	1,144,467	4.16	Tennessee.....	2,747,536	7.20
Kentucky.....	1,620,604	3.77	Texas.....	7,000,402	6.03
Louisiana.....	4,111,377	7.10	Utah.....	348,269	2.27
Maryland.....	263,547	.76	Vermont.....	352,268	3.83
Mississippi.....	2,071,453	7.89	Washington.....	1,103,526	1.86

THE U. S. FEDERAL GOVERNMENT

Total revenue derived from tobacco..... \$530,150,000
 Percent of total revenue derived..... 1.10

Authority: Tax Policy, vol. VI, Nos. 2-3, December 1938, January 1939.

† Approximate.

That even more States and the political subdivision thereof, as well as the Federal Government, are at this moment contemplating adding to the great tax burden being carried by the tobacco farmers is made evident by the following data:

A 15-percent tobacco tax law in New Hampshire was approved by the Governor on June 7, bringing the total of States with excise taxes on tobacco products to 24.

The New Hampshire law goes into effect on July 1, and the State has announced that, since a 15-percent tax on popular-priced cigarettes would bring the tax per package to a fraction over 2 cents, it will forego the fractional part of the tax, keeping the levy at 2 cents per package.

The law establishing the tax directs that of the estimated annual yield \$1,000,000 be used to abate the real-estate tax.

On August 10, Massachusetts became the twenty-fifth State to impose a cigarette tax. The tax, effective September 1, is at a rate of 2 cents per package, and in addition the law provides for a \$25 wholesaler's license and a \$1 retailer's license.

The Massachusetts Act is unique among the 25 now in force in that it provides for the collection of the tax without the use of stamps or metering machines. In place of the conventional method of collecting the tax through the sale of stamps, Massachusetts will rely on monthly reports from distributors.

Commissioner Long estimates that a stamp system of collection would cost the State \$700,000 annually, and hopes to save a great part of this sum by the use of records and audits alone.

Authority: *Ibid.*, vol. 3, No. 8, August 1939.

May we now point out to the members of the Finance Committee that all of the above revenues, some of which are even now scheduled for increase by the States, which impose them, are collected in addition to the \$530,159,000 collected in the last year by the Federal Government.

In the States that now impose taxes on tobacco the volume of their sales decreased about 9 percent, whereas in the other States where there is no "State tax" and where they are still sold for "10 cents a package" they have gained 15 percent in their sales last year.

The daily press has carried a number of articles and news items telling of the "bootlegging" which went on in New York City after New York City put on its cigarette tax.

It was suggested that the loss in the sales in New York might have been taken up by New Jersey and Delaware.

Consolidated figures, however, on the sales in New York and New Jersey, presented by one concern which handles both States in their trade territory, showed that their sales fell off in both New York and New Jersey about 45 percent, while in Connecticut, another adjacent State, they lost 21 percent.

We would have you know with us that this was the direct result of the imposition of an extra 1-cent tax in New York City where they ran a "10-cent cigarette" above a 10-cent sale price. There the "10-cent tailor made" ran into direct competition with "the roll your own" and, as a result, the Federal revenue decreased.

It is estimated that between 20 and 25 percent of all cigarettes smoked today are made by the "roll your own." It is further estimated that in the last year some 43,000,000,000 cigarettes smoked were made by the "roll your own" cigarette machines. On these the Government would derive a tax of 1 cent instead of the present 6 cents a pack which is derived or the 7 cents per package tax proposed in this bill.

The attention of the Senate Committee on Finance is specifically directed to this one important fact. To wit:

That if in this case the cigarette tax is increased from 6 to 7 cents per package by the Federal Government through the adoption of the tobacco provision in H. R. 10039, and if, the manufacturers were able actually to pass it on to the consumer, then the question of "diminishing returns" would immediately enter into this problem in calculating the revenue that would be derived from the increased tax.

If the increase in tax diminishes the consumption by as much as even one package, it will require the sale of seven additional packages to make up the loss of the tax that will be sustained by the decrease in consumption of one package. If one cigarette customer is lost by increasing the tax from 6 to 7 cents, you would have to find seven more customers for "tailor made cigarettes."

The present cigarette tax levies emerge from World War financing efforts on the part of the United States Government. In many respects tobacco is different from other commodities, particularly from the standpoint of a revenue producer. Owing to its widespread use, tobacco offers a large and fairly stable volume of revenue. The tax imposed is paid a few cents at a time. It is paid largely by smokers who are not presumed to be easily detached from the habit of smoking or chewing.

That this is entirely erroneous is clearly proven by the history of the tobacco industry. Nothing could be more indicative of the ease with which the tobacco habits of the American people can be changed than the history of the plug and chewing industry in the United States. When taxes on chewing tobacco were 8 cents a pound the annual sales of that product amounted to nearly 180,000,000 pounds but, with each succeeding increase in Federal taxes the sales declined almost in direct ratio to the increase in the taxes imposed.

The average annual consumption of chewing tobacco for the 20-year period prior to 1919 was in the sum of 167,398,754 pounds annually. Under the 18-cent per pound tax rate and by the year 1938, the consumption had decreased to a mere 54,911,152 pounds, a decline under the 18-cent tax rate of 124,501,955 pounds or approximately 75 percent of the historic volume.

The records of the year, 1940, already show a still further decline in sales, and hence a further loss in the market for that class of the product of tobacco farmers whose crop is not suited for smoking, either in pipes or in cigarettes.

Temptation is strong among tax-making bodies to add to the tobacco-tax burden. To make demonstration of this point let us take the newly adopted tax policy of the State of New Hampshire as an example. New Hampshire is not a tobacco-producing State, therefore there are no tobacco farmers to protest tax increases. Their legislature, availing themselves of the ease with which tobacco taxes can be levied, decided to cut down the tax on real property, and by what means?

The law establishing the tobacco tax directs, "that of the estimated annual yield, \$1,000,000 shall be used to abolish real-estate tax."

However, there is such a thing as that of working a willing horse to death. All tobacco producers are already overtaxed in proportion to all other commodities. Other industries have been relieved of much of the extra tax burden imposed during and subsequent to the World War, but tobacco is still paying wartime tax rates and now proposal is made to impose supertaxes on the present overburdening rates.

The tobacco industry in all of its many ramifications provides a livelihood for hundreds of thousands of growers, warehousemen, buyers, industrial workers, salesmen, including those in advertising and radio industry. Increased Federal taxes upon this product may easily cripple much of this activity, already hard hit by the loss of foreign markets in consequence of the European war. Moreover, it is feared that what has happened to the plug, chewing, and twist industry may happen to the cigarette tobaccos as well.

Be assured that the tobacco farmer and the industry in general will make every sacrifice and "do their bit" in the American defense program. It would seem the wiser plan however, for the Congress, in the imposition of all taxes of this nature to broaden all bases, in order that no one industry or class of goods be unduly burdened to a point of abatement or extinction.

We believe that if Congress taxes tobacco still more and burden it still further, that you will place tobacco in a position where its continuation, not alone as a revenue-producing crop, but as a money crop to our farmers, is very problematical.

We heartily support the program for national defense. We are confident that there is not a farmer in the land that does not want this Congress to do the things that you are going to do in the matter of national finance and defense under H. R. 10039, but we ask in behalf of our tobacco farmers a fair apportionment of the expense. They stand ready to pay their part.

In presenting this argument against the proposal to levy supertaxes on tobacco and tobacco products, every effort has been made to avoid all sections: social, moral and cultural considerations of the problem. We have endeavored to address this brief solely from the standpoint of our national agricultural, tobacco and tax economies in their relation to the problem of national defense and to approach the same in a sense of equity and justice to the tobacco farmers of the Nation.

It is because of the foregoing, among other reasons, that as representatives of agriculture, we ask the Senate Finance Committee in their review of the provisions of H. R. 10039 to take into consideration the foregoing facts.

Confident as we are, that any increase in the taxes on tobacco will have most serious repercussions upon the tobacco farmers as well as the industry in general and because of that belief, this brief is respectfully submitted to the Senate Finance Committee in behalf of American Agriculture and particularly our tobacco farmers by--

THE NATIONAL GRANGE,
FRED BRECKMAN,
Washington Representative.

THE ASSOCIATION, SOUTHERN
COMMISSIONERS OF AGRICULTURE,
C. C. HANSON, *Secretary.*

The CHAIRMAN. We will now hear from Mr. Ogg, representing the American Farm Bureau Federation.

STATEMENT OF W. R. OGG, REPRESENTING THE AMERICAN FARM BUREAU FEDERATION, CHICAGO, ILL.

Mr. Ogg. Mr. Chairman, my name is W. R. Ogg, representing the American Farm Bureau Federation.

I have here a statement which President O'Neal requested me to present to your committee. It will only take about 5 minutes to read it, and in order to conserve the time of the committee I would like to ask the privilege of reading it, if I may, as it states the views of our organization on this bill.

The CHAIRMAN. All right.

Mr. Ogg. The American Farm Bureau Federation commends the work of the Congress in the preparation of a national-defense revenue measure. Our organization will continue to give our support to patriotic and nonpartisan legislation of this character.

Following the introduction of the original national-defense bill, H. R. 9966, I transmitted by telegram on June 3 to Senator Harrison, chairman of the Senate Finance Committee, and to Congressman Doughton, chairman of the House Ways and Means Committee, a resolution of our board of directors adopted that day in Chicago, stating our position relative to this matter, copy of which I should like to incorporate in the record.

(The resolution referred to is as follows:)

CHICAGO, June 4.—The board of directors of the American Farm Bureau Federation, in session here today adopted the following resolution and sent it to Chairman Pat Harrison and R. L. Doughton, of the Senate Finance Committee and the House Ways and Means Committee:

"We wholeheartedly support steps being taken by the President and Congress of the United States to strengthen our defenses in the present emergency. We recognize that this will impose new burdens upon the finances of this country and feel that the farmers and people of the country will willingly pay taxes that are levied equitably and expended efficiently for this purpose. We feel that it is important that burdens be imposed in accordance with ability to pay and that adequate tax provision be made to check all profiteering. Care must be taken to avoid further increases in hidden taxes upon our national consuming power. The pending measure proposing horizontal increase in all taxes does weigh primarily on consumption and upon low-income members of the community. Recognizing the difficulty in preparing a comprehensive and equitable tax measure to meet the expenditures that will be required we recommend that steps be taken to adjust the national debt limit as required by the emergency and that a congressional joint committee immediately be constituted with instructions to formulate at the earliest practical date equitable and adequate legislation to cover these and future expenditures for national defense. Sound legislation prepared by this committee will receive our patriotic support."

Mr. Ogg. (continuing). As indicated in this telegram, we felt that the proposal for a horizontal increase in tax rates, as contemplated in the bill as originally introduced, would be unwise because it placed an undue share of the burden upon the low-income groups. I am glad to note that the bill has since been very materially improved.

In the bill as originally introduced, about two-thirds of the proposed additional taxes consisted of consumption taxes and about one-third were based primarily on ability to pay. In the bill as it passed the House, approximately \$624,000,000 would be raised by income taxes, estate and gift taxes, and approximately \$380,000,000 would be raised from consumption taxes.

This adjustment in the tax burden more nearly to a basis of ability to pay is commendable. We approve the broadening of the income tax base. Our organization has advocated this for many years.

The increase in the total amount of revenues to be raised by taxation from about \$600,000,000 to a little over \$1,000,000,000 is likewise commendable. It accords with the growing need for revenue to meet not only our national defense requirements, but urgent domestic needs.

While we urge the passage of a bill at this time, we would like to make the following recommendations with respect to this bill:

1. We are especially concerned over the heavy imposts on specific commodities, most notably tobacco and gasoline. Since these taxes without exception, are passed on to the consumer or back to the producer, they are not ordinarily resisted by manufacturers and refiners. It becomes the responsibility of producer and consumer groups to warn against too heavy reliance on these levies, so long as our national fiscal problem is one of raising revenue rather than reducing consumption. We believe it is unwise to extend excise tax levies for 5 years ahead, in this temporary emergency tax bill.

We recommend that the tobacco taxes not be increased by 16% percent, as proposed in this bill.

In the case of tobacco, it is to be noted that present Federal taxes on this commodity now yield a total of approximately \$580,000,000, as compared with a total cash income to farmers from this commodity, totaling on the average only \$269,000,000 (1938 crop). We would also draw attention to the extremely serious situation now facing tobacco producers as the result of the sudden loss of the great portion of their export markets. It was necessary last autumn for the Commodity Credit Corporation to come to the rescue of the tobacco growers, and the situation during the present crop year promises to be worse, rather than better.

2. We regret that no provision has been made in this measure for taxation of excess profits, in particular the excess profits arising from production of and speculation in war commodities. We feel this is of vital importance and we hope that Congress will take steps to formulate proper legislation to this end.

3. We oppose the proposal which has been made in some quarters for a horizontal 10 percent reduction in all present appropriations. This method of cutting expenditures we feel to be arbitrary and unwise. It is one which may seriously handicap certain departments of the Government in meeting problems which have arisen out of the war emergency. We will give our support to sound measures of economy, but feel that especially at this time it should be on a careful and selective basis.

As expressed in the telegram to which I have referred, we believe that Congress also should immediately undertake a comprehensive revision of our revenue laws to provide for national defense and domestic needs so as to assure a sound fiscal policy and an equitable distribution of the tax burden. In formulating such a tax program, we feel that primary reliance should be had on taxes based upon ability to pay, such as income, inheritance, gift and excess-profits taxes, and that care should be exercised to avoid undue dependence upon consumption taxes, the effect of which would be to burden unduly low-income groups who make up the great mass of consumers.

While the present measure relies less heavily on consumer taxes than the original proposal for a horizontal increase, nearly 40 percent of the estimated total revenue will still come out of consumer expendi-

tures and will fall with greatest weight upon small incomes. We feel that such taxation checks the increase in total national income that is urgently needed at this time, while making more difficult the problems of post-war readjustment. The latter will be difficult, indeed, if we find our national income strangled by a heavy system of consumer taxation, while large untaxed incomes flow into idle pools of saving. Our organization will oppose further increases of consumer taxation until such time as income taxes have been put far above present levels.

In conclusion, we wish to reiterate our belief that farmers and all other groups of citizens stand ready to make any necessary sacrifice in support of measures for national defense and to bear their equitable share of whatever additional taxes are needed.

Thank you very much.

The CHAIRMAN. Mr. Davis, I understand you want to read a letter from Mr. Steinberg on behalf of the National Retail Liquor Package Stores Association, Inc.?

STATEMENT OF MANUEL J. DAVIS, PUBLIC RELATIONS COUNSEL, NATIONAL RETAIL LIQUOR PACKAGE STORES ASSOCIATION, INC., WASHINGTON, D. C.

Mr. DAVIS. That is correct, and I might state that I am just as willing to have the letter written into the record rather than read it in, in order to expedite matters.

The CHAIRMAN. Thank you, and it will be included in the record. (The letter referred to is as follows:)

NATIONAL RETAIL LIQUOR PACKAGE STORES ASSOCIATION, INC.,
Washington, D. C., June 13, 1940.

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

DEAR SENATOR HARRISON: H. R. 10039, a bill introduced in the House of Representatives by Mr. Doughton, provides for the expenses of national preparedness by raising revenue and issuing bonds, to provide a method for paying for such bonds, and for other purposes.

This bill is designed solely to raise such funds as the administration feels is necessary to meet its preparedness program. The National Retail Liquor Package Stores Association, Inc., comprising of over 32,000 retail liquor package store dealers throughout the United States, for off-premise consumption, is wholeheartedly in support of this bill and any other bill which the administration and Congress may deem necessary in the protection of our country. The members of the association are proud to be able to play such an important part in enabling this country collect the necessary funds to meet this emergency program and at the same time are undertaking an extensive program to educate the public to the end that the bootlegger will be destroyed and the taxes rightfully due and forthcoming to the Government of the United States will be collected into its Treasury.

Section 213, distilled spirits, set out in paragraph B on page 23, provides for the increase in the tax on distilled spirits of \$0.75 on each proof-gallon. In the drafting of this section it became very evident to the Ways and Means Committee that some provision must be provided for in order that the small independent retailer may not be destroyed in the interim between the effective date of the tax and at such time as they can readjust the price levels. In furtherance thereof, the Ways and Means Committee, in executive session, wrote a provision into the bill providing for an exemption of 100 wine gallons on the floor stocks of the retail merchants. It should be noted that this exemption merely applies to retailers.

It is readily understandable that the small merchant operating a package store in the United States cannot afford to pay this large sum of money unless a floor

tax exemption is herein provided for. A retailer's business is small and taking into consideration the State and city taxes which he pays in addition to the Federal tax, it is impossible for him to pay such a large sum of money if a floor tax exemption were entirely overlooked.

The retailers throughout the country are agreeable to any reasonable proposition which will bring relief to the small independent merchant. They are more than pleased that the Ways and Means Committee realized the condition of their business and provided an exemption in the bill.

We appreciate the fact that the Senate Finance Committee is cognizant of our problem. It should be noted that the Congress of the United States has never reported out a bill, wherein, a spirit tax was raised that they did not provide for a floor-tax stock exemption for the retail trade.

We are hopeful that you will give this matter the attention which we believe it deserves in the light that the retailer may receive the exemption so necessary to the condition of his business.

Very truly yours,

WILLIAM STEINBERG.

The CHAIRMAN. Mr. Marsh, yesterday you were not present and some others were not present whom we have heard since then, so we will hear you this morning. I wish you would be as brief as possible.

**STATEMENT OF BENJAMIN C. MARSH, EXECUTIVE SECRETARY,
THE PEOPLE'S LOBBY, INC., WASHINGTON, D. C.**

Mr. MARSH. I will be very brief.

I want to apologize to the committee for my misunderstanding of the appearance on yesterday, and I want to ask the protection of the committee for the first suggestion that I am going to make, and that is this:

That people in my class should pay two to four times as much Federal income tax as we do pay, including every blooming lobbyist in the city of Washington, and I am going to give you the reasons, as I see them.

Our democracy has proceeded upon the assumption that you could arrive by merely postponing the deluge. Our tax policy is an illustration. Totalitarian governments are the result of the failure of the efficiency of democracy, or of democracy to be efficient.

I want to give you a few figures showing how this House bill does not begin to tax incomes, and I am going to make a comparison of the total income taxes under the House defense bill for a married man, without dependents, and such a man in Great Britain with one dependent.

On a \$2,000 income here, no income tax; in Britain, \$171.25; on a \$4,000 income here, \$70.40; in Britain, \$796.25; on a \$6,000 income here, \$149.60; in Britain, \$1,421.25; and on a \$8,000 income here, \$316.80; in Britain, \$2,171.25.

Up to the \$8,000 in Britain, approximately 10 times as much is paid in the direct income tax for the classes I have mentioned, with this distinction that there the married couple has one dependent, here it doesn't have. When you come to the \$8,000 income, you will notice that it is only about 7 times as much in Britain as here.

The wealthy are evidently not afraid of Hitler's annexing the Western Hemisphere, or they would be insisting they be taxed as the British are. To me that is about the most reassuring thing regarding the safety of America, the complete failure of the wealthy to ask that they be taxed for national defense. When they start getting scared, I am going to get scared, too.

Real defense of the United States can be achieved only on practically a pay-as-you-go basis. And as I see Senator La Follette here, I recall that in the World War when his father was on the Senate Finance Committee, I appeared and advocated what I am going to advocate now, and every year since when you have had hearings on taxation, and, gentlemen, I hope you won't put off until tomorrow the writing of a definite and thorough-going tax bill.

I noticed this in the New York Times, the first column—I won't read the New York Times—but here are three lines:

"Congress to stay in Capital in fear of new war crisis," stating that the leaders have given up the plans of adjourning. I hope you will, gentlemen, because I don't need to tell you that we have lost the war on poverty, and unless we reorganize our country on an efficient basis we are going to fail to defend our country against enemies of poverty here or any aggression from abroad.

Don't get mad when I suggest that the Democratic platform tax plank should be resurrected for the duration of the defense program. That was an admirable tax plank in 1932, in the 1932 platform, thoroughly untouched to date.

Senator KING. You particularly refer to the plank of the platform pledging to reduce the taxes 25 percent, don't you?

Mr. MARSH. Well, I have got so used recently to having the administration promise two utterly contradictory things, and simultaneously to be carried into effect, that I have not been surprised any more. But I refer to the pledge to balance the Budget by taxation based on the principle of ability to pay, and it can be done. We might as well face it. You can't win any war by simply protecting the property classes.

Under the House bill, as I understand it, only about \$70,000,000 more will be obtained from the corporation income taxes and \$252,000,000 more from the personal income taxes. The corporation tax should yield at least \$250,000,000 more. Now that seems a low figure, but I am quite sure that the administration is planning, which I think is very wise, to keep down profiteering prices, and I think it is necessary, for United News charges that one reason for the failure of the Allies to date is that they couldn't get the material which their buying commissions came here to get, because they were charged such exorbitant prices.

If you want me to read four or five lines on that, I will do so.

The CHAIRMAN. No; that is not necessary.

Mr. MARSH. If they don't maintain prices and prevent high profits, then they should raise \$1,000,000,000, at least, through the profits tax; and the individual tax should raise at least \$1,500,000,000 more, with the present national income. The Treasury Department can give you, in about a week, I understand, maybe a couple of weeks, certainly before the Democratic Convention is over, the rates necessary to yield these amounts.

Third, we recommend in addition to these progressive taxes on incomes, personal and corporate, an excise tax on the privilege of owning land, based on the value, with a small exemption which would exclude the little-home owner and the little farmer, but would make the Morgenthau's and the Astors and the Roosevelts pay a lot more tax on their land.

Senator GEORGE. Down my way, we pay a tax for the privilege of owning land.

Mr. MARSH. It is strange that you haven't attracted more people from up North, then. Such a tax would yield \$250,000,000.

The House tax bill compels families with incomes under \$2,500 to pay most of the additional revenue to be raised, and the Government will borrow almost all from families with incomes over \$3,000.

Of course, we hope you will repeal the tax-exempt feature. I think you will have to make it retroactive, and take a chance, I am pretty sure the Supreme Court is well enough housebroken now [laughter] so that they would entirely uphold any such emergency legislation, and let me add that I own some tax-exempt bonds, and I want to be taxed on them.

I would like to file, if you will permit me, a short statement on "What the income tax could yield," by Congressman Hill of Washington.

The CHAIRMAN. All right.

(The statement referred to is as follows:)

WHAT THE INCOME TAX COULD YIELD

Extension of Remarks of Hon. Knute Hill, of Washington, in the House of Representatives, Tuesday, March 5, 1940

RADIO ADDRESS BY HON. KNUTE HILL, OF WASHINGTON

Mr. HILL. Mr. Speaker, under leave to extend my remarks in the Record, I include the following radio address which I delivered over the Columbia Broadcasting System at a luncheon of the People's Lobby, March 2, 1940.

"During these early days of the month of March a great many of us are engaged in making out our annual income-tax reports. It may seem rather strange to some when I say that this is one of my pleasant duties. In these days of so much unemployment and distress, I for one, am certainly thankful that I am permitted to earn an income on which to pay a tax. Taxes should be levied on the basis of ability to pay and benefits received. It takes money to run a complex modern government; and we who receive the benefits and protection of that Government and have the opportunity of earning an income because of the existence and functioning of that Government should be glad and willing to bear our share of the expense in connection therewith. To those who are disposed to complain may I call attention to income taxes paid in Great Britain:

"An Englishman with a wife and one child will pay in income taxes this year as follows:

Income:	Tax
\$2,000.....	\$171. 25
\$4,000.....	796. 25
\$6,000.....	1, 421. 25
\$8,000.....	2, 171. 25

"Statistics are rather tiresome but let me just briefly outline the situation in the United States:

"Figures recently reported by the Treasury Department on personal incomes for 1938, and Treasury data on corporation profits, show that the Federal Government could get at least two to two and a half billion dollars a year more than it does, from taxes on personal and corporation income.

"The Treasury reports that in 1938, almost 3,000,000 taxable incomes were reported, with a total net income of about twelve and two-thirds billion dollars.

"Upon this enormous income the total Federal income tax, and surtax was only \$765,000,000, an average of \$255, or 6 percent.

"The average income of these nearly 3,000,000 individuals was \$4,215.

"If these 3,000,000, who received the major part of rent, interest, and profits paid in 1938, had paid an average of about \$700 more in income tax and surtax, they would still have had left an average of about \$3,500—which was nearly three-quarters more than the average family income in 1938.

"This would have given the Government a little over \$2,000,000,000 more than it got from income taxes and surtaxes in 1938.

"Of course, under our system of progressive income taxes and surtaxes, people with incomes under \$5,000 would not pay much more income tax, not over \$100 to \$150 more at most, while those with incomes of over \$10,000 could pay \$1,000 to \$50,000 more than they do.

"In 1938 almost 176,000 people reported net incomes of over \$10,000 with a total of \$3,987,000,000, upon which they paid just under \$625,000,000 in taxes. After paying these taxes they had left \$2,000,000,300, an average of \$13,433.

"In 1936 the reporting corporations paid in cash and stock dividends over seven and a half billion dollars. In 1939, 3,058 companies paid \$3,241,000,000 in dividends. In 1939, 3,239 companies paid \$3,566,000,000.

"In addition to these huge dividend payments, the surplus and undivided income of corporations, estimated on their reports for 1936, are about \$50,000,000,000.

"This is more than the total national debt, upon which the interest payment alone, next year, will be \$1,100,000,000.

"Every year about 20,000 people get nearly one-third of all dividends paid, and they also have rights to about one-third of the \$50,000,000,000 of corporation surplus and undivided profits.

"On the basis of British income-tax rates, we could raise nearly \$3,000,000,000 more in income taxes than we do, through the personal and corporation income tax.

"Today the National Government raises nearly three-fifths of its income by taxes which fall heaviest on those least able to pay.

"You are probably asking yourselves why Congress doesn't change this tax system, now, and tax according to ability to pay. The real reason is that those who could and should pay are opposed to it.

"Every progressive Member in both branches of Congress, and in all parties represented, want Congress to do this. No individual Member, however, and no small group of Members can force this.

"Under the Constitution all revenue bills, that is, tax bills, have to start in the House of Representatives. That means the House Committee on Ways and Means has to have hearings on amending the present revenue act. The chairman of the committee is the Honorable Robert L. Doughton. If enough people will write him, urging that his committee hold hearings, and get their Representatives to also ask him, the hearings can be held.

"Unless income-tax rates are raised, needed relief and farm-aid must be cut. The American people must make themselves heard on this question in Washington.

"We must revise our outmoded tax system so as to place the burden of taxation on those best able to pay and in such a way as to make collections certain and economical and, lastly, to raise enough revenue to run our Government and retire our debt."

Mr. MARSH. And I would also like to file an article on "Income Tax Deductions," because I hope you will repeal all these increases in consumption taxes. The little fellow who can't deduct one penny or one dollar before he pays sales tax, and those consumption taxes, and those who filed incomes made deductions of \$1,600,000,000—it is a short article and I think it would be helpful.

The CHAIRMAN. It may be incorporated.
(The statement referred to is as follows:)

INCOME TAX DEDUCTIONS

The Bureau of Internal Revenue reports that for the year 1937, the total net income of the 608,575 persons, not families, reporting net incomes over \$5,000, was \$8,816,000,000.

Their total deductions were \$1,600,200,000, or about one-fifth of their total income.

Of these deductions, \$431,600,000 were taxes paid to State and local governments, but that still gives one and one-quarter billion dollars deductions for some 500,000 families—which is a lot.

Suppose you have an income of \$2,000 a year, and a wife and three minor children—or even only two—and have to pay \$400 a year rent.

You don't get any deduction for that rent, even though \$150 of it is taxes—which of course you pay in your rent.

The Bureau of Internal Revenue shows that in 1937, 57 percent, nearly three-fifths, of the aggregate income of those having over \$5,000 incomes, was from ownership or control of property.

They didn't need heavy deductions, but got them.

There are no deductions before paying sales taxes and other consumption taxes—which amount to three-fifths of all taxes collected by Federal, State, and local governments.

The 49 persons receiving in 1937, incomes over \$1,000,000 had a total income of \$85,400,000, and deductions of \$18,300,000, and had left on the average, after paying all taxes and deductions—\$1,369,390.

Stockholders got a much bigger cut of the national income in 1937 also.

In 1933 they got 4.9 percent, and in 1937, 7.2 percent.

Stockholders' share of the national income in 1937 was 47 percent, nearly half, larger than it was in 1933.

America has about \$6,000,000,000 of involuntary unemployment, and poverty due to taxation of poverty, instead of taxation of land values, incomes, and estates.

No—we can't blame either Hitler or Stalin for that—just our fool selves.

Mr. MARSH. I thank the committee for its courtesy.

The CHAIRMAN. All right, thank you.

Senator King has been requested by someone representing the moving-picture industry to give them an opportunity to be heard.

Mr. Pettijohn.

**STATEMENT OF CHARLES C. PETTIJOHN, GENERAL COUNSEL,
MOTION PICTURE PRODUCERS AND DISTRIBUTORS OF AMERICA,
INCORPORATED, NEW YORK, N. Y.**

Mr. PETTIJOHN. Before submitting to you what we believe to be a practical and economically sound plan for producing revenue slightly in excess of what has been contemplated, may I very briefly call your attention to a very serious situation confronting the American motion-picture industry today. I say "slightly in excess," gentlemen. That may sound strange, but in distributing it in what we believe by past experience, not what might happen but what has happened before, we find that we do have in excess of what was originally contemplated under the bill which has passed the House.

Senator KING. That is, you are advocating—

Mr. PETTIJOHN (interposing). More money, but easier for us to raise, briefly putting it in that form.

Up to the present moment our industry has lost approximately 75 percent of our foreign markets, which amounted, in normal times, to about 40 percent of our total gross revenues. In addition to the loss of that revenue we are faced also with the absolute necessity of keeping up the quality of our product, making it better, if possible, and more attractive to our customers, just as we have done year after year.

Also we must keep the price of that product within the reach of every man, woman, and child in the only markets we have left. We must keep alive and open every theater in every city, town, village, and hamlet in the United States. These theaters are more of a necessity today than they were 6 months ago.

They have a moral value and did have once before.

It is my sincere belief that there is not a single individual in any branch of the motion-picture business who is not ready and willing to do his bit to help your committee meet not only the present crisis but any future crisis, and we anticipate in this schedule that there may be additional moneys asked for, possibly next year, or the year after, but we have set up our house in such order that it is much easier for us to absorb it and meet it and economically administer it.

The sole question is how best to do it and keep our industry economically sound.

Just a few more words about our foreign problem. What few sales still being made abroad are, of course, hampered by rates of exchange, embargoes, and other restrictions. For instance, Germany was the first to place restrictions on account of a gold embargo. Then when Germany annexed Austria, Czechoslovakia, Poland, and now has invaded Holland, Belgium, Norway, and so forth, the same conditions prevail. There is no income derived now from those countries and no one knows what the future may be.

American motion pictures are entirely out of Italy. Since the hostilities of the present war began, France placed an embargo and England has only a temporary arrangement for this year's product only and which permits a small portion of the revenue to be taken out. In other words, almost weekly during late months, our foreign markets have diminished under the feet of invading armies.

Now, I had no experience in the operation of theaters. I have had no such experience, don't know a thing about it. I am speaking from the production and distribution angle.

The CHAIRMAN. Do you represent the exhibitors?

Mr. PETTIJOHN. No; I am going to come to that real quickly. Sitting here in the front row is Mr. Carter Barron of our own city here in Washington, who operates a large circuit of theaters; also Mr. S. P. Skouras, who started with a little theater in St. Louis, and is now known throughout the trade without any question as not only one of the soundest but most efficient operators of all times, of theaters, and he is a man who has been very highly successful.

These men have drawn in their own language, and neither of them are lawyers, a memorandum which is very brief, and which I would like to read, and then if the committee would like to have it, I will give each one of you a copy. I say this isn't in legal phraseology and that might prove to be refreshing for once to this committee, because it is based upon their experience that they have had in the operation of all types of theaters, and in my honest opinion it is absolutely and accurately a reflection of the real problem that confronts us. This memorandum, and it is brief, reads as follows:

Sixty million dollars in Federal taxes from the motion picture theaters of this country, instead of the twenty-five millions anticipated by the Government in its new revenue measure, is the suggestion in this plan, with the hope that it will be seriously considered.

The present tax bill H. R. 9966, proposes to reduce the tax exemption now starting at 41 cents, down to 31 cents. It is estimated, to increase Federal revenue from motion picture theaters from about \$9,000,000 presently returned, to a potential \$25,000,000. Under the proposal here outlined the Federal Government will collect from the very same source approximately \$60,000,000 each year.

To bring about such a return we recommend that the tax bill, as it affects motion-picture admissions, embody this schedule: Up to 9 cents, no tax; 10 cents to 25 cents, 1 cent on each admission; 26 cents to 49 cents, 2 cents on each admission; 50 cents and up, 10 percent as is currently in effect.

This schedule will yield approximately 60 millions in taxes, based on an estimated 80,000,000 to 85,000,000 admissions nationally each week, on a conservative estimate of 1½ cents tax per admission.

Various estimates, based on various cross-section groups of theaters produced very similar results, indicating that the United States Department of Commerce is accurate in their statement that the

average price of admission to motion-picture theaters in the United States is somewhat between 24 and 25 cents. It therefore becomes apparent, that under the schedule submitted herewith that approximately one-third of the revenue would be derived from those paying an admission of 25 cents or less, and two-thirds from those paying in excess of 25 cents.

There is a vital question of economics involved that cannot be unheeded. When the present 40-cent tax level was made law, there were about 2,500 theaters charging 40 cents or more. Because of that law there are today less than 150 theaters charging 40 cents or more. Why?

Because ours is a highly competitive business. A theater charging 45 cents when that became law, was faced with the need of charging 50 cents so that the tax could be absorbed. Theater operators found that business would be vitally affected. So a general practice came into being and that 45 cents admission was reduced to 40 cents. Thus theater attendance was sufficiently increased for awhile to absorb what would have been decreased attendance. But the Government lost revenue. Yet the industry suffered, too.

A reduction of the tax level to 30 cents will unquestionably revive this wave of price-cutting. Precisely what happened in 1933 is certain to prevail again. Theaters now charging 35 and 40 cents will drop to a 30-cent admission. Similarly, to meet this competition smaller theaters will drop to a quarter, with correspondingly lower levels on down. This means still less revenue for the Government, and unsurmountable set-backs for the industry. Prices now in effect are at their lowest possible level; they cannot be reduced. The industry cannot stand these further inroads.

The motion-picture business is not a domestic business. It is an international business. Its market is world-wide. Its production costs are based on world-wide distribution. Before the present march of hatred and destruction abroad, 35 to 40 percent of our total revenue came from abroad. Today that foreign market and revenue are virtually nonexistent. The swiftness with which Europe, as we know it, is vanishing bodes an almost complete annihilation of our markets abroad.

Thus we must stabilize our American market. A reduction of admissions will immediately call for fewer and less expensive pictures. This in turn foreshadows curtailment of personnel. It also means a poorer quality of product. It means, too, that our Government will face severe losses in income taxes from this important industry. Neither the film industry nor the Government can conscientiously sanction a plan which is economically unsound. Particularly so when the industry stands ready with a sound, practical plan.

Senator BAILEY. How much more than the House bill?

Mr. PETTJOHN. The difference between \$25,000,000 and \$60,000,000 per year.

A plan which serious minds of the industry believe to be sound; a plan which provides the Federal Government \$25,000,000 more each year than H. R. 9966 proposes to get, and a plan that will maintain and perhaps improve the present economic position of the business itself.

We submit this plan, with the knowledge that among its virtues is that it will erect a Maginot Line against the toppling of this business

for the little-theater owner who above all cannot afford reduced admissions. The smaller operator works on a limited budget. And a limited margin of profit. Unlike the large theater which can hope to retrieve loss of revenue through reduced admissions by larger seating capacities, the little fellow cannot have this hope. His business is gaged by an admission lower than that of larger theaters. Force the larger theaters to reduce prices and you force the smaller operator to meet that competition. For him that is economic suicide.

Incidentally, if it should not be found practicable to adapt this schedule to forms of admission other than motion-picture theaters, it might be adopted for motion-picture theaters only because of loss of revenue to the industry from foreign markets with which no other forms of admissions are faced today. In other words, this formula will bring to the Government more revenue than the present schedule adopted by the House on June 11, will help the motion-picture industry to maintain its present economic structure, in the face of all of its present difficulties. It will be of particular service to the small-town theaters, whom the industry must keep in business in times such as these.

Senator RADCLIFFE. Is it your opinion that the House bill would cause a reduction in the rates?

Mr. PETTIJOHN. Yes.

Senator RADCLIFFE. And that your suggestion would not cause any reduction but there might be an increase along certain lines?

Mr. PETTIJOHN. May I be perfectly frank about that, Senator, and very brief?

We have for years been selling a Rolls Royce in a theater at the same price as we sell our Fords and Chevolets—the admission is the same for a knock-out picture as it is for a cheaper production. We cannot base the success of a picture on the costs of production. A picture which costs \$300,000 may be worth three times as much as a picture that costs \$800,000. We can't base it on box-office value because we do not know that until after the picture has been out for some time. We are confronted with difficult economic problems.

It is like Rembrandt painting a picture. He may paint a very large one on the wall, and take a lot of time, and he may paint a very small picture, and the small picture may be worth a great many more times what the large picture is.

And that has been true in this case. You can't anticipate that. Nobody tries to make a bad picture.

But I do say this, this is one thing we want to avoid and we are now faced with doing something we never had to do before, because of this loss of the foreign market. We are going to be forced, gentlemen, and this I say to you in all frankness—there may be a difference of opinion in it, but watch and see if I am not right—we are going to be forced to take our 12 to 15 best outstanding pictures each year, and we are going to have to charge more money for them than we do for what you call "horse operas," the western pictures and the cheaper grade of pictures.

Now, don't think I am stating anything wrong about David Selznick, because the Senator and some of the others on this committee know that I was his father's lawyer, and practically raised the boy. He was like a brother to me. He made *Gone With the Wind* and it was a great picture, and the public did give \$1.10 to see it, and the

theater men did give up 70 percent of their gross for it. But, gentlemen, we can't run the picture business by charging the public \$1.10, we have got to have the best pictures we make every year going to the smallest theater in the land, in the smallest village, town, and hamlet, and that is the biggest thing about our business today.

Give us 10 *Gone With the Wind's* next year, and we won't worry about any of these taxes, but they come only once in a decade, we can't depend on them. We have got to face this problem and there are some men in our business, there are some good businessmen in our business who face these economic problems logically.

We ask you only to give us a tax program that is economically sound, and we anticipate now—I will say it to you very frankly—that maybe we will be asked to go still further, but we will have the structure built that will permit us to do it in an economic and a sensible manner.

Senator KING. You are absolutely sure that this will give to the Government a great deal more than under the House bill?

Mr. PETTIJOHN. Yes; and I have submitted my figures to Mr. Stam.

The CHAIRMAN. Mr. Pettijohn, would you mind talking to the Assistant Secretary of the Treasury in charge of these matters?

Mr. PETTIJOHN. That will be a pleasure.

The CHAIRMAN. Because in considering this matter we will have to seek the views of the Treasury.

The CHAIRMAN. For the information of the committee, I wish to have incorporated in the record certain letters, telegrams, and briefs addressed to the chairman by Mr. Fred A. Caskey, general counsel, Distilled Spirits Rectifiers, Inc.; Mr. Henry F. Long, commissioner of corporations and taxation, State of Massachusetts; Mr. Lee Pressman, general counsel, Congress of Industrial Organizations; Mr. Noel Sargent, secretary, National Association of Manufacturers; and Mr. Richard A. Staderman, president of the American Good Government Society. In addition, I wish to incorporate in the record a letter addressed to me by Mr. J. E. Savacool, vice president and comptroller, Mack Manufacturing Corporation, Long Island City, N. Y., which communication was handed me by Mr. John E. Walker, an attorney of Washington.

(The letters, etc., referred to by the chairman are as follows:)

LEAGUE OF DISTILLED SPIRITS RECTIFIERS, INC.,
Washington, D. C. June 13, 1940.

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

SIR: The League of Distilled Spirits Rectifiers, Inc., is the national trade association of the independent rectifiers of distilled spirits. Obviously league members are vitally interested in the bill H. R. 10039, now pending before your committee.

At the outset we desire to state most emphatically that it is not the purpose of any member of this league to shirk the obligation which he owes to bear his just proportion of the additional tax burden, which we appreciate must be imposed at this time in order to meet the national emergency. On behalf of the members of the league I wish to state that we are in entire accord with the provisions of the bill as they now stand.

Section 1650 of the bill proposes to amend the Internal Revenue Code so as to provide for a supertax for 5 years by increasing the present rate of excise taxes with respect to 43 different items listed in said section. It is proposed *inter alia* to increase the occupational tax now imposed upon rectifiers under section 3250 (f) (1) of the Internal Revenue Code from \$100 and \$200 to \$110 and \$220 per

annum, or an increase of 10 percent. This proposed increase is in line with the increases proposed in the cases of the other items listed in section 1650, and no objection whatever is noted with respect to this proposal. On the contrary, the members of this league are in entire harmony with the proposed increase, since the tax burden is fairly distributed among the taxpayers affected.

Section 213 of the bill proposes to increase the tax on distilled spirits generally from \$2.25 to \$3 and the tax on brandy from \$2 to \$2.25 per proof gallon. No objection whatever is noted with respect to these proposed increases in tax. Both the tax on distilled spirits generally and the tax on brandy will be passed on to the rectifier when he purchases these basic commodities for use in the manufacture of his products. These taxes will be borne by the distiller and the rectifier alike, and the competitive position of these two branches of the industry will not be affected by the proposed increases.

Section 14 of the original House bill, H. R. 9906, contained a provision under which it was proposed to increase the rectification tax of 30 cents per proof gallon, now imposed by section 2800 (a) (5) of the Internal Revenue Code, to 40 cents per proof gallon. This provision was stricken from the bill by the House Ways and Means Committee. We submit that any increase in the rectification tax over the 30 cents per proof gallon now provided by law would result in an unjust discrimination and unnecessarily penalize the members of the rectifying industry.

In order that our position may be clearly understood it is necessary to review briefly something of the history of the internal-revenue taxes heretofore imposed upon rectifiers as "occupational" taxes and as "gallonage" taxes on the products of rectification. A so-called occupational tax on rectifiers of distilled spirits was first imposed by section 59 of the act of July 20, 1868, and the tax on its present form was imposed by section 1 of the act of April 10, 1869. This is the tax which we have already referred to and which it is proposed to increase in section 1650 of the bill. As heretofore stated, no objection whatever is voiced with respect to this proposed increase.

The first tax on the production of distilled spirits became effective on August 1, 1862, and the rate of tax on the production of distilled spirits has fluctuated widely, as indicated by the following schedule:

Aug. 1, 1862 to Mar. 7, 1864.....	\$0. 20
Mar. 7 to July 1, 1864.....	. 60
July 1, 1864, to Jan. 1, 1865.....	1. 50
Jan. 1, 1865, to July 20, 1868.....	2. 00
July 20, 1868, to June 6, 1872.....	. 50
June 6, 1872, to Mar. 3, 1875.....	. 70
Mar. 3, 1875, to Aug. 27, 1894.....	. 90
Aug. 27, 1894, to Oct. 3, 1917.....	1. 10
Oct. 3, 1917, to Feb. 25, 1919:	
Basic rate.....	2. 20
Withdrawn for beverage use.....	3. 20
Feb. 25, 1919, to Jan. 1, 1927:	
Basic rate.....	2. 20
Withdrawn for (from Nov. 23, 1921, if "diverted to") beverage use.....	6. 40
Jan. 1, 1927, to Jan. 1, 1928:	
Basic rate.....	1. 65
Diverted to beverage use.....	6. 40
Jan. 1, 1928, to Jan. 11, 1934:	
Basic rate.....	1. 10
Diverted to beverage use (prior to repeal of prohibition, Dec. 6, 1933).....	6. 40
Jan. 12, 1934, to June 30, 1938.....	2. 00
July 1, 1938, and thereafter.....	2. 25

From 1860 no tax was imposed upon rectifiers of distilled spirits other than the occupational taxes of \$100 or \$200 per annum, depending upon the quantity of spirits rectified, until the War Revenue Act of October 3, 1917. Section 304 of the latter act imposed a tax of 15 cents on each gallon of distilled spirits rectified, purified, or refined in such manner that the person so operating would be a rectifier within the meaning of section 1 of the act of April 10, 1869 (now sec. 3250 (f) (1) of the Internal Revenue Code). The so-called gallonage tax on the act of rectification was, therefore, in its inception an emergency war revenue measure.

It will be noted that section 300 of the War Revenue Act of October 3, 1917, also increased the tax upon the production of distilled spirits to a basic rate of \$2.20 per gallon, or \$3.20 per gallon if withdrawn for beverage purposes.

The act of February 24, 1919 (commonly known as the Revenue Act of 1918), increased the rectification tax to 30 cent per proof gallon (sec. 605) and also provided for a tax of \$6.40 per proof gallon on distilled spirits in bond, or that might thereafter be produced or imported into the United States, if such spirits were withdrawn for beverage purposes or for use in the manufacture or production of any article intended for use as a beverage. This was the highest rate of tax ever imposed by the Congress upon distilled spirits for beverage purposes, and the same tax rate continued until the repeal of prohibition on December 8, 1933, although under the provisions of some later acts, and during the prohibition era, the differential between the basic rate and the beverage rate was held to be in the nature of a penalty rather than a tax (*Waterloo Distilling Corporation v. United States*, 51 (S. Ct. 282, 282 U. S. 577)).

Let us consider next the period immediately following repeal of the National Prohibition Act. It is significant that in the act of January 11, 1934, section 1150, the Congress provided for a tax of \$2 per proof gallon on all distilled spirits produced or imported into the United States from and after January 12, 1934. In other words, both the emergency created by the first World War, as well as the prohibition era, had now come to a close and the Congress accordingly determined the fair and proper rate of tax which should apply to the production of distilled spirits under normal conditions. That rate was fixed at \$2 per proof gallon, as contrasted with the \$6.40 per gallon rate imposed by the act of February 24, 1919, on spirits withdrawn for beverage use. But nothing whatever was done with respect to the rectification tax. This tax was born as a war-revenue measure. It was originally fixed at 15 cents per gallon in 1917, and subsequently increased to 30 cents per gallon by the Congress in February 1919. Clearly, this tax should have been repealed in its entirety, or the rate should have been drastically reduced as in the case of the distilled-spirits tax, and many other war taxes, after the emergency was over. No such action has been taken, however, and the rectification tax has continued at the wartime peak of 30 cents per proof gallon specified in the act of February 24, 1919.

Any increase in the gallonage tax on rectification at this time, we submit, would impose an unwarranted penalty and burden upon a relatively small group of taxpayers who cannot afford to pay any further taxes and continue to maintain their position in competition with the bottlers of straight whisky. The rectifier has been paying taxes at a wartime peak ever since the enactment of the Revenue Act of 1918. To add to his burden by increasing the gallonage tax at this time would result in such a gross inequity that we feel confident that once this matter is brought to the attention of your committee, the equities of our position will be fully apparent and no action will be taken toward increasing the rectification gallonage tax.

At the hearing before your committee yesterday morning some discussion took place with respect to the difference in cost of production of a blended whisky, manufactured in part from neutral spirits, as compared with the cost of production of a straight whisky. It should be borne in mind at the outset that, from a tax standpoint, no advantage is gained by the rectifier who produces such a blended whisky. For example, under the distilled spirits rate proposed in the bill, 2 gallons of straight whisky at 100 proof would bear a tax of \$3 per gallon, or \$6. On the other hand, let us assume that a rectifier uses 1 gallon of 100-proof whisky and 1 gallon of 100-proof neutral spirits in preparing a blended whisky. He would have to pay a tax of \$3 on the gallon of straight whisky used, and \$3 on the gallon of neutral spirits of 100 proof, or a total tax of \$6, which is the identical amount paid by his competitor who produced the straight whisky. It is apparent, therefore, that there is nothing to equalize between the rectifier and the bottler of straight whisky from a tax standpoint.

The complaint is made, however, that the producer of the straight whisky is obliged to pay carrying charges while the whisky is aging and that, therefore, he is placed at a disadvantage as compared with the rectifier, who uses an amount of neutral spirits in preparing a blended whisky, since the neutral spirits do not require aging. One of the common errors indulged in by those who advance this line of argument is that they invariably add 4 years carrying charges in computing the cost of the straight whisky, although it is a fact of common knowledge that the vast bulk of straight whiskys on the market today are much less than 4 years old. Generally, these same individuals also lose sight of the fact that the carrying charges on the whisky used by the rectifier in the manufacture of a blend are passed on to him by the distiller. By ignoring these factors, an entirely unwarranted cost differentiation is generally presented by the proponents of the increase in tax. But conceding, for the sake of argument, that there exists a

difference in cost of production of a so-called spirit blend, as compared with a straight whisky, and assuming that this presents a proper field for Federal taxation, we submit that such tax should not be in excess of the rates now imposed.

It was argued at the hearing yesterday morning that the cost of production and carrying of whisky was higher today than it was in 1919 and that, therefore, the rectification tax should be increased. This argument loses sight of the fact that there is necessarily a corresponding increase in the cost of doing business by the rectifier. Furthermore, we most strongly urge that any tax which attempts to equalize an advantage which one branch of an industry enjoys over another by reason of scientific progress and changes in the art of manufacture and production of a commodity is not a tax at all, but an unwarranted interference with industry. We know of no case where a tax on such a basis has ever before been imposed by the Congress. The measure of the tax should be a reasonable levy for the privilege of engaging in the operations which are the subject of taxation. We submit that the present gallonage tax of 30 cents per gallon, together with the occupational taxes of \$110 or \$220, which the rectifier will pay under the bill, constitute the very limit of the payment which should be exacted. It is a heavy price to pay for the privilege of engaging in the rectifying business. In this connection we call attention to the fact that while the rectifier pays an annual occupational tax of \$110, or \$220, depending upon the extent of his operations, no occupational tax whatever is imposed upon the distiller who bottles straight whisky.

A further important feature, which is generally overlooked by those who favor an increased tax, is the fact that there are a great number of popular blends on the market today which are manufactured entirely from pure straight whiskys and without the use of neutral spirits. If any of the component whiskys in such blends are less than 4 years old, they are subject to the rectification tax. Furthermore, there are likewise a number of excellent blends of pure straight whiskys more than 4 years old which contain some slight amount of blending material, and these blends are likewise subject to the rectification tax. In addition, the rectifier who produces cordials, liqueurs, specialties, or cocktails must pay the rectification tax. It is at once apparent that any argument which might be advanced with respect to spirit blends—and that is the only argument that has been advanced in support of the proposed increase in the tax—is entirely inapplicable in the case of these latter products. And yet they are all subject to the rectification tax, just as is the spirit blend, and they would likewise have to bear any increase in the tax rate without any offsetting advantage whatsoever. This demonstrates the gross inequity that even now exists in the rectification tax and which would be aggravated to such a point that the very life of the business of industry members would be jeopardized if any increase in tax should result.

We have been challenged to show a reason why the rectification tax should not be increased by 33½ percent at the present time, since the tax on distilled spirits is being increased by that amount. The following table shows the results which would obtain if the rectification tax had been adjusted to keep pace with the tax on distilled spirits for beverage purposes, beginning with the Revenue Act of 1918, which imposed the highest rates on both taxes:

	Distilled-spirits tax	Rectification tax
Revenue Act of 1918.....	\$6.40	30 cents.
Liquor Taxing Act of 1934.....	2.00	9.3 cents (reduction 69 percent).
Revenue Act of 1938.....	2.25	10.4 cents (increase 12½ percent).
H. R. 10039.....	3.00	13.8 cents (increase 33½ percent).

We think the foregoing figures furnish an entirely adequate answer to the above challenge. If the rectification tax had been adjusted to correspond to the reductions and increases in distilled-spirits tax, the rectifier would be faced with a tax of only 13.8 cents per proof gallon in H. R. 10039. Instead of that happy situation, however, he now pays a tax under existing law of 30 cents per proof gallon, just as he has always done, ever since the enactment of the Revenue Act of 1918. Under these circumstances, we submit that there can be no justification whatever for any increase in this already overwhelming burden.

Respectfully submitted,

FRED A. CASKEY, *General Counsel.*

Hon. PAT HARRISON,
Washington, D. C.:

Finding it impossible to reach Washington to attend the public hearings today and tomorrow am hoping that you will permit me, through this telegram, to call to your attention the worth whileress of making the revenue bill now before you temporary until the next session of Congress instead of having it run for the period apparently established. Am unable to wire in respect to detail because discover that bill available to me in print has had many amendments and the effect of this it is difficult to sense instantly. It does occur to me that the Federal Government perhaps more now than ever would desire not to enact a Federal revenue measure which will interfere with the revenue production of the States to an unfair extent.

The States are and will be faced with substantial burdens and there are tax structures developed that will be seriously affected, as I see it, by the passage of the new revenue bill. This is particularly true in respect to Massachusetts where the tax structure contemplates a completely balanced budget each year by interlocking the State, its 14 counties, and 351 cities and towns, so that by one supplementing the other the ultimate tax bill on property satisfies the entire governmental requirements of that year. In the process of keeping stable this structure which does not ever permit a deficit or a surplus various subjects as well as persons have been subjected to a tax either in the form of a property tax or an excise. The proposed Federal bill cuts into Massachusetts in respect to individuals and corporations subject to the income tax by further invading a source which because of the high rates in the existing Federal revenue bill has already forced the State to employ supplementary measures for financing its government on the three layers of State, county, and municipal.

It seems to me to be fair that Massachusetts have an opportunity to be heard before a permanently established or even a temporarily established structure is developed other than for the immediate emergency in order that their tax structure may not be in danger. The proposed rates seemingly have been written into the bill without any regard to the States' tax structure. While the inroads and the effect on Massachusetts will be great in respect to the corporate and individual income tax, the effect on them in respect to the inheritance tax and excise generally is going to be very severe and it will not be easy to amend so as to give the States a place in revenue production after the law has been put upon the statute books as proposed by H. R. 9966, which, I understand, is still the number of the bill before you.

This is a plea to make this bill if the existing features of it are to be maintained only for the balance of this period so that the next Congress can have before it for consideration a bill which the Treasury Department, I am hoping, will draft after consultation with the States and bring about a result which will bring the necessary revenue to the United States but will not merely for the sake of a small amount of revenue disrupt the State tax structures and make impotent some of their present revenue measures. The particular effect on the States is going to be in relation to the excise on gasoline, liquor, and tobacco. Massachusetts has a tax on each of those and as it is obvious that the tax ultimately falls on the consumer every tax measure must be considered in the light of the monetary system and existing units used in the purchase of the commodities on which the excise is laid. Take, for example, cigarettes with the increase proposed in this new Federal revenue bill.

It will be a very substantial upset of the normal merchandising of cigarettes in Massachusetts which now are made available to Massachusetts in over-the-counter sales and through vending machines which of necessity are faced with the requirement of using the existing monetary system of the United States. It will avail the Federal Government but little if in the establishment of these taxes there is a lessening of the merchandising of cigarettes which still is the main source of revenue to the Federal Government from the tobacco tax and is the sole revenue from that source to Massachusetts. If in putting the tax on a package of cigarettes so high, the sale of the cigarettes is very substantially reduced, and if as the proposed Federal law seems to me likely to do, stagnation of the normal flow of commodities through the established merchandising channels results, the revenue proposed will not be as productive as would be the case if consideration were given to what the States lay by way of a cigarette tax, working back the total tax impact on the amount that a package of cigarettes should sell for so as to make it attractive to the purchaser.

This same rule holds true in respect to gasoline and particularly in respect to liquor where the merchandising has confined itself not to sale in bulk but to sale in small quantities such as individual servings. This trade practice requires that in establishing a tax structure, consideration be given to the method of merchandising of this particular commodity.

It is idle even to suggest that the merchandising of a commodity such as liquor can quickly readjust itself to the increased tax because by adding the State and Federal taxes to the liquor, a consumer price can be established which will not in any way interfere with the volume sold. I am of the opinion that those drafting the Federal tax law should have in mind the States' tax laws in respect to cigarettes, liquor, and gasoline, as well as in respect to corporation and individual income taxes as well as excises generally, so that both the States and Federal Government will get the maximum amount of yield but without interfering with the merchandising of these commodities, which I think it is easy to establish rests on the movement of these commodities through to the consumer by the use of the units established by the monetary system of the United States.

Split cents in the determination of a tax are unimportant if you look at the cent, but if you look at the volume which ultimately is determined in its tax by the yardstick of a cent, it is easily established that a monetary system or a State plan will have to be developed to provide for fractions of a cent to bring about even an approach to orderly merchandising of the commodities used by the majority of people and through which the States, as well as the Federal Government, should get its revenue. It is clear that the existing proposal before the Senate Finance Committee could be either placed temporarily as a measure to stopgap until the next session of Congress and during such period a study could be made which would bring about a result which would not interfere with the States or a flat surtax could be established without excursions into the fields heretofore left untouched by the Federal Government and without any readjustment of the rates so that something raising \$600,000,000 will be available to the Federal Government without any real upset either in the administration by the Federal Government or by the States.

Admittedly the States cannot now instantly readjust their tax structures because many of the legislatures are not now in session and there has been no opportunity afforded for the States to confer with the Federal Government in the devising of a tax bill which will meet the needs of both sovereignties. The States must still continue to exist. They must still tax their persons and property and as the Federal Government relies upon the same sources for their revenue, it is seemingly obvious that there should not be a hastily enacted bill under the pressure of the immediate situation when a temporary bill will raise the necessary revenue for the balance of this year and afford the opportunity during the intervening period for a well thought out plan which will not upset revenue production.

Massachusetts is very likely to contribute under any proposal substantial sums to the Federal Government and as it has a very large cost of government itself, it is in my opinion, entirely justified in asking that consideration be given to the Commonwealth of Massachusetts in any tax measure which is passed. There is no question but what Massachusetts in company with its sister States senses the need and is willing even to suffer some revenue loss to accomplish the necessary objectives of the Federal Government, but it feels that under pressure, particularly where a tax bill has not been considered in connection with the States, the passage of a revenue measure under such conditions is not only forcing Massachusetts to make a substantial contribution but in addition, without any good reason, is compelling it to forego revenues because with a Federal tax the development of a tax base very substantially decreases. Even if the present bill is made effective only for the period until next Congress it may do some damage because it will affect, in my opinion, the sale of commodities that will have to adjust themselves to new taxes. But if the amount to be raised, which I understand is something short of \$1,000,000,000, can be obtained just as well by let us say putting 15 percent surtax on the tax established under the existing Federal law the money will be made available to the Federal treasury and a bill which is to be considered by the next Congress passed on careful consideration by the Federal Government representatives and representatives of States will permit the passage of a tax act by the Federal Government which will allow both the State and the Federal Government to operate without injury to the other and without injury to commerce generally.

HENRY F. LONG.
Commissioner of Corporations and Taxation.

CONGRESS OF INDUSTRIAL ORGANIZATIONS,
Washington, D. C., June 12, 1940.

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

DEAR SENATOR HARRISON: I am writing you to present the views of the Congress of Industrial Organizations respecting H. R. 10039, and respectfully request that this letter be incorporated in the record of hearings pertaining to this measure. This bill provides for the issuance of 4 billion in bonds during the next 5 years and for tax increases amounting to a little over \$1,000,000,000 annually to meet the cost of the armaments program.

The Congress of Industrial Organizations is wholeheartedly in support of necessary measures to modernize and extend our defenses. One of the most pressing problems that will arise in connection with this program is that of providing necessary taxes and borrowings to defray its cost. It is at this point that we are faced with the crucial question of whether the cost of the armaments program will be imposed upon the consumers and wage earners of this country, thus breaking down the standards of living of the American people.

We believe that the present tax bill fails to meet the fundamental tests of a sound tax measure. The Congress of Industrial Organizations, at its 1939 San Francisco convention, and again at the recent June meeting of the executive board board, adopted as the principles of a sound tax system: First, taxes should serve the double purpose of providing adequate revenue and correcting the present maldistribution of income; second, complete opposition to all forms of sales and other consumer taxation, direct or indirect; and third, the taxation of large aggregates of wealth and income through excess-profits taxes, increases in inheritance and gift taxes, increased rates and elimination of loopholes in taxes upon upper-bracket incomes, and elimination of the tax exemption for Government securities.

The present measure fails to make ordinary safeguards which can be made in the present emergency. In the first place, of the \$1,000,000,000 to be raised in additional taxes, nearly one-half is imposed upon workers and low-income groups through raising the excise taxes on such popular consumer products as cigarettes, gasoline, and beverages, and through the imposition of income taxes upon wage earners and low incomes. Until sources of revenue from large aggregates of wealth and income are fully utilized, we believe it unjust and uneconomic to place so heavy a burden upon the mass purchasing power of the American people.

The bill also fails to eliminate the tax exemption for the Government bonds to be issued under its provisions. This means that, in fact, a large part of the taxes collected from the low-income groups are to be paid over to those, with excess incomes, who will invest in the Government bonds. At the same time, the light burden placed upon upper-bracket incomes is further relieved by the receipt of these same tax-exempt interest payments.

Finally, the bill makes no substantial attempt to levy just taxes upon the increased profits that will accrue to corporations supplying the materials in the armaments program. Even if no thorough excess-profits tax is now to be established, at least the rates on corporate and upper-bracket income, largely dependent upon dividends and interest from armament profits, should be increased.

We believe that these objectionable features of the tax bill can be remedied at the present time, upon the basic principles of a sound national tax system.

Sincerely yours,

LEE PRESSMAN,
General Counsel.

NATIONAL ASSOCIATION OF MANUFACTURERS,
New York, N. Y., June 13, 1940.

HON. PAT HARRISON,
Chairman, Senate Finance Committee,
Senate Office Building, Washington, D. C.

DEAR SENATOR HARRISON: On behalf of the National Association of Manufacturers, I submit the following observations concerning the revenue bill passed by the House of Representatives, which is now under consideration by your committee:

1. It is recognized that the proposed Revenue Act of 1940 is an emergency tax bill. We anticipate, therefore, that there will subsequently be adequate opportunity to present the views of taxpayers before such congressional committees as may study the entire tax question prior to January 1941.

2. We approve as an emergency measure the principle of the imposition of a 10-percent supertax to be levied on individual incomes earned beginning January 1, 1940, or on corporation incomes for fiscal years beginning after January 1, 1940.

3. We believe, however, that the imposition of such a supertax will increase the burden of any inequities which may exist in the present law and therefore urge that these inequities be removed as quickly as possible.

4. We approve as an emergency measure the additional excise taxes which would be imposed by the pending Revenue Act of 1940.

5. We approve as an emergency measure the 1-percent increase in corporation income-tax rates.

6. We approve the proposed decrease in personal exemptions from \$1,000 to \$800 for single persons and from \$2,500 to \$2,000 for married persons and heads of families.

7. We approve in principle an adjustment in the effective surtax rates designed to obtain an increase in total revenue, but recommend that changes in these rates be made in a permanent tax measure to be introduced and considered in the next session of Congress rather than in an emergency measure at the present time.

8. We desire to stress the belief that in times of greatly increased expenditures for national defense, it is essential to scrutinize with the utmost care all expenditures for other Government functions in order that substantial reduction in these other costs may be made.

Respectfully submitted.

NOEL SARGENT, *Secretary.*

MACK MANUFACTURING CORPORATION,
Long Island City, N. Y., June 13, 1940.

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

DEAR SENATOR: We desire to call your attention to an inequity in H. R. 10039 in the case of our installment sales contracts consummated prior to June 30, 1940, due to the provision of the bill requiring the application of the additional tax provided in section 210 applying to the payments made subsequent to June 30, 1940.

Subdivision (c) of section 3441 of the Internal Revenue Code provides as follows:

"In the case of (1) a lease, (2) a contract for the sale of an article wherein it is provided that the price shall be paid by installments and title to the article sold does not pass until a future date notwithstanding partial payment by installments, or (3) a conditional sale, there shall be paid upon each payment with respect to the article that portion of the total tax which is proportionate to the portion of the total amount to be paid represented by such payment."

In the case of our installment sale contracts now outstanding, the last installment in certain cases will not become due until 1945. We now have approximately \$19,000,000 payable under contracts consummated prior to June 30, 1940. The automobile tax which will become due with respect to these sales at the rates now in effect is estimated at approximately \$300,000.

It will be practically impossible for us to pass the additional one-half percent imposed under the pending bill on to the purchaser, and if exemption is not provided in the bill, our company will have to absorb the additional tax.

We feel that the imposition of such tax in these cases will be very inequitable, and we sincerely hope that your committee will deem it proper to exempt such installment sales from the imposition of the proposed additional tax.

Respectfully submitted.

S. E. SAVACOO, *Vice President and Comptroller.*

STATEMENT OF RICHARD A. STADERMAN, PRESIDENT OF THE AMERICAN GOOD GOVERNMENT SOCIETY, REGARDING THE PROPOSED \$1,000,000,000 INCREASE IN TAXES

My name is Richard A. Staderman, of New York City and Washington, D. C. I am president of the American Good Government Society, which has headquarters here in Washington, D. C., and I appear on behalf of the society. Our organization is a national, nonpartisan patriotic association which strives to do what little it can to keep the ship of state on a firm and even keel so as to make

steady and sane progress forward on the basis of constitutional, representative government. You may have heard some of the coast-to-coast radio network broadcasts which our society from time to time sponsors and upon which able Members of this Senate and House of both major parties have appeared. You may also have seen some of our public releases which are regularly carried by the legal papers served by the Court and Commercial Newspaper Syndicate, these papers being in the North, the South, the East, and the west coast. Metropolitan dailies also carry our statements. For examples of our views I might also refer you to the many items indexed under American Good Government Society in the revised, red-bound editions of the 1939 Congressional Record, both the first and second sessions.

One of the officers of our society, Mr. Knight, is directly descended from James Wilson, signer of the Declaration of Independence and of the United States Constitution. Our vice president, Lincoln, is a direct descendant of the grandfather of President Lincoln and our vice president, Grant Wells, is a descendant of the grandfather of President Grant as well as of the family of Confederate President Jefferson Davis. The general counsel of the American Good Government Society is Col. O. R. McGuire, who has approved this statement of mine. He is chairman of the committee on administrative law of the American Bar Association. In my own case, I was educated under such economic authorities as Prof. Davis Dewey, of Massachusetts Institute of Technology; Prof. Edwin F. Gay and Frank W. Taussig, of Harvard, Taussig having been chairman of the United States Tariff Commission during the Wilson administration. I am a former assistant to Prof. Irving Fisher, of Yale, and Prof. W. Z. Ripley, of Harvard, and I formerly taught economics in Ohio. I am editor of the magazine published by our society and of the American History Series of books we issue from time to time.

For the rapid rearming approved by the Congress, the putting of additional newly coined money into circulation is essential "to make the wheels go round." The proposed \$1,000,000,000 higher tax rate now pending before Congress would simply legally rob Peter's factory to try to pay for Paul's. On the other hand, expansion of coinage of idle bullion would so increase the total national income that more dollars would come into the Treasury even though present tax rates were left unchanged in percentage. Then if more revenues were needed in future years than expanded coinage or present tax rates provided, there would be a larger reservoir of incomes available for tax purpose than if the pending \$1,000,000,000 tax hoist were adopted.

Out of over \$21,000,000,000 gold and silver bullion in the United States Treasury, at least \$12,000,000,000 is unneeded as a reserve. Behind the \$7,000,000,000 currency in public (not bank-held) circulation and behind the various other parts of the national credit structure, nine of the twenty-one billions would be more than ample reserve. Coining this idle twelve billions into sound, "hard" money to pay for defense equipment would benefit farmer, factory owner, laborer, and consumer. Present high taxes hinder business.

Now we are treated to the sorry spectacle of public officials and certain Congressmen advocating "broadening the base of taxation" as a permanent law to raise more revenue. The excuse is given that new taxation is needed to help pay for increased defense expenditures.

If existing taxation is so harmful to farmers, businessmen, and labor, would not higher taxes be a still greater discouragement? How can it aid true national defense to still further penalize people who would start new businesses, including those to make defense equipment?

Adding the prospective deficit of several billions of dollars due to nonmilitary activities, and the several billions additional deficit due to rearming, we find a total prospective deficit for the coming fiscal year of something over \$5,000,000,000.

It is obvious that the proposed \$1,000,000,000 in new Federal taxes will hardly even begin to balance the Budget or take care of such a deficit. Although the proposed new taxes amount to only a few "drops in the bucket" of the entire Federal debt and Budget situation, they would greatly increase the hesitation of the man thinking of building a new factory, who is already burdened with excessive taxation.

Are there no other possibilities of doing something to reduce the prospective deficit? Senator Byrd advocates a 10 percent cut in nonmilitary Federal expenditures other than certain fixed charges. The White House seems to have accepted part of Byrd's idea, and is seeking cuts of somewhat less than 10 percent net.

\$3,000,000,000 COULD BE SAVED

In its suggested balanced budget last January, the American Good Government Society showed item by item how the vital functions of the Federal Government could be administered for not over \$6,872,000,000 a year, even including what then seemed liberal increases for national defense funds. This figure represented about \$3,000,000,000 less than the present yearly rate of expenditures, and brought the budget into balance after allowing for certain miscellaneous income items. We repeat these January suggestions of a 30 percent cut in the general budget by pruning nonmilitary items.

\$1,000,000,000 ADDITIONAL SAVINGS

In addition to the possible \$3,000,000,000 deficit-reduction, it would be possible to save another \$1,000,000,000 if nonmilitary expenditures were pruned to the point President Franklin D. Roosevelt reached in his commendable economies for regular departmental and bureau outgo (not counting emergency or extra items) for the year ended June 30, 1934.

\$4,000,000,000 TOTAL SAVINGS POSSIBLE

Adding the possible three plus one billions, we find a total of some \$4,000,000,000 of economies that would permit financing of the rearming deficit without new taxes and without even raising the present national debt limit. This is our first choice of the various alternatives now before the Congress and the President.

Should this vigorous economy method not be followed, the deficit of \$5,000,000,000 upward still remains as an excuse for those who want to impose the \$1,000,000,000 new taxes. But could not this sum be raised in other ways?

WHY NOT USE IDLE GOLD IN THE TREASURY?

There is \$2,000,000,000 in the Treasury stabilization fund. Of this, as Secretary of the Treasury Morgenthau told the United States Senate Banking Committee, never more than \$200,000,000 has been used for stabilizing operations, leaving \$1,800,000,000 untouched. Present foreign conditions still further limit the operations of the fund, so the \$200,000,000 is more than ample for stabilizing purposes.

The bulk of the gold in the Treasury has come there, however, due to the 1933 and 1934 statutes forbidding everyone except the Treasury to hold or use gold for monetary purposes. Thus all foreign or domestic gold deposited in local banks is turned over to the 12 Federal Reserve banks who pay for it by giving the local bank either currency, or credit in the form of a deposit account. The 12 Federal Reserve banks turn the gold over to the Treasury and receive in return either nonnegotiable gold certificates (total of about \$3,000,000,000 now held), or credit in the Treasury's gold certificate fund (totaling \$14,000,000,000 now).

Adding these two sums, we find that the 12 Federal Reserve banks hold some \$17,000,000,000 altogether in gold certificates and credits entitling them to certificates, against which the Treasury holds an equal \$17,000,000,000 of gold. That this is an unnecessarily high gold reserve, is shown by the fact that the Treasury holds only about \$156,000,000 in gold behind about \$348,000,000 of certain currency (United States notes and Treasury notes of 1890). This is about 45 percent gold behind that currency, which all persons are anxious to accept at full value.

SIMPLE STATUTORY CHANGE NEEDED

Since this 45 percent reserve is unquestioned, why not apply the 45 percent principle to the \$17,000,000,000 of gold certificates or credits therefor, held by the 12 Federal Reserve banks? Forty-five percent of \$17,000,000,000 would be around \$7,600,000,000. Since the 12 Federal Reserve banks have outstanding only about \$5,000,000,000 of paper money, a \$7,600,000,000 reserve would not only more than secure the paper money but would give a safe reserve behind the \$12,000,000,000 of deposits by local banks in the 12 Federal Reserve banks. Thus a change to a 45 percent gold reserve would not bring any lack of public confidence in the Federal Reserve currency.

A brief, simple act of Congress could provide that the Treasury need keep only a 45-percent gold reserve as backing for the certificate or credits therefor issued to the 12 Federal Reserve banks. By legalizing the 45 percent figure of \$7,600,000,000 the remainder of the \$17,000,000,000 now held, or \$9,400,000,000, would be released for defense expenses.

EXCESS GOLD TO BE COINED

This \$9,400,000,000 excess gold, plus the \$1,800,000,000 unused gold in the Stabilization Fund (above described), makes a total of over \$11,000,000,000 available for payment of Uncle Sam's defense bill. If this entire sum were converted into gold coins and these paid out as needed, there could be no question of the soundness of this new money.

IDLE SILVER TOO

There is a billion or more unobligated ounces of silver in the Treasury. At the coinage value of \$1.29 per ounce, there is no question that at least \$1,000,000,000 of now unused silver could be coined and used to defray national-defense expenditures.

MONEY STIMULATES BUSINESS—TAXES DEPRESS IT

The total of \$11,000,000,000 of gold coin and \$1,000,000,000 of silver coin would mean \$12,000,000,000 of new "hard money" of precious metals available as needed. Such an amount devoted to military expenditures would go far toward equaling the estimated defense needs determined by the Congress. Let us hope we shall never need to spend the \$17,000,000,000 a year for military purposes as Germany is reported to have done in each of the past 4 years.

NO PRINTING PRESS MONEY

Not a single dollar of the gold and silver coin we suggest the issuance of would be run off on the printing press. There is no question of inflation, because the new money has intrinsic value. Therefore no one would refuse to accept it.

MONEY MAKES THE WHEELS OF INDUSTRY HUM

Many eminent economists have long held that the principal cause of depression and unemployment is a lack of money in active circulation; in other words, not enough money passing from hand to hand rapidly enough. If new taxes are imposed, that merely diverts parts of the present insufficient stream of money to defense uses, increasing the hardship for non-military industries, with resultant bankruptcies and unemployment.

On the other hand, the preparedness program can be a real aid in cutting unemployment if we provide new coin to finance it, because then it will serve to take up the slack in our employment structure. New coin will finance many more new industries than mere tax-diverted present money, and do it much more soundly than making Federal loans to try to stimulate defense industries, since the latter course would only serve to put another heavy hand of Government domination on the already harassed businessman.

As a practical matter, we must convert the idle bullion into new, sound money, or we shall not have enough capital for building enough factories for defense equipment as rapidly as the United States people demand. As to using a substantial part of our bullion in coining new money, let us remember that it was new money, new purchasing power, and even using tax-exempt warrants to anticipate Government income that Germany was enabled to finance her rearmament program. By our using coin instead of paper, our monetary expansion will be sound, whereas Germany's present paper money standard is open to all the dangers of the German inflation and collapse in 1923. By adhering to hard money we can avoid the "Pitt-falls" described by a wag a century and a half ago in the following poem:

Of Augustus and Rome, the poets still warble
How he found it of stone, and left it of marble.
Of Pitt and England, men say without vapor,
How he found it of gold, and left it of paper.

RICHARD A. STADEMAN,
President, American Good Government Society.

The CHAIRMAN. The hearings are now closed, and the committee will recess until 10 o'clock tomorrow morning, promptly, in this room. (Whereupon, at 12:15 p. m. the hearing was closed and the committee recessed.)

(At the request of Senator Herring, the following communication from Humphrey Robinson & Co., certified public accountants, Louisville, Ky., addressed to Joseph E. Seagram & Sons, Inc., Louisville, Ky., submitting a summary of estimated cost of whiskies and spirits contained in specific blended and straight case whiskies, was inserted in the record:)

HUMPHREY ROBINSON & Co.
CERTIFIED PUBLIC ACCOUNTANTS

COLUMBIA BUILDING,
Louisville, Ky., February 26, 1940.

JOSEPH E. SEAGRAM & SONS, INC.,
Louisville, Ky.

GENTLEMEN: We submit herewith a summary of estimated cost of whiskies and spirits contained in specific blended and straight case whiskies.

We have made an independent computation of the cost of whiskies and spirits contained in a typical low-price blend, such as "Kessler's Private Blend" as compared with a representative 3-year-old straight bourbon whisky. These average figures, based upon our experience in comparing distilling costs, were estimated for whiskies and neutral spirits produced at Louisville, Jefferson County, Ky., and Greendale, Dearborn County, Ind.

Our computations are based upon present grain and cooperage prices, an estimated normal distilling expense, i. e., wages, depreciation, and sundry manufacturing expenses, prevailing taxes, and reasonable warehousing costs. In computing the whisky cost, we have elected a mash containing 35 percent small grains (i. e., rye and barley malt) with an average yield of 4.75 gallons per bushel of grain mashed. Neutral spirits are based upon the use of a content of 2 percent small grains with an estimated yield of 4.90 proof gallons per bushel. This latter yield takes into account the loss resulting from redistillation and the removal of undesirable ingredients.

In computing the cost of whiskies and spirits contained in the private blended case goods, we have used the formula of Kessler's Private Blend, which has been made available to us. A summary of the estimated costs of whiskies and spirits contained in certain case goods on the basis stated herein follows:

	Louisville production	Greendale (Indiana) production
<i>90 proof</i>		
Private blend:		
25 percent aged straight Bourbon whiskies		
75 percent aged and unaged neutral spirits		
3-year-old straight Kentucky Bourbon	7.04	7.80
<i>90 proof--Lower price whiskies</i>		
Blend:		
20 percent 2-year-old straight Bourbon (aged in new cooperage)		
80 percent unaged neutral spirits	7.60	
2-year-old straight Bourbon (new cooperage)	7.50	
Blend:		
20 percent 2-year-old corn whisky in reused cooperage		
80 percent unaged neutral spirits	7.57	
2-year-old corn whisky aged in reused cooperage	7.02	
<i>60 proof</i>		
4-year-old straight Bourbon whisky--Aged in new cooperage	7.77	
<i>100 proof</i>		
4-year-old--Aged in reused cooperage	8.30	
<i>Bottled in bond</i>		
4-year-old straight Bourbon whisky	8.63	

NOTE.- Our computation of blended spirits excludes Kentucky production tax of 8 cents per gallon on neutral spirits contained therein.

It will be observed from the above summary that the estimated cost of a blend such as Kessler's Private stock is 23 cents per case in excess of a 3-year-old straight bourbon whisky. The blended costs in Louisville include Kentucky production tax of 5 cents per gallon on whisky content of 25 percent and excludes such tax on neutral spirits contained therein. This additional tax would be approximately 11 cents per case.

It will be noted that our computation shows the estimated costs at Greendale, Ind., to be slightly lower than Louisville. This is principally due to lower ad valorem taxes and slightly cheaper grain costs. Distilling overhead expenses are assumed to be the same at both locations.

The above represents estimated cost of whisky content only, and do not include the following items:

1. Bottling costs—Consisting of package supplies, Federal and State stamps, labor and bottling-plant expenses.
 2. The cost of blended spirits excludes Kentucky production tax of 5 cents per gallon on neutral spirits used in the blends.
 3. Interest on investment in bulk spirits during period goods are held in storage for aging.
 4. Sales expense—Including commission, advertising, etc.
 5. Administrative and general overhead expense.
 6. Provision for profit on sale of case goods.
- Respectfully submitted.

HUMPHREY ROBINSON & Co.,
Certified Public Accountants.

(The following communication from the United States Savings and Loan League, of Chicago, Ill., submitted by Mr. C. Clinton James, of Washington, D. C., its legislative committee chairman, was received and ordered printed in the record:)

UNITED STATES SAVINGS AND LOAN LEAGUE
 CHICAGO, ILL.

FEDERAL LEGISLATIVE COMMITTEE,
 Washington, D. C., June 12, 1940.

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

DEAR SENATOR: H. R. 10030, which is now pending in the Senate and upon which we understand you are holding hearings, contains subsection "c" of section 7, dealing with information returns. On behalf of the United States Savings and Loan League, I enclose a proposed revised language for said subsection "c" of section 7 which we request you to consider and to incorporate in the legislation.

The reason for making this request is that at present a discrimination exists against savings and loan associations and similar institutions. Under the present law, section 147 of the Internal Revenue Code requires information returns as to interest and certain other items paid in excess of \$1,000 but our institutions are being required to make information returns of amounts in excess of \$100 paid as dividends. The result of this situation is that banks are required to make the information returns as to interest payments to savers in excess of \$1,000 while our institutions are required to make information returns as to our payments of dividends to savers in excess of \$100.

You will see at once that this discrimination arises from a purely technical situation in that the banks call their payments to savers "interest" whereas the savings and loan associations call their payments to savers "dividends." The savings and loan associations do not belong in the class with the great industrial corporations paying dividends but more appropriately belong in the class of financial institutions having large numbers of small savers.

The reason we make this request is that our institutions are being called upon to make a great many information returns as to members most of whom are not subject to income tax because of the low income of working people, who are our principal savers. We will appreciate very much your careful consideration and removal of this discrimination.

Very truly yours,

C. CLINTON JAMES, *Chairman.*

(c) *Information returns.*—Section 147 (a) of the Internal Revenue Code (relating to information at the source) is amended by inserting after the word "income" and before the parentheses, as follows:

"and dividends paid by mutual savings banks, co-operative banks and savings and loan associations"

and it is further amended by striking out "\$1,000" wherever occurring therein and inserting in lieu thereof "\$800".

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