TAX EVASION AND AVOIDANCE

HEARINGS

BEFORE THE

JOINT COMMITTEE ON
TAX EVASION AND AVOIDANCE

SEVENTY-FIFTH CONGRESS
FIRST SESSION

PURSUANT TO
PUBLIC RESOLUTION NO. 40, SEVENTY-FIFTH CONGRESS,
FIRST SESSION, TO CREATE A JOINT CONGRESSIONAL COMMITTEE ON TAX EVASION 
AND AVOIDANCE

PART 1

JUNE 17, 18, 22, 23, AND 24, 1937

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III
TAX EVASION AND AVOIDANCE

THURSDAY, JUNE 17, 1937

JOINT COMMITTEE ON TAX EVASION AND AVOIDANCE,
Washington, D. C.

The joint committee met in the hearing room of the Committee on Ways and Means in the New House Office Building at 10 a. m., Hon. Robert L. Doughton presiding.

The CHAIRMAN. The committee will be in order. Visitors will please take their seats.

In order that there may be no misunderstanding or misquoting of what I, as chairman of the joint committee, have to say in my preliminary statement, I have reduced it to writing.

The Joint Committee on Tax Evasion and Avoidance, created pursuant to Public Resolution 40, Seventy-fifth Congress, first session, meets this morning, in accordance with the action taken by the committee, at a meeting held on June 15, to start hearings on the methods of tax evasion and avoidance disclosed in the message of the President to the Congress on June 1, and also other methods that may be disclosed.

As chairman of the joint committee, and in behalf of its members, I feel justified in saying that it will be our purpose to do everything reasonable to unearth the various devices and subterfuges employed by tax dodgers, and to prevent as far as possible the further use of such schemes by recommending and seeking the enactment of remedial legislation wherever found necessary.

In carrying out this purpose, I feel that it should be our sincere desire to afford to honest taxpayers freedom from unjust criticism and embarrassment and to assure them that they will not be subjected to inquisitorial persecution. We should be just as anxious to protect the reputation of honest taxpayers as we are diligent in discovering and exposing those who attempt to evade, or do evade, the payment of taxes that the law contemplates they should pay. Only those who have employed flagrant tax dodging methods need be uneasy with respect to the purpose and effect of this investigation and the publicity that may result therefrom.

I also desire to state that all persons whose names may be disclosed in the proceedings will be given the fullest opportunity to be heard on their own behalf.

Senator Harrison, have you any preliminary statement you would like to make?

Senator Harrison. No; except that I am sure that the other members agree with the statement of the chairman.

The CHAIRMAN. The first thing we will ask to be inserted in the proceedings, in the hearings, unless some member desires it to be
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read, is the message of the President of the United States, on which these hearings are based.

(The document referred to is as follows:)

[H. Doc. No. 260, 78th Cong., 1st sess.]

TAX EVASIONS AND EVADERS

To the Congress of the United States:

A condition has been developing during the past few months so serious to the Nation that the Congress and the people are entitled to information about it.

The Secretary of the Treasury has given me a report of a preliminary study of income-tax returns for the calendar year 1936. This report reveals efforts at avoidance and evasion of tax liability so widespread and so amazing both in their boldness and their ingenuity that further action without delay seems imperative.

We face a challenge to the power of the Government to collect, uniformly, fairly, and without discrimination, taxes based on statutes adopted by the Congress.

Mr. Justice Holmes said, "Taxes are what we pay for civilized society." Too many individuals, however, want the civilization at a discount.

Methods of escape or intended escape from tax liability are many. Some are instances of avoidance which appear to have the color of legality; others are on the border-line of legality; others are plainly contrary even to the letter of the law.

All are alike in that they are definitely contrary to the spirit of the law. All are alike in that they represent a determined effort on the part of those who use them to dodge the payment of taxes which Congress based on ability to pay. All are alike in that failure to pay results in shifting the tax load to the shoulders of others less able to pay, and in mulcting the Treasury of the Government's just due.

I commend to your attention the following letter from the Secretary of the Treasury:

THE SECRETARY OF THE TREASURY,


The President,
The White House.

My Dear Mr. President: As you know, the Treasury was surprised and disturbed by the failure of the receipts from the income tax on March 15 to measure up to the Budget estimates. Therefore, we undertook an immediate investigation. Only a preliminary report can be made at this time, because the complete investigation covering all the income-tax returns filed will require the balance of this year. Furthermore, since many of the returns of large manufacturing corporations have not yet been filed, the present report is confined almost wholly to data disclosed by the individual tax returns.

But even this preliminary report discloses conditions so serious that immediate action is called for. More than the usual examination and audit by the Treasury is needed. It seems clear that if tax evasion and tax avoidance can be promptly stopped through legislation and regulations resulting from a special investigation a very large portion of the deficiency in revenues will be restored to the Treasury.

I have with me a list of some of the principal devices now being employed by taxpayers with large incomes for the purpose of defeating the income taxes which would normally be payable by them. As we continue our preliminary examination other devices are being disclosed.

1. THE DEVICE OF EVADING TAXES BY SETTING UP FOREIGN PERSONAL HOLDING CORPORATIONS IN THE BAHAMAS, PANAMA, NEWFOUNDLAND, AND OTHER PLACES WHERE TAXES ARE LOW AND CORPORATION LAWS LAX

Americans have formed 49 such companies in the Bahamas alone in 1935 and 1936, and 22 more were organized by Americans in the Bahamas during the past 2 months. Panama and Newfoundland seem to be even more fertile territory, since their corporation laws make it more difficult to ascertain who the actual stockholders are. Moreover, the stockholders have resorted to all manner of devices to prevent the acquisition of information regarding their companies.
The companies are frequently organized through foreign lawyers, with dummy incorporators and dummy directors, so that the names of the real parties in interest do not appear.

One American citizen with a $3,000,000 Bahamas corporation has apparently attempted to prevent the Bureau of Internal Revenue from catching up with him by filing his individual tax returns in successive years from towns in New Brunswick, British Columbia, and Jamaica.

Another individual believes that he has been so successful in removing his assets from the United States to the Bahamas that he is defying the Treasury to collect a tax upon a $250,000 fee he has received; and by way of insult, he has offered to compromise his admitted tax liability of $33,000 for past years by a payment of $1,700.

Still another individual showed a large net loss on his personal return for 1936. In considerable part the loss was due to the large deduction he claims for interest on a loan made to him by his personal holding company. But the man in question is no object of charity, for his personal holding company, organized in Canada, had an income of over $1,500,000 from American dividends in 1936, though it has not yet filed a return.

Perhaps the most flagrant case of this character is that of a retired American Army officer with a large income from valuable American securities which he desires to sell at a very large profit. To escape our income- and inheritance-tax laws, he used the device of becoming a naturalized Canadian citizen, and 6 days later organized four Bahamas corporations to hold his securities. He and his lawyers apparently think that he can now sell his securities free from any taxes on his profits, since there are no income taxes in the Bahamas, and that he has adroitly escaped American taxes.

2. THE DEVICE OF FOREIGN INSURANCE COMPANIES

Two New York insurance agents have caused the organization of insurance companies in the Bahamas with a view to enabling taxpayers to secure spurious deductions for interest through an ingenious scheme for the issuance of life-insurance policies. Americans who went into the scheme purported to pay a large single premium for their policies, but immediately borrowed back practically the entire sum. Under the plan the so-called policyholders sought to obtain a large deduction for interest on this loan, although the fact was that no interest was really paid. By this means five prominent Americans sought to evade nearly $550,000 in income taxes in the years 1932 to 1936. This fraud was discovered by the Treasury's investigators and all of the taxpayers have now submitted offers to pay the full amount of taxes evaded, plus interest. Until our investigation is completed we do not know how many similar companies may have been organized in other countries, and utilized by our citizens; nor do we yet know whether this newly invented type of fraud has other ramifications.

3. THE DEVICE OF DOMESTIC PERSONAL HOLDING COMPANIES

The rates of tax applicable to personal holding companies were reduced in 1930 at the time of the enactment of the undistributive profits tax. It was believed at that time that the combined rates of the two taxes would be sufficient to insure the distribution of the entire incomes of these companies, and the consequent imposition of surtaxes upon their owners. This expectation has not been realized.

Thus, the single stockholder of one large personal holding company saved himself $322,000 by causing his company to distribute none of its income to him.

In another case, a man and his wife saved $791,000 through the use of personal holding companies in 1936.

In a third case, the personal holding company reported over $500,000 of net income but the total taxes paid by the two stockholders, husband and wife, were less than $80,000, due principally to credits for payments on indebtedness the holding company prudently incurred in accumulating properties for its owners. If the personal holding company had not been in existence, the stockholders would have paid over $200,000 additional income taxes.

Another favorite device is to organize a considerable number of personal holding companies, not only for the sake of reducing the tax, but of increasing the Treasury's difficulties in auditing transactions between companies. At
last accounts one man had caused to be set up some 96 companies scattered all over the country. Two other individuals were utilizing 23 personal holding companies.

4. THE DEVICE OF INCORPORATING YACHTS AND COUNTRY ESTATES

Many wealthy taxpayers today are dodging the express provisions of the law denying deductions for personal expenses by incorporating their yachts or their country estates, turning over to the yacht or to the estate securities yielding an income just sufficient to pay the entire expenses of operation. Hundreds of thousands of dollars in income taxes are annually avoided in this way.

Thus, one man’s yacht is owned by his personal holding company, along with $3,000,000 in securities. He rents the yacht from his company for a sum far less than the cost of upkeep, and the company uses its income from the securities to pay the wages of the captain and crew, the expenses of operating the yacht, and an annual depreciation allowance. None of these items would be deductible if this individual owned the yacht personally.

A great many wealthy taxpayers are utilizing a similar arrangement for the operation of their country places and town houses.

One man has placed his $5,000,000 city residence in such a corporation, another his racing stable whose losses last year were nearly $200,000. The tax savings he thus sought to obtain through the use of the holding company were $140,000.

One wealthy woman has improved on the general plan of evasion by causing her personal holding company, which owns her country place, to employ her husband at a salary to manage it. She can thereby supply him with pocket money, and in effect claims a tax deduction for the expense of maintaining him.

5. THE DEVICE OF ARTIFICIAL DEDUCTIONS FOR INTEREST, LOSSES, ETC.

Taxpayers are seeking greatly to reduce their personal income taxes by claiming deductions for interest on loans to them by their personal holding companies, or on loans to them by their family trusts. These transactions normally have no business purpose, but are merely an artificial means of shifting income from one member of the family subject to high surtax rates to another member of the family subject to lower rates.

Thus, one woman claims a large annual deduction for interest on a loan made to her by her husband as trustee of a trust which she created for their children. The mother thereby seeks to secure a deduction for her contribution to the children’s support, and since the trust is revocable by her husband, the parents still have the desired control over the property and its income.

In the same category are losses deducted by taxpayers who claim that their racing stables or hobby farms were operated for profit, even though a profit is never realized. Thus, a prominent manufacturer seeks a deduction of over $125,000 against his income from his business, on account of his losses in operating a chicken farm.

6. THE DEVICE OF THE CREATION OF MULTIPLE TRUSTS FOR RELATIVES AND DEPENDENTS

Splitting income two ways, between husband and wife, reduces income taxes and leaves the family income intact. Splitting the family income many ways by means of many trusts, all for the same beneficiaries, may effect a much greater saving, while leaving the money actually in the same hands. For the creator of the trust often constitutes himself or his wife as trustee, and thus retains full control over the investment and disposition of the fund itself and of its income.

One thrifty taxpayer has formed 04 trusts for the benefit of four members of his immediate family, and thereby claims to have saved them over $485,000 in 1 year in taxes.

Another thrifty pair have constituted 40 trusts for their relatives, and a prominent lawyer and his wife utilize 13 trusts for the same purpose. The first pair maintains numbered brokerage accounts, and only at the end of the year are the beneficial owners identified. In this way innumerable transactions are carried on, often between accounts, which do not actually affect the beneficial interests of their owners, but which are designed solely to reduce tax liability.
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7. THE DEVICE OF HUSBAND AND WIFE OR FATHER AND CHILDREN PARTNERSHIPS

The purpose of these partnerships, like the multiple trusts, is to split the family income artificially into two parts; or, if the children are taken in, into still smaller fractions.

There are many instances of this kind; but to illustrate the point, it is sufficient to cite the case of a New York brokerage firm which late in 1935 admitted into partnership the four minor children—two boys and two girls—of one of the partners. The tax saving he sought thereby in 1936 amounted to over $50,000.

8. THE DEVICE OF PENSION TRUSTS

For 10 years the revenue acts have sought to encourage pension trusts for aged employees by providing corporations with a special deduction on account of contributions thereto, and exempting the trust itself from tax. Recently this exemption has been twisted into a means of tax avoidance by the creation of pension trusts which include as beneficiaries only small groups of officers and directors who are in the high income brackets. In this fashion high-salaried officers seek to provide themselves with generous retiring allowances, while at the same time the corporation claims a deduction therefor, in the hope that the fund may accumulate income free from tax.

Thus, in one case $43,000 is annually appropriated by the corporation to a pension trust for the benefit of its two chief owners. One of the coowners will retire at the age of 65 with a monthly pension of $1,725, and the other will retire at 60 with a monthly pension of $1,425.

These eight types of tax avoidance are sufficient to show that there is a well-defined purpose and practice on the part of some taxpayers to defeat the intent of Congress to tax incomes in accordance with ability to pay. In some cases, the Bureau of Internal Revenue under existing law can establish a liability or, indeed, proceed on the ground of fraud; but many of these cases fall in the category of a legal though highly immoral avoidance of the intent of the law. It seems, therefore, that legislation should be passed at this session of the Congress in order to eliminate those loopholes which our preliminary investigation has proved; and that as a result of the further investigation this summer and autumn the next session of the Congress should finally close any further loopholes which may be discovered.

In addition to these cases of moral fraud, there are three other major instances in which the law itself permits individuals and corporations to avoid their equitable share of the tax burden.

1. PERCENTAGE DEPLETION

This is perhaps the most glaring loophole in our present revenue law. Since 1928 large oil and mining corporations have been entitled to deduct from 5 to 27 1/2 percent of their gross income as an allowance for the depletion of their mines or wells, and the deduction may be taken even though the cost of the property has been completely recovered. Thus, in 1936, one mining company deducted nearly $3,000,000 under this provision, although it had already completely recovered the cost of its property.

The amount of the deduction was a sheer gift from the United States to this taxpayer and its stockholders, and the revenue that we lost thereby was $318,000. Similar annual losses of revenue in the cases of a few other typical companies are $594,000, $567,000, $512,000, $272,000, $207,000, $202,000, and $180,000. The estimated annual loss of revenue due to this source alone is about $75,000,000. I recommended in 1933 that this provision be eliminated, but nothing was done at that time; and it has since remained unchanged.

2. THE DIVISION OF INCOME BETWEEN HUSBAND AND WIFE IN THE EIGHT COMMUNITY-PROPERTY STATES

This is another major cause of revenue loss, which is unjustifiable because obtained at the expense of taxpayers in the 40 States which do not have community-property laws. A New York resident with a salary of $100,000 pays about $32,025 Federal income tax; a Californian with the same salary may cause one-half to be reported by his wife and the Federal income tax payable by the two will be only $18,020. The total loss of revenue due to this unjustifiable discrimination against the residents of 40 States runs into the millions.
3. TAXATION OF NONRESIDENT ALIENS

The 1936 act eliminated the requirement that a nonresident alien (without United States office or business) should file a return; fixed the withholding rate for individuals at 10 percent; and freed the nonresident alien from taxation on American capital gains. Since the total Federal tax upon a citizen or resident amounts to 10 percent of his total net income at about $25,000 (in the case of a married individual with no dependents), the withholding rate has proved in practice to be too low as applied to wealthy nonresident alien individuals. There are a number of cases of nonresident aliens with large incomes from American trusts or with large American investments whose taxes have been cut to one-third or one-fifth of what they paid under the prior act.

Thus, one American woman who married an Englishman had an income from this country in 1935 of nearly $300,000. Her tax for 1936 will, therefore, be approximately $30,000 as against over $160,000 under the prior law.

Another American woman who married a Frenchman has an income of over $150,000 from American trusts on which she paid a tax of about $35,000 in 1935. Her tax is reduced to about $15,000 by the 1936 law. Although the tightening of the withholding provisions in 1936 will tend to insure more revenue from nonresident aliens in the lower-income brackets, the present taxing provisions are not satisfactory as applied to nonresident aliens with incomes in the higher brackets.

The problem of tax avoidance is not new. The Congress devoted particular attention to it in 1933 and 1934, and by legislation effectively put a stop to many evasive devices discovered then as having been in use. The practices outlined above can and should be stopped in the same way.

In conclusion, I have two observations to make from the evidence before me. In the first place, the instances I have given above are disclosed by a quick check of comparatively few individual returns. As I have said before, most of the large corporation returns have not yet been filed. The general audit of 1936 returns is just beginning. Nevertheless, it is likely that the cases I have digested above are symptomatic of a large number of others, which will be disclosed by the usual careful audit.

In the second place, the ordinary salaried man and the small merchant does not resort to these or similar devices. The great bulk of our 5,500,000 returns are honestly made. Legalized avoidance or evasion by the so-called leaders of the business community is not only demoralizing to the revenues; it is demoralizing to those who practice it as well. It throws an additional burden of taxation upon the other members of the community who are less able to bear it, and who are already cheerfully bearing their fair share. The success of our revenue system depends equally upon fair administration by the Treasury, and upon completely honest returns by the taxpayer.

The disclosures are so serious that I recommend that authority be given to the Treasury Department with an adequate appropriation in order that a complete and immediate investigation may be conducted. The cost of such an investigation will be returned many times over to the Treasury of the United States.

Faithfully,

HENRY MORGENTHAU, JR.

A feeling of indignation on reading this letter will, I am confident, be yours, as it is mine.

What the facts set forth mean to me is that we have reached another major difficulty in the maintenance of the normal processes of our Government. We are trying harder than ever before to relieve suffering and want, to protect the weak, to curb avarice, to prevent booms and depressions, and to balance the Budget. Taxation necessary to these ends is the foundation of sound governmental finance. When our legitimate revenues are attacked, the whole structure of our Government is attacked. "Clever little schemes" are not admirable when they undermine the foundations of society.

The three great branches of the Government have a joint concern in this situation. First, it is the duty of the Congress to remove new loopholes devised by attorneys for clients willing to take an unethical advantage of society and their own Government. Second, it is the duty of the executive branch of the Government to collect taxes, to investigate fully all questionable cases, to prosecute where wrong has been done, and to make recommendations for closing loopholes. Third, it is the duty of the courts to give full consideration to the intent of the Congress in passing tax laws, and to give full consideration to all evidence which points to an objective of evasion on the part of the taxpayer.
Very definitely, the issue immediately before us is the single one relating to the evasion or unethical avoidance of existing laws. That should be kept clearly in mind by the Congress and the public. Already efforts to befog this issue appear. Already certain newspaper publishers are seeking to make it appear, first, that if an individual can devise unanticipated methods to avoid taxes which the Congress intended him to pay, he is doing nothing unpatriotic or unethical; and, second, that because certain individuals do not approve of high income-tax brackets, or the undistributed earnings tax, or the capital gains tax, the first duty of the Congress should be the repeal or reduction of those taxes. In other words, not one but many red herrings are in preparation.

But it seems to me that the first duty of the Congress is to empower the Government to stop these evil practices, and that legislation to this end should not be confused with legislation to revise tax schedules. That is a wholly different subject.

In regard to that subject, I have already suggested to the Congress that at this session there should be no new taxes and no changes of rates. And I have indicated to the Congress that the Treasury will be prepared by next November to present to the appropriate committees information on the basis of which the Congress may, if it chooses, undertake revisions of the tax structure.

The long-term problem of tax policy is wholly separate from the immediate problem of glaring evasion and avoidance of existing law.

In this immediate problem the decency of American morals is involved.

The example of successful tax dodging by a minority of very rich individuals breeds efforts by other people to dodge other laws as well as tax laws.

It is also a matter of deep regret to know that lawyers of high standing at the bar not only have advised and are advising their clients to utilize tax-avoidance devices, but are actively using these devices in their own personal affairs. We hear too often from lawyers, as well as from their clients, the sentiment, "It is all right to do it if you can get away with it."

I am confident that the Congress will wish to enact legislation at this session specifically and exclusively aimed at making the present tax structure evasion proof.

I am confident also that the Congress will give to the Treasury all authority necessary to expand and complete the present preliminary investigation, including, of course, full authority to summon witnesses and compel their testimony. The ramifications and the geographical scope of a complete investigation make it necessary to utilize every power of Government which can contribute to the end desired.

THE WHITE HOUSE, June 1, 1937.

The CHAIRMAN. Next we will insert the public resolution under which we are acting today.

(The document referred to is as follows:)

[Public Resolution—No. 40—75th Congress]

(Chapter 816, 1st Session)

(S. J. Res. 155)

JOINT RESOLUTION To create a Joint Congressional Committee on Tax Evasion and Avoidance

Resolved by the Senate and House of Representatives of the United States of America in Congress assembled, That (a) there is hereby established a joint congressional committee to be known as the Joint Committee on Tax Evasion and Avoidance (hereinafter referred to as the joint committee).

(b) The joint committee shall be composed of six Members of the Senate who are members of the Committee on Finance, appointed by the President of the Senate, and six Members of the House of Representatives who are members of the Committee on Ways and Means, appointed by the Speaker of the House of Representatives. A vacancy in the joint committee shall not affect the power of the remaining members to execute the functions of the joint committee, and shall be filled in the same manner as the original selection.

Sec. 2. It shall be the duty of the joint committee to investigate the methods of evasion and avoidance of income, estate, and gift taxes, pointed out in the
message of the President transmitted to Congress on June 1, 1937, and other methods of tax evasion and avoidance, and to report to the Senate and the House, at the earliest practicable date, and from time to time thereafter, but not later than February 1, 1938, its recommendations as to remedies for the evils disclosed by such investigation.

SEC. 3. (a) The joint committee, or any subcommittee thereof, shall have power 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. Subpoenas shall be issued under the signature of the chairman of said joint committee, and shall be served by any person designated by him. Amounts appropriated for the expenses of the joint committee shall be disbursed one-half by the Secretary of the Senate and one-half by the Clerk of the House. The provisions of sections 101 and 102 of the Revised Statutes shall apply in case of any failure of any witness to comply with any subpoena, or to testify when summoned, under authority of this joint resolution.

(b) (1) The Secretary of the Treasury and any officer or employee of the Treasury Department, upon request from the joint committee, shall furnish such committee (at a public hearing or otherwise, as the joint committee or a subcommittee thereof consisting of two or more members, may determine) with any date of any character contained in or shown by any return of income, estate, or gift tax.

(2) The joint committee shall have the right, acting directly as a committee, or by or through such examiners or agents as it may designate or appoint, to inspect any or all such returns at such times and in such manner as it may determine.

(3) The joint committee shall have the right to submit any relevant or useful information thus obtained to the Senate and the House of Representatives, and shall submit such information to the Committee on Ways and Means and the Committee on Finance. The Committee on Ways and Means or the Committee on Finance may submit such information to the House or to the Senate or to both the House and the Senate, as the case may be. The joint committee (but no subcommittee or member of the joint committee) shall have the right to make public any such information, in such cases and to such extent as it may deem advisable, but no such information shall be made public with respect to any particular taxpayer unless specifically authorized by the joint committee; but this sentence shall not apply to information made public through the medium of a public hearing as provided in paragraph (1) of this subsection.

SEC. 4. The joint committee shall have power to employ and fix the compensation of such officers, experts, and employees as it deems necessary for the performance of its duties, but the compensation so fixed shall not exceed the compensation fixed under the Classification Act of 1923, as amended, for comparable duties. The joint committee is authorized to utilize the services, information, facilities, and personnel of the departments and agencies in the executive branch of the Government; and of the Joint Committee on Internal Revenue Taxation.

SEC. 5. The joint committee may authorize any one or more persons to conduct any part of such investigation on behalf of the committee, and for such purpose any person so authorized may hold such hearings, and require by subpoena or otherwise the attendance of such witnesses and the production of such books, papers, and documents, administer such oaths, and take such testimony, as the committee may authorize, but nothing in this section shall be construed as authorizing a public hearing. In any such case subpoenas shall be issued under the signature of the chairman of the joint committee and shall be served by any person designated by him.

SEC. 6. All authority conferred by this joint resolution shall expire on February 1, 1938.

Approved, June 11, 1937.

The CHAIRMAN. We will next insert the letter from the chairman to the Secretary of the Treasury, relating to compliance with the resolution.

(The document referred to is as follows:)
Rev. Henry MORGENTHAU, Jr.,
Secretary of the Treasury, Washington, D. C.

My dear Mr. Secretary: On June 15, 1937, the Joint Committee on Tax Evasion and Avoidance, appointed pursuant to Public Resolution No. 40, Seventy-fifth Congress, adopted the following motion:

"I move that, pursuant to the authority granted in Public Resolution No. 40 Seventy-fifth Congress, the Secretary of the Treasury be requested, by himself or by any officer or employee of the Treasury Department whom he may designate, to furnish this committee at public hearings before this committee beginning on June 17, 1937, at 10 a.m., information (including data of any character, contained in or shown by any return of income, estate, or gift taxes) relating to the methods of evasion or avoidance of income, estate, or gift taxes, pointed out in the message of the President transmitted to Congress on June 1, 1937, and other methods of tax evasion or avoidance."

Pursuant to such motion, I hereby, on behalf of the joint committee, respectfully request compliance with such motion.

Very sincerely yours,

R. L. Doughton,
Chairman, Joint Committee on Tax Evasion and Avoidance.

The CHAIRMAN. The first witness this morning will be Hon. Henry Morgenthau, Jr., Secretary of the Treasury.

STATEMENT OF HON. HENRY MORGENTHAU, JR., SECRETARY OF THE TREASURY

The CHAIRMAN. Mr. Morgenthau, everyone knows the capacity in which you appear, I presume. Do you prefer to make your main statement without interruption?

Secretary MORGENTHAU. I would appreciate it.

The CHAIRMAN. Any questions will be asked after you have concluded your main statement.

Secretary MORGENTHAU. I would appreciate it very much.

The CHAIRMAN. You will be accorded that privilege.

Secretary MORGENTHAU. Mr. Chairman and gentlemen of the committee, the problem of closing loopholes in tax laws is continuing and ever-present. It is never settled by any particular legislation. Tax administration today requires a succession of laws to prevent the use of ingenious devices which distort the original purpose of the act and which create what to the average man seems unethical and unwarranted avoidance of taxes.

This is not the result of activities on the part of any particular group of persons. Nor is it the result of concerted action on the part of taxpayers as a whole. It is caused by pressures which come from deep-seated attitudes in certain quarters toward taxation. These attitudes and these pressures must be realistically considered as part of the problem of tax administration. I will describe them briefly because they furnish the background against which tax administration must operate.

In the first place, we have developed in this country a group of ingenious lawyers and accountants who make their living by showing to people who can afford to employ them ways by which they may pay the least possible taxes. This may be a legitimate business. Nevertheless, by virtue of its highly competitive character, it brings about the following situation: The ordinary accepted standard by which many wealthy taxpayers judge the efficiency of the tax attorney is the amount that he can save in taxes. The most ingenious
attorney, therefore, becomes the most successful and the most sought after. He feels that his sole duty is toward his client. If he is honest, he will not condone perjury, but he feels little moral or social responsibility to the Government. Therefore, if he can invent a new scheme for circumventing the intent of tax laws, which will be upheld by the courts, he is well within the ethics of his profession, regardless of the unfortunate effect that such a scheme will have upon the general application of such laws.

We have now a bar of registered attorneys and tax accountants numbering approximately 45,000. Against them are pitted some 2,800 field agents actively engaged in tax investigations for the Government. The contest is, of course, unequal. The fees of the tax lawyer exceed by thousands of percent the pay of his opponent employed by the Government. In this manner the most resourceful brains of the legal world are engaged actively in trying to avoid taxes for their clients. Among these are men who received their early training from the Government, and who use the skill they acquired in that service against the younger men who take their places. The Government then becomes a training school for many of its opponents.

I am not attaching any blame to anyone in particular for this situation. I am only pointing out that it exists and that it is one of the reasons requiring continual revision of the tax laws.

A second factor which creates the problem which now confronts us is the fact that tax avoidance, as opposed to tax evasion, is considered by many a legitimate and honorable aim. Where private obligations are concerned, the same people who now hire ingenious attorneys to cut down their taxes would scorn to use the same subtle devices in avoiding payments to their creditors. Here again I am simply calling attention to an existing attitude. The ethics of tax avoidance have grown up out of a variety of circumstances, and the problem is not solved by blaming anyone. It is only important to recognize those ethics as an existing fact, because they are a very important element in the problem which faces the Treasury.

I hope that in the future an atmosphere may be created in which men will hesitate to use ingenious devices to avoid the payment of taxes. Nevertheless, that happens to be the present attitude of some persons toward payment to the Government.

A third factor in the situation is the difficulty of distinguishing, at least before a case is tried, between tax avoidance which is supposed to be proper, and tax evasion which is supposed to be immoral. I will not attempt to define these terms. So hazy is the line between tax evasion and tax avoidance that it is always possible to classify any complicated scheme as tax avoidance, so long as there is no absolute certainty that it will be adjudged invalid at the end of long litigation.

These attitudes have created what might be called the sporting theory of tax administration. So long as these attitudes exist, the process of tax legislation will be somewhat as follows: A law will be passed; ingenious devices for circumventing its application to individuals will be tried out. This will take time. Finally, when sufficient of those devices have become current so that a great loss in governmental revenue begins to appear, legislation will have to be
drafted specifically directed at the new tax-avoidance inventions which have appeared since the last law.

Today, because of the variety of devices to avoid taxes, the situation calls for remedial legislation. That this is a recurring situation is illustrated by the tax history of the last few years. Prior to 1934, the provisions permitting deductions for losses resulting from stock sales had become one of the largest loopholes in our tax administration. Ingenious use of these deduction provisions permitted individuals to establish losses by exchanging stocks with each other and calling the transaction a sale. However, it was the kind of a sale which would never have taken place had it not been for the desire to avoid taxes. That loophole was plugged in 1934. Since that date new devices of even greater complexity and ingenuity have been developed, imitated, and copied, until they are now in very general use. As is usual in such cases, it takes time before sufficient interest is created to demand reform. For example, in 1935, 2 years ago, under my instructions, Mr. Robert H. Jackson called to the attention of the Committee on Finance many of the methods of tax evasion which are now the subject of this inquiry. The use of those devices was then a less serious obstruction to the collection of revenue and nothing was done about them. Resort to them has now increased to such an extent that some reform is imperative.

Of course, the attitudes which create this continuous task of circumventing new tax-avoidance devices cannot be legislated away. The immediate objective in the present emergency is practical tax legislation. Nevertheless, I am hopeful that the continued publicity which hearings of this sort give with respect to the game of tax avoidance may help to create an atmosphere in which men will hesitate to use these artificial devices to avoid the payment of taxes, just as today they hesitate to use such devices to escape the payment of private debts. The great body of citizens already display the same attitude toward their obligations to the Government that they display toward their private obligations. An examination of their returns year after year discloses no attempts to push the letter of the law to its limit, and no use of corporate forms or other elaborate subterfuges for the sole purpose of avoiding their normal tax burden. Perhaps continued publicity given to the more fantastic methods of tax avoidance now considered legitimate may make such an attitude more nearly universal. This may be an important byproduct of public hearings on current tax devices.

I will therefore attempt briefly to describe the general character of some of the methods now in use in terms which the average taxpayer may understand. One characteristic runs through all of them. It is the creation of a multiple personality in the taxpayer. By this device he ceases to be a single individual and becomes a whole group of people, some of whom are earning money while others are losing it. He divides himself into several people, sometimes incorporated and sometimes not. He purports to carry on business transactions with his family at arm's length. Often he convinces himself that these separate people actually exist. Each one of these imaginary individuals into which the taxpayer divides himself deals and trades with all the other imaginary individuals.
The total result is a series of losses which would not have been deductible for tax purposes had the taxpayer remained a single personality. The different methods by which the parts of this multiple personality deal with each other are varied and intricate. We will attempt to classify them later. They are, however, of this general character. A taxpayer creates a separate personality to engage in an activity which is a hobby or a luxury or an ordinary living expense or even a method of investing funds. He then charges the expenses and the losses of such activity against himself. Thus, he is able to pay interest to himself, to charge himself for vacations and pleasures, to give himself pensions, to be his own insurance company, and so on. These transactions partake of the same unreal character as if a small taxpayer incorporated his household kitchen as a restaurant and deducted the expenses and losses from his taxable income because he had so few customers.

Practically all of the devices which we will cite later would look absurd if applied to persons of small incomes whose activities were necessarily more restricted. They are important as tax-dodging devices only for the very rich. Not only do they look absurd when applied to the small taxpayer, but they are also too expensive to be useful unless large sums are involved.

The analogies which are used to support these devices are found in the corporate structure by which business in this country is conducted. The distinguishing feature, however, between the corporation used for a business purpose and the corporation used for a tax-avoidance purpose is the fact that in the latter case were it not for the tax laws no such corporations would have been formed.

The use of the corporate device in order to split a single man into a number of personalities is often extraordinarily intricate. However, of late some tax attorneys have felt that it was not necessary to go to so much trouble. They have in effect split individuals up into different persons without bothering to incorporate. A rich man runs a racing stable as a hobby. He calls himself a horse-breeder and in this character loses money very heavily indeed. He never makes a financial success as a horse breeder because racing demands too much luxury on his farm. This raises his expenses. He then charges off the loss on his racing stable against his income.

No small taxpayer would think of calling himself a golf instructor and then charge the expense of his golf game against his income because he had no pupils. However, we find an individual who in one capacity charters a pleasure yacht to himself at a loss and deducts it from his income because, though as a businessman he is successful, as a professional yachtsman he is a heavy loser.

These instances are not yet as frequent as the use of the complicated corporate personality, which is harder to see through. Nevertheless, unless legislative action is soon taken, such pleasant methods of taking vacations and getting rid of taxes at the same time will be limited and constitute a serious threat to the revenue.

Most of these people have talked themselves into believing that the methods which they use are socially legitimate. They profess complete personal irresponsibility, contending that if their methods are wrong it is the duty of the tax administration to ferret them out and to conduct long and expensive litigation in order to determine their validity. The individual believes that he is morally en-
titled to take the sporting chance and that he has nothing to lose and everything to gain by taking it.

The device of the multiple personality of the single taxpayer is of course not the only loophole which requires immediate attention. The Under Secretary of the Treasury, Mr. Roswell Magill, who will follow me, will undertake to classify the principal ones for you in detail. I will only summarize the principal schemes which are being devised, copied, and imitated today. They may be divided roughly into three classes:

First, there is the device which I have just described of making the taxpayer a multiple personality whose characters deal with each other.

Second, there is a variation on that device by which the taxpayer deals with his family at arm's length and creates taxable losses out of the performance of personal obligations which he owes to them. He takes his wife into partnership with him. He splits his income between himself and his children instead of maintaining them.

The third device is one where the individual doing business in this country makes it appear by a series of corporate personalities which he controls that he is actually doing business abroad in some country where he cannot be taxed. In other words, transfers of title which might result in taxable income are made to appear to have occurred outside of the United States.

We do not know how extensively this latter device is being used. We do know that within the last 2 years 585 foreign corporations have been formed which probably represent business interests in America. We do not know how many have been used for tax-avoidance purposes, but we do know that some have been so used. We believe, however, that the use of this device is spreading. It is most important that its growth be stopped before vested interests arise which make it a still more difficult problem to deal with in the future.

For these reasons I believe that the use of the multiple personality by the taxpayer has now reached the stage where Congress should consider corrective legislation. The process of fighting in the courts all the different schemes which may be woven around this concept is too slow for efficient tax administration. We intend to give examples of a large number of cases, not all of which would be upheld by the courts but many of which are sufficiently plausible so that they can delay and hinder tax collection. It is the history of tax litigation that it takes years to finally outlaw a tax avoidance device, once it gets a foothold among tax attorneys. In the meanwhile the Government revenue is impaired in two ways: First, by the actual loss of revenue in specific cases; and second, by the expenditure of the time and energy of the tax-enforcing agencies in litigation.

It is true that many of the devices which we have referred to are being limited and restricted by the courts. Nevertheless, the situation is sufficiently confused so that a great deal of litigation is required because each case deals with only the particular facts involved and distinctions in intricate situations can always be made.

And what effect has the increasing use of these devices on revenues? That, of course, cannot be exactly determined. Nevertheless,
it is a substantial factor which is cumulative in effect, just as the influence of a continued course of sharp practices in bankruptcy cases tends to reduce the total dividends to creditors. The nearest estimate which we can make of the loss in revenues caused by such practices in the tax field has been arrived at in the following way:

As you know, each November the Treasury Department is required to make an estimate of the revenue of the Federal Government for the balance of the current fiscal year ending on the following June 30. I need hardly say that the problem of estimating the revenue is an exceedingly complicated one; and that some margin of error in the annual estimates, resting as they do upon forecasts of business conditions, prices, and a host of other factors, is inevitable. I take great satisfaction in the accuracy of the revenue forecasts made since I assumed the responsibilities of the office of Secretary of the Treasury. The first estimate of income-tax receipts made under my supervision was for the fiscal year 1935. Actual receipts for that year proved to be 4.6 percent greater than my estimate. In the following fiscal year, 1936, actual receipts were only 1.5 percent under my estimate for that year. For the fiscal year 1937, the Treasury Department employed the same methods and the same personnel in making the revenue estimates as had been employed in the two preceding years. When, therefore, the March 15 income-tax collections indicated that total income tax receipts for the fiscal year 1937 might be as much as 10.4 percent below the estimate made last November, I became concerned.

I realized fully, as I am sure you do, that all the care in the world could not always prevent a substantial error from entering into our revenue estimates, for, as I have already said, these estimates depend upon forecasts of the future; and the capacity is not given to mere human beings to foretell the future with accuracy. I was aware also that my predecessors in the Treasury Department had overestimated the Government's income-tax receipts in the 3 years 1931, 1932, and 1933, by 15.1 percent, 7.8 percent and 13.3 percent, respectively.

Nevertheless, I decided to investigate the details, so far as possible, of our March 1937 income-tax collections. This investigation disclosed the following very significant fact:

Collections in certain areas where there is a considerable concentration of wealth and income had not increased by as large a percentage as had the total income-tax receipts for the country as a whole.

In connection with this fact it is particularly important to note that dividends represent a larger percentage of the net income of people with large incomes than they do for people with small incomes. We knew that dividend disbursements by corporations during the calendar year 1936 had increased materially over those of the preceding calendar year.

It seemed reasonable to suppose, therefore, that part at least of the discrepancy between our original estimate of income-tax receipts and the receipts that might be estimated on the basis of our actual collections in March 1937, might be due to a wider use of various methods of tax evasion and tax avoidance. And when Mr. Magill undertook a field investigation of this possibility at my request he found much to support this conclusion.
Mr. Magill will describe to you in some detail the character of his investigation. Necessarily, it was a quick survey, and the further audit of the 1936 returns will undoubtedly disclose additional data to enable us to determine with greater accuracy the methods of avoidance employed by some taxpayers. In this connection, it must be borne in mind that the Bureau of Internal Revenue faces tremendous physical problems in the audit of the returns and in its effort to prevent tax evasion and avoidance. There were about 6,000,000 returns filed for the taxable year 1936, and it has been our experience in the past that only about 500,000 can be audited with the force of about 3,000 men that we have available.

I believe that it may be appropriate to say a few words regarding the Bureau's progress in the last few years in connection with the making of these detailed audits. Prior to 1935 the field investigations of returns were not commenced until approximately 1 year after filing and were not completed until about 2 years after filing. At present, field investigations are begun 3½ months after filing and are completed 15½ months after filing—an advance in the conduct of the work of field investigations of approximately 9 months.

The collection of additional taxes, a substantial portion of which represents recoveries in instances when tax avoidance or evasion has been attempted, has constantly been increasing. Our revenue agents' recommendations for the assessment of additional taxes increased from 203 million in 1934 to 355 million in 1936.

Experience has shown that, through litigation or agreement with the taxpayer, about 70 percent of these recommended additional taxes are ultimately collected by the Treasury. For the first 10 months of the present fiscal year agreements with taxpayers for the collection of additional taxes amounting to about 130 million have been secured, and Commissioner Helvering has informed me that he is confident that the Bureau will collect by agreements more taxes during this fiscal year than it has ever collected in that manner at any time in its history.

Undoubtedly, prevention of tax avoidance and evasion would be aided by an examination of a greater volume of returns. I think that fully 750,000 returns, rather than the present 500,000, deserve yearly audit. However, in consideration of the small personnel of the Department compared with the very large number of accountants and attorneys who are constantly engaged in the preparation of returns and in the defense of the taxpayers' contentions, the record of the Bureau is good. With our limited force, we must collect the maximum of revenue, and we must do so in such a way that we are not years behind in our work.

These tax-avoidance devices to which I have alluded have affected revenues of the Government in the following ways:

1. They create the belief that rich men with expensive attorneys do not have to pay taxes. There is just enough truth in this to have far-reaching consequences on the morale of hundreds of thousands of taxpayers. No one can possibly calculate how many petty evasions which can never be detected among 6,000,000 returns are due to the belief that cleverness, rather than fairness, is a proper criterion of the taxpayer. Thus, tax ethics generally today are where business ethics and trade practices were in the nineties.
2. In the highly competitive situation which exists among expert tax attorneys, plausible devices spread rapidly and tax evasion and avoidance increase without anyone realizing the extent of the impairment of tax administration until the end of the taxable year. Even then an exact estimate of the effect of tax avoidance is impossible.

3. Vested interests grow up in tax-avoidance devices in the course of time, so that it becomes very difficult to change them after they receive a semirespectable standing. This factor makes quick action advisable to decapitate new schemes before they achieve the force and respectability of law.

4. After tax-avoidance devices have become an accepted part of tax law, any attempt to change them is heralded as a persecution of the rich. Today, for example, we are met by the charge made in some quarters that this attempt on the part of the Treasury, forced on us by a gradual accumulation of tax-avoidance devices since the passage of the Revenue Act of 1934, is an attack on wealth. Actually, anyone who gives the matter unbiased consideration will realize that it is for the benefit of the rich to plug loopholes in tax laws, since this raises more revenue without raising rates. The prevalence of the devices we are going to describe has cast a suspicion on many rich men who do not deserve such suspicion. There is certainly no possible advantage to the conscientious man of large income to allow fantastic schemes of tax avoidance to continue.

5. And finally, there is the very important question of the revenue. Those tax devices which defeat the intent of Congress cost the Government huge sums which Congress never actually intended to give away. Moreover, they create continual and expensive litigation. No collecting agency can operate effectively if it is hampered at every turn by lawsuits.

For these reasons, I considered it imperative to call these matters to the attention of Congress at this time. I thank you.

Senator Walsh. Mr. Chairman.

The Chairman. Senator Walsh.

Senator Walsh. Mr. Secretary, is it your wish and object that this committee should report a bill changing the administrative tax laws during this session?

Secretary Morgenthau. Yes.

Senator Harrison. As I understand, Mr. Secretary, your experts in the Treasury Department have been working upon some drafts of legislation, have you not, to submit to the committee, that might plug some of these loopholes?

Secretary Morgenthau. We have been working with the staff of the Joint Committee on Internal Revenue Taxation, and just how far they have progressed I don’t know, but we have been working with them along those lines.

The Chairman. Mr. Secretary, on page 8 of your statement, referring to the class of people you have mentioned previously, you state:

Most of these people have talked themselves into believing that the methods which they use are socially legitimate.

Just what do you mean by “socially legitimate”?

Secretary Morgenthau. Well, it grows up—
The Chairman. It is not morally legitimate. I never did hear the words “socially legitimate” used.

Secretary Morgenthau. Well, I would describe it, I think, this way: That they believe that they can follow these practices without being criticized by their associates for doing something against society, possibly.

Senator George. They will at least escape ostracism?

Secretary Morgenthau. Thank you, sir.

The Chairman. In other words, the moral standards of their associates will not be such as to condemn these practices which you have enumerated?

Secretary Morgenthau. Well, that seems to be what has happened. The people who are engaging in these practices, and their friends, seem to think it is all right, and if they can get away with it—fine, in their opinion.

Mr. Cooper. Mr. Chairman.

Under Secretary Magill. Mr. Chairman, the various particular devices we expect to take up a little later. The Secretary did not refer, as you observed, to each of the different methods which may be used for tax evasion or tax avoidance. Now, as the President's message indicated, there are several methods which may be regarded as inequitable, as I, for instance, regard the community-property situation, but which, nevertheless, are legal under the laws as they stand now. That is, as you know, in the community property situation you have the difficulty that there are a number of Supreme Court decisions that may prevent you from doing anything effective about discriminating against taxpayers in the other 40 States.

Mr. Crowther. Then that would be recognized as legal avoidance at present?

Under Secretary Magill. I have the same difficulty that the Secretary expressed in deciding what is evasion and what is avoidance, but certainly, under the law as it stands now, these taxpayers are honestly reporting their incomes.

Mr. Cooper. Mr. Chairman. Will you yield?

Mr. Crowther. I yield.

The Chairman. Mr. Cooper.

Mr. Cooper. Of course, it is true, is it not, Doctor, that the question of community property is nothing new; we have had that before us all along?

Under Secretary Magill. That is true.
Mr. Cooper. And the Ways and Means Committee has time after time given consideration to that, and there was not any special occasion for the Secretary to call attention to that, because that has been constantly before the committee for years? Isn't that true?

Under Secretary Magill. Well, I recall, for example, as you know, that the Ways and Means Committee went over the whole thing very thoroughly in 1934, with the result that, after careful consideration, no recommendations were made.

Mr. Cooper. And there is a very serious legal question involved in that?

Under Secretary Magill. Undoubtedly, under the Supreme Court decisions.

Mr. Crowther. And also a very considerable loss of revenue?

Under Secretary Magill. Unquestionably.

Mr. Vinson. Mr. Chairman, will the gentleman yield?

Mr. Cooper. I yield.

The Chairman. Mr. Vinson.

Mr. Vinson. While we are on that subject, is it fair to state that the income taxed by the Federal Government is the income recognized by law, by the State law?

Under Secretary Magill. To a large extent that is true.

Mr. Vinson. Isn't it also true that in several of the community-property States they had laws for their people before they became a part of the United States?

Under Secretary Magill. I believe that is true.

Mr. Vinson. And isn't it further true that they came into the Union in some instances under a treaty which recognized the civil law under which the community-property system grew up?

Under Secretary Magill. Well, not being a resident of a community-property State, I don't know those legal details, but it is true, I believe——

Mr. Vinson. I say to you that that is true as true.

Under Secretary Magill. Well, I take it then.

Mr. Treadway. Mr. Chairman.

The Chairman. Mr. Treadway.

Mr. Treadway. In that connection, Doctor, may I call attention to the paragraph on page 5 of the Secretary's letter to the President, dealing with the subject of community property, and showing the very definite loss to the Treasury as a result of the difference in the amount that a resident of California would pay and the amount that that same person would pay with the same income residing in New York?

I ask that paragraph 2 on page 5 be incorporated in the hearings at this point.

Mr. Cooper. Mr. Chairman, in that connection I raise a point of order. The entire message is in the hearings.

Mr. Treadway. Then I will interrogate Dr. Magill, rather than have any question raised as to its insertion.

You are familiar, are you not, Dr. Magill, with the letter of the Secretary of the Treasury addressed to the President?

Under Secretary Magill. I have read it; yes, sir.

Mr. Treadway. And probably helped in its preparation?

Under Secretary Magill. I was present when it was being prepared.
Mr. TREADWAY. Yes; I assumed so. You are familiar with the details as designated on page 5 of the President's message?

Under Secretary MAGILL. Yes, sir.

Mr. TREADWAY. With reference to the division of income between husband and wife in the eight community-property States?

Under Secretary MAGILL. Yes, sir.

Mr. TREADWAY. It is correct, is it not, that eight States receive a benefit from this method of taxation that 40 States do not receive?

Under Secretary MAGILL. That is true, I believe, yes.

Mr. TREADWAY. Is it a customary procedure to have majority rule or minority rule?

Under Secretary MAGILL. I dare say you can answer that better than I, but I—

Mr. TREADWAY. Isn't it a fact that it has been suggested that the other 40 States comply in their State laws with the laws of the 8 States that have community-property laws?

Under Secretary MAGILL. You, again, I think would know the answer better than I. My understanding is that suggestions have been made in Massachusetts, for instance, along that line. I don't know how widespread those suggestions have been.

Mr. TREADWAY. Well, then, is it a fact that a resident of New York State with a salary of $100,000 would pay $32,525 Federal income tax and a Californian with the same salary may cause one-half to be reported by his wife so that the combined Federal income tax payable by the two would only be $18,626?

Under Secretary MAGILL. Yes sir.

Mr. TREADWAY. Those figures have been worked out, I suppose?

Under Secretary MAGILL. I did not make those computations, but they were made for me and I think they are accurate.

Mr. VINSION. Will the gentleman yield to me on that point?

Mr. TREADWAY. Well, I was going to ask—

Mr. VINSION. Right on that point?

Mr. TREADWAY. Very good.

Mr. VINSION. Now, Mr. Magill, when this statement says that—a Californian with the same salary may cause one-half to be reported by his wife and the Federal income taxes payable by the two will be only $18,620—is that technically accurate, when you say that they may cause that report to be made?

Under Secretary MAGILL. Well, I think it was put that way for this reason, Mr. Vinsion—I see your point, and if I may explain it a little I think I can make it clear: I presume that it would be possible, so far as our tax law is concerned, for the husband to report his entire income, because we provide for joint returns by the husband and wife if they so choose, as you know.

Now, on the other hand, as I understand the California law—and I don't know it, I will yield to you on that—my understanding is that the law in substance is that the moment the husband earns that income a vested interest in one-half of it arises in his wife, and that consequently the one-half is regarded as being hers under the laws of those States; and, as you know, the Supreme Court in Poe v. Seaborn (282 U. S., 101), in 1930, recognized that situation and said accordingly that the husband could not be taxed on the entire income. So that is where we are, I believe, on that.
Mr. Vinson. Then do you think that you are technically accurate when you say the term "may cause" the income to be divided, when under the law of the particular State it is divided?

Under Secretary Magill. That perhaps might be a better way to put it.

Senator George. Dr. Magill, on this question of community property, it is simply a tax problem, one of the problems on which the two committees of the House and Senate have labored for many years, and strictly, actually, it does not present avoidance or evasion any more than investment in tax-exempt securities, any more than the nontaxation by the Federal Government of the salaries paid to State officials in office. It is a problem of taxation, is it not?

Under Secretary Magill. I would think they rest on very much the same footing. In both cases you have a series of decisions of the Supreme Court, with which the Treasury, of course, must comply, that lead to the situation which we have. I am sure the Secretary had no intention, and no one else in the Department had any intention, of saying that a taxpayer in California is evading the law in reporting his income in this way. He clearly is not.

Senator George. The problems growing out of community property did not grow up because of the income-tax laws. It long predated it. And, just as the theory that the Federal Government could not tax the salary of the State official, it had no necessary connection. Of course, it is a fact, and therefore is a problem with which we are always attempting to deal.

Under Secretary Magill. That is right; yes, sir.

Mr. Treadway. Mr. Chairman.

The Chairman. Mr. Treadway.

Mr. Treadway. One other question on this subject, if I may, Doctor.

Under Secretary Magill. Yes, sir.

Mr. Treadway. The concluding sentence of the paragraph to which I referred reads as follows:

The total loss of revenue due to this unjustifiable discrimination against the residents of 40 States runs into the millions.

Do your computations in the Treasury justify that statement, that there are millions lost to the Federal Government by the community property taxation?

Under Secretary Magill. There are millions lost in this way: That if the 8 States did not have the community property law, and if the incomes in those States were reported in the same way in which incomes are reported in the other 40 States, the Treasury would be the gainer by a good many millions.

Mr. Treadway. So this is one of the very serious complications resulting from diversified laws, is it not?

Under Secretary Magill. I would say, as Senator George has put it, it is a situation which we confront under the revenue laws, and the Supreme Court decisions as they now stand.

Mr. Treadway. And of course it has been known indefinitely—

Under Secretary Magill. For a long time.

Mr. Treadway. This form of tax avoidance?

Under Secretary Magill. Yes.

Mr. Treadway. It is nothing new? It has not been just injected into the problem?
Under Secretary Magill. No. I think there has been litigation about it for 10 or 15 years.

Mr. Treadway. Now, Mr. Chairman, if I may, I would like to pass to just one other subject.

The Chairman. Mr. Treadway.

Mr. Treadway. I would like to turn to page 6 of the President's message, Doctor. The last sentence in the Secretary's letter to the President reads as follows [reading]:

The disclosures are so serious that I recommend that authority be given to the Treasury Department with an adequate appropriation in order that a complete and immediate investigation may be conducted.

If I recall correctly, the original resolution that was presented to both branches of Congress, I think June 1, if I am not mistaken—

Under Secretary Magill. Yes, sir.

Mr. Treadway. Provided for that form of investigation, did it not?

Under Secretary Magill. Yes; in the last section of the resolution.

Mr. Treadway. The resolution presented to both branches corresponded with the views of the Treasury?

Under Secretary Magill. Yes. The Treasury did not prepare the resolution. It was prepared by the legislative experts up here, and they can tell you better than I what it provided for.

Mr. Cooper. Will you yield there?

Mr. Treadway. Very well.

Mr. Cooper. Isn't it true, Doctor, that section 5 in its original form of that joint resolution provided that investigation was to be made by the joint committee but the joint committee could delegate certain activities to officials and agents of the Treasury Department?

Mr. Treadway. In that connection, Mr. Chairman, I would like to—

The Chairman. Well, let him answer that question, Mr. Treadway, will you please? Let him answer Mr. Cooper's question.

Mr. Treadway. I thought he had finished.

The Chairman. So as to keep the record straight.

Under Secretary Magill. Mr. Cooper, you are undoubtedly more familiar with its terms than I. As I say, the resolution was not drafted in the Department. I saw it after it was introduced. As I understood it, it was along the lines that you stated; that is, the joint committee might employ officers and employees of the Treasury Department to make an effective investigation.

Mr. Cullen. Mr. Chairman.

Mr. Cullen. In order that the record may be kept straight in that regard, the Treasury Department or any of its officials had nothing whatever to do with drafting the resolution which was presented for this investigation of Congress?

Under Secretary Magill. That is correct.

Mr. Treadway. Mr. Chairman, in that connection wouldn't it be fair to say that the whole procedure is the result of the Treasury's anxiety and desire for this investigation? And I am just as anxious to have this investigation of tax evasion and avoidance as the Treasury.

Mr. Cullen. Mr. Chairman, that is another question.
Mr. Treadway. But it strikes me that undoubtedly the original resolution, whoever its actual drafters may have been, was not prepared, and Dr. Magill says it was not prepared by the Treasury, but met with the approval of the Treasury officials, and the draft that contained the original section 5 would absolutely authorize the joint committee to employ officers or employees of the Treasury Department to conduct any part of the investigation. I don't know as we need to get into any argument about it, but at any rate, it is fair to say that the resolution now before us, having all the authority in the hands of Congress, differed from the original draft as submitted to both branches of Congress. Isn't that correct?

Under Secretary Magill. Well, you gentlemen can tell better than I. There were amendments made to it in the House.

The Chairman. Right in that connection, if the gentleman from Massachusetts will permit, the original resolution provided that this joint committee could authorize representatives of the Treasury Department to make investigation. This resolution provides that they can authorize any person. It is even broader than the original. It says, “authorize representatives of the Treasury Department or any other person.” So I don't see anything in that. This resolution is broader than the original in that respect.

Mr. Cooper. Mr. Chairman, will you yield there? In order that there may be no misunderstanding about this point, which I do not regard as material especially, let us give attention to the language in the resolution itself as it passed the Senate before any amendments were made by the House:

SEC. 5. The joint committee may authorize any one or more officers or employees of the Treasury Department to conduct any part of such investigation on behalf of the committee, and for such purpose any person so authorized may hold such hearings, and require, by subpoena or otherwise, the attendance of such witnesses and the production of such books, papers, and documents, administer such oaths, and take such testimony, as the committee may authorize. In any such case subpenas shall be issued under the signature of the chairman of the joint committee and shall be served by any person designated by him.

The fact is that under the language itself the investigation was always under the control of the joint committee. That is correct, isn't it?

Under Secretary Magill. Yes, sir; certainly, on that language; and I assumed that that was true, because my understanding was that the resolution was drawn by legislative counsel for the two Houses at the direction of Senator Harrison and Mr. Doughton.

The Chairman. That is correct.

Senator Harrison. Mr. Chairman, Mr. Magill had a statement to make. Suppose we let him proceed.

Mr. Vinson. There is one question before you get to that.

The Chairman. One more question, Mr. Vinson.

Mr. Vinson. Mr. Secretary, on page 5 of your statement I note that you say that Mr. Robert H. Jackson in 1935, under your instructions, “called to the attention of the Committee on Finance many of the methods of tax evasion which are now the subject of this inquiry.” Was that while the 1935 tax bill was under consideration?

Secretary Morgenthau. Yes; the answer to the question is yes; and his statement was published in your hearing.
Mr. Vinson. I don't recall that there were any statements made before the Committee on Ways and Means during the consideration of that tax bill in regard to loopholes of this kind.

Secretary Morgenthau. If my memory serves me right, it was before the Senate Committee on Finance.

Senator Harrison. Mr. Chairman, in that connection, Mr. Jackson at that time was assistant general counsel of the Treasury Department. Representing the Treasury he appeared before the Finance Committee and in a general discussion he mentioned some methods employed in trying to evade or avoid taxes.

Mr. Vinson. I just wanted to keep the record straight, because of the criticism here that nothing was done about it. So far as the Ways and Means Committee was concerned, we did not hear from Mr. Jackson on that subject.

Mr. Cooper. Mr. Chairman.

The Chairman. Mr. Cooper.

Mr. Cooper. Mr. Secretary, inviting your attention to page 13 of your statement as it has been presented to members of the committee, the statement is there made:

There were about 6,000,000 returns filed for the taxable year 1933, and it has been our experience in the past that only about 500,000 can be audited with the force of about 3,000 men that we have available.

Now, is it your thought that additional personnel to investigate a greater number of returns would be profitable to the Government?

Secretary Morgenthau. Yes; distinctly so.

Mr. Cooper. It is your thought that sufficient personnel should be provided to make it possible to investigate or audit more than the 500,000 returns that you are now able to examine with your present personnel?

Secretary Morgenthau. Yes; it would.

Mr. Vinson. Has Congress ever refused to appropriate money for any personnel that you have requested of it?

The Chairman. Mr. Helvering.

Mr. Guy T. Helvering (Commissioner of Internal Revenue). Generally we have found on this particular question the committee has met us very fairly. These investigations of the last few years involved sending to the field many returns that the personnel could not possibly get to, and that study has come to a point where we have reached the conclusion that if half again of the large returns were investigated it would be profitable.

Mr. Cooper. Two or three years ago I recall that it was the condition then, and an additional amount of $8,000,000 would return $60,000,000 or $75,000,000 added money, and I know that we cooperated in securing the appropriation for that personnel.

Mr. Treadway. How many additional employees were allowed to be put on at the time you brought this to the attention of the Ways and Means Committee about 2 years ago?

Mr. Helvering. Seven hundred and fifty agents.

Mr. Treadway. Extra ones?

Mr. Helvering. Yes.

Mr. Treadway. Additional at that time?

Mr. Helvering. Yes.
Mr. Cooper. This matter was considered, as I now recall, following the study we made which resulted in the 1934 Revenue Act, and the Ways and Means Committee was then very definitely of the opinion that additional personnel should be provided.

Mr. Helvering. I might say, for the information of Mr. Cooper and the committee, that we kept a tabulation of these new men put on. This is subject to verification as to the exact amount, but they saved about $80,000,000 the first year.

Mr. Cooper. Your estimate was 75 million, as I recall it.

Senator Walsh. Mr. Chairman.

The Chairman. Senator Walsh.

Senator Walsh. Though this committee hasn't any jurisdiction over false and fraudulent returns, are you in a position to furnish the committee with the number of cases and the names of the taxpayers who are assumed to be guilty of making false and fraudulent returns, whose cases have been referred to the Department of Justice for prosecution?

Secretary Morgenthau. Yes.

Senator Walsh. Will you furnish the committee with that record?

Secretary Morgenthau. Would you mind repeating, so I can get just what you want, please?

Senator Walsh. The number of cases your Department has referred to the Department of Justice alleging that in their opinion false and fraudulent tax returns have been made by taxpayers.

Secretary Morgenthau. We will be very glad to furnish that.

Senator Walsh. Are there many such cases?

Mr. Herman Oliphant. There is a large number.

Senator Walsh. Have they all been referred to the Department of Justice?

Mr. Oliphant. Yes.

Senator Walsh. Have any of them been prosecuted?

Mr. Oliphant. Yes; they are referred in the regular routine to the Department of Justice.

Senator Walsh. You can supply us with the details?

Mr. Oliphant. Yes; I can and will.

The Chairman. Mr. Secretary, if there are no further questions, who is your next witness?

Secretary Morgenthau. Dr. Magill.

Senator Harrison. I would like to make this observation, that if you need an additional force down there to ferret out these various income-tax returns to ascertain whether there is evasion, I am sure that you are close enough to our friend Mr. Bell there, who is the Director of the Budget, and if he will recommend it, Congress will be good enough to make the appropriation.

Secretary Morgenthau. Mr. Bell and I do see each other occasionally, but I am informed by Mr. Russell that this year he sent up a request for $900,000 for this purpose and Congress cut it down to—how much?

Mr. Charles T. Russell (Deputy Commissioner of Internal Revenue). $450,000.

Secretary Morgenthau. So we got just half what we asked for.

Mr. Cooper. You did pretty well.
The Chairman. We thank you for the testimony you have given the committee.

Secretary Morgenthau. I thank you.

The Chairman. Dr. Magill, will you please give the stenographer your name and address, the position you hold in the Treasury Department, and the capacity in which you appear before the committee?

STATEMENT OF HON. ROSWELL MAGILL, UNDER SECRETARY OF THE TREASURY

Under Secretary Magill. I am Under Secretary of the Treasury Roswell Magill.

The Chairman. Do you prefer to make your main statement without interruption, Doctor?

Under Secretary Magill. It might be better. I am quite at your pleasure.

The Chairman. Without objection, that course will be pursued. You may proceed.

Under Secretary Magill. Mr. Chairman and members of the committee, the President stated in his Budget message of April 20, 1937, "that there is an immediate need for a careful survey of the present tax structure." The Treasury had begun its work upon this general survey early in 1937, working in cooperation with the experts of the Joint Committee on Internal Revenue Taxation. As the President stated in his Budget message, we expect to be able to present the detailed results of this survey to the appropriate committees of Congress next November. We want to present full information as to the operation and effect of the present tax system, the incidence of taxation upon taxpayers in the different income classes, and in general the effect of our present forms of taxes upon the social and economic life of the country.

It is our hope that on the basis of these data, the Congress may be enabled to formulate a new revenue law which will represent the best present thought as to a permanent fiscal system for the Federal Government. Changes in rates may then be made from time to time, but the citizens of the country can plan on the basis that the major forms of taxation thereby imposed will constitute the backbone of the Federal tax system.

If tax legislation is adopted along these lines, its effective date may not be earlier than January 1, 1938. It may not take effect in all its aspects until some later period. Consequently, if loopholes exist in our present system of taxes, through which considerable amounts of revenue are escaping, it is important that efforts to prevent further loss of revenue during the fiscal year should be made at this particular time.

The income-tax returns filed on March 15 produced a large increase in revenue over the previous year, but a somewhat less increase in revenue than the Treasury had anticipated. The Secretary of the Treasury has already given the reasons why we believe that our machinery for making estimates is satisfactory for the purpose. It seemed desirable, therefore, to undertake a quick, special investigation of the returns filed on March 15, in order to determine whether the somewhat disappointing revenues from the income tax
were due to methods of tax avoidance which had not been previously employed, or to an increased use of old methods.

Although the audit of returns for 1936 is now in process, it is obvious that not all of the returns could be audited in time to enable the Treasury to analyze them and to make recommendations to this session of Congress. Moreover, corporations asked for and received extensions of time for filing returns in much greater numbers this year than ever before, presumably because of the application to them of a new form of tax, the undistributed-profits tax adopted in 1936. We have therefore found it impossible to make any extensive study of the returns of large operating corporations up to this time, although we fully expect to complete a careful audit and analysis of these returns before the fall. Hence the investigation during the past 3 months was almost wholly confined to individual returns and the returns of personal holding companies.

We asked the revenue agents in charge in each of the 38 internal-revenue districts to submit full information of any new forms of tax avoidance which had come to their attention, and of any existing loopholes in the revenue laws which were causing a substantial loss of revenue. Particular attention was devoted to those major districts in which the increases in income reported had been significantly less than the average increase for the country as a whole. The cases thereby collected were carefully analyzed, and further investigations made when necessary.

We found that the major devices for tax avoidance which had been employed are not particularly new, but that all of them had been put to increased use. The cases which we examined fell into comparatively few categories. It ought to be possible, therefore, to frame legislation which will stop these particular gaps in the law, in advance of the general tax program of next fall. During the summer and fall the Treasury will of course continue its audit and investigation of tax returns and, if further tax avoidance devices become manifest, additional data will be presented to the appropriate committees.

We are prepared to present to the committee a number of examples of each of the forms of tax avoidance which the Secretary outlined in his letter to the President under date of May 29, 1937. The cases which we shall present are merely examples. There may be many or few additional instances of the various types of tax avoidance under discussion. However, the number of illustrations which can be presented is in general unimportant. One or two examples of incorporated yachts are adequate to present the problem in its general outlines and to suggest the need for corrective legislation. There are doubtless other insurance companies besides the one in the Bahamas organized by two New Yorkers which have been formed or availed of for the purpose of enabling American taxpayers to claim deductions for interest on so-called policy loans. The problem, however, is fully and specifically presented by the cases of the particular Bahamas insurance company which our investigators examined, and of the five or six Americans who employed it in an attempt to reduce their income taxes. We shall attempt to present enough cases of each form of tax avoidance to make the details of the scheme as clear as possible, so that any corrective legislation may have a sound, practical basis. And perhaps I should add here that
we have by no means completed our investigation. We are going on with the subject, first, as you will see, on this Bahamas corporation situation. We have gone into that rather fully, but our information as to Panama is comparatively incomplete, and we are advised that similar situations exist in Newfoundland and Prince Edward Island and Liechtenstein and various other places, which, of course, we have not been able to go into thoroughly in the time that we have had to do this.

The Treasury can, of course, present only the data which it has accumulated in its investigations; it cannot present the taxpayer's reasons or motives for employing the particular device. The settlor may have an explanation for organizing 64 trusts for the benefit of a wife and 8 children, when it would seem that not over 4 trusts would have served the purpose. The committee will doubtless wish to give the settlor an opportunity to make an explanation if he chooses to give it. The Treasury's interest is in the existence and use of a device whereby substantial revenue is being lost, not in the name of the men using it.

There has been some suggestion that the Treasury should have waited until next November before presenting information to Congress regarding the various schemes for tax avoidance which have come to our particular attention during the spring. It is our view, however, that the Treasury should not wait until a particular method of tax avoidance has become common before it acts to prevent it. A tax-avoidance device which appears plausible is apt to be employed more and more frequently, so that what was originally a trickle of lost revenue becomes a sizable stream.

Moreover, as a means of preventing tax-avoidance publicity may be almost as useful as legislation. The thought that perhaps some day they may have to make public acknowledgment that they employed an absurd tax-avoidance trick is a real deterrent to men who might otherwise use it. The design of most tax-avoidance devices is so obviously against the real substantive intent of the statute that if they are given publicity they are much less likely to be used in the future.

Take for an example the man who incorporated his yacht. His name and all the details will be given later in this hearing. When spread upon the public records this device achieves such a ludicrous aspect that it is extremely doubtful whether it will be used again. I should doubt very much whether any more yachts will be incorporated during 1937. Men do not like to get the reputation of being technically honest but entirely too clever in avoiding the payment of their debts or of their taxes.

The detailed publicity which will be given to the various types of tax avoidance which we are going to present to you during the course of this hearing is one of the most important weapons in our struggle to administer the tax laws fairly and efficiently. The real effects of publicity will be obtained from the fact that many of the tax-avoidance devices are inherently ridiculous, and the public will realize this when they are fully presented. Once this is generally recognized, it will inevitably follow that fantastic methods of tax avoidance will not longer be regarded as a mark of intelligent and careful husbanding of wealth. This will go a long way toward
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solving the problem so far as the ordinary man of wealth, anxious for public regard, is concerned.

The criminal and intentionally dishonest evasion of taxes is an entirely different problem. That cannot be solved by amendment of tax laws, but by effective enforcement of the laws we have, and by increasing the present inadequate personnel of the tax-administration arm of the Government.

I will now classify in general terms the types of tax avoidance which we believe require present consideration. Not all of them are yet in common use. Every one of them, however, presents a potential stumbling block in the administration of tax laws by our already overburdened staff. Those which are finally declared to be illegal will require long and expensive litigation to relegate them to the limbo of devices which fall on the side of tax evasion rather than avoidance.

First, foreign personal holding companies:
The outlines of this device are staple. A person whose income originates in this country chooses a nation whose taxes are low and which has no income tax at all. He forms a corporation. His income, which is derived in the United States, is paid to that corporation instead of to himself. Various excuses are given for this payment to a foreign corporation. The theory is that all transactions between the corporation and the individual are at arm's length. Thus, the money is transferred to foreign parts, where the tax administration has no investigating agents. It is almost impossible to trace what becomes of it when it reaches there.

However, assuming that everything which is done by the foreign corporation is honestly disclosed, we find this situation: The foreign corporation buys securities on the London, or even on the New York Exchange. It makes money on those securities and accumulates a surplus which, of course, cannot be reached directly in the United States, because the corporation does not do business here. Then, whenever the individual who formed the corporation needs money, he borrows it from the foreign corporation. Of course he has to pay interest on this money, but the interest is deductible from his income tax. In this way he is enabled to hold in the surplus of the foreign corporation any large profits on which the tax would be heavy and to keep his taxes down, even assuming the device of paying interest to the foreign corporation does not work.

This device is easy to see through in the case of an individual. If a group should use it, and there is no logical difficulty of its being used by a group, it would be a very complicated method of tax evasion to untangle. I would like to add there that if the individuals use it—and many of them do, as we will show you here—a series of these foreign corporations in a series of countries, one in Panama, one in Newfoundland, one in Bahamas, and so on, it is almost an impossibility to straighten out their affairs with the machinery that we have now.

As the Secretary has said, we do not know how prevalent this device is. The Bahama Islands are not a suitable place for the development of great corporate enterprises. The inhabitants are poverty stricken. There is a small trade in liquor. There are a few hotels for winter tourists. Yet suddenly long lists of impressive sounding corporations, financed by American capital, appear on the
directories of the local office buildings. I understand there are two
shacks on either side of the street down there—unfortunately I have
not been to Nassau—with a long list down the side of these houses
of these fine sounding corporations, which add up to have several
hundred million dollars of capital.

So much for the general description of foreign personal holding
corporations. The detailed cases which we will present later by other
witnesses will show that the device of the foreign holding company
has been used in the following ways:

1. By assignment of income to the foreign personal holding cor-
poration in order to avoid taxation of that income in the United
States.

2. By transfer of assets to the foreign personal holding corpo-
ration in order to have the income on the assets paid to a foreign corporation
and so reduce the personal tax of the sole stockholder.

3. By creating large interest deductions when the sole stockholder
of the personal holding corporation borrows back its capital or its
annual income and pays interest thereon.

4. By consummating abroad in the name of the foreign personal
holding corporation a profitable deal which the sole stockholder
negotiated in the United States.

5. By selling personally held securities to a foreign personal hold-
ing corporation to create a profit in order to offset personal realized
losses on securities and step up the cost basis of the securities sold.

6. By assigning royalty income to a foreign personal holding cor-
poration, thus avoiding taxes in the high surtax brackets.

There are several other methods by which foreign personal holding
corporations are used in order to avoid taxation, but the cases have
not been sufficiently investigated to warrant making any definite
statements concerning them as yet. These are sufficient to outline
the character and uses of the device.

Second, the device of foreign insurance companies:

This method is both artificial and amusing. An insurance agent
forms a foreign insurance company with only nominal assets. He
persuades a few men to buy policies for one million, three million,
and five million each on a single-premium basis. These premiums
are not actually paid, because the insurance company is not a real
insurance company. The fiction of payment of the premium is
accomplished in this way: The taxpayers give checks to the insur-
ance company for the amount of the single premium. Immediately
the insurance company gives them back checks for the amount of
the surrender value, which is nearly the same as the premium. This
is done under the guise of a loan. Since it is dressed up as a loan,
the taxpayer claims in his return that he is paying interest on it.
That interest he deducts on his income-tax return, and thereby
greatly reduces his net taxable income.

The net result of the entire transaction is this: By trading checks
with an alleged foreign insurance company, the taxpayer in effect
becomes a borrower from himself and claims a deduction for interest
on money loaned to himself. Later we will give you the details of
a case whereby, for a net outlay of $8,000, the taxpayer attempted
to gain a deduction in 1 year from gross income of about $140,000.
By means of these fictitious steps it becomes possible to make state-

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ments in a return which would otherwise be clear perjury. It is another ingenious and ludicrous device, but nevertheless one for which plausible contentions have been made in legal language by attorneys for the taxpayer.

Senator Harrison. How many of those are there?

Under Secretary Magill. This particular insurance company that we will describe to you has, I think, six policyholders. There are other cases of insurance companies in other jurisdictions, but we have not investigated them so fully.

Senator George. On the facts stated, isn't it a fraudulent transaction?

Under Secretary Magill. That is what we are now trying to determine. I may say that all six of these particular taxpayers here have offered to settle on the basis of the tax and interest. They have not yet offered us the fraud penalty.

Senator Harrison. Some of us are curious and want to get those names. You are going to give them to us?

Under Secretary Magill. Well, the plan of organization which we worked out here, and which, of course, is subject to your approval, was to give you an outline of the picture that we are going to present, and then start in with the first device, which is this Bahamas corporation, and go through them in complete detail. You will get all the names as soon as we sketch the picture.

Third, the device of domestic personal holding companies for creating surpluses and artificial deductions:

This is a difficult device to deal with so long as personal holding corporations have a legitimate place in our business organization. In its legitimate form an individual sets up a corporation to insulate himself against unlimited personal liability in the conduct of business. The corporation earns money, some of which may be retained for future business purposes. This legitimate use of the corporation then changes by gradual degrees to a purely fictitious use for purposes of tax avoidance. For example, an investor buying and selling securities, and collecting the income therefrom, may carry on his activities in the name of a corporation. The use of the corporate device has no business purpose, but permits him to accumulate a surplus and pay different and lower rates on his security income collected by the corporation than he would if he collected it individually.

The problem of the personal holding company has been one requiring the continuing attention of Congress since the first income-tax law in 1913. Specific statutory provisions have been enacted and amended since that date, but the loophole of accumulating corporate surplus for the purpose of evading surtaxes is still partly open. There are still a good many cases in which it is cheaper for an individual to accumulate income in a personal holding company, with no distribution at all, than to cause a distribution and pay surtaxes upon it.

The accumulation of a large surplus in a domestic holding company is only one of the tax avoidance methods for which this device is used. Others include cases where the personal holding corporation is utilized for the purpose of establishing artificial deductions for alleged losses, business expenses, interest paid, and so forth.

This will appear from a detailed examination of the particular cases using this device. A classification of the methods illustrated
by these cases shows the following to be the most frequently occurring ways in which it is used:

1. By not distributing income to stockholders, where individual surtaxes would be higher than the corporation's total taxes.

2. By spreading assets among several personal holding corporations, and thus avoiding the higher surtax rates on the income therefrom.

3. By establishing losses through sale or exchange of capital assets between one personal holding corporation and another, thereby taking advantage of any adverse change in market price without actually transferring the assets into other hands; and also taking advantage of the unlimited deduction of losses for surtax purposes.

4. By establishing losses for two personal holding corporations owned by different persons, who are associated in business, through simultaneous sale of the same kind and quantity of securities, or securities of like value, by corporation A to corporation B and vice versa.

5. Where the sole stockholder (or the family group of stockholders) of a personal holding corporation "borrows" all or the major part of its annual net income and pays interest thereon.

Fourth, the incorporation of yachts and country estates.

A rich man treats a hobby as a business. Whether it is an actual business or not becomes one of those vague questions of fact which are never settled. For example, courts have held in particular cases that losses on racing stables were losses incurred in transactions entered into for profit. Perhaps it is possible to make money on racing stables, and one can never be sure they are a hobby. The incorporation of a farm by a wealthy man is a closer question. The incorporation of a yacht, however, reaches the border of complete absurdity.

The difficulty of drawing the line is this: Many rich men's hobbies are businesses when conducted by smaller taxpayers or conducted in other ways. A farm conducted on a luxurious scale is not apt to make a profit under present conditions in America. The ordinary farmer knows that farming in this country cannot be conducted on such a scale. He feels that a joke is being made of the income-tax law. The moral effect is most unfortunate.

Fifth, the device of the creation of multiple trusts for relatives and dependents:

The principal object of this device is to split income between several taxable entities, all in the family. By splitting the family income a saving may be realized in several ways. First, exemptions may be taken for each trust. Second, surtaxes may be reduced to a minimum by preventing the income from reaching the higher brackets. There are two general classifications of the use of this device which may be described as follows:

1. By splitting among a number of trusts (created for the benefit of family members) a large block of stock which is about to be sold at a substantial profit and which is promptly sold by the respective trustees. I believe that was the background of the case which we will present of the man who organized the 64 trusts. He thereby split the profit 64 ways and consequently greatly reduced his tax. Without these trusts, the entire taxable profit from such sale would be taxed to the owning individual and would run into the higher surtax brackets. By effecting a split of the profit among a number of trusts qualifying as separate taxable entities, the taxpayer attempts to avoid the higher surtax rates.
2. By a transfer of substantial income-producing properties to a number of trusts created for the benefit of the transferor's wife and for the benefit of his minor children whose maintenance and education are adequately provided for by their parents without regard to such trusts. In the ordinary course of events, the entire income from these properties would be taxed to the parent and would run into the higher surtax brackets. By effecting a split of the income among several trusts, the taxpayer tries to escape the higher rates. That I believe was the case of the New Yorker with the 40 trusts.

Sixth, the device of husband and wife or father and children partnerships:
This is a variation of the multiple-trust device and achieves practically the same objectives. The device is usually brought into play:
By accepting into membership in the partnership the minor children of the principal partner or partners. The children are then alleged to be entitled to receive, or have conserved for them, their respective shares of the partnership's annual income. By this method the family income, which ordinarily would be taxed to the parent or parents as a unit, is split into a number of taxable units and the higher surtax rates are avoided.

Seventh, the device of the pension trust:
The pension trust is a new device. It is yet in the formative state. It nevertheless should be examined carefully to determine whether it represents a dangerous tendency in tax avoidance.
The Revenue Act of 1936 permitted corporations to deduct from income amounts paid into a pension fund. Wide latitude is permitted a corporation both as to the deduction of the regular payments as to each employee benefited and also as to the contributions to this fund to place it on a sound financial basis, with the result that the profits turned over to this fund are exempted from tax as to the corporation and are not taxed to the employee, until distributed to him in later years and in small amounts.

One corporation is attempting to place in effect a pension scheme whereby a favored few of the employees and principal stockholders will have placed in this fund to their credit each year, without it being taxed, an amount equal to approximately 60 percent of their annual salaries.

Numerous insurance representatives have called upon the Bureau attempting to secure advance rulings as to particular devices which they have in mind, and which they hope to "sell" to corporations if they can be assured that it will be a nontaxable scheme.

The foregoing classifications reflect the present uses of the more important tax-avoidance devices, as disclosed by the investigations which I have previously outlined for you. That, however, does not present the complete picture of the deficiencies which are inherent in the income-tax law as presently constituted.

As I have said earlier, what we have had in mind here is to present to you at this time merely some of the more glaring loopholes which we fear may give rise to a substantial loss of revenue, and which are already causing a substantial loss of revenue.

As I have said, some of these other defects will no doubt be presented to the appropriate committees for consideration next fall, after the present investigation has been prosecuted further. And I may say we are actively prosecuting it at present with a good many
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men. There are, however, three other patent inequalities, two of long standing, on which we already have full information. Needless, to say, these inequalities are productive not only of real hardships so far as the general taxpaying public is concerned, but also result in a serious loss of revenue.

Mr. Vinson. Mr. Chairman.

The Chairman. Mr. Vinson.

Mr. Vinson. Did not the pension trust come into the law in 1928?

Under Secretary Magill. I am not an expert on the pension trust, but it has been in the law for some time.

Mr. Vinson. Do you say the Revenue Act of 1936 permitted corporations to deduct from income amounts paid into a pension fund?

Under Secretary Magill. Simply for clarity we described the 1936 provisions. You will find, Mr. Vinson, that they were changed from time to time, year after year.

Mr. Vinson. My recollection is that the pension-trust provision came into the statute in the Revenue Act of 1928.

Under Secretary Magill. Oh, yes. I did not mean to give the impression that it was an invention of 1936. It was not. It had been in the law for some time before that.

One, percentage depletion:

The Secretary of the Treasury called attention to the desirability of amending the provisions of the law with respect to percentage depletion in his statement presented to a subcommittee of the Committee on Ways and Means in 1933. At that time he said:

Our experience shows that the percentage depletion rates set up in the law do not represent reasonable depletion rates in the case of the designated properties, but are much higher than the true depletion to which the taxpayer is fairly entitled. Moreover, these provisions enable a taxpayer to obtain annual depletion deductions, notwithstanding the fact that he has already recovered the full cost of the property. The deduction is, therefore, a pure subsidy to a special class of taxpayers. For this reason the Treasury recommends that these provisions be eliminated, in order to put all taxpayers upon the same footing.

The annual loss of revenue from this source is estimated at between fifty and one hundred million dollars. The Treasury strongly reaffirms its recommendation made in 1933.

Perhaps I should say again what I said earlier, that this is not a case of tax evasion or tax avoidance. The things for which these deductions are being taken are clearly permissible under the law as it stands. The question is whether or not they should not be eliminated in view of the reasons which the Secretary gave.

Two, the division of income between husband and wife in the eight community-property States.

The Secretary of the Treasury also called attention in 1933 to the desirability of eliminating the discrimination which now exists between spouses residing in community-property States and those resident in the other 40 States. In the community-property States each spouse may report one-half of the community income even though it was all earned by and was expended under the control of the husband. This situation not only results in a large loss of revenue to the United States, but also operates most inequitably as between spouses in community and those in noncommunity property States. If the law were amended to require that the spouse earning the income should report the entire amount, as is the case in the noncommunity-prop-
erty States there would be a large net increase in revenue to the Treasury.

Three, nonresident aliens.

The strengthening of the withholding provisions in the Revenue Act of 1930 will result in a considerable increase in revenue from alien taxpayers with income from American sources who have not previously filed returns in this country. We can give you the figures on that in due course. We have already got them, and there is a very large increase in revenue due to work which was done in 1930.

On the other hand, the 10-percent withholding rate is too low as applied to nonresident aliens with large American incomes, many of whom have previously been filing returns and paying American taxes at the higher rates applicable to American citizens with similar large incomes.

As you know there are a considerable number of American women with trusts in their favor set up in this country with American trustees, who are married to aliens and who are now living abroad, and who fall in the category of nonresident aliens. All or a very large part of their income is American income, and since it comes from American trusts the trusts have previously been filing returns. The 10-percent rate which is now applicable is usually less than the rates which are applicable to the larger ones of those trusts.

It is unlikely that Congress intended to reduce the tax of wealthy nonresident aliens below the levels which we require our own citizens to pay. Consequently, the committee may desire to recommend at this time a suitable change in the law which will preserve the present effective withholding provisions but will insure the taxation of wealthy aliens at rates corresponding to those applicable to Americans with similar incomes.

The Treasury is prepared to present examples of the defective operation of the law in each of these three respects.

One of the chief benefits of this investigation will be to make a record of information which will form a groundwork for intelligent and practical improvements in our present revenue laws. To stop effectively even the relatively limited number of loopholes that I have described is no easy matter; but we believe that suitable legislation can be formulated promptly on the basis of the data which will be presented during the course of these hearings. I am hopeful that this investigation will have the beneficial effect of eliminating for the future the major leaks in our revenue system which will be described in detail to you during the next few days by the officials of the Department who are familiar with them.

As I said at the beginning of the statement, subject to your approval, what we had in mind as to the orderly way to proceed is this: These investigations into these different points which I have mentioned have had to be conducted by a variety of people. As you can see we were working under severe limitations of time. We were anxious that if there were serious loopholes the Congress should have a chance to consider them and if necessary make amendments at this session, in order that there should not be this serious loss of revenue during the current fiscal year. Hence we would like to propose to you that on each of these various points we bring up one of the officials of the Department and his staff who have actually made the
investigations and who are in a position to present the facts to you most effectively.

The CHAIRMAN. In that connection, Dr. Magill, you speak of the investigations which you are conducting and have conducted. These investigations are still in progress, as I understand.

Under Secretary MAGILL. That is true.

The CHAIRMAN. Have you a sufficient staff or personnel to adequately do this work?

Under Secretary MAGILL. Frankly, it has been difficult to present to you such information as I thought you would like at this time. You see it is only 3 months since the March returns were filed, and we worked at it as intensively as we knew how, but we could not let the work of auditing the 6,000,000 returns go by the boards for the sake of this work; but we do have a special staff, under Mr. Irey as head, investigating these matters, and another staff under Mr. Russell as head going into them also.

Senator Harrison. Has it been necessary in some instances to send employees of the Treasury Department into foreign countries?

Under Secretary MAGILL. That is true, of course we could not do much, but you may want us to do more. What we have done on that is to send agents to the Bahamas and also to Panama to make pretty thorough studies. The difficulties of getting information will be described to you. Obviously the persons in those islands are profiting very much by the influx of American corporations and capital and so forth, consequently no one wants to tell you anything.

So far as the individual returns are concerned, no American who employs this device is at all apt to disclose to you the fact that he owns stock in one of these companies. However, we have pretty elaborate information on these two places which we have examined.

Senator Harrison. Have the foreign governments cooperated with the Treasury Department in obtaining the information it desires?

Under Secretary MAGILL. Some do and some do not. Some are completely uncooperative. As a rule, even the more cooperative ones put a great many obstacles in your way. You have to go about getting the information very indirectly. For instance, as a rule the Treasury cannot get it; it must be obtained through diplomatic channels.

The CHAIRMAN. Are you ready now, Dr. Magill, to take up individual cases under the different headings or topics and explain what you have discovered in these investigations?

Under Secretary MAGILL. Yes, sir; we are. It has gone somewhat faster than we anticipated, as a matter of fact. We have expected to present these things in the order in which I have them, and if it is agreeable to you I should like to put the first witness on tomorrow.

Senator Harrison. Mr. Chairman.

The CHAIRMAN. Senator Harrison.

Senator Harrison. I desire to second the suggestion of the Treasury Department, and since we have proceeded now nearly 2 hours and it is necessary for the Senators to be on the Senate floor immediately, I move that we take an adjournment until tomorrow morning at 10 o'clock.

(The motion was agreed to; accordingly at 11:45 a.m., the committee adjourned until tomorrow, Friday, June 18, 1937, at 10 a.m.)
The joint committee met, pursuant to adjournment, in the hearing room of the Committee on Ways and Means in the New House Office Building at 10 a.m., Hon. Robert L. Doughton presiding.

The CHAIRMAN. The committee will be in order, please. Dr. Magill, who is your next witness? Are you ready to proceed?

Under Secretary Magill. We are; yes, sir. As we told you yesterday, it is our intention this morning to put on evidence with respect to the use of foreign corporations, particularly in the Bahamas, for purposes of avoiding American taxes, and we want to go into a number of these individual cases of American taxpayers who have resorted to this device, by way of illustration of the tax avoidance which can be accomplished by this method. It seemed best that Mr. Irey, who is head of the Intelligence Service for the Bureau, should present this point, in view of the fact that his agents made the investigation and is thoroughly familiar with the facts. I am here, and Mr. Kent and the Commissioner are here to answer any questions which you may have as to any legal details or other questions that may be beyond Mr. Irey's immediate knowledge.

STATEMENT OF ELMER L. IREY, CHIEF OF THE INTELLIGENCE UNIT, BUREAU OF INTERNAL REVENUE, TREASURY DEPARTMENT

The CHAIRMAN. Mr. Irey, will you give the stenographer your name, address, and the capacity in which you appear before the committee?

Mr. IREY. Elmer L. Irey; Chief, Intelligence Unit, Bureau of Internal Revenue, Treasury Department.

The CHAIRMAN. I understand, Mr. Irey, that you have been designated by the Secretary of the Treasury to give the committee information which the Treasury Department has on methods of tax evasion and avoidance, especially, and particularly by the organization of foreign personal holding companies. Will you please proceed to give the committee the information you have on that or any other subject you have to discuss?

Mr. IREY. Thank you, sir. Mr. Chairman and gentlemen, as Mr. Magill has pointed out, one of the most dangerous methods of tax avoidance consists in the use by American citizens of corporations formed in countries where taxes are low. Some of these countries
make a sort of ambulance-chasing racket out of the possibility of attracting wealthy American taxpayers. The scheme has sufficient plausibility so that no one can be sure at this time whether it is or is not a legal method of tax avoidance under our present law. However, it has an important effect in the avoidance of tax and the consequent loss of revenue. It permits the taxpayer to transfer his income to countries where tax investigation by American Treasury officials is almost impossible.

The Chairman. Just one moment, Mr. Irey. Pardon me. The Chair neglected to ask if you preferred to make your statement without interruption.

Mr. Irey. I would prefer, Mr. Chairman, if I might conclude the statement, and then I will be glad to answer any questions that might be asked.

The Chairman. You may conclude your main statement, after which you will yield for questions.

Under Secretary Magill. I think if the committee wants to ask Mr. Irey questions with respect to these particular cases as they come along, it might be well to do that.

Mr. Irey. Oh, yes.

Under Secretary Magill. Rather than wait, and that will be entirely agreeable.

The Chairman. After he finishes with each separate one?

Under Secretary Magill. Yes; after he gets through with each separate one.

Mr. Treadway. As I understand it, he is making a general statement now?

Under Secretary Magill. Yes; he is going to make a general statement.

Mr. Treadway. And that is the part that he would like to not be interrupted upon?

Under Secretary Magill. Yes.

Mr. Irey. And just in the latter part of the statement or about the middle of the statement will come names and typical cases and deductions and you gentlemen may wish to ask questions at that time.

Mr. Treadway. We favor your using as much lung power as you have available.

Mr. Irey. Very good, Mr. Treadway. Thank you.

The cases which we will present to you were uncovered only after considerable expense and under great difficulties. Such have been these difficulties that I am inclined to say that adequate enforcement of the tax laws is impossible so long as this loophole exists.

I am unable to say how much money is lost by the Government through this device. A conservative estimate is that 585 personal holding companies have been formed by Americans in the following places: Bahama Islands, 94; Newfoundland, 202; Panama, 40; and Prince Edward Island, 243.

An examination of the financial conditions in these places shows no justification whatever for such extensive business organization.

In order to make clear the significance of the cases which are to follow, I must do two things: First, I must give a very brief survey of the situation in all the different countries where this device is used. Second, I must show you in detail the handicap under which
the Bureau must work in collecting information in these countries and which makes efficient investigation and collection of taxes impossible.

I will take up, first, the situation in the Bahama Islands. The use of foreign corporations as a tax-avoidance method dates from 1935. Prior to that time the Bahama Islands were not financial centers for any considerable amount of American wealth. The population consists of about 60,000 Negroes, who work for small wages, and several thousand whites, who control the limited business of the island. During the prohibition era in the United States a great deal of liquor was shipped from these islands to this country. However, since the repeal of prohibition and prior to 1935, the business of the islands has consisted almost entirely in gathering sponges, fishing, and catering to tourists.

Beginning with 1935 corporations began to be formed in the islands in astonishing numbers. Some of them, of course, are for legitimate business. However, there is frequently no way of checking the precise character of the business of these corporations because of the fact that the directors and stockholders are dummies. The law requires that the real ownership of the corporation be disclosed within 1 year. This provision, however, has not been of any advantage to us as yet for two reasons. In the first place, for most of the corporations the year has not yet elapsed, and, in the second place, there are not sufficient facilities in the colonial office of the islands to take care of the recent rush of business. They are far behind in the filing of these registrations.

While we do not know in the case of each individual corporation whether it has been formed for a business or a tax-avoidance purpose, the economic conditions in the islands clearly indicate that a great majority must have been formed because of attempts to avoid the effects of taxation.

This is further corroborated by the experience of our agent, Mr. Brenner, who investigated the situation in the islands. He remarks the existence of a thriving business among attorneys whose chief occupation seems to be the formation of such companies. Those corporations have no regular places of business, and, therefore, use for their headquarters merely the office of the attorney who incorporates them. There is a peculiar law in the islands requiring the name of the corporation to be posted on the outside of the building in which it maintains its resident office. The building occupied by Mr. Kenneth Solomon, one of the most prominent attorneys on the islands—

Mr. Cooper. Mr. Chairman.

The Chairman. Mr. Cooper.

Mr. Cooper. Pardon the interruption, but I suggest that when you give a name you give it not only distinctly but spell it out.

Mr. Irey. Very good, sir.

Mr. Cooper. So that there may be no confusion about the name used.

Mr. Irey. That is Mr. Kenneth Solomon, one of the most prominent attorneys on the islands, who has been instrumental in the organization of perhaps 50 percent of the companies, is literally plastered from foundation to roof with these corporate names. The name
plates are about 30 inches long and 8 inches wide, and the building is so covered with them as to constitute one of the major curiosities of Nassau. We are having a picture made of some of these buildings, and we propose submitting that to the committee later on for their information, in order that they might understand just what a curiosity this is on Bay Road in Nassau.

Mr. Treadway. Mr. Chairman.

The CHAIRMAN. Mr. Treadway.

Mr. TREADWAY. Do I understand Mr. Solomon is a resident of Nassau?

Mr. IREY. That is right. He is a resident lawyer there.

Mr. TREADWAY. I believe you said you did not wish to be interrupted?

Mr. IREY. Mr. Solomon——

Mr. TREADWAY. Mr. Magill said you could be interrogated as you mentioned the names.

Mr. IREY. It is perfectly all right.

Mr. TREADWAY. I was wondering as to the nationality of this gentleman, whether he had ever been an American citizen.

Mr. IREY. So far as I know, he has never been an American citizen. He is a British subject and a resident of Nassau.

Mr. TREADWAY. And did not come there recently, so far as your records show?

Mr. IREY. Mr. Brenner, he has been there for many years?

Mr. BRENNER. Oh, yes; he has been there a long time. Mr. Solomon has been a resident of the islands and has lived there for many years. I understand his family and his great-grandparents were colonizers of the island, so he is a native of Nassau.

Mr. TREADWAY. Thank you.

Mr. IREY. This method of avoiding taxes has become so popular and has grown so rapidly that it is one of the outstanding topics of conversation and comment in the islands.

Mr. John Herbert Anderson, a Nassau accountant, advises that the formation of personal holding corporations in the Bahama Islands has created a shortage of bank-vault space there. A company called the Bahamas General Trust Co., Ltd., has been formed with a capitalization of $100,000 to erect a building which will contain large-sized vaults for the storage of the securities which are being transferred there.

In the Bahama News of March 11 in an article entitled "Let's Pay Our Share", we find this observation——

Mr. VINSON. What year?

Mr. IREY. Of the current year, March 11, 1937.

Why should not the rich people who are coming down here, building homes, setting up enterprises, escaping taxation in their own countries, help John Bull to carry the burden that he is carrying—and the load is going to be greater to make the seas safe for the property boom in the Bahamas? We ask the Americans who are using these islands as "the Promised Land" to band together and help the old country make the British Empire a place safe for Americans to live in.

On June 1 of this year, just within the past couple of weeks, the Nassau Guardian published an editorial which started with the following paragraph:
The question of tax evasion in the United States has now been definitely brought into the open by President Roosevelt who, according to a report published in another column “accused a group of rich Americans of immorally and unethically evading payment of millions of dollars in income taxes.” The position of the Bahamians in this matter is fundamentally much the same as the one they occupied in the days of prohibition. There was nothing in our laws to prevent Bahamians from selling spirits to Americans outside of American waters at that time and there is nothing now to prevent Americans from organizing as many companies here as they like so long as they meet our requirements. Of course in the former case our customers were law breakers while now we are only dealing with evaders of the law but the moral difference could hardly be located with a microscope.

The editor then went on to discuss whether the Bahama Islands had any additional responsibility on account of this condition. He came to the following very sensible conclusion:

In the last analysis the whole problem is for the United States to make its laws proof against evasion or nearer to that ideal than they have yet been able to come and that is evidently the next move being planned by the present administration. It will be strange indeed if these new laws do not affect the revenue of the Bahamas from registration fees.

In other words, the Bahama Islands quite justifiably feel that if the United States chooses to permit this kind of tax avoidance it is not their moral responsibility. Even the Bahamas editor expects, however, that the Congress will act to stop this loophole, which is rapidly becoming notorious.

In 1935 there were 41 personal holding companies formed. In 1936 there were 51. In the first 4 months of 1937 there were approximately 30 companies, making a total of personal holding companies for foreigners incorporated in the Bahama Islands of 122 in a little more than 2 years.

Mr. Treadway. Pardon me; are you reading still from the press? Where did your quotation from the newspaper cease?

Mr. Irey. Pardon me?

Mr. Treadway. You quoted the paper, but you did not say where the quotation stopped.

Mr. Irey. When I commented on the quotation from the paper, wherein I said that, “in other words, the Bahama Islands quite justifiably feel that if the United States chooses to permit”—

Mr. Treadway. That is the beginning of your comment?

Mr. Irey. That is the beginning of my comment; yes, sir. I beg your pardon.

Some of these corporations were formed by Americans. Others were set up by Canadians, but the personal holding company formed by Canadians can be used as a device for American tax avoidance as readily as those formed by Americans. Under Canadian laws personal holding companies formed by Canadians cannot be used by them for tax-avoidance purposes.

Compared with this growth of corporations in the last 2 years, we find that in the 45 years from 1880 to 1924 only 93 corporations were formed for any purpose, business or otherwise, and that during the next 10 years new corporations averaged 20 a year. In our computation we have left out the 60 business corporations formed since the beginning of 1935.

Mr. Brenner, our special agent, learned in the islands that it is customary for the attorneys forming these corporations to meet
wealthy Americans on winter vacations and if the opportunity presents itself to explain the advantages of Bahamas corporations for avoiding American taxes.

Mr. Magill has already described in broad outline how this device operates and I will, therefore, not repeat it here. It will be illustrated in detail by the individual cases which will follow.

Among the personal holding corporations formed in the Bahamas by Americans are the following: Southern Securities, Ltd.; Foley Securities Co.


We will file with the committee a complete list—

Mr. Treadway. Pardon me; what does that word “limited” refer to?

Mr. Irey. That is used in the British Isles in place of “incorporated in our country. We will file with the committee a complete list of all the companies understood to have been formed by Americans in the last few years.

(The list of Bahamas corporations referred to, as submitted by Mr. Irey, was marked “Committee Exhibit No. 1”, and will be found in the record at the end of today’s proceedings, p. 72.)

Mr. Cooper. Pardon me just a moment, Mr. Chairman. What did you say that document was?

Mr. Irey. That is a complete list of the companies formed in the Bahamas in the last 2 years and 4 months. I have given you some samples of them, and I am giving you a complete list there.

Mr. Cooper. I did not quite understand the companies that you named. Were they formed by one individual or more?

Mr. Irey. No; they were formed by different individuals. They are simply samples of the companies which have been formed in the Bahamas.

Mr. Cooper. Isn’t it your purpose to give the names of individuals who formed those companies?

Mr. Irey. Yes, sir; to some extent. Whenever we have that information, it is our purpose to give it. I will explain later the difficulty of securing information indicating those names.

Mr. Vinson. This is the 122 personal holding companies that have been formed within the period you state?

Mr. Irey. Yes.

Senator Harrison. Does that list include the 40 concerns that you said were business concerns?

Mr. Irey. No; it does not. That is not included in this.

Under Secretary Magill. Perhaps I might say at this time, this list which we are filing with the committee is a very long list, as Mr. Irey has said, of one hundred and twenty-five-odd corporations, with the stockholders registered in the Bahamas. He is going to speak of several particular cases now. If at the end of that time, you want him to read to the gathering all of these companies and all their stockholders, of course, that can be done.

Mr. Treadway. Just a moment, Mr. Magill. Does the list that you have filed give names of American citizens who are stockholders?
Under Secretary Magill. So far as they appear from the Bahamas record. The information which is contained in that list was all secured by the agent, Mr. Brenner, in a trip to the Bahama Islands, getting this information from the Bahamas stock record; and, as Mr. Irey said, in not all cases do the names of stockholders completely appear. But we have pretty good information as to a good many of them. He is going to give a number of the more striking examples now.

Senator Walsh. Are the names fictitious in some instances?

Under Secretary Magill. I don't think they are fictitious. We don't know they are fictitious. They are dummies. In some cases the real stockholder is there disclosed; in some cases he is not.

Senator Walsh. So, by reading the name of one of these limited organizations, it is impossible to tell whether they are genuine Americans or not?

Under Secretary Magill. That is true; yes. The cases which Mr. Irey is going into are cases which were verified as far as is humanly possible, because—

Senator Walsh. Is the method by which these organizations are formed the same in all of these lists?

Under Secretary Magill. I would think so; yes, sir.

Senator Walsh. And they all deal with securities?

Under Secretary Magill. Yes. As he said, in going over the records, we tried to take out any company which seemed to be formed for a legitimate business purpose and only put in the American personal holding companies.

Senator Harrison. You said something about dummies; under the law they have a right to designate a dummy for a year. What was it you said about that?

Mr. Irey. They can designate dummies, but the law requires that within 1 year after the creation of the company they must file a statement showing the true names of the owners or stockholders.

Senator Harrison. And some of the companies do not resort to the dummy idea, others do; is that right?

Mr. Irey. That is true. Philip DeRonde is a native-born American citizen, who was formerly president of the Hibernia Trust Co. of New York, director of the Empire Trust Co. of New York, chairman of the board of Phoenix Securities Corporation of New York, and also engaged in financing and operating steamships. He now owes the United States Government $33,000 for unpaid taxes and interest.

Mr. Vinson. I didn't catch that, please.

Mr. Irey. He now owes the United States Government $33,000 for unpaid taxes and interest. On January 7 last he made a sworn statement that he was without any substantial funds and that he was seeking to settle his liability of $33,000 by offering a compromise of $1,700, to be paid in installments. We learned that on January 8, 1937, 1 day before he submitted his offer in compromise, he received $250,000 from the General Investment Co., an American corporation for which he had acted as agent in the sale of the subway in Buenos Aires, Argentina. He instructed the General Investment Co. to pay this $250,000 to a Bahama corporation named Phillip DeRonde, Ltd., instead of to him. The records of the registrar in the Bahamas show that this corporation had been formed just 3 months before this
transaction, apparently in anticipation of the completion of contract of sale and his receipt of this large commission.

In a hearing before the Securities and Exchange Commission on May 7, 1937, it appeared that the $250,000 was received from the General Investment Co. by Mr. DeRonde in person in the form of a check for $100,000 and currency in the amount of $150,000.

The testimony of DeRonde before this Commission continued as follows:

Question. Now, how was the check to be drawn in the first instance, in whose name?
Answer. In my corporation.

Question. What is the name of the corporation?
Answer. Philip DeRonde, Ltd.

Question. Where was that organized?
Answer. In Nassau.

Question. Are you an officer of the corporation?
Answer. I am.

Question. Are you a director?
Answer. Yes, sir.

Question. Are you a stockholder?
Answer. No.

Question. In this corporation which bears your name, you are just an officer and director and don't own a single share of stock of that corporation?
Answer. Correct.

Question. The check for $100,000, what did you do with that?
Answer. Took it to Buenos Aires.

Question. And deposited where?
Answer. In Buenos Aires in the corporate name. I delivered it to the corporation.

Question. What did you do with the $150,000 cash?
Answer. I delivered that also to the corporation.

Question. Did you deposit it in the bank?
Answer. Sir, I can only say I delivered it to this corporation, which is a foreign corporation.

Question. I understand that but I have not only legal difficulties but natural difficulties. I can't visualize you walking up to Philip DeRonde, Ltd., and handing the money to Philip DeRonde, Ltd. You turned that money over to somebody.
Answer. I turned it over to the corporation who disposed of it in various manners.

Question. As far as the payment of $250,000 was concerned, you carried on all the negotiations?
Answer. That is right.

Question. You were the one hired by Mr. Warrener?
Answer. That is right.

Question. You were the one that did the work and you were the one entitled to the compensation. Is that so?
Answer. My corporation was.

Question. You did the work?
Answer. Yes, sir.

Question. Who are the stockholders in Philip DeRonde, Ltd.?
Answer. They constitute a group of Argentinean, Paraguayan, and English friends of mine.

Question. What are their names?
Answer. I must decline even if I knew at this time.

Question. Did you have an agreement with Philip DeRonde, Ltd., that your compensation was to be out of this $250,000?
Answer. No; because this firm of Philip DeRonde, Ltd., was not organized for that sole purpose. It is actively engaged in many lines of business and has been in spite of its organization in 1936.

That is the conclusion of the quotation from the hearing before the Securities and Exchange Commission.

Now, then, the ultimate result of this manipulation was that Mr. Philip DeRonde took out of the United States $250,000, of which
$33,000 belonged to the United States Government and the whole of it was subject to the United States income taxes as his income. This transaction took place on January 7, 1937, and Mr. DeRonde may still think it wise to file an income-tax return and report this income for tax purposes. This case clearly illustrates how a foreign corporation may be used by assigning to it income belonging to an American taxpayer, who thus tries to avoid paying income taxes thereon to the United States.

This DeRonde case illustrates a tax-avoidance device of doubtful legality, to say the least. Many of the uses of this tax-avoidance plan, however, are probably legal.

We cite the case of Jules S. Bache——

Senator Harrison. Before you get away from Mr. DeRonde——

The CHAIRMAN. Senator Harrison.

Senator Harrison. Has he made any offer to settle this account?

Mr. Irey. Not since he made that offer of $1,700 in compromise of the $33,000 liability, and at that time he made a sworn statement that he was without funds and offered to pay the $1,700 in installments.

Mr. Vinson. Mr. Chairman.

The CHAIRMAN. Mr. Vinson.

Mr. Vinson. What was the date upon which he received the $250,000?

Mr. Irey. January 6, 1937.

Mr. Vinson. And what was the date upon which he testified he had no money?

Mr. Irey. January 7, the following day.

Mr. Vinson. And he made the statement under oath?

Mr. Irey. That is correct.

Mr. Vinson. On January 7, the day after he had collected the $250,000?

Mr. Irey. After he had completed that transaction; yes, sir.

The CHAIRMAN. You say he has offered $1,700 in settlement of the $33,000 that he owes the Government?

Mr. Irey. That is right.

The CHAIRMAN. Does he dispute that? Is that according to his return, or is it an assessment of $33,000?

Mr. Irey. We are assessing that $33,000.

The CHAIRMAN. Did he make any returns at all?

Mr. Irey. He filed returns.

The CHAIRMAN. What did the return show he owed the Government?

Under Secretary Magill. As I understand it, Mr. Chairman, the $33,000 is shown to be due on returns which he has filed for prior years.

The CHAIRMAN. That is what I was trying to get.

Under Secretary Magill. Yes. Now he seeks to compromise that liability shown to be due in that way by paying $1,700 and by swearing to the Treasury that he does not have any money, when the day before he got the quarter of a million dollars, most of it in cash.

The CHAIRMAN. On the ground of inability to pay?

Under Secretary Magill. That is right.

The CHAIRMAN. And not that the assessment was unjust?

Under Secretary Magill. That is right.
Mr. Vinson. When was this money taken physically to Buenos Aires?

Under Secretary Magill. So far as I know, we don't know exactly when he did do it. You can see from his testimony here he was completely evasive. So that you would not get anything by asking him as to when he took it there.

Senator Walsh. Mr. Chairman.
The CHAIRMAN. Senator Walsh.

Senator Walsh. I assume the Legal Division of the Bureau of Internal Revenue in the Treasury acted on these facts, as to whether this was an evasion or a criminal fraud. What ruling did you make on those facts?

Under Secretary Magill. Well, as to this quarter of a million, I think the case has not been submitted to the Legal Department, because the payment was made only in the beginning of this year, as you see.

Senator Walsh. Have any inquiries or steps been taken to see if these facts which are before you constitute a fraud or a crime?

Under Secretary Magill. That is what we are doing now.

Senator Walsh. In other channels than through this committee, I assume?

Under Secretary Magill. Yes.

Mr. Vinson. This money was not this year?

Mr. Irey. That is this year. It is a 1937 transaction.

Mr. Vinson. On 1937 income. Consequently, the tax return is not due until——

Mr. Irey. March 1938.

Mr. Vinson. March 1938. Where did you get your assessment?

Mr. Irey. The assessment was on prior years. We point that out simply to show that he owed the Government $33,000.

Mr. Vinson. I caught that figure first; then I got around to the point where I thought I had evidently misunderstood it. Are there two $33,000's?

Mr. Irey. No; there is the one $33,000 which he owed the Government, for which he offered $1,700 in settlement.

Mr. Vinson. That was for taxes prior to January 1, 1937?

Mr. Irey. That is true.

Mr. Vinson. And then, of course, the tax liability upon this $250,000 transaction is for the taxable year of 1937?

Mr. Irey. That is true.

Mr. Cooper. Mr. Chairman.
The CHAIRMAN. Mr. Cooper.

Mr. Cooper. Of course, that will have to be shown in his tax return filed after the first of next year?

Mr. Irey. That is correct.

Mr. Cooper. But the whole point in presenting this evidence, as I comprehend it, is to show that he testified on one day that he did not have any money, and the fact is that he had received a quarter of a million dollars the day before?

Mr. Irey. That is correct.

Mr. Vinson. Mr. Chairman.
The CHAIRMAN. Mr. Vinson.
Mr. Vinson. Was there any consideration given to declaring his taxable year terminated and making a jeopardy assessment on this $250,000?

Mr. Trey. That has not been done.

Under Secretary Magill. Of course, the case is now in the hands of the Legal Division, with a view to such prosecution as we may be able to make. It would appear that the man did make a false and fraudulent offer in compromise.

Senator Watson. Was that sworn to?

Under Secretary Magill. Oh, yes; those are sworn to.

Mr. Vinson. Well, but, Dr. Magill, that refers to old taxes.

Under Secretary Magill. That is right.

Mr. Vinson. That refers to a liability that has been fixed. Now, in speaking of the income tax upon that $250,000, which is income for this year, as I understand it, it would be within your power to make a jeopardy assessment upon that income; is that correct?

Under Secretary Magill. I think you are right. Of course, the difficulty here is, as explained in the DeRonde story, that the money is down in the Bahamas in this company.

Mr. Vinson. Now it seems to me that you might make a jeopardy assessment.

Under Secretary Magill. I think that is an excellent suggestion.

Mr. Vinson. But let him have a few more months before the ordinary taxable year terminates and he will just have that much more time to get away with it.

Senator Harrison. Mr. Chairman.

The Chairman. Senator Harrison.

Senator Harrison. I would like to make the observation that I think this is one of those cases where Mr. DeRonde ought to come before the committee, and ought to be subpoenaed before the committee if he does not come willingly so that we may ascertain who these persons are in this DeRonde Corporation, Ltd., whether they are his employees who acted as dummies, and to ascertain the reason for forming this corporation at Nassau.

The Chairman. In that connection, Senator, I suggest he first be invited, and in case he does not come, he be subpoenaed.

Senator Harrison. Yes; I think he might be asked to come up in executive session first. I merely make the observation that he might be invited first, and if he does not come, then we ought to subpoena him. We need not take any action at this time.

Mr. Vinson. Now, Mr. Chairman, it just occurs to me that this is the character of a case where a subpoena ought to issue. While you are inviting him to appear here, he might go to the Bahamas. You cannot get process on him there.

The Chairman. I think we might deal with this case and other similar cases in executive session. It will not take so much time and space for the stenographer.

Mr. Trey. Next I am citing the case of Mr. Jules S. Bache.

Senator George. Mr. Chairman—

The Chairman. Senator George.

Senator George. Is the Treasury making an investigation of that alleged corporation or limited company?
Mr. Irey. Well, we made such inquiry in the Bahamas as we were able to make in the brief visit that the agent made to the Bahamas in securing all of this information.

Under Secretary MacNiel. Senator, as I think you will see when we go a little further, or perhaps you see now, it is practically impossible to find out about any of these cases except by putting the particular individual under oath and making him tell the story. Now, you could go down to the Bahamas and you would find Philip DeRonde, Ltd., with a couple of Paraguayans as stockholders. Well, where are you? You don't know where the owners are. They may be in New York; they may be in the Bahamas; they may be in Paraguay. If you get DeRonde on the stand you can say, "How about that $250,000 fee? Where did it go?" And, "How about Philip DeRonde, Ltd.?"

Senator George. Yes. I just merely made the inquiry, though, as to whether or not there was a corporation down there.

Under Secretary MacNiel. There is, I think, a corporation, so far as formal incorporation is concerned.

Senator George. You have no information, though, except what he disclosed before the Securities and Exchange Commission?

Under Secretary MacNiel. Right.

Senator George. As to the nature and the character of the business?

Under Secretary MacNiel. Yes, sir.

Senator Harrison. And they were unable to ascertain to whom he paid this $150,000 in currency?

Under Secretary MacNiel. That is true; yes, sir.

Senator Harrison. You only ascertained that the check was put on deposit in a bank in Buenos Aires?

Under Secretary MacNiel. That is right; yes, sir.

Mr. Irey. Shall I proceed, Mr. Chairman?

The Chairman. You may proceed.

Mr. Treadway. May I ask one question?

The Chairman. Mr. Treadway.

Mr. Treadway. Have you the tax returns of this Mr. DeRonde that he made under which the $33,000 assessment lies for which he offered to compromise for $1,700?

Mr. Irey. I haven't that with me.

Mr. Treadway. Those returns are, of course, in the hands of the Internal Revenue Bureau?

Mr. Irey. They are available; yes, sir.

Mr. Treadway. They would be available to this committee?

Mr. Irey. That is correct.

Mr. Treadway. They would show the nature of his business under which he ran up this debt to the Government of $33,000?

Mr. Irey. That is correct.

Mr. Treadway. What was the nature of his business?

Mr. Irey. I have not reviewed those returns.

Mr. Treadway. Beg pardon?

Mr. Irey. I have not reviewed those returns, Mr. Treadway. I was concerned with this later problem and did not go into the old tax liability the one under which the $33,000 is due.

Under Secretary MacNiel. As you see, Mr. Treadway, since he made this offer in compromise I take it he is essentially admitting he owes the money, and the question is simply how much he is going to pay.
TAX EVASION AND AVOIDANCE

His business, as I understand it, is financing, but just how this particular $33,000 tax liability arose we will have to give to you later, if you want it. We can bring the returns here and you can see the whole story.

Mr. TREADWAY. I should think it would be part of this record, advantageously.

Under Secretary MAGILL. I think so. If you want it, we will give it to you.

Mr. TREADWAY. I think it would be desirable, Mr. Chairman, to have them available.

Mr. VINSON. I don't see where it illustrates anything. That amount has become fixed. There is no question involved as to the amount of taxes due for former years, is there?

Mr. INREY. No; there is no question as to the amount, so far as we are concerned.

Mr. TREADWAY. So I make the request that those returns be available to the committee.

The CHAIRMAN. Mr. Treadway makes the request that those returns referred to be made available to the committee. Is there objection?

Mr. COOPER. Well, Mr. Chairman, I rather concur in the view expressed here. The particular item to which attention has been directed here is not disclosed by the return that is now on file. This item will have to be shown in the next return, and I am unable to see how any advantage will be served by having an investigation of that return here, because it is simply a question of back taxes that have been assessed against him.

Mr. TREADWAY. Well, I think, Mr. Chairman——

Senator Harrison. Mr. Chairman——

The CHAIRMAN. Senator Harrison.

Senator Harrison. I do not understand that Mr. Treadway has asked for an investigation.

Mr. TREADWAY. No, sir.

Senator Harrison. But that the returns merely be made available to the committee, I can see no harm in the Treasury Department having them ready to make available to the committee if the committee wants to look into them. I don't think they have any bearing on this particular case to which he is referring, but I think it is all right for any of these tax returns to be available to the committee.

The CHAIRMAN. The Chair sees no objection to that unless there is objection raised to the request that the returns be made available for the inspection of the committee or any member of the committee.

Senator Walsh. Mr. Chairman——

The CHAIRMAN. Senator Walsh.

Senator Walsh. Dr. Magill, will you inform the committee whether or not the Treasury Department under existing law can call in a taxpayer and put him under oath and examine him in regard to his return? Don't you have to first go to court for an order?

Under Secretary MAGILL. I am not fully advised on that. Can you give it, Mr. Helvering?

Commissioner HELVERING. We have full authority to call witnesses under the law.

Senator Walsh. Any witnesses relating to a tax return?

Commissioner HELVERING. Yes.
TAX EVASION AND AVOIDANCE

Under Secretary MACILL. Can you examine them under oath?
Commissioner HELVERING. Yes; section 618 is the authority.

Mr. TREY. I referred to the case of Jules S. Bache, a prominent capitalist, who has been connected for a long time with many financial concerns. As will appear from the details of this case, Mr. Bache apparently acted with an honest conviction that he was within his legal rights in utilizing foreign corporations as he did.

Senator HARRISON. In New York?
Mr. TREY. In New York City; yes, sir.

We, therefore, cite the case not in criticism of Mr. Bache but to illustrate the fact that if the law is as Mr. Bache interpreted it the present situation regarding foreign personal holding companies offers great inducements to the wealthy taxpayers for tax savings.

Mr. Bache organized two Canadian corporations, through which he traded extensively in stocks and bonds. In 1930 he transferred assets to a Canadian corporation in excess of $13,000,000. Efforts have been made by internal-revenue agents of the United States often and again to obtain complete information about this Canadian foreign corporation, which is called the Wenonah Development Co., Ltd. The transfer of this sum of money to the Wenonah Development Co., Ltd., relieved Bache of the receipt of incomes which had previously resulted in the payment of substantial taxes to the United States Government. Apparently this Canadian company has been very prosperous, because its assets appear to have been increasing constantly.

In 1932 Mr. Bache obtained $2,300,000 from the Wenonah Development Co., Ltd., as a loan, and on his 1934 return he deducted $225,000, representing interest paid to a corporation which he personally owned. This deduction was sufficient to reduce his return to a non-taxable status. He repeated the same operation in 1935 and 1936. The interest charge was under $100,000 annually, with the result that he paid little tax in 1935 and no tax in 1936.

On May 23, 1934, Mr. Bache formed another corporation under the laws of the Bahama Islands by the name of Richmill Bahamas Co., Ltd., which was capitalized at $500,000 and owned by the Wenonah Development Co., Ltd. It is understood that this corporation was formed to hold all or part of the capital stock which Mr. Bache owned of Domes Mines, Ltd., a Canadian corporation.

It appears that by this means Mr. Bache is attempting to avoid the payment of American taxes on dividends received from Domes Mines, Ltd., although indirectly retaining control of the stock and its income through his domination of the Wenonah Development Co., Ltd. That is the conclusion of the Bache case, if there are any questions.

Mr. VINVSON. Did you ascertain who else was in this corporation with Mr. Bache, or in any of these corporations? There are other stockholders?

Under Secretary MACILL. It is my understanding that the stock is all owned either by Mr. Bache or by two trusts which he set up in favor of his daughters.

Mr. VINVSON. How did he get the stock from the Domes Mines into the Bahamas corporation?

Under Secretary MACILL. I am not fully informed. I presume he exchanged it for the Bahamas corporation stock.
Mr. Vinson. I thought you said though that the Bahamas corporation was wholly owned by the Wenonah?

Under Secretary Magill. Of course, he could have done it. I do not know, but he could have done it the other way; that is, transfer the Domes Mines stock to the Canadian company, and then have it organize the Bahamas company, using that stock as capital.

Mr. Vinson. What advantage would he gain by the formation of the Bahamas corporation if he went that route?

Under Secretary Magill. I do not see the immediate advantage except to have two foreign companies which can deal with each other, and on neither of which you can check up.

Mr. Vinson. You have not been able to check up on the Canadian company, have you?

Under Secretary Magill. No; nor on the Bahamas.

Mr. Vinson. Just spreading it out a little more?

Under Secretary Magill. That is right.

Senator Harrison. Do all of these represent the same character of business that Jules S. Bache conducts in New York, dealing in securities, and so forth?

Under Secretary Magill. So far as I am aware, these companies are investment companies, not brokerage companies.

Senator Walsh. That is, involving American securities and American assets?

Under Secretary Magill. American and Canadian.

Mr. Treadway. I would like to see if I understood Mr. Irey correctly in his opening remarks about Mr. Bache. I understood you to say "if the law is as Mr. Bache interprets it." Did you use some such expression as that?

Mr. Irey. That is correct; yes.

Mr. Treadway. Is it not up to the Government officials to interpret the law? How does Mr. Bache come to be the interpreter of our laws?

Mr. Irey. I am not setting him up as an interpreter of our laws for our guidance, but if we find that his interpretation is as we find it, then it was a legal transaction. That was the point I was trying to make.

Senator Harrison. What has the Treasury Department ascertained? What is their opinion about it?

Under Secretary Magill. I think his setting up of these corporations was legal enough, in this sense, that I do not think there is any criminal liability at all from anything he did. He sets up foreign holding companies because they will save him money which he accumulates as income and assets in these companies. He causes those companies to loan him money on which he takes a deduction for interest. It is all legal, in the sense that I take it, it is all disclosed, there is no fraud. It is simply taking advantage of the situation.

Senator Harrison. Instead of receiving dividends from these companies, on which he would have to pay a tax, he borrows money from these corporations and pays interest on it, and takes it out as a deduction in his tax return?

Under Secretary Magill. That is right. In 1936 my recollection is that Mr. Bache's own return shows a considerable loss. His Canadian company had an income that year of $1,000,000.
Mr. TREADWAY. Mr. Chairman.
The CHAIRMAN. Mr. Treadway.

Mr. TREADWAY. Then, Mr. Chairman, Dr. Magill considers that while such an example as he is giving us of Mr. Bache is not illegal, you would class it as immoral, would you not?

Under Secretary Magill. I feel the same difficulty that was expressed here yesterday in drawing lines between what is evasion and what is avoidance, and what is immoral, and so forth. Some cases you can classify as clearly fraudulent. I feel certain in my own mind this is not one of those.

Mr. TREADWAY. Do you consider that the DeRonde case was?

Under Secretary Magill. I think the DeRonde case is; yes. You see as I get this, in the DeRonde case it would appear that a plain misstatement of facts was made, under oath, as to what his assets were.

Mr. TREADWAY. Then, as I understand it, you are laying before us the cases that you regard both as illegal and other types possibly as immoral, as we know and use the word in this connection?

Under Secretary Magill. Yes.

Mr. TREADWAY. That is with a view of asking Congress to stop the loopholes?

Under Secretary Magill. Exactly. As we said to you yesterday, our interest is in perfecting the law. That is, we are not really interested in persecuting any of these people. What we want to do is to show you what the loopholes in the law are by giving you as good examples as we can get out of it.

Mr. TREADWAY. And as you have previously said, or as I think the Secretary said yesterday, the loopholes have been taken advantage of very largely recently?

Under Secretary Magill. That is true.

Mr. TREADWAY. It has been extended?

Under Secretary Magill. That is right.

The CHAIRMAN. You say that in this case you do not think there is criminal liability, it is not fraudulent. He is protected against criminal liability, but is he exempt from other liability in that situation as a matter of law?

Under Secretary Magill. That is a nice question. I do not think there are any cases on it, but Mr. Shafroth can perhaps help us on that. I think the legal department has ruled that these foreign holding companies are subject to taxation if they are owned by American citizens, under the personal holding company provisions in our revenue laws. You can see that there is going to be a good deal of difficulty in enforcing that position, and I do not think it has yet been tried out in court.

The CHAIRMAN. It will be your endeavor to collect those taxes?

Under Secretary Magill. Oh, yes; I think there is no doubt; but you start in to collect these taxes and, as you know, you are going to be 5 or 6 years in litigation before you actually collect them, and in the meantime you are losing or may be losing similar amounts through other companies that are doing the same thing.

The CHAIRMAN. Proceed.

Mr. IREY. Next we have the case of Mr. Wallace Groves, who is prominent in New York financial circles and has been associated with the Interstate Equities Corporation, later succeeded by the Equity
Corporation, the Chain & General Equities, Inc., the Yosemite Holding Corporation, and the Franklin Plan Investment Trust of Philadelphia. Through his control of holding corporations or investment trusts he is understood to control the United Cigar Store chain and also the Whelan Drug Store chain.

Mr. Vinson. Mr. Chairman.

The Chairman. Mr. Vinson.

Mr. Vinson. Are all of these domestic corporations?

Mr. Irey. Yes. He has been in constant litigation with the Bureau of Internal Revenue for many years. From testimony and documentary evidence produced at recent hearings before the Securities and Exchange Commission, it appears that in 1936 Mr. Groves owned the Nassau Securities, Ltd., which he had organized the year before in the Bahama Islands. This corporation had a capital stock of $50,000, and only five shares were issued. Mr. Groves was able to control the General Investment Corporation, which, unlike the Nassau Securities, Ltd., was a substantial business enterprise having many stockholders.

The General Investment Corporation deposited $2,500,000 in the Royal Bank of Canada. Then Mr. Groves caused the General Investment Corporation, which he controlled, to agree to buy its own stock from the Nassau Securities, Ltd., at $102 a share, the transaction to be consummated in Montreal, Canada.

At the time the agreement was made the Nassau Securities, Ltd., owned no stock in General Investment Corporation. It therefore made an open offer to all the stockholders of General Investment Corporation to purchase their stock at $87.50 a share. It was stipulated that any stock so acquired should be deposited in escrow in Montreal. The agreement further provided that such stock was to be deposited on January 23 and paid for on January 25, 1937.

It is important to note that the delivery to the General Investment Corporation of its own stock by Nassau Securities, Ltd., was also to be consummated on January 23. In other words, by this agreement Nassau Securities, Ltd., did not have to pay the individual stockholders of General Investment Corporation (from which it had purchased stock at $87.50 a share) anything until after General Investment Corporation had paid Nassau Securities, Ltd., $102 a share for that same stock.

The details of this financial legerdemain are very difficult to explain without a chart. The net effect, however, was this: Mr. Groves, acting through his personal corporation, Nassau Securities, Ltd., bought stock from the stockholders of General Investment Corporation and sold the same stock to General Investment Corporation at a profit of $14.50 a share.

Senator Harrison. Mr. Chairman?

The Chairman. Senator Harrison.

Senator Harrison. How much would that amount to?

Mr. Irey. About $350,000 profit, $356,000, I think.

The Securities and Exchange Commission is engaged in determining whether these transactions were a fraud on the stockholders of General Investment Corporation. With that question, of course, we are not here concerned. We are concerned with the fact that the method by which Mr. Groves attempted to free the gains from the
transactions from income taxation in this country was the use of a foreign corporation, which apparently had no function other than that of making possible an avoidance of United States taxes.

That is the conclusion of the Wallace Groves case.

Mr. Vinson. Mr. Chairman.

The Chairman. Mr. Vinson.

Mr. Vinson. When did that transaction occur?

Mr. Irey. Just in January of this year.

Mr. Vinson. Of this year?

Mr. Irey. Yes.

The Chairman. If there are no further questions, you may proceed with the next case.

Mr. Irey. Mr. Percy K. Hudson, who was formerly a member of the New York Stock Exchange, has availed himself of a Newfoundland personal holding company in a rather novel way. It should be stated in fairness to Mr. Hudson that his transactions seem to fall within the letter of the law.

Under the present income-tax law, deductions for losses on sales of securities by individuals are limited to only $2,000 in excess of any reported capital gains. Mr. Hudson, in 1936, lost $130,000 on a sale of securities on the stock exchange. He had realized no profits against which the offset could be made. Therefore he created a profit of $130,000 by selling other securities to his own corporation. He accomplished this in the following way: He was the owner of 78 percent of the stock in a Newfoundland corporation, Laurentian Mines, Ltd., the balance being held by his brother and a close friend. He sold $400,000 of his personally owned securities to this foreign corporation which he dominated. This transaction gave him the needed profit of $130,000 to which we have referred.

Moreover, the securities which he sold to the Newfoundland corporation now have a basis for the purpose of computing future profits which is increased by $130,000. By this method if the Newfoundland corporation which Mr. Hudson controls sells these securities in a later year for $130,000 more than Mr. Hudson originally paid for them, its income-tax return for that year will show no profit.

This same method might have been employed so far as stepping up the value of the securities is concerned, with a domestic personal holding corporation. However, the foreign corporation was no doubt used for this purpose in order to attempt to escape surtaxes on the dividends on the stock held by the foreign corporation.

While this particular situation does not represent tax avoidance of a very large amount, the method can very readily be used time and time again, and thus enable not only this taxpayer, but all others resorting to the same scheme, to step up cost bases of securities and to have their American income paid to foreign personal holding corporations.

Now we have the case of Jacob Schick. He was commissioned in the Engineer Corps of the United States Army. He served his country with distinction until his retirement some years ago as a lieutenant colonel. He drew a pension as a retired United States Army officer until December 18, 1935, when he became a Canadian citizen by special dispensation from the Prime Minister of Canada.

The Chairman. Prior to that time he was a citizen of what State?
Mr. Irey. In this country, he was a citizen of the State of Connecticut, I believe.

Colonel Schick is the inventor of the Schick electric dry shaver, which article is manufactured by the Schick Dry Shaver Co. of New Haven, Conn., and is sold universally. It is common knowledge that this invention has proved very profitable to the inventor through sales to citizens of the United States. Naturally, such profits are taxable under the United States income-tax laws.

In November 1933 Colonel Schick formed a corporation in Nassau, Bahama Islands, which he named Schick, Ltd., and assigned his royalty income from the American operating company to that foreign corporation. This royalty amounted to $129,000 in 1934, and there was a withholding tax thereon of $17,737. If Colonel Schick had received and reported this money in his personal return, he would have been liable for a much larger income tax.

Apparently Colonel Schick was not satisfied with this saving in taxes, so on December 18, 1935, he became a Canadian citizen, and 5 days later formed three other companies in Nassau, Bahama Islands. He named these companies Schick Industries, Ltd., Schick Shaver, Ltd., and Schick International, Ltd., and he transferred to them 57,791 shares of Schick Dry Shaver, Inc., the American manufacturing company. This was practically all the stock outstanding of the American company.

It is very interesting to note at this time that Colonel Schick's change in citizenship was absolutely necessary for him to consummate this transaction and avoid taxes in the United States. There are tax laws designed to prevent American citizens or resident aliens from transferring American holdings abroad for tax-avoidance purposes. If an individual is neither a citizen of the United States nor a resident, then there is no way in which our law as presently constituted can prevent him from transferring his securities to whomsoever he pleases, even though all the stock owned by this individual yielded income through American companies.

Senator Walsh. Has he transferred his residence?

Mr. Irey. Yes; to Montreal, Canada, I understand.

The Chairman. Did he have any business operations at all in Canada?

Mr. Irey. Not so far as I know, with the exception of these personal holding corporations.

The Chairman. I understand.

Senator Harrison. Where is his plant that manufactures the razors located?

Mr. Irey. It is in New Haven, Conn.

Senator Harrison. It is still there?

Mr. Irey. Yes.

Senator Harrison. Has he any other plant anywhere?

Mr. Irey. I know of no other plant. I think all of the razors are manufactured in that one plant.

Senator Walsh. Is he still getting his Army retirement pay?

Mr. Irey. No. At the time of taking Canadian citizenship he received his December 1935 check early in January 1936 and he wrote to the Secretary of War pointing out to him that he had become a Canadian citizen on December 18, and asked what he should do with his check.
TAX EVASION AND AVOIDANCE

Senator Harrison. He was very gracious in the matter of the pension.

Mr. Irey. Most of these cases are selected from the Bahama Islands because that was the only locality which the Bureau has had sufficient time to investigate thoroughly.

Senator Harrison. Prior to moving to Canada and becoming a citizen there, did Colonel Schick pay much income tax?

Mr. Irey. He did not. Of course, this Schick dry shaver is a rather recent invention, and the real income from it has come only within the last couple of years. Before that period he was the inventor, as you know, of the Schick ejector razor, which was a losing investment, and he had losses in the early years. Then, when he manufactured his Schick electric dry shaver and it became a very profitable venture, he took his earnings away from this country.

The Chairman. As soon as he began to make money he changed his place of residence?

Mr. Irey. That is right.

However, in order to show the possibilities of the foreign personal holding company, we thought it important to review briefly conditions in other countries which make them equally available for tax avoidance.

Mr. Vinson. Mr. Chairman.

The Chairman. Mr. Vinson.

Mr. Vinson. Have you the picture, or can you tell us just how he manipulated the three later additions to his foreign personal holding company family?

Mr. Irey. Those three that he established after he became a Canadian citizen?

Mr. Vinson. Yes.

Under Secretary Magill. We do not know. I do not know why he has three instead of six or one. It does not look necessary, but he apparently thought it was.

Mr. Vinson. I thought perhaps you had some information as to what use he puts them to.

Under Secretary Magill. It is the same story that Senator Walsh brought out a minute ago. I do not think there is any way of finding out what the purpose was or the motives or anything else, unless you get the individual in.

Mr. Treadway. Mr. Chairman.

The Chairman. Mr. Treadway.

Mr. Treadway. Do you consider that this Schick illustration is capable of being indefinitely elaborated upon by other business people making profits?

Under Secretary Magill. Yes, sir. It is what I would call one of those fighting chances. Take for instance the assignment of royalties to this Bahamas company. It is conceivable that we could convince the court that that was simply a dodge, that the royalties actually belonged to Schick in person, they were being earned in the United States, and they ought to be taxable here in the usual way in his return. Whether a court would so hold or not no one can know. Similarly the transfer of the stock of this Connecticut corporation to the Bahamas company and the subsequent receipt of dividends by the Bahamas company—conceivably we can make out a case for taxation, but in this case it is going to be practically im-
possible, I should say, because of Schick having changed his citizenship.

Mr. Treadway. You say "practically impossible" to hit that kind of case, the change of citizenship puts it in a different category?

Under Secretary Magill. That would make our lot particularly hard in trying to collect anything from him.

Mr. Vinson. Do you collect your corporate tax?

Under Secretary Magill. What we collect is this: In view of the strengthening of the withholding provisions which you made in 1934, we can collect the tax on the dividends; that is, at the withholding rate, 10 percent, payable to the Bahamas company. We cannot collect surtaxes on those dividends.

Mr. Vinson. No. You can withhold as to the first Bahamas corporation, but it just occurred to me that the setting up of the second, third, and fourth might permit him to avoid payment of that tax.

Under Secretary Magill. You may be right. Of course, I do not want to admit anything, but we will go after him as hard as we can under the laws we have, but our whole case is as you see that we think the laws can be amended to put us on a much better footing.

Mr. Treadway. Do you think this particular type of case can be hit by changing the law?

Under Secretary Magill. I yield to you on that. I do not think you can do anything, however, as to his becoming a Canadian citizen. If our taxpayers want to go off and become citizens of other countries, all right, I suppose, that is their status from then on; but the device of causing royalty income and dividend income to be paid to these foreign companies is one that could be utilized without changing any citizenship, and that of course is what we are primarily concerned with. This is just a striking case, because the man went the whole route to eliminate American taxes as far as he could.

Mr. Vinson. Could you not make it right generous withholding tax rate in a case that could be pictured such as this?

Under Secretary Magill. I am glad you are thinking along those lines, because we have been, too. A right generous rate seems to be indicated.

Senator Harrison. Mr. Chairman.

The Chairman. Senator Harrison.

Senator Harrison. May I ask the witness a question? You said something about this retired Army officer, who had a fine record in the service, I think you said, and who has now a better record as an evader. He went to Canada, and through the Prime Minister, you say, obtained citizenship. Was there anything unusual in the way he obtained his citizenship up there?

Mr. Irex. Our information in that connection, Senator, is this, that he is a personal friend of the Prime Minister, or whoever may have been the Prime Minister of Canada at that time, and under Canadian laws a man must have been a resident of Canada for a period of 5 years before he can become a citizen. He had not lived in Canada, of course, any such length of time, and the only way in which he could have become a citizen within that tax period before January 1, 1936, was by a special dispensation by the Prime Minister, and that special dispensation was granted in his case, we are informed.
Senator Harrison. It was an unusual case?
Mr. Irrey. Unusual; yes.

Senator Harrison. I had understood that the Canadian Government had cooperated quite fully with the Treasury Department in running down tax evaders. That was the information I think I received from the Treasury Department.

Under Secretary Magill. That is true, Senator. I do not know whether the present Government or the present Prime Minister of Canada is the same as the one that helped Colonel Schick out in 1935, but it is true that the present administration of inland revenue in Canada has been very cooperative with us in attempting to run down tax evasion. They have one of the best records of any country.

Senator Harrison. In this case they slipped a cog? Let me ask you a question along another line. In connection with his royalties, I imagine he had a patent on this particular kind of safety razor, did he not?

Mr. Irrey. That is right.

Senator Harrison. I do not know the modus operandi of transferring a patent of a United States citizen or corporation to a foreign corporation. Have you looked into that phase of it?

Under Secretary Magill. I have not, sir, in the time that I have had on this, but I shall be glad to do so. It sounds like a good idea.

Senator Harrison. I do not know whether there is anything in it or not.

Under Secretary Magill. We can at least find out.

Senator Harrison. All right.

Senator George. Mr. Chairman?

The Chairman. Senator George.

Senator George. May I ask, regarding this retired Army officer, Schick, as I believe you called him, did he receive both dividends from the American operating company and royalty payments?

Under Secretary Magill. I believe so; yes, Senator.

Senator George. He had the two sources of income?

Under Secretary Magill. Yes, sir. He originally owned the stock of this company and also had income from the royalties on the patents, as I understand it, and he first transferred the royalties to one of these Bahama companies, and then later on after he had become a Canadian citizen he transferred the stock to one of them.

Senator George. And as long as he remained an American citizen, did he not have constructive receipt of his royalties?

Under Secretary Magill. Yes; I should suppose so.

Senator George. I should suppose any royalty that he received, although it was assigned or transferred, while he was an American citizen, would be subject to tax here.

Under Secretary Magill. I should think so; yes. Of course, it goes without saying that we are making a careful investigation of his returns for all of these back years to see what can be done, and that we will complete something during the summer. It is perhaps also interesting to note that immediately after he became a Canadian citizen and after he transferred this stock to the Bahama company he declared a large dividend from his Connecticut company, but he waited until the transfer had been made first.

Senator Harrison. Mr. Chairman.

The Chairman. Senator Harrison.
Senator HARRISON. May I suggest, Dr. Magill—I think it ought to go into the record sometime—that you give us an idea about the taxes one has to pay in these various countries to which people have gone from this country to form these corporations. I think it would be quite illuminating.

Under Secretary Magill. I think I can give that to you right now. There is no income tax in the Bahamas at all, as I understand. I think the entire revenue that the islands obtain is obtained from customers, so they have no income tax. In Panama, which will be referred to presently, I believe there is a small income tax. I am informed there is no income tax in Newfoundland. Usually, of course, the man going into this kind of scheme picks a country where there is no income tax, or at least no income tax on the kind of transactions that he is going into.

For instance, in Panama, my understanding is that there is no tax on sales of securities other than Panama securities, so that it is a good place to organize a company which is going to deal in American and Canadian securities. We can give you that in a table if you would like it, Senator.

The CHAIRMAN. This man, Schick, would be more appropriately named "Slick." Have you any evidence as to where he has spent the major portion of his time since he changed his citizenship to the Canadian Government from Connecticut, where his business is, whether it is over there?

Under Secretary Magill. I do not know, sir. We have not trailed him. His business is in Connecticut. He says he is a resident of Montreal.

The CHAIRMAN. You do not know where he spends the greater portion of his time?

Under Secretary Magill. Whether he is physically in Montreal or physically in Nassau or in Connecticut, I really do not know. I should think he would have to come down here once in a while.

Mr. Vinson. Mr. Chairman.

The CHAIRMAN. Mr. Vinson.

Mr. Vinson. Have there been any recent changes in the Canadian income-tax law?

Under Secretary Magill. I cannot answer you very accurately on that, Mr. Vinson.

Mr. Vinson. I would like for you to put into the record the rates under the income-tax law in Canada at present, and what they were 5 years ago. It is my understanding that they were less burdensome a few years back than they are now.

Under Secretary Magill. We had better give that to you in documentary form, but I know one thing that we want to give you, the provision of the Canadian law that they have enacted for the purpose of stopping this Bahamas racket. They have a provision whereby a Canadian stockholder in a Bahamas company must report his stockholdings in that company and must pay the tax on the income of that company.

Mr. Vinson. The point I wanted to get, there, was the fact that several years ago the income-tax laws of Canada were more favorable for the formation of Canadian companies than they are today. They have a withholding dividend tax now, do they not?

Under Secretary Magill. Yes, sir.

Mr. Vinson. And that is a recent development, is it not?
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Under Secretary Magill. That is right. That is quite possible. As you can see here, Canada is probably not very widely used by Americans in this connection, and the Bahamas are much better.

Mr. Vinson. Yes; but formerly?

Under Secretary Magill. It was.

Mr. Vinson. Americans went into Canada?

Under Secretary Magill. That is right.

Mr. Vinson. And then Canada rather tightened her income-tax laws, and it was not such a propitious place for Americans?

Under Secretary Magill. That is true.

Mr. Vinson. Then they turned toward the Bahamas and other places?

Under Secretary Magill. That is right. The Canadian authorities, as I have said before, have expressed a willingness to cooperate with us in any way with respect to this tax-evasion business.

The Chairman. You may proceed, Mr. Irey.

Mr. Irey. The principal foreign localities where it is becoming evident that this type of tax avoidance is being used are Newfoundland, Panama, the principality of Lichtenstein, and Prince Edward Island in Canada. We will briefly review the probable extent of the use of foreign corporations to avoid taxes in these countries.

First, let us take up Newfoundland.

From all indications it appears that the device of the personal holding company has been used for some time in this country. In Newfoundland there are a total of 202 personal holding companies which appear to have been formed by Americans in the last 4 years. Forty-six of them were formed in the 18 months after November 1935. The Bureau has not been able as yet to send an agent to Newfoundland, so details are not available. Nevertheless it is difficult to see any reason why 202 personal holding companies should be in operation in that country except for tax-avoidance purposes. The principal industries are the production of paper, which amounts to $12,000,000 annually, and fishing, which produces six millions.

In a cable dated May 7, 1937, the United States consul at St. Johns, Newfoundland, reports:

Large majority of corporations are shown to have been organized by the law firm of Hunt, Emerson, Sterling & Higgins, by subscription for one share by each of three of the partners.

Senator Harrison. Is that firm located at St. Johns?

Mr. Irey. St. Johns, yes, sir.

Shares are immediately transferred to members of Canadian law firms. Since in most cases American shareholders are not indicated it is believed that most corporations although American-controlled are organized for the purpose of tax evasion. This cannot be corroborated except by reference to corporations previously investigated, where it was shown that organization was completed in the same manner and the American shareholders were not shown until long after incorporation. It is presumed the same procedure is now being followed.

The annual report of the Commission of Government of Newfoundland shows government fees from personal holding corporations for calendar years as follows: 1934, $10,857; 1935, $11,864; 1936, $17,323.

This increase in revenues to the Newfoundland Government is clearly due to the increased formation of such companies because the corporation tax rate has not been changed.
Let us next take up Panama. Here we find laws very favorable toward the formation of foreign corporations. No annual statements are required as to the stockholders or as to their financial condition. There is no tax on income or profits from sources outside Panama.

In Panama there were 46 personal holding companies formed by Americans from January 1935, to March 8, 1937. Practically every company which has been formed by Americans has the firm of Fabrega & Fabrega as resident agent. They are the ranking lawyers in Panama City. The head of the firm was once Secretary of State of the Republic of Panama.

For reasons which we will set out later it has been impossible to ascertain the exact nature of the business of these personal holding companies. There is every indication, however, that they were formed for no other purpose than the purchase and sale of securities. In connection with this, it is interesting to note that Mr. Ofilio Hazera, Chief of the Section of Receipts, Department of Treasury, Republic of Panama, advises that a special decree has been issued exempting profits from the sale of foreign securities from the Panamanian income tax.

Next comes Lichtenstein.

Senator Harrison. Mr. Chairman.

The Chairman. Senator Harrison.

Senator Harrison. Is it difficult to get information from the authorities in Panama?

Mr. Irey. It is very difficult; yes, sir.

Senator Harrison. Where, in the case of these various countries, would you say it is more difficult to get information?

Mr. Irey. Of course, Senator, we have sent an agent to Bahama. I am more familiar with the conditions in the Bahamas than at other places. It is almost impossible to secure anything in Lichtenstein. We have sent no one.

Senator Harrison. Where is Lichtenstein?

Mr. Irey. It is near Switzerland, I believe.

Senator Harrison. They have gone over to Europe?

Mr. Irey. Yes.

Lichtenstein: From the information available we believe that there are a large number of corporations formed for tax avoidance in this small principality. This belief is based upon the fact that the tax-incorporation laws of Lichtenstein offer unusual opportunities for the operation of this device. It is impossible, however, to give the committee definite information here. The American consul on May 13, 1937, reported to the Bureau that the government officials of Lichtenstein declined to supply any information whatever concerning incorporation of American companies in that country. The following information given to us by the consul, however, is very significant:

In the year 1935 the total tax revenue is stated as 747,749 Swiss francs. The income from incorporation taxes in that year amounted to 849,128 Swiss francs.

One person is sufficient to constitute a company or trust. It is not necessary for a promoter to go to Lichtenstein for that purpose. All that is required is representation by a firm or citizen of Lichtenstein.
We have no real information available about Prince Edward Island.

Senator Harrison. Mr. Chairman.
The Chairman. Senator Harrison.

Senator Harrison. You may have stated it, but how many corporations have been formed in Lichtenstein by American citizens?

Under Secretary Magill. We have no way of finding out, because the Lichtenstein officials will not give you any information.

Senator Harrison. You spoke about some having been formed over there.

Under Secretary Magill. We do very strongly suspect, because of the very generous character of the corporation laws——

Senator Harrison. Is the Principality of Lichtenstein a separate unit of government?

Under Secretary Magill. Lichtenstein is itself a place about 6 miles square over there that has a duke to run it.

Senator Harrison. It is not under the Republic of Switzerland?

Under Secretary Magill. No; I believe not.

Senator Harrison. It is a free state?

Under Secretary Magill. I believe so.

Mr. Cooper. Mr. Chairman.

Mr. Cooper. Will you kindly restate the amount of revenue that you mentioned a moment ago, which, as I caught it, was slightly less than a million dollars?

Mr. Irey. I was speaking in Swiss francs.

Mr. Cooper. I mean a million of Swiss francs.

Mr. Irey. The total tax revenue in 1935 was 747,749 Swiss francs.

Mr. Cooper. Is that the total revenue received by the country?

Under Secretary Magill. Yes; apparently that is all they get; and half of that comes from incorporation fees.

Mr. Irey. The income from incorporation taxes in that year amounted to 349,128 Swiss francs.

Mr. Cooper. That is exactly the point I was trying to develop. Substantially half of the entire revenue received by that country is from corporations?

Under Secretary Magill. That is right.

Mr. Treadway. Mr. Chairman.
The Chairman. Mr. Treadway.

Mr. Treadway. Is there any indication that all that corporate money came from American corporations?

Under Secretary Magill. I do not think we know, but my understanding is from what the consul gave us that officials in Lichtenstein will tell you nothing, and that there are no records that you can get; so this, so far as we know, may be English incorporations or French incorporations, or something else.

Mr. Treadway. In other words, our folks need not necessarily be the only guilty ones?

Under Secretary Magill. Oh, no; probably not.

Mr. Vinson. Mr. Chairman.
The Chairman. Mr. Vinson.

Mr. Vinson. Do I understand that they use the trust device there as well as the corporation device?
Under Secretary Magill. I think they do, yes, sir; but again our information is extremely scanty, because it is practically impossible to find out anything.

Mr. Irey. We have no real information available about Prince Edward Island. Prince Edward Island is within the Dominion of Canada. Nevertheless, it offers another excellent field for the incorporation of personal-holding companies by foreigners. Under the provincial act, holding companies are required to give only very limited information when registering. The information on their annual returns is still more limited. The Public Accounts of the Island for 1936 show receipts of $120,919.90 from corporation taxes, of which $70,208.34 was from investment companies. Only the lawyers know the real names of the investors.

Other foreign countries: The use of foreign corporations in foreign countries other than those listed here for tax-avoidance purposes is, of course, possible. It is, however, extremely difficult to locate such companies. We have at this time only one case—the case of Mr. Charles Laughton, motion-picture actor, who has caused his salary earned in this country to be paid to an English corporation.

Mr. Laughton is a British citizen. He formerly a personal holding company in England. He then entered into a contract with that holding company to pay him a salary of $20,000 for the year 1935. By virtue of that contract the foreign holding company became entitled to all of his earnings in this country as a motion-picture actor, which amounted to $190,280.22 in 1935. The earnings of the British company consisted entirely of the Laughton American income. It is true that his personally owned British company paid a tax here. Yet through that company Laughton effected a substantial reduction in the amount of taxes which otherwise would have been payable to the United States Government on these earnings.

The conduct of Mr. Laughton in this instance may be perfectly legal. The case, however, is cited as another illustration of the rapidly growing use of the foreign corporation for the purpose of reducing the amount of taxes which an individual would otherwise be required to pay on his earnings within the United States.

The difficulties of gaining any information about foreign corporations in the countries which we have discussed create a situation in which only the personal ethics of the taxpayer determine whether he will indulge in deliberate tax evasion rather than tax avoidance. The expense of sending agents to these countries is prohibitive. Moreover, when agents are sent they are unfamiliar with the law and the governmental institutions with which they are dealing, and often with the language itself. There is no possible pressure which can be put upon the foreign attorneys who form these foreign corporations, or upon the foreign corporation itself, to compel them to disclose its ownership, the extent of its activities or its American income.

Therefore no one knows or ever will know until our income-tax law is made more stringent how many of the hundreds of corporations organized by Americans in these countries are used for tax evasion, how many of them for tax avoidance, and how many represent genuine business activity. As the editorial quoted from the Bahamas newspaper indicates, the present situation is a challenge to Congress and to the Treasury to make our revenue laws really effec-
tive against those of our citizens who seek sanctuary for their investments by taking them to foreign shores.

Mr. Cooper. Mr. Chairman.

The Chairman. Mr. Cooper.

Mr. Cooper. From your present knowledge and information of the various cases cited here, is it your view that effective legislation may be enacted to meet these various cases presented?

Under Secretary Magill. Mr. Chairman, perhaps I had better answer that, because Mr. Irey, I think, has not been working on the legislation.

As soon as these situations came to our attention we at once put our men to work to see what kind of plugs might be put in these loopholes. Now, as has been pointed out, we have already got various plugs for this situation. The withholding provisions were much improved in the last law. So far as this situation is concerned, you see what you have is this: The company which has the money is in a foreign country. The foreign country may or may not be willing to give you any information about the company, and ordinarily is not. As the committee knows, it is not possible for us to sue for taxes in the foreign country, so that the company and its assets are out of here and there is no possibility of an effective suit against the company. Hence our recourse necessarily is against our citizen personally who owns the stock in this company.

The reason why it is so difficult to ascertain the facts, or so difficult to enforce the laws effectively, is the fact that we need provisions in the law to compel the American owner of stock in these countries to report what stockholdings he has, under penalties, and then I think, since the fact seems to be that practically all of these personal holding companies are simply used for avoidance, that they have no business purpose, it seems to me it would be constitutional to provide as Canada does, and as I believe England does, that the income of these companies shall be taxable prorata to the shareholders who own the stock. Now, that is one possibility.

We have been working along those lines and have discussed it with experts. Possibly Mr. Beaman and Mr. Parker can work out some scheme or additional provisions which will be even more effective, but I wanted to give you frankly the way in which our minds have been running with respect to this particular proposition.

Mr. Cooper. It is true that a very determined and, we think, effective effort was made in the 1934 Revenue Act to close loopholes that had developed up to that time.

Under Secretary Magill. That is true.

Mr. Cooper. Now, these cases that have been cited here have developed since that time?

Under Secretary Magill. That is true. As you see in your history of the Bahamas there were comparatively few corporations organized there for any purpose until about 1935, when Americans and Canadians began going down there, and so far as what was done in 1934 is concerned, it is true that section 351, which you put into the law at that time, has been a most effective aid with respect particularly to domestic personal holding companies.

Senator Harrison. Mr. Chairman.

The Chairman. Senator Harrison.
Senator Harrison. Of course, we want to plug these loopholes by amending the law, but has the Treasury explored the thought—since you state that you have been working with Canada and others and they have been cooperating—of trying to arrange some kind of conferences where there might be reciprocal agreements entered into with reference to these tax problems?

Under Secretary Magill. We have; yes, sir. We have been in correspondence with the State Department, asking that negotiations be instituted along those lines, and the State Department has shown every inclination to foster such negotiations. Not many of the countries are interested in them, because this present business is obviously profitable immediately to some of these places, which are using it. Canada has indicated an interest, and France, in particular, has indicated an interest in cooperation between the tax administrations.

Senator Harrison. It would strike me that no matter what law we may write, it would be of great assistance to get some form of agreement on the part of the countries.

Under Secretary Magill. I think there is no question in the world about it, that if we can work out a situation whereby we can exchange information with some of these countries, it will be of immense benefit to both of us.

The Chairman. Did I understand you to say that as to the corporations doing business in this country, which have organized holding companies in other countries, their assets are where they have organized these holding companies, or did I misunderstand you?

Under Secretary Magill. What I meant is this: That is necessarily true, and I can illustrate the proposition.

The Chairman. Their main assets are here, are they not?

Under Secretary Magill. The tangible assets may be here, and if you will turn over in your mind Colonel Schick's situation, you will see what I have in mind. The razor factory is in Connecticut, as I understand it. Now, where the certificates of stocks are which are owned by that Bahama company, I do not know. They may be in the Bahamas, they may be in New York. Technically the stock is owned by the Bahama company.

Mr. Crowther. It seems to me, Mr. Magill, with the exception of the one case here where this man Schick expatriated himself and became a Canadian citizen, we have not very much that is new, here, so far; nothing newer than we had before us in 1934, in the kind of tax avoidance or so-called tax evasion. There may be a little further development on these schemes that were outlined to us at that time, when the subcommittee of this Ways and Means Committee made a rather intensive study of these matters, together with the Treasury employees and Mr. Parker of the joint committee.

Is this all the list that you have? The reason I ask that is this, that it seems pitifully small. That is, do you think that such a list as you have given us today would account for the discrepancy in the lack of revenue that has occurred?

Under Secretary Magill. No; this is only one of the various devices which we are presenting to you at this time. This is a very important one. Now, the reason why the information is, as you say, "pitifully small" that we have tried to give you, is that it is practically impossible to get very much of it unless you enable us to compel American taxpayers to give us the information.
Senator Harrison. Will the gentleman yield?

Mr. Crowther. Yes.

Senator Harrison. It does not appear to every member of the committee to be at all "pitifully small." I think that the DeRonde case and the Bache case in particular are rather startling, and there have been put into the record something more than a hundred cases, were there not, which you have gone into?

Under Secretary Magill. That is true.

Senator Harrison. But you were presenting these cases as illustrations of evasion and avoidance?

Under Secretary Magill. Yes. Maybe we have not made it sufficiently clear, but what we were trying to do was to give you one rather striking example of each of the different phases of tax avoidance which these foreign corporations present. We could multiply instances, if you want them, but I think that what we have tried to do is to select cases which will show you the need for such legislation as I have informally presented here.

Mr. Crowther. If Senator Harrison will permit, my reference to it being pitifully small was not regarding the merits or the demerits of the case and the illegal methods used, but it seemed to me that it was pitifully small, insofar as the returns due to a correction of this evil would be very small, would they not?

Under Secretary Magill. No; I think that is not quite accurate, sir. So far as these particular individuals are concerned, they may only owe us a few hundred thousand dollars in taxes, I do not know. So far as the several hundred others which are involved in those other corporations, a list of which has been put in the record, there may be a good many more millions of dollars involved; but, as I said in my statement yesterday, what we are afraid of is that what may now be simply a trickle of lost revenue comparatively, in the long run will become a big stream unless something is done about it, because there is at present very active solicitation of wealthy American taxpayers to go into this particular form of tax-avoidance device.

Mr. Crowther. Then, as we proceed, you are to present other methods of leakage and loss?

Under Secretary Magill. Oh, yes; this is just one.

Senator Harrison. I understand, Dr. Magill, that there were set forth about eight of these methods of tax avoidance or tax evasion. You have discussed this morning only the first, namely, the personal holding company in foreign countries?

Under Secretary Magill. Right.

Senator Harrison. And that the next you will take up will be the question of the device of foreign insurance companies and discuss that matter?

Under Secretary Magill. Yes, sir.

Senator Harrison. When you finish the device of the domestic personal holding companies?

Under Secretary Magill. That is correct.

Mr. Crowther. Are you going to discuss the incorporated yacht later?

Under Secretary Magill. Yes, sir. I probably did not make it clear yesterday what we had in mind. I think we would confuse perhaps rather than aid in giving a whole list of names of a lot of people
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who have been doing the same thing. We want to concentrate attention on the device and legislation which can be adopted to stop the loss of revenues. We are not interested, as we said yesterday, in pillorying several hundred Americans. What we want to do is to correct the laws.

Mr. Crowther. Mr. Chairman, I agree with Mr. Magill regarding that, and I think we ought to make a very careful sensible investigation and not make a Roman holiday out of it, and have our investigation calculated to be such as to provide some cure for the problem that is presented to us here.

Senator La Follette. Mr. Chairman.

Mr. Chairman. Senator La Follette.

Senator La Follette. Dr. Magill, how many additional names of individuals who have indulged in this foreign personal holding-company practice is the Treasury now in possession of?

Under Secretary Magill. We could give you the stockholders as they appear, for instance, of these various Bahama corporations, 100 or more of them.

Senator La Follette. Who are American citizens?

Under Secretary Magill. Some of them are and some of them are not. Some of them are dummies and some of them are the real people. Now, for example, one case that has not been mentioned here this morning is the case of George Westinghouse, Jr., who formed a corporation in the Bahamas, which is capitalized at $3,000,000, and, as was pointed out in one of the reports, Westinghouse reports one year from New Brunswick, the next year from British Columbia, and the third year from the Bahamas or Jamaica, so there is no catching up with him. Now, we could give you, I suppose, a dozen other similar instances, if you want them. What we have tried to do here is just to present you nothing that we have not verified and checked and gone over and audited as carefully as we know how, and, as you can appreciate, that takes quite a lot of time.

Mr. Cooper. Mr. Chairman, I think it was while the Senator was detained a moment that Mr. Magill put a list of more than 100 in the record.

Senator La Follette. He put in a list of the corporations, as I understand it.

Under Secretary Magill. And their stockholders, so far as they appear in the records, in the Bahamas.

Senator La Follette. But, as I understand it, Mr. Irey, you have given us now all of the cases of individuals, where the Treasury has had an opportunity to make a preliminary study and audit of their returns?

Under Secretary Magill. In general, that is true. We doubtless have other cases at hand now, but we wanted to give you those which we have fully documented.

Judging from the joint resolution, we have assumed that there might be another meeting of the committee in the fall, in which you might want to go into some more of these cases, but at any rate what we wanted to do now was to give you enough examples to form a basis for legislation, if you wished to enact it at this time.

Senator La Follette. What I am trying to get at is upon what basis you selected the cases which you presented, and eliminated cer-
tain others. Is it because your study has not progressed so far with regard to them?

Under Secretary Magill. Yes, sir.

Senator La Follette. But those studies are being prosecuted?

Under Secretary Magill. Yes, sir.

Senator La Follette. And you will bring the additional names to the attention of the committee, as soon as they are in the same category as these others, insofar as the completeness of the study is concerned?

Under Secretary Magill. As the committee desires. Mr. Irey is the head of a staff which is now actively analyzing that information and pursuing additional investigations.

Senator La Follette. I would just like to suggest, Mr. Chairman, that it seems to me that as rapidly as these cases come into the category of those which have now been presented, they should be presented to this committee. Otherwise, there is no rule to be followed, and I cannot see why certain individuals who have indulged in this practice should be brought out and put into the record, and others eliminated, and it seems to me that otherwise both this committee and the Department will be charged with discrimination. It seems to me that this committee ought to adopt the rule that as fast as the Department is ready to report these cases, they should be reported, in the same way that the others have been.

The Chairman. The Chair would think it reasonable to presume that the Treasury Department will report these cases to the committee as rapidly as their investigation of the facts warrants or permits, but it is a pertinent suggestion. If they do not do it, I think the committee should call on them to do it.

Senator La Follette. If it is necessary, Mr. Chairman, I propose a motion to that effect. I move that the Department be instructed to furnish these cases of this particular device of avoidance or evasion as rapidly as they are ready for presentation and are in the same situation as those that have been presented this morning.

The Chairman. You have heard the motion of Senator La Follette. Is there any discussion?

(The motion was agreed to.)

Senator Harrison. Mr. Chairman.

The Chairman. Senator Harrison.

Senator Harrison. Mr. Magill, in this group of corporations, a list of which has been placed in the record, are there some others that you want to discuss now? You have not discussed all of those.

Under Secretary Magill. Mr. Irey tells me that the evidence is not developed to a sufficient extent on them to make it justifiable to go into them at this time. We are getting it as fast as we can, but as I think you appreciate, we have had to work pretty fast on this situation.

Senator Harrison. Yes; we do appreciate that.

Mr. Vinson. Mr. Magill, I am reading section 901 of the Revenue Act of 1932 into the record:

There shall be imposed upon the transfer of stock or securities by a citizen or resident of the United States, or by a domestic corporation or partnership, or by a trust which is not a foreign trust, to a foreign corporation as paid-in surplus or as a contribution to capital, or to a foreign trust, or to a foreign
partnership, an excise tax equal to 25 per centum of the excess of (1) the value of the stock or securities so transferred over (2) its adjusted basis in the hands of the transferor as determined under section 113 of this Act.

Now, subsequently to the 1932 Revenue Act, and referring specifically to the 1936 act, is it not true that the Congress made taxable the exchange of corporate stock, stock in a domestic corporation for stock in a foreign corporation?

Under Secretary Magill. That is true; by the section that you read.

Mr. Vinson. Now, what moneys have been derived—what revenues have been derived from the exchange of domestic stock for foreign stock, or stock in a domestic corporation for stock in a foreign corporation?

Under Secretary Magill. The Commissioner can answer that more accurately. The actual amount collected has been very small. What is it; $100,000 or so?

Commissioner Helvering. I could not state.

Under Secretary Magill. I got a report on it at one time earlier this spring, and the total is relatively inconsiderable.

Mr. Vinson. Where you have the direct exchange, it would be possible?

Under Secretary Magill. Right.

Mr. Vinson. But, if they make an exchange one time to a foreign corporation, and then the foreign corporation sets up one, two, three additional foreign corporations, why, you are getting lost in the shuffle?

Under Secretary Magill. That is true. Then, of course, further, you can see again the great difficulty of discovery in a case of this kind. Suppose an individual goes down to the Bahamas with a black satchel with some securities in it, and down there he transfers it to a Bahamas company and brings its stock back to New York. How are we to know about it?

Mr. Vinson. Well, you cannot know; but if it should be determined that this exchange was made of stock in a domestic corporation for stock in a foreign corporation, then that exchange is taxable.

Under Secretary Magill. That is true.

Mr. Cooper. Mr. Chairman.

The CHAIRMAN. Mr. Cooper.

Mr. Cooper. Just one question, Dr. Magill, if I may: A few moments ago you mentioned a Mr. Westinghouse. Will you further identify him for us, please?

Under Secretary Magill. Mr. Brenner?

Senator Walsh. His residence, and so forth.

Under Secretary Magill. It is George Westinghouse, Jr. As you see, it is hard to identify him, because he skips around like a bug. He reported first—in the last 3 years we have looked at—from, I believe, New Brunswick, and the next year from British Columbia, and the next year from Jamaica. So George Westinghouse, Jr., is about all I can give you. He evidently has $3,000,000. [Laughter.]

Mr. Treadway. Mr. Chairman.

The CHAIRMAN. Mr. Treadway.

Mr. Treadway. I would like to ask Dr. Magill one question about the Schick case. You made some reference to a suggestion of taxing
American citizens if they made these transactions such as you have referred to, did you not?

Under Secretary Magill. Yes, sir.

Mr. Treadway. That would not apply to the Schick example, would it?

Under Secretary Magill. No; your—

Mr. Treadway. If he could legally establish that he had changed his residence, his nationality?

Under Secretary Magill. The Schick case—quite true. You have put your finger on the fact that Schick in one sense belonged in this last category I spoke of yesterday; that is, the question of the taxation of nonresident aliens, because that is what Schick now is, according to his theory.

Now, as to those, we will have some recommendations to make to try to increase the yield of the income tax with respect to those people with large American incomes.

Mr. Treadway. In other words, you would endeavor in some way to reach that type of case through the main plant in New Haven?

Under Secretary Magill. That is true. I assume, and the theory we are working on is, that the committees in Congress had no intention of taxing wealthy nonresident aliens less than American citizens with similar incomes. It seems a safe assumption.

Mr. Treadway. Especially if they probably have taken out alien-ship for the purpose of avoiding our taxes.

Under Secretary Magill. Yes. We are going to try to present some illustrations that you can consider.

Mr. Treadway. Of that particular type of case?

Under Secretary Magill. To bring about that result.

Mr. Vinson. Let me ask—

Mr. Treadway. Certainly.

Mr. Vinson. I think it should be stated, because of Congress, and particularly the Ways and Means Committee, that initiated the legislation and fixed the rate on the income of nonresidents at 10 percent, that it was stated to us that there were many millions in taxes lost because you did not have the rate on nonresident aliens. Originally the rate tentatively agreed upon in the Ways and Means Committee was 221/2 percent, but, due to representations made by the State Department, in which the Treasury concurred—and I see gentlemen here who were present when that agreement was reached—the 10 percent was reluctantly agreed upon by the Ways and Means Committee. I think that should be stated for the record in self-defense.

Under Secretary Magill. Maybe I should follow your lead by saying I was not there. I don't know whether that is important or not.

Mr. Vinson. There are other gentlemen here who were there.

Under Secretary Magill. I have talked to them, and I understand they feel guilty about it.

But what you did, as a matter of fact, as I said yesterday, was very effective so far as it went. We are getting very much more revenue from nonresident aliens this year than we ever got before. There is no question about that. Now, as to some of the wealthier
ones, we ought to get more still. But it went to about the high in 1936.

Mr. Treadway. Mr. Chairman, may I ask another question?

The Chairman. Mr. Treadway.

Mr. Treadway. This may not be a relevant question, but I happened to take a vacation—not a residential trip or for the formation of a corporation—to Bermuda last fall, and I am positive that on the way back I saw a notice on the ship that only one Schick electric razor could be sold to an individual coming through the port of New York. That is a customs provision. Now, am I right or wrong about that recollection? Has it something to do with the royalty, and some connection with this? Is there some significance about that being a royalty of a foreign company that won't permit of but one article coming in?

Under Secretary Magill. I would like to look that up.

Mr. Treadway. I would be glad if you would. It may have no bearing on this matter, but, as a matter of personal interest, I would be glad to know of that circumstance.

Under Secretary Magill. If Mr. Kent will make a note. I don't know about that customs regulation.

Mr. Treadway. I want it distinctly understood I was not down there forming a corporation. [Laughter.]

The Chairman. Dr. Magill, I understand you are citing these cases of tax evasion and tax avoidance to show that it is not only the last few years, but alarming, so far as our revenues are concerned in the future, unless it is effectively dealt with?

Under Secretary Magill. We believe that to be true. We are afraid of it, because you may have observed that the number of these Bahamas corporations organized in the first few months of this year shows an increase over what was organized last year and the year before. So that it looks as if the device is being resorted to more and, in view of the large amounts of money involved, it is evident that it can be used a great deal further.

Senator Harrison. Mr. Chairman.

The Chairman. Senator Harrison.

Senator Harrison. Could we not have an executive session for about 2 or 3 minutes? It is necessary that the Senators go to the Senate floor early today.

The Chairman. If it is agreeable, we will now go into executive session. If it is agreeable to the members of the committee, we will take an adjournment until Tuesday morning. The Committee on Ways and Means has some matters that it is necessary for us to attend to as early as possible. It is understood that the committee will adjourn until 10 o'clock Tuesday morning.

Under Secretary Magill. Yes, sir.

Mr. Cooper. Mr. Chairman, it is understood that the public hearing is adjourned until 10 o'clock Tuesday morning?

The Chairman. Ten o'clock Tuesday morning, the public hearing of this committee.

(Whereupon, at 12:08 p. m., an adjournment was taken until 10 a. m., Tuesday, June 22, 1937.)
Details of Bahamian corporations formed by Americans from Jan. 1, 1935, to May 1, 1937

Post & Co., Ltd. (file no. 425):
Annual statement dated March 24, 1937.
Filed through attorney, Kenneth Solomon.
Capital stock £10,000, of 1,000 shares at £10 each; all issued; all paid up.

(Notes—Addresses of stockholders not stated.)

<table>
<thead>
<tr>
<th>Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>James Post Eblen, merchant of New York, president and director</td>
</tr>
<tr>
<td>Newton Calvin Eblen, merchant of New York, vice president and treasurer</td>
</tr>
<tr>
<td>Sonia Faith Hall, merchant of New York, secretary</td>
</tr>
<tr>
<td>Balance of stock issued to Nassau residents</td>
</tr>
<tr>
<td>Total</td>
</tr>
</tbody>
</table>

Cat Cay Manor, Ltd. (file no. 426):
Louis Rice Wasey, president and director,
Owen B. Winters, vice president and director,
Margaret C. Cowley, secretary and treasurer,
James E. Rushin, treasurer.

Western Securities, Ltd. (file no. 372):
Annual statement dated April 7, 1937.
Capital stock £20,000, divided into 2,000 shares of £10 each, of which 1,886 shares were issued as fully paid.

<table>
<thead>
<tr>
<th>Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>Anthony Joseph Drexel, 1 share</td>
</tr>
<tr>
<td>Marjorie Gould Drexel, 1,881 shares</td>
</tr>
<tr>
<td>Balance of 18 shares held by qualifying Bahamian individuals</td>
</tr>
<tr>
<td>Address given by the Drevels is Nassau. Mr. Drexel is listed as a retired banker, and is president and director of this company.</td>
</tr>
</tbody>
</table>

Asphalt International, Ltd. (file no. 431):
Annual statement filed December 25, 1930.
Capital stock £5,000, of 5,000 shares at £1 each; 105 shares issued.

<table>
<thead>
<tr>
<th>Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>W. G. Thomas, 90 Broad St., New York City, president</td>
</tr>
<tr>
<td>H. H. Thomas, Jr., 90 Broad St., New York City, vice president</td>
</tr>
<tr>
<td>T. C. Fitzgerald, 90 Broad St., New York City, secretary and treasurer</td>
</tr>
<tr>
<td>Doris Louis Barlow, 324 Bay St., Nassau</td>
</tr>
<tr>
<td>Alice M. A. Farrington, 324 Bay Street, Nassau</td>
</tr>
<tr>
<td>Total</td>
</tr>
</tbody>
</table>

Company was formed through Claude S. Richardson, advocate of 360 St. James St., West, Montreal, Canada.

Trinidad International, Ltd. (file no. 433):
Letter of December 20, 1930, gives officers (not Nassau residents):
E. L. Sanborn, president and director,
Samuel L. Fuller, vice president and director,
Earle H. Rodney, director,
Bertram Sneden, secretary and treasurer.

Kelsey Trading Co., Ltd. (file no. 436):
Letter of January 8, 1937.
Arthur R. Sproule, Toronto, Canada, vice president and treasurer,
H. C. McLean (manager, Royal Bank of Canada, Nassau Branch), secretary,
John H. Anderson, president.

Roco, Ltd. (file no. 443):
Capital $150,000, consisting of 15,000 shares at $10 par value each,
11 shares issued to—
TAX EVASION AND AVOIDANCE

Shares

Elwyn Evans, care of Wilmington Trust Co., Baltimore, Md. 7
H. H. Mears, care of Wilmington Trust Co., Baltimore, Md. 1
F. M. Donohue, care of Wilmington Trust Co., Baltimore, Md. 1
D. S. Foster, care of Wilmington Trust Co., Baltimore, Md. 1
J. W. Chinn, care of Wilmington Trust Co., Baltimore, Md. 1

Total

All of the above give their occupation as bankers.

The Ruby Shipping Co., Ltd. (file no. 445):
Letter of January 11, 1937.
William Henry Handford Maura, Nassau, president and director.
Walter Wrightson, Mobile, Ala., United States of America, vice president and director.
Montague Putnam Maura, Nassau, treasurer and director.
Ruby Wrightson, Mobile, Ala., United States of America, director.

Cumberland Insurance Co., Ltd. (file no. 446):
Letter of February 1, 1937.
Russell L. Hammons, Exeter, N. H., president and director.
Walter S. Hammons, Miami, Fla., vice president and director.
Caswell D. Strout, Portland, Maine, secretary, treasurer, and director.
Two other Nassau residents are directors to qualify the company.

Caribbean Steamship Co., Ltd. (file no. 450):
Letter of April 3, 1937.
Charles Tatt, 242 West Bay Street, Jacksonville, Fla., president.
Harold Johnson, 711 Faragut Street, Jacksonville, Fla., vice president.
Ernest Pitman, 2106 Delwood Avenue, Jacksonville, Fla., secretary and treasurer.

Lynros Development Co., Ltd. (file no. 452):
Letter of January 10, 1937.
Clarence M. Schwerin, New York City, president, treasurer, and director.
Clarence M. Schwerin, Jr., New York City, vice president and director.
Mary C. Schwerin, New York City, director.
Other directors are Nassau individuals.

Sessom Co., Ltd. (file no. 455):
Annual statement filed Jan. 28, 1937.
Capital stock $5,000, consisting of 5,000 shares at $1 each. Eight shares issued.

Shares

Henry L. Moses, lawyer, 30 Pine St., New York City, president 4
Henry R. Singer, lawyer, 30 Pine St., New York City, vice president 1
Lillian Eckstein, secretary, 30 Pine St., New York City, secretary 1
Lucy G. Moses, wife, 30 Pine St., New York City 1
Wooling Realty Corporation 1

Total

Bahamas Land Syndicate, Ltd. (file no. 456):
Letter of February 28, 1937.
Arnold R. Perpall, 342 Madison Avenue, New York City, president, treasurer, and director.
Grace R. Perpall, 342 Madison Avenue, New York City, vice president and director.
Other directors are qualifying Nassau people.

Coral Islands Plantations, Ltd. (file no. 331):
Annual statement dated February 18, 1937.
Capital stock $10,000, consisting of 100 shares. All issued.

Directors

Albert R. Palmer, Midwood Road, Madison, N. J., president 88
Robert C. Palmer, 425 East 86th St., New York City, secretary 6
Raymond J. Walsh, Chester Terrace, Hastings on Hudson, N. Y. 2
Joseph A. Clossick, Overlook Terrace, Bloomfield, N. J. 2
Frank R. Series, Jr., 5 Prospect Pl., New York City 2

Total 100
Nomy Finance Corporation (file no. 332):
Annual statement dated Mar. 10, 1937.
Capital £20,000, consisting of 20,000 shares, at $1 each.
1,000 shares issued.

Francis George Bush, 360 St. James St., West Montreal, Canada--- 1
Claude Sartoris Richardson, 360 St. James St., West Montreal, Canada
John Lawrence McCorry, 360 St. James St., West Montreal, Canada-- 1
Thomas James Madden, 360 St. James St., West Montreal, Canada-- 1
Malcolm Smith Mugford, 360 St. James St., West Montreal, Canada-- 1
Nomy (Canada) Ltd., 119 Richmond St., Charlottetown, Prince Edward Island-------------------------------- 995

Total------------------------------------------------------------- 1,000

Consolidated Investments, Ltd. (file no. 329):
Letter of November 28, 1935.
J. G. Thompson, 600 Richmond Street, London, Ontario, president and director.
J. O. Good, 600 Richmond Street, London, Ontario, vice president, director, and secretary.
Ainley S. Thompson, 600 Richmond Street, London, Ontario, director.

National Investments, Ltd. (file no. 327):
Capital $3,000,000, divided into 30,000 shares at $100 each.
22,649 shares issued, paid in $2,264,900.

Pioneer Petroleum & Trading Co., Ltd. (file no. 321):
Statement dated September 9, 1936.
Capital $250,000, consisting of 25,000 shares, $10 par value.
6,625 shares issued, paid in $66,250.

Supertest Petroleum Corp., Ltd., 600 Richmond St., London, Ontario-- 6,620
5 others who appear to be clerks hold 1 share each, and all give their address as, 600 Richmond St., London, Ontario-------- 5

Total--------------------------------------------------------------- 6,625

John Gordon Thompson, 600 Richmond Street, London, Ontario, president and director, 1 share.
James David Good (same address as above) vice president and director, 1 share.
Walter Leeson Baragar (same address as above) secretary-treasurer.

Texas-Canadian Oil Corp. (file no. 319):
Statement dated June 15, 1936.
Capital $2,500,000, consisting of 2,500,000 shares, $1 par.
2,200,000 shares paid in full, Toronto office, address 610 Metropolitan Building, Toronto, Canada.
Field office—ARP—Texas, United States of America.
The list of stockholders consists of 12 pages of closely typed names, addresses, and shares held.
The following large American stockholders are listed:

P. D. Bowlen, 523 South Fannin St., Tyler, Texas-------------------------------- 343,408
O. M. Johnston, Muskegon Machine Co., Newburgh, N. Y.-------------------------------- 1,000
E. F. Seagram, in care of Frowdes, Ltd., Waterloo, Ontario------- 10,000
T. W. Seagram, care of Frowdes, Ltd., Waterloo, Ontario-------- 12,500
A number of other small blocks are held by Americans. Other large
blocks are held in the names of brokerage companies who give Canadian
addresses. Most of the small blocks are held by Canadians.

**London Investment Co., Ltd. (file no. 318):**
Statement dated May 26, 1936.
Capital Stock £1,000 and £70,000 debenture stock.
All issued and paid for.

<table>
<thead>
<tr>
<th>Address given</th>
<th>Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sherwood Johnston, Los Mochis, Sinaloa, Mexico, sugar planter</td>
<td>1</td>
</tr>
<tr>
<td>H. F. Jones, Los Mochis, Sinaloa, Mexico, manager</td>
<td>1</td>
</tr>
<tr>
<td>Nassau Trust, Nassau</td>
<td>992</td>
</tr>
<tr>
<td>A. S. Johnston, Nassau, housewife</td>
<td>4</td>
</tr>
<tr>
<td>2 other shares held by nominal stockholders</td>
<td>2</td>
</tr>
</tbody>
</table>

Total: 1,000

London Securities Trust of Nassau holds £70,000 debentures.

**British Investment Co., Ltd. (file no. 316):**
Statement of May 20, 1936.
Capital £1,000 of 1,000 shares common stock, £100,000 debenture stocks,
10,000 shares.
All issued and paid up.

<table>
<thead>
<tr>
<th>Shares</th>
<th>Common Debentures</th>
</tr>
</thead>
<tbody>
<tr>
<td>H. F. Jones, Los Mochis, Sinaloa, Mexico</td>
<td>1 10,000</td>
</tr>
<tr>
<td>United Sugar Co., S. A., Sinaloa, Mexico</td>
<td>996 10,000</td>
</tr>
</tbody>
</table>

Balance of common held by 3 Nassau residents.
See Charles Hudson, attorney, Chicago, Ill., who may have complete
information on this matter.

**Wilita, Ltd. (file no. 309):**
Statement dated April 7, 1937.
Capital $5,000, consisting of 50 shares, $100 par each.
All shares issued.

<table>
<thead>
<tr>
<th>Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chain Merchandising, Ltd., 119 Richmond St., Charlottetown, Prince Edward Island</td>
</tr>
<tr>
<td>Balance of shares held by law clerks at 300 St. James St., West Montreal</td>
</tr>
</tbody>
</table>

Total: 50

See William G. Taylor, accountant, at 40 Wall Street, New York City.
Lillian A. Burton, secretary, at 40 Wall Street, New York City.
They should have full knowledge of the facts in this case.

**Nassau Securities, Ltd. (file no. 306):**
Statement dated June 20, 1936.
Capital $50,000 of 500 shares, at $100 each.
Five shares issued.

<table>
<thead>
<tr>
<th>Shares</th>
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</thead>
<tbody>
<tr>
<td>Wallace Groves, 44 Wall St., New York City, president, treasurer, and director</td>
</tr>
<tr>
<td>Albert A. Sommerwerck, 44 Wall St., New York City, secretary and director</td>
</tr>
<tr>
<td>Balance of 3 shares held by qualifying Nassau residents, directors</td>
</tr>
</tbody>
</table>

Total: 5

**International, Ltd. (file no. 208):**
Statement dated December 29, 1936.
Capital $1,000, consisting of 20 shares.
All shares issued.

<table>
<thead>
<tr>
<th>Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>Balance of 5 shares held by Nassau residents to qualify corporation</td>
</tr>
</tbody>
</table>

Total: 20

See Thomas D. Sinclair, of Richmond, Va., who may know something
about this corporation.
Merchants Ltd. (file no. 297):
Capital £25,000, consisting of 25,000 shares, £1.
Shares issued, 1,000; paid for.
Herbert C. Wachs, Murfreesboro, Tenn. 300
Wm. Fullerton, Chilton, Wis. 250
H. M. Ruddick, Los Angeles, Calif. 100
G. Mason, Owlet, Wellsboro, Pa. 50
C. H. Reynolds, Greenville, Tenn. 300

Total 1,000

Overseas Service Co., Ltd. (file no. 295):
Letter of March 4, 1935.
Chester O. Swain, 30 Rockefeller Plaza, New York, president.
R. W. Gallagher (same address as above).
R. P. Resor (same address as above).
M. II. Eawes (same address as above), secretary.
This corporation was formed through Harold C. F. Mockridge, solicitor,
of 68 Yonge Street, Toronto, Canada.

West India Oil Company, S. A. (file no. 294):
Statement of April 29, 1936.
Capital $3,500,000, consisting of 35,000 shares.
25,003 shares issued.
W. T. Helm, Panama City, Panama, president and director 1
D. W. Ramsey, Jr., Panama City, Panama, vice president and director 1
C. C. Johnson, Panama City, Panama, secretary-treasurer and director 3

Total 25,003

A. A. Sobalvarro, Guatemala City, Guatemala, director.
See F. B. Bigelow and M. H. Eames, of 30 Rockefeller Plaza, New York.
They should have information concerning this corporation.

Transvaal Development Co., Ltd.:
Capital stock, $30,000.
Walter Siligman, broker, of 54 Wall Street, is listed as a stockholder.
Company appears to have been formed through use of Canadian attorney.

Wellington Fund, Ltd.:
Capital stock, $50,000, consisting of 500 shares.
Fifty shares issued.
W. L. Morgan, Medford Lakes, N. J. 40
H. W. McClurken, accountant, Packard Bldg., Philadelphia 1
H. F. Dungan, accountant, Packard Bldg., Philadelphia 1
D. B. Morgan, investments, Medford Lakes, N. J. 1
Chas. Cassil, Packard Bldg., clerk, Philadelphia 1

Total 50

Victoria Limited:
Ralph Knup, 35 William Street, Norwich, Conn., president.
Andre Charbin, 23 Amherst Road, Great Neck Estates, Long Island, treasurer and director.
E. G. Hillyar, 27 Scotland Road, Norwich, Conn.

California Texas Oil Co. Overseas, Ltd. (file no. 401):
Formed August 1936.
Capital stock, $100,000.
James Andrew Moffett, 130 E. Forty-third Street, New York City, director.
Efford Armone Beverly, 130 E. Forty-third Street, New York City, director.
William Kinnstradter, 130 E. Forty-third Street, New York City, director.
Richard Thurman McCoy, Westfield, N. J.
Joseph Vincent Murray, Mt. Vernon, N. Y.
British American Co., Ltd.:
Lawrence F. Lee, president.
L. C. Cortwright, vice president.
J. R. Anthony, secretary and treasurer.
R. M. Anderson, vice president and actuary.
B. R. Russell, assistant secretary.
On April 30, 1937, public notice appeared that Schick, Ltd., was struck off company register. Its affairs have been wound up, but Schick Industries, Ltd., Schick Shaver, Ltd., Schick International, Ltd., still in being.

British Hoffman, Ltd. (file no. 314):
Memorandum of association filed July 5, 1935.
Albert Frederick Hoffman, South Orange, N. J., manufacturing, 1 share.
Thomas Frazier Leach, Elizabeth, N. J., realtor, 1 share.
Balance of three shares held by Nassau residents.
Capital stock, $75,000, divided into 7,500 shares, at $10 each.

Frostello Company, Ltd. (file no. 178):
Resolution of July 11, 1935.
(Miss or Mrs.) M. M. Schafer of Wheeling, W. Va. was appointed to transfer the assets of this corporation to "Carmar Co., Ltd." another Bahamian Corporation formed August 24, 1929, with a capital stock of £20,500.
She was authorized to specifically withdraw all funds, securities of the company from the Royal Bank of Canada (701 Royal Bank Bldg.), Montreal, Quebec, and from Bankers Trust Co.

National Investments, Ltd. (file no. 327):
Memorandum of association dated September 27, 1935.
George Westinghouse, Jr., gave his address as Seabold post office, Seabold, Washington, United States of America.
On annual statement he gives his address as Saanichton post office, Saanichton, Vancouver Island, B. C.

Scanlon Estates, Ltd. (file no. 133):
Resolution of August 31, 1935.
Meeting held at Chicago, Illinois, August 31, 1935.
Helen S. Sample and J. Victor Jaeger authorized to liquidate assets of above company.
Peter Knotzer, assistant secretary of Scanlon Estates, Ltd., filed the resolution.

Antilles Development Co., Ltd. (file 93):
Resolution of October 10, 1935.
"Further resolved that all debts and obligations of and claims against the company be paid and that all assets of the company be distributed in accordance with such agreement and plan of reorganization as shall be finally worked out between this company, the Selkirk Co., Ltd., Elmherst Corporation, and Farchild Corporation (said last named three companies being respectively corporations duly organized and existing under and by virtue of the laws of the Dominion of Canada and the State of Delaware, United States of America, and filed with the Commissioner of Internal Revenue, Washington, D. C."
"Further resolved that Robert Lee Boyd of Wheeling, W. Va., be, and he hereby is appointed liquidator of the company * * * .”
Palmer & Series, counselors at law, 44 Cedar Street, formed the Coral Island Plantations, Ltd. I believe that they are one of the larger firms of attorneys in New York, who are advising clients on the use of foreign personal holding companies.

West India Chemicals, Ltd. (file 343):
Letter of February 27, 1936.
Capital £2,000, divided into 2,000 shares £1 each—

| Shares |
|-----------------|---|
| Cecile Mary Erickson, Nassau | 400 |
| Arloch Wentworth Erickson, Nassau | 400 |
| Josiah Mary Erickson, Nassau | 400 |
| Arloch Wentworth Erickson, Jr., Swampscott, Mass., United States of American, vice president | 400 |
| Douglas Erickson, Swampscott, Mass., vice president | 400 |
| Total | 2,000 |

570—37—pt. 1—6
West India General Store (file no. 344):
Letter of February 27, 1930.
Capital £1,000, divided 1,000 shares £1 each.
Same shareholders as above, each one holds 200 shares.

The Gulf Co., Ltd. (file no. 346):
Memorandum of association dated November 30, 1935.
Capital $330,000, divided into 3,500 shares, $100 each.
Karl Beebe Cortland Smith, architect of Englewood, New Jersey, United States of America, is one of the incorporators; holds 1 share.
The balance of four shares are held by Nassau residents.

Southern Securities, Ltd. (file no. 371):
Certificate of incorporation dated March 9, 1936.
Capital £60,000, divided into 6,000 shares of £10 each.
Henry Howard (consulting engineer), Paradise Road, Newport, R. I., president.
Alice Sturtevant Howard, Paradise Road, Newport, R. I., secretary, treasurer, and director.
Other stockholders are qualifying Nassau residents.

De Mille International, Ltd. (file no. 374):
Certificate of incorporation dated March 17, 1936.
Cynthia Hardy Beal, housewife.
Carl Hugh Beal, geologist.
Neil Steere McCarthy, lawyer.
Gave the British Colonial, Nassau as their address. They are not local residents. The hotel is closed now—cannot check their register.
The company was formed to distribute motion-picture films, etc., and they may be Americans. I believe, however, that this is a Canadian personal holding company based on other collateral facts.

Foley Securities Co. (file no. 213):
Resolution of April 23, 1936.
Increased capital from $50,000 to $150,000.
Lester W. Foley, Jacksonville, Fla., president.

Coupey, Ltd. (file no. 390):
Certificate of incorporation dated May 28, 1936.
Capital £3,000, divided into 300 shares of £10 each.
Eric Henri Coupey, broker, of 6 St. Lukes Place, New York, organizer.
Balance of four shares held by Nassau qualifying shareholders.

Eleuthera, Ltd. (file no. 477):
Letter of March 13, 1937.
Austin T. Levy, Harrisville, R. I., president and director.
June R. Levy, Harrisville, R. I., vice president and director.
Others are Nassau persons.

United Securities, Ltd. (file no. 380):
Annual statement dated April 27, 1937.
Capital stock £20,000, consisting of 2,000 shares of £10 each.
All shares issued.

<table>
<thead>
<tr>
<th>Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>360 Kyrie Bernice Peene Betz, Miami, Fla., director</td>
</tr>
<tr>
<td>557 Alfred Wavell Peene, Ontario, Canada, president</td>
</tr>
<tr>
<td>360 Reginald Hampt Nottle Peene, Ontario, Canada, vice president and director</td>
</tr>
<tr>
<td>360 David Dalkeith Peene, Ontario, Canada, secretary, treasurer, and director</td>
</tr>
<tr>
<td>360 Alberni Vida Hampt Peene, Ontario, Canada, director</td>
</tr>
</tbody>
</table>

Three shares held by Nassau individuals.

Bahama companies formed by International Corporation Co., Inc., as per report of April 22, 1937, Revenue Agent Albert Schwarts (lower New York division):
(a) Carribbean Trading Co., Ltd. (file no. 413):
   Formed through Kenneth Solomon on September 8, 1936.
   Capital stock £10,000.
(b) General Metal Powders, Ltd. (file no. 427):
   Formed through Kenneth Solomon on November 21, 1936.
   Capital stock £10,000.
   William E. Buckley, president and director.
   A. S. Forsyth, vice president and director.
   Robert H. Walsh, secretary, treasurer, and director.
TAX EVASION AND AVOIDANCE

(c) Sinclair Trading Co., Ltd. (file no. 412):
Formed through Kenneth Solomon on September 2, 1936.
Capital stock £1,000.

Large American stockholders of Texas-Canadian Oil Corporation

<table>
<thead>
<tr>
<th>Shares</th>
<th>Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>P. D. Bowlen, 523 South Fannin Street, Tyler, Tex</td>
<td>343,468</td>
</tr>
<tr>
<td>O. M. Johnston, Muskegon Machine Co., Newburgh, N. Y</td>
<td>1,000</td>
</tr>
<tr>
<td>E. F. Seagram, c/o Frowdes Ltd., Waterloo, Ontario</td>
<td>12,500</td>
</tr>
<tr>
<td>T. W. Seagram, c/o Frowdes Ltd., Waterloo, Ontario</td>
<td>12,500</td>
</tr>
</tbody>
</table>

A number of other small blocks are held by Americans. Other large blocks are held in the names of brokerage companies who give Canadian addresses. Most of the small blocks are held by Canadians.

London Investment Co., Ltd. (file no. 318):
Statement dated May 20, 1936.
Capital stock £1,000, and £70,000 debenture stock; all issued and paid for.

<table>
<thead>
<tr>
<th>Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sherwood Johnston (sugar planter) Los Mochis, Sinaloa, Mexico</td>
</tr>
<tr>
<td>H. F. Jones (manager) Los Mochis, Sinaloa, Mexico</td>
</tr>
<tr>
<td>Nassau Trust, Nassau</td>
</tr>
<tr>
<td>A. S. Johnston (housewife) Nassau</td>
</tr>
<tr>
<td>Two other shares held by nominal stockholders</td>
</tr>
</tbody>
</table>

Total | 1,000 |

London Securities Trust of Nassau holds £70,000 debenture stock.

Pasig Sugar Refining Co., Ltd. (file no. 470):
Letter of March 11, 1937.
Edward W. Freeman, New York, president and director.
Benjamin D. Holt, New York, secretary and director.
Charles S. Payson, New York, director.

Other qualifying directors are Nassau individuals.

Foreign Investments, Ltd. (file no. 476):
Letter of April 6, 1937.
Fannie F. Cross, New York, president and director.
Edward L. Hicks, Jr., New York, vice president and director.
Siebel C. Harris, New York, secretary and director.

Two other directors are Nassau individuals.

Sulane Co., Ltd. (file no. 493):
Letter of April 22, 1937.
Directors.—Hovey D. Carter, Old Marmoneck Road, Scarsdale, N. Y.; Susan J. Carter, Old Marmoneck Road, Scarsdale, N. Y.; John S. Keith, 76 Beaver Street, New York, N. Y.

Bahamas Investments, Ltd. (file no. 419):
Letter of October 8, 1936.

California Texas Oil Co. (file no. 397):
Annual statement dated July 9, 1936.
Amount of capital, $1,000,000, consisting of 10,000 shares at $100 each; all stock issued.

<table>
<thead>
<tr>
<th>Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>James Andrew Moffett, New York, director</td>
</tr>
<tr>
<td>Howard Marvin Herron, New York, president and director</td>
</tr>
<tr>
<td>Richard Howard Morrison, Dallas, Tex, director</td>
</tr>
<tr>
<td>Max Thornburg, Berkeley, Calif., director</td>
</tr>
<tr>
<td>Joseph Vincent Murray, Mount Vernon, N. Y., director</td>
</tr>
<tr>
<td>William Kunstadter, Grantwood, N. J, secretary and director</td>
</tr>
<tr>
<td>The Bahreim Petroleum Co., Ltd., New York City</td>
</tr>
</tbody>
</table>

Total | 10,000 |
TAX EVASION AND AVOIDANCE

Mines, Ltd. (file no. 396):
Annual statement dated July 6, 1936.
Capital stock, $530,000, consisting of 500,000 preferred shares at $1 each and 3,000,000 ordinary shares at 1 cent each; 500,000 preferred shares issued.

<table>
<thead>
<tr>
<th>Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sidney B. Wood, Jr., 76 Beaver Street, New York, vice president and treasurer.</td>
</tr>
<tr>
<td>Scott McLunahan, 40 Wall Street, New York.</td>
</tr>
<tr>
<td>David L. Landy, 302 Erie Co., Bank Building, Buffalo, N. Y., assistant treasurer and secretary.</td>
</tr>
<tr>
<td>Lindsey Hooper, 35 Congress Street, Boston, Mass.</td>
</tr>
<tr>
<td>Ewart L. Petley, 76 Beaver Street, New York, president.</td>
</tr>
<tr>
<td>R. O. Sweetey, 210 St. James Street West, Montreal, Canada.</td>
</tr>
</tbody>
</table>

Total: 11

Gunyan, Ltd. (file no. 396):
Letter of March 4, 1937.
Capital stock £1,000, consisting of 1,000 shares at £1 each; 5 shares issued.
Guy George Gabrielson (attorney), 70 Pine Street, New York, one share.
Balance of four shares held by four individuals with Canadian addresses.

East Landing, Ltd. (file no. 364):
Letter of March 12, 1936.
Sidney Alexander Mitchell (banker), secretary, treasurer, and director.
Mary Addison Mitchell (housewife), president and director.

The Sand Beach Co. (file no. 365):
Annual statement dated February 20, 1937.
Capital stock $45,000, consisting of 4,500 shares; 1,000 shares issued.
Joseph Schwerin, New York, president, treasurer, and director.
Clarence Maurice Schwerin, Jr., New York, N. Y., secretary and director.
Balance of directors are qualifying Nassau individuals.

Selected Golds, Ltd. (file no. 345):
Statement dated January 14, 1936.
Capital stock $1,015,000, divided into 10,000 shares preferred shares at $100 each and 15,000 ordinary shares at $1 each; 5,007 preferred issued and 7,518 ordinary issued.

<table>
<thead>
<tr>
<th>Companies register, Nassau, N. P., Bahamas Islands</th>
</tr>
</thead>
</table>

<table>
<thead>
<tr>
<th>File no.</th>
<th>Name</th>
<th>Attorney</th>
<th>Capital</th>
<th>Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>210</td>
<td>Nassau Marine &amp; Fuel Supply Co., Ltd.</td>
<td>H. P. Sands</td>
<td>(?)</td>
<td>Mar. 25, 1931</td>
</tr>
<tr>
<td>211</td>
<td>Overseas Central Trust Co., Ltd.</td>
<td>H. S. Malcolm</td>
<td>$1,500,000</td>
<td>Apr. 1, 1931</td>
</tr>
<tr>
<td>212</td>
<td>Lyford Cyn Co., Ltd.</td>
<td>Kenneth Solomon</td>
<td>$120,000</td>
<td>Apr. 13, 1931</td>
</tr>
<tr>
<td>213</td>
<td>Foley Securities Co., Ltd.</td>
<td>(?)</td>
<td>$30,000</td>
<td>May 14, 1931</td>
</tr>
<tr>
<td>214</td>
<td>Nassau Cyn Co., Ltd.</td>
<td>Kenneth Solomon</td>
<td>$200,000</td>
<td>May 28, 1931</td>
</tr>
<tr>
<td>215</td>
<td>International Investment Co., Ltd.</td>
<td>(?)</td>
<td>$1,500,000</td>
<td>Aug. 17, 1931</td>
</tr>
<tr>
<td>216</td>
<td>Teshquilt Corporation, Ltd.</td>
<td>(?)</td>
<td>$150,000</td>
<td>Sept. 9, 1931</td>
</tr>
<tr>
<td>217</td>
<td>Saratoga Holdin Co., Ltd.</td>
<td>(?)</td>
<td>$20,000</td>
<td>Oct. 23, 1931</td>
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<td>218</td>
<td>The Drapery Co., Ltd.</td>
<td>Kenneth Solomon</td>
<td>$5,000</td>
<td>Nov. 2, 1931</td>
</tr>
<tr>
<td>219</td>
<td>Diversified Investment Co., Ltd.</td>
<td>do</td>
<td>$50,000</td>
<td>Nov. 4, 1931</td>
</tr>
<tr>
<td>220</td>
<td>St. Lawrence Securities, Ltd.</td>
<td>do</td>
<td>$2,000</td>
<td>Nov. 12, 1931</td>
</tr>
<tr>
<td>221</td>
<td>Nassau-Jacksonville Steamship Co., Ltd.</td>
<td>A. F. Adderley</td>
<td>£10,000</td>
<td>Dec. 8, 1931</td>
</tr>
<tr>
<td>222</td>
<td>Standard Life Insurance Co., Ltd.</td>
<td>Kenneth Solomon</td>
<td>£50,000</td>
<td>Dec. 28, 1931</td>
</tr>
<tr>
<td>223</td>
<td>Shields International, Ltd.</td>
<td>do</td>
<td>£75,000</td>
<td>Dec. 28, 1931</td>
</tr>
<tr>
<td>224</td>
<td>Wasey International, Ltd.</td>
<td>do</td>
<td>£50,000</td>
<td>Do.</td>
</tr>
<tr>
<td>225</td>
<td>Prudent Industrial Life Insurance Co.,</td>
<td>K. W. Frickard</td>
<td>£2,000</td>
<td>Jan. 13, 1932</td>
</tr>
<tr>
<td></td>
<td>Ltd.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>226</td>
<td>The Cat Cyn Co., Ltd.</td>
<td>Kenneth Solomon</td>
<td>$200,000</td>
<td>Mar. 7, 1932</td>
</tr>
<tr>
<td>227</td>
<td>Kenbrook, Ltd.</td>
<td>do</td>
<td>$150,000</td>
<td>Apr. 18, 1932</td>
</tr>
<tr>
<td>228</td>
<td>Hopbrook, Ltd.</td>
<td>(?)</td>
<td>£10,000</td>
<td>Do.</td>
</tr>
<tr>
<td>229</td>
<td>Amsterdam Corporation, Ltd.</td>
<td>A. F. Adderley</td>
<td>£5,000</td>
<td>May 17, 1932</td>
</tr>
<tr>
<td>230</td>
<td>Nassau Enterprises, Ltd.</td>
<td>H. F. Sands</td>
<td>£5,000</td>
<td>May 21, 1932</td>
</tr>
<tr>
<td>231</td>
<td>The Bahamas Supply Co., Ltd.</td>
<td>do</td>
<td>£1,000</td>
<td>July 9, 1932</td>
</tr>
<tr>
<td>File no.</td>
<td>Name</td>
<td>Attorney</td>
<td>Capital</td>
<td>Date</td>
</tr>
<tr>
<td>---------</td>
<td>----------------------------------------------------------------------</td>
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</tr>
<tr>
<td>226</td>
<td>Kelly's Lumber Yard, Ltd.</td>
<td>Kenneth Solomon</td>
<td>£20,000</td>
<td>Sept. 19, 1932</td>
</tr>
<tr>
<td>227</td>
<td>Lumber Investments, Ltd.</td>
<td>H. S. Malcolm</td>
<td>£1,000</td>
<td>Sept. 19, 1932</td>
</tr>
<tr>
<td>228</td>
<td>Acadia Investments, Ltd.</td>
<td>do</td>
<td>£1,000</td>
<td>Do</td>
</tr>
<tr>
<td>229</td>
<td>Maratima Shipping Co., Ltd.</td>
<td>A. P. Pritchard</td>
<td>£2,000</td>
<td>Nov. 2, 1932</td>
</tr>
<tr>
<td>230</td>
<td>Nassau East India Co., Ltd.</td>
<td>Kenneth Solomon</td>
<td>£600</td>
<td>Nov. 19, 1933</td>
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<tr>
<td>231</td>
<td>Trade Winds, Ltd.</td>
<td>do</td>
<td>£10,000</td>
<td>Do</td>
</tr>
<tr>
<td>232</td>
<td>Trade Reserve, Ltd.</td>
<td>do</td>
<td>£100,000</td>
<td>Nov. 29, 1932</td>
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<tr>
<td>233</td>
<td>Nassau Finance Co., Ltd.</td>
<td>P. H. Christie</td>
<td>£20,000</td>
<td>Jan. 3, 1933</td>
</tr>
<tr>
<td>234</td>
<td>Ina K Co., Ltd.</td>
<td>do</td>
<td>£43,000</td>
<td>Feb. 13, 1933</td>
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<tr>
<td>235</td>
<td>The Catarina Shipping Co., Ltd.</td>
<td>do</td>
<td>£15,000</td>
<td>Feb. 27, 1933</td>
</tr>
<tr>
<td>236</td>
<td>Tatonic Transatlantic Corporation, Ltd</td>
<td>Kenneth Solomon</td>
<td>£302,000</td>
<td>Mar. 15, 1933</td>
</tr>
<tr>
<td>237</td>
<td>The Harborside Co., Ltd.</td>
<td>do</td>
<td>£300,000</td>
<td>Mar. 27, 1933</td>
</tr>
<tr>
<td>238</td>
<td>The Island Realty Co., Ltd.</td>
<td>do</td>
<td>£30,000</td>
<td>Do</td>
</tr>
<tr>
<td>239</td>
<td>The Nassau Yacht Club, Ltd.</td>
<td>Kenneth Solomon</td>
<td>£1,500</td>
<td>Apr. 1, 1933</td>
</tr>
<tr>
<td>240</td>
<td>Producers, Ltd.</td>
<td>£20,000</td>
<td>May 31, 1933</td>
<td></td>
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<tr>
<td>241</td>
<td>Nassau Magazine, Ltd.</td>
<td>£20,000</td>
<td>June 24, 1933</td>
<td></td>
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<tr>
<td>242</td>
<td>Macfarri Co., Ltd.</td>
<td>£2,500</td>
<td>June 30, 1933</td>
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<tr>
<td>243</td>
<td>South Coast Securities, Ltd.</td>
<td>(£)</td>
<td>(£)</td>
<td>(£)</td>
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<tr>
<td>244</td>
<td>Bahamas Mutual Insurance Co., Ltd.</td>
<td>(£)</td>
<td>(£)</td>
<td>(£)</td>
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<tr>
<td>245</td>
<td>British Bonded Warehouse Co., Ltd.</td>
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<td>(£)</td>
<td>(£)</td>
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<tr>
<td>246</td>
<td>Gulf Stream Securities, Ltd.</td>
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<td>(£)</td>
<td>(£)</td>
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<tr>
<td>247</td>
<td>Atlantic Securities, Ltd.</td>
<td>(£)</td>
<td>(£)</td>
<td>(£)</td>
</tr>
<tr>
<td>248</td>
<td>Schick, Ltd.</td>
<td>do</td>
<td>£2,000</td>
<td>Nov. 22, 1933</td>
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<tr>
<td>249</td>
<td>The Montague Park Racing Association, Ltd.</td>
<td>do</td>
<td>£3,000</td>
<td>Nov. 24, 1933</td>
</tr>
<tr>
<td>250</td>
<td>The Emerald Beach Bathing Club, Ltd.</td>
<td>do</td>
<td>£1,000</td>
<td>Do</td>
</tr>
<tr>
<td>251</td>
<td>The Abaco Lumber Co., Ltd.</td>
<td>Kenneth Solomon</td>
<td>£2,000</td>
<td>Nov. 27, 1933</td>
</tr>
<tr>
<td>252</td>
<td>The Island Fisheries Association, Ltd.</td>
<td>do</td>
<td>£50,000</td>
<td>Do</td>
</tr>
<tr>
<td>253</td>
<td>International Patents, Ltd.</td>
<td>£100,000</td>
<td>Do</td>
<td>(£)</td>
</tr>
<tr>
<td>254</td>
<td>Imperial Pictures Corporation (Nassau), Ltd.</td>
<td>(£)</td>
<td>(£)</td>
<td>(£)</td>
</tr>
<tr>
<td>255</td>
<td>Bahama’s Fish Market, Ltd.</td>
<td>(£)</td>
<td>(£)</td>
<td>(£)</td>
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<tr>
<td>256</td>
<td>S. American Securities Co., Ltd.</td>
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<td>(£)</td>
<td>(£)</td>
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<tr>
<td>257</td>
<td>Bahamas Realty Co., Ltd.</td>
<td>(£)</td>
<td>(£)</td>
<td>(£)</td>
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<tr>
<td>258</td>
<td>New Providence Co., Ltd.</td>
<td>(£)</td>
<td>(£)</td>
<td>(£)</td>
</tr>
<tr>
<td>259</td>
<td>Imperial Bottlers, Ltd.</td>
<td>(£)</td>
<td>(£)</td>
<td>(£)</td>
</tr>
<tr>
<td>260</td>
<td>British Tobacco Co., Ltd.</td>
<td>(£)</td>
<td>(£)</td>
<td>(£)</td>
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<tr>
<td>261</td>
<td>Rodney Corporation, Ltd.</td>
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<td>(£)</td>
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<tr>
<td>262</td>
<td>General Industries, Ltd.</td>
<td>(£)</td>
<td>(£)</td>
<td>(£)</td>
</tr>
<tr>
<td>263</td>
<td>Imperial Tobacco Co., Ltd.</td>
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<td>(£)</td>
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<tr>
<td>264</td>
<td>Southern Tobacco Co., Ltd.</td>
<td>(£)</td>
<td>(£)</td>
<td>(£)</td>
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<tr>
<td>265</td>
<td>J. S. Sands Lumber Co., Ltd.</td>
<td>Kenneth Solomon</td>
<td>£10,000</td>
<td>Mar. 31, 1934</td>
</tr>
<tr>
<td>266</td>
<td>Reynolds, Ltd.</td>
<td>(£)</td>
<td>(£)</td>
<td>(£)</td>
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<td>267</td>
<td>Nassau Commercial Co., Ltd.</td>
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<tr>
<td>268</td>
<td>Imperial Trust Co., Ltd.</td>
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<td>269</td>
<td>Richmill Bahamas Co., Ltd.</td>
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<tr>
<td>270</td>
<td>The English Bottling Co., Ltd.</td>
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<tr>
<td>271</td>
<td>The Southern Transportation Co.</td>
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<tr>
<td>272</td>
<td>Lucky Strike Mines, Ltd.</td>
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<td>(£)</td>
<td>(£)</td>
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<tr>
<td>273</td>
<td>Varilux Holding Corporation, Ltd.</td>
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<td>(£)</td>
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<tr>
<td>274</td>
<td>Consolidated Investments, Ltd.</td>
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<tr>
<td>275</td>
<td>Federated Investments, Ltd.</td>
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<td>(£)</td>
<td>(£)</td>
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<tr>
<td>276</td>
<td>The Island Investment Co., Ltd.</td>
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<td>(£)</td>
<td>(£)</td>
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<tr>
<td>277</td>
<td>Lucky Strike Mines, Ltd.</td>
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<td>(£)</td>
<td>(£)</td>
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<tr>
<td>278</td>
<td>Seminole Corporation, Ltd.</td>
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<td>(£)</td>
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<td>279</td>
<td>The New Colonial Hotel Co., Ltd.</td>
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<td>(£)</td>
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<td>280</td>
<td>Nassau Tours, Ltd.</td>
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<td>281</td>
<td>Roygo Co., Ltd.</td>
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<td>(£)</td>
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<tr>
<td>282</td>
<td>Kelley Shippe Co., Ltd.</td>
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<td>(£)</td>
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<td>283</td>
<td>Airdmore Investments, Ltd.</td>
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<td>284</td>
<td>Caribbean Securities, Ltd.</td>
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<td>285</td>
<td>Cordillers Investments, Ltd.</td>
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<td>(£)</td>
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<tr>
<td>286</td>
<td>Interisular Mills, Ltd.</td>
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<td>(£)</td>
</tr>
<tr>
<td>287</td>
<td>Ambah Co., Ltd.</td>
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<td>(£)</td>
<td>(£)</td>
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<tr>
<td>288</td>
<td>West Island Oil Co., Ltd.</td>
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<td>(£)</td>
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<tr>
<td>289</td>
<td>Overseas Service Co., Ltd.</td>
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<td>(£)</td>
<td>(£)</td>
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<tr>
<td>290</td>
<td>Geithner Investments, Ltd.</td>
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<td>(£)</td>
</tr>
<tr>
<td>291</td>
<td>Merchants, Ltd.</td>
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<td>(£)</td>
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<tr>
<td>292</td>
<td>International, Ltd.</td>
<td>(£)</td>
<td>(£)</td>
<td>(£)</td>
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<tr>
<td>293</td>
<td>Defence &amp; Co., Ltd.</td>
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<td>(£)</td>
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<tr>
<td>294</td>
<td>Ocean &amp; Lake View Co., Ltd.</td>
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<td>(£)</td>
<td>(£)</td>
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<tr>
<td>295</td>
<td>Seabury Co., Ltd.</td>
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<td>296</td>
<td>Lakhani Estates, Ltd.</td>
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<td>(£)</td>
<td>(£)</td>
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<tr>
<td>297</td>
<td>Dimitri Martin &amp; Romantch Club, Ltd.</td>
<td>(£)</td>
<td>(£)</td>
<td>(£)</td>
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<td>298</td>
<td>North American, Ltd.</td>
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<td>(£)</td>
<td>(£)</td>
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<td>299</td>
<td>Nassau Securities Co., Ltd.</td>
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<tr>
<td>300</td>
<td>Adjusting Bureau, Ltd.</td>
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<td>301</td>
<td>Bahamas Trust Co., Ltd.</td>
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<td>(£)</td>
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<tr>
<td>302</td>
<td>Wills, Ltd.</td>
<td>(£)</td>
<td>(£)</td>
<td>(£)</td>
</tr>
<tr>
<td>303</td>
<td>Dome, Ltd.</td>
<td>(£)</td>
<td>(£)</td>
<td>(£)</td>
</tr>
<tr>
<td>File no.</td>
<td>Name</td>
<td>Attorney</td>
<td>Capital</td>
<td>Date</td>
</tr>
<tr>
<td>---------</td>
<td>------</td>
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<td>311</td>
<td>Cagenay, Ltd</td>
<td>(£)</td>
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<td>Nasson, Ltd</td>
<td>(£)</td>
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<td>Royal Investment Trust, Ltd</td>
<td>(£)</td>
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<td>June 20, 1935</td>
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<td>Hammons &amp; Co., Ltd</td>
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<td>Tankers, Ltd</td>
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<td>Midway, Ltd</td>
<td>(£)</td>
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<td>Aug. 15, 1935</td>
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<td>London Investment Co., Ltd</td>
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<td>Aug. 15, 1935</td>
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<td>Aug. 23, 1935</td>
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<td>Marine Import &amp; Export Co., Ltd</td>
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<td>Pioneer Petroleum &amp; Trading Co., Ltd</td>
<td>(£)</td>
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<td>Rauchlin, Ltd</td>
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<td>Nassoak, Ltd</td>
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<td>Robertson &amp; Symonette, Ltd</td>
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<td>(£)</td>
<td>£100,000</td>
<td>Nov. 19, 1935</td>
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<td>338</td>
<td>Colombo &amp; Co., Ltd</td>
<td>(£)</td>
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<td>Investments, Ltd</td>
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<td>Nov. 27, 1935</td>
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<td>St. Alban's Park, Ltd</td>
<td>(£)</td>
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<td>(£)</td>
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<td>West India General Store, Ltd</td>
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<td>(£)</td>
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<td>Schick Industries, Ltd</td>
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<td>Schick Shaver, Ltd</td>
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<td>Schick International, Ltd</td>
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<td>Do.</td>
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<td>North Atlantic Insurance Co., Ltd</td>
<td>(£)</td>
<td>£17,000</td>
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<td>Dec. 28, 1935</td>
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<td>T. P. Osborn, Ltd</td>
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<td>Dec. 30, 1935</td>
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<td>The Southern Co., Ltd</td>
<td>(£)</td>
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<td>Jan. 9, 1936</td>
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<td>The City Meat Market, Ltd</td>
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<td>International Ins. Co., Ltd</td>
<td>(£)</td>
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<td>Jan. 19, 1936</td>
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<td>East Trading, Ltd</td>
<td>(£)</td>
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<td>Jan. 24, 1936</td>
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<td>The Sand Beach Co., Ltd</td>
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<td>366</td>
<td>International (Nassau) Ltd</td>
<td>(£)</td>
<td>£30,000</td>
<td>Feb. 11, 1936</td>
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<td>Bahamas Co., Ltd</td>
<td>(£)</td>
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<td>Feb. 25, 1936</td>
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<td>Canadian Capital Corporation, Ltd</td>
<td>(£)</td>
<td>£300,000</td>
<td>Feb. 21, 1936</td>
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<td>369</td>
<td>Victoria Investments, Ltd</td>
<td>(£)</td>
<td>£25,000</td>
<td>Feb. 23, 1936</td>
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<td>The Queen Street Co., Ltd</td>
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<td>Mar. 5, 1936</td>
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<td>Western Securities, Ltd</td>
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<td>Mar. 9, 1936</td>
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<td>Inter Oils, Ltd.</td>
<td>(£)</td>
<td>£20,000</td>
<td>Mar. 10, 1936</td>
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<td>Inter Oils Corporation, Ltd</td>
<td>(£)</td>
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<td>Mar. 14, 1936</td>
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<td>Bahamas Provident Ins. Co., Ltd</td>
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<td>£25,000</td>
<td>Mar. 19, 1936</td>
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<td>Shaver, Ltd</td>
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<td>£25,000</td>
<td>Mar. 25, 1936</td>
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<td>Mar. 30, 1936</td>
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<td>Gunyon, Ltd</td>
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<td>Edward, Ltd</td>
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<td>May 18, 1936</td>
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<td>(£)</td>
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<td>File no.</td>
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<td>Attorney</td>
<td>Capital</td>
<td>Date</td>
</tr>
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<td>Panama Co., Ltd</td>
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<td>June 20, 1935</td>
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<td>Charles Alexander</td>
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<td>June 20, 1935</td>
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<td>Mines, Ltd</td>
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<td>June 20, 1935</td>
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<td>Colombia Texas Oil Co., Ltd</td>
<td>Godfrey Higgs</td>
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<td>July 17, 1935</td>
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<td>Godfrey Higgs</td>
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<td>July 12, 1935</td>
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<td>California Texas Oil Co. (Overseas)</td>
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<td>July 24, 1935</td>
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<td>July 24, 1935</td>
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<td>July 24, 1935</td>
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<td>405</td>
<td>Victoria, Ltd</td>
<td>do</td>
<td>$25,000</td>
<td>July 24, 1935</td>
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<td>The Transportation Co., Ltd</td>
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<td>July 24, 1935</td>
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<td>July 24, 1935</td>
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<td>July 24, 1935</td>
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<td>Godfrey Higgs</td>
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<td>Aug. 21, 1935</td>
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<td>Sept. 2, 1935</td>
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<td>Sept. 17, 1935</td>
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<td>Kenneth Solomon</td>
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<td>H. S. Malcolm</td>
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<td>Mahogo, Ltd</td>
<td>do</td>
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<td>Nov. 2, 1935</td>
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<td>The Golf Course, Ltd</td>
<td>do</td>
<td>$500,000</td>
<td>Nov. 2, 1935</td>
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<td>Nov. 2, 1935</td>
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<td>Co., Ltd</td>
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<td>$100,000</td>
<td>Nov. 2, 1935</td>
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<td>Cat Cay Manor, Ltd</td>
<td>do</td>
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<td>Nov. 18, 1935</td>
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<td>General Metal Powders, Ltd</td>
<td>do</td>
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<td>Nov. 21, 1935</td>
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<td>Berob Co., Ltd</td>
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<td>Nov. 21, 1935</td>
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<td>Nov. 21, 1935</td>
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<td>Bahamas Airways, Ltd</td>
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<td>Dec. 1, 1935</td>
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<td>431</td>
<td>Asphalt International, Ltd</td>
<td>Kenneth Solomon</td>
<td>$5,000</td>
<td>Dec. 1, 1935</td>
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<td>H. P. Sands</td>
<td>$100,000</td>
<td>Dec. 12, 1935</td>
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<td>Kelsey Trading Co., Ltd</td>
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<td>$25,000</td>
<td>Dec. 12, 1935</td>
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<td>Bahamas Corn Products, Ltd</td>
<td>A. F. Adderley</td>
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<td>Dec. 15, 1935</td>
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<td>The Ruby Shipping Co., Ltd</td>
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<td>Jan. 2, 1936</td>
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<td>do</td>
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<td>H. P. Sands</td>
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<td>Jan. 2, 1936</td>
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<td>Kent Investment, Ltd</td>
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<td>Jan. 2, 1936</td>
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<td>Asson Co., Ltd</td>
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<td>Jan. 9, 1936</td>
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<td>455</td>
<td>Bahamas Land Syndicate, Ltd</td>
<td>do</td>
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<td>Jan. 9, 1936</td>
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<td>The Medway Estates, Ltd</td>
<td>Kenneth Solomon</td>
<td>$20,000</td>
<td>Jan. 9, 1936</td>
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<td>Jan. 9, 1936</td>
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<td>Nassau Holdings, Ltd</td>
<td>do</td>
<td>$20,000</td>
<td>Jan. 9, 1936</td>
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<td>$20,000</td>
<td>Jan. 9, 1936</td>
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<td>A. F. Adderley</td>
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<td>do</td>
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<td>do</td>
<td>$100,000</td>
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<td>Oregon, Ltd</td>
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<td>$1,000</td>
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<td>Name</td>
<td>Attorney</td>
<td>Capital</td>
<td>Date</td>
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<td>Mar. 10, 1937</td>
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<td>Do.</td>
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<td>Do.</td>
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<td>do</td>
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<td>Godfrey Higgs</td>
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<td>480</td>
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<td>do</td>
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<td>Mar. 27, 1937</td>
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<td>Kenneth Solomon</td>
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<td>$5,000</td>
<td>Do.</td>
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<td>Island Development Co., Ltd.</td>
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<td>Apr. 5, 1937</td>
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<td>490</td>
<td>Andrin Valley Plantation</td>
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<td>$20,000</td>
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<td>495</td>
<td>Chipper Orange Co., Ltd.</td>
<td>A. F. Adderley</td>
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<td>Curry Investments, Ltd.</td>
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<td>497</td>
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<td>do</td>
<td>$20,000</td>
<td>Apr. 29, 1937</td>
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<td>499</td>
<td>Ked Co., Ltd.</td>
<td>H. P. Sands</td>
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<td>500</td>
<td>The H. H. Co., Ltd.</td>
<td>Kenneth Solomon</td>
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<td>May 1, 1937</td>
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TAX EVASION AND AVOIDANCE

TUESDAY, JUNE 22, 1937

JOINT COMMITTEE ON TAX EVASION AND AVOIDANCE, Washington, D.C.

The joint committee met, pursuant to adjournment, in the hearing room of the Committee on Ways and Means in the New House Office Building at 10 a.m., Hon. Robert L. Doughton (chairman) presiding.

The CHAIRMAN. The committee will be in order. Dr. Magill, we are ready to proceed. Who is your first witness?

Under Secretary MAGILL. Mr. Chairman, and members of the committee, as you recall on Friday we dealt with the device of the foreign personal holding company, and what we tried to bring out at that time was the utility of this device as a means of siphoning assets and income out of the United States into foreign countries where there are no income taxes, or where such taxes are low.

The result so far as we are concerned is to greatly increase the difficulty first of obtaining any information respecting the taxpayer's actual income, and secondly in collecting the tax once we ascertain what his income actually was. Because we cannot sue for taxes in the foreign country, in which these companies are organized, our action must be brought against the individual here; and if, as seemed to be true in the DeRonde case, for example, the individual has no assets here and his assets are simply in the Bahamas, the difficulties of tax collection may be very great.

As we said to you on Friday, the reason that relatively few cases were presented to you was twofold. In the first place we are anxious to focus attention on the device that we are seeking to correct; that is, in this case, on the foreign personal holding company; and we were trying to show you the different ways in which that company might be used, by illustrations. We did not multiply the illustrations, because we thought we made the point sufficiently with those which we had.

In the second place, as you can appreciate, it is very difficult to sift these cases down to the bottom, particularly when they involve foreign companies. In fairness to the taxpayer, it is our desire to present no cases which we have not thoroughly examined and thoroughly analyzed. We have plenty of partly completed cases, but we want to give you only those which we have gone through fully.

Mr. TREADWAY. May I interrupt you, Mr. Magill?

Under Secretary MAGILL. Yes.

The CHAIRMAN. Mr. Treadway.

Mr. TREADWAY. That is, you are saying you have numerous instances of other methods of tax avoidance than this particular one?

Under Secretary MAGILL. Yes, sir.
Mr. Treadway. How are you selecting the names that you present to the committee? I think the press announced that you had several hundred names available. In what manner are these names brought before us?

Under Secretary Magill. I am glad to answer that. So far as we are concerned, we have no list of names which we have presented or planned to present. What we are concentrating on, as I have indicated, is the devices which we want to correct—these loopholes—and, as I said to you last week, the reason for presenting this material at this time is that we hope that these loopholes may be corrected at this session of Congress, so that we may not have this leakage of revenue not only in later years but in 1937 and 1938.

Now, as to how we pick the particular cases. As I told you on Thursday, when we discovered this discrepancy in revenue about which the Secretary spoke, the Bureau of Internal Revenue sent out communications to all of its men in the field asking them to make a quick examination, as rapidly as they could, and advise us of devices which were being used for the avoidance of taxes, or loopholes which appeared to exist in the 1936 or prior laws. We made no selection of cases except that. That is, we asked these men in the field to send us what they had.

Now, what we are doing at present is going over that material and, as rapidly as it can be analyzed and verified and checked through, we are giving you what we have got.

Mr. Treadway. Dr. Magill, in the President's message, in Mr. Morgenthau's letter to the President, in your testimony the other day, and just now, there has been used the expression "discovered discrepancies." Your revenue receipts in March were very much less than the estimates that the administration had previously made. Is that correct?

Under Secretary Magill. The receipts were less than the estimates; yes.

Mr. Treadway. Now, are you not giving us to understand that just at that time you found these discrepancies, whereas a book you published shows that you knew of these loopholes years ago? It cannot be that these millions of dollars that you were short of your estimates in March were the result of your suddenly finding these loopholes, because you wrote about that thing several years ago. Now, do not mislead the public nor us. I do not say that these loopholes do not exist, but I do not believe you discovered them in March.

Under Secretary Magill. Of course, there are two points you are making there; first, with respect to the loopholes; and secondly, with respect to the book. Let us take the first, because I suppose that is the only one you are much interested in.

Mr. Treadway. Oh, no. That is a very valuable book.

Under Secretary Magill. I do not know about that.

Mr. Treadway. Two of them.

Under Secretary Magill. As to the discovery, as I told you on Thursday, and as you are aware, we have attempted to be completely frank with you at all times in respect to this investigation. As I told you on Thursday, most of these matters which we are presenting to you are not particularly new.
Mr. TREADWAY. I am glad to have you admit that.
Mr. VINSON. He has already admitted that.
Mr. COOPER. There has not been any confusion in the mind of anyone but yourself.
Mr. TREADWAY. Mine is a very poor mind, but I do not want you criticizing it.
Mr. COOPER. I will do as I please.
Mr. TREADWAY. Well, so will I do as I please. I am not sitting here just like a bump on a log to have you tell me what to do.
[The gavel fell.]
Mr. TREADWAY. Rap all you have a mind to, Mr. Chairman. I do not care how much you rap.
The CHAIRMAN. The thing started off very badly. A suggestion was made that the witness was trying to mislead the committee.
Mr. TREADWAY. Oh, well, I do not care whether you like it or not.
Mr. VINSON. It will get his name in the paper. That is all he is after.
Mr. TREADWAY. To thunder with your papers—tear them up.
Mr. COOPER. That is all he is after.
Mr. TREADWAY. Now, if you are going to have any muss, I am with you. I am only backing up what Senator La Follette did last week, in asking where these names came from and who selected them. Now, if that is not a fair inquiry, call me down for it.
The CHAIRMAN. Nobody is going to call you down, Mr. Treadway, but the Chair will make this remark—
Mr. TREADWAY. I do not care for the personal remarks of certain members of the committee.
The CHAIRMAN. Can you not wait?
Mr. TREADWAY. Yes.
The CHAIRMAN. I will wait until you get through.
Mr. TREADWAY. I am all through.
The CHAIRMAN. I would like to make this observation, that nothing that has ever occurred, so far as I know, since Dr. Magill has been connected with the Treasury Department, would justify anyone in even insinuating, much less stating, that he was trying to mislead the committee. I feel that Mr. Treadway ought to withdraw that statement.
Mr. TREADWAY. Why, Mr. Chairman, Dr. Magill knows what my opinion of him is. I have been more complimentary of him than any other man connected with the administration, and I do not hesitate to repeat it. I was very sorry when he left the administration, because I felt he was the one competent person that came up here from the departments, and I have not had any reason during this hearing to change that opinion of Dr. Magill. He did use the words “discovered discrepancy”, and a certain member of the committee took offense at my bringing up the question of discovering the discrepancy, which he now says and has previously said was not a new discovery. Now, on the other hand, if I have said anything disagreeable to Dr. Magill, I have not intentionally done so, and I am only too glad to withdraw it. But I do think we are entitled to the information I am seeking.
The CHAIRMAN. Proceed. You made the suggestion that he was misleading the committee.
Mr. Treadway. I had no intention of making that remark; I did that possibly under the heat of interruption by certain members of the committee.

The Chairman. Very well. Proceed. We will try to get down to normal temperature.

Under Secretary Magill. I think we understand each other.

Mr. Treadway. Absolutely, Doctor; you and I do. Perhaps some of the others do not.

Under Secretary Magill. Now, do you understand, or should I say anything more to you respecting the way in which this material has been brought together? Because, if there is anything else I can tell you, I will be only too glad to do it.

Mr. Cooper. Your book.

Mr. Treadway. That is perfectly satisfactory. As I understand you, the field agents were asked to find why there was such a marked difference in the estimates of the Department and the actual receipts in March.

Under Secretary Magill. That is true.

Mr. Treadway. But, among other things, they told you that there were either incorporations or there were foreign holding companies, and various other devices, such as incorporated yachts, and so forth.

Under Secretary Magill. The whole story is this: When there was this discrepancy in the revenue, it is obvious to anyone that the discrepancy might have been due to a miscalculation of the estimates themselves, or it might have been due to increased use of loopholes which existed in the law, or to the development of some new loopholes. I knew, as we all do, that the law had been changed last year, and it was possible that some amendments had been made at that time, or some practices worked out, which were causing the loss of revenue.

Mr. Vinson. Mr. Chairman.

The Chairman. Mr. Vinson.

Mr. Vinson. Mr. Magill, you have had Bahama corporations for many years?

Under Secretary Magill. Not for many years; no, sir. I mean, there have been such things, but their use as a matter of tax avoidance I think goes back only a few years.

Mr. Vinson. My statement is you have had Bahama corporations for many years, have you not?

Under Secretary Magill. Oh, yes; there have been such corporations.

Mr. Vinson. And that corporate device has been used in less degree in past years probably for tax evasion?

Under Secretary Magill. Yes, sir.

Mr. Vinson. But within the last year you noticed on your investigation that there was an increased use of the Bahama corporation?

Under Secretary Magill. Right.

Mr. Vinson. You listed 122 corporation that had been formed in the Bahamas—within what period?

Under Secretary Magill. I believe 2 years.

Mr. Vinson. Within 2 years?

Under Secretary Magill. Two years and four months.
Mr. Vinson. Statements have been made that the particular cases to which reference has been made would not total up in tax evasion the amount of money that would evidence the shortage in estimate of tax yield. Do you know, or can you know without a most exhaustive investigation, just how many more millions of dollars of taxes have been avoided through the setting up of these 122 corporations in the Bahamas?

Under Secretary Magill. I do not think there is any way to know because, as I have indicated to you, we presented to you the cases which we completely investigated, and those were comparatively few out of the 122.

Mr. Vinson. Those were illustrative?

Under Secretary Magill. Now, without knowing what the assets of these companies are, and what their income is, it would, of course, be quite impossible to tell how much tax has been avoided in that way.

Mr. Vinson. For instance, you might have a case where the incorporators were all natives, with a stipulated or stated capitalization of $10,000, that might have $50,000,000 in it?

Under Secretary Magill. That is quite possible. There is literally no way of telling, unless you can compel the American stockholder under penalty to disclose what his interest in these companies is, and what his income from those sources has been.

Mr. Treadway. Mr. Chairman.

The Chairman. Mr. Treadway.

Mr. Treadway. Have I understood you to say, Mr. Magill, that you expect to present suggestions for legislation that will compel that disclosure?

Under Secretary Magill. Our thought, so far as this first point is concerned, is this: My reason for speaking at all this morning is simply to summarize the ground we have been over, and try to make it clear how our minds were running on it. What we have had in mind is this: As you may have noticed in some of the Sunday papers, the British and the Canadians have confronted this same problem. This tax evasion is nothing unique in the United States. They have it elsewhere. Both of them have met it in substantially the same way.

You will find that Mr. Neville Chamberlain, now Prime Minister, presented this whole thing to the House of Commons about a year ago, except that he was talking about British taxpayers, and we are talking about Americans.

Now, the way that they have both used is this: To provide under penalty that the British individual taxpayer or the Canadian taxpayer shall disclose his stock ownership in personal holding companies, defining them, perhaps similarly to the way they are defined now in section 351, and then that this individual stockholder shall be liable to the tax upon his pro-rata share of the income of such companies.

They regard that as fair, and I do, too, for the reason that since these companies appear to be set up merely for purposes of evasion—there is no other apparent reason why you should incorporate a personal holding company in the Bahamas or in some other country—that it is fair to treat them as essentially a nullity for the purposes of our tax laws, as a matter of form and not of substance, and that we
will look through them and tax the true income of the individual who has set them up; so our proposal for legislation would be along that line.

Mr. Cooper. Mr. Chairman.

The Chairman. Mr. Cooper.

Mr. Cooper. In other words, from a practical standpoint, here is the individual taxpayer, and here is a corporation that he owns. In other words, treat him and his individually owned and controlled corporation on the same status?

Under Secretary Magill. That is right; treat them as one for this purpose.

Now, we intend to develop this morning for the committee the second of these devices which were mentioned in the Secretary's statement; that is, the device for the foreign insurance company.

Mr. Treadway. Before you enter on that, Mr. Chairman, may I ask one other question?

The Chairman. Mr. Treadway.

Mr. Treadway. Either you or Mr. Morgenthau or the President—it is all one—lists eight or nine different methods of tax avoidance. The resolution under which we are acting, I think, extends to other forms of avoidance of taxes. Are you expecting to show the committee in the course of these hearings any other methods than those which appear in that list?

Under Secretary Magill. We are at the service of the committee in this matter, under the resolution. The information which we have presented, collected, and are now organizing as fast as we can has to do with these 8 or 10 devices which were listed in the Secretary's letter, and our intention is to present those matters. Now, if the committee should ask us to present something on some other point, no doubt we would try to obtain the information.

Mr. Treadway. In that way probably other names would be brought to your attention, than those you you are going to suggest to the committee?

Under Secretary Magill. That is quite possible; yes. As I have said—I do not think I can repeat it too often—we are not interested in names. What we are interested in is trying to stop this loss of revenue, the leakage of revenue.

Mr. Treadway. There are a few names that some of us are interested in, that perhaps will not come to the surface unless they are brought out other than through the Treasury witnesses.

Under Secretary Magill. I can only say that if the committee has in mind some devices which are to be used in this way, or individuals who are using devices of this character, let us know, and we will go into them.

Mr. Treadway. Thank you.

Mr. Vinson. Mr. Chairman.

The Chairman. Mr. Vinson.

Mr. Vinson. I am reading from an exhibit which you filed on June 18, in regard to the Bahama corporations. It seems that corporation, file no. 358, has a date of birth in the Bahamas of January 9, 1936. Then at the end, May 1, 1937, the file number is 500. Would that indicate that there had been 143 corporations formed in the Bahamas between those dates?
Under Secretary Magill. I do not know personally about that discrepancy, because I did not make the investigation. As we told you, or as Mr. Irey told you the other day, we attempted to take out any corporations which appeared to be organized for ordinary business or mercantile purposes.

Mr. Vinson. I see.

Under Secretary Magill. And that probably explains the difference.

Mr. Vinson. Yes. The 122 corporations that we have been hearing about are those that apparently were not organized for legitimate corporate business.

Under Secretary Magill. So far as we get them simply from the records.

Mr. Vinson. I see.

Under Secretary Magill. I may say again, if you bring the individuals who organized those corporations in here, you might discover that some of those corporations were organized for perfectly legitimate purposes. We have no way of knowing. All we can go by is the record, because we have no reports at present of the stockholdings of individuals or of the assets concentrated in these companies.

Mr. Treadway. Will the gentleman yield?

Mr. Vinson. Yes.

Mr. Treadway. What were the numbers?

Mr. Vinson. From 358 to 500, or about 143.

Mr. Treadway. About 150 corporations, in between those numbers?

Now, are these only American corporations?

Under Secretary Magill. I believe, the American and Canadian. Is that not true?

Mr. Brenner (Special Agent, Intelligence Unit, Bureau of Internal Revenue). Yes.

Mr. Treadway. So that there might be some Canadian companies there that had no connection with any stockholders in this country. Is that right?

Under Secretary Magill. That is my understanding; yes, sir.

Mr. Treadway. Thank you.

Under Secretary Magill. This foreign insurance company matter will be presented by Mr. Mason B. Leming, who is an attorney in the General Counsel's Office of the Treasury Department, and is now General Assistant to the Chief Counsel to the Bureau of Internal Revenue. He has gone into the matter very thoroughly and has here all of the exhibits and other papers that have to do with this particular device, as he will, I think, bring out to you. So far as we are aware at present, this device is used by relatively few people. On the other hand it appears to be capable of considerable extension, and for that reason it seems desirable to stop it as a device before it becomes commonly widespread. Mr. Leming.

The Chairman. Please give your name and address to the stenographer, and the capacity in which you appear before the committee.

STATEMENT OF MASON B. LEMING, SPECIAL ATTORNEY, GENERAL COUNSEL'S OFFICE, BUREAU OF INTERNAL REVENUE

Mr. Leming. I am an attorney, as Dr. Magill says, in the office of the General Counsel for the Treasury Department, and I am a gen-
eral assistant to the Chief Counsel for the Bureau of Internal Revenue.

The Chairman. Have you prepared a statement, Mr. Leming, that you would like to present to the committee without interruption?

Mr. Leming. No; I haven't, if you please, Mr. Chairman.

The Chairman. Do you object to being interrupted as you go along, or do you prefer to make your main statement without interruption?

Mr. Leming. It is immaterial.

The Chairman. All right; you may proceed.

Mr. Leming. On the matter of my voice, I hope it improves as I go along. First, I usually have the same complaint that is made of any witness—he doesn't talk loud enough—but I trust as I work it it will get better.

Now, before proceeding with the detailed description of the particular device I would like to approach it in this way: I would like to read section 23 of the Revenue Act of 1936, a provision which is similar in prior acts. I think in proceeding this way we can get a better idea of what I am trying to do, and you may be able to follow me better.

Section 23 is captioned, "Deductions From Gross Income", and quoting the first part of that section:

"In computing net income there shall be allowed as deductions—then we pass subparagraph (a) and go to subparagraph (b), which reads this way:

Interest: All interest paid or accrued within the taxable year on indebtedness, except on indebtedness incurred or continued to purchase or carry obligations (other than the obligations of the United States issued after September 24, 1917, and originally subscribed for by the taxpayer), the Interest upon which is wholly exempt from the taxes imposed by this title.

In short, section 23 (b) simply allows as a deduction from your gross income all of the interest you pay in the taxable year. Now that provision has remained more or less constant. There can't be, it seems, a great deal of difference of opinion as to what that provision of the law means. I take it that when Congress enacted that provision in the 1936 act it had in mind interest actually paid or accrued. It had in mind that there was an indebtedness upon which interest had to be paid.

Probably this item of interest is closer to most of us than any other item. The man who is buying a home must pay interest upon the mortgage upon that home, and he certainly is entitled under the law to deduct that interest. So everybody knows what we mean when we talk about an interest deduction. My excuse for going into this in this more or less elementary way, I hope I will show you a little later—is because I want to bring out here as we approach this particular device that Congress had some real purpose in mind in the enactment of that section. That was not a trick or device to entrap any taxpayer. On the other hand, Congress must have had in mind he must have an indebtedness—not a fictitious indebtedness but an actual, a real obligation to pay money borrowed or money that he owes.

Now, proceeding just a little further in that way, if one has an income of say $150,000, upon which, in the absence of some deduction, he must pay a tax, then he has a substantial tax to pay under present
rates as well as in the past. But if he had an interest deduction of $150,000 he would not pay any tax, because under the law he would be entitled to deduct that from his income.

This device was used in the year 1936, as disclosed by at least two 1936 returns and by at least one other—or rather I will say one other started to use it and went through the device, but did not take the deduction.

Now, I have this further thought about this device, and that is this, that it is not so much the device itself that we have spoken of as a foreign insurance device, but it is a device of the whole system. Congress had certain intent when it passed this particular act, this particular subdivision, as it did with respect to every other subdivision and section in the law.

Now, we get to this point, we get into litigation, for instance, and the litigants or, perchance the Government, want to find out what the intention of Congress was, and we go about that in all the ways we can to get the evidence of that intention, and once the intention is definitely established, that prevails. So throughout this whole system we have, in a way, an intention of Congress, perchance, in some instances an intention of the taxpayer, and the clash.

Now, it has been said in the press fairly recently, in quoting some citizen of prominence—and I am not trying to quote with precision, and bear in mind I am quoting it only because of the point I am trying to make—that Congress, in effect, did not know how to pass a law which would get the revenue. Now that leads us right into the heart of this thing: What did Congress intend with respect to the particular sections of the law that it has enacted, and will an intention to thwart the congressional intent prevail? Now, that is just part of the underlying thought that rides through this device, and I think through all of them.

Going back now to the example I indicated, a man with a net income without deductions of $150,000, and in the absence of a deduction, he pays the tax—starting from that point I will try to state in brief outline and a little later with more detail the plan of operation of this particular scheme. In order to get an indebtedness which will produce a sufficient interest to wipe out the $150,000 of income you can, if your interest is to be paid at the rate, say of 5 percent, divide that net income by 5 and multiply it by 100, and you get an amount of indebtedness that will produce enough interest to wipe out your income. That was the system, the starting point of this foreign insurance device, and Mr. Baber, of New York City, and incidentally not a citizen of this country——

Mr. VINSON. What are his initials?
Mr. LEMING. W. C.—Walter C.
Mr. VINSON. And what is his last name, again?
Mr. LEMING. Baber.
Mr. VINSON. Of New York City?
Mr. LEMING. Yes.

Senator WALSH. A citizen of what country?
Mr. LEMING. A citizen of Great Britain. There was organized at his instance in the Bahaman Islands a Nassau corporation known as the Standard Life Insurance Co., Ltd. That organization of the company took place, I believe, in about November 1931. It stayed
in that status, then, until December 1932, when the first meeting of
the directors was held, and it was organized by the election of officers.
Five shares of its stock were held by the incorporators in the
Bahaman Islands, and five shares were held by W. C. Baber. The
total number of shares, I believe, was 5,000, authorized 5,000, and
the par value of those shares was $10 a share. There were only 10
shares subscribed for and those 10 shares, amounting to a par value of
$100, were not paid for.
Mr. Cooper. Mr. Chairman, would it be of any interest to give
the names of these incorporators?
Mr. Lemin. I will be glad to do that. The incorporators were
Kenneth Solomon, Stafford Sands, Carl Elmer Robertson, Doris
Louize Barlow, Alice Maude Farrington, all of Nassau.
Mr. Cooper. Just a moment—is this man Solomon whose name
you have given the same attorney we heard about the other day?
Mr. Lemin. Yes; that is my understanding; he is. Now, that in-
corporation took place on December 8, 1931, and on December 27,
1932, was the first meeting of the stockholders. At that time there
was elected as president of the company Artemas Paul Pritchard,
and as vice president, William C. Knowles, and their secretary and
treasurer, Reginald Pritchard.
The Chairman. They all live in Nassau?
Mr. Lemin. Yes, Senator, please. And at this meeting of the
incorporators the shares were transferred to the following individuals
who are the present stockholders, according to the last statement of
the company: Artemas Paul Pritchard, Reginald William Pritchard,
William C. Knowles, C. Trevor Kelly, Frederick Pender, all of
Nassau, had one share each, and Walter C. Baber, of New York City,
had the other five shares of issued stock.
Now, some time along in the latter part of 1932, about 1932, Mr.
Baylis—that is William Baylis, who was a partner of Mr. Baber
under the firm name of Baber, Baylis & Co.—
Senator George. What is his particular business?
Mr. Lemin. William Baylis gives his business in 1933 as insur-
ance and tax business. On his 1934 return he gives his business as
salesman—insurance.
Mr. Treadway. Is he a resident of Nassau also?
Mr. Lemin. He is a resident of 411 Willow Grove Avenue, Phila-
delphia, Pa., and he states that he is a citizen of this country.
Now, business of the partnership as shown by the partnership re-
turn of Baylis, Baber & Co., whose address is 45 East Fifty-fifth
Street, New York, is given as brokers and tax consultants.
As I had started to say, in the latter part of 1932 Mr. Baylis
approached an attorney in New York City, a Mr. Richard E. Dwight,
who is and was an outstanding attorney in that city.
Mr. Vinson. With what firm is he connected?
Mr. Lemin. At that time and until recently it was the firm of
Hughes—I will get that—Hughes, Schurman & Dwight. I would
just like to mention this, so you will understand why I move a little
slowly sometimes. I want to give you these matters as carefully as
I can, and I have these folders here so that I may be able to do that.
It will take a moment here to get them in a little better order, and I
can proceed maybe a little bit more rapidly. That firm name is
Hughes, Schurman & Dwight, 100 Broadway, New York, N. Y.
The CHAIRMAN. Is it an old-established law firm in New York City?
Mr. LEMING. I so understand; yes, sir.
The CHAIRMAN. Who are the members of that firm? What are their initials?
Mr. LEMING. Richard E. Dwight, Charles E. Hughes, Jr., and the Schurman initial I don't see at the moment. I understand he is deceased.
Mr. TREADWAY. Mr. Leming, you said as I understood you, "until recently" that firm—just what did you mean by "until recently"? I understood you to use those words.
Mr. LEMING. I did, Congressman, thank you. I have this recollection—I got the impression some way that that firm has been recently dissolved. Now, I don't have official confirmation of that, but that was my understanding.
The CHAIRMAN. You mean yesterday, last week, week before last, or 3 years ago?
Mr. LEMING. It is my recollection that I first heard it said last week.
Mr. TREADWAY. Isn't it a matter of common knowledge that the firm has been dissolved? It has been in the press.
Mr. LEMING. That may be so, Congressman. As I say, I have no doubt that what you say perhaps is true, if it has been in the press.
Mr. TREADWAY. Isn't it a fact that the name of the firm with which Mr. Dwight is now connected is known now as Dwight, Harris, Koegle & Gaskey?
Mr. LEMING. I really don't know. I thought it might be appropriate, first, to bear in mind the reference to the net income and the requisite interest deduction to take care of that income. Mr. Dwight had an income in the year 1932 which could be wiped out by a deduction of approximately $143,000 of deductions. Now, it was in that situation he undertook with the Standard Life Insurance Co., Ltd., of the Bahamas, to enter into a contract for insurance.
The CHAIRMAN. When was this?
Mr. LEMING. Richard E. Dwight.
The CHAIRMAN. I say, when was this?
Mr. LEMING. This was on December 20, 1932.
The CHAIRMAN. You say Mr. Baylis approached Mr. Dwight?
Mr. LEMING. Mr. William Baylis, yes; and thereafter Mr. Dwight made an application for an insurance policy with the Standard Life Insurance Co., Ltd., of the Bahamas.
The CHAIRMAN. Prior to that time, had they issued insurance policies, this Standard Life Insurance Co.?
Mr. LEMING. I believe this was the first policy that was issued—yes, I am pretty sure it was the first policy issued in the company.
Mr. VINSON. How many have they issued since that date?
Mr. LEMING. Our information shows that a total of eight policies was issued to six individuals. There were two of the individuals who took out additional policies in the year 1936.
The CHAIRMAN. Could you give us the names of the parties to whom the insurance was issued?
Mr. LEMING. Yes; I can, Senator, if you please. I am just wondering if it might be desirable to approach more the detail now of
the plan, as we can show it by these sundry documents in order to get the better grasp of the plan itself, and then I will come to that, if that is agreeable.

Mr. Treadway. One question there, Mr. Chairman. I understood you to say this was commenced in 1932?

Mr. Leming. That's right; yes, sir.

Mr. Treadway. And that Mr. Dwight tried to cover it up, the fact that he had done this sort of thing, that he had taken out this kind of policy, or did it appear on his tax return?

Mr. Leming. I will come to that presently, Congressman. I shall be very glad to show you just what occurred. What I have in mind, I had a rough idea as to how I would proceed, and if from time to time it is agreeable to pass these things along I will take care of them, I will not overlook them.

I think it might be helpful if we read at this time the application for one of these policies, bearing in mind, as Dr. Magill mentioned awhile ago, the individual here is subordinated altogether to the point we are trying to make about that. Let us proceed with this thought in mind: Here is a thing; does it thwart the intention or will of Congress or does it? Is it a part of this picture, does it go to this whole tax problem?

Now, if we approach it with that thought in mind—that is the way I am going to try to present it, and for that reason I would like to read the letter.

I will read that, step by step, to show how the plan goes on. This is a letter dated December 20, 1932. It is addressed to the Standard Life Insurance Co., Ltd., Solomon Chambers, Nassau, Bahama Islands.

Gentlemen: I hereby make application to you for a single premium annual dividend life-insurance policy guaranteeing the payment of $4,000,000, subject to the conditions of (1) at my death, to my estate, as beneficiary. I was born at Onarga, Ill., on the 21st day of June 1875. My occupation is attorney-at-law. My address is 100 Broadway, New York City, N. Y.

This application is made subject to the following conditions:

(1) That the policy will be issued by you at your regular rate of premium for my age, nearest birthday, viz. $2,793,720, but without medical examination, being on this account issued by you subject to a lien or first charge in your favor against the principal sum, in the event of my death from any cause; the amount of said lien and its annual rate of decrease being those usually applied by you to policies issued under such conditions.

(2) That you will make a loan of $2,832,540—

(being the loan value at the end of the first policy year), at 5-percent interest in advance upon payment of the single premium, upon the sole collateral of the policy, on the terms and conditions of your regular form of policy-loan agreement.

(3) That on payment by me of any year's interest on this loan (or any increased loan) in advance you will also loan me at that time the amount of the annual dividend which would be payable to me at the end of the then current policy year, if I were living, discounted at 5 percent; that you will make me such a loan for the first policy year, the discounted amount being $94,848.

(4) That this application and the policy and the two loan agreements are to be the entire contract between us as contracting parties.

(5) That you accept this application by cable advice to reach me at my above address not later than Tuesday, December 27, 1932, subsequently confirming same by letter. On receipt of your cable acceptance I will arrange to pay the amount of the single premium and 1 year's interest on the policy
loan with the Royal Bank of Canada, Nassau, Bahama Islands, to be paid by it to you on condition that they are to receive from you the above policy loan and discounted dividend loan. Your written acceptance of my application, policy loan, and discounted dividend loan agreements executed by you and to be executed by me on their receipt here, and receipts for the single premium on the policy-loan interest.

I agree to sign receipts for the policy loan and discounted dividend loan, and to execute the two loan-agreement forms on their receipt here. Please forward me also direct certified copy of the policy for my files.

Yours very truly,

____________________________

Senator Harrison. That letter was written from New York City?

Mr. Lmino. Yes, sir.

Senator Harrison. To Mr. Solomon, at Nassau?

Mr. Lmino. Yes, sir; to the Standard Life Insurance Co., Ltd., in care of Solomon Chambers, Nassau, Bahama Islands.

Mr. Vinson. I understand you to say that he wanted a certified copy of the policy.

Mr. Lmino. Yes, sir; that is right. Now, there are one or two other letters here that I think will be helpful in just carrying through that thought that I tried to start out with, and forgetting all about the individuals for the moment, altogether.

On December 22, 1932—and, incidentally, I believe that was prior to confirmation of the acceptance of the policy—this letter was written by Mr. Dwight to the Royal Bank of Canada, Nassau, Bahama Island [reading]:

ROYAL BANK OF CANADA,
Nassau, Bahamas.

GENTLEMEN: I desire to transact the following business with the Standard Life Insurance Co., Ltd., Nassau, Bahama:

(1) Pay the company a single premium for a single-premium annual dividend life-insurance company of $4,000,000—$2,793,720.

(2) Receive from the company a loan on the sole collateral of the policy, $2,832,540.

(3) Pay the company 1 year's interest on said loan at 5 percent per annum, $141,628.

(4) Receive from the company a discounted dividend loan also on the sole collateral of the policy, $94,848.

Then we have the two columns balanced, "$2,935,348" and "$2,927,388." I said "balanced"—it is a total of the debits and the credits as they then stood.

And I have caused to be transmitted to you by Royal Bank of Canada, New York, the sum of $8,361, to be placed to my credit with your bank.

I hereby appoint Mr. Walter Crosbie Baber as my agent to act for me and in my place and stead to borrow from you the sum of $2,972,388.

Senator Harrison. Is Mr. Baber the man who originated this idea? He is a British subject living in New York. Is that right?

Mr. Lmino. Well, in any event, Senator, he and Mr. Baylis were selling. I am unable to say whether the idea was original with him or not, but we find them selling this plan, and it was through Mr. Baylis and Mr. Baber that it was sold to Mr. Dwight.

Senator Walsh. He was the canvasser for this scheme among the rich American taxpayers in New York City?

Mr. Lmino. Yes. Thank you. And may I digress just a moment, along that line? I think those questions may be very helpful here in bringing up just that very thing. For instance, here is
what you might call a “prospectus”, which was turned over by Mr. Baber to one of the agents, and it starts off this way [reading]:

The following is a lawful method of lowering the taxable category of an individual’s net income. It may be advantageously applied to net incomes of $75,000 or more.

It is only applied after all exemptions and deductions have been taken advantage of by the taxpayer, if his net income, then subject to tax, is $75,000 or more.

The principles of the method have been successfully used by numerous taxpayers during the past 10 years on the recommendation of their legal counsel.

Mr. Treadway. May I ask what you are reading from?

Mr. Leming. I am reading from a prospectus, or whatever you call it, Congressman, that was turned over to the investigating officers by Mr. Baber.

Mr. Treadway. This is an advertisement of the Baber Co.?

Mr. Leming. Yes, sir; I should say that is what you would call it.

Mr. Treadway. A form of solicitation of insurance?

Mr. Leming. Yes, sir.

Mr. Treadway. And what is the date of that?

Mr. Leming. Oh, you mean the date on this circular itself?

Mr. Treadway. Yes.

Mr. Leming. I do not believe there is a date on it, Congressman.

Mr. Treadway. By the Treasury Department?

Mr. Leming. Yes.

Mr. Treadway. By the Internal Revenue Bureau?

Mr. Leming. Yes. Now, understand, Congressman, I am not here to say that no one ever heard of it before, or anything of that sort. I am talking now about this document. So far as I know—that is all I know about it, and this thing was presented to the investigating officers in 1933. I just wanted to make it clear.

Mr. Treadway. That is what we wanted. I wanted to get the date for that reason in order to have it clear.

Mr. Leming. Yes.

Senator Harrison. Is that a very long prospectus?

Mr. Leming. It is, Senator, but I did not intend to read all of it.

Senator Harrison. Do you think it ought to be entered in the record?

The Chairman. Without objection, it will be inserted in the record.

Mr. Leming. We will be glad to insert it in the record.

(The prospectus referred to, marked “Exhibit 2”, was received and made a part of the record, and will be found at the end of today’s proceedings, p. 118.)

Mr. Leming. Shall I proceed with this prospectus, to discuss it at the moment?

Senator La Follette. Mr. Chairman, may I ask a question?

The Chairman. Senator La Follette.
Senator La Follette. Mr. Leming, did the Bureau investigate this office of Mr. Baber? Where did this material come from? Did they investigate his office?

Mr. Leming. Yes, sir; they did, Senator.

Senator La Follette. How many people did they find he had sold this device to?

Mr. Leming. In this Bahama corporation? This particular company, the Standard Life Insurance Co., Ltd., had sold to six persons.

Senator La Follette. Did they find that he had any other company, any other life-insurance company?

Mr. Leming. It is not my recollection that they did, Senator; no, sir. The agents say they did not find that he represented any of the other similar companies.

Senator La Follette. He had all these circulars printed, and he only sold the device to six taxpayers, according to the Bureau's investigation?

Mr. Leming. That is right.

Senator Walsh. Were the form of the application and the borrowing and the other proposals the same in all six cases?

Mr. Leming. Essentially so; yes. The percentages of the lien charge and the loans and things of that sort would vary. The forms of the policies I believe were identical.

Mr. Treadway. Mr. Chairman, may I ask a question?

The Chairman. Mr. Treadway.

Mr. Treadway. In view of that circular being dated 1933, how far did the Bureau go with any investigation as to this form of selling insurance, at that time or since then, up to now?

Mr. Leming. The circular is not dated, Mr. Congressman. It was acquired by the agents in 1933.

Mr. Treadway. I wanted to be sure. The Bureau of Internal Revenue has had that circular of Baylis & Baber, or whatever that firm is, since 1933?

Mr. Leming. Yes, sir.

Mr. Treadway. That is correct?

Mr. Leming. Yes, sir.

Mr. Vinson. What was done with reference to the 1932 income of Mr. Dwight?

Mr. Leming. The additional tax which the Bureau determined; or, I should not say "determined", because that term is sometimes used technically. It has not been collected. The Commissioner has determined within his own office already that that deduction is not allowable.

Mr. Vinson. As I understand it, they looked through the device and reached the conclusion that that particular deduction was not allowable?

Mr. Leming. That is right.

Mr. Vinson. And arrived at the tax for that particular year?

Mr. Leming. Yes, sir.

Senator Walsh. Mr. Chairman, I think the committee would like to know in what way this taxpayer applied this device in reducing his taxes, the normal taxes he would have to pay the Government. Have you got that tax return here?

Mr. Leming. I thank you, Senator. I would be very glad to explain that.
Senator Walsh. What did he say was his income, and how much did he deduct as a result of the application of this scheme? How much did the Government lose thereby?

Mr. Leming. Maybe I can give you this photostat here. I believe we have enough of those. I can see, if I may be permitted. Understand, I do not mind the question, but in view of the Senator’s question here, I can see that if I could be permitted to proceed here for a little bit and give you a little clearer idea just how the device was used, then the figures would come to you better.

Senator Walsh. You may go your own way.

Mr. Leming. Mind you, I am agreeable to going any way, Senator, that you want.

Senator Walsh. That is all right; but, of course, the important thing is the deception, the fraud, the evasion, or whatever it is, appears in the overt act of making out his tax return?

Mr. Leming. Yes.

Senator Walsh. And we want to get that sometime.

Mr. Leming. Yes. Now, we have an insurance company here that had no invested capital. It had no income. It had nothing. It was a shell. As I recall, the first money that went into that insurance company at all, actual money, was $8,361, which was paid by Mr. Dwight.

Now, you recall that letter I read. He was borrowing from a bank down there almost $3,000,000, and the insurance company was loaning him a little larger amount than he was borrowing from the bank allegedly, yet the only actual cash involved in this whole thing was $8,361. I think, Senator Walsh, you might sum it up this way, and we can get then maybe right down to your question there—that for that $8,361 he got a tax reduction by reason of the interest on that huge loan; his taxes were actually reduced $53,448.48. The insurance company got the only cash there that was involved, as I say, $8,361, and that in turn, some of it, went to the Royal Bank of Canada, $401, for a so-called 1-day loan of that sum of money at the bank. Other parts of it went for traveling expenses. Other parts of it were paid out to Mr. Baber as advances or salaries or commissions, or things of that sort.

I would like to just digress right here again a moment and tell you a little something about this man Pritchard down at Nassau.

Mr. Vinson. Before we get to that, what was the amount of interest deducted from the return because of this particular transaction?

Mr. Leming. I will give you the precise amount here. The amount was $141,628.

Senator Walsh. And no principal sum ever moved from the bank or insurance company to the taxpayer?

Mr. Leming. No, sir. It was all pure fiction, if I may so characterize it.

Senator Walsh. I think it was more than fiction.

Mr. Crowther. It was stern reality.

Mr. Vinson. It was financial romance.

The Chairman. He was never physically in possession of this loan, on account of which he takes credit for the interest?

Mr. Leming. O, no, no. What I started out to try to do was to avoid characterization, Mr. Chairman, but when you get to talking you forget about that, one way or the other. My thought is there
was not any loan, and there was not any interest. There was not any payment. The corporation had no assets. It could not have paid a dividend. There just was not anything.

The CHAIRMAN. You say that is your thought. That is the fact disclosed by the evidence, is it not?
Mr. LEMING. Yes. Thank you, that is right.

The CHAIRMAN. That is fact, that is not opinion, is it not?
Mr. LEMING. Yes; that is a fact.

Now, suppose I let you have these photostats, and I would like, however, even though you have these there, to continue along and try to give you this whole picture.
Senator HARRISON. Sometime, Mr. Leming, I would like for you to tell us what was the income tax paid by Mr. Dwight in 1932, before he made that loan.
Mr. LEMING. None. That wiped out all of his income. He paid no taxes.

Senator HARRISON. I am talking about 1932. This policy was not issued until 1932?
Mr. LEMING. December 1932.

Senator HARRISON. So he took his deduction in his return that he made in 1933?
Mr. LEMING. No, Senator, he took that in 1932. You see, the first deduction—that is, he got the policy, and this swapping or matching of checks, that business took place down at Nassau at the end of December. Mind you, he told them that he had to have confirmation of that transaction by December 27, 1932, so he got his confirmation by cable and subsequently by letter, that that transaction had taken place.

Senator HARRISON. But he did not make his return, did he, until January 1933, on his 1932 income?
Mr. LEMING. That is right. He made his return in 1933.

Senator HARRISON. That is what I am trying to get at. On his income tax of 1931, what did he pay in taxes?
Mr. LEMING. I do not have his 1931 return.

Senator HARRISON. I wish you would give that to the committee.
Mr. LEMING. We would be very glad to get that.

Senator HARRISON. Let us see what he was paying before that time. And then he wiped it out in the 1932 income-tax return by virtue of this loan, as I understand.
Mr. LEMING. Yes.

Senator HARRISON. When he made his return in 1932, was this deduction approved?
Mr. LEMING. No, sir.

Senator HARRISON. What happened?
Mr. LEMING. The Commissioner has determined the tax, and the processes of collection have not yet proceeded to the point of final collection.

Senator WALSH. The same method, Senator, was repeated in his return of 1933, 1934, and 1935.

Mr. LEMING. Yes.

Senator WALSH. So you have the claim of evasion on an income which ranged from $143,000 in 1932 to $158,000 in 1933, do you not? He paid no tax in 1932, 1933, and 1934, and only $299.63 in 1935?
Mr. LEMING. That is right; $141,628 in 1932 to $147,391 in 1935.
Senator Walsh. Because of these deductions, which amounted in 1 year to $141,628, in another year to $143,567, in another year to $145,486, and in another year to $147,391?

Mr. Leming. That is right.

Senator Walsh. In other words, he deducted almost exactly the amount of his income?

Mr. Leming. Yes. The device lent itself to that. It was elastic. You could use it any way. It did not make any difference what your income might be.

Senator Walsh. Can some of the experts tell us, if the deductions were not allowed on this income, what the proper tax is that he would have paid for those years?

Mr. Vinson. Will the Senator yield?

Senator Walsh. Certainly.

Mr. Vinson. At this point in the record, Mr. Chairman, I suggest that the data which has been presented to us in photostatic form as affecting Mr. Dwight be inserted in the record.

The Chairman. Without objection, that will be done.

(The analysis of 1932-36 returns of six Standard Life policyholders was received as a part of the record, and the same will be found on p. 111.)

Mr. Leming. Congressman, may I make this observation?

Senator Walsh. On the record, may we show that the evasion was about $50,000 a year?

Mr. Leming. I just want to call attention to the column on the right-hand side there. It says "Actual cash expended." That is not entirely clear there on the chart.

Mr. Vinson. You may make any explanation you wish.

Mr. Leming. I was just going to say if you changed that column, the last column on the right-hand side, to the "Actual amount of cash paid out by the taxpayer", which went to that insurance company—that is what that means there—in the acquisition of the policy and the loan in the various years.

The Chairman. Without objection, it will be inserted as part of the record.

Mr. Treadway. In that same connection, wouldn't it be advisable to include the answer to Senator Harrison's inquiry as to what his tax returns showed for 1932?

The Chairman. Will you furnish the committee that?

Mr. Leming. Yes; I will be very glad to.

The Chairman. We want that furnished for the record.

Mr. Leming. We will be glad to furnish it.

The Chairman. I notice he reported these deductions in his income-tax returns for 1933, 1934, and 1935. They were not used in 1936. How do you explain that?

Mr. Leming. Well, he went through the same procedure down there in the Bahamas, but for some reason he did not use the deductions.

The Chairman. Was it because there came a controversy in the Treasury Department between the taxpayer and the Department?

Mr. Leming. I should say so.

The Chairman. What did they do when these deductions were made and they disallowed them—what was done, if anything, about the collection of his true income-tax return?
Mr. Leming. Well, Senator, perhaps the best I can answer you on that is this way: After all, a 1932 return, the fellows who are handling returns all the time, is not a very old return. In point of time, for the personnel who have to handle these things year after year, that is not a great length of time. Now, it so happens that in this case the taxpayer's returns were from 1932 down have been accumulated, awaiting final action. It has not altogether been neglected.

Senator Walsh. About what date did the Internal Revenue Department discover this scheme in this taxpayer's return?

Mr. Leming. I think it was about June 1934 that the first report was made.

Senator Walsh. Has the case ever been referred to the Department of Justice?

Mr. Leming. No; it has not.

Senator Walsh. Why not?

Mr. Leming. Well, I don't know as I am in position to just answer that question.

Commissioner Helvering. On Mr. Dwight's return he stated that the deduction of $141,000 in his 1933 return when it was examined was the result of an insurance policy on which he paid a previous premium and borrowed the money, and the interest on this borrowed money was equal to this deduction. The agent disallowed that. He protested that. The following year it was examined and the agent that examined that disallowed it, and he protested that, claiming that the deduction was a proper one. The reason that I did not recommend it to the Department of Justice was that he had noted on his return that the deduction was made in a certain way and for certain reasons, giving us notice.

Senator Walsh. You did not know the facts at his disposal?

Commissioner Helvering. No.

Senator Walsh. When did you learn these facts?

Commissioner Helvering. These were learned very recently in an investigation.

Senator Walsh. So there was nothing on the face of the return to indicate that the insurance company was in existence?

Commissioner Helvering. We did not know it at the time.

Senator Walsh. And through research and study you were able to find these facts?

Commissioner Helvering. I want to say, in answer to the Senator's question, the reason it was not referred to the Department of Justice was because that notation was made on there that gave us notice so we could investigate it.

The Chairman. These deductions were not allowed?

Commissioner Helvering. They were not.

The Chairman. What was done then toward payment by the taxpayer?

Commissioner Helvering. They protested that they were deductible and really just took that position until recently, perhaps in January of this year, when we were going to make an assessment, and they came in for a conference in the General Counsel's office relative to this matter, and the General Counsel held it was paid. Since that time an offer of payment has been made.
TAX EVASION AND AVOIDANCE

Senator Walsh. That offer to pay these deductions was made after all these years?

Commissioner Helvering. I want to say to you, Senator, that offer was made in my office about 2 weeks ago, a certain amount, including all the taxes and interest occasioned by the deduction for these 4 years.

Senator Walsh. But that has not been accepted?

Commissioner Helvering. No; it has not.

Senator Walsh. Has the assessment ever been made?

Commissioner Helvering. The assessment has never been made. We just told them they were not going to allow it. We first sent out what we call a 30-day letter; that is the way we designate it. It is a computation of the tax that the agent has made and we have approved. We also give them an opportunity to appear and contest any item. After they have appeared, or if they do not appear, we then issue a 90-day letter, under the law, giving them 90 days if they want to object and appeal to the Board. At the end of 90 days we assess them.

The Chairman. How much is the amount they have offered to pay?

Commissioner Helvering. $267,000.

Mr. Vinson. In the offer of compromise, was the penalty included?

Commissioner Helvering. No, sir.

Mr. Vinson. What is the penalty?

Commissioner Helvering. Fifty percent penalty and costs.

Mr. Crowther. I call attention to the following statement made by the Commissioner, page 3, the letter of the Secretary of the Treasury dated the 29th of May, 1937, in which he says:

The fraud was discovered by the Treasurer's investigators and all of the taxpayers have now submitted offers to pay the full amount of taxes evaded, plus interest.

That was on May 29, before this message of the President. You stated awhile ago the offer was made: since the message of the President.

Commissioner Helvering. I say the offer made to me in the record form was made 2 weeks ago. In Mr. Shafroth's office, the general counsel, the offer was made some time ago.

Mr. Crowther. How long ago?

Commissioner Helvering. Since the 1st of January some time; I don't know the date.

Mr. Crowther. I just wanted to correct the impression that these offers in settlement were not made until after the President's message.

The Chairman. When were the first steps taken to ascertain these devices? That suspicion seems to have been aroused as the result of the income-tax returns for the years 1932 and 1933. When did you take the first steps in this matter?

Commissioner Helvering. It came to my attention some time in the early part of this year, and we sent an agent down to endeavor to unearth all this information Mr. Leming has been giving you at this time. We had no history whatever of these facts. I did not know about it, and I don't think anybody else did in the Bureau, as to the way the matter was handled.
The Chairman. Someone would have had to know this if there was the same suspicion year after year.

Commissioner Helvering. I think both agents that handled the returns had this suspicion, because they disallowed this deduction.

Under Secretary Magill. There is another point there that the Commissioner might bring out. Of course, these loans on insurance policies are an old thing; there is nothing new about that. As the Commissioner has said, Mr. Dwight on his return said he had borrowed money on an insurance policy from the Standard Life Insurance Co. and had paid so much interest. On the face of it—I haven't seen the returns myself, but I dare say that on the face of it that looked like a perfectly bona fide transaction and the objection to it arises when we go into it and see that the whole thing was a hollow shell. Since it was a Bahama company it required sending an agent down there to carefully examine the situation there before you could see what it was all about.

Senator La Follette. But, Dr. Magill, the agent must have been suspicious, or he would have allowed the deduction in 1932. Four years went by before the Bureau found out about it.

Commissioner Helvering. The first examination of these returns was made, as I recall, in 1934.

Senator La Follette. Two or three years had gone by before the Bureau found out about it?

Under Secretary Magill. "The Bureau", as you know, is an all-inclusive term. Some individual found this out in the course of the field examination of the return, as I understand, in the summer of 1934. He goes into it and he decides this interest deduction should be disallowed. Then that is protested and then the case would normally come down here, in due course, to be heard. I suppose the history was that there were various deductions that went on between 1934 and 1936, and then the agents were sent down to the Bahamas to look into it.

Senator La Follette. The agents were sent down in January of this year, as I understand it.

Under Secretary Magill. So the Commissioner said.

Senator La Follette. If there is not some way to speed up this information concerning these various devices and if they can be used for 2 or 3 or 4 years, without any thorough investigation made of them, what hope is there of ever catching up with these smart tax lawyers? Isn't it part of our problem to try to improve the procedure in the Bureau?

Under Secretary Magill. That is very true, and that is one thing I am down here to try to do, and that the Commissioner is trying to do. As the Secretary said to you, you remember, the first day, our machinery is not sufficient at present to make an elaborate audit of all the returns which are submitted to us. We do the best we can with the force we have. In this particular case I entirely agree with you that it would have been much better for all parties if the matter had been discovered and gone into and could have been worked out back there 2 or 3 years ago.

Senator La Follette. As a matter of fact, Dr. Magill, do you really know whether these 1931, 1932, 1933, 1934, 1935, and 1936 cases are the only cases where this phony life insurance device was in use?

Under Secretary Magill. No; not at all. We have no way of knowing really one way or the other. I think you see the difficult
problem you have in this case. I suppose there must be thousands of people who deduct interest on bona-fide insurance loans on their policies. They are perfectly good, and what we have to do is to try to educate the agent in the field, so that he can detect the difference between the company which is a hollow shell and one which is not.

Senator La Follette. You can't very well blame the agent, because he seems to have been on the job when he disallowed the deduction. Two or three or four years go by before anybody comes in to find out whether the Bahamas Life Insurance Co., Ltd., is a phony company or not.

Under Secretary Magill. There you are. Perhaps the Commissioner can give you a further explanation. So far as I can see, what you have here is a Bahaman company which appears to be a life-insurance company, which the taxpayer said was a life-insurance company. He was protesting any determination that it was anything else but an insurance company. Only after quite a bit of investigation did we find out what the situation is.

Senator La Follette. In the meantime several thousand wealthy taxpayers might have availed themselves of this device?

Under Secretary Magill. It is quite possible.

Mr. Cooper. Just one question of the Commissioner there. You state that recently this taxpayer had made an offer of $264,000, covering the tax and interest, but wanted to be relieved of the penalty assessment of 50 percent in addition?

Commissioner Helvering. Yes.

The Chairman. There has been no official action taken on that matter?

Commissioner Helvering. No, sir. That was received—I can't give you the exact date, but within the last 2 weeks.

Mr. Treadway. Mr. Helvering, I notice one column shows "Corrected tax"; another column shows this disallowance; and then there is the item of "Corrected tax" following it. When were those corrected taxes made up in your Bureau?

Commissioner Helvering. I could not give you that date.

Mr. Treadway. Well, my point is this: Have these corrections been made recently when this case came up, or were they made each year?

Commissioner Helvering. I might answer you by giving you what our procedure is. I might say, too, that insurance companies have been writing policies and deductions made are correct deductions. I have an idea—this is only my surmise—that the agent, when he saw this deduction, exactly what the income was, thought there was something the matter with it, and wanted to call attention to it. When it comes to the Bureau these cases are examined, and when we come to the conclusion that it is not a deductible item we compute the tax. That, under that item is "corrected tax" and we assess it.

Mr. Treadway. But you don't know personally whether in this instance it has been recently corrected or whether it was annually done after the returns were filed?

Commissioner Helvering. They are annually done.

Mr. Treadway. So that the various amounts of corrected tax, you think, were levied at the time the report was made or examined by your field agent?
Commissioner Helvering. The tax was set up on the return that was under protest.

Mr. Vinson. And not at the time of the examination by the field agent, the assessment is not made until it came in to you?

Commissioner Helvering. No.

Mr. Treadway. That is current with the year, isn't it, Mr. Commissioner?

Commissioner Helvering. It reached my office 2 or 3 years after the transaction, because we do not reach those—the quickest we can reach those is from a year to 15 months.

Mr. Treadway. One other question if I may, Mr. Helvering. I note that in 1936 the interest deduction of Mr. Dwight is marked as "not used." That is correct, isn't it? You haven't used, in making up this statistical list, his return of 1936?

Senator Walsh. You mean he didn't use this device—isn't that what he means?

Mr. Treadway. Or, you couldn't use the device that year?

Commissioner Helvering. No.

Mr. Treadway. Well, it is the same point. This great deficiency that has been talked about and written about was discovered, the most of it, last month, as has been testified, so that this $145,000 claimed to be deducted by Mr. Dwight was no part of the tax deficiency at that time, because Mr. Dwight did not use the device in 1936?

Commissioner Helvering. No. I might say, so the committee understands it, Mr. Dwight has had conferences with the Bureau and was advised before he made a return for 1936 that we were not intending to allow that deduction.

Senator La Follette. Doesn't the agent's report, when it comes into the Bureau, necessarily show the reasons for disallowing the deduction?

Commissioner Helvering. Yes; I think they do set that out on all of the agents' reports.

Senator La Follette. As a matter of fact, this agent's report must have come into the Bureau on this first return of 1932 a long time ago. I would like to see the reports of the agent.

Commissioner Helvering. May I say to the committee that it is not the policy of the Bureau, when a taxpayer who presents what he considers a logical reason, sets out his legal reasons, to say, "Out with you; we are going to assess this tax." We generally have many conferences about these matters, and it consumes considerable time, and Mr. Dwight is a very able man to present his side of the case.

Senator La Follette. I would like to get the agent's reports on these matters, because I would like to find out if the agent did not give his reasons for disallowing this deduction in 1932 and find out how long the Bureau was on notice. I want to know why it took so long for the Bureau to get around to investigating this phony life-insurance company down in the Bahamas.

The Chairman. The Commissioner will comply with the request of Senator La Follette and furnish the committee a little later the reports made to the Department.

Commissioner Helvering. May I go a step further? The taxpayer, when this matter is up, has a right to appeal to the Board, of course. We want to be sure of our ground. We do not want to
assess a tax just because we think it is due. It has been the policy since I have been there to do that. We try to get down to facts. We arrived at these facts in January, I think, that we were not going to allow this deduction, but we wanted the basis, and that is the reason we ordered an examination to find out the basis of this insurance policy. To use the common phrase, we thought there was something "screwy" about it and we wanted it investigated.

Mr. Vinson. What was the taxable income reported by Mr. Dwight for the taxable year 1936?

Commissioner Helvering. I don't have the figures. I wouldn't want to state, because I don't know exactly.

Mr. Vinson. Will you put it into the record?

Commissioner Helvering. Yes; we will put it into the record.

Mr. Morrison Shafroth (Chief Counsel, Bureau of Internal Revenue). I want to say just a word about the way this matter happened to be investigated in January. The matter was first called to my attention some time early in the year. A tax lawyer came to my office and said that this law firm in New York was about to break up and Mr. Hughes, Jr., had learned of this scheme of Dwight's and was insisting that Dwight straighten this up with the Bureau immediately, and that if he did not get it straightened up he was going to break up the law firm, and had asked that I take immediate action on an oral offer to compromise the matter for the amount of the taxes and the interest due. We looked into it a little and we thought the matter ought to be investigated further before we could recommend to the Commissioner any settlement of that kind, and suggested that agents be sent down to the Bahamas to look into the entire picture before the settlement was made. That is the way the agent happened to go down at this time into the Bahamas to get the matter straightened out.

Mr. Treadway. What was the date of that, please, Mr. Shafroth?

Mr. Shafroth. I can't give you the exact date, but some time early in this year.

Mr. Treadway. What month do you think it was?

Mr. Shafroth. Approximately February 19.

Mr. Treadway. That the oral interview took place?

Mr. Shafroth. It was a little prior to February 19. I can't give you the exact date.

Mr. Treadway. Prior to that?

Mr. Shafroth (reading from a memorandum handed to him). February 6, I think I state here.

Mr. Treadway. That was the time when word came to you that Mr. Hughes insisted on this settlement; is that correct?

Mr. Shafroth. Insisted on the settlement and said he was going to break up the law firm.

Senator La Follette. Is the substance of your testimony, Mr. Shafroth, that we can thank Mr. Hughes for getting this device investigated, or would the Bureau have eventually got to it?

Mr. Shafroth. As soon as it came to my attention I requested that the Penal Division look into it and see whether or not it should be settled for the amount of the taxes and penalty.

The Chairman. Through what source, or channel, did it come to your attention?

Mr. Shafroth. Through a tax lawyer bringing it to my attention and saying it ought to be settled immediately.
TAX EVASION AND AVOIDANCE

Senator La Follette. It is my understanding, Mr. Chairman, they are going to furnish the file of this case so we can look into it.

The Chairman. You can do that, Mr. Commissioner, and comply with the request of Senator La Follette?

Commissioner Helvering. Yes; we can furnish the file.

The Chairman. Are you through, Mr. Leming. If not, you may proceed.

Mr. Leming. No, Mr. Chairman, I had only just started. The first thing for the record—this chart here that the committee has been examining and on which Congressman Treadway had pointed out down here in the last line, "1936, not used"—now let us go back up to the top under "Dwight, 1936", and opposite that, as the Congressman pointed out, the words "not used." I don't understand that in the preparation of this chart there was any attempt to show the tax liability one way or the other for 1936. I just wanted to clear that up.

Senator Walsh. I think we understand that, that the Department gave him the premise of an honest return, in view of the fact that he had not used this device.

Mr. Leming. Senator, if you please, there just wasn't anything put on that line because the device was not involved that year.

Mr. Treadway. Have you his return for 1936?

Mr. Leming. Not with me. We undoubtedly have it, Congressman, and I believe there has already been a request for the 1936 return also, and we will be very glad to furnish it.

Senator Harrison. We won't be able to continue much longer this morning. I notice on this list you have given insurance policies issued to other individuals. Wouldn't it be well to give those names at this time? The newspapers may want the names on this list and then we can discuss the cases at the next sitting of the committee.

Mr. Leming. I shall be very glad to comply with the Senator's request.

Senator Harrison. All right; proceed. I take it that these names on this list are others in addition to Mr. Dwight, who received insurance policies from this Standard Life Insurance Co.?

Mr. Leming. Yes; and two of them took out additional policies in the year 1936.

Senator Harrison. What are Mr. Ayres' initials?

Mr. Leming. Winfield Ayres, M. D.

Senator Walsh. What is his residence?

Mr. Leming. 133 East Fifty-eighth Street, New York.

Senator Harrison. What is the amount of the insurance policy issued to him?

Mr. Leming. $400,000.

Senator Harrison. When was that?

Mr. Leming. That was in December 1932.

Senator Harrison. Did he follow largely the same idea that Mr. Dwight did in borrowing on this policy?

Mr. Leming. Yes, sir; the plans were in all respects the same.

Senator Harrison. In all these cases?

Mr. Leming. Yes, sir.

Senator Harrison. Now, let's get to Mr. Lowe. Who is Mr. Lowe?

Mr. Leming. Henry W. Lowe, 67 Wall Street, New York, N. Y. and he notes here certain income, Johnson & Higgins, 67 Wall Street,
New York City, and as I recall, that is the address; yes, 67 Wall Street.

Mr. Cooper. Mr. Chairman, do your records show what Mr. Lowe's business is? Give that in connection with his name and address.

Mr. Leming. He is associated with, or a member of the brokerage firm of Johnson & Higgins. They are insurance brokers.

Mr. Treadway. Johnson and what?

Mr. Leming. Johnson and H-i-g-g-i-n-s.

Senator Harrison. What is Mr. Ayres' business?

Mr. Leming. He is a doctor.

Senator Harrison. What is the amount of the policy issued to Mr. Lowe?

Mr. Leming. The Lowe policy was $2,500,000.

Senator Walsh. He used this device in 1933, 1934, 1935, and 1936? Mr. Leming. Yes; I believe he was one of those who used it in 1936.

Senator La Follette. And his additional tax is $137,495.08?

Mr. Leming. As shown by the chart.

Senator Harrison. Were all those deductions held up in a similar way to the case of Mr. Dwight?

Mr. Leming. Yes. It is my recollection that on one of these there was a letter sent out.

Senator Harrison. Who is Mr. Marx, what are his initials and address?

Mr. Leming. Lawrence Marx, and his address is 93 Franklin Street, New York, N. Y.

Senator Harrison. What is his business?

Mr. Leming. Cotton broker.

Senator Harrison. What was the amount of his insurance policy?

Mr. Leming. $2,500,000 was the first one. Then he took out an additional policy in 1936 of $2,500,000.

Senator La Follette. And with the actual expenditure of $2,500 did he reduce his tax according to his return $129,337.99, is that correct?

Mr. Leming. If that is as shown by the chart, that is correct.

Senator Walsh. It is interesting to note in connection with this case that in 1934 and 1935, when he used his device his policy was $2,500,000. In 1936 that income jumped from $86,000 to $179,000. Therefore, he jumped his insurance policies and took out two insurance policies.

Mr. Leming. It seems it was a very elastic arrangement.

Senator Walsh. I should say it was.

Senator Harrison. What about Mr. Schwab?

Mr. Leming. Jacob W. Schwab, 93 Franklin Street, New York, N. Y., treasurer of Cohn, Hall & Marx Co.

Mr. Cooper. What is their business?

Mr. Leming. They are cotton brokers.

Mr. Crowther. Was he a partner of Lawrence Marx? They have the same address, 93 Franklin Street?

Mr. Leming. Yes.

Senator Harrison. What about the next name, Mr. Thoms?

Mr. Crowther. What was the amount of Mr. Schwab's policy?

Mr. Leming. Well, there would be about $1,500,000.
Senator La Follette. By the expenditure of actual cash of $1,637.80, he reduced his tax for 1934, 1935, and 1936 by a total of $45,476.98? Is that correct?

Mr. Leming. Yes. You see, he took out another policy, Senator, in 1936. Due to the increase in income it necessitated an additional policy.

Senator Harrison. Mr. Thorns?

Mr. Leming. George Thorns, 15 William Street, New York, N. Y., and he is an attorney at law.

Mr. Cooper. And his address is 15 William Street?

Mr. Leming. Yes.

Senator Harrison. What was the amount of his policy?

Mr. Leming. His policy was $875,000. That is the face amount of that policy.

Senator Harrison. I notice he didn't use the deduction in 1936.

Mr. Leming. Yes; it is only used there in 1 year.

Senator La Follette. Mr. Chairman, the photostat seems to indicate that these six taxpayers, by the use of $67,726.01 in actual cash, reduced their tax, according to their returns, $549,501.97. Is that right?

Mr. Leming. Yes.

Mr. Vinson. I suggest that we insert this chart at this point in the record respecting the six taxpayers.

Mr. Leming. All right.

(The chart headed "Analysis of 1932-36, returns of six Standard Life policyholders", was received in evidence.)

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<th>Taxpayer</th>
<th>Year</th>
<th>Income reported</th>
<th>Interest deduction disallowed</th>
<th>Correct income</th>
<th>Tax paid</th>
<th>Corrected tax</th>
<th>Additional tax</th>
<th>Actual cash expended</th>
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<td>None</td>
<td>$599,085.27</td>
<td>$599,085.27</td>
<td>$10,586.24</td>
</tr>
<tr>
<td></td>
<td>1936</td>
<td></td>
<td></td>
<td></td>
<td>(i)</td>
<td></td>
<td>(i)</td>
<td>$1,098.00</td>
</tr>
<tr>
<td>Total...</td>
<td></td>
<td>$17,518.09</td>
<td>$178,072.00</td>
<td>$195,590.09</td>
<td>(i)</td>
<td></td>
<td>(i)</td>
<td>$37,115.49</td>
</tr>
<tr>
<td>Ayres....</td>
<td>1932</td>
<td>$6,049.66</td>
<td>$10,010.00</td>
<td>$22,059.66</td>
<td>245.98</td>
<td>$1,086.07</td>
<td>$1,042.09</td>
<td>None</td>
</tr>
<tr>
<td></td>
<td>1932-6</td>
<td></td>
<td></td>
<td></td>
<td>(i)</td>
<td></td>
<td>(i)</td>
<td>None</td>
</tr>
<tr>
<td>Total...</td>
<td></td>
<td>$6,049.66</td>
<td>$10,010.00</td>
<td>$22,059.66</td>
<td>245.98</td>
<td>$1,086.07</td>
<td>$1,042.09</td>
<td>None</td>
</tr>
<tr>
<td>Lowe......</td>
<td>1932</td>
<td>2,168.78</td>
<td>91,719.19</td>
<td>94,887.97</td>
<td>None</td>
<td>23,285.80</td>
<td>23,285.80</td>
<td>823.19</td>
</tr>
<tr>
<td></td>
<td>1933</td>
<td>1,618.63</td>
<td>88,453.00</td>
<td>90,071.63</td>
<td>None</td>
<td>22,749.60</td>
<td>22,749.60</td>
<td>8,268.48</td>
</tr>
<tr>
<td></td>
<td>1934</td>
<td>$44,264.73</td>
<td>$92,331.10</td>
<td>$137,595.83</td>
<td>5,433.53</td>
<td>48,180.37</td>
<td>42,036.84</td>
<td>6,141.10</td>
</tr>
<tr>
<td></td>
<td>1935</td>
<td>27,966.11</td>
<td>95,276.00</td>
<td>123,242.11</td>
<td>3,670.30</td>
<td>62,499.64</td>
<td>58,823.44</td>
<td>3,665.60</td>
</tr>
<tr>
<td>Total...</td>
<td></td>
<td>$76,018.15</td>
<td>$360,762.34</td>
<td>$437,800.49</td>
<td>9,219.78</td>
<td>146,715.41</td>
<td>137,495.88</td>
<td>$28,249.72</td>
</tr>
<tr>
<td>Marx......</td>
<td>1934</td>
<td>14,194.86</td>
<td>70,407.48</td>
<td>84,592.34</td>
<td>790.69</td>
<td>25,781.50</td>
<td>25,030.67</td>
<td>1,750.83</td>
</tr>
<tr>
<td></td>
<td>1935</td>
<td>8,391.72</td>
<td>94,543.00</td>
<td>102,934.72</td>
<td>None</td>
<td>23,105.88</td>
<td>23,105.88</td>
<td>None</td>
</tr>
<tr>
<td></td>
<td>1936</td>
<td>21,404.69</td>
<td>164,503.00</td>
<td>185,907.69</td>
<td>671.77</td>
<td>81,273.51</td>
<td>81,273.51</td>
<td>None</td>
</tr>
<tr>
<td>Total...</td>
<td></td>
<td>$42,981.27</td>
<td>$324,455.48</td>
<td>$367,436.75</td>
<td>1,222.66</td>
<td>100,660.85</td>
<td>100,660.85</td>
<td>$2,500.00</td>
</tr>
<tr>
<td>Schwab...</td>
<td>1934</td>
<td>6,943.50</td>
<td>44,107.90</td>
<td>51,051.40</td>
<td>93.04</td>
<td>9,227.03</td>
<td>9,227.03</td>
<td>1,137.80</td>
</tr>
<tr>
<td></td>
<td>1935</td>
<td>(2,669.23)</td>
<td>44,740.00</td>
<td>45,409.23</td>
<td>None</td>
<td>7,926.66</td>
<td>7,926.66</td>
<td>None</td>
</tr>
<tr>
<td></td>
<td>1936</td>
<td>9,749.59</td>
<td>70,722.00</td>
<td>80,471.59</td>
<td>356.33</td>
<td>26,702.23</td>
<td>26,702.23</td>
<td>500.00</td>
</tr>
<tr>
<td>Total...</td>
<td></td>
<td>$14,043.86</td>
<td>$165,119.80</td>
<td>$179,163.69</td>
<td>379.34</td>
<td>45,856.32</td>
<td>45,476.98</td>
<td>$1,637.80</td>
</tr>
<tr>
<td>Thomas...</td>
<td>1935</td>
<td>$3,729.88</td>
<td>$32,006.00</td>
<td>$35,735.88</td>
<td>91.38</td>
<td>5,240.87</td>
<td>5,149.49</td>
<td>$2,983.33</td>
</tr>
<tr>
<td></td>
<td>1936</td>
<td>$3,729.88</td>
<td>$32,006.00</td>
<td>$35,735.88</td>
<td>91.38</td>
<td>5,240.87</td>
<td>5,149.49</td>
<td>$2,983.33</td>
</tr>
<tr>
<td>Total...</td>
<td></td>
<td>$3,729.88</td>
<td>$32,006.00</td>
<td>$35,735.88</td>
<td>91.38</td>
<td>5,240.87</td>
<td>5,149.49</td>
<td>$2,983.33</td>
</tr>
<tr>
<td>Grand total...</td>
<td>150,240.81</td>
<td>1,482,457.52</td>
<td>1,667,288.21</td>
<td>11,556.73</td>
<td>601,058.69</td>
<td>549,501.97</td>
<td>67,726.01</td>
<td></td>
</tr>
</tbody>
</table>

1 Not used.
The Chairman. I would like to ask you if any of the persons whose names appear on this chart, other than Mr. Dwight, have made any overtures to settlement?

Mr. Leming. All have, Mr. Chairman, except in the case of the estate of the deceased Dr. Ayres, either formally or informally.

The Chairman. All have made some offers of settlement?

Mr. Leming. Yes; either formal or informal.

Senator La Follette. Is it correct that none of them have been settled officially?

Mr. Leming. That is right, Senator. None of these cases has been officially closed.

Mr. Vinson. The last column on the right-hand side of the chart as it appears to us as actual cash expended?

Mr. Leming. That means the actual cash that he paid in that transaction to the insurance company, Congressman.

Senator George. Would you be able to tell us this, whether all of these taxpayers show on their annual returns the facts on which they base their claims for interest paid?

Mr. Leming. That is one of the things, Senator, I wanted to go into with you to show you the whole set-up. You can't answer it just one or the other, yes or no. I would just like to take all these returns and go into that feature of it with you. Congressman Treadway inquired about that and I promised him some time ago I would do that, and I can do it now or when it is agreeable.

Senator Harrison. Mr. Leming, then from this chart it appears that the total amount of interest deduction disallowed by the Treasury on these six cases was $1,482,427.52?

Mr. Leming. That's right.

Senator Harrison. I think we ought to go into the others just as we have finished the Dwight matter. We can't finish today.

Mr. Leming. I haven't finished with the Dwight matter yet.

Mr. Vinson. Under the head of "Additional tax", if I understand it correctly, that is the computation of tax inclusive of interest?

Mr. Leming. No; just tax alone. It does not include interest.

If you add interest you get a much greater amount.

Mr. Vinson. It also does not include penalties?

Mr. Leming. No, sir.

Mr. Vinson. It does not include interest though?

Mr. Leming. It does not include interest.

The Chairman. I would like to supplement that request, that the original returns of these other cases be furnished along with that of Mr. Dwight: if that is agreeable to the committee.

Mr. Treadway. I would like to ask Mr. Helvering, if there has been any extended correspondence with these various men? You have explained Mr. Dwight's case particularly. Has there been correspondence running over a period of years concerning these disallowances, in addition to the conversation with the man who came to see Mr. Shafroth some time ago?

Commissioner Helvering. The matter has perhaps been in discussion for 2 years.

Mr. Treadway. With the taxpayers or in the Department?

Commissioner Helvering. With the taxpayers and in consultation with their attorneys in the Department.
Mr. TREADWAY. It is not a new proposition coming to your attention. That has been brought out several times.

Mr. LEMING. No.

Mr. ARTHUR H. KENT, Assistant General Counsel, Treasury Department. In fairness to all the parties concerned, I suggest that there be included in the record the cards which were sent out on June 10, 1937, announcing the dissolution of the firm of Hughes, Schurman & Dwight in New York and the constitution of two new firms, these cards containing the names of the members of the two firms resulting from the dissolution of the old one.

The CHAIRMAN. Have you the cards?

Mr. KENT. I have the cards here.

The CHAIRMAN. Without objection they will be inserted in the record.

(The cards referred to read as follows:)

100 BROADWAY, NEW YORK.

The firm of Hughes, Schurman & Dwight, having been dissolved, the undersigned have formed a partnership for the practice of law under the name of Hughes, Richards, Hubbard & Ewing.

CHARLES E. HUGHES, Jr.
AUGUSTUS L. RICHARDS.
ALLEN S. HUBBARD.
OSCAR R. EWING.
HAROLD L. SMITH.
LEIGHTON HOMER SURBECK.
WILLIAM T. GOSSETT.
FRANCIS C. REED.

JUNE 10, 1937.

100 BROADWAY, NEW YORK.

The firm of Hughes, Schurman & Dwight, having been dissolved, the undersigned have formed a partnership for the practice of law at the above address under the name of Dwight, Harris, Koegel & Caskey.

RICHARD E. DWIGHT.
RALPH S. HARRIS.
OTTO E. KOEGEL.
JOHN F. CASKEY.
FRANK C. FISHER.
FREDERICK W. R. PRIDE.

JUNE 10, 1937.

(Whereupon, at 12:15 p. m., an adjournment was taken until 10 a. m., Wednesday, June 23, 1937.)

EXHIBIT 2

The following is a lawful method of lowering the taxable category of the individual's net income. It may be advantageously applied to net income of $75,000 or more.

It is only applied after all exemptions and deductions have been taken advantage of by the taxpayer, if his net income, then subject to tax, is $75,000 or more.

The principles of the method have been successfully used by numerous taxpayers during the past 10 years on the recommendation of their legal counsel.
**Example of a hypothetical taxable income of $150,000**

If a taxpayer's taxable income in 1932 is $150,000, subject to Federal normal and surtax and to New York State income tax, his taxes, payable in 1933, will be $65,600.

If he can establish an allowable deduction of $130,728 against this taxable income, his reduced taxable income will be $19,272, on which Federal and New York taxes, payable in 1933, will be $1,990.

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Difference in taxes</td>
<td>63,670</td>
</tr>
<tr>
<td>If the establishment of this deduction has resulted from an outlay of</td>
<td>18,340</td>
</tr>
<tr>
<td>Difference in taxes less outlay</td>
<td>45,330</td>
</tr>
<tr>
<td>If he pays a service fee of</td>
<td>11,330</td>
</tr>
<tr>
<td>Net saving</td>
<td>34,000</td>
</tr>
</tbody>
</table>

The taxpayer purchases a single-premium, participating, life-insurance policy for $3,500,000; the single premium for which, at age 55, is $2,343,220.

Because a loan is to be made at once on the policy and of the conditions of the policy, no physical examination is required.

To enable him to pay the premium on the policy and the interest on the loan in cash, arrangements are made for him to borrow from a bank, on his demand note, $2,455,617, which is placed to his credit, and to which he adds funds of his own of $18,340, giving him a total credit with the bank of $2,473,957.

He pays the premium on the policy and has remaining with the bank a credit of $2,376,885.

He then makes a loan from the insurance company, on the sole collateral of the policy, of the reserve value of the policy at the end of the first policy year.

Leaving him a credit of $2,507,613.

Under the terms of the loan agreement which he enters into with the company, the loan cannot be called during his lifetime, except with his consent; also, the loan agreement is not a negotiable instrument.

He pays the company one year's interest on the loan at 5½ percent in advance.

Leaving him a credit of $2,376,885.

Under the Revenue Act of 1932, sec. 23 (b), all interest paid during the taxable year on indebtedness is deductible from gross income, except on certain forms of indebtedness not applicable to the above circumstances.

The company also loans him the discounted value of the dividend payable under the policy at the end of the first policy year.

Leaving him a credit with the bank of $2,455,617.

With which credit he repays his demand note bank loan of that amount. He pays the bank 1 day's interest on the loan.

His net cash outlay in the above transaction has been (plus 1 day's interest on his bank loan) $18,340.
### Examples of Various Taxable Incomes

**Taxable Income subject to Federal normal and surtax and New York State income tax (married man, no dependents, age 55)**

<table>
<thead>
<tr>
<th>Taxable income</th>
<th>$75,000</th>
<th>$100,000</th>
<th>$150,000</th>
<th>$200,000</th>
<th>$250,000</th>
<th>$500,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interest paid on loan</td>
<td>115 percent.</td>
<td>115 percent.</td>
<td>115 percent.</td>
<td>115 percent.</td>
<td>115 percent.</td>
<td>115 percent.</td>
</tr>
<tr>
<td>Federal and New York taxes on reduced taxable income</td>
<td>1,938</td>
<td>3,223</td>
<td>6,569</td>
<td>9,101</td>
<td>10,480</td>
<td>18,801</td>
</tr>
<tr>
<td>Differences in taxes</td>
<td>18,915</td>
<td>31,435</td>
<td>63,760</td>
<td>95,360</td>
<td>125,480</td>
<td>240,460</td>
</tr>
<tr>
<td>Net outlay to insurance company</td>
<td>7,860</td>
<td>10,460</td>
<td>18,800</td>
<td>26,920</td>
<td>31,224</td>
<td>61,448</td>
</tr>
<tr>
<td>Gross saving</td>
<td>11,055</td>
<td>20,955</td>
<td>45,530</td>
<td>70,440</td>
<td>94,350</td>
<td>218,400</td>
</tr>
<tr>
<td>Fee</td>
<td>2,754</td>
<td>5,299</td>
<td>11,330</td>
<td>17,524</td>
<td>23,045</td>
<td>54,711</td>
</tr>
<tr>
<td>Net saving</td>
<td>8,291</td>
<td>15,656</td>
<td>34,200</td>
<td>52,916</td>
<td>70,955</td>
<td>164,135</td>
</tr>
</tbody>
</table>

The revenue act of 1932 provides:

**Sec. 23. Deductions from gross income.** In computing net income there shall be allowed as deductions:

(b) Interest: All interest paid or accrued within the taxable year on indebtedness, except on indebtedness incurred or continued to purchase or carry obligations or securities (other than obligations of the United States issued after Sept. 24, 1917 and originally subscribed for by the taxpayer) the interest upon which is wholly exempt from the taxes imposed by this title, or (2) on indebtedness incurred or continued in connection with the purchasing or carrying of an annuity.

New York State personal income-tax law provides:

**Sec. 360.** In computing net income there shall be allowed as deductions:

(2) All interest paid or accrued during the taxable year on indebtedness. Note change in revenue act of 1932 regarding stock losses.

Rev. Act 1932, Sec. 23. Deductions from gross income. In computing net income there shall be allowed as deductions:

(e) Losses by individuals. Subject to the limitations provided in subsection (r) of this section, in the case of an individual, losses sustained during the taxable year and not compensated for by insurance or otherwise.

(2) If incurred in any transaction entered into for profit, though not connected with trade or business.

(r) Limitations of stock losses. (1) Losses from sales or exchanges of stocks and bonds (as defined in subsection (t) of this section) which are not capital assets (as defined in section 101) shall be allowed only to the extent of the gains from such sales or exchange (including gains which may be derived by a taxpayer from the retirement of his own obligations).

**Assuming the net annual income to remain constant at $150,000 and Federal and New York State taxes to remain on their present bases, the following additional savings can be made in the second to the fifth years.**

<table>
<thead>
<tr>
<th></th>
<th>Second year</th>
<th>Third year</th>
<th>Fourth year</th>
<th>Fifth year</th>
</tr>
</thead>
<tbody>
<tr>
<td>Additional loan on policy</td>
<td>$33,831</td>
<td>$33,789</td>
<td>$33,067</td>
<td>$33,955</td>
</tr>
<tr>
<td>Discounted dividend loan</td>
<td>79,030</td>
<td>80,157</td>
<td>80,281</td>
<td>82,408</td>
</tr>
<tr>
<td>Total additional loan for year</td>
<td>112,861</td>
<td>113,946</td>
<td>115,348</td>
<td>116,381</td>
</tr>
<tr>
<td>1 year's interest on policy loan</td>
<td>102,601</td>
<td>103,644</td>
<td>105,515</td>
<td>106,561</td>
</tr>
<tr>
<td>Net cash outlay to insurance company</td>
<td>60,730</td>
<td>28,065</td>
<td>21,067</td>
<td>21,623</td>
</tr>
<tr>
<td>Federal and New York taxes on present taxable income</td>
<td>65,660</td>
<td>65,660</td>
<td>65,660</td>
<td>65,660</td>
</tr>
<tr>
<td>Federal and New York taxes on reduced taxable income</td>
<td>2,058</td>
<td>1,745</td>
<td>1,451</td>
<td>1,024</td>
</tr>
<tr>
<td>Difference in taxes</td>
<td>63,602</td>
<td>63,872</td>
<td>64,209</td>
<td>64,996</td>
</tr>
<tr>
<td>Gross saving: difference in taxes less net cash outlay to insurance company</td>
<td>43,872</td>
<td>43,400</td>
<td>43,142</td>
<td>42,813</td>
</tr>
<tr>
<td>Service fee</td>
<td>1,774</td>
<td>0,611</td>
<td>1,314</td>
<td>1,281</td>
</tr>
<tr>
<td>Net saving for year</td>
<td>35,098</td>
<td>32,869</td>
<td>31,833</td>
<td>31,532</td>
</tr>
<tr>
<td>Total saving to date</td>
<td>60,908</td>
<td>105,995</td>
<td>144,524</td>
<td>183,356</td>
</tr>
<tr>
<td>Total saving to date plus 5 percent</td>
<td>70,788</td>
<td>111,130</td>
<td>165,065</td>
<td>202,039</td>
</tr>
</tbody>
</table>

* 20 percent.  
* 15 percent.  
* 10 percent.
To whom it may concern:

With reference to the foregoing uses of single premium life-insurance policies, the figures quoted and the specimen forms displayed are the figures and forms which, we are informed, are used by the Standard Life Insurance Co., Ltd., of Nassau, Bahama Islands.

We are further informed that this company is not licensed to do business in the United States, and for those further interested in the matter it will be necessary to communicate directly with the company.

We are not acting as agents or representatives of the company, and have no power to do so. In the event of policies being purchased directly from the company, we certify that we will receive no commission or other compensation from it on such business.

Our services are limited to advising prospects of the general advantages of this particular type of insurance. We make no representations as to the law and give no legal opinions of any kind.

Those interested may also compare the rates quoted with the standard rates used by any of the leading domestic companies.

Baylis-Baber Co.,
45 East Fifty-fifth Street, New York.

It is believed that the method herein described is sound and can be successfully used, but no representations as to the law are made.

Any person interested in adopting it should first consult his own legal counsel.

Baylis-Baber Co.,
45 East Fifty-fifth Street, New York.

THE SUPREME COURT OF THE UNITED STATES

In the case of U. S. v. Isham (17 Wallace Rep. 490), held that although a specific transaction may be a device to avoid the revenue acts and although its operation may have the effect of avoiding them, yet, if the device be carried out by means of legal forms, it is subject to no legal censure.

The Solicitor of Internal Revenue in his opinion no. 1062, rendered in the year 1921, has cited the above case and has announced its doctrine as controlling the action of the Internal Revenue Department. He says: "The fact that the transaction here involved had for its purpose the reduction of taxes does not make it fraudulent, provided the means employed were in themselves legal. This principle was clearly stated by the Supreme Court of the United States in U. S. v. Isham, which has never been modified or overruled."

In the case of Bullen v. Wisconsin it was held: "We do not speak of evasion, because, when the law draws a line a case is on one side of it or the other, and if on the safe side, is not the worse legally because a party has availed himself of what the law permits."

In the case of Sup. Oil v. Miss. it was held: "The fact that it is desired to evade the law, as it is called, is immaterial, because the very meaning of a line in the law is that you intentionally may go as close to it as you can if you do not pass it."

For those further interested in this particular phase of the subject, reference may be made to such publications as Sears on Minimizing Taxes, Klein on Federal Income Taxation, Hartman on Tax Avoidance.
The joint committee met in the hearing room of the Committee on Ways and Means in the New House Office Building, at 10 a.m., Hon. Robert L. Doughton (chairman) presiding.

The CHAIRMAN. The committee will be in order. When we adjourned yesterday Mr. Leming had not concluded his statement. Will the gentleman please take the stand. Is there something more that you would like to state independent of questions?

STATEMENT OF MASON B. LEMING—Resumed

Mr. Leming. My thought is this, Mr. Chairman, that in what I said yesterday and the questions which were asked, perhaps I should simply better say this, this morning, that I have nothing further to say, unless the committee wishes to ask me some further questions.

Senator HARRISON. I want to ask the witness some questions.

The CHAIRMAN. Senator Harrison.

Senator HARRISON. You discussed at some length the case of Mr. Dwight. In that case you stated that on the tax return of 1932 the examiner representing the Treasury had detected that the deductions were not allowable, and they were not allowed. How about the case of Ayres, whose name you called yesterday, and to whom an insurance policy was issued in 1932?

Mr. LEMING. I believe the file will show, Senator, that they were all handled similarly. That is my recollection of the file.

Senator HARRISON. When the examiner ascertained that he was taking an interest deduction on this insurance loan, on the policy issued to him, that was not allowed?

Mr. LEMING. No.

Senator HARRISON. And I noticed, in the case of Mr. Ayres, that in the case of 1932 the deduction disallowed was $10,010, but that from the years 1933 to 1936 the device was not used. Will you tell the committee whether or not he claimed them in those years, or whether he abided by the protest of the examiner and the Department that year, and did not claim this deduction for the succeeding years?

Mr. LEMING. He did not claim it in those years.

Senator HARRISON. He did not claim it?

Mr. LEMING. No, sir.

Senator HARRISON. But he paid his income?
Mr. LEMING. I understand there was no reduction by reason of that device; I do not know what tax, if any, he paid.

Senator HARRISON. Let us take the case of Mr. Lowe. The interest deduction disallowed in 1933 was $91,000, plus. In 1934 the deduction disallowed was $86,000, plus; in 1935, $93,000, plus; and in 1935, $95,000, plus. So he took his deductions, or attempted to?

Mr. LEMING. Yes.

Senator HARRISON. Do you have any facts as to whether or not Mr. Ayres was told that in similar cases to his the deduction had not been allowed, or to Mr. Lowe, that in the case of Mr. Ayres, who had a similar policy to Mr. Lowe, that Mr. Ayres was not claiming it, but that Mr. Lowe was still claiming his deductions, or to any of the other parties whose names are mentioned in this memorandum?

Mr. LEMING. I am sorry, Senator, but I did not get the full import of the question.

Senator HARRISON. Was the information carried to any of the other parties here, except Mr. Ayres, who when it was pointed out to him that the deduction was not allowed, did not claim it, then, in the succeeding years after 1932. Was that fact pointed out to these other gentlemen named in this memorandum who were similarly situated to Mr. Ayres?

Mr. LEMING. My answer to that would be this: That where they had no income for its use it would not be used. In all of those cases we have shown on the chart, there, that you have examined, Senator, with those disallowances, that the device was used. If I get the further part of your question it is this: Did they discontinue, after being advised that the deductions were not good?

Senator HARRISON. Yes.

Mr. LEMING. Is that the question?

Senator HARRISON. That is the question.

Mr. LEMING. In the case of Mr. Dwight, of course, as I believe the record already shows, he did not discontinue. I think the record will show this, too, that copies of the agents' reports as they were made were furnished to him, and following through that procedure without going back to the file for actual verification, I should say that each time an agent made that report on one of them in the ordinary course, that taxpayer would get a copy of that report. He would therefore be advised of the agent's recommendation, as of the time.

Senator HARRISON. Your reason advanced why Mr. Ayres did not claim these deductions is probably borne out by the facts, because he only paid a tax in 1932 of $248. It does not state here whether he paid any tax or not in succeeding years. This chart says "This deduction was not used."

Mr. LEMING. As I said yesterday, where that statement occurs on that chart—the chart could have been made fuller in this respect, showing the tax liability where the device was not used—but that note simply means this, that there was either no tax due, or the device was not used.

Senator HARRISON. What you said about Mr. Lowe in that respect would apply also to Mr. Marx, Mr. Schwab, and Mr. Thomas?

Mr. LEMING. I should say so; yes, sir.
Senator Harrison. When these deductions, in the case of Mr. Lowe, were made and disallowed, what did he do, if anything, and what did the Government do?

Mr. Lening. The usual procedure in cases of that kind is this—and I have in mind particularly Mr. Dwight's case here, because I have followed it through step by step, and the others follow along the same line—as soon as the revenue agent makes his report, and a copy of that is served upon the taxpayer, the original report is held in the office of the agent in charge in that district. As in the Dwight case, for instance, while the report was made, or the examination I think was made sometime in about June 1934—

Mr. Vinson. Examination by whom?

Mr. Lening. By the revenue agent. That report went to the office of the agent in charge in New York, with a copy to Mr. Dwight. Thereafter Mr. Dwight filed a protest with the agent in charge in New York. There was then a conference of some sort in the agent's office in New York City. Afterward, and after that conference, the agent then forwarded the report and all papers to the Commissioner. As I recall, that occurred, perhaps, in January 1935.

Mr. Vinson. Senator Harrison, will you yield?

Senator Harrison. Certainly.

Mr. Vinson. It just seems to me we ought to have a definite history in regard to the manner in which that return and other returns were handled, in regard to the time when a certain man made a report, just what happened to the return, and it seems that you are really indefinite as to dates.

Under Secretary Magill. Mr. Chairman, I think Mr. Vinson is quite right. Why do we not give you a timing schedule of what happened? At such time, the return was filed, and it had such and such on it, and there were these hearings, and so on, as to each of these men. That can be prepared, and you can have it.

Senator Harrison. Are you ready to give that this morning?

Under Secretary Magill. I do not think we have it now, but it will be prepared.

Mr. Vinson. I suggest, Mr. Chairman, that it be inserted in the record at this point.

Under Secretary Magill. I think it should be. I think you are quite right.

The Chairman. Without objection, that will be inserted in the record.

(The data referred to was to be subsequently furnished for the record, and when furnished will be found later in the printed hearing.)

Senator Harrison. Without reference to the Dwight case, the same thing, it seems to me, should be done with reference to the Lowe, Marx, Schwab, and Thoms cases.

Under Secretary Magill. I had that in mind. My feeling as to that is that we ought to give you the complete facts as to all of these people, and it can easily enough be prepared. It is just a matter of running through the files, which are pretty voluminous, and setting down the dates, which we will do.

The Chairman. The committee will certainly appreciate that, if you can furnish it.
Under Secretary Magill. Certainly. We will have that at the next session of the committee.

The Chairman. Give it to the stenographer and it will be inserted in the record.

Mr. Cooper. Mr. Chairman?

The Chairman. Mr. Cooper.

Mr. Cooper. Mr. Leming, you have given this information with reference to these six taxpayers listed on this chart.

Mr. Leming. Yes.

Mr. Cooper. It is my understanding that all six of these men availed themselves of the use of the same insurance company at Nassau. Is that right?

Mr. Leming. Yes.

Mr. Cooper. Do you have any information that you desire to present to the committee at this time as to any other similar insurance companies that might have been used by other people?

Under Secretary Magill. Mr. Chairman, I do not know whether Mr. Leming has gone into other insurance companies or not, but the fact is we do have partially prepared facts as to some other similar situations which we will be glad to give you. As I have said earlier, what we are giving you here is the completely prepared case which we have, and I think it is quite clear that there are other instances in which this device has been used.

Mr. Cooper. The information thus far given on the device of foreign insurance companies has been limited to one company that issued six policies. That is correct, is it not?

Under Secretary Magill. Right.

Mr. Cooper. Was it six or eight policies issued to them?

Under Secretary Magill. There were eight. I think, to six people.

Mr. Cooper. To six people? Two of them had two policies each?

Under Secretary Magill. Yes.

Mr. Cooper. I was just wondering whether or not it had thus far been discovered by the Treasury Department agents as to whether any other insurance companies in Nassau or any of these other places similarly situated had been used by other taxpayers and whether or not you were prepared at this time to give us that information?

Under Secretary Magill. I can answer that last part. We have not the information prepared to give you at this time. As to the rest of it, this particular device has been used, I know, in the case of other companies; and, as I believe was said yesterday by Mr. Leming, you get all gradations of this device from the ordinary perfectly legitimate policy loan that any insured person may make with his own insurance company, which loans, of course, have been made in millions of dollars during the depression. You get all those cases on the one end, then grading along to these cases where the company is simply a shell with no assets. We have presented you that extreme case.

Mr. Cooper. I agree with you that the information thus far presented illustrates the point that you have in mind and that we are anxious to know about, but I was just wondering whether or not other insurance companies of a similar type had been used by other taxpayers for the same purpose.
Under Secretary Magill. As you see, I cannot tell you definitely on that subject. We are working here, as you know, under rather severe limitations of time.

Mr. Cooper. Yes; I appreciate that and agree with you in that conclusion.

Under Secretary Magill. And we want to cooperate with you, whether it appears that way or not. We are very anxious to give you no case that we have not analyzed thoroughly and completely, because we want to be entirely fair to the persons who are being brought into this.

Mr. Cooper. I think you are exactly right in that position. Would you be prepared at this time to give us any idea as to about how many other insurance companies that you might know of that were used in a similar manner?

Senator Walsh. Will the Representative yield?

Mr. Cooper. Yes; with pleasure.

Senator Walsh. I understand him to say that he knows of no other insurance companies of this character, that have no assets, that have negotiated contracts with taxpayers similar to this.

Under Secretary Magill. So far as my personal knowledge is concerned, it’s true.

Senator Walsh. I understood that to be true. You suspected it, but you did not know.

Under Secretary Magill. So far as I am concerned, I have not made the investigations in these cases. All I know is what I get from the men who have.

Mr. Vinson. As a matter of fact, have you sufficient personnel working on these matters? And if that embarrasses you to say it, it seems to me that you have not, and it seems to me that it is of such prime importance that you ought to get personnel to do this job. Here are eight policies in which it is admitted that there is $561,000 plus, exclusive of interest, that has not been paid into the Treasury. Now, it just seems to me that there ought to be a complete overhauling and scrutiny of the deductible items within the period of limitation.

Under Secretary Magill. You are entirely right.

Mr. Vinson. It just seems to me that if you are embarrassed about lack of personnel, you ought to get it.

Under Secretary Magill. I am glad to hear you say so. As you will recall, in the Secretary’s statement he brought out the fact that we were dubious about bringing out, but we wanted to give you the actual situation, that a comparatively small number of the total number of returns that are filed can be carefully audited with the personnel which we now have available. If we had more personnel, I think it is clearly true that the amount of revenue which would be brought in would far exceed the salaries of the personnel. That has been our experience in the past, and I think it would be in the future.

Mr. Vinson. I am talking now not only about that personnel, but the personnel that will enable you to get this information to the joint committee at the earliest possible moment, because I know the regular work has to be carried on.
Under Secretary Magill. That is our supreme difficulty at the moment. We have 6,000,000 returns that we have to audit and examine in the ordinary course. We have got to carry on our ordinary administrative work; and, of course, the staff which has been detached for this work, from myself down, is compelled to devote its time to this day and night, instead of doing our ordinary administrative tasks. We have to see that that goes on, anyway.

Senator Walsh. Mr. Chairman.

The Chairman. Senator Walsh.

Senator Walsh. Is it not, after all, the business of the Treasury Department to investigate these cases originally in detail and take action, and that it is our business to know the methods and systems—one case is as good as a hundred—where there is evasion, for the purpose of correcting the law? It does not seem to me it is necessary to have every one of the hundred cases presented to us. We might have that list, if you wish, but it seems to me we have accomplished the purpose of this resolution if dependable examples of evasion are presented to us, in every phase of evasion. Then if a bill is presented covering the whole we shall have done our duty.

Mr. Vinson. If I understood it, though, he said there is gradation, there is difference in degree, and unless they look into these matters we may be able to plug one particular hole, but unless they know about the others some other slick artist may be getting by.

Senator Walsh. I agree with you, if there are gradations we ought to have that; but I infer from what he says that there is a suspicion that some people in dealing with legitimate insurance companies have borrowed when they did not need to. That is what I have inferred from the witness's statement, and he has no reason to know it was dishonest or that it could have been so.

Under Secretary Magill. I, of course, referred to the two extreme cases, as you appreciate. That is, you or I might have insurance policies in the Equitable Life Insurance or the Northwestern or some others. We might find ourselves in the need of money and borrow money on the policies. No one in the world will question that the interest is a legitimate deduction under the present law. Then you grade all the way from that case to the case where the insurance company is simply a shell.

Senator Walsh. May I ask you a question or two about procedure, in order that I may understand?

Under Secretary Magill. Yes, sir.

Senator Walsh. On the 15th day of March, every taxpayer in the country makes a return. Is that correct?

Under Secretary Magill. Not quite, because if the taxpayer is on a fiscal-year basis he may make his return—

Senator Walsh. But it is filed in the Treasury, in the collector's office in some part of the country?

Under Secretary Magill. So far as returns made on a calendar-year basis are concerned, they are filed on March 15.

Senator Walsh. All right. Now, there is an assumption that they are all honest returns, of course?

Under Secretary Magill. Yes, sir.

Senator Walsh. At some later date somebody in the Internal Revenue Bureau, or some group of employees goes through all of
these returns and selects a certain number for special examination and special study. Is that correct?

Under Secretary Magill. That is true.

Senator Walsh. What percentage are selected for special examination and special study?

Under Secretary Magill. The Commissioner can answer that better than I.

Senator Walsh. I understand it is not all of them. Is that correct?

Under Secretary Magill. Or perhaps Mr. Russell can.

Mr. Charles T. Russell (Deputy Commissioner, Bureau of Internal Revenue). Of the 6,000,000 returns last year, perhaps 500,000.

Senator Walsh. So that 500,000 and some after March 15 are selected for special study and examination. The others are never examined, and there is an assumption that they are honest taxpayers and have paid an honest tax, is that correct?

Mr. Russell. Of the 6,000,000 returns probably 700,000 or 800,000 are sent to the field, and they are all the larger ones, and the agents pick out 500,000 of them for examination.

Senator Walsh. On what basis are these 500,000 or 700,000 selected? Is it the heavier taxpayers or the larger ones, or is it something in the appearance of the return that raises questions?

Mr. Russell. It is both, Senator.

Senator Walsh. But all are large returns?

Mr. Russell. Yes, sir.

Senator Walsh. Wouldn't it put you on notice immediately, at once, if a taxpayer had a large income of $175,000, such as these men had; wouldn't that put you on notice immediately without a Senate investigation and inquiry being made?

Mr. Russell. They would probably be examined.

Senator Walsh. Now, then, in connection with these 600,000 returns that are examined, when do you get reports on them?

Mr. Russell. Prior to 1935 they started in the field investigating returns filed March 15 on the following March 15 and continued them for approximately 1 year.

Senator Walsh. So that all the time you are approximately 2 years behind?

Mr. Russell. But not now; we have advanced the examinations 9 months.

Senator Walsh. So it takes about 2 years to make an examination into a questionable return for the purpose of the Department determining whether or not further negotiations are to be taken up with the taxpayer?

Mr. Russell. At that time it did, but not now.

Senator Walsh. Now, as to the other tax returns, the only way we have of discovering errors or mistakes is when somebody may write in from outside and say that John Brown made an incorrect return?

Mr. Russell. No, sir; the balance of the returns move through the Audit Division in the office here, and an auditor goes over them and if anything looks wrong they are sent to the field.

Mr. Treadway. Speaking of personnel, I think there was an added personnel provided in the law 2 years ago. That has come out in
the hearing already, hasn’t it? Didn’t we provide for a large num-
ber of new employees?

Mr. Russell. That is right, Congressman.

Mr. Treadway. What is their official title?

Mr. Russell. Internal-revenue agents.

Mr. Treadway. Are they field men or located here?

Mr. Russell. They are field men.

Mr. Treadway. None of them are here in Washington?

Mr. Russell. No, sir.

Mr. Vinson. They pick up $80,000,000 annually?

Mr. Russell. Approximately $80,000,000 last year.

Mr. Treadway. The fact that you were 2 years behind, as you told
Senator Walsh, and now are only 9 months behind—didn’t I under-
stand you to say that?

Mr. Russell. No; we advanced the examinations 9 months.

Mr. Treadway. That is, then, you are now a year and three months
behind; is that the idea?

Mr. Russell. Prior to 1935 a return filed on March 15 we did not
start examination until the following March 15, but now a return
filed on the 15th of this year we will start checking July 1 of this
year, 3 months after filing. Of course, we can’t check them all, but
we start now examining returns 3 months after filing.

Mr. Treadway. Have you increased also the number you send back
to the field for examination as a result of the employment of these
new men 2 years ago?

Mr. Russell. That is right; and that will be increased for two
reasons. As recovery from the depression comes, we get more of the
larger returns that we have to send back to the field. An agent in
charge knows that his men can only examine so many returns. Out
of the batch of returns sent him he picks that many returns, probably
plus a few hundred more that he will check if he has time.

Mr. Treadway. Is that selection determined by localities particu-
larly, or is it where the larger taxpayers are found?

Mr. Russell. No.

Mr. Treadway. How many field districts have you?

Mr. Russell. Thirty-eight.

Mr. Treadway. That is less than one to a State?

Mr. Russell. Yes, sir.

Mr. Treadway. Some States, as New York, for instance, have more
than one district?

Mr. Russell. New York has three.

Mr. Treadway. Naturally your largest returns would be in the
centers like New York, Philadelphia, Chicago, Boston, and San
Francisco?

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

Mr. Treadway. So there you center on these particular examina-
tions, is that correct?

Mr. Russell. That is right.

Mr. Treadway. Just one other reference to personnel, and this is
more or less on the side—how many representatives of the Treasury
and Internal Revenue Bureau are here in the room at this minute?

Mr. Russell. I imagine about 15 or 16.

Mr. Treadway. About 16?

Mr. Russell. That is right.
Mr. TREADWAY. Are all of them needed here this morning, or could some of them be occupied downtown?

Mr. RUSSELL. Well, I think they are probably all needed here. They have to know what is going on in order to prepare this material for you gentlemen.

Mr. TREADWAY. It looked to me as though there was a pretty good supply of personnel at the present time, from appearances here.

Mr. VINSON. Mr. Russell, reference has been made to the 500,000 or 700,000 returns where there are examinations and audits made. I think it would be well for you to state for the record what sort of inspection or examination is made of the other 5,000,000 returns.

Mr. RUSSELL. Well, the smaller returns, what we call the 1040a, with gross income less than $5,000, are retained in the collector's office.

Mr. VINSON. They are inspected in the collector's office?

Mr. RUSSELL. That is right. They never move to Washington.

Mr. VINSON. They are inspected in the collector's office?

Mr. RUSSELL. That is right. The rest of the returns here in Washington move through the Audit Division, and if an auditor sees something wrong when he examines them, if anything looks wrong, he sends it to the field. Every return where something looks wrong, that goes to the field.

Mr. VINSON. How many 1040a returns are there?

Mr. RUSSELL. There are about a million eight hundred thousand, possibly 2 million.

Mr. TREADWAY. In that connection, are they civil-service employees or are they exempt?

Mr. RUSSELL. Every one of them civil service.

Mr. TREADWAY. There are no additional funds being used other than the direct appropriation—I am referring directly to the W. P. A. funds?

Mr. RUSSELL. Outside of the W. P. A. funds which we used for a year or so, there are no other funds being used.

Mr. TREADWAY. There are no W. P. A. funds being used at the present time?

Mr. RUSSELL. We are discontinuing the W. P. A.

Mr. TREADWAY. Does that apply to the central office and to the field as well?

Mr. RUSSELL. We never had any W. P. A. employees in Washington.

Mr. TREADWAY. They were all employed in field work?

Mr. RUSSELL. Yes, sir.

Mr. TREADWAY. And you are reducing them as rapidly as you can?

Mr. RUSSELL. Yes.

Mr. TREADWAY. Dr. Magill, in connection with the single-premium insurance policies to which reference has been made, as I understand, the single payment is largely the criticism being made of these policies that Mr. Leming has explained to us?

Under Secretary MAGILL. Not quite, Mr. Treadway—I am not an expert on this particular device and these other men are. The objection in this case is not the fact that a taxpayer paid a single premium. That could be done with a legitimate policy. The objection here, I
take it, is primarily that the company itself had no bank account, was in no position to write insurance policies, certainly in such size as it did, and that, so far as the payment of the premium and the loan is concerned, they were simultaneous transactions carried out by one man, so that the whole thing looks like a sham.

Mr. Treadway. Doctor, would you object if I refresh your memory? I don't know that I need to, but would you object to my calling attention to the book that is entitled "Federal Taxes on Estates, Trusts, and Gifts", by Robert H. Montgomery and Roswell Magill? I assume that is the Roswell Magill I am addressing at the moment?

Under Secretary Magill. I think it is.

Mr. Treadway. I quote from page 398, Mr. Chairman, of that book:

It is sometimes possible to make substantial savings in income tax, estate tax, or both, by investing a large part of an estate in annuities and in single-premium life insurance in any proportion desired. The owner of 5 millions worth of property realizes that the estate tax will cause his estate to shrink by 38 percent at his death, and thus he can transfer only $3,008,600 to his wife, the sole beneficiary under his will.

The owner of $5,000,000 worth of property realizes that the estate tax will cause his estate to shrink by 38 percent at his death, and thus he can transfer only $3,098,600 to his wife, the sole beneficiary under his will. His property produces income of 3 percent per year, or $150,550 net after income tax. At age 55 he purchases a life annuity for $1,342,000, which will yield him the same amount of income, after deducting an income tax assessed on only 3 percent of the purchase price. With the remainder of his funds he takes out $4,543,476 of life insurance, paying a single premium of $2,979,748. He then makes a gift to his wife of insurance policies having a face amount of $4,463,476 (for which he paid a premium of $2,927,282). He retains no incidents of ownership in the policies and therefore pays the gift tax of $78,252 on the premium. The remaining $80,000 of insurance, of which the wife is beneficiary, is retained because this amount is exempt from the estate tax. Under this arrangement his wife will receive at his death $4,543,476, the face amount of the insurance policies, or only $456,524 less than the original $5,000,000 estate, which has therefore suffered a shrinkage of only 9.1 percent instead of 38 percent.

That is practically the logic of the Bermuda Co., isn't it?

Under Secretary Magill. I would say clearly not. As I said to you a minute ago, we are presenting to you here the case of a fake insurance company and fake payments, and, so far as the book is concerned, we are showing you how insurance may be used in connection with an estate with a real insurance company and real payments.

Mr. Vinson. Will the Congressman yield?

Mr. Treadway. I am not yielding the floor at this time.

This is a new type of witness. He wants to explain things more than some witnesses do. Now, just this thought, aside from the fact that the Bermuda Co. was a foreign set-up, this possibility of beating the Government out of estate taxes by the purchase of single-premium insurance policies is pretty accurately described in that book, isn't it?

Under Secretary Magill. No.

Mr. Treadway. I am sorry—I have always taken you to be an expert on this line of business.

Mr. Vinson. Dr. Magill, isn't the relationship just about the same as it is between zero and infinity?

Mr. Treadway. Oh, what an illustration that is.
Mr. Vinson. In connection with an insurance company—

Mr. Treadway. May I interrupt? I would like to say to my colleague on the committee I don’t think Dr. Magill needs any tips as to how to answer questions. He is very expert on that.

Under Secretary Magill. You flatter me, Mr. Treadway. I would say rather that the distinction is between the two types of cases which Senator Walsh was bringing out earlier in this morning’s meeting. You and I probably both have insurance policies. I know I do. Why do I take out insurance? Because I think it is a good way to take care of my wife and children. I could put my money in bonds or stocks or some other place.

In considering whether I will put it in insurance or in bonds or stocks I must necessarily consider the gift and estate tax, both of which are important elements with respect to any estate these days, particularly those estates which are much larger than mine will ever be. I am sure you or I would not object to an individual buying an insurance policy from a bona-fide insurance company and paying his premium, and if the proper taxes were levied on his estate, with the proper deductions made, neither you nor I would criticize. On the other hand, if the man goes through the form of taking out an insurance policy in a company which is virtually nonexistent except in form, I think both of us would criticize. That is, we would say he is trying to defeat the revenues by a mere device which is completely distinguishable from the case of a man who is taking out a real insurance policy in a real company.

Mr. Treadway. These cases that are cited in the Bermudas Co.—

Under Secretary Magill (interposing). Understand, I have no objection to his taking out a policy in the Bermudas or in the Sun Life Insurance Co. of Canada.

Mr. Treadway. You don’t need to go to Bermuda as far as getting an actual insurance policy is concerned.

Under Secretary Magill. No; that is the thing. If a man wanted $5,000,000 insurance, can you or I imagine his passing up the Massachusetts Mutual and going down to the Bermudas? To me it looks absurd. If you wanted $5,000,000 insurance, why in the world would you not take one of these American companies that have billions of dollars in assets, thoroughly reputable companies, instead of running down here to a little company with a 30-inch sign on some law office, a company which has no assets?

Mr. Treadway. I understood one of these men on the list has died.

Under Secretary Magill. Dr. Ayres.

Mr. Treadway. Has it been brought out—if so, I haven’t heard it—what happened to his large policy?

Under Secretary Magill. I don’t know. The provisions of the policy, as they have been reported to me, are to the effect that the loan is the first claim on the proceeds of the policy; so no doubt the proceeds of the policy, if paid, were used to pay off the loan.

Mr. Vinson. Will the gentleman yield?

Mr. Treadway. I yield.

Mr. Vinson. That is the point, that is the reason that the difference between the bona-fide loan on a bona-fide insurance policy and the Bahama Insurance Co. is the difference between zero and infinity. When the insured dies, holding a Bahama policy such as we have been discussing, his estate gets zero in money, whereas if it is a bona-
hile insurance company and the insured dies, then the sum in excess of the loan value is paid to the beneficiary of the estate; isn't that correct?

Under Secretary Macill. That is true.

Mr. Vinson. In other words, the Bahama Insurance Co. had no assets, they had nothing with which to pay the insured at the time of death, because he is ahead of the game; isn't that true?

Under Secretary Macill. That is true.

Mr. Vinson. And ahead of the game, under the expressed terms of the letter that Mr. Dwight wrote, which was a condition upon his taking out the policy?

Mr. Treadway. But the Dwight letter, Doctor, has no bearing on the Ayres transaction itself, has it? Mr. Dwight was not making any conditions for the Ayres' policy. It was only his case. So I don't think your illustration holds.

Mr. Vinson. What did Mr. Ayres say when he took out his policy?

Mr. Treadway. If he read it, it is all right.

Mr. Leming. You mean in the Bahaman Co.?

Mr. Vinson. Yes.

Mr. Leming. It is my understanding it is precisely the same as the Dwight one.

Mr. Treadway. I heard you read long conditions of the Dwight policies under which he took it out in 1932.

Mr. Leming. They were all the same.

Mr. Treadway. The 1932 application of Ayres was the same?

Mr. Vinson. The application of all of them was the same.

Mr. Leming. Our investigation showed they were all precisely the same. I would not want to say to you that there was not the changing of an "i" or "e", or something; but they were all substantially the same.

Mr. Treadway. Dr. Ayres is one of the men on this list that has died?

Mr. Leming. Right.

Mr. Treadway. Do you know of your own knowledge just what happened? Does it result as Mr. Vinson supposes? What became of the Ayres' policy on the death of Dr. Ayres?

Mr. Leming. I understood it is computed to be a liability of $158 on the part of the company.

Mr. Treadway. How is that?

Mr. Leming. The company would owe him $158.

Mr. Treadway. And that was $158 to be paid; is that the idea?

Mr. Leming. That is right, and it was in a foreign country and they would have to go down there to collect.

Mr. Treadway. That is what I was trying to get at—what became of the policy after he died.

Mr. Leming. I don't know what they did with the physical instrument.

Mr. Vinson. I will have to withdraw my zero to infinity example.

Mr. Treadway. It is $158 from infinity.

Mr. Vinson. The chairman says he has not collected the $158, so the zero to infinity still stands.

Mr. Leming. I take it that it has not been paid. That is the amount that has been figured out.
Mr. Treadway. One other question and then I will retire. Mr. Dwight did not use this scheme in 1936, but some of the others did, didn't they?

Mr. Leming. He used the scheme but he did not take the deduction—Mr. Dwight. I judge he simply lost his $10,000 that year. You see, he went through the same procedure in 1936 and paid something like $10,000 for the operation of the scheme again, but then before the filing time of his 1936 return came around, he decided for some reason not to avail himself of the deduction.

Mr. Treadway. The filing time was March 15, 1937, for 1936 income returns?

Mr. Leming. That is right.

Mr. Treadway. And in the meantime Mr. Shafroth testified yesterday that a representative of the firm, or a tax expert, whatever he was, a tax attorney, approached him and informed him of this difficulty in the Dwight firm, and that was the first information Mr. Shafroth had of this proposition, and of course if that occurred early in February, naturally Mr. Dwight would not have filed his return. Doesn't that explain why he did not use the device in his 1936 return?

Mr. Leming. Of course, that is a question Mr. Dwight himself would have to answer.

Mr. Treadway. Oh, no; you can answer it, with your legal wisdom. You don't need to avoid an answer and say you don't know that is the reason, but as a sensible man, isn't that the reason, in your mind?

Mr. Leming. Now, Congressman, I want to give you the right answer. You asked me this, why didn't he take the deduction in 1936?

Mr. Treadway. Yes.

Mr. Leming. Is that the question?

Mr. Treadway. You said for some unknown reason. I thought I explained the reason why he did not take it. Perhaps I didn't. Don't you agree with my reason?

Mr. Leming. Congressman, I could not answer for the operation of his mind.

Mr. Treadway. Of his mind or yours or mine, or all three?

Mr. Leming. Pardon me, yes; or Mr. Dwight's, either.

Mr. Treadway. You are a hard man to pin down, Mr. Leming.

Mr. Leming. I would like to tell you this, Mr. Congressman—

Mr. Treadway (interposing). I am not justifying Mr. Dwight; I am just trying to get some information.

Mr. Leming. We are talking about delays, Congressman. I want to say this, which is a fact: It was in January 1936, I believe, that Mr. Dwight asked us not to make an emergency assessment for 1932 or any other year. He wanted to try to continue to negotiate about the thing.

Mr. Treadway. In other words, Mr. Dwight was not trying to put anything over on the Bureau, was he?

Mr. Leming. I don't know.

Mr. Treadway. All you know is what you have got there for a record, isn't it?

Mr. Leming. Right. All I know is what the investigation of the case disclosed.

The Chairman. Are there any further questions?
Senator Harrison. I want to ask a question. It was stated here that Mr. Dwight recently has offered a check for $264,000, I believe, to the Government. That check included the amount of taxes claimed to be due, plus interest, without the penalty attached. Did any of the other of these five or six gentlemen offer a check to the Government in the payment of the tax?

Mr. Leming. I understand there are checks in all of them except Mr. Thoms.

Senator Harrison. Let us have the facts with reference to all of these cases.

Senator Walsh. Will you repeat what you just said?

Mr. Leming. I understand checks were offered in the cases of all except Mr. Thoms.

Senator Harrison. And, of course, in the estate of Dr. Ayres. When were these checks offered?

Mr. Leming. Senator, as I stated awhile ago, we can give you a complete schedule from our files. Those checks were offered in the last 4 weeks, all of them.

Senator Harrison. About the same time Mr. Dwight made his offer?

Mr. Leming. I should say on or around that time.

Senator Harrison. With reference to this company in the Bahamas, you sent some gentlemen down there to make an investigation, as I understand it.

Mr. Leming. Yes, sir; the Commissioner did.

Senator Harrison. How many employees did you find in the offices of this company?

Mr. Leming. As I remember, there was only a lawyer there. I assume he had a clerk. He had no employees.

Senator Harrison. No employees at all, and yet he had offices in this lawyer's office to whom reference has been made?

Mr. Leming. Yes.

Senator Harrison. That is where his office was domiciled?

Mr. Leming. Yes.

Senator Harrison. I understood the insurance office was in the same building with this law firm.

Mr. Leming. Yes; in his office.

Senator Harrison. And that there was no employee of this insurance company?

Mr. Leming. Except the lawyer.

Senator Harrison. And that the only policies which were issued were these eight policies that have been referred to. Did you in your investigation conclude anything with reference to the leadership of Mr. Dwight in getting these other gentlemen into this scheme, or didn't you know anything about that?

Mr. Leming. Yes, sir; to this extent: He denies that he did have any of the others participate; or rather, that any of the others participated at his recommendation. I believe that is the extent of our knowledge about that, except this, and I simply state this, then, as a fact, that Mr. Lowe is a client of Mr. Dwight, but Mr. Dwight says he did not advise Mr. Lowe to take out this policy.

Senator Harrison. Are any of the others who took these insurance policies employees of this law firm, or clients of Mr. Dwight.

Mr. Leming. Well; no, sir.
Senator Harrison. They are not?
Mr. Leming. No, sir.
Senator Harrison. That is all.
Senator Walsh. I don't quite understand whether the insurance company was in the lawyer's office or in a separate room of the same building as the lawyer's office.
Mr. Leming. There wasn't anything to have an office about, as I understand.
Senator Walsh. Will you answer that?
Mr. Leming. Yes, sir. There wasn't anything to have an office about, because—well, in the way of books, for instance, they had a cashbook of some sort and then another little journal, as I remember. There were about three books.
Senator Walsh. Was there a sign somewhere on the building indicating the existence of the insurance company?
Mr. Leming. Yes, sir; in front.
Senator Walsh. And did it designate the room?
Mr. Leming. Yes, sir; the lawyer's office.
Senator Walsh. Was the lawyer's office and the insurance office one and the same?
Mr. Leming. As I understand it.
Senator Capper. It is not yet quite clear in my mind how the individual was to conceive and develop this scheme for evading taxes.
Mr. Leming. Well, now, as I said yesterday, Mr. Baber and Mr. Baylis were the gentlemen who were selling it, as a result of which these policies were issued. Now, whether they got it from somebody else or it was original with them is a matter I don't know about, but they were the gentlemen—William Baylis and W. C. Baber. Incidentally, William Baylis was a classmate of Mr. Dwight at Princeton.
Senator Capper. Were they primarily interested in this as just a clever scheme for making money?
Mr. Leming. I have looked at their returns, and they seem to have reported the fees they got out of this. For instance, they report some fees there received from Mr. Dwight; and as far as I know, they did not themselves use the device, if that is what you asked.
Senator Capper. That is the point I wanted to get.
Senator Harrison. What were the fees they received?
Mr. Leming. You know there was a contingent-fee contract. There was some fairly substantial sum paid down, and then there was a contingent-fee contract providing the payment of so much a year thereafter. I think for the first year that contingent-fee contract was 25 percent. Then it decreases a little each year after that, a little lower each year for subsequent use of the device.
Senator Harrison. I did not get that; 25 percent of what?
Mr. Leming. Of the savings in tax.
Senator Harrison. Of the savings in tax?
Mr. Leming. Yes, sir. Now, that contingent-fee contract—Senator Harrison. Was that contract in writing?
Mr. Leming. Yes, sir.
Senator Harrison. You have that with you?
Mr. Leming. I thought it was already in the record. We have it. It is in the record. The contract provided, among other things, that
the fee was to be payable, I believe, these contingent-fee portions, when the returns of the taxpayer were finally closed. That is the language in the Dwight contract. In the Henry Lowe contract, as I recall, it concluded by saying, "When these amounts were finally determined to be allowable"—some such language as that; a little variation in the language, but the fee scale was the same.

Senator Harrison. Due to the fact that the case has not been closed then, they have not received their pay under the contract, have they?

Mr. Leming. The query was raised in my own mind about that the other day, and I was looking, for instance, at the 1933 and 1934 return of Baber & Baylis. I noticed they indicated the receipt of fees there. I have not had time, Senator, to run that down to see whether those were part of the fees which perhaps ought not to have been paid until the return was closed, or what.

Mr. Cooper. Mr. Chairman.

The Chairman. Mr. Cooper.

Mr. Cooper. Let me see if I get this correctly, please, Mr. Leming. The first man you mentioned when you began your statement was a man by the name of Baber. Now is this a clear conception of it—that this man Baber, who was a member of the firm of Baylis & Baber, set up this insurance company in the Bahamas?

Mr. Leming. Yes, sir.

Mr. Cooper. Then these eight policies were issued to six individuals by this Bahamas insurance company, that belonged to Baber?

Mr. Leming. Yes, sir. Baber owned 5 out of the 10 shares.

Mr. Cooper. The firm of Baber & Baylis, or Baylis & Baber, whichever it is, I believe it is said collected a fee from all of these policyholders for the issuance of these policies to them. Is that correct?

Mr. Leming. Yes. They were entitled to a fee. Now, I wonder whether right there, Congressman, if I could read the contract, for instance, in the Dwight case. Would that be helpful?

Mr. Cooper. That is all right; yes.

Mr. Leming. It is not so long.

Mr. Cooper. All right, read it.

Mr. Leming. It is dated New York, January 31, 1933, addressed to Baylis-Baber Co., 45 East Fifty-fifth Street, New York:

GENTLEMEN: In connection with my purchase of a single premium life-insurance policy from the Standard Life Insurance Co. of Nassau, Bahama Islands, and the making of a policy loan thereon, I hereby undertake to pay you the following fees for services rendered:

(a) Twenty-five percent of the estimated saving which I may effect in my Federal and New York State income taxes on my 1932 income through the deduction of interest on said policy loan from my gross income, such estimated saving being $57,340, payable as follows: $3,581 paid to William Baylis on December 31, 1932; balance ($10,745), as, if, and when my income tax returns for the year 1932 are finally closed in regard to this particular deduction, by the Federal and State authorities.

(b) Twenty-five percent of the estimated saving through payment of interest on said policy loan and the deduction thereof from my gross income when the second interest payment on said loan is made; 15 percent of the estimated saving when the third interest payment is made; 10 percent of the estimated saving when each or any subsequent interest payment is made.

In each case payment of the fee is to be made as follows: Twenty-five percent of fee when interest payment on said loan is paid to the said company, balance of fee as, if, and when each of any year's income-tax returns are finally closed in regard to the said interest deduction by the Federal and New York State authorities.
Mr. Cooper. Mr. Chairman, I would like to ask that that contract be inserted in the record.

The Chairman. Without objection, it will be made a part of the record.

(The contract referred to appears later in today's hearings on p. 143 in a memorandum submitted by Mr. Leming, p. 140.)

Mr. Leming. We have a photostat here somewhere. I thought it was already in.

Mr. Cooper. Allow me to ask you right there—then in practical effect this insurance company was set up in Nassau by this man Baber, who was a member of the firm of Baylis & Baber, and then they sold the benefits received from this insurance device to these individuals listed on this chart here?

Mr. Leming. Yes; I think that is right.

Mr. Cooper. And received a definite fee for the use of this device, which according to the contract was for the specific and sole purpose of evading the payment of Federal and New York State income taxes?

Mr. Leming. That is the way the contract reads.

The Chairman. Would you inform us how you came into possession of this correspondence and these records, disclosing all of these questionable methods?

Mr. Leming. Some of it was obtained originally from the taxpayer, I think, at the time of the first investigation. Others of it have been furnished by him from time to time as further inquiries were made of him, and other parts of it were obtained by the agent in the Bahamas and in their own investigations.

Senator Walsh. Mr. Chairman.

The Chairman. Senator Walsh.

Senator Walsh. I would like to ask you how this committee, or any other committee, can pass any law stopping any such loophole as that which you have described? If that is not a downright fraud, a conspiracy to defraud the Government, that contract and all the other facts, and subject to prosecution, when is there ever a case subject to prosecution? What law can we pass to stop men entering into a conspiracy to defraud the Government, except a criminal law?

Mr. Oliphant. I beg your pardon, Senator?

Senator Walsh. I am asking you or some lawyer connected with the Department. What law can we pass—what form of statute can we make, to make fraud other than what it is, a crime, anyway?

Mr. Oliphant (General Counsel, Treasury Department). I should like, if I might, to answer that question. I will take a little time. We are undertaking to present these matters ex parte, and that, of course, is the principal reason for our disinclination to present any except complete cases, and by the same token we would like, with your permission, to present you the facts in these cases, and so far as the Treasury is concerned, to refrain from characterizing them.

Senator Walsh. But there is plenty of law now on the statute books to punish fraud, is there not?

Mr. Oliphant. Yes.

Senator Walsh. Then the sole question is: Is this a fraud or is it not a fraud? If it is not a fraud, then we have got to have some legislation. If it is a fraud, then there is no need of legislation.
Mr. Oliphant. That is right.

Mr. Vinson. Mr. Chairman?

The Chairman. Mr. Vinson.

Mr. Vinson. In that connection, even though it is a fraud, and even though it might be a crime, is it not within the realm of probability that Congress could place an excise tax upon a transaction of this kind that would be in addition to the income taxes and would be in addition to the penalties of the criminal law?

Mr. Oliphant. That and similar civil sanctions could be added to the present criminal sections.

Mr. Vinson. There is one other question I wanted to ask in regard to this income that Mr. Baber derived from these transactions. Now, as I recall it, in regard to the 1932 transaction with Mr. Dwight, there was some $8,000 paid by him. I just wonder if any part of that $8,000 found its way into the income of Mr. Baber; and if so, how much?

Mr. Leming. We have a detail on that we can give you. Some of it was paid to him direct, and others were put on the little book they have as “advances” or “loans” to him. We could give you a complete statement of those disbursements.

Mr. Vinson. I would like you to break down that sum of $8,361.

Mr. Leming. We have it broken down, Congressman. We could give you the detail of it in a statement all right.

Mr. Vinson. Did Baber get substantially all of that amount?

Mr. Leming. Yes, sir; I think so.

Mr. Vinson. And he reported that as income?

Mr. Leming. I would have to check his return on that. He reported certain fees and things; but those matters that were still recorded on the books as “loans”, I understand he reported all of that he got from the company except those amounts which were recorded on the insurance company’s books as “loans” to him.

Mr. Vinson. In other words, he was paid by Mr. Dwight the cash fee and had an agreement for this contingent fee? He was paid the cash fee, and then he also was paid by the insurance company out of the cash that Mr. Dwight put up?

Mr. Leming. That is right.

Mr. Vinson. And was that course followed in connection with the other cash payments made by the policyholder?

Mr. Leming. Yes, sir.

Senator Harrison. Mr. Chairman—

The Chairman. Senator Harrison.

Senator Harrison. In the case of Mr. Ayres, Mr. Lowe, Mr. Marx, Mr. Schwab, and Mr. Thoms, are there similar letters of contract with this firm of financiers, similar to the letter that you have read from Mr. Dwight to Mr. Baber?

Mr. Leming. I am quite sure there are, Senator. I do not have those letters at hand, but I do know this: The investigation was sufficiently full and complete to satisfy us—and by that I mean from the investigations in this country and in the Bahamas, and by the interviews with the various and sundry people involved—that there was no difference in the procedure, and that was necessarily so because this thing, after all, was a paper proposition. They had to sit down at a table somewhere and pass checks and letters and things of that sort to make the record. They could not have done it without a lot of records, checks, and things of that sort.
I wonder if I might, just following along there, call your attention to one instance of an exchange of checks? I think it might be of interest. I would like for the committee to see these particular letters.

Senator Harrison. Won't you read them? What are they—charts?

Mr. Leming. It has been suggested to me the detail is a matter that will all be in these files you have called for, anyway, and it will take more time than you wish. If you wish me to go ahead I shall be glad to do so.

Senator Harrison. What do they purport to do?

Mr. Leming. Here is what I wanted to show you—that in the year 1934, for instance, in going through this machinery to establish the necessary deduction through the interest procedure, they did not in the case of Dwight that year pass the checks through the Royal Bank of Canada, as in other years, but the insurance company issued them an advance payment of a "dividend" so-called, one check of $97,480, and as an "increased loan value on the policy" in that year, $38,376. Those checks were delivered to Mr. Dwight's agent, and the agent in turn endorsed them, payable to the insurance company; they were handed back to the insurance company; the insurance company acknowledge receipt; so there those checks, totaling, I believe, something over $134,000, never even went through the bank. There was no money in the first place for them to be drawn against. They were written there in the insurance company's office, handed to Dwight's agent, Baber; he endorses them and hands them back to the insurance company; they go back in their file; and the interest deduction of $140,000 plus is established.

Senator Harrison. Was the same procedure followed with reference to these other gentlemen named in this list?

Mr. Leming. In short-cutting like that?

Senator Harrison. Yes.

Mr. Leming. This particular instance of the short-cut here in Dwight's case is the one I have noted particularly. Whether it occurred in some of the other cases I am not sure about, but I understand they did use the short-cut sometimes in the other cases also. That is, instead of passing the checks through the bank, where there would be that matching of checks, to establish a record, they would short-cut it this way.

Mr. Treadway. Mr. Chairman.

The Chairman. Mr. Treadway.

Mr. Treadway. I want to ask Mr. Oliphant a question. Then I would like to ask Dr. Magill one also, if I may.

Mr. Oliphant, early in these hearings reference was made to the fact that legislation would be prepared, or it was hoped we could get legislation. In answer to Senator Walsh's questions about legislation, I got the idea—and I would like to have you explain it—that you preferred not to present at this time the suggestions that the Treasury and others may have as to how to cure such evils as Senator Walsh was speaking about. Am I correct in that?

Mr. Oliphant. No; that was not the thought I intended to express.

Mr. Treadway. I could not quite hear you.

Mr. Oliphant. Congressman Vinson suggested, after the Senator had raised the question of the application of the criminal penalties to this situation, the possibility of an excise tax in addition.
Mr. Treadway. No; this was before Mr. Vinson got into the picture. It was when Senator Walsh was inquiring. Did not Senator Walsh ask you a direct question?

Mr. Oliphant. Yes.

Mr. Treadway. As to how this broad situation could be cured? What was your answer to that?

The Chairman. That question was directed to Mr. Leming, was it not?

Mr. Treadway. No, sir. At least Mr. Oliphant was answering Senator Walsh's interrogatory. I am not sure who was the witness.

Mr. Oliphant. Let me answer directly the question that I think is on your mind. There is no disinclination to state at this time what legislative measures we have in mind, except for this: As you know, the group in the Treasury has been working along for some time with the legislative experts on the Hill, and that work is in progress now, and at the appropriate time, when the committee is ready, the combined group will, I assume, have suggestions to make to the committee.

Mr. Treadway. You assumed that I knew one thing that I did not know. You said "as you know." I did not know that your experts were working with other experts. Have you not experts enough of your own?

Mr. Oliphant. I think that is one of the happiest situations in this town, the splendid personnel——

Mr. Treadway. Cooperation?

Mr. Oliphant. The splendid personnel which the Congress has on matters of tax legislation, and the hearty and continuous cooperation between the men working on those problems down here and the men working on the legislative problems in the Treasury. They are in constant contact, discussing their mutual problems.

Mr. Treadway. Then, as I understand you, your people in the Treasury—under you, I assume?

Mr. Oliphant. Yes, sir.

Mr. Treadway. And those under Mr. Parker and those with Mr. Beaman are all cooperating in an effort to answer the inquiry that Senator Walsh made of you. Am I correct?

Mr. Oliphant. That is right. That is correct.

Mr. Treadway. That is correct?

Mr. Oliphant. That work is going on at present and continuously.

Mr. Treadway. How far has that work progressed?

Mr. Oliphant. Mr. Kent is in immediate charge of the work, under me. Shall I ask Mr. Kent to answer that question?

Mr. Arthur H. Kent (assistant general counsel, Treasury Department). Considerable progress has been made, Mr. Treadway, more progress on some problems than others, because some problems lend themselves more readily and more obviously to legislative treatment.

Mr. Treadway. Let me ask you about this particular problem that Senator Walsh brought up. How much progress has been made in an effort to cure it by suggested legislation?

Mr. Kent. So far as the problem is bound up with the general problem of the use of foreign corporations for tax avoidance or evasion purposes, very substantial progress has been made.
Mr. Treadway. Can you give us any idea as to the date that a final report could be brought before this committee of the work of those three coordinate groups?

Mr. Kent. We will be in a position to submit suggestions almost anytime that the committee wishes to consider them.

Mr. Treadway. Would this not be a very opportune time, if your group is ready, to take up the question?

Mr. Vinson. Will the gentleman yield?

Mr. Treadway. Yes.

Mr. Vinson. It just seems to me that if, at this point, we go to considering different methods of meeting this situation it will be interminable. It seems to me that is a matter for executive session.

Mr. Treadway. I am perfectly willing to go into executive session on it.

Mr. Vinson. I know; but we have other problems that are going to be presented, and there is no use going at it piecemeal. My friend from Massachusetts might be willing to do it piecemeal.

Mr. Treadway. Oh, no.

Mr. Vinson. But so far as I am concerned, I want to take the picture as a whole, and then gather here, as is our custom, in executive session of the full committee, with all the experts, and do a real job; and I know my friend from Massachusetts wants a real job done.

Mr. Treadway. Absolutely; but is this not somewhat an independent proposition? As a matter of fact, did not Dr. Magill himself say they hoped before this session was over that plugs for some of these loopholes could be found?

Mr. Vinson. That is right, and the session is not over yet.

Mr. Treadway. But by your statement it is going to be interminable.

Mr. Vinson. No. My friend did not understand me.

Mr. Treadway. Probably not.

Mr. Vinson. If we start now discussing methods of dealing with this particular problem, we could have joint debates, political debates, and all that sort of thing.

Mr. Treadway. Certainly. We probably will have.

Mr. Vinson. When we get behind closed doors, in the calm serenity of the executive session, we always do more effective work.

Mr. Treadway. But, Mr. Vinson, that calm serenity is sometimes interrupted even in executive session. I yielded to Mr. Vinson, but I have not finished. I would like to get back to another subject, Mr. Chairman.

Dr. Magill, in connection with this single premium life insurance policy that you referred to, you spoke of it being perfectly right and legitimate that you and I should pay premiums on millions of dollars worth of insurance if we had the cash to pay with. Is not that correct?

Under Secretary Magill. I suspect you know more about it than I.

Mr. Treadway. No; I do not, I admit. I want to find out.

Under Secretary Magill. I have no million-dollar policies myself, but my understanding is, within the limitations of my knowledge of insurance policies, that we can take out a policy and agree to pay all our lives, or agree to pay 20 years, or pay once.

Mr. Treadway. Once.
Under Secretary Magill. But so far as the insurance company or ourselves are concerned it all comes out to the same thing.

Mr. Treadway. My question was this, Doctor, and that is all—assuming that you—I cannot see the picture myself, because I never could assume that at my age I could ever see a million dollars.

Under Secretary Magill. Neither do I.

Mr. Treadway. But assume that you, as an active and energetic man, eventually would be able to buy a single-premium million-dollar policy in a legitimate company. If that took place, and you borrowed some money on the policy and took a deduction on your tax return for interest paid, the Government would be out a certain amount of taxes with the legitimate company exactly as it is with this Bahama company, would it not? The Government would be losing its tax there, say $140,000, if the policy happened to be in the Massachusetts Mutual, for instance, or the New England Mutual, or the Boston Life Insurance or some of those companies—the one up in my section is the Berkshire—let us advertise all of them a little bit.

Under Secretary Magill. All right, put them in.

Mr. Treadway. If they divide up a million-dollar policy, and money was borrowed against that policy, the Government could not collect a tax, could it, on the interest paid? You get my idea on that?

Under Secretary Magill. I think so. As Mr. Leming told you yesterday, under this present section 23 [b] of the law, interest on indebtedness is deductible, so that if there were true indebtedness and were a true interest payment on the indebtedness, it is deductible.

Now, as to what the effect is on my tax, that of course depends on what I do with this money I get from the insurance company. If I really get some money and invest it in something, and so on, conceivably my income may be increased.

Mr. Treadway. You do not feel that if these large policies are purchased in bona-fide companies, with large assets, that the Government is still out the amount?

Under Secretary Magill. Oh, no; certainly not. The whole issue here, as I have tried to bring out—and I am always glad to do it—is between the hollow-shell transaction, which is not a transaction at all but is merely a tax-avoidance device in which the fees are to be split with the man who tells you how to do it; the difference is between that kind of case and the kind of case where you have a perfectly honest mortgage on your house, or an honest loan on your insurance policy, or any other kind of honest business transaction involving a deduction for interest. I cannot assure you too often that the Treasury has no attention of attacking honest taxpayers or honest transactions. Our difficulty is to analyze these cases as they come in. As you know, the returns do not present the full story. The return is just a summary of the transactions for the year; and, as Mr. Russell has tried to show you, an agent, if he is good, has to have a sort of sixth sense about these things if he is really going to get into the tough cases.

Mr. Treadway. Now, you are so courteous always I hesitate to impose on your kindness to answer questions.

Under Secretary Magill. You may ask me questions at any time.

Mr. Treadway. Thank you. Just this one further thought in connection with what Mr. Kent and Mr. Oliphant have said: What is
your idea as to whether or not the officials should present at this time recommendations to the joint committee on such a big problem as this insurance one, or wait until we see the whole group of tax-avoidance schemes that are referred to in the President's message?

Under Secretary MaGill. I had been thinking myself along the latter lines; that is, that we would present legislation after the evidence on all of these things had been laid before the committee. The fact is that as soon as we started in to investigate these cases, Mr. Kent's division of legislation started to work drafting suggestions for legislation on these various matters, and as I said in my initial statement on Thursday, the whole reason for presenting these matters at this time is to see if we can show you enough examples of these situations so that you will feel as we do that it is possible to pass legislation at this session of Congress to cure these evils before they get any worse.

Mr. Treadway. When you speak of "this session of Congress" are you referring to this present session which will expire some time before next January, or do you refer to the entire Seventy-fifth Congress?

Under Secretary MaGill. I am not sure of the technical terminology. By "this session" I mean the one that you are now engaged in.

The CHAIRMAN. I would like for the gentleman from Massachusetts to explain what session of Congress expires next January.

Mr. Treadway. There are supposed to be two sessions. There is no expiration date and the present session may run as Mr. Vinson said, "interminably," I guess.

Senator Harrison. Mr. Chairman.

The CHAIRMAN. Senator Harrison.

Senator Harrison. I would like to ask the witness a question. Do you know, or has it come out, how old these gentlemen are who took these insurance policies?

Under Secretary MaGill. I believe it is on one of the tables that were given to you, Senator.

Senator Harrison. Refresh our minds about that. How old a man was Dwight?

Under Secretary MaGill. May I at this time say this? It really belongs to Mr. Leming to say it. He has a summary statement here of these facts he has been through, which I think should be offered of record, since it contains a summary of a good deal of this information that has been given to you.

Mr. Cooper. Mr. Chairman, will the Senator yield?

Senator Harrison. Yes.

The CHAIRMAN. Mr. Cooper.

Mr. Cooper. The Senator will recall, I think, upon reflection that the letter written by Mr. Dwight, which was read at length, stated his age.

Senator Harrison. Yes.

Mr. Cooper. But he took the precaution to specify that he was not to have any physical examination.

Senator Harrison. Yes; that is what prompted me to ask these questions.

Mr. Cooper. And I assume from the further statement that was made that similar letters of application were written in the case of all these other policyholders. Is that right?

Mr. Leming. Yes.
Mr. Cooper. So I assume in each letter of application the man's age was stated. And he also specified as a condition precedent to the transaction that there was to be no physical examination.

Senator Harrison. Those facts I recall. That is why I was asking the question. Do all insurance companies generally have a limit on the applicant's age, or, as the age advances, does the premium become higher? I am asking for information.

Under Secretary Magill. I believe so, Senator. Of course, I have not yet reached a non-insurable age, but it is my understanding that you get to some point in your life when they will no longer write insurance on you.

Senator Harrison. I had the impression that when you took a life-insurance policy you were examined.

Under Secretary Magill. Always.

Senator Harrison. To see what your condition is.

Under Secretary Magill. I think that is always true.

Senator Harrison. And when you read the letter from Mr. Dwight, which said that he was not to be examined, and so on, that was a very peculiar thing. And that is in all the other letters, is it?

Under Secretary Magill. That is my understanding; yes, sir.

Senator Harrison. And this insurance company did not examine them medically to see what their condition was?

Under Secretary Magill. That is my understanding.

Senator Harrison. And they paid no attention to the age limit?

Under Secretary Magill. I believe that is true.

Mr. Chairman, has this statement been received in evidence, or are you willing to receive it now?

Senator Harrison. Just before you do that, it is pointed out to me that Mr. Ayres was 68 years of age.

Under Secretary Magill. Yes, sir.

Senator Harrison. Can a man of that age get an insurance policy in an ordinary life-insurance company?

Under Secretary Magill. I do not know. It seems very unusual.

Senator Harrison. Mr. Dwight was 58, and so on, down the line. That is in the record.

The Chairman. Without objection, the memorandum presented by Dr. Magill on behalf of Mr. Leming will be inserted in the record at this point.

Mr. Vinson. Do you mean the complete memorandum?

The Chairman. Yes; the complete memorandum.

(Memorandum Prepared for Presentation of the Joint Committee on Tax Evasion and Avoidance by Mason B. Leming, General Assistant to the Chief Counsel of the Bureau of Internal Revenue, June 22, 1937)

The next tax avoidance device we will discuss is that of foreign insurance companies which was referred to in the statement of the Under Secretary last Thursday.

The outline of the plan in question has already been given. We will repeat here for purposes of clarity. It consists solely of an apparent purchase of a so-called single-premium payment participating life-insurance policy in a substantial sum from a so-called insurance company, and a simultaneous borrowing from the same company of a sum the interest upon which is sufficient virtually to wipe out the taxpayer's gross income. By this creating the appearance of a loan from an insurance company the taxpayer attempts to secure the benefit of
a deduction under section 23 (b) of the Revenue Act of 1936 and corresponding sections of previous acts, permitting the deduction of interest paid on indebtedness.

These sections were obviously never intended to permit such a deduction. Their purpose, as everyone well knows, is to authorize the deduction by taxpayers of interest on mortgages and loans made in the regular course of business and for valid personal reasons.

Though alleged insurance company purports to issue an insurance policy and lend money on the strength of it, the insurance company employed by the salesmen of this tax avoiding device is not a real insurance company. In the cases now to be presented, it was organized under the laws of the Bahama Islands, American insurance companies having abandoned this practice. At the instance of one A. P. Pritchard, an attorney of Nassau, the legislature of the Bahama Islands passed an act at its 1932 session purporting to regulate the making of certain insurance contracts. The insurance company in question, organized under this statute, has no paid-up capital stock. It has none of the records kept by insurance companies. It has no appreciable bank account or other assets, yet it writes checks in the millions. It makes no attempt to maintain reserves in a manner customary in the insurance world, yet it purports to issue policies nominally running into the millions and pretends to make loans likewise in the millions against such fictitious policies. The so-called insurance policy issued by this unreal company is not a real insurance policy. It is not real because the company by which it is issued is a mere shell and because it has certain significant variations from the conventional type of similar insurance policies. For instance, the policy employed under the usual insurance deduction scheme provides that the policy shall not lapse at the end of any given policy year even thought the taxpayer takes no steps to comply with its provisions. By this means the taxpayer may keep the policy alive without further payment so that it may be used in any year in which it may be advantageous to use it.

It should also be noted that the policy carries a peculiar "lien" feature whereby there is a first charge in favor of the company against the principal sum in any settlement at death in excess of 25 percent. This lien is in exchange for the waiver of medical examination and deprives the contract of the basic features of a standard insurance policy. Again, "because a loan is to be made once on a policy and of the conditions of the policy", no physical examination is required. In addition, the taxpayer is immediately enabled under the policy to obtain a loan on the sole collateral of the policy of the so-called reserve value of the policy at the end of the first policy year. In a typical case, the policyholder pays a single premium of $2,793,720 and immediately "borrows" $2,832,510. The policy speaks of the determination of "dividends" by a company which has nothing which can earn dividends.

The simple conclusion is that there is no insurance, no loan, no indebtedness, no interest paid; there is nothing but a labyrinth of artificiality. Obviously, no person really wanting insurance would, in the first instance, go to the Bahama Islands to secure a policy. A person who did have some legitimate reason to go abroad would not insure in a company having no assets and maintaining no reserves. As I have said, neither the insurance company nor the insurance policy which are the underlying props of this scheme have any substantial reality. The sole purpose of the motions made is to secure through an elaborate artifice a deduction which will offset gross income and relieve from all income tax liability.

The Barlow's investigation disclosed the following information with respect to the Standard Life Insurance Co., Ltd., of Nassau. The company was formed December 8, 1931, by one Kenneth Solomon, a lawyer of Nassau, with an authorized capital stock of $50,000, represented by 5,000 shares having a par value of $10 each. It is understood that he acted for one W. C. Baker, of New York City, in the formation of the company. The incorporators were Kenneth Solomon, Stafford Sands, Carl Elmer Robertson, Doris Louis Barlow, Alice Maud Anderson Farrington, all of Nassau. The company remained dormant until December 27, 1932, when the first meeting of stockholders was held and the following officers were elected: President, Artemas Paul Pritchard; vice president, William C. Knowles; secretary and treasurer, Reginald Pritchard. At this meeting the shares of the incorporators were transferred to the following individuals, who are the present stockholders, according to the last statement filed by the company: Artemas Paul Pritchard, Reginald William

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Pritchard, William C. Knowles, C. Trevor Kelly, Frederick Plunder, all of Nassau, 1 share each, and Walter C. Baber, New York City, 5 shares. The foregoing 10 shares of stock are all that have been issued by the company.

A. P. Pritchard and Reginald Pritchard, president and secretary-treasurer, respectively, are attorneys of Nassau. During the period from December 1932 to December 1938 the company wrote a total of only eight life-insurance policies and for only six individuals, all American citizens, in amounts as follows:

<table>
<thead>
<tr>
<th>Policy no.</th>
<th>To</th>
<th>Age</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>A48</td>
<td>Winfield Ayres</td>
<td>68</td>
<td>$400,000</td>
</tr>
<tr>
<td>A47</td>
<td>Richard E. Dwight</td>
<td>68</td>
<td>4,000,000</td>
</tr>
<tr>
<td>A49</td>
<td>Henry W. Lowe</td>
<td>68</td>
<td>2,500,000</td>
</tr>
<tr>
<td>A50</td>
<td>Lawrence Marx</td>
<td>68</td>
<td>2,500,000</td>
</tr>
<tr>
<td>A51</td>
<td>Jacob W. Schwab</td>
<td>48</td>
<td>1,200,000</td>
</tr>
<tr>
<td>A52</td>
<td>George Homs</td>
<td>58</td>
<td>$75,000</td>
</tr>
<tr>
<td>A53</td>
<td>Lawrence Marx</td>
<td>50</td>
<td>2,500,000</td>
</tr>
<tr>
<td>A54</td>
<td>Jacob W. Schwab</td>
<td>45</td>
<td>1,000,000</td>
</tr>
</tbody>
</table>

Total insurance in force: $15,275,000

The books of the company consist of an elementary type of cash book operated on the single entry system, a check book, a minute book, and some correspondence files, all which are kept in the law offices of the Pritchards in Nassau.

The cash accounts of the company for 1931 show no deposits or withdrawals. According to the books, no part of the capital stock was paid in. Aside from the deposits and withdrawals representing the payment of the premiums and policy and dividend terms, all of which were, as will be shown later, mere paper transactions or exchanges of checks, the only actual cash that the company received in 1932 consisted of $7,200 out of the $8,300 actual cash paid by Richard E. Dwight. The company had two cash disbursements, $300 to W. C. Baber and $180 to R. W. and A. P. Pritchard, leaving the company a bank balance on December 31, 1932, of $7,300.

The cash balances of the company on December 31 for the years 1933 to 1935, inclusive, were as follows:

<table>
<thead>
<tr>
<th>Year</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>1933</td>
<td>$3,170.10</td>
</tr>
<tr>
<td>1934</td>
<td>7,653.27</td>
</tr>
<tr>
<td>1935</td>
<td>8,093.70</td>
</tr>
</tbody>
</table>

The insurance company not being an actual operating company, had only minor expenses during these years. Practically all of its actual receipts were withdrawn by W. C. Baber as compensation for personal services rendered and to be rendered in the future, traveling expenses and as personal terms which were still unpaid at the time of the Bureau's examination of the company's books in March 1937.

Such, it turned out, was the so-called Standard Life Insurance Co., Ltd., of Nassau, which those taxpayers had named in their returns as an insurance company in which they held policies on which they had obtained loans.

The Bureau's investigation further disclosed that Walter C. Baber acted in a dual capacity in connection with each policy issued by the Standard Life Insurance Co., Ltd., that is, as attorney-in-fact for the insured and as the broker or agent of the company, of which he also was the sole real stockholder.

It will be sufficient to give the details as to one of the six taxpayers using this company as a device for tax avoidance purposes, viz. Richard E. Dwight, a practicing attorney of New York City. In the description of the device as employed by Mr. Dwight, it is necessary to refer to the transactions in technical terms. However, it must be remembered that such expressions as insurance company, policy, dividends, loan, borrow, interest, etc., are used in the fictitious sense of the entire plan.

For the years 1932, 1933, and 1934 Mr. Dwight filed income-tax returns showing no tax due. For the year 1935 his return showed tax due in the amount of $220.83. For these 4 years the Bureau of Internal Revenue has determined that Mr. Dwight owes additional taxes in the total amount of $230,820.74, exclusive of penalties and interest. Mr. Dwight's returns for these
years disclosed no taxable net income, except for a nominal amount reported in 1935, mainly because he claimed in each year an interest deduction alleged in the return to have been paid by him to the Standard Life Insurance Co., Ltd., of Nassau, Bahama Islands. Mr. Dwight’s correct taxable income for each year and the interest deductions used by him to reduce his income to a nontaxable basis are shown in the following tabulation:

<table>
<thead>
<tr>
<th>Year</th>
<th>Correct income</th>
<th>Income reported</th>
<th>So-called interest deductions disallowed</th>
<th>Tax reported on returns</th>
<th>Under statement of tax on returns</th>
</tr>
</thead>
<tbody>
<tr>
<td>1932</td>
<td>$143,629.27</td>
<td>$171,08</td>
<td>$141,629</td>
<td>None</td>
<td>$13,449.48</td>
</tr>
<tr>
<td>1933</td>
<td>119,230.28</td>
<td>3,432.76</td>
<td>113,597</td>
<td>None</td>
<td>50,471.25</td>
</tr>
<tr>
<td>1934</td>
<td>147,308.15</td>
<td>2,620.37</td>
<td>145,486</td>
<td>None</td>
<td>57,555.37</td>
</tr>
<tr>
<td>1935</td>
<td>158,384.88</td>
<td>10,933.88</td>
<td>147,304</td>
<td>200.60</td>
<td>62,924.64</td>
</tr>
<tr>
<td>Total</td>
<td>590,185.58</td>
<td>17,518.60</td>
<td>578,072</td>
<td>200.60</td>
<td>230,390.74</td>
</tr>
</tbody>
</table>

1 There were some other minor deductions disallowed.

Attached to Mr. Dwight’s returns for the years 1932, 1933, 1934, and 1935 was a general statement in explanation of the “interest” deduction claimed.

The Bureau’s investigation has disclosed the following information with respect to these interest deductions claimed by Mr. Dwight.

In the fall of 1932 the insurance device under consideration was presented to Mr. Dwight by one William Baylis. Associated with Mr. Baylis in the promotion of this scheme was Walter C. Baber, already mentioned. Mr. Baylis and Mr. Baber were partners under the firm name of Baylis-Baber Co., at 45 East Fifty-fifth Street, New York City. Their business has been stated to be that of “tax consultants and specialists.” Mr. Dwight decided to employ the scheme in connection with his own income-tax returns and appointed Mr. Baber as his attorney in fact to carry the plan through.

The plan in Mr. Dwight’s case was carried out in the following manner:

Mr. Baber went to Nassau where on December 30, 1932, all of the following steps were taken. Mr. Baber presented to the Standard Life Insurance Co., Ltd., Mr. Dwight’s application for what purported to be a $4,000,000 single premium life-insurance policy, the premium on which was $2,793,720. On the same day there was deposited with the Royal Bank of Canada at Nassau personal funds of Mr. Dwight in the amount of $8,361, and the bank extended to Mr. Dwight a credit of $2,927,388, which altogether gave him a total credit at the bank of $2,935,749.

Against this credit Mr. Baber, as attorney in fact for Mr. Dwight, drew a check payable to the insurance company in the sum of $2,793,720, the amount of the premium, and immediately pretended to borrow back from the insurance company $2,927,388, the total loan value of the policy, and an additional $94,818, which was supposed to represent the discounted value of the first annual dividend on the policy, pledging the policy as security for these loans. These two so-called loans, aggregating $2,927,388, were used to discharge Mr. Dwight’s loan at the Royal Bank of Canada and to pay to the insurance company the first year’s interest on the alleged policy loan. The interest on the policy loan thus paid amounted to $141,628, which amount Mr. Dwight deducted as “interest paid” on his 1932 return.

It should be noted that the only amount actually expended by Mr. Dwight in connection with the foregoing transaction was the sum of $8,361 deposited with the Royal Bank of Canada. Under date of January 31, 1933, Mr. Dwight addressed the following letter to Baylis-Baber Co.:

BAYLIS-BABER CO.,
New York.

GENTLEMEN: In connection with my purchase of a single premium life-insurance policy from the Standard Life Insurance Co., of Nassau, Bahama Islands, and the making of a policy loan thereon, I hereby undertake to pay you the following fees for services rendered:

(a) Twenty-five percent of the estimated saving which I may effect in my Federal and New York State income taxes on my 1932 income through the deduction of interest on said policy loan from my gross income, such estimated
saving being $57,340, payable as follows: $3,581 paid to William Baylis on December 31, 1932; balance ($10,745) as, if, and when my income-tax returns for the year 1932 are finally closed, in regard to this particular deduction, by the Federal and State authorities.

(6) Twenty-five percent of the estimated saving through payment of interest on said policy loan and the deduction thereof from my gross income when the second interest payment on said loan is made; 15 percent of the estimated saving when the third interest payment is made; 10 percent of the estimated saving when each or any subsequent interest payment is made.

In each case payment of the fee is to be made as follows: 25 percent of the fee when interest payment on said loan is paid to the said company, balance of fee as, if, and when each or any year's income-tax returns are finally closed, in regard to the said interest deduction, by the Federal and New York State authorities.

RICHARD E. DWIGHT.

For the year 1934, Mr. Dwight, still acting through his attorney, Mr. Baber, simplified the procedure in arriving at the amount of interest that he could deduct. As in the previous year, the insurance company again notified Mr. Dwight that the annual dividend, payable in December 1934, would pay off the discounted dividend loan made to him in December 1933. On December 21, 1934, Mr. Dwight deposited in his account at the Royal Bank of Canada in Nassau actual cash in the amount of $9,630, and on December 20, 1934, he withdrew this money and paid it to the insurance company.

On the same day, December 20, the insurance company issued to Mr. Dwight two checks, one in the amount of $97,480, which was supposed to represent a "loan" of the discounted annual dividend, and the other in the amount of $38,370, which was supposed to represent the increase in his policy loan necessary to bring it up to the full loan value of $2,900,720. These two checks were not deposited by Mr. Dwight in the bank, but were simply endorsed back to the insurance company. The insurance company likewise did not put these checks through its bank accounts. These two checks, totalling $135,850, plus the $9,260 cash paid to the company, made up the sum of $145,486, which was the amount of so-called interest on the increased policy loan. This sum of $145,486 was deducted by Mr. Dwight as "interest paid" in his 1934 return, notwithstanding the fact that the only amount of cash actually paid out by Mr. Dwight in this year was the sum of $9,630. The short cuts taken in this year to simplify the transaction even more clearly disclose its fictitious nature. The sham bank loan was not employed to dress up the alleged interest payment. The two undeposited insurance-company checks which were returned to the company, plus the relatively small amount of actual cash disbursed by Mr. Dwight, completed the deal.

As in previous years, the insurance company, in December 1935, notified Mr. Dwight that the annual dividend on his policy, payable in December of that year, would pay off the discounted dividend loan made to him in 1934. On December 21, 1935, Mr. Dwight deposited in his account at the Royal Bank of Canada, Nassau, $10,503. On December 30, 1935, the insurance company issued to Mr. Dwight two checks, one in the amount of $86,784, supposed to represent a discounted dividend loan, and the other in the amount of $38,104, supposed to represent the amount of additional policy loan necessary to bring that loan up to the maximum loan value of $2,947,824. These two checks were deposited in Mr. Dwight's account at the Royal Bank of Canada, bringing the total in that account to $147,391, and on the same day, December 30, 1935, a check for this total amount was delivered to the insurance company as payment of alleged 1 year's interest on the policy loan. The full amount of $147,391 was deducted by Mr. Dwight as interest paid in his 1935 return, notwithstanding the fact that the only cash actually disbursed by him in that connection was the sum of $10,503.

This insurance scheme adopted by Mr. Dwight and a number of other taxpayers is another instance of how a foreign corporation is employed by American taxpayers to avoid the payment of taxes. The difficulty of investigating the facts is always intensified where foreign corporations are employed as instrumentalties of tax avoidance. It was necessary to send a revenue agent to the Bahamas to get at the essential facts of this scheme. The process of the audit of the 1936 returns being in its early stages, the Bureau is not sure how many additional taxpayers have been "sold" by the schemes of efficient peddlers. Investigation is being conducted to determine how widely the scheme has spread. It strikes at the heart of the income tax and suppression is absolutely vital to the interests of the revenue.
The CHAIRMAN. Mr. Leming, have you any further statement that you would like to make?

Mr. Leming. If the Chairman please, I think perhaps it was Senator Harrison inquired of me yesterday about Mr. Dwight's 1931 return, and possibly Senator Walsh about the 1930 return. I just want to say I have them here if you want to see them or know about them at this time.

The CHAIRMAN. Senator La Follette was asking about it, I think, and he is not present. We will perhaps take that up in executive session and determine it later. Have you anything further?

Mr. Leming. I have nothing further.

The CHAIRMAN. Dr. Magill, who is your next witness?

Under Secretary Magill. Commissioner Helvering.

STATEMENT OF HON. GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

The CHAIRMAN. Do you prefer to make your main statement without interruption, Mr. Helvering, and respond to questions later?

Commissioner Helvering. I would like to do that.

The CHAIRMAN. Without objection, you may proceed with that understanding.

Senator Harrison. Mr. Chairman.

The CHAIRMAN. Senator Harrison.

Senator Harrison. I know that this statement of Mr. Helvering is quite lengthy.

Commissioner Helvering. Yes.

Senator Harrison. And we have about 30 minutes more to run. He has given this statement to the press. I do not think he will be able to finish it this morning.

The CHAIRMAN. Can you read it in 30 minutes, do you think, if you are not interrupted?

Commissioner Helvering. No; I cannot do that.

Senator Harrison. Mr. Chairman, I submit that if he does not finish it, the prepared statement be made a part of the record this morning, so that it may be released.

Commissioner Helvering. Yes.

The CHAIRMAN. The portion that he does not read?

Senator Harrison. The portion that he does not read.

The CHAIRMAN. Yes; without objection—

Mr. Treadway. Mr. Chairman, may I ask one question first? What time is it proposed that we recess this morning? Will it be necessary for the House Members to be on the floor promptly at 12 this noon?

[Discussion off the record.]

The CHAIRMAN. Mr. Commissioner, you may proceed.

Commissioner Helvering. I might state to you this mimeographed copy does not have the list of names that I may use in the course of this talk or testimony before the committee.

The CHAIRMAN. You have copies for each member of the committee?

Commissioner Helvering. Yes.
Mr. Cooper. A little louder. What was it you said about a list of names?

Commissioner Helvering. As I understand, in the preparation of the mimeographed copies certain names which I may give have not been inserted, but I understand there is a place left there for those names, if anybody wants to write them in.

Senator Harrison. Mr. Helvering, would you prefer to proceed this morning, or would you prefer to proceed in the regular way here, so that your entire statement may be made at one time?

Commissioner Helvering. This is a statement that ought to be given consecutively, but I do not mind. There is a convenient point that I could stop in here. It will take about 30 minutes to read to that point.

The Chairman. Suppose we go ahead then.

Commissioner Helvering. I am directing my remarks to the personal holding company.

The corporate device is probably the most widespread and fruitful method for avoiding the full impact of taxes. The use of the corporate entity as a tax-avoiding mechanism is complex and varied in the extremes. Frequently it is coupled with other mechanisms, such as trusts, which we shall present to the committee. Any one corporation, furthermore, may be used in a multitude of ways to accomplish one basic objective—reduction of taxes.

Mr. Magill described to you in general terms the way in which corporations are used for these purposes. I propose to limit my discussion to a detailed consideration of the use of the personal holding company to avoid taxes. I am speaking here of corporations which are subject to the surtax under section 351 of the Internal Revenue Act. As you know, this section defines a personal holding company as one which receives at least 80 percent of the gross income from royalties, dividends, interest, annuities, and capital gains, and 50 percent of its stock is owned by not more than five individuals; the term “individual” also being described and defined in the statute to include members of the same family. Frequently corporations which are not within the strict statutory definition of personal holding companies but controlled by one individual, a family, of a small group of persons are also employed to accomplish tax avoidance.

For example, a closely held industrial corporation may accumulate a substantial surplus and invest it in stocks and bonds, but its income from such assets might be less than the amount required to make it a personal holding company. Many modern large industrial corporations have huge surpluses which represent nothing more than accumulated undistributed corporate profits of the stockholders. Yet it is often difficult to sustain an argument in court that this accumulated surplus is not required for some present or future activity of the corporation. This problem may require the attention of Congress at a later date. I shall confine myself today to the personal-holding-company device, namely, the personal holding company described in the present section 351 of the income-tax law.

Before going into the details of this matter, it is probably advisable to summarize the general situation. In brief, tax avoidance by use of the personal holding company arises because many wealthy taxpayers of the Nation have split themselves into multiple personali-
ties with the single purpose of avoiding the payment of taxes which would be due if they followed the natural, untax-conscious course of remaining one personality. The typical personal holding company in practice is a device whereby assets of an individual, or a family, or a closely associated group, are transferred to or acquired by a corporation. The assets may be stocks and bonds, a country estate, an incorporated farm, a yacht, patents, and copyrights. No conceivable type of income-producing or taxable assets has been neglected.

This corporation then derives the income from those assets, which may take the form of royalties, dividends, interest, annuities, and capital gains on sales of stock or securities. A personal holding company may also buy assets and sell them. Sometimes it will buy from and sell to its owner. Sometimes it will buy from and sell to another personal holding company of the same owner. We shall hereafter discuss cases of this sort and show their consequences.

In many instances, a person or group may hold assets in several holding companies. Sometimes we find an astonishing number of separate corporations under substantially one beneficial ownership. For instance, in some cases an individual or a family may have as many as 15 holding companies. We shall later describe cases of this sort and comment upon the reason for the use of the multiple holding company and its effect.

A person who did not appreciate the results obtained in reduction of taxes by the use of the personal holding company might very well be bewildered by their use. The corporate device is historically a means for collecting capital for productive business operations and insulating individual investors from personal liability because of those operations. But this is hardly ever the purpose of the modern personal holding company. Frequently it does not conduct any business, as that term is generally understood, and it ordinarily has no liabilities except to its owners, and these liabilities are often arbitrarily created for tax purposes, as we shall later describe. Certainly these owners need no insulation against liability to themselves.

In brief, what happens is that these individuals have divided themselves into multiple personalities, and they have done it with the single, unadulterated purpose of avoiding payment of taxes. As Mr. Magill pointed out, this is not a new problem. Ever since the first income-tax law in 1913, Congress has struggled with the problem of the personal holding company. Congress has continually tried to enact an income-tax law which seemed to it fair and equitable to the taxpayers. The incidence of the tax has been related to ability to pay by these enactments of Congress and measured by the income of the taxpayer. But the efforts of Congress have been continually and progressively frustrated by division of the income of many taxpayers between corporations and artificial personalities created and used for that particular purpose.

Prior to 1934 and as far back as 1913, the income-tax law contained a provision now in section 102, formerly known by the famous number 220 in the Bureau of Internal Revenue, imposing a surtax upon the net income of every corporation formed or used to prevent the imposition of the surtax upon its shareholders through accumulating income or profits without distributing them. This provision was difficult to enforce because of the virtual impossibility of deter-
mining, first, what constitutes an unreasonable accumulation, and second, whether there is a purpose to avoid the imposition of surtax upon the individual stockholder.

For example, sometime ago a corporation was formed for Cecil de Mille, which he completely dominated, consisting of himself, members of his family, and his attorney. This was an incorporation of what may be called the "earning personality" of Mr. de Mille. In other words, de Mille's earning power was almost the sole corporate asset. De Mille, the individual, then went to work for de Mille, the corporation, at a salary far less than he knew he could command as a director. I refer there to the director of a moving picture. The corporation then sold de Mille's services to producing companies. The difference between Cecil de Mille's salary from his own corporation and his actual earnings as a motion-picture director was put into the corporation.

The Government claimed that the accumulation of this surplus was unreasonable and a purposeful attempt to evade surtaxes. De Mille answered that his corporation was saving up money to go into the production of pictures at a later date, which was a proper accumulation of surplus. The court sustained de Mille.

I will say that this case was litigated through the Board of Tax Appeals and the courts, and the court findings sustained de Mille in his contentions, and the citation is given there of the cases (Commissioner v. Cecil R. de Mille Productions, Inc., C. C. A. 9th, Apr. 16, 1937, affirming 31 B. T. A. 1161).

Contrast this case with an individual who does not have his earnings paid to a corporation. Such an individual cannot avoid taxes on the money he is attempting to save to go into business in the future.

The vice of this transaction is that the individual is using a corporation artificially in a way which no one would have thought of had it not been for the income-tax laws. The difficulty is that many courts apparently find it difficult to draw the line between the artificial and the genuine use of a corporation.

To obviate these difficulties, Congress passed section 351 of the Revenue Act of 1934 which imposed a surtax on the income of personal holding companies, over and above the ordinary corporate tax. The specific purpose, as shown by the committee reports, was to do away with the necessity of proving an unusual and unreasonable accumulation and a purpose to avoid the imposition of the surtax. The section was amended in 1936, apparently to adjust the surtax rates to the undistributed profits surtax which was included in that act.

The Bureau's study of returns by personal holding companies indicates progressive utilization of the "personal holding company" device. As taxpayers and their lawyers and other advisers became more familiar with section 351, they became increasingly aware of the possibility of its affirmative use for the purpose of tax avoidance, and therefore the bolder to make use of the provision to accomplish avoidance. The amount of revenue lost to the Government in this way in 1934, 1935, and 1936 is undoubtedly huge, as we shall later indicate; and without question it will increase unless remedial legislation is passed by Congress.
We are calling this situation to the committee’s attention because we believe there is an enormous loss of revenue to the Government as section 351 now stands and because a statutory provision originally designed to prevent tax avoidance has been perverted by certain individuals to the end of accomplishing that very thing—tax avoidance. As a result, many individuals who should bear a substantial share of the tax burden, have entirely escaped taxation on all or a substantial part of their income.

This is true, generally speaking, of those wealthy taxpayers who were eager to escape the tax. Taxpayers who were not advised by resourceful counsel, or who were not eager to arrange their affairs to avoid payment of taxes, or whose incomes were so modest that the use of the personal holding company was too costly, have borne an undue share of the expense of Government. Those who had incomes large enough to make it worth while, who were careful to secure the advice of astute lawyers, and who were not unwilling to avoid payment of the full taxes on some or all of their income, have used the personal holding company with results which I shall show.

As I have said, the purpose of the tax provisions concerning personal holding companies was to make their use unprofitable and thereby prevent diversion of income from individual taxpayers to a separate entity. But, strange as it may seem, the actual rate of surtax upon the holding companies turns out to be so as to discourage their use only by individuals whose net income was in the lower brackets. In other words, the actual rate of surtax succeeded in hindering only individuals with comparative modest incomes. The very wealthy were helped by it and not hindered.

I say the actual rate because our experience proves that the statutory rates are delusive, and in fact merely nominal. The rates stated in the statute run from 8 percent to 48 percent. Actually the preliminary report on 1935 returns shows the collection of surtax of less than $2,000,000 on personal holding company incomes of approximately $115,000,000. This, as you see, is a rate of less than 2 percent, and results from the over-generous deduction provisions now provided in the statute.

Our experience shows that individuals in the lower brackets find it cheaper to pay the individual tax than to pay the personal holding company tax, in addition to the other corporate taxes, on all or part of their income. But when incomes are in the higher brackets, the act works the other way around.

It is frequently cheaper, under both the 1934 and the 1936 acts, for an individual in the higher brackets to pay the taxes levied on a personal holding company, in addition to corporate taxes. These will be lower than the taxes which would be levied if he received directly all income diverted to a personal holding company. In other words, in the higher brackets, the surtax upon the individual is greatly in excess of the total corporate tax, including the tax on the personal holding company. This is true even though there is no particular manipulation of the affairs of the individual and the holding company, such as I shall hereafter describe. It follows directly from the mere fact of the division of income between an individual and a personal holding company, coupled with the existing rate structure of the act.
These are minimum results. In most of the personal holding company cases, however, the individual has not been content passively to accept the benefits of the operation of an act which is all in his favor. He has arranged his transactions and those of his holding company so as to escape even further the obligation of paying taxes.

One way of accomplishing this object consists in the highly ingenious use of certain provisions of section 351 permitting deductions in arriving at taxable income of the personal holding company—that is, his undistributed adjusted net income. I shall summarize the most important of these deductions as follows:

First, personal holding companies may deduct 20 percent of their adjusted net income less dividends received from other personal holding companies.

Second, personal holding companies may deduct any reasonable amounts used or set aside to retire indebtedness incurred prior to January 1, 1934.

Third, personal holding companies, to arrive at adjusted net income, may deduct losses from the sale or exchange of capital assets, without limitation. If such losses are incurred by an individual, they can be allowed only to the extent of $2,000, plus gains from such sales or exchanges. In other words, an individual is less favored than a personal holding company.

I can show the effect of these and other provisions of the section by referring to preliminary analyses made by the Bureau of a group of returns of the personal holding companies. We have analyzed 4,457 returns under the 1934 act, filed for the calendar year 1934 and for the fiscal year ended in the period January through June 1935.

All of these companies showed net income in the aggregate amount of over $53,000,000. But only 374 of them, or less than 9 percent, showed income taxable under the surtax provisions of section 351, relating to personal holding companies. These showed taxable income of only $5,000,000, or less than 10 percent of the total net income of the group. They paid a personal holding-company surtax of only $1,695,000, or about 3 percent of their aggregate net income. The remaining 4,083 companies in the group paid not a cent under 351. They were subject only to the ordinary tax on corporate income, which, as you know, is much less than the tax on individuals in the higher brackets. To refresh your recollection, the highest bracket of the normal tax on corporations under the 1934 law was 13¾ percent, whereas the individual surtax bracket (not including normal tax of 4 percent) reached 59 percent. The individuals who owned these corporations were, therefore, taxed on the income from assets held by these companies as if they were bona-fide operating corporations instead of merely ephemeral subdivisions of the personalities of the individual owner and creator.

We shall hereafter show in detail just what individuals in certain typical cases have saved by use of the personal holding-corporate device. I can most readily present this situation to you in a summary way by description of the results shown on a group of the 17 personal holding company cases which happened to be pending in the conference division of the Bureau of Internal Revenue at the time of this investigation.

I took those, gentlemen, with the idea that those 17 cases, being right there under consideration at that time, would show no selection.
Senator Harrison. Before you get into these 17 cases, we have to adjourn in about 3 minutes to go over to the Senate. Why wouldn't that be a very good place to stop? We are now getting into specific cases.

Commissioner Helvering. It is perfectly agreeable to me, gentlemen of the committee. We can stop very logically here and then take up these cases later.

Senator Harrison. Is not this the most logical place to stop?

Commissioner Helvering. I had anticipated going to about page 15 of my memorandum, but that would take possibly 15 minutes. Just as you gentlemen say.

Senator Walsh. Mr. Chairman, I move we suspend at this point and adjourn until tomorrow morning.

(The motion to adjourn was carried.)

(Whereupon, at 11:55 a. m., an adjournment was taken until 10 a. m. Thursday, June 24, 1937.)
The joint committee met in the hearing room of the Committee on Ways and Means in the New House Office Building, at 10 a. m., Hon. Robert L. Doughton, chairman, presiding.

The CHAIRMAN. The committee will be in order.

Mr. VINSON. Mr. Chairman.

The CHAIRMAN. Mr. Vinson.

Mr. VINSON. I would like to have Dr. Magill at this point elaborate upon the history of section 351, that came into the revenue laws of the country for the first time in 1934, which deals with the incorporated pocketbook, or taxes upon personal holding companies.

The CHAIRMAN. Dr. Magill, you have heard the request of Representative Vinson. Is that agreeable to you?

Under Secretary MAGILL. Yes, sir. I think the history is about this: Of course, I am trying to refresh my recollection from 3 years ago when the provision came in, and all of you gentlemen I think on the committee are quite as familiar with it as I, because the fact is that you devised the provision.

As the Commissioner said yesterday, we originally had this provision, section 102.

Mr. VINSON. When did that come into the law?

Under Secretary MAGILL. There was a provision of that general character back in the first income-tax law in 1913.

Mr. VINSON. And what was the penalty? What was the tax?

Under Secretary MAGILL. I do not know that I can follow the rates all the way through.

Mr. VINSON. Say in 1934.

Under Secretary MAGILL. But they had been 50 percent through a period of years.

Mr. VINSON. And how much of all the money had been collected under that section 102?

Under Secretary MAGILL. Inconsiderable amounts, and as the Commissioner brought out yesterday—perhaps I had better make that a little clearer—the provision in 1913, which was continued from then on, first as section 220 and then later, section 104 and 102, was to the effect that if a corporation was formed or availed of for the purpose of preventing the imposition of the surtax upon its shareholders, and so forth, by improperly accumulating a surplus, that then this special tax should be imposed. As the Commissioner explained, the difficulty the Department ran into seems to have been that it was very hard to prove that the corporation was formed or
availed of for this purpose of improperly accumulating the surplus, so that the fact was that the provision was practically ineffective in practice.

Mr. Vinson. That was the situation which existed at the time of the report filed by the Hill subcommittee of the Ways and Means Committee on December 4, 1933?

Under Secretary Magill. That is correct.

Mr. Vinson. And I would like to insert in the record at this point, Mr. Chairman, that portion of the Hill subcommittee’s report beginning at paragraph 4, “Personal holding companies”, on page 6, and running through down to paragraph no. 5, “Exchanges and reorganizations”, on page 8.

The Chairman. Without objection, that will be done.

The matter referred to is as follows:

[From preliminary report of a subcommittee of the Committee on Ways and Means, entitled “Prevention of Tax Avoidance”, 73d Cong., 2d sess.]

(4) PERSONAL HOLDING COMPANIES

Perhaps the most prevalent form of tax avoidance practiced by individuals with large incomes is the scheme of the “incorporated pocketbook.” That is, an individual forms a corporation and exchanges for its stock his personal holdings in stock, bonds, or other income-producing property. By this means the income from the property pays corporation tax, but no surtax is paid by the individual if the income is not distributed.

For instance, suppose a man has $1,000,000 annual income from taxable bonds. His tax under existing law will be $571,000. However, if he forms a holding company to take title to the bonds and to receive the income therefrom, the only tax paid will be a corporate tax of $137,500 as long as there is no distribution of dividends. Thus, a saving of $433,600 has been effected.

It is true that section 104 of our income-tax law puts a 50-percent penalty on this accumulation of profits to avoid surtaxes, but, nevertheless, there seems no doubt that this form of tax avoidance is still practiced to a large extent. By making partial distribution of profits and by showing some need for the accumulation of the remaining profits, the taxpayer is able to defeat the Government in proving a purpose to avoid surtaxes.

Your subcommittee, therefore, recommends that the present section 104 be divided into two parts, one dealing with the personal holding company and the other with all other corporations which accumulate unreasonable surpluses. The part dealing with personal holding companies has been entirely rewritten, while the present law has been retained with a few modifications to provide for the other companies.

In regard to the personal holding companies, your subcommittee recommends that they be defined as any corporation 80 percent of whose gross income for the taxable year is derived from rents, royalties, dividends, interest, annuities, and gains from the sale of securities, and whose voting stock to the extent of more than 50 percent is owned by not more than five individuals at the close of the taxable year. In computing the number of individuals who own the majority of the voting stock of a corporation it is proposed to count as one all members of a family in the direct line as well as the spouse and brothers and sisters.

It is recommended that a tax of 35 percent be levied on the “undistributed adjusted net income” of such corporations.

This undistributed adjusted net income is determined by adding to the net income of a corporation the amount of dividends received from other corporations and the amount of partially tax-exempt interest and by subtracting therefrom Federal income taxes paid, contributions or gifts not otherwise allowed for income-tax purposes, and actual losses from the sales or exchanges of capital assets to the extent to which they are not otherwise allowed. From the result of this computation, which gives what is called the “adjusted net income”, there is to be subtracted an arbitrary allowance of 10 percent of the adjusted net income and the dividends paid to stockholders during the taxable year. The purposes of the two last-named deductions are (1) to allow such corporations a reason-
able reserve for contingencies and (2) to prevent the additional tax from applying to sums actually distributed.

The effect of this system recommended by your subcommittee is to provide for a tax which will be automatically levied upon the holding company without any necessity for proving a purpose to avoid surtaxes. It is believed that the majority of these corporations are formed for the sole purpose of avoiding the imposition of the surtax upon the stockholders.

In regard to the tax on other corporations which improperly accumulate surpluses for the avoidance of surtaxes, only two major changes need be made. First, it is recommended that the rate of tax on these other corporations be reduced to 25 percent. The 50 percent rate now imposed is entirely too high to be readily enforceable. It represents a tax on much more than would have been imposed if the surplus had been distributed.

Moreover, such surplus, even after the payment of tax, is still subject to the surtax in the hands of the individual when ultimately distributed. Second, the present law imposes the tax upon the entire net income; that is, the tax is the same whether 50 percent of the net income was distributed or whether none of it was distributed. It is, therefore, recommended that the tax be applied to the net income after the amount of such net income has been diminished by the amount of dividends paid during the taxable year.

Much more might be said in regard to corporations which are formed or availed of for the purpose of preventing the imposition of surtaxes upon the stockholders. Several instances have recently been developed in connection with the investigations of the Senate Committee on Banking and Currency, and, therefore, it is believed unnecessary to go into this matter further.

Your subcommittee believes that its recommendation now made in respect to these companies is of the utmost importance; and furthermore, that it will result, directly or indirectly, in increasing the annual revenue of the Government by not less than $25,000,000.

Senator Harrison. Mr. Chairman.

The Chairman. Senator Harrison.

Senator Harrison. In this connection, does that report show this whole section of the law with reference to personal holding companies? That ought to be inserted in the record at this point, too.

Mr. Vinson. Senator, at that time we did not have section 351. The only section that we had to meet this problem was section 104.

Senator Harrison. That ought to be in the record.

Mr. Vinson. Yes, sir; and I think it is a good thing to put that section in.

Under Secretary Magill. Yes; I think so.

The Chairman. Without objection, that will also be included in the record.

(See. 104 of the Revenue Act of 1932 is as follows:)

SEC. 104. ACCUMULATION OF SURPLUS TO EVADE SURTAXES

(a) If any corporation, however created or organized, is formed or availed of for the purpose of preventing the imposition of the surtax upon its shareholders through the medium of permitting its gains and profits to accumulate instead of being divided or distributed, there shall be levied, collected, and paid for each taxable year upon the net income of such corporation a tax equal to 50 per centum of the amount thereof, which shall be in addition to the tax imposed by section 13 and shall be computed, collected, and paid upon the same basis and in the same manner and subject to the same provisions of law, including penalties, as that tax.

(b) The fact that any corporation is a mere holding or investment company, or that the gains or profits are permitted to accumulate beyond the reasonable needs of the business, shall be prima facie evidence of a purpose to escape the surtax.

(c) As used in this section the term "net income" means the net income as defined in section 21, increased by the sum of the amount of the dividend deduction allowed under section 23 (p) and the amount of the interest on obligations of the United States issued after September 1, 1917, which would be subject to tax in whole or in part in the hands of an individual owner.
(d) The tax imposed by this section shall not apply if all the shareholders of the corporation include (at the time of filing their returns) in their gross income their entire distributive shares, whether distributed or not, of the net income of the corporation for such year. Any amount so included in the gross income of a shareholder shall be treated as a dividend received. Any subsequent distribution made by the corporation out of the earnings or profits for such taxable year shall, if distributed to any shareholder who has so included in his gross income his distributive share, be exempt from tax in the amount of the share so included.

SECTION 102. SURTAX ON CORPORATIONS IMPROPERLY ACCUMULATING SURPLUS

(The 1934 net provision is section 102 and reads as follows:)

(a) Imposition of Tax.—There shall be levied, collected, and paid for each taxable year upon the adjusted net income of every corporation (other than a personal holding company as defined in section 351) if such corporation, however created or organized, is formed or availed of for the purpose of preventing the imposition of the surtax upon its shareholders or the shareholders of any other corporation, through the medium of permitting gains and profits to accumulate instead of being divided or distributed, a surtax equal to the sum of the following:

1. 25 per centum of the amount of the adjusted net income not in excess of $100,000; plus
2. 35 per centum of the amount of the adjusted net income in excess of $100,000.

(b) Prima Facie Evidence.—The fact that any corporation is a mere holding or investment company, or that the gains or profits are permitted to accumulate beyond the reasonable needs of the business, shall be prima facie evidence of a purpose to avoid surtax.

(c) Definition of "Adjusted Net Income."—As used in this section, the term "adjusted net income" means the net income computed without the allowance of the dividend deduction otherwise allowable, but diminished by the amount of dividends paid during the taxable year.

(d) Payment of Surtax on Pro Rata Shares.—The tax imposed by this section shall not apply if all the shareholders of the corporation include (at the time of filing their returns) in their gross income their entire pro rata shares whether distributed or not, of the "adjusted net income" of the corporation for such year. Any amount so included in the gross income of a shareholder shall be treated as a dividend received. Any subsequent distribution made by the corporation out of earnings or profits for such taxable year shall, if distributed to any shareholder who has so included in his gross income his pro rata share, be exempt from tax in the amount of the share so included.

(e) Tax on Personal Holding Companies.—For surtax on personal holding companies, see section 351.

Under Secretary Magill. I would like to point out this one other thing if I may. The de Mille case was referred to yesterday, and that, of course, was a court decision, and as the Commissioner said, this was a case where the Bureau tried to enforce this old provision, section 104 and took it to court. The facts were as the Commissioner described, and the Bureau was unsuccessful. Of course, I had myself nothing to do with that case; but as I understand it from the legal department, the de Mille case is regarded as giving at least very great difficulty in connection with any further enforcement of section 104.

That brings you up to your 1934.

Mr. Vinson. When that bill was originally introduced by Chairman Doughton, after we had had summer and fall work in 1933, and then considerable work in 1934, section 102 dealt with personal holding companies, and I would like to have included in the record that part of the original bill that was reported to the House. As a matter of fact, the old 104 was numbered in that bill 103, as your 50-per cent tax.

Mr. Kent. One hundred and four.
Mr. Vinson. One hundred and three in the original bill. It was suggested, and the suggestion was concurred in by the Treasury, to reduce the tax on the old 104 from 50 percent to 25 percent. That is correct, is it not?

Under Secretary Magill. I believe so; yes.

Mr. Vinson. After the bill got to the Senate evidently they wanted to keep the old 104 for the penalty tax, and a new section was put in, section 351, which dealt with personal holding companies, and I want to have inserted in the record that section 351 that deals with personal holding companies.

The Chairman. That is in the present law?

Mr. Vinson. No, sir; that is in the 1934 act.

(The matter referred to is as follows:)

[Revenue bill of 1934, H. R. 7835, Feb. 12, 1934]

SECTION 102. TAX ON PERSONAL HOLDING COMPANIES

(a) TAX ON PERSONAL HOLDING COMPANY.—In addition to the tax imposed by section 13, there shall be levied, collected, and paid, for each taxable year, upon the undistributed adjusted net income of every personal holding company, a tax of 35 per centum thereof. Such tax shall be computed, collected, and paid in the same manner and subject to the same provisions of law (including penalties) as the tax imposed by section 13.

(b) DEFINITIONS.—As used in this section—

(1) The term "personal holding company" means any corporation (other than a banking or insurance corporation) if—(A) at least 80 per centum of its gross income for the taxable year is derived from rents, royalties, dividends, interest, annuities, and (except in the case of regular dealers in stock or securities) gains from the sale of stock or securities, and (B) on the last day of the taxable year more than 50 per centum of its voting stock is owned, directly or indirectly, by or for not more than five individuals. For the purpose of this paragraph—(C) stock owned, directly or indirectly, by a corporation, partnership, estate, or trust shall be considered as being owned proportionately by its shareholders, partners, or beneficiaries; (D) an individual shall be considered as owning, to the exclusion of any other individual, the stock owned, directly or indirectly, by his family, and this rule shall be applied in such manner as to produce the smallest possible number of individuals owning, directly or indirectly, more than 50 per centum of the voting stock; and (E) the family of an individual shall include only his brothers and sisters (whether by the whole or half blood), spouse, ancestors, and lineal descendants.

(2) The term "undistributed adjusted net income" means the adjusted net income minus the sum of—

(A) 10 percentum of the adjusted net income; and

(B) Dividends paid during the taxable year.

(3) The term "adjusted net income" means the sum of—

(A) The net income determined without regard to the provisions of this section;

(B) The amount of the dividend deduction allowed under section 23 (p); and

(C) The amount of interest upon obligations of the United States issued after September 1, 1917, which would be subject to tax in whole or in part in the hands of an individual owner; minus the sum of—

(D) Federal income, war-profits, and excess-profits taxes paid or accrued, but not including the tax imposed by this section;

(E) Contributions or gifts, not otherwise allowed as a deduction, to or for the use of donees described in section 23 (o) for the purposes therein specified; and

(F) Losses from sales or exchanges of capital assets which are disallowed as a deduction by section 117 (d).
TAX EVASION AND AVOIDANCE

[Revenue Act of 1931]

SECTION 351. SURTAX ON PERSONAL HOLDING COMPANIES

(a) IMPOSITION OF TAX. There shall be levied, collected, and paid, for each taxable year, upon the undistributed adjusted net income of every personal holding company a surtax equal to the sum of the following:
(1) 30 per centum of the amount thereof not in excess of $100,000; plus
(2) 40 per centum of the amount thereof in excess of $100,000.

(b) DEFINITIONS. As used in this title:

(1) The term "personal holding company" means any corporation (other than a corporation exempt from taxation under section 104, and other than a bank or trust company incorporated under the laws of the United States or of any State or Territory, a substantial part of whose business is the receipt of deposits, and other than a life insurance company or surety company) if (A) at least 50 per centum of its gross income for the taxable year is derived from royalties, dividends, interest, annuities, and (except in the case of regular dealers in stock or securities) gains from the sale of stock or securities; and (B) at any time during the last half of the taxable year more than 50 per centum in value of its outstanding stock is owned, directly or indirectly, by or for not more than five individuals. For the purpose of determining the ownership of stock in a personal holding company (C) stock owned, directly or indirectly, by a corporation, partnership, estate, or trust shall be considered as being owned proportionately by its shareholders, partners, or beneficiaries; (D) an individual shall be considered as owning, to the exclusion of any other individual, the stock owned, directly or indirectly, by his family, and this rule shall be applied in such manner as to produce the smallest possible number of individuals owning, directly or indirectly, more than 50 per centum in value of the outstanding stock; and (E) the family of an individual shall include only his brothers and sisters (whether by the whole or half blood), spouse, ancestors, and lineal descendants.

(2) The term "undistributed adjusted net income" means the adjusted net income minus the sum of:

(A) 20 per centum of the excess of the adjusted net income over the amount of dividends received from personal holding companies which are allowable as a deduction for the purposes of the tax imposed by section 13 or 204;

(B) Amounts used or set aside to retire indebtedness incurred prior to January 1, 1934, if such amounts are reasonable with reference to the size and terms of such indebtedness; and

(C) Dividends paid during the taxable year.

(3) The term "adjusted net income" means the net income computed without the allowance of the dividend deduction otherwise allowable, but minus the sum of:

(A) Federal income, war profits and excess-profits taxes paid or accrued, but not including the tax imposed by this section;

(B) Contributions or gifts, not otherwise allowed as a deduction, to or for the use of donees described in section 23 (a) for the purposes therein specified; and

(C) Losses from sales or exchanges of capital assets which are disallowed as a deduction by section 117 (d).

(4) The terms used in this section shall have the same meaning as when used in title I.

(c) ADMINISTRATIVE PROVISIONS. All provisions of law (including penalties) applicable in respect of the taxes imposed by title I of this Act shall, so far as not inconsistent with this section, be applicable in respect of the tax imposed by this section, except that the provisions of section 111 of that title shall not be applicable.

(d) PAYMENT OF SURTAX ON PRO RATA SHARES. The tax imposed by this section shall not apply if all the shareholders of the corporation include (at the time of filing their returns) in their gross income their entire pro rata shares, whether distributed or not, of the "adjusted net income" of the corporation for such year. Any amount so included in the gross income of a shareholder shall be treated as a dividend received. Any subsequent distribution made by the corporation out of earnings or profits for such taxable year shall, if distributed to any shareholder who has so included in his gross income his pro rata share, be exempt from tax in the amount of the share so included.

(e) IMPROPER ACUMULATION OF SURPLUS. For surtax on corporations which accumulate surplus to avoid surtax on stockholders, see section 102.
Mr. Vinson. Now, Dr. Magill, that rate was a 30-percent rate on personal holding companies where the income was less than $100,000?

Dr. Magill. Was it not 30 and 40?

Mr. Vinson. It was 40 above $100,000, as I recall.

Dr. Magill. Yes.

Mr. Vinson. Now, you were with us. We remember you quite pleasantly. At first, according to the printed report of the Treasury, made subsequent to the report of the Hill subcommittee, certain statements were made in regard to the old 102 and the personal holding company suggestions that had been made. I would like to have included in the record the statement of the Treasury, on page 8 of their report which they presented some time in 1934, on this subject.

The Chairman. Without objection, that will be inserted in the record.

(The matter referred to is as follows:)

(From statement of the Acting Secretary of the Treasury regarding the preliminary report of a subcommittee of the Committee on Ways and Means, relative to methods of preventing tax avoidance and evasion, 1934)

(4) Personal holding companies. There is no doubt that personal holding companies have frequently been organized and utilized as a device to reduce the income taxes of their shareholders. For 15 years the law has contained a presumption that the fact that a corporation is a mere holding company (and for 10 years the fact that it is an investment company), shall constitute prima-facie evidence of a purpose to escape the surtax. Recently this provision of the law has been more energetically enforced and considerable revenue collected under it. One principal difficulty encountered in the enforcement of the tax has been, as the subcommittee states, that the tax rate imposed in the case of such corporations is too high. The Treasury therefore concurs in the recommendation that this rate be reduced, and that the tax be applied to the income remaining after an adjustment for dividends actually paid.

The Department is also in accord with the general plan of subjecting the undistributed income of personal holding companies to a higher rate of tax than that of other corporations. The Department does not believe, however, that the specific method suggested by the subcommittee is entirely desirable. The subcommittee defines a personal holding company in explicit details, thereby placing very definite limitations upon the tax in the case of such companies. Hence if legal ingenuity can devise a kind of company which does not fall within this particular described class, the company escapes this particular tax. There appear to be several forms which such a company might take and thus escape the tax. On the other hand the proposed provision would seem improper to include within its scope certain legitimately organized corporations such as corporations formed by the beneficiaries of an estate merely to facilitate the sale and distribution of its assets. In the opinion of the Department, therefore, the provision in question is open to the criticism which the subcommittee addresses to the present reorganization provisions, viz., that it is overspecific legislation, which not only complicates the revenue law and allows no flexibility in administration but also facilitates evasion.

Mr. Vinson. Section 351 appeared in the 1934 act, and was considered to be an improvement upon the tax laws that were then existing, was it not?

Dr. Magill. I think it was a very great improvement. As I started to say a few minutes ago, section 220 or 102, the original provision, had been found to be comparatively ineffective in practice. Section 351 was a large improvement, in that section 351 did not require proof of a purpose to evade the surtaxes, but provided that if the company fell within the definition of a personal holding company, then these rates were automatically applicable, and the result has been that the Treasury has been able to collect the revenue under
section 351 on these personal holding companies. I think it is very
doubtful whether it could have been collected under section 102.

Mr. Vinson. The rates in the 1934 act, section 351, were 30 and 40
percent. In 1935 two new brackets were included, as I recall it
which made the rates run from 20 to 60 percent. Is that correct?

Under Secretary Magill. I believe that is true. As you know, I
was not here then, but I think that is correct.

Mr. Vinson. When the 1936 Revenue Act came we had the undi-
distributed profits tax. It was recognized the corporation paid the
normal corporate tax. Then you had your pressure rates in regard
to undistributed profits, with the capital-stock tax, and it was recog-
nized that the rates should be lowered in 351. Is not that correct?

Under Secretary Magill. Mr. Kent can answer that better than I,
because he was here at the time.

Mr. Vinson. Is not that correct, Mr. Kent?
Mr. Kent. Yes; that is substantially correct.

Mr. Vinson. And in agreement with the Treasury, those rates were
lowered from 20 to 60 percent in the 1935 act, to rates of 8 to 48
percent. Is not that correct?

Mr. Kent. It was done in conference, Mr. Vinson. I was not
present at that time. I do not know what happened.

Mr. Vinson. Did anybody ever hear from you or anyone else that
the lowering of those rates was objectionable?

Mr. Kent. I could not say as to that, Mr. Vinson, because I was
not here during the conference.

Mr. Vinson. I say, do you know of anybody that objected to the
action in conference?

Mr. Kent. I have no knowledge on that fact.

Mr. Vinson. On page 8 of Mr. Helvering's statement, I read:

...I say actual rate because our experience proves that the statutory rates are
delusive, and in fact merely nominal. The rates stated in the statute run from
8 percent to 48 percent. Actually a preliminary report on 1935 returns shows
the collection of surtax of less than $2,000,000, on personal holding company
income of approximately $115,000,000.

The rates referred to there are the rates in the 1936 act. The re-
turns therein referred to are 1935 returns, and the rates on the 1935
returns run from 20 to 60 percent. Is not that correct?

Mr. Kent. The 1935 act, however, was effective only as to returns
for calendar years or fiscal years beginning after December 31, 1935.
Therefore, as I understand the situation, Mr. Vinson, the 1935 rates
never actually became effective.

Mr. Vinson. What rate was effective, then? It was the 30- to 40-
percent rate that was effective, was it not, on the 1935 returns?

Mr. Kent. It was the 1934 rates. That is right.

Mr. Vinson. Yes; 30 and 40 percent. In other words, the rates
then were higher as affecting the 1935 returns than they are now,
and yet the statement would indicate that the rates that were appli-
cable to the 1935 returns were from 8 to 48 percent.

Now, the statement is made that only $2,000,000 was collected on
personal holding companies in 1935 on income of approximately
$115,000,000. I ask you, Dr. Magill, if the purpose of section 351
is not to force out dividends as income instead of keeping it in the
personal holding company, and rendering it subject to the surtax?
TAX EVASION AND AVOIDANCE

Under Secretary Macill. That is our clear understanding, yes, sir; that Congress had no idea of legitimatizing the personal holding company, but sought to put these rates on at such an amount as would compel them to distribute their income to their stockholders.

Mr. Vinson. Can you tell us how much money has been forced out into the hands of individual taxpayers, making it subject to surtax, as the result of section 351?

Under Secretary Macill. I doubt if you could show that.

Mr. Vinson. It would be a very considerable sum?

Under Secretary Macill. Oh, yes; it would be a large sum. Of course, the other side of it is, as you appreciate. The matter which the Commissioner is going to present later in the morning is, I believe, that through some of these credit provisions, which still remain in the law, companies are able to retain a very large amount of earnings.

Mr. Vinson. I have not referred to that. I am talking about your pressure rates. It is a pressure rate?

Under Secretary Macill. Oh, yes; there is no doubt about it.

Mr. Vinson. And do you think that it shows the picture when you say that less than $2,000,000 has been collected in taxes because of section 351? Do you think it is fair to the Congress to say that, to overlook the millions of dollars that you admit have been collected in taxes due to payment of the surtax of individuals upon income that is declared as dividends by personal holding companies?

Under Secretary Macill. Of course, the sentence that you referred to on page 8 of the Commissioner's statement——

Actually a preliminary report on 1935 returns shows the collection of surtax of less than $2,000,000——

and so forth, I believe "surtax" as used there is intended to mean the surtax under section 351.

Mr. Vinson. I understand that.

Under Secretary Macill. Yes; and that consequently we are not talking there——

Mr. Vinson. I know, but Doctor, do not sidetrack.

Under Secretary Macill. That is impossible.

Mr. Vinson. I recognize what this $2,000,000 is. This $2,000,000 is the tax that is collected under 351. The point I am making is, Do you think that it is fair to Congress and to the operation of section 351 to rest your case upon the collection of less than $2,000,000, because of section 351, when you admit that many millions of dollars have been collected because of the pressure tax in section 351 paid by individuals?

Under Secretary Macill. Let me answer it in two ways. We thought our statement was clear, but if it is not I am glad to have the explanation which you have brought out. Now, further, so far as the question of additional taxes, additional surtaxes being collected from individuals due to the pressure of section 351, the Commissioner, I think, is going to take that up later in this same statement.

Mr. Vinson. You will admit with me that much added revenue has come to the Federal Treasury because of section 351?

Under Secretary Macill. Oh, there is no question about that at all.

Mr. Vinson. Many, many millions of dollars?

Under Secretary Macill. Certainly.
Senator LA FOLLETTE. Before leaving the historical review of this situation I would like to point out in the record that the report of the Joint Committee on Internal Revenue Taxation submitted under date of January 22, 1927, had a great deal to do with directing the attention of Congress to the ineffectiveness of this section that has been discussed. As a result of this report in 1928, the House incorporated in its bill and passed a provision designed to check these situations, and the Senate rejected it.

Mr. VINSON. And if the Senator will permit, as I recall, that report at the time it was made, the statement was that no moneys had been collected under section 102. But subsequent to that time, I think someone from the Treasury came up and asserted that $75,000 had been collected under section 102.

The CHAIRMAN. Are you through, Senator?
Senator LA FOLLETTE. Yes.

The CHAIRMAN. We are ready for Commissioner Helvering to proceed. You wish to proceed with the same understanding we had yesterday, that you will not be interrupted in your statement?
Commissioner HELVERING. If you please; yes, sir.

STATEMENT OF GUY T. HELVERING—Resumed

Commissioner HELVERING. Yesterday, Mr. Chairman and gentlemen, I was discussing the effect of the personal holding company and taking up for consideration certain cases which, at the time of the announcement of this investigation were under consideration in the Conference Section of the Internal Revenue Department. I was just to the point of coming to those 17 cases, and I think the clerk has that statement.

The CHAIRMAN. Top of page 12 of your statement.
Commissioner HELVERING. I had finished page 11 and commenced on page 12 of the statement.

Mr. COOPER. Mr. Chairman, this supplemental mimeographed statement that has been submitted to the committee this morning, does that give the 17 cases to which you refer?
Commissioner HELVERING. Yes, sir. That is the detail of those 17 cases, with one or two changes. I might say further to the members of the press that there will be some slight changes in these figures as I go along.

Mr. COOPER. I suggest, Mr. Chairman, that he call specific attention to any changes that may occur in order that we may make some notations on these mimeographed figures that we have, as well as the press.

Commissioner HELVERING. Of those 17 cases, only 3 paid surtaxes under section 351. I will say that two of them are inconsequential. The remaining 14 paid nothing. The total net income of the 17 companies before any deductions under 351 was $4,602,824.87.

Mr. COOPER. Give that again, please.
Commissioner HELVERING. $4,602,824.87. There is a change in that figure, amounting to a few hundred dollars.

Mr. COOPER. That is the figure that appears on your original mimeographed statement.

Commissioner HELVERING. Well, I have been advised that they got that change and it is made on the copy. They paid in the aggregate under section 18, which imposes the ordinary corporate tax, only
$18,068.07. From the entire group only $25,905.28 was collected as a surtax under section 351. As I said, this amount was paid by only three corporations. The total corporate taxes reported by these 17 corporations was only $43,973.35.

 Those three companies that I have mentioned will be on your report there, the Senior Investment Co., E. W. Scripps Co., and W. W. Hawkins Co., the latter two being the inconsequential ones.

 Senator Harrison. Show where those are, so that we can get some description of them.

 The Chairman. Their place of business.

 Mr. Fortas.

 The Chairman. Give your name if you are going to testify.

 Mr. Fortas. I am Abe Fortas, adviser to the Treasury in this matter. The Senior Investment Corporation, Mr. Chairman, was incorporated in the State of Michigan. The E. W. Scripps Co. was incorporated in Ohio, and the W. W. Hawkins Co. was incorporated in the State of Delaware.

 Commissioner Helvering. The respective cities being Detroit, Cincinnati, and Wilmington.

 If all the income of these companies had been paid directly to their stockholders without the intervention of an artificial holding company, the tax paid would certainly have been much higher. We have made a computation which will serve to give the committee an idea of the extent to which personal holding companies have been employed as tax-avoidance instrumentalities. The computation necessarily makes certain assumptions, but it is believed that these assumptions are reasonable and that any corrections therein would not substantially change the basic result. The first assumption is that each company was beneficially owned by one person. It is realized that personal holding companies are sometimes beneficially owned by a group of individuals. But it is believed that any exaggeration of the tax upon the owners of personal holding companies on account of the assumption of single ownership is more than offset by another assumption; namely, that the owners of the personal holding companies had no income other than that derived from the one personal holding company listed. In many cases they had such other income as would frequently throw their income into higher tax brackets and thereby enhance the rates used in making our assumed calculations.

 On the assumptions stated, which are believed to be fair and to err in favor of conservatism, it appears that the individual owners of the 17 holding companies examined would have had to pay an aggregate of $1,638,023 if no personal holding company had been organized. What did the personal holding companies organized to prevent the incidence of this tax of $1,638,023 actually pay as a tax on personal holding companies? The mere sum of $25,905, to which we should add, to obtain the entire corporate liability, $18,068, making a total corporate tax liability of only $43,973.

 The computation of the individual tax which would have to be paid, in the amount of $1,638,023, takes no account of the 4 percent normal tax of the individual. Inclusion of this item would show an even greater amount of tax avoided, on the stated assumptions. The stockholders of every single personal holding company case under consideration would have been subject to a substantial tax if no
personal holding company had been utilized, and as I have said, in only three cases was the personal holding company utilized—those figures there are changed—subject to personal holding company surtax.

I shall illustrate this general conclusion by reference to the individual cases included in this analysis.

For example, the Robert P. Scripps, of Cincinnati, Ohio—Senator Harrison (interposing). Give their location and their business.

Commissioner Helvering. This is a personal holding company of Robert P. Scripps Co., publisher, of Cincinnati, Ohio. They reported no income tax or surtax for 1934 on a net income of $173,599.03.

We estimate, on the assumptions stated above, and after deducting dividends paid by the company to its stockholders that an additional surtax of $59,840 would have been paid by Mr. Scripps if the personal holding company device had not been employed.

Upon these same assumptions, we compute that payment of surtax for 1934 in the amount of $449,134 was avoided by use of the E. W. Scripps Co., a personal holding company of E. W. Scripps who appears to be the son of Robert P. Scripps. The net income of this corporation was $1,705,405. This company paid personal holding company surtax in the amount of $67.04, and no ordinary corporate tax.

Senator Harrison. Under these two illustrations, you say that E. W. Scripps is a son of Robert Scripps?

Commissioner Helvering. As I understand; yes, sir.

Senator Harrison. What business are they engaged in—the newspaper business?

Commissioner Helvering. Yes, sir.

Senator Harrison. How many papers have they got and how many organizations are they interested in, do you know? Give the committee those facts.

Commissioner Helvering. It has a large organization, several papers in different cities of the United States. I can’t state just now.

Senator Harrison. You don’t know how many papers they run?

Commissioner Helvering. No.

Senator Harrison. But they are interested in various corporations engaged in publishing newspapers?

Commissioner Helvering. Yes, sir.

Senator Harrison. And these personal holding companies get the profit from these various corporations that ordinarily pay a dividend tax, and in this way they only paid $67.04; is that right?

Commissioner Helvering. On an income of one-million-seven-hundred-and-five-thousand-and-odd dollars?

Senator La Follette. May I ask a question, Mr. Chairman?

The Chairman. Senator La Follette.

Senator La Follette. If these companies paid no tax in 1934, they must have had losses, didn’t they?

Commissioner Helvering. Mr. Fortas could answer that.

Mr. Fortas. Mr. Senator, I think the Commissioner will come to that in just a moment. Just for the purpose of the record at this point, I may state the statute allows certain deductions which the Commissioner will explain in detail, and those deductions, together
with certain other aspects of the operation of section 351, are, so far as we can ascertain, responsible for the tax return and payment reflected in the Commissioner's statement.

Senator La Follette. Well, but if losses were a substantial factor in creating this situation, we could not assume that they would always have losses, and in order to give us a more complete picture of this situation, could not the Bureau furnish information as to what happened in 1935 or 1936?

Mr. Fortas. That might be done. I can't tell you offhand whether it is possible or not, on the basis of the information presently available.

If I might explain in a little more detail in response to that question, there are three principal types of deductions that the Commissioner is coming to in a moment in his statement. Those three principal types of deductions do not necessarily represent losses in the sense that you and I understand it in connection with the operation of a business. They may represent a number of things which the Commissioner will explain in a moment.

Senator La Follette. My reason for asking for the situation of these companies in 1935, and particularly in 1936, is that in 1936, as you know, the undistributed profits tax would apply, and therefore in order to get a picture of the situation as it exists today it would be very important, if possible, for the committee to know what happened with these particular companies in 1935 and 1936, to see how the existing law, with all of its provisions, was working.

Mr. Vinson. Will the gentleman yield to me?

Senator La Follette. Yes, sir.

Mr. Vinson. And it would be well to view what has been done in prior years before there was a section 351 that put the tax on personal holding companies.

Under Secretary Macill. As indicated, Mr. Chairman, we are perfectly willing to give you any information which we have or can make available to you. If the committee wants this for past years, or for 1935 and 1936, we will, of course, be glad to make it available as rapidly as we can assemble it.

Mr. Vinson. Mr. Commissioner, now, of course, the corporations paid the normal corporate tax; that is correct, isn't it?

Commissioner Helvering. Yes.

Mr. Vinson. In other words, it was 15 percent at that time. Now, in regard to the E. W. Scripps Co. I note that dividends were paid totaling $850,000, and, of course, that money in the hands of the individual paid the usual income tax, including surtaxes?

Commissioner Helvering. On their personal returns.

Mr. Vinson. On their personal returns?

Mr. Helvering. Yes.

Mr. Vinson. And, of course, that same thing applies to the Robert P. Scripps Co. and all of the rest of them?

Commissioner Helvering. Yes; all distributions.

Mr. Vinson. Where dividends were declared?

Commissioner Helvering. Yes.

Mr. Vinson. The individual on his personal returns paid tax on that; that is, in addition to the corporate tax that they paid of 15 percent?

Commissioner Helvering. Yes; the rate at that time being 13 3/4 percent.

Mr. Vinson. I guess that is right; it is 1935.
Commissioner Helvering. The next company, the Food Industries, Inc., of Philadelphia, Pa., a personal holding company owned by E. W. Dietrich, showed a net income for 1934 in the amount of $293,274. This corporation paid no ordinary corporate tax and no personal holding-company surtax. On the assumption stated above, the owner of this company avoided payment of surtax in the amount of $60,000 by use of this personal holding company.

This same sort of situation appears in the remaining 14 cases included in this analysis. I submit to the committee for admission in evidence, if the committee so desires, a table showing in detail the facts with respect to the 17 cases described above. This table is identified as "Table I—Analysis of 17 personal holding-company returns." That is the table which you have there.

The Chairman. Without objection, the table will be inserted in the record. You want it inserted at this point in your remarks?

Commissioner Helvering. Yes; insert the table.

(The table referred to, identified as "Table I—Analysis of returns for 1934 filed by 17 personal holding companies", was made a part of the record and is appended hereto.)

<table>
<thead>
<tr>
<th>Name</th>
<th>Principal owner</th>
<th>Net income before any adjustments under sec. 381</th>
<th>Ordinary corporate tax paid, sec. 13</th>
<th>Personal holding company surtax paid, sec. 381</th>
<th>Dividends paid</th>
<th>Additional surtax that would have been paid if no personal holding company, after deducting dividends paid (assuming only one stockholder and no other income)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Robert P. Scripps Co.</td>
<td>Robert P. Scripps</td>
<td>$173,599.63</td>
<td>None</td>
<td>None</td>
<td>$45,000</td>
<td>$59,440</td>
</tr>
<tr>
<td>E. W. Scripps Co.</td>
<td>E. W. Scripps</td>
<td>1,708,405.12</td>
<td>None</td>
<td>$47.04</td>
<td>$50,000</td>
<td>440,134</td>
</tr>
<tr>
<td>Kovik Investments, Ltd.</td>
<td>Charles M. Higginson</td>
<td>45,072.87</td>
<td>None</td>
<td>None</td>
<td>6,350</td>
<td></td>
</tr>
<tr>
<td>The Tennessee Co.</td>
<td>W. W. Hawkins</td>
<td>96,929.09</td>
<td>None</td>
<td>None</td>
<td>None</td>
<td>28,422</td>
</tr>
<tr>
<td>Peter Barkey Corporation</td>
<td>Peter Barkey</td>
<td>111,673.00</td>
<td>None</td>
<td>None</td>
<td>34,032</td>
<td></td>
</tr>
<tr>
<td>Laurence Industrial Corporation</td>
<td>Selon E. Summerville</td>
<td>142,286.00</td>
<td>9,955.45</td>
<td>None</td>
<td>45,220</td>
<td>43,000</td>
</tr>
<tr>
<td>Consolidated Publishers</td>
<td>Paul Block</td>
<td>1,100,278.00</td>
<td>None</td>
<td>None</td>
<td>11,250</td>
<td>558,000</td>
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<tr>
<td>Falk Investment Co.</td>
<td>Herman W. Falk</td>
<td>32,854.00</td>
<td>9,354.82</td>
<td>None</td>
<td>None</td>
<td>3,650</td>
</tr>
<tr>
<td>Food Industries, Inc.</td>
<td>D. W. Dietrich</td>
<td>233,274.00</td>
<td>None</td>
<td>None</td>
<td>179,946</td>
<td>60,000</td>
</tr>
<tr>
<td>Senior Investment Corporation</td>
<td>F. J. Fisher</td>
<td>303,426.62</td>
<td>4,781.00</td>
<td>25,857.00</td>
<td>None</td>
<td>100,960</td>
</tr>
<tr>
<td>Terrace Finance Corporation</td>
<td>Clement C. Smith (deceased) and wife.</td>
<td>89,299.04</td>
<td>None</td>
<td>None</td>
<td>10,000</td>
<td>22,000</td>
</tr>
<tr>
<td>Marion Finance Co.</td>
<td>Estate of George P. Miller</td>
<td>83,625.00</td>
<td>None</td>
<td>None</td>
<td>None</td>
<td>20,900</td>
</tr>
<tr>
<td>Adason Tobacco Corporation</td>
<td>C. Louis Allen, C. D. Marshall, A. W. Mellon, R. B. Mellon.</td>
<td>177,773.00</td>
<td>115.00</td>
<td>None</td>
<td>20,250</td>
<td>20,500</td>
</tr>
<tr>
<td>Penn Tobacco Corporation</td>
<td>C. Louis Allen, C. D. Marshall, A. W. Mellon, R. B. Mellon.</td>
<td>192,600.00</td>
<td>None</td>
<td>None</td>
<td>None</td>
<td>70,585</td>
</tr>
<tr>
<td>Smoot Sand and Gravel Co. of Canada, Ltd.</td>
<td>L. E. Smoot</td>
<td>174,387.10</td>
<td>None</td>
<td>None</td>
<td>None</td>
<td>56,900</td>
</tr>
<tr>
<td>W. W. Hawkins Co.</td>
<td>W. W. Hawkins</td>
<td>154,483.00</td>
<td>None</td>
<td>281.24</td>
<td>85,000</td>
<td>36,000</td>
</tr>
<tr>
<td>Allan Co., Ltd.</td>
<td>A. S. Brown</td>
<td>81,500.00</td>
<td>None</td>
<td>None</td>
<td>None</td>
<td>20,600</td>
</tr>
</tbody>
</table>

*Return of Allan Co., Ltd., for 1933 is included, as indicated in the table.*
Senator Harrison. What is this Adason Tobacco Corporation and Penn Tobacco Corporation? Where are they located?

Mr. Fortas. The Adason Tobacco Corporation has its address at 420 Lexington Avenue, New York City; and the Penn Tobacco Corporation—is that the one you are interested in?

Senator Harrison. Yes; for the present.

Mr. Fortas. Has its address at Greenwich, Conn. Both of these are Delaware corporations.

Senator Harrison. Who are the principal stockholders?

Mr. Fortas. The principal stockholders of the Adason Tobacco Co. are C. Louis Allen, who is identified as a manufacturer of tobacco products; C. D. Marshall, a steel manufacturer and bridge builder.

Senator Harrison. What is his address? Is it stated there?

Mr. Fortas. I have his address as Pittsburgh, Pa.

Senator Harrison. What is Mr. Allen's address?

Mr. Fortas. I am sorry; I don't have that. The third principal owner is A. W. Mellon.

Senator Harrison. Of what place have you his address?

Mr. Fortas. Pittsburgh.

The Chairman. Is he the former Secretary of the Treasury?

Mr. Fortas. So I understand; that is correct; and R. B. Mellon, who, I understand, is a brother of A. W. Mellon and also located in Pittsburgh.

Senator Harrison. Are the same individuals in both the Adason and the Penn Tobacco Corporations?

Mr. Fortas. That is right. I might say, however, that the percentage of ownership allocated to these individuals seems to differ in connection with the Adason Tobacco Corporation and the Penn Tobacco Corporation.

Senator Harrison. Let us have the facts.

Mr. Fortas. All right, sir. With respect to the Adason Tobacco Corporation, Mr. Allen owns 296 shares of common and no preferred. Mr. Marshall owns 252 shares of common and 8,750 shares of preferred. Mr. A. W. Mellon owns 126 shares of common and 1,500 shares of preferred; and Mr. R. B. Mellon, who is now deceased, owned also 126 shares of common and 1,500 shares of preferred.

Now, with respect to the Penn Tobacco Corporation, the ownership is as follows: This corporation has no preferred stock outstanding. The ownership of the common is as follows: Mr. Allen, 66,247 shares; Mr. Marshall, 19,094 shares; Mr. A. W. Mellon, 9,547 shares; and the estate of Mr. R. B. Mellon, also 9,547 shares.

Senator Harrison. When were these corporations organized; do you know?

Mr. Fortas. This table shows that the Penn Tobacco Corporation was organized April 2, 1930. The Adason Tobacco Corporation was organized April 6, 1931, approximately a year after the organization of the Penn Corporation.

Senator Walsh. What were the assets of these holding companies—what securities?

Mr. Fortas. I am sorry, sir, but we don't have those figures. They are not shown on the returns, as I understand.
Senator Wals. Is there any connection between the use of the word "tobacco" and the title of these corporations?

Mr. Fortas. That is quite possible, sir, I don't know.

Senator Walsh. Apparently in a holding company for the stocks and bonds of other companies?

Mr. Fortas. I think that is true, as we shall show later.

Senator Walsh. These were holding companies, without the profits being distributed?

Mr. Fortas. That frequently happens; yes, sir.

Mr. Vinson. What was the nature of the income received by these holdings?

Commissioner Helvering. Mostly dividends and stocks and bonds.

Mr. Vinson. Were any of them engaged in industrial activities?

Commissioner Helvering. Once in awhile you will find one.

Mr. Vinson. I am speaking of these.

Commissioner Helvering. I don't think so, not a one of them, were they?

Mr. Fortas. No, sir; so far as our investigation shows, no one of these was engaged in industrial activity. It may be that if a more complete investigation were made we would find that perhaps one of them was so engaged; but to the best of our present information and to the best of my belief, they were not so engaged. I might say, Mr. Chairman, we are going to describe in great detail later on the assets and the nature of the receipts and the income of certain typical personal holding companies, and at that time I think many of these questions will be answered in detail.

Mr. Vinson. It makes a lot of difference as to whether the income is derived purely from dividends and royalties and income of that character. Some of the holding companies have an industrial activity hooked on to the personal pocketbook proposition.

Mr. Fortas. That is quite possible, sir. That is not the typical picture, I should say.

Mr. Vinson. Now, the intercorporate dividend tax does not come into this picture, does it?

Mr. Fortas. No, sir.

Mr. Vinson. Because that tax, a tax of 1½ percent, the tax on intercorporate dividends, was not put upon the books until the 1935 act?

Mr. Fortas. Yes, sir.

Mr. Vinson. Now, any dividends that were received by any of these companies, or any other personal holding companies, since the enactment of the 1935 Revenue Act, of course, would be subject to that rate.

Mr. Cooper. Mr. Chairman, just one point further with respect to this Adason Tobacco Corporation and the Penn Tobacco Corporation, in order to try to be as clear as possible on it. I understood you to say that both of these were purely holding companies?

Commissioner Helvering. Yes.

Mr. Fortas. So far as we know, that is correct.

Mr. Cooper. And not engaged in any industrial production or activity?

Mr. Fortas. That is correct, sir.
Mr. Cooper. Well, now, do you have any information to show why they use the word “tobacco” in the name of this holding company? Why was it called the Adason Tobacco Corporation and the Penn Tobacco Corporation if they had nothing to do with tobacco?

Mr. Fortas. I don’t know, sir. I can repeat Senator Walsh’s suggestion. He suggested that perhaps they held a large amount of the securities of tobacco companies, and I submit that merely as a fairly reasonable guess.

Mr. Cooper. But there is nothing in the record that you have examined to indicate that either of these companies were engaged in any phase of the tobacco business?

Mr. Fortas. That is correct. Now, if you would permit me, I would like to make a further search on that question and report back to the committee at its next session.

Mr. Cooper. Well, of course, it is reasonable to assume that a corporation carrying the name “Penn Tobacco Co.” is engaged in some kind of tobacco business? Is not that a reasonable assumption?

Mr. Fortas. That is the way it would strike me, sir.

Mr. Cooper. Your records indicate that it was in no sense engaged in the tobacco business?

Mr. Fortas. Subject to check; that is correct.

Mr. Cooper. All right.

The Chairman. Do you have anything further, Senator Walsh?

Senator Walsh. No, Mr. Chairman.

The Chairman. You may proceed, Mr. Commissioner.

Commissioner Helvering. These cases concern the following personal holding companies, in addition to those already given:

The Tennessee Co., owned by W. W. Hawkins, Cleveland, Ohio, who subscribed to all the capital stock of this company on its incorporation. More than 50 percent of its stock appears to be held by James Hammond, publisher and editor, during the last half of 1934, and continuously since.

I will just read these other names of these cases, Mr. Chairman, that will be explained later, and again repeating that these cases are the 17 cases that happened to be in the Bureau.

Senator Harrison. What did you say was the address of this man Hawkins?

Commissioner Helvering. Cleveland, Ohio.

Senator Harrison. And Mr. James Hammond, whom you mentioned?

Commissioner Helvering. James Hammond had 50 percent and more than 50 percent of the stock.

Senator Harrison. What was his address?

Commissioner Helvering. I do not have that, unless it is at Cleveland. I do not know.

The Chairman. Could you supply it for the record?

Commissioner Helvering. I think we can find it from the records.

The Chairman. Please do that if you can, so we can keep abreast of it.

Mr. Vinson. Mr. Commissioner, is it your purpose to give us the break-down on the deduction?

Commissioner Helvering. Yes; we expect to bring that all in.
Mr. Vinson. It would seem to me that would give us a real picture of the problems that we have to confront.

Commissioner Helvering. I have some illustrations further on. Now, Mr. Chairman, if I may, I will just read these other 13 or 14 companies that I have not mentioned specifically that were in this group examined:

The Laurence Industrial Corporation, owned by Solon E. Summerfield.

Mr. Cooper. Mr. Chairman?

The Chairman. Mr. Cooper.

Mr. Cooper. I suggest you give the address as you give the name, so we can try to locate them.

Mr. Fortas. That is Jersey City, N. J.

Commissioner Helvering. Laurence Industrial Corporation, owned by Solon E. Summerfield, Jersey City, N. J.

Consolidated Publishers, owned by Paul Block, New York City.

Falk Investment Co., owned by Herman J. Falk, Milwaukee, Wis.

Senior Investment Corporation, owned by F. J. Fisher, Detroit, Mich.

Terrace Finance Corporation, owned by Clement C. Smith, deceased, and his wife; that is at Milwaukee.

Marion Finance Corporation, owned by the estate of George P. Miller, Milwaukee.

Addison Tobacco Corporation, owned by C. Louis Allen, C. D. Marshall, A. W. Mellon, and R. B. Mellon—the one that was just under discussion—New York City.

Penn Tobacco Corporation, owned by the same persons, Greenwich, Conn.

W. W. Hawkins Co., the one I mentioned above, owned by W. W. Hawkins. That is New York City.

Mr. Cooper. Mr. Chairman.

The Chairman. Mr. Cooper.

Mr. Cooper. I did not catch it if you mentioned Smoot Sand & Gravel Co., of Canada, Ltd.

Commissioner Helvering. Oh, that is the next one here.

Mr. Cooper. Oh, you are not through? I thought you had finished the list.

Commissioner Helvering. No.

Mr. Cooper. Go ahead.

Commissioner Helvering. Smoot Sand & Gravel Co. of Canada, Ltd., owned by L. E. Smoot, living in Toronto, Canada.

Altew Co., Ltd., apparently owned by A. S. Brown, who appears to be president of the company. This is a Newfoundland corporation, its address being shown on the return as Paris, France.

The Kovik Investment Co.—

Mr. Cooper. So far as you know, is that where Brown lives, Paris, France?

Commissioner Helvering. I do not know, Mr. Congressman.

Kovik Investments, Ltd., owned by Charles Melbourne Higgins. The address of this corporation is Montreal, Canada.

That, Mr. Chairman, completes the list of the 17 cases that we had under consideration.
Mr. Vinson. What about Peter Berkey Corporation? Did you mention it?

Mr. Fortas. I think, Mr. Vinson, that the Commissioner has that in the record. It was owned by Peter Berkey, and the address of the corporation is Chicago, Ill.

Mr. Crowther. Chicago, Ill.

Mr. Crowther. May I ask if the Commissioner knows whether W. W. Hawkins is the identical person that has the Tennessee Co., W. W. Hawkins?

Mr. Fortas. It appears, Mr. Crowther, that the stock of the Tennessee Co. was originally taken down by W. W. Hawkins' Co., the personal holding company which is owned by W. W. Hawkins. Subsequently and apparently beginning in the last part of 1934 about half of the stock of the Tennessee Co. was acquired by Mr. James Hammond.

Mr. Crowther. Who is Mr. James Hammond?

Mr. Fortas. I understand that he is a publisher and editor.

Mr. Crowther. Then they are functioning as two separate holding companies now, are they, the Tennessee Co. and the W. W. Hawkins Co.?

Mr. Fortas. They are two separate holding companies; yes, sir. The Commissioner will later comment upon the situation existing when one individual or one group owns several holding companies.

Commissioner Helvering. As I said earlier, we shall hereafter present to the committee other individual cases in which the personal holding company has been used to avoid taxes. We shall limit our presentation at the moment to the cases upon which we have been able, in the time at our disposal and with the sources of information at our immediate command in Washington, to collect the facts. I cannot too strongly emphasize to the committee the problem of the Bureau in connection with the assembly of returns in respect of investigation of personal-holding corporations. It is necessary to interconnect individual and corporate returns which, while related in terms of beneficial ownership of income, contain no data on their face leading to immediate determination of such beneficial ownership. Individual and personal holding returns are often filed in widely separated collection districts, and it is a prolonged undertaking to obtain the information necessary for present purposes. The proper assembly and connection of these returns is a major administrative project and the difficulties we have experienced to date in this task suggest imperatively that some changes in the statute should be made to facilitate the work of the Bureau in this respect. I shall comment further upon these difficulties in a few moments.

Senator Harrison. As I understand, Commissioner Helvering, you are giving us these facts without trying to impute fraud on the part of any of these individuals in organizing them, or a purpose to do anything illegal?

Commissioner Helvering. No; I do not understand that that is true in any of these cases.
TAX EVASION AND AVOIDANCE

Senator HARRISON. Legally they have a perfect right to do it, but you are stating these facts with a view to the committee doing something legislatively that might cure this situation. Is that right?

Commissioner HELVERING. That is right.

Mr. COOPER. Mr. Chairman.

The CHAIRMAN. Mr. Cooper.

Mr. Cooper. It is my understanding, Mr. Commissioner, as you proceed with your statement you are going to elaborate further on these 17 companies.

Commissioner HELVERING. No; not on the 17 companies, but on the device and the effect of the deductions under the present section 351.

Mr. Cooper. I understood the gentlemen at your right [Mr. Fortas] to state time after time that further information would be given on certain points that have been raised here.

Commissioner HELVERING. That is true, but I thought you asked the question if I was intending to do that in this statement.

Mr. Cooper. Oh, I see.

Commissioner HELVERING. I am not in this statement.

Mr. Cooper. But you are going to give it for the record?

Commissioner HELVERING. Yes. I think we have the record of all those cases.

Mr. Cooper. And I think it would be helpful if you could in that connection give a little more definite identification of these various individuals mentioned.

Commissioner HELVERING. I think that can be done.

Mr. Cooper. All right.

Commissioner HELVERING. In fact, I know it can be done.

I now wish to show the committee, in a general way, how the various deductions provisions of section 351 have been used to avoid taxes, and to describe in more detail how these provisions are used for that purpose. Other witnesses before the committee will discuss the individual case histories which will show in more detail just how the various possibilities of the personal holding company have been used, in highly ingenious and complex ways, to avoid taxes.

Mr. Vinson. Mr. Chairman.

The CHAIRMAN. Mr. Vinson?

Mr. Vinson. Before section 351 ever came on the statute books, you had personal holding companies?

Commissioner HELVERING. Surely.

Mr. Vinson. And they were avoiding much more tax than they are now? In other words, you had no surtax, you had no added rate upon personal holding companies until section 351 was written into the law, except that which is referred to in section 102, which was admitted by all to be ineffective!

Under Secretary MAGILL. That is true. I think if the committee please, if the Commissioner can go along without interruption and finish the balance of the statement, you will get the general picture much better.

Mr. Vinson. Mr. Magill, this statement here said that under section 351 these evasions were happening. That statement is correct,
and certainly I am wholeheartedly cooperating with the Bureau and the Treasury to prevent that. But the fact yet remains that those things were going on in larger degree, many more millions of dollars were not subject to taxation, before Congress wrote section 351.

Under Secretary Magill. That is quite true. I think we could perhaps summarize it this way, if you agree that we both did the best we could in 1934 to correct a situation that was bad. The situation at present is undoubtedly better than it was in 1934.

The Chairman. It is not satisfactory yet.

Under Secretary Magill. We still hope to improve it further. That is the purpose of this.

Mr. Crowther. Will the gentleman yield?

Mr. Vinson. Certainly.

Mr. Crowther. I would like to ask the gentleman from Kentucky if he does not think this is the fact: That there was never a real, earnest, sincere effort made to enforce section 102, and that it became practically a dead issue?

Mr. Vinson. It was dead; and they said to us that it could not be enforced.

Mr. Crowther. Yes; that was the information, as I remember it, that it could not be enforced.

Mr. Vinson. In other words, the penalty of 50 percent was stated to us to be such a burden, and the facts necessary to be shown in court so hard of proof, that section 102 was practically a nullity.

Under Secretary Magill. Yes.

Mr. Crowther. If the gentleman will permit me I should like to say that, as I remember it, the statement was made that it was so difficult to determine what was a reasonable withholding and what was a reasonable amount.

Under Secretary Magill. Dr. Crowther, if you will refer back to what we went over yesterday to that de Mille case, which is the most recent case dealing with the operation of section 102, you will see exactly the situation that the Bureau was in in trying to enforce that provision. It just does not work.

Mr. Crowther. Well, we helped you with 351?

Under Secretary Magill. You certainly did. The situation is much better. You unquestionably stopped a great deal of the leakage of revenue; and what we are here for now is to see if we can stop the rest.

Mr. Crowther. In fact, some of these cases we have got here arose when 351 was not in existence, did they not?

Under Secretary Magill. As to some that the Commissioner has presented; yes. So far as this table of 17 companies is concerned, as I understand it, they are concerned with the first year of the operation of section 351.

Commissioner Helvering. Mr. Chairman, we have analyzed 1,300 returns filed under the 1936 act, representing various districts in the country. These returns were selected purely at random. They are returns which happened to be readily available in the Washington office at the beginning of our investigation. They represent a portion of 4,616 returns by personal holding companies which were on file at that time.
Of these 1,300 cases, 278 claimed the 20-percent deduction allowed in section 351 (b) (2) (A); 46 claimed deductions for capital losses allowed in section 351 (b) (3) (C) over and above those allowed to individuals; and 56 claimed deductions on account of a "reasonable" retirement of debt incurred before January 1, 1934, as allowed in section 351 (b) (2) (B).

The comparatively small number claiming deductions under each of these items, peculiar to personal holding companies, again shows that the personal-holding-company device has been most effectively used by comparatively few persons, but these few persons are among those best able to bear a substantial part of the tax burden. They appear to be persons whose total income, including that of their personal holding companies, is in the highest brackets. Here again we see that by taking assets out of their personal boxes and transferring them to an "incorporated pocketbook", certain large, wealthy taxpayers have avoided paying their full share of taxes.

This is apparent from the amount of the deductions claimed on each of the returns. On the 278 returns claiming the 20-percent exemption, this deduction was taken in the aggregate amount of $4,878,471. The tax reduction attributable to these deductions was $929,831. If the income of these personal holding companies had been paid directly to the individuals who owned them, no such deduction would be allowed.

Because of this deduction alone, the individual owners of the 278 companies saved 62.90 percent of the personal holding surtax which their specially created corporations would otherwise have to pay. The Government, by the same token, lost $929,831. If an analysis of the entire 4,516 returns filed under the 1936 act to April 30, 1937, produced comparable results, it would show at least $3,000,000 of aggregate savings to individuals who were willing and able to form personal holding companies.

The 50 companies, included in the 1,800 returns analyzed, which claimed credit for debt retirement, claimed deduction in the amount of $5,606,444. The tax reduction attributable to the deductions amounted to $982,967.

These personal holding companies, if they had not taken this credit, would have had to increase their tax payments 813.84 percent over the tax actually reported under section 351. The individual owners of these companies, therefore, saved 813.84 percent of the tax paid by their personal holding companies under section 351 by claiming deductions for moneys paid in retirement of their debts. Without question, as we shall hereafter show, some of these debts were owed to the stockholders themselves. The result was that payment of taxes was avoided by paying or setting aside money to pay themselves.

An individual without a personal holding company cannot reduce his taxable income on account of payments in retirement of debts to himself.

If a survey of the entire group of 4,516 personal holding-company returns produced a result comparable to the analysis of the 1,800 returns, it would show that the debt-retirement provision permits an annual avoidance of personal-holding surtax in the amount of at least $3,250,000.
Perhaps the most striking results appear with respect to deductions allowed to personal holding companies for capital losses in excess of the amount allowed to individuals. The 46 companies claiming deductions on this account, listed capital losses in the sum of $11,251,535.60. The tax reduction obtained was $725,509.07, or 704.36 percent of the tax which they paid under section 351. In other words, if the owners of these personal holding companies had not availed themselves of this deduction, they would have had to pay a tax over 700 percent larger than the tax actually paid under section 351.

Mr. Vinson. What did that amount to?
Commissioner Helvering. $4,700,000 plus.
This deduction for capital losses is not available to individuals. They can deduct their capital losses only to $2,000, unless they are offset by capital gains. Assuming that the capital losses listed by the 46 companies were sustained on sales or exchanges involving a real change of ownership, it is reasonable to suppose that the individuals who created and owned the personal holding companies taking the losses otherwise not deductible, avoided payment of a substantial amount in taxes.

However, some of these capital losses were undoubtedly a mere shift from one pocket to another. In other words, they represented transfer, as Mr. Magill pointed out, between two companies owned by the same or associated people, or between a personal holding company and an individual. In these cases, the tax avoided was even greater in amount. The personal holding company is here clearly being used indefensibly as a tax-avoiding mechanism.

If a survey of the total group of 4,516 returns showed results comparable to the analysis of the 1,800 returns, it would reveal that the payment of tax in the amount of $2,500,000 has been avoided by the use of the provisions allowing the deduction of capital losses to personal holding companies.

In order to summarize this information for the committee, let me say that the use of the personal holding company by these individuals, together with resort to the three types of deductions allowed under section 351 resulted in a saving in the tax that would otherwise have been paid by these personal holding companies in the amount of $2,638,307. This figure is the amount of tax saved by claiming the three deductions mentioned, by the 1,800 personal holding companies specifically analyzed. We estimate that an analysis of the larger group of 4,516 personal holding companies would show a similar tax reduction, because of resort to these three provisions, in the amount of $9,237,000. However, neither the actual figure given for the 1,800 cases, nor the estimate for the 4,516 cases represents the total loss resulting from use of these deductions by all personal holding companies which will come under the provisions of the 1936 act. An indeterminate number of holding companies have not yet filed returns and therefore are not included within the group of 4,516 mentioned above.

I would like at this time, Mr. Chairman, to have distributed some tables to be used in connection with the next few statements.

The Chairman. Do you wish this table inserted in the record at this point, Mr. Commissioner?
Commissioner Helvering. I want it to go into the record where it will fit best in this statement, and I think that is a little further over, but I thought in talking about this you might want to compare it with the table.

The Chairman. All right.

Commissioner Helvering. These figures also do not take account of the increased savings to the few wealthy individuals who have created holding companies and used them in the manner indicated, resulting in a decrease in their individual surtax rates. If the income received by these personal holding companies had been paid directly to their individual owners, these individuals would, as a result of receiving this income, have found themselves in a higher surtax bracket for individual returns. As a matter of fact, the aggregate figures given above are without doubt just a fraction of the amount of tax avoided within the period covered by use of the personal holding companies and reliance on the deductions permitted such companies; by the same token they represent just a small fraction of the revenue which has been diverted from the Government by reason of this device.

The table marked “Exhibit A” shows a break-down and detail for the 46 corporations which claimed a deduction for capital losses over and above that allowed to individuals. It gives the name of the company, its adjusted net income—that is, its net income less deductions and credits under the act, including deductions for capital losses and its tax liability under section 351 and the rate. It also shows the deductions taken under the capital losses provision of section 351, and the tax and rate which would have prevailed had these capital losses not been deducted.

Exhibit B shows comparable data respecting credits for debt retirement which I have discussed.

Exhibit C shows comparable material for 50 of the 278 companies which have claimed deductions under the 20-percent provision. Only 50 of these cases are shown because of the mechanical difficulty of working out in time for presentation to the committee the data for the entire group. These 50 cases include, however, some of the largest instances of use of this provision in the group of 278.

Exhibit D is a composite of the information shown on exhibits A, B, and C with respect to 80 cases. These 80 cases were selected at random from the group shown on the other exhibits. They happened to be readily available at the time the composite table was made. This table, exhibit D, clearly shows that some of the personal holding companies did not content themselves with resort to only one of the deduction provisions of section 351. A good many utilized the 20-percent credit provision and the capital loss provision, some of them utilized these two provisions as well as the debt retirement provision.

This table shows the adjusted net income of each of the companies, together with such deductions as they took under the three provisions described above and also deductions for dividends paid to their stockholders. It also shows what the tax would have been if deductions under the provision permitting 20 percent credit, credit for retirement of indebtedness and for capital loss, had not been taken. The table further shows the tax rate which was actually applied and the
tax rate which would have been applied had these deductions not been used.

Now, if it is the desire to the committee, I would like to offer these tables in evidence, if the committee sees fit.

The Chairman. How is that?

Commissioner Helvering. I would like to offer these four tables at this time.

The Chairman. Without objection, they will be inserted in the record.

(The four tables headed "Personal holding companies", and marked, respectively, exhibits A, B, C, and D, were thereupon received and they are as follows.)
### PERSONAL HOLDING COMPANIES

**EXHIBIT A.—Statistics with respect to repeal of sec. 351 (b) (3) (C)—Losses from sales or exchanges of capital assets which are disallowed as a deduction by sec. 117 (d)**

<table>
<thead>
<tr>
<th>Name of corporation</th>
<th>Adjusted net income, line 7, 1126H</th>
<th>Losses disallowed by sec. 117 (d)</th>
<th>Sec. 351 tax liability as reported</th>
<th>Sec. 351 tax after eliminating 117 (d) losses</th>
<th>Maximum surtax rate as reported</th>
<th>Maximum surtax rate as revised</th>
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</thead>
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<tr>
<td>Baltic Securities Corporation (New Jersey)</td>
<td>$10,996.34</td>
<td>$863,149.49</td>
<td>$1,383.47</td>
<td>$131,356.99</td>
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<td>18</td>
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<td>Claytona Co., Ltd. (New Jersey)</td>
<td>12,386.86</td>
<td>137,010.70</td>
<td>1,583.15</td>
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<td>28</td>
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<td>Beech Corporation (New Jersey)</td>
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<td>25,000.00</td>
<td>27,167.02</td>
<td>5,785.92</td>
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<td>28</td>
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<tr>
<td>Jerlyn Securities Corporation (New Jersey)</td>
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<td>1,694.00</td>
<td>3,000.00</td>
<td>5,497.08</td>
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<tr>
<td>The New Englandern Corporation (New Jersey)</td>
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<td>3,555.88</td>
<td>3,971.82</td>
<td>5,160.76</td>
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<td>151 Corporation (New Jersey)</td>
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<td>1,137.45</td>
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<td>6,597.90</td>
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<td>4,313.61</td>
<td>7,151.33</td>
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<td>Bradley Estates, Inc. (3d New York)</td>
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<td>Habakt Trading Corporation (2d New York)</td>
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<td>Briggs Commercial &amp; Development Co. (Delaware)</td>
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<td>8,758.72</td>
<td>0</td>
<td>18</td>
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**TAX EVASION AND AVOIDANCE**
Berchris Corporation (Utah) .................................................. (302.83) 14,834.43 0 7,921.30 0 18
Trustees of the Smith Securities Co. (Washington) ............ (21,336.79) 43,853.62 0 2,890.24 0 18
The Phillips Properties Inc. .............................................. (1,568,012.24) 1,652,591.21 0 11,856.76 0 18
Lane Investment Co. (Florida) ......................................... (1,667.84) 1,677.06 0 1,561.14 0 18
Rowland Co. (Florida) ..................................................... (159,359.83) 183,395.65 0 3,274.18 0 18
Union Investment Co. (Maine) ........................................... (20,644.88) 44,285.38 0 4,227.00 0 18
Alexander Timberlands Co. (Delaware) ............................. 185,256.58 49,432.09 0 5,284.78 0 18

Additional tax if sec. 117(d) losses were eliminated, $725,509.07.

Note.—The above-listed data have been taken from 46 original personal holding company returns, Form 1120H, which returns have been selected from almost every district of the country. The foregoing 46 corporations claimed the credit for capital losses out of a group of 1,300 taxable and nontaxable returns recently examined for this feature.

Total taxable 1120H’s filed in all districts from Jan. 1 to Apr. 30, 1937 .................................................. 1,483
Total nontaxable 1120H’s filed in all districts from Jan. 1 to Apr. 30, 1937 .................................................. 3,033
Total of all 1120H’s filed in all districts from Jan. 1 to Apr. 30, 1937 .................................................. 4,516

It appears reasonable to conclude that if the 1,300 returns examined results in additional tax of $725,509.07, an additional tax of approximately $2,500,000 would be produced by a complete survey of the 4,516 returns filed to Apr. 30, 1937. Or, stated otherwise, if sec. 351 (b) (3) (C) of the Revenue Act of 1936 were repealed additional revenue would be produced in the amount of $2,500,000.
<table>
<thead>
<tr>
<th>Name of corporation</th>
<th>Adjusted net income, line 7, form 1120H</th>
<th>Amount used or set aside to retire indebtedness, item 12, form 1120H</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rockland Corporation</td>
<td>$271,459</td>
<td>$150,000</td>
</tr>
<tr>
<td>The Roy W. Howard Co.</td>
<td>511,904</td>
<td>251,135</td>
</tr>
<tr>
<td>The New York Sun, Inc.</td>
<td>196,842</td>
<td>300,000</td>
</tr>
<tr>
<td>The W. W. Hawkins Co.</td>
<td>252,245</td>
<td>100,853</td>
</tr>
<tr>
<td>Haban Trading Corporation</td>
<td>11,385</td>
<td>4,000</td>
</tr>
<tr>
<td>Senior Investments Corporation</td>
<td>706,458</td>
<td>8,100</td>
</tr>
<tr>
<td>M. K. Inc.</td>
<td>49,546</td>
<td>8,955</td>
</tr>
<tr>
<td>Warren Investment Company</td>
<td>16,712</td>
<td>639</td>
</tr>
<tr>
<td>The Kemper Investment Co.</td>
<td>38,885</td>
<td>30,000</td>
</tr>
<tr>
<td>Dayton Investment Co.</td>
<td>205,883</td>
<td>101,247</td>
</tr>
<tr>
<td>The Robert P. Scripps Co.</td>
<td>271,920</td>
<td>820,581</td>
</tr>
<tr>
<td>The U. W. Scripps Co.</td>
<td>1,048,935</td>
<td>1,003,000</td>
</tr>
<tr>
<td>Standard Railway Equipment Co.</td>
<td>765,632</td>
<td>38,500</td>
</tr>
<tr>
<td>Midland Investment Co.</td>
<td>255,456</td>
<td>88,550</td>
</tr>
<tr>
<td>Spring Mills, Inc.</td>
<td>204,662</td>
<td>75,184</td>
</tr>
<tr>
<td>Mount Hebron Corp.</td>
<td>2,754,041</td>
<td>513,944</td>
</tr>
<tr>
<td>Delaware Realty &amp; Investment Co.</td>
<td>5,631</td>
<td>8,000</td>
</tr>
<tr>
<td>The Claborn Co.</td>
<td>76,132</td>
<td>2,402</td>
</tr>
<tr>
<td>Hanan Securities Corporation</td>
<td>5,385</td>
<td>5,000</td>
</tr>
<tr>
<td>Crosett Investment Corporation</td>
<td>13,770</td>
<td>5,000</td>
</tr>
<tr>
<td>Indianapolis Water Works Securities Co.</td>
<td>14,606</td>
<td>62,500</td>
</tr>
<tr>
<td>The Pierce Co.</td>
<td>415,223</td>
<td>225,000</td>
</tr>
<tr>
<td>Elkhart Co.</td>
<td>55,653</td>
<td>44,577</td>
</tr>
<tr>
<td>Third Security Co.</td>
<td>128,265</td>
<td>58,923</td>
</tr>
<tr>
<td>United States Investment Co.</td>
<td>23,699</td>
<td>26,696</td>
</tr>
<tr>
<td>Central West Securities Co.</td>
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<td>120,000</td>
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<tr>
<td>The Amsco Securities Corporation</td>
<td>31,572</td>
<td>30,000</td>
</tr>
<tr>
<td>National Industrial Service, Inc.</td>
<td>34,272</td>
<td>63,000</td>
</tr>
<tr>
<td>Keeler Coal Co. of Illinois</td>
<td>10,197</td>
<td>862</td>
</tr>
<tr>
<td>Hanan Investments, Inc.</td>
<td>223,534</td>
<td>200,000</td>
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<tr>
<td>The Houghton Co.</td>
<td>5,300,401</td>
<td>370,000</td>
</tr>
<tr>
<td>The Coalced Co.</td>
<td>456,611</td>
<td>100,000</td>
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<tr>
<td>Smithfield Securities Corporation</td>
<td>98,917</td>
<td>9,034</td>
</tr>
<tr>
<td>Cherokee Securities Corporation</td>
<td>14,917</td>
<td>15,000</td>
</tr>
<tr>
<td>International Participation Corporation</td>
<td>5,931</td>
<td>27,200</td>
</tr>
<tr>
<td>Bloomfield Center Corporation</td>
<td>135,649</td>
<td>23,199</td>
</tr>
<tr>
<td>Lay Improvement Corporation</td>
<td>216,250</td>
<td>57,667</td>
</tr>
<tr>
<td>Lyngsley Realty Corporation</td>
<td>1,369</td>
<td>620</td>
</tr>
<tr>
<td>Woodruff-Owen Co.</td>
<td>14,473</td>
<td>17,837</td>
</tr>
<tr>
<td>Minnetonka Investment Co.</td>
<td>36,814</td>
<td>3,000</td>
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</table>

B.—Statistics with respect to repeal of the credit for debt retirement as provided under sec. 351 (b) (2) (B) of the Revenue Act of 1936

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TAX EVASION AND AVOIDANCE

---

<table>
<thead>
<tr>
<th></th>
<th>Sec. 351 tax liability as reported</th>
<th>Sec. 351 tax liability after eliminating column 3</th>
<th>Maximum surtax rate as reported</th>
<th>Maximum surtax rate as revised</th>
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<tbody>
<tr>
<td>Rockland</td>
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<td>0</td>
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<td>W. W.</td>
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<td>Haban</td>
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<td>9</td>
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<td>M. K.</td>
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<td>9,137</td>
<td>9</td>
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<td>Robert P.</td>
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<td>Pierce</td>
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<td>0</td>
<td>18</td>
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<td>Elkhart</td>
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<td>0</td>
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<td>0</td>
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<td>United</td>
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<td>0</td>
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<td>Central</td>
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<td>Amsco</td>
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<td>0</td>
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<tr>
<td>National</td>
<td>6,574</td>
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<td>0</td>
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<td>Keeler</td>
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<td>0</td>
<td>18</td>
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<td>Coalced</td>
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<td>18</td>
</tr>
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<td>Smithfield</td>
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<td>1</td>
<td>38</td>
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<td>Cherokee</td>
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<td>18</td>
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<tr>
<td>International</td>
<td>619</td>
<td>0</td>
<td>0</td>
<td>18</td>
</tr>
<tr>
<td>Bloomfield</td>
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<td>0</td>
<td>0</td>
<td>18</td>
</tr>
<tr>
<td>Lay</td>
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<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Lyngsley</td>
<td>22</td>
<td>22</td>
<td>2</td>
<td>18</td>
</tr>
<tr>
<td>Woodruff</td>
<td>2,354</td>
<td>0</td>
<td>0</td>
<td>18</td>
</tr>
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<td>Minnetonka</td>
<td>83</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>D. R. Fish Co.</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Company Name</td>
<td>Shares</td>
<td>Market Value</td>
<td>Dividend</td>
<td>Price</td>
</tr>
<tr>
<td>----------------------------------------</td>
<td>--------</td>
<td>--------------</td>
<td>----------</td>
<td>-------</td>
</tr>
<tr>
<td>To. O. W. Fisher Co.</td>
<td>99,336</td>
<td>35,000</td>
<td>0</td>
<td>2,683</td>
</tr>
<tr>
<td>O. D. Fisher Investment Co.</td>
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<td>11,000</td>
<td>0</td>
<td>5,27</td>
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<tr>
<td>The Scripps Newspapers, Inc.</td>
<td>52,461</td>
<td>44,753</td>
<td>0</td>
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<td>The Thomas L. Stiles Co.</td>
<td>72,967</td>
<td>51,894</td>
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<td>7,988</td>
</tr>
<tr>
<td>Burton Securities Co.</td>
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<td>125,000</td>
<td>0</td>
<td>464</td>
</tr>
<tr>
<td>Arthur J. Collins Estate, Inc.</td>
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<td>63,186</td>
<td>0</td>
<td>1,714</td>
</tr>
<tr>
<td>C. C. Clark, Inc.</td>
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<td>30,000</td>
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<td>170</td>
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<tr>
<td>Milton, Mann &amp; Monzon, Inc.</td>
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<td>3,500</td>
<td>0</td>
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</tr>
<tr>
<td>The C. B. Goddard Investment Co.</td>
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<td>15,500</td>
<td>0</td>
<td>2,552</td>
</tr>
<tr>
<td>Ero Mercantile Co.</td>
<td>55,049</td>
<td>26,000</td>
<td>0</td>
<td>1,937</td>
</tr>
<tr>
<td>Edie Corporation</td>
<td>14,836</td>
<td>14,381</td>
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<td>138</td>
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<tr>
<td>Franklin Investment Co.</td>
<td>16,357</td>
<td>5,000</td>
<td>0</td>
<td>60</td>
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<tr>
<td>New York &amp; London Management Co., Ltd. (Delaware)</td>
<td>937</td>
<td>1,000</td>
<td>0</td>
<td>293</td>
</tr>
<tr>
<td>Chegas Corporation</td>
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<td>293</td>
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<tr>
<td>Belleair Securities Corporation</td>
<td>23,618</td>
<td>39,666</td>
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<td>3,201</td>
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<tr>
<td><strong>Total</strong></td>
<td>23,949</td>
<td>5,606,444</td>
<td>313,212</td>
<td>1,296,179</td>
</tr>
</tbody>
</table>

**Increase in tax due to elimination of credit for debt retirement, $982,967**

**Note.**—The above-listed data have been taken from 55 original personal holding company returns, form 1120H, which returns have been selected from almost every district of the country. The foregoing 55 corporations claimed the credit for debt retirement out of a group of 1,000 taxable and nontaxable returns recently examined for this feature.

Total taxable 1120H's filed in all districts from Jan. 1 to Apr. 30, 1937, .................................................. 1,483

Total nontaxable 1120H's filed in all districts from Jan. 1 to Apr. 30, 1937 .................................................. 3,093

Total of all 1120M's filed in all districts from Jan 1 to Apr. 30, 1937 .................................................. 4,516

It appears reasonable to conclude that if the 1,000 returns examined results in additional tax of $982,967, an additional tax of approximately $3,250,000 would be produced by a complete survey of the 4,516 returns filed to Apr. 30, 1937. Or, stated otherwise, if sec. 351 (b) (2) (B) of the Revenue Act of 1936 were amended additional revenue would be produced in the amount of $3,250,000.
<table>
<thead>
<tr>
<th>Name of corporation</th>
<th>1936 adjusted net income</th>
<th>20 percent of item 10, sec. 351 (b) (2) (A)</th>
<th>Sec. 351 tax liability as reported</th>
<th>Sec. 351 tax liability eliminating 20-percent provision</th>
<th>Maximum surtax bracket after eliminating 20-percent provision</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rockland Corporation</td>
<td>$271,459</td>
<td>$54,292</td>
<td>0</td>
<td>$117</td>
<td>0</td>
</tr>
<tr>
<td>Baltic Securities Corporation</td>
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<td>1,779</td>
<td>18</td>
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<tr>
<td>Claytons Co., Ltd.</td>
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<td>1,585</td>
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</tr>
<tr>
<td>Beech Corporation</td>
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<td>27,107</td>
<td>67,677</td>
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<tr>
<td>F. A. Emerick &amp; Co., Inc.</td>
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<tr>
<td>Jaxon Corporation</td>
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<td>166,542</td>
<td>40,701</td>
<td>88,332</td>
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<td>Jaycor Securities Corporation</td>
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<td>14,145</td>
<td>18,183</td>
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<tr>
<td>Junyn Securities Corporation</td>
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<td>Marquette Corporation</td>
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<td>New Castle Corporation</td>
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<tr>
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<td>Northern Exploration Corporation</td>
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<td>The Transit Corporation</td>
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<tr>
<td>The United Telegram Co.</td>
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<td>100,905</td>
<td>128,683</td>
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<td>Western Merchandise Corporation</td>
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<td>The Roy W. Howard Co.</td>
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<td>Chenery Corporation</td>
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<td>2,400</td>
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<td>Rogers Trading Corporation</td>
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<td>Corporation</td>
<td>Tax Due</td>
<td>Credit Due</td>
<td>100% of Tax Due</td>
<td>20% of Credit Due</td>
<td>Total Tax Due Due to Elimination of 20% Exemption</td>
</tr>
<tr>
<td>--------------------------------------------------</td>
<td>---------</td>
<td>------------</td>
<td>-----------------</td>
<td>-------------------</td>
<td>-----------------------------------------------</td>
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<td>Aviation Securities Corporation of New England</td>
<td>118,157</td>
<td>23,637</td>
<td>16,819</td>
<td>22,892</td>
<td>18,201</td>
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<td>The W. W. Hawkins Co.</td>
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<td>33,019</td>
<td>0</td>
<td>3,650</td>
<td>18,201</td>
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<td>Triangle Conduit Co., Inc.</td>
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<td>37,896</td>
<td>49,807</td>
<td>28,992</td>
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<td>The Grace Co.</td>
<td>214,310</td>
<td>42,862</td>
<td>155</td>
<td>1,330</td>
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<td>Alba Corporation</td>
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<td>6,588</td>
<td>12</td>
<td>511</td>
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<td>Mason &amp; Olney Corporation</td>
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<td>3,790</td>
<td>12</td>
<td>511</td>
<td>18,201</td>
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<td>Driggs Corporation</td>
<td>55,198</td>
<td>11,640</td>
<td>1,656</td>
<td>163</td>
<td>18,201</td>
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<td>Lorimer Investment Co.</td>
<td>55,227</td>
<td>11,648</td>
<td>1,643</td>
<td>163</td>
<td>18,201</td>
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<tr>
<td><strong>Total</strong></td>
<td>13,878,875</td>
<td>2,422,159</td>
<td>705,019</td>
<td>1,192,714</td>
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<tr>
<td>Increase in tax due to elimination of 20 percent exemption</td>
<td>12,201,580</td>
<td>2,455,312</td>
<td>773,104</td>
<td>1,215,240</td>
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<tr>
<td><strong>Grand total</strong></td>
<td>25,360,435</td>
<td>4,878,471</td>
<td>1,478,123</td>
<td>2,407,954</td>
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<tr>
<td><strong>Total increase in tax due to elimination of 20 percent exemption, $929,831</strong></td>
<td></td>
<td></td>
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</tr>
</tbody>
</table>

1 Various.
3 Average of 18 percent.

NOTE.—The above-listed data have been taken from 278 original personal holding company returns, form 1120-H, which returns have been selected from almost every district of the country. The following 278 corporations represent the taxable returns examined which disclosed a credit for the 20 percent exemption. Many of the nontaxable returns also claimed credit for this 20 percent exemption.

Total taxable 1120-H's filed in all districts from Jan. 1 to Apr. 30, 1937 — 1,483
Total nontaxable 1120-H's filed in all districts from Jan. 1 to Apr. 30, 1937 — 3,633

Total of all 1120-H's filed in all districts from Jan. 1 to Apr. 30, 1937 — 4,516

It appears reasonable to conclude that if the 1,300 returns examined results in additional tax of $929,831, an additional tax of approximately $3,487,000 would be produced by a complete survey of the 4,516 returns filed to Apr. 30, 1937. Or, stated otherwise, if sec. 351 (b) (2) (A) of the Revenue Act of 1936 were repealed additional revenue would be produced in the amount of $3,487,000.
<table>
<thead>
<tr>
<th>No.</th>
<th>Name of corporation</th>
<th>1936 adjusted net income</th>
<th>20-per cent credit</th>
<th>Amount used or not used to retire indebtedness</th>
<th>Loss from sale or exchange of capital assets</th>
<th>Dividends paid credit</th>
<th>Revised undistributed net income</th>
<th>Tax reported on revised undistributed net income</th>
<th>Maximum surtax bracket</th>
</tr>
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<tbody>
<tr>
<td>1</td>
<td>The Amoco Securities Corporation (Delaware)</td>
<td>$472,179</td>
<td>$75,920</td>
<td>$120,000</td>
<td>$823,149</td>
<td>$276,000</td>
<td>$196,179</td>
<td>$1,383</td>
<td>$44,730</td>
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<td>2</td>
<td>Aetna Securities Corporation (New Jersey)</td>
<td>16,618</td>
<td>4,724</td>
<td>39,656</td>
<td>98,327</td>
<td>170,000</td>
<td>121,945</td>
<td>2,301</td>
<td>333,621</td>
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<td>3</td>
<td>Beneficial Securities Corporation (Delaware)</td>
<td>22,618</td>
<td>7,191</td>
<td>11,920</td>
<td>1,170,710</td>
<td>150,000</td>
<td>39,003</td>
<td>6,621</td>
<td>6,621</td>
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<tr>
<td>5</td>
<td>Buron Securities Corporation (Florida)</td>
<td>176,685</td>
<td>35,338</td>
<td>125,000</td>
<td>137,635</td>
<td>39,003</td>
<td>25,698</td>
<td>4,093</td>
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<tr>
<td>6</td>
<td>Central West Securities Co. (Delaware)</td>
<td>23,695</td>
<td>4,728</td>
<td>23,695</td>
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<tr>
<td>7</td>
<td>Chasag Corporation (Delaware)</td>
<td>9,093</td>
<td>1,981</td>
<td>3,000</td>
<td>5,150</td>
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<td>8</td>
<td>Cherokee Securities Corporation (Delaware)</td>
<td>36,917</td>
<td>7,783</td>
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<td>22,100</td>
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<tr>
<td>9</td>
<td>Chase Securities Corporation (Delaware)</td>
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<td>(562,645)</td>
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<tr>
<td>10</td>
<td>Clayton Investment Co. (Delaware)</td>
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<td>(9,601)</td>
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<td>11</td>
<td>Coalesced Co. (Delaware)</td>
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<td>13</td>
<td>Dayton Investment Co.</td>
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<td>7,779</td>
<td>30,000</td>
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<td>14</td>
<td>Delaware Realty &amp; Investment Co. (Delaware)</td>
<td>7,794</td>
<td>337,928</td>
<td>513,944</td>
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<tr>
<td>15</td>
<td>Col. H. A. DuPont Co. (Delaware)</td>
<td>(1,892)</td>
<td>(10,300)</td>
<td>22,100</td>
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<tr>
<td>16</td>
<td>Edic Corporation (Delaware)</td>
<td>14,936</td>
<td>2,967</td>
<td>14,936</td>
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<tr>
<td>17</td>
<td>Elv прог Co. (Delaware)</td>
<td>415,223</td>
<td>11,114</td>
<td>225,000</td>
<td>2,951</td>
<td>207,200</td>
<td>22,100</td>
<td>2,474</td>
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<td>18</td>
<td>Elton Investment Co., Inc. (Delaware)</td>
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<td>(10,300)</td>
<td>13,936</td>
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<tr>
<td>19</td>
<td>F. A. Emerick &amp; Co. (New Jersey)</td>
<td>21,473</td>
<td>4,295</td>
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<tr>
<td>20</td>
<td>D. R. Fisher &amp; Co. (Washington)</td>
<td>9,814</td>
<td>1,981</td>
<td>3,000</td>
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<tr>
<td>21</td>
<td>O. D. Fisher Investment Co. (Washington)</td>
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<td>11,000</td>
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<tr>
<td>22</td>
<td>The O. W. Fisher Co. (Washington)</td>
<td>99,336</td>
<td>13,936</td>
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<td>Franklin Investment Co. (Delaware)</td>
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<td>Frankfurt Corporation (Delaware)</td>
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<td>281,527</td>
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<td>Green Estate, Inc. (New York)</td>
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<td>88,365</td>
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<td>Haban Trading Corporation (New York)</td>
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<td>2,233</td>
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<td>27</td>
<td>Hanan Investments, Inc. (Delaware)</td>
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<td>28</td>
<td>Hanan Securities Co. (Delaware)</td>
<td>22,245</td>
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<td>2,967</td>
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<tr>
<td>29</td>
<td>W. W. Hawkins Co. (C-New York office)</td>
<td>22,245</td>
<td>33,019</td>
<td>100,857</td>
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<td>Hutton Association (New Jersey)</td>
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<td>166,542</td>
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<td>31</td>
<td>The Houston Corporation</td>
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<td>44,767</td>
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<td>32</td>
<td>The Roy W. Howard Co. (C-New York)</td>
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<td>33</td>
<td>Hudson Co. (Delaware)</td>
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<tr>
<td>34</td>
<td>Invwood Corporation (New York)</td>
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<td>Jaxon Corporation (New Jersey)</td>
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<tr>
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<td>1,095</td>
<td>8,000</td>
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<tr>
<td>Kentucky Merchants Corp. (New York)</td>
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<td>12,000</td>
<td>10,267</td>
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<tr>
<td>M-K, Inc. (Michigan)</td>
<td>49,546 5,906</td>
<td>8,964</td>
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<tr>
<td>Marquette Corporation (New Jersey)</td>
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<td>Midland Investment Co. (Delaware)</td>
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<td>Mount Hebron Corporation (1 New York)</td>
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<td>Nenno's Corporation (Delaware)</td>
<td>146,202 499,966</td>
<td>125,682</td>
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<td>New Castle Corporation (New Jersey)</td>
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<tr>
<td>The New Market Corporation (New Jersey)</td>
<td>542,373 108,475</td>
<td>128,142</td>
<td>16,859</td>
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</tr>
<tr>
<td>The New York Sun, Inc. (2 New York)</td>
<td>193,652 29,768</td>
<td>149,593</td>
<td>149,593</td>
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<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>The New York Corporation (New Jersey)</td>
<td>90,288 1,838</td>
<td>90,012</td>
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<tr>
<td>Orchard Corporation (New Jersey)</td>
<td>10,119 2,630</td>
<td>34,450</td>
<td>34,450</td>
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<tr>
<td>Ormond Corporation</td>
<td>225,399 43,250</td>
<td>21,493</td>
<td>66,056</td>
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<tr>
<td>The Park Corporation (New Jersey)</td>
<td>103,583 20,921</td>
<td>75,000</td>
<td>65,000</td>
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<tr>
<td>The Phillips Corporation (New York)</td>
<td>80,442 17,883</td>
<td>30,370</td>
<td>30,370</td>
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<tr>
<td>The Phillips Properties, Inc. (District of Columbia)</td>
<td>(1,565,928) 1,565,928</td>
<td>244,574</td>
<td>12,000</td>
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<tr>
<td>The Prince's Co. of Delaware, Inc. (Delaware)</td>
<td>7,257 1,451</td>
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<td>7,916</td>
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<tr>
<td>Regent Corporation (Delaware)</td>
<td>513,943 121</td>
<td>172,617</td>
<td>172,617</td>
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<tr>
<td>Renapi Corporation (Delaware)</td>
<td>37,618 1,451</td>
<td>337,179</td>
<td>337,179</td>
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<tr>
<td>Rene Corporation (New Jersey)</td>
<td>97,600 19,332</td>
<td>120,000</td>
<td>120,000</td>
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<tr>
<td>Rockland Corporation (New Jersey)</td>
<td>271,459 64,092</td>
<td>150,000</td>
<td>150,000</td>
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<tr>
<td>Ruppert Holding Corporation (New York)</td>
<td>375,031 75,806</td>
<td>129,031</td>
<td>129,031</td>
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<tr>
<td>Samusa Corporation (Delaware)</td>
<td>17,114 3,425</td>
<td>31,885</td>
<td>31,885</td>
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<tr>
<td>The Travelers Corporation (Washington)</td>
<td>252,463 50,892</td>
<td>44,756</td>
<td>44,756</td>
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<tr>
<td>The Thomas L. Skill Co. (1 Ohio)</td>
<td>72,887 51,091</td>
<td>27,500</td>
<td>27,500</td>
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<tr>
<td>The Thomas L. Skill Co. (1 Ohio)</td>
<td>255,436 51,091</td>
<td>27,500</td>
<td>27,500</td>
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<tr>
<td>Springs Mills, Inc. (Delaware)</td>
<td>166,737 133,333</td>
<td>166,757</td>
<td>166,757</td>
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<tr>
<td>Standard Industries (New Jersey)</td>
<td>54,036 54,036</td>
<td>54,036</td>
<td>54,036</td>
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<tr>
<td>Standard Railway Equipment Co. (Delaware Corporation) (Delaware)</td>
<td>1,408,933 1,408,933</td>
<td>25,401</td>
<td>475,198</td>
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<tr>
<td>Stanwood Investment Corporation (Delaware)</td>
<td>1,218 249</td>
<td>249</td>
<td>249</td>
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<tr>
<td>Steeplechase. Ltd. (Maryland)</td>
<td>55,812 128,025</td>
<td>153,892</td>
<td>153,892</td>
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<tr>
<td>The Still Pond Co. (Delaware)</td>
<td>141,533 141,533</td>
<td>133,012</td>
<td>133,012</td>
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<tr>
<td>The Transit Corporation (New Jersey)</td>
<td>215,337 43,337</td>
<td>132,069</td>
<td>132,069</td>
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<tr>
<td>Trunellizing Process Corp. (New York)</td>
<td>166,096 26,522</td>
<td>129,011</td>
<td>129,011</td>
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<tr>
<td>The United Texile Co. (New Jersey)</td>
<td>496,068 99,992</td>
<td>149,194</td>
<td>149,194</td>
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<tr>
<td>Western Merchandise Corporation (New Jersey)</td>
<td>56,197 19,923</td>
<td>11,265</td>
<td>11,265</td>
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<td></td>
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<tr>
<td>Wether Bros. Corporation (Delaware)</td>
<td>757,174 143,025</td>
<td>22,852</td>
<td>22,852</td>
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<td></td>
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<tr>
<td>Western Leasing Corp. (Delaware)</td>
<td>757,174 143,025</td>
<td>22,852</td>
<td>22,852</td>
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<tr>
<td>Bradie Estates, Inc. (New York)</td>
<td>17,213 7,213</td>
<td>6,984</td>
<td>6,984</td>
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<tr>
<td>Cherven Corporation (New York)</td>
<td>65,158 25,719</td>
<td>235,575</td>
<td>235,575</td>
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<td></td>
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<td></td>
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</tr>
<tr>
<td>Curtis Southwestern Corporation (2 New York)</td>
<td>(1,912,993) (1,912,993)</td>
<td>1,986,096 1,986,096</td>
<td>1,986,096</td>
<td></td>
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</tbody>
</table>
Commissioner Helvering. We have attempted to obtain the names of the owners of the companies shown on exhibits A, B, C, and D. Because of mechanical difficulties beyond our control, which I here-tofore described, we have thus far been unable to obtain the names of owners of all these corporations. I have here, however, a list of such of the personal holding companies shown on these exhibits, together with their owners, as we have been able to obtain them. I have table no. II, which is a small table that I would like to give to the committee at this time.

Mr. Cooper. I ask that it be put in the record.

The Chairman. Without objection, it will be inserted in the record.

Mr. Cooper. That is table no. II.

The Chairman. Yes.

(Table II is as follows:)

<table>
<thead>
<tr>
<th>Principal owners</th>
<th>Personal holding companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Thomas W. Lamont</td>
<td>Beech Corporation.</td>
</tr>
<tr>
<td>Mrs. F. C. Lamont</td>
<td>Rockland Corporation.</td>
</tr>
<tr>
<td>Isabel Willys</td>
<td>Clayton Co., Ltd.</td>
</tr>
<tr>
<td>Alfred P. Sloan, Jr.</td>
<td>Newcastle Corporation (one-half).</td>
</tr>
<tr>
<td>Mrs. Irene Jackson Sloan</td>
<td>Marquette Corporation, Rene Corporation, Newcastle Corporation (one-half).</td>
</tr>
<tr>
<td>Charles Hayden (deceased)</td>
<td>United Telegram Co., Northern Exploration Corporation.</td>
</tr>
<tr>
<td>Jeremiah Milbank</td>
<td>The Transit Corporation.</td>
</tr>
<tr>
<td>Roy W. Howard and wife</td>
<td>The Roy W. Howard Co.</td>
</tr>
<tr>
<td>W. S. Paley</td>
<td>The Park Corporation.</td>
</tr>
<tr>
<td>Jacob Ruppert</td>
<td>Ruppert Holding Corporation.</td>
</tr>
<tr>
<td>W. L. Burton</td>
<td>Burton Securities Co.</td>
</tr>
<tr>
<td>Mr. and Mrs. W. W. Hawkins</td>
<td>W. W. Hawkins Co.</td>
</tr>
<tr>
<td>Harry A. Hatry</td>
<td>Habalu Trading Corporation.</td>
</tr>
<tr>
<td>Fred Fisher</td>
<td>Senior Investment Corporation.</td>
</tr>
<tr>
<td>Wm. A. Kent</td>
<td>M-K, Inc.</td>
</tr>
<tr>
<td>Geo. D. Dayton</td>
<td>Dayton Investment Co.</td>
</tr>
<tr>
<td>Robert P. Scripps</td>
<td>The Robert P. Scripps Co.</td>
</tr>
<tr>
<td>E. W. Scripps</td>
<td>The E. W. Scripps Co.</td>
</tr>
<tr>
<td>Robert Nixon</td>
<td>Midland Investment Co.</td>
</tr>
<tr>
<td>Pierre du Pont</td>
<td>Delaware Realty &amp; Investment Co.</td>
</tr>
<tr>
<td>Herbert T. Hamman</td>
<td>Hamman Securities Corporation.</td>
</tr>
<tr>
<td>F. V. du Pont</td>
<td>Elalfred Co.</td>
</tr>
<tr>
<td>Wm. Dewart and wife</td>
<td>The New York Sun, Inc.</td>
</tr>
<tr>
<td>Allisal Munnon Bruce</td>
<td>The Coalseed Co.</td>
</tr>
<tr>
<td>W. R. Coe</td>
<td>Cherokee Securities Corporation.</td>
</tr>
<tr>
<td>T. L. Sidlee</td>
<td>The Thomas L. Sidlee Co.</td>
</tr>
<tr>
<td>Charles E. Merrill</td>
<td>Baltic Securities Corporation.</td>
</tr>
<tr>
<td>Edmund C. Lynch</td>
<td>Jeruslum Securities Corporation, Orchard Corporation, Staples Products, Ltd., Western Merchandise Corporation.</td>
</tr>
<tr>
<td>Paulina du Pont</td>
<td>Nemours Corporation.</td>
</tr>
<tr>
<td>Mrs. Ethel H. du Pont</td>
<td>The Still Pond Co.</td>
</tr>
<tr>
<td>W. du Pont Ross</td>
<td>Renapfi Corporation.</td>
</tr>
<tr>
<td>H. F. du Pont</td>
<td>Col. H. F. du Pont Co.</td>
</tr>
<tr>
<td>R. C. du Pont</td>
<td>Elton Investment Co., Inc.</td>
</tr>
</tbody>
</table>
Valentine E. Macy, Jr.---------- Hudson Co.
Virginia Campbell------------ Chesapeake Securities Corporation.
John W. Grove---------------- Prudence Co. of Delaware, Inc.
Duncan Phillips------------- The Phillips Properties, Inc.

Commissioner HELVERING. If the committee examines table II, it will note that in some cases one person is the principal beneficial owner of a number of the personal holding companies shown thereon. As I previously stated, sometimes this ownership and use, for tax reduction, of multiple personal holding companies reaches huge proportions. Some individuals do not confine their ownership to one personal holding company but employ a multiplicity of companies undoubtedly to reduce the surtax applicable to a consolidation of assets in a single personal holding company.

Mr. COOPER. Mr. Chairman.

The CHAIRMAN. Mr. Cooper.

Mr. COOPER. If you will permit me to interrupt you there, Mr. Commissioner, on this table II just presented to the committee, I notice that on the left is shown the principal owner, and on the right the personal holding companies. Am I correct in assuming that the personal holding companies listed on the right of the table are the companies owned by the individuals listed on the left?

Commissioner HELVERING. That is right.

Mr. COOPER. The first two names appear to be Thomas W. Lamont and Mrs. F. C. Lamont. Are they related in any way?

Mr. FORTAS. If I may answer that, Mr. Cooper, Mrs. F. C. Lamont appears to be the wife of Mr. Thomas W. Lamont.

Mr. COOPER. Then Thomas W. Lamont is the owner of the Beech Corporation, which is a personal holding company, and his wife, Mrs. F. C. Lamont, is the owner of the personal holding company under the name of Rockland Corporation. That is correct, then, is it?

Mr. FORTAS. That is correct, sir.

Mr. COOPER. Do you happen to know whether any of these other people listed on the left of the table as principal owners are related to any of these other people here, shown as principal owners?

Mr. FORTAS. I may call your attention, Mr. Cooper, to the names of Alfred P. Sloan, Jr., and Mrs. Irene Jackson Sloan, appearing on the first page of table II.

Mr. COOPER. All right.

Mr. FORTAS. I understand that Mrs. Irene Jackson Sloan is the wife of Alfred P. Sloan, Jr. Now, you will notice opposite these names the names of four personal holding companies. The Newcastle Corporation appears at the beginning and at the end of that list of four companies; but as a matter of fact, the stock of all these four separate personal holding companies is owned by Alfred P. Sloan, Jr., and Mrs. Irene Jackson Sloan, in various proportions, in fact.

Mr. COOPER. And she is his wife?

Mr. FORTAS. That is correct, sir. Now, you will notice that Mr. Roy W. Howard and wife are listed as owning the Roy W. Howard Co. I have no information as to the relationship, if any, between the various Fishers that are shown at the bottom of page 1.
TAX EVASION AND AVOIDANCE

Now, if you will look on page 2, Mr. Cooper, you will see "Robert P. Scripps" and "E. W. Scripps", and we have already commented upon the relationship of these two persons.

Mr. Cooper. E. W. Scripps is the son of Robert P. Scripps?

Mr. Fortas. So it appears.

Mr. Cooper. As you stated awhile ago?

Mr. Fortas. That is correct; yes, sir. It may be, Mr. Cooper—I am informed that Mr. Robert P. Scripps is a son of E. W. Scripps. I am sorry I can't give you precise information on that point.

Mr. Cooper. Your information is it is daddy and boy, or the other way around?

Mr. Fortas. That seems to be perfectly clear. You will notice several du Ponts on table II, and again I can't personally at this time give you exact information as to their relationship. I am advised, however, that they are members of the same family.

You will also notice on that table Charles E. Merrill and Edmund C. Lynch. I am advised that Mr. Merrill and Mr. Lynch are partners in the investment banking business, the investment banking firm now being in liquidation. I think that covers my present information on these names, in response to your question.

Senator Harrison. Would it be possible for you to give in the record their business addresses in this table no. II?

Mr. Fortas. Yes, Senator; I have that information here in respect to a number of these companies. I think it would save the time of the committee if I were permitted to insert in good form in the record a list containing that information. It would take a good deal of time for me to search that out and read it to the committee now.

Commissioner Helvering. As I say, this procedure serves to divide income among personal holding companies and permits escape from the higher personal holding company surtax brackets. Another purpose is served in that a multiplicity of personal holding companies gives flexibility in the matter of the sale or exchange of assets without effecting any actual beneficial change of ownership. Further tax avoidance over and above that resulting from the use of these incorporated pocketbooks and the deduction provisions thereby results from the pyramiding of the pocketbooks. We shall hereafter show, in specific cases, the result of the use of this device.

Witnesses who will appear before this committee after me, if it meets with the committee's wishes, will explain in detail the many and various ways by which these possibilities of escaping taxation are used by some of our taxpayers.

In conclusion, I want to say, as an officer of the Bureau whose duties are primarily administrative, I wish to emphasize the administrative problem created by the use of corporations to avoid taxes. This method of tax avoidance shades by imperceptible degrees from the use of companies having a substantial separate existence to mere shams. Courts have great difficulty in drawing the line at any particular point. Plausible arguments can be made by so-called tax experts, who convince taxpayers that they have a sure method of saving them money in almost any case.

Therefore even the most transparent scheme has in it the danger of litigation. Many taxpayers think that they always have at least a fighting chance in a lawsuit. It must be apparent that the Depart-
TAX EVASION AND AVOIDANCE

ment’s tax collections cannot be conducted effectively under constant litigation. Devices of the sorts described and to be described before this committee are spreading very rapidly under present tax-avoidance publicity conditions.

The atmosphere in which such schemes grow so rapidly is well illustrated by a recent statement appearing in the press in which Mr. J. P. Morgan is reported to have said, “If the Government doesn’t know enough to collect its taxes, a man is a fool to pay them.” That attitude is fairly general. It stimulates both corporations and individuals to distribute circular letters, advertising their skill in enabling individuals to avoid taxes.

There is now much literature on tax avoidance and an increasing number of concerns who are developing it into what may be termed a racket. Later in the hearing we expect to develop this in some detail.

I am asking now, Dr. Crowther, that the “47 ways to save taxes” be put on your table as an illustration of one of those methods constantly being used by certain so-called experts to provoke our trouble still further.

The Vice Chairman. Do you want to distribute that?

Commissioner Helvering. Yes.

The Vice Chairman. All right; go ahead.

Senator Harrison. You have cited the names so that the gentlemen who are interested in publishing them may have them. Is that correct?

Commissioner Helvering. In the 17.

Senator Harrison. Yes; and this list, table II.

Mr. Vinson. The 17 cases were not taken from random. The 17 were on the Commissioner’s desk at the time of the President’s message.

Mr. Fortas. That is correct and, Senator, if I may recall something that the Commissioner said with respect to the 1,300 cases from which those names were selected——

Mr. Cooper (interposing). Is that the names on table II?

Mr. Fortas. Yes, sir; on table II, and among those 1,300 cases which show deductions they are reflected on tables A, B, C, and D. The list of names that you have on table II is a list of the names of the owners of such of those corporations as the Bureau could identify. The 1,300 cases were selected purely at random as a fairly substantially large list, and we believe representative sample of the 4,516 returns on file at that time. I don’t think we can emphasize too much to the committee the fact that this is purely a random selection, and that no particular individuals have been singled out here—purely a random selection.

Senator La Follette. Mr. Chairman.

Senator Harrison. Senator La Follette.

Senator La Follette. May I ask whether the Bureau, in the preparation for these hearings, has gone over the testimony given before the Finance Committee in executive session in 1936 to ascertain whether there were not some cases given there that might have been examined? Can someone answer that question?

Under Secretary Magill. I am just informed that that was not done.
Senator La Follette. Might it not be productive of some very interesting information?

Under Secretary Magill. I think it is an excellent suggestion. We will do it.

Senator La Follette. I presume, Mr. Chairman, that those hearings having been taken in executive session and the information on income-tax returns having been revealed and the secrecy ban never having been removed, that I am not in position to quote from them; but I would like to direct the attention of the Bureau to some of the cases which they presented to us in arguing in behalf of the undistributed profits tax, and one of the most startling examples, more startling than any that have been presented here, is not in the information furnished the committee today, and I would like to request that those hearings in executive session before the Finance Committee be gone over by the Bureau, and I think some interesting examples will be found there which might be very helpful to the committee.

Under Secretary Magill. We will do that as soon as we can.

Senator Harrison. Without objection, that will be done.

Mr. Oliphant. To be sure that we exactly understand the Senator's request, do I understand the Senator is requesting us to present all the information we have on all the cases we have mentioned in those hearings?

Senator La Follette. The ones we are just now dealing with are personal holding companies, and I think this might be a considerable line of information on some of the other topics; but right now I am directing my request to the personal holding company feature.

Mr. Oliphant. I intended to limit my request to the Senator in that same way. Does the Senator request the Department to supply the committee with all the information it has on the personal holding companies covered in that hearing?

Senator La Follette. I do; and I would also like to suggest to the members of the Department and Bureau that it might be well to survey these hearings and ascertain whether there may not be other information there that would be helpful to the committee if it were presented in a public hearing.

Mr. Oliphant. I should like to call attention of the committee again to the fact that we have sought to limit our presentation of cases in this hearing to those upon which we have relatively complete information. The request of the Senator, as he has now further defined it to the Department, is that we furnish this information on each of the holding-company cases, even though as to some of those cases the information may be relatively incomplete.

Senator La Follette. Mr. Chairman, I don't know what the situation is. Here is some testimony that Mr. Russell gave. Would it be in order for him to repeat that testimony?

Senator Harrison. He could do it, but I think it would be better to withhold it now so as to avoid repetition in picking out these special cases later.

Mr. Cooper. Mr. Chairman, just for a moment, referring again to table II and the names of Robert P. Scripps and E. W. Scripps, which have heretofore been mentioned, I have just been informed that the father has been deceased for a number of years. Do you know whether that is accurate or not?
Commissioner Helvering. I am advised that is true.

I will give you that advertisement put out by one company, under the caption, "Forty-seven Ways to Save Taxes."

(The photostatic document referred to, under the caption "Forty-seven Ways to Save Taxes", was made a part of the record and is as follows:)

**47 WAYS TO SAVE TAXES**

The 47 Tax-Saving Items Listed Below Are But A Small Fraction of the Scores of Tax-Control Methods Now Available in the Alexander Federal Tax Service. This Complete, Up-to-Date Tax Guide Is the Only Tax-Saving Service Available Today—The Only Service That Offers You Concrete, Practical Plans for Tax Reduction. Here Are 47 Examples of the Tax-Control Methods Available to You in the Alexander Service:

1. Tax-saving method whereby actual losses on foreclosures may be definitely established and deducted in full (par. 591).
2. Method whereby earned surplus and depreciated assets may be distributed as dividend without tax on the earned surplus distributed (par. 703).
3. United States Supreme Court indicates proper manner of wording corporate resolution to avoid double taxation where appreciated assets are being distributed as a dividend (par. 703).
4. How to carry forward excise taxes for 1 or more years (par. 75).
5. How part of next year's deductions may be taken this year (par. 53).
6. How losses on "interfamily" transactions can be deducted (par. 301).
7. How corporation may deduct salaries (ultimately never paid) which will not constitute income when canceled (par. 303).
8. Circuit court shows method for avoiding income tax on deposits for bottles, barrels, boxes, syphons, and the like (par. 310).
9. Postponement of gain on appreciated assets by transfer from corporation to individual and possible avoidance of two taxes (par. 705).
10. Contingency bonus deductions denied Fuller Brush Co., Horn & Hardart, and others, may be taken by following proper procedure (par. 304).
11. Tax savings from multiple trusts as compared to single trust (par. 101).
12. Coca-Cola Co.'s plan of offering options found advantageous to stockholders as compared with usual plan (par. 503).
13. Partnerships may have different taxable year from partners; may use different accounting basis (par. 103).
14. Method whereby recapitalization loss may be deducted immediately or postponed at stockholder's discretion (par. 551).
15. Method for avoiding reporting 100-percent gain before receipt of liquidating dividend (par. 704).
16. Tax saving involved by abandoning instead of selling assets (par. 600).
17. Tax saving by prorating contributions over more than one period (par. 801).
18. Most advantageous valuation to declare for capital stock tax (par. 1003).
19. Realty—value of improvements by lessee may be reported by owner at time of completion, or over life of lease (par. 75).
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A corporation has assets in its surplus account, now valued at $100,000 but purchased several years ago for $20,000. A dividend of $100,000 is to be declared. If the assets are sold for $100,000 and this money is used to pay the dividend, the corporation will become subject to a tax on the gain of $80,000. However, if the corporation declares the dividend payable in those specific assets, there will be no recognized gain and no tax at all to the corporation. A simple change in the wording of the dividend resolution saves this company a tax on $80,000. See item no. 8.

Under the new Revenue Act of 1936, it may be advisable for certain corporations to replace present preferred stock with new "debenture preferred stock." The debenture stock sets up a definite obligation on the part of the corporation to pay interest, and enables the corporation to accrue the interest on its books as a deduction—even though not paid. Such a plan would reduce expenses, preserve liquid assets, and avoid any dispute as to surplus distribution. See item no. 31.

A taxpayer has a mortgage of $35,000 against a property which has depreciated in value to $8,000. Unless he forecloses, it would be difficult to prove a fractional bad-debt loss, and if he sells the mortgage the loss would be limited to $2,000. However, if this taxpayer executes a new mortgage at $8,000 to replace the old one, this is considered under the law as a "fractional bad-debt loss", and the full amount of $27,000 is deductible. See item no. 1.

THE ALEXANDER PUBLISHING CO., INC., 60 WALL STREET, NEW YORK CITY

Commissioner Helvering. I want to emphasize that that is going on continuously, and they got us outnumbered. We have a hard time keeping up with them.

Senator La Follette. May I interrupt right there, Mr. Helvering? That is a phase of this situation that I, as one member of the committee, am very much interested in; that is, the enormous turn-over which I understand exists in the Bureau personnel, and I was wondering if it would be feasible at some stage before these hearings are concluded, for the Bureau to furnish to the committee a list of those who had been employees of the Bureau, say over a period of years, who have gone out of the Bureau and gone into
private practice in tax cases and tax matters. If that could be done I think it would be very helpful to the committee and to the Congress in getting the picture on a part of the problem which, as I understand it exists, namely, that many of these people go into the Bureau, stay there until they are pretty well equipped on various decisions and rulings and the procedure, and then they go out into private practice and they find that it is not lacking in remuneration.

It seems to me that in considering the problem that the Bureau confronts in this situation it would be very helpful to the committee if that information could be furnished. I am not pressing for it in a hurry, but I mean before we conclude our hearings. I would like to go back over a representative period of years, if it is not too much of a task.

Senator Harrison. Would you say 10 years?

Senator La Follette. Yes.

Senator Harrison. Without objection, then, the committee will request these records and the names of the employees who have left the Department and who are now in the practice of income-tax matters.

Commissioner Helvering. That is to be confined to the larger ones, not all the clerks. That would be an enormous task.

Senator La Follette. Find out as much as you can about it. I think it is one of the real problems in this struggle between the Government and the taxpayers to collect taxes and the resistance of certain taxpayers to paying taxes.

Commissioner Helvering. That is quite true. I say I have the information and that is the way the Bureau is handling it, and so forth and so on, and convincing the taxpayers they know what they are talking about.

Mr. Cooper. Just one question, if I may—this exhibit "Forty-seven Ways to Save Taxes", is that a photostat of an actual advertisement that was issued by this publishing company shown at the bottom of it?

Commissioner Helvering. Yes, sir; and later in the hearings we expect to develop this in some detail.

Mr. Vinson. Mr. Chairman, while we are asking for information I would like to have some submitted to the committee. I would like to have the total revenue yield from section 102, dating back 10 years, say, to the taxable year of 1927, and then I would like to have submitted for the record the revenues derived, the additional taxes paid into the Treasury because of the existence of section 381.

The Vice Chairman. Without objection that request will be granted.

Mr. Crowther. I would like to ask the Commissioner this, if the names on these lists A, B, C, and D were selected at random, too?

Commissioner Helvering. The A, B, and C were the cases available here in the Bureau. Table D was taken at random from those that had more complete information.

Mr. Crowther. And this no. II, did they all appear on some of these four sheets?

Commissioner Helvering. Yes, sir.

Mr. Crowther. They all follow?

Commissioner Helvering. Yes, sir.

Mr. Crowther. These were picked at random and then these were picked at random out of the whole?
Commissioner Helvering. That is right.

Mr. Crowther. I observe the random method of selection is stressed.

Mr. Fortas. Might I explain that a bit further, Mr. Crowther?
Table II contains the names of all owners of all such corporations appearing on exhibits A, B, C, and D as we could ascertain; that is to say on the basis of our present information, table II is a complete list of owners.

Mr. Crowther. Individual owners; nobody else owns any of the stocks; they are individual owners of these companies?

Commissioner Helvering. They are at least the principal owners of these companies.

Mr. Crowther. The principal owners, not the entire owners, you don't mean to say in all cases?

Commissioner Helvering. Not in all cases.

Mr. Crowther. You have a list of pretty prominent people there in view of the random method of selection.

Mr. Oliphant. May I verify, Mr. Chairman, the nature of Congressman Vinson's request? I understand the request is for an estimate of the revenue produced, both directly and indirectly, from section 351, so far as the latter can be roughly determined?

Mr. Vinson. Right.

Senator Harrison. Mr. Commissioner, did you put into the record this publishing company's advertisement?

Commissioner Helvering. I wanted to call attention to it in the record, if the committee cares to put it in. In this connection, I want to call attention, Senator, to item 22, which advises the avoidance of tax by the use of the personal-holding company, the subject I am discussing.

Senator Harrison. I would like to draw the attention of the committee to the fact that it is absolutely necessary for the Senate Members to be on the floor of the Senate at 12 o'clock.

Mr. Cooper. That is true of the House Members also.

Commissioner Helvering. May I say at this point there are just a few more paragraphs in my statement. May I conclude?

Senator Harrison. Yes; I thought you had finished. You may proceed.

Commissioner Helvering. For the time being, it is sufficient simply to call the attention of the committee to a typical advertisement of the kind which is sent to taxpayers all over the country. Through these channels he hears about the skill of the rich in avoiding taxes and he sees no reason why he should not take advantage of some of these ingenious plans. The random example which we now hand you for admission in evidence, if you so desire, is headed, "Forty-Seven Ways to Save Taxes."

You will note that item 22 reads: "How tax on personal holding companies can be avoided."

The spreading of such tax schemes not only puts the Government at a serious disadvantage, but also is often disastrous to the small taxpayer. We have instance after instance of taxpayers who incurred penalties, interest, and expense of litigation which they could ill afford, because they listened to the advice of some of these so-called tax experts. The cases we present are those of large taxpayers who have been led into putting themselves into a most unfortunate position.
I would like to impress on the committee this fact: That there is only one way in which the Bureau's administrative problems, which are due both to actual litigation and constantly threatened litigation can be solved—that is, by constant revision and clarification of law. The contest between the Bureau and the litigious taxpayer and quack tax-avoidance experts results in the invention of tax-avoidance schemes faster than we can keep up with them. Courts cannot act rapidly enough to clarify the situation. Most of the cases which clog up the administrative machinery in the Bureau are finally won by the Government, but final victory is no relief from the expenses of running down the use of these tax-avoidance devices, coupled with endless conferences and dispute with taxpayers and the expense and trouble of years of litigation. Only constant clarification of the law by Congress can solve the problem.

Senator Harrison. Without objection the committee will adjourn until 10 o'clock Tuesday morning, June 29.

(Whereupon, at 11:50 a. m., June 24, the hearing was adjourned until 10 o'clock Tuesday morning, June 29, 1937.)
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