RAPID AMORTIZATION OF EMERGENCY FACILITIES

HEARINGS

BEFORE THE

COMMITTEE ON FINANCE

UNITED STATES SENATE

EIGHTY-FIFTH CONGRESS

FIRST SESSION

ON

S. 1795

A BILL TO AMEND SECTION 168 OF THE INTERNAL REVENUE CODE OF 1954, SO AS TO RESTRICT THE ISSUANCE OF CERTIFICATES FOR RAPID AMORTIZATION OF EMERGENCY FACILITIES TO THOSE FACILITIES PRODUCING NEW DEFENSE ITEMS FOR USE BY THE DEPARTMENT OF DEFENSE OR THE ATOMIC ENERGY COMMISSION IN THE NATIONAL DEFENSE PROGRAM

MAY 7 AND 9, 1957

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CONTENTS

STATEMENTS

ADDITIONAL INFORMATION

RAPID AMORTIZATION OF EMERGENCY FACILITIES

TUESDAY, MAY 7, 1957

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

The committee met, pursuant to call, at 10:15 a. m., in room 312, Senate Office Building, Senator Harry F. Byrd, chairman, presiding.

Present: Senators Byrd, Frear, Anderson, Gore, Martin, Williams, Flanders, and Bennett.

Also present: Colin F. Stam, chief of staff, Joint Committee on Internal Revenue Taxation.

The CHAIRMAN. The committee will come to order. Some other members will be in shortly.

Senate bill 1795 is under consideration.

(S. 1795 and the reports of the Bureau of the Budget, the Defense Department, and the Treasury Department.

[S. 1795, 85th Cong., 1st sess.]

A BILL To amend section 168 of the Internal Revenue Code of 1954, so as to restrict the issuance of certificates for rapid amortization of emergency facilities to those facilities producing new defense items for use by the Department of Defense or the Atomic Energy Commission in the national defense program

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Emergency Facility Amortization Act of 1957".

SEC. 2. Section 168 (e) of the Internal Revenue Code of 1954 (relating to determination of adjusted basis of emergency facility) is amended—

(a) by striking out "There" in paragraph (1) and inserting in lieu thereof the following: "CERTIFICATION BEFORE EMERGENCY FACILITY AMORTIZATION ACT OF 1957.—In the case of a certificate made on or before the date of the enactment of the Emergency Facility Amortization Act of 1957, there"; and

(b) by striking out paragraph (2) and inserting in lieu thereof the following:

"(2) CERTIFICATIONS AFTER EMERGENCY FACILITY AMORTIZATION ACT OF 1957.—In the case of a certificate made after the date of the enactment of the Emergency Facility Amortization Act of 1957, there shall be included only so much of the amount of the adjusted basis of such facility (computed without regard to this section) as is properly attributable to such construction, reconstruction, erection, installation, or acquisition after December 31, 1949, as the certifying authority designated by the President by Executive order, has certified is to be used—

"(A) to produce new defense items or components of new defense items (as defined in paragraph (4)) during the emergency period, or

"(B) to provide research, developmental, or experimental services during the emergency period for the Department of Defense (or one of the component departments of such Department), or for the Atomic Energy Commission, as a part of the national defense program.

and only such portion of such amount as such authority has certified is attributable to the national defense program. Such certification shall be

under such regulations as may be prescribed from time to time by such certifying authority with the approval of the President. An application for a certificate must be filed at such time and in such manner as may be prescribed by such certifying authority under such regulations but in no event shall such certificate have any effect unless an application therefor is filed before the expiration of 6 months after the beginning of such construction, reconstruction, erection, or installation or the date of such acquisition. For purposes of the preceding sentence, an application which was timely filed under this subsection on or before the date of the enactment of the Emergency Facility Amortization Act of 1957, and which was pending on such date shall be considered to be an application timely filed under this paragraph.

"(3) SEPARATE FACILITIES; SPECIAL RULE.—After the completion or acquisition of any emergency facility with respect to which a certificate under paragraph (1) or (2) has been made, any expenditure (attributable to such facility and to the period after such completion or acquisition) which does not represent construction, reconstruction, erection, installation, or acquisition included in such certificate, but with respect to which a separate certificate is made under paragraph (1) or (2), shall not be applied in adjustment of the basis of such facility, but a separate basis shall be computed therefor pursuant to paragraph (1) or (2), as the case may be, as if it were a new and separate emergency facility.

"(4) DEFINITIONS.—For purposes of paragraph (2)—

"(A) NEW DEFENSE ITEM.—The term 'new defense item' means only an item—

"(i) which is produced, or will be produced, for sale to the Department of Defense (or one of the component departments of such Department), or to the Atomic Energy Commission, for use in the national defense program,

"(ii) for the production of which existing productive facilities are unsuitable because of its newness or of its specialized defense features.

"(B) COMPONENT OF NEW DEFENSE ITEM.—The term 'component of a new defense item' means only an item—

"(i) which is, or will become, a physical part of a new defense item, and

"(ii) for the production of which existing productive facilities are unsuitable because of its newness or of its specialized defense features."

EXECUTIVE OFFICE OF THE PRESIDENT,
BUREAU OF THE BUDGET,
Washington, D. C., May 6, 1957.

HON. HARRY F. BYRD,
Chairman, Committee on Finance, United States Senate,
Senate Office Building, Washington, D. C.

MY DEAR MR. CHAIRMAN: This will acknowledge your letter of April 5, 1957, inviting the Bureau of the Budget to comment on S. 1795, "to amend section 168 of the Internal Revenue Code of 1954, so as to restrict the issuance of certificates for rapid amortization of emergency facilities to those facilities producing new defense items for use by the Department of Defense or the Atomic Energy Commission in the national defense program."

In the report which he is making to your committee on this bill, the Secretary of the Treasury expresses agreement with the statutory limitation of amortization certificates to strict defense purposes, but recommends that the categories for which rapid amortization is permitted be revised to cover:

1. Laboratories, research, and development for direct defense.
2. Production or transportation facilities for direct military and atomic-energy procurement.
3. Special strategic minerals, metals, or gases in short supply for direct military or atomic energy requirements.

The Bureau of the Budget, in general, concurs with the views contained in the report of the Secretary of the Treasury. We recognize, however, that the national interest might conceivably make it advisable to adopt a more liberal policy with an absolute minimum of delay. Therefore, while we would support

the enactment of appropriate statutory restrictions, we recommend that the bill also authorize the President, upon notification to the Congress, to suspend such restrictions temporarily.

Sincerely yours,

PERCIVAL BRUNDAGE, *Director.*

THE SECRETARY OF COMMERCE,
Washington, D. C., May 16, 1957.

HON. HARRY F. BYRD,
Chairman, Committee on Finance,
United States Senate, Washington, D. C.

MY DEAR MR. CHAIRMAN: This letter is in reply to your request dated April 5, 1957, for the views of this Department with respect to S. 1795, a bill to amend section 168 of the Internal Revenue Code of 1954, so as to restrict the issuance of certificates for rapid amortization of emergency facilities to those facilities producing new defense items for use by the Department of Defense or the Atomic Energy Commission in the national defense program.

This bill would amend section 168 of the Internal Revenue Code so as to restrict the application of rapid tax amortization to those facilities producing new defense items, or providing research, developmental, or experimental services, for the Department of Defense or the Atomic Energy Commission. This Department recommends against enactment of S. 1795 in its present form.

The effect of this bill would be to discontinue the granting of certificates of necessity for rapid amortization of emergency facilities unless the facility is to be used (*a*) to produce new defense items or components of new defense items (as defined) during the emergency period, or (*b*) to provide research, developmental or experimental services during the emergency period for the Department of Defense or the Atomic Energy Commission as part of the national defense program. The definition of the term "new defense item" includes only an item (1) which is produced or will be produced for sale to the Department of Defense (or one of its component departments) or to the Atomic Energy Commission and (2) for the production of which existing productive facilities are unsuitable because of their newness or specialized defense features. The term "component of new defense item" means only an item (1) which is or will become a physical part of a new defense item and (2) for the production of which existing productive facilities are unsuitable because of their newness or specialized defense features.

It has been accepted as sound government policy during this and previous emergencies to grant to industry, on a selective basis, rapid amortization of those facilities which are clearly required for the national defense. This is accomplished through the device of establishing an expansion goal for that service or product which after a careful study of defense, defense-supporting, and minimum essential civilian requirements, would not be in sufficient supply to meet those demands under wartime conditions. Certificates of necessity are processed strictly within the terms of that goal. Open expansion goals, which during the Korean buildup numbered over 200 and involved a variety of products and materials, have now been reduced in number to 9 and cover only those products and services directly attributable to national-defense needs in accordance with the policy established by the Director of the Office of Defense Mobilization December 26, 1956, as follows:

"Tax amortization will be granted only to applications directly involving procurement of the Department of Defense and the Atomic Energy Commission or where an expansion goal has been established and publicized because of a clear showing that, under conditions of full mobilization, the military and war-supporting requirements, plus the requiremnts of a rock-bottom civilian economy, would be in excess of the supplies available."

On April 25, 1957, ODM announced that 5 of the 9 open expansion goals are currently undergoing a new review to determine whether they should be continued.

Mobilization studies continually underway in the Office of Industrial Mobilization have indicated certain areas in which expansion goals can be supported under the criteria established by ODM. A recent example was expansion goal No. 229, covering liquid oxygen and nitrogen for defense use.

The national-defense program is proceeding at a high rate of activity, and international tensions seem to foretell the need for a continuation of this rate

of industrial preparedness. The changes in weapons and other military needs and the currently accelerated scientific activity indicate industrial requirements for defense and for research and development facilities which may well result in little or no postemergency market for the output of the particular facility. It is our feeling, therefore, that the incentive of rapid tax amortization for these types of facilities should be continued as a minimum inducement to get industry into those areas having the possibility of little or no postemergency usefulness. Under the exacting criteria set up by the Director of ODM it would appear that the possibility of abuse of this privilege has been eliminated.

The enactment of this bill would not permit the establishment of a goal such as the goal covering liquid oxygen and nitrogen for defense use because of the failure of the item to fall within the framework of the definition section of the proposal. Liquid oxygen, and perhaps other expansion goals currently open or for which a unique or special defense requirement problem may be involved undoubtedly will not meet the criterion of newness or have specialized defense features which do not permit production in existing productive facilities. The current expansion goal No. 224, production facilities for military and atomic energy procurement, which is being administered under the strict criteria set forth by the Director of ODM on March 21, 1957, can be considered substantially similar to the Senate bill. The care with which proposals for new goals are being considered is evidenced by the fact that expansion goal No. 229 is the only industrial goal which was established for a very considerable length of time.

The enactment of the Senate bill with its strict application of the definitions contained therein would not permit the executive branch of the Government to meet military needs in those areas in which direct purchasing by the Department of Defense would not be involved or to produce those products which lack newness. The application of the rigid criteria of the bill would not permit the President or his designee administrative discretion in granting some measure of Government assistance to those vitally important defense needs which have little or no nondefense market or utility, but which do not fall within goal No. 224 or meet the terms of the definition section of the Senate bill.

For these reasons the enactment of S. 1795 which would forbid the use of rapid tax amortization with respect to any but specified classes of facilities would, in the opinion of this Department, have effects detrimental to our defense posture. However, it is our understanding that the Department of Treasury is recommending that the bill be modified to expand somewhat the categories for which rapid amortization would be permitted.

We are also informed that the Bureau of the Budget is recommending that in addition to the amendments proposed by the Secretary of Treasury, the legislation be modified to authorize the President, upon notification to the Congress, to suspend such restriction temporarily.

The Department of Commerce believes that the amendments proposed by the Department of Treasury and the Bureau of the Budget would, in a large measure, overcome the deficiencies in S. 1795, outlined above.

This Department would interpose no objection to the enactment of the legislation if modified as suggested by the Department of Treasury and the Bureau of the Budget.

We have been advised by the Bureau of the Budget that there would be no objection to the submission of this report to your committee.

Sincerely yours,

SINCLAIR WEEKS, *Secretary of Commerce.*

GENERAL COUNSEL OF THE DEPARTMENT OF DEFENSE,
Washington, D. C., May 8, 1957.

Hon. HARRY F. BYRD,
Chairman, Committee on Finance,
United States Senate.

MY DEAR MR. CHAIRMAN: Reference is made to your request for comment on the bill (S. 1795) to amend section 168 of the Internal Revenue Code of 1954, so as to restrict the issuance of certificates for rapid amortization of emergency facilities to those facilities producing new defense items for use by the Department of Defense or the Atomic Energy Commission in the national defense program.

S. 1795 would amend section 168 (e) of the Internal Revenue Code of 1954 to limit future certificates for accelerated tax amortization to facilities which provide research, developmental, or experimental services for the Department of Defense or the Atomic Energy Commission or which produce new defense items or components of new defense items. The bill defines the term, "new defense item" to mean only an item—

"(i) which is produced, or will be produced, for sale to the Department of Defense (or one of the component departments of such Department), or to the Atomic Energy Commission, for use in the national defense program,

"(ii) for the production of which existing productive facilities are unsuitable because of its newness or of its specialized defense features."

Similarly, the term "component of a new defense item" is defined to mean only an item—

"(i) which is, or will become, a physical part of a new defense item, and

"(ii) for the production of which existing productive facilities are unsuitable because of its newness or of its specialized defense features."

In the matter of obtaining defense production, where new or expanded industrial facilities are required, it is the policy of the Department of Defense that its procuring activities exhaust every alternative before obligating Government funds to acquire industrial facilities under a facilities contract. One such alternative is the financing of such facilities through the incentive of accelerated tax amortization. S. 1795 might well be construed to deny the granting of a certificate for new facilities needed to meet expanded requirements for an existing military item or for new facilities to produce a basic industrial material or component needed to support an expanded military requirement. An example is liquid oxygen, where essential war-supporting uses have increased due to technological changes, and military requirements have increased due to the missile program.

Accordingly, it is recommended that the bill be amended to strike out wherever it appears the term "new defense items" and to substitute in place therefor the term "defense item." In addition it is recommended that identical paragraphs (4) (A) (ii) and (4) (B) (ii) on pages 4 and 5 of the bill be amended to read as follows:

"(ii) for the production of which existing facilities are inadequate because of its newness or because of expanded defense requirements."

Subject to the foregoing, the Department of Defense has no objection to S. 1795.

The Bureau of the Budget has advised that there is no objection to the submission of this report to the Congress.

Sincerely yours,

ROBERT DECHERT, *General Counsel.*

THE SECRETARY OF THE TREASURY,
Washington, D. C., May 13, 1957.

Hon. HARRY F. BYRD,
Chairman, Committee on Finance,
United States Senate,
Washington, D. C.

MY DEAR MR. CHAIRMAN: This is in reply to your request for a report on your bill, S. 1795. This would impose a strict statutory limitation on the use of 5-year amortization certificates. Future certifications would be confined to facilities to produce new defense items or components of new defense items or to provide research, development, or experimental services during the emergency periods for Department of Defense or the Atomic Energy Commission, as a part of the national defense program. Such a limitation is, in principle, consistent with the limitations imposed under present administrative policy.

The Treasury Department favors a statutory limitation which would restrict amortization certificates to strict defense purposes. Widespread use of amortization certificates is very costly in terms of revenue during the period when they are effective. Their availability and use in other than strict defense applications will result in dislocation and unfair advantages both as between whole industries and as between individual companies within an industry.

The use of 5-year amortization for some part of the cost of general purpose plants or equipment to stimulate earlier construction of capacity is neither fair nor logical. The margin of excess capacity, deemed to be needed for defense

purposes at any one time, will regularly be absorbed by civilian demands in a growing economy and would have to be regularly reestablished in later years. There would be continuing revenue lags and continuing creation of new competitive problems.

Subject to possible technical changes consistent with the bill's objectives, the Treasury Department strongly supports the general purpose of S. 1795 to limit emergency amortization to strictly defense items.

The Director, Bureau of the Budget, has advised the Treasury Department that there is no objection to the presentation of this report.

Sincerely yours,

G. M. HUMPHREY,
Secretary of the Treasury.

The CHAIRMAN. Mr. Secretary, we are very happy to have you, sir. You may proceed.

STATEMENT OF HON. GEORGE M. HUMPHREY, SECRETARY OF THE TREASURY

Secretary HUMPHREY. Mr. Chairman, I am very glad to appear before the Senate Finance Committee in response to your invitation to testify on your bill, S. 1795. I strongly support the general purpose of this proposed legislation to limit emergency amortization to strictly defense items.

In July 1955, I first expressed publicly before this very committee my growing concern about the emergency amortization program before a subcommittee of the House Committee on Government Operations. I stated that while emergency amortization may have served a useful purpose during the Korean emergency, it was an artificial stimulus of a dangerous type.

From November 1950 to March 20, 1957, almost 22,000 certificates were issued under the 5-year amortization program. The total cost of these projects was almost $39 billion. Almost $23 billion, or about 60 percent, was made eligible for the 5-year writeoff.

Some degree of defense mobilization on a substantial scale may be essential for years to come. But expansion of our major productive facilities should be an integral part of our long-range, natural economic growth. Our basic defense capacity, except for a few very special items, cannot be separated from the broad base of our productive capacity.

Artificial stimulants may well become artificial controls. Because rapid amortization is not applied universally, it could create a competitive imbalance in the sound, vigorous growth of our free economy. It is not the American way.

The revenue lag from certificates issued through 1956 probably exceeds $5 billion during these early years which will be recovered in the years after 1960. But the interest cost to the Government, over the entire period of lag in tax collections, will be roughly $3 billion.

The effects of a broadly applied amortization program go far beyond the effects on Government revenue. First, there is the stimulating effect which can temporarily add to inflation, with the possibility of a lag later. Then when rapid writeoffs are permitted for facilities which will be largely used to supply eventual regular civilian demand, there inevitably will be dislocations and unfair advantages between whole industries—and individual companies within an industry.

Much of the total has been of this type. For example, over 14 percent of the total amortizable cost of facilities through December 28, 1955, was granted to utilities and sanitary services; over 16 percent more went to railroads; and about 20 percent went to primary metal industries. Other whole industries had none.

There are many industries where some percentage of production would be required in the event of war; but where without war our increases population and productivity will require their continued expansion. These are in sharp contrast to limited-purpose defense facilities such as shell loading or specialized aircraft or armament plants.

Five-year amortization may be an alternative to direct Government construction and ownership of limited-purpose facilities since private capital is not likely to go into them. But this is far different than giving rapid writeoff to selected industries for general-purpose plants or equipment in an expanding economy.

There is no fair or logical end to such a program. The margin of excess capacity in such industries at any time will regularly be absorbed by growing civilian demand and have to be regularly reestablished in later years. There would be continuing costs and revenue lags and the creation of new competitive problems.

We are not unaware both of the desirability as well as of the financial problems involved in modernizing and replacing old capital equipment. Nothing is more important than obtaining the capital to increase our productivity and make new and better jobs.

Our high productivity of labor is possible only because of tremendous capital investment—over $10,000 per man in general manufacturing, and over $50,000 in several industries.

Getting funds for the construction of new plants or facilities is a continuing serious problem. High tax rates make it harder to save from current income. They also lessen the incentive and discourage the productive and perhaps risky use of savings.

It is essential to reduce tax rates as rapidly as can be done soundly. But tax reduction for favored groups only postpones the day when general tax reduction can be enjoyed by all the people.

The program, cut back by the executive branch of the Government, now applies only and strictly to limited direct-defense items. I have consistently advocated this and feel sure that the present limitations should be continued.

S. 1795 is in line with this administration's policy in granting emergency amortization certificates. Subject to some possible changes in language consistent with its objectives to be worked out by the technicians, I am glad to support this legislation.

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

Mr. Secretary, as you remember, I wrote to Mr. Arthur Flemming, the Director of the Office of Defense Mobilization, on October 22, 1956, expressing the hope that the policy of granting these rapid writeoff certificates could be deferred until Congress could act.

In the meantime, as you remember, the staff on the Joint Committee on Internal Revenue Taxation made a very exhaustive investigation, a copy of which was sent you, I think. It was made a Senate document.

Mr. Flemming replied and said that—

At a meeting this morning, the Defense Mobilization Board considered the question of the policy which should be followed in the future in the establishment of expansion goals and the granting of rapid tax amortization certificates within these goals.

Consideration of this matter grew out of the requests that had been made for the reestablishment of new steel expansion groups.

It was determined that no final decision would be made on the policy to be followed until the matter has been discussed at the Cabinet level. After this discussion has taken place, a decision will be made and announced on the policy to be followed and on the relationship of the decision to the request for new steel expansion goals.

I received no further communication from Mr. Flemming. In fact, I was under the impression that this was to be deferred until Congress could act.

He sent me at that time, last October, a list of pending applications which totaled, I think, about $4 billion. Do you recall whether the Cabinet considered this matter and what action was taken?

Secretary HUMPHREY. I don't, Senator, but I do very distinctly recall that these goals were reduced from a large number down to 20 or 30, I guess 30 or 40 to start with and then down to 20 or so, and then finally down to—I don't recall exactly, but I'll say it was—12 or 13, something of that kind, and they were gradually closed off over this period from when we first started talking about this, which was—I had that date right here—July 1955.

From July 1955 on we just kept pushing these down by Executive order and by action in the ODM, eliminating goals where these were available until we got them down to a very small number.

I think that is where they were when you had your letter from Mr. Flemming. I assume that what you have in mind is this last authorization that was issued just a few days ago, and frankly I read about this myself for the first time in the newspaper.

I have since made inquiry as to how that occurred. I think Mr. Gray can explain to you just what he had in mind and just what the circumstances were.

There were special circumstances, as I understand it, affecting that particular item.

The CHAIRMAN. Mr. Gray was unable to be here today but we will have him as a witness.

Secretary HUMPHREY. Yes.

The CHAIRMAN. This resolution of the Defense Mobilization Board was passed on September 21, 1956.

Secretary HUMPHREY. That was last September.

The CHAIRMAN. Yes; Mr. Flemming said this was going to be reviewed by the Cabinet and some definite policy adopted.

I received no further communication from him, and I was under the impression that only those very directly connected with the defense program would be approved, and I was shocked when I was told and saw in the newspaper that the Idaho Power Co. had been granted a rapid amortization of $65 million.

Secretary HUMPHREY. You are entirely correct in your general understanding. That was the understanding and that was the basis on which they were operating.

On this particular thing, Mr. Gray had some special circumstances that he can explain to you.

As I say, I read it for the first time in the newspaper.

The CHAIRMAN. It seems to me there is no justification whatever for a power utility to get a rapid tax depreciation. They are guaranteed profits and, secondly, in this instance the construction had already started. It had been going on for 6 months and, therefore, they were able to go ahead without the understanding that they would get a rapid depreciation writeoff.

Secretary HUMPHREY. He has it very definitely in mind, and I think it would probably be better for him to give you the explanation himself than for me to try to do it.

The CHAIRMAN. Mr. Gray came to see me and we had quite a long talk, and I won't quote him now because I think in fairness to him he should be permitted to testify.

I am also somewhat concerned by the fact that since the peace was declared in 1953 6,000 certificates of necessity were issued covering investments of $18 billion and tax writeoffs of $7 billion.

That is since the end of the Korean war.

Secretary HUMPHREY. Mr. Chairman, as I have indicated in my statement, this went right along until July of 1955. In July of 1955 we began shutting it down very rapidly. That was when the change in policy was first adopted and it took hold very rapidly from then on.

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

Any questions?

Senator MARTIN. I haven't any questions to ask, Mr. Chairman. I am fully in accord with what you have stated and the statement of the Secretary.

I was surprised that the cost in interest would be $3 billion.

Secretary HUMPHREY. I was surprised myself, Senator. We have had it gone over very carefully and I think it is a reasonably accurate estimate, a reasonably illustrative estimate, I will put it that way.

It has to be estimated you know. You can't measure it exactly. But it is reasonably illustrative, it is not deceptive, of what is involved.

The CHAIRMAN. Have you got a breakdown, Mr. Secretary, on the interest involved in the 6,000 certificates, the tax writeoffs of $7 billion?

Secretary HUMPHREY. As to the different dates?

The CHAIRMAN. No. The total interest, as I understand your statement, $3 billion included all of it.

Secretary HUMPHREY. That is correct.

The CHAIRMAN. 6,000 of the 22,000 were tax writeoffs after the end of the Korean war?

Secretary HUMPHREY. We have no breakdown on it.

The CHAIRMAN. Could you furnish the committee with an estimate?

Secretary HUMPHREY. I don't know that it would be possible. What happens, you have these things in process, and if you take filing date you would have one thing, if you take process dates you would have another thing.

There is really no very effective date until you take the granting date for the whole business.

The CHAIRMAN. If you take the report of the Joint Committee on Internal Revenue taxation staff, it was $7 billion. That was the

amount of writeoffs. You can figure it on that basis. I don't mean to go into each individual item but just a rough figure.

If this report is correct, and the staff is usually correct, the writeoffs covered investment of $13 billion and the tax writeoffs were $7 billion. That is after the end of the Korean war.

Secretary HUMPHREY. That is right. I think you might get at it probably reasonably accurately by taking relative amounts in the percentage of the interest but we will check and see what we can do.

The CHAIRMAN. What are the total writeoffs, $23 billion?

Secretary HUMPHREY. Total costs were $39 billion, almost $23 billion of which, 60 percent, is what was deferred. We would have to check to see if the ones you refer to had about the same percentage.

The CHAIRMAN. Let us assume——

Secretary HUMPHREY. If they had the same percentage of amortization, then you could, I think, get very close and it would be fairly illustrative to take the same proportion of the total.

The CHAIRMAN. I only want a rough figure and not to deal with each individual item, but this $23 billion, I assume, compares to the $7 billion referred to in the report?

Secretary HUMPHREY. That would be it.

The CHAIRMAN. Which would indicate about one-third of the writeoffs occurred after the war ended.

Secretary HUMPHREY. That probably wouldn't be too far off.

The CHAIRMAN. I am more concerned about that than I am on those writeoffs that occurred during time of war. There was some justification for that.

If that is correct then, one-third of the $3 billion loss on interest would come on those projects that were given writeoffs after the war ended.

Secretary HUMPHREY. We will check that to see how close it is, but I think you will find that isn't unduly out of line.

The CHAIRMAN. Thank you very much.

Senator Frear.

Senator FREAR. Mr. Secretary, in the third paragraph of your statement, 22,000 certificates were issued and 60 percent were made eligible.

Do you mean after a certificate has been issued, they really are not subject to the rapid amortization, only 60 percent of them?

Secretary HUMPHREY. No. What you do, Senator, is this: If I have a project that costs me a thousand dollars, then they can give me a rapid amortization on some proportion of that.

Senator FREAR. It is 60 percent of the project.

Secretary HUMPHREY. And they would say $600 of that thousand is subject to rapid amortization and the $400 takes the regular rate.

Senator FREAR. Yes; I misunderstood. I think it was 60 percent of the projects.

Secretary HUMPHREY. They vary that. Their practice was to vary the percentage that was subject to rapid amortization by the degree of necessity and various other things they took into account, and they might get as high as 90 percent or they might get down to 50 percent.

Senator FREAR. Yes, sir; I think I understand it now. It is each project.

Secretary HUMPHREY. That is right, it is a percentage of the total which is subject to the amortization.

Senator FREAR. Thank you.

The CHAIRMAN. Senator Bennett.

Senator BENNETT. No questions.

The CHAIRMAN. Senator Anderson.

Senator ANDERSON. Do I understand that you are not familiar with the defense so-called of the Hells Canyon rapid amortization that is to be made by Mr. Gray?

Secretary HUMPHREY. That is correct.

Senator ANDERSON. Could you apply the general principles of your statement to the general principles behind that defense? For example, you say in your statement:

> Our basic defense capacity, except for a few very special items, cannot be separated from the broad base of our productive capacity.

There would be no reason why we shouldn't just separate the Hells Canyon situation from that of the Snake River generally; is there? Is there anything in the vicinity of the Snake River that makes it especially adapted to separate and split off from the rest of our general economy?

Secretary HUMPHREY. Senator, it is a little difficult to discuss that. As the chairman says, in fairness to Mr. Gray, he really ought to make his own explanation of how it came about.

I will say this in answer to your question: That except for special circumstances with respect to it, it would not be available at the present time under our general policy.

Senator ANDERSON. I was only trying to draw on your very fine and broad business experience, Mr. Secretary, to see what there might be in the Snake River that made it so attractive.

Secretary HUMPHREY. You see the difficulty is that when you have a program going on, you have great difficulty in curtailing it fairly because you already have certificates and you are upsetting competitive conditions and that is one of my principal objections to the whole program, that it causes dislocations and unfairness as between competitors depending on the dates when applications are made and when building is done.

Senator ANDERSON. I have been trying to find Mr. Gray's statement. We will have it undoubtedly when he gets here.

Secretary HUMPHREY. That is right.

Senator ANDERSON. He points out undoubtedly that there was no justification for a Hells Canyon tax writeoff except that somebody else got it. I don't know his exact words.

Secretary HUMPHREY. Even that, Senator, in fairness in the administration of a program is something that is right to take into account.

Senator ANDERSON. Why?

Secretary HUMPHREY. That is one of the basic reasons why I object to this program. It is a program that applies to some and not to all, and I think that is one of the difficulties with it.

Senator ANDERSON. As a general program just because one utility had gotten an unfair and bad writeoff, is there any reason why another utility should get the writeoff?

Secretary HUMPHREY. Wait a minute, I don't think it is quite right to say that it is unfair and bad. This was a law that was passed and a great deal of development was done under it.

You and I might have some different ideas as to how the original act should have been enacted perhaps, but nevertheless it was the law. It did aid very materially in the development of the defense of this country, and it was applied very broadly. We are talking now about the detail. We are not talking about whether there was a law or not. There was a law.

We are just talking now about the detail of fair operation under it.

Senator ANDERSON. Mr. Secretary, there was a law and it related to things relating to defense. These are just the last hearings on S. 1333. We had a shortened hearing this year trying to economize on the printing bill.

Secretary HUMPHREY. Good.

Senator ANDERSON. But last year we went this far in the holding of hearings in the Senate alone to consider the Hells Canyon bill, and time after time we tried to find out if the proponents of the private utility dams, a series of them, were going to come in and claim amortization on them. Surely that was not part of the program.

But just as soon as the final decision got written by the Federal Power Commission, then it is learned, you remember, that they were going to be for amortization all the time and Mr. Gray granted it without a word.

These had no connection with defense, had no connection so far as I can tell with the need of the company to get the amortization before they could go ahead, because they went ahead in haste to make sure that the Congress didn't pass that high Hells Canyon bill.

Furthermore, there is available in the Snake River some 12 million kilowatts of energy and they are going to take six or eight hundred thousand of them and put them into their dam whereas the high Hells Canyon Dam would have taken a million kilowatts.

The difference between four or five hundred thousand and a million kilowatts of current isn't very great. There is 10 or 11 million kilowatts still left so there was no possibility of connecting this thing to defense.

I am just interested in finding out if there is any way that you see that this can tie back into things you are talking about here.

Secretary HUMPHREY. I think that you will have to talk that part of it over with Mr. Gray because as I say, I read about it in the newspaper.

Senator ANDERSON. I am very happy to do it, Mr. Secretary. I just wanted to be sure that Mr. Gray didn't come in and say this was part of a Cabinet decision that we would continue these things.

You know of no Cabinet decision to continue them, in view of the letter to the chairman?

Secretary HUMPHREY. This particular item was not discussed at a Cabinet meeting; no.

Senator ADERSON. You speak of the modernization and replacing of old capital equipment. The construction of a brandnew dam on the stretches of the Snake River would not by any stretch of the imagination in your business experience come under modernization and replacing of old capital equipment, would it?

Secretary HUMPHREY. Let me say this, Senator: I again am not familiar with the detail of this particular thing, but under this law

as passed, and in the way this law was administered right from the beginning, if there was a locality where there was a power shortage that was required for the production of materials that contributed to our defense effort, it was very proper in the early days that that should have amortization, and a great deal of it was granted.

As a matter of fact, I have the figure right here. A substantial percentage of the total was for exactly that kind of thing, and it was granted right straight along.

I have trouble finding my own figures but here it is: 14 percent of the total was for exactly this sort of thing.

Senator ANDERSON. Fourteen percent of utilities, was it not?

Secretary HUMPHREY. Yes; that is utilities. That is to supply power, and this is a utility to supply power.

Senator ANDERSON. The Secretary of the Interior, for whom I have very great respect as I have for you, as you well know, just issued a statement talking about the fact that the utilities were going to need $90 million in some period in the future to modernize their plants.

I am wondering if they are going to get an amortization bill for all of that?

Secretary HUMPHREY. They are not if I can help it.

Senator ANDERSON. I am glad to hear that, but I think you would join with the able chairman of this committee in saying you may not be able to help it.

The CHAIRMAN. If we pass the pending bill they won't get it.

Senator ANDERSON. I am only trying to point out that in your statement you recognize something I think is important. It says:

> We are not unaware both of the desirability as well as the financial problems involved in modernizing and replacing old capital equipment.

Secretary HUMPHREY. Of course, it applies to new as well as replacement.

Senator ANDERSON. In order to apply it to new, you would have to show there was a power shortage existing in the area, wouldn't you?

Secretary HUMPHREY. That is correct.

Senator ANDERSON. That was holding back defense?

Secretary HUMPHREY. That is right.

Senator ANDERSON. And as long as the representatives of Bonneville Power and the Grand Coulee Dam and others could come in and testify there was not, at that time, a power shortage which could be alleviated only by the dams they rushed into construction, one alternative remained—and the dams would hardly come under your rule of modernization and replacement of old capital equipment.

Then the testimony will come from Mr. Gray?

Secretary HUMPHREY. That is correct, because he is qualified and I am not.

The CHAIRMAN. The Chair would like to announce that Mr. Gray will be heard Thursday morning at 10 o'clock. The Senator from New Mexico seems concerned.

Senator ANDERSON. That is one of the few mornings that I have got to be away.

The CHAIRMAN. Would Friday morning suit you?

Senator ANDERSON. I will talk to the chairman about it.

The CHAIRMAN. Mr. Secretary, we certainly thank you, sir.

Senator ANDERSON. Thank you, sir, very much.

The CHAIRMAN. We are very pleased, indeed, to have you before our committee and hope you will appear here many more times.

The next witness is Mr. Alexander Hudgins.

Mr. Hudgins, will you take a seat, sir? I might state that Mr. Hudgins is a Virginian. He is the executive secretary of the Virginia Association of Electric Cooperatives.

He has been very much concerned about this rapid depreciation problem for a long time. We are very glad to have him before the committee.

You may proceed.

STATEMENT OF ALEXANDER HUDGINS, VIRGINIA ASSOCIATION OF ELECTRIC COOPERATIVES

Mr. HUDGINS. Mr. Chairman and gentlemen, I don't know the procedure that you always require of your witnesses.

The CHAIRMAN. You proceed in your own way, Mr. Hudgins.

Mr. HUDGINS. I prefer, if I may, Mr. Chairman, not to read my statement but to file it with the committee for its study, and to comment on some of the very unusual things that happened in the past few weeks.

The CHAIRMAN. Without objection your complete statement will be printed in the record.

(The prepared statement of Mr. Hudgins is as follows:)

STATEMENT OF ALEXANDER HUDGINS ON S. 1795 BEFORE THE SENATE FINANCE COMMITTEE ON TUESDAY, MAY 7, 1957

Mr. Chairman and members of the committee, my name is Alexander Hudgins. I am executive secretary of the Virginia Association of Electric Cooperatives. This association represents 19 rural electric cooperatives in Virginia, Maryland, and Delaware. In all, these cooperatives have some 150,000 members scattered throughout the 3 States. I am appearing before your committee in support of S. 1795.

I would like to limit my observations on and discussion of the rapid tax amortization program as it affects the electric utility industry. I believe, however, that the observations and suggestions I make will apply in principle to all the industrial categories which have taken advantage of this program.

As you gentlemen know, the "accelerated amortization" program has been with us in one form or another since World War I. To a limited extent during World War II, the Congress permitted industry to accelerate depreciation on defense facilities as an incentive to private expansion of production. Presumably, the logic used in granting such certification was that industry needed an incentive if they were to spend millions in expanding existing plant and equipment when such expansion would not be warranted after hostilities had ceased.

With the outbreak of hostilities in Korea in 1950, the need was again created for rapid expansion of productive facilities for defense purposes. As a means of providing the necessary incentive to industry to expand productive facilities, Congress enacted section 124–A of the Internal Revenue Code, amending the Revenue Code of 1939. This amendment, which was similar in nature and intent to the World War I and II legislation, provided for 5-year amortization, for tax purposes, of emergency facilities. This provision has been extended by reenactment in the Internal Revenue Code of 1954 (sec. 168).

From November 1, 1950, through December 12, 1956, the total number of accelerated amortization certificates issued covers investment valued at $38.2 billion, and provides for rapid amortization of $22.4 billion of this value. Most, if not all, manufacturing and nonmanufacturing industries have participated in this program.

The Office of Defense Mobilization, the administrating agency, has been given authority to issue certificates of necessity authorizing accelerated amortizatio-,

ODM, upon advice of and consultation with the respective delegated agencies, has the responsibility for determining the necessity of various types of facilities to meet defense production goals. Further, ODM, with the advice of delegated agencies, is also responsible for determining what portion of a facility's cost is subject to the special 5-year accelerated writeoff privilege. In the case of the electric utility industry, ODM relies on the Department of the Interior, Defense Electric Power Administration, headed by Assistant Secretary Fred G. Aandahl, as its delegated agency.

This, briefly, is a summary of the procedural machinery set up to expedite the growth of the electric utility industry under section 124–A of the Internal Revenue Code.

Now, let us assume, and it is quite an assumption, that the ODM and the DEPA carry out their function in good faith; estimate accurately what future needs will be; estimate accurately what percent of these future needs will emanate from normal growth; estimate accurately what capacity will be needed; estimate what percentage growth will be needed in addition to normal growth for full or partial mobilization.

What, then, is the effect of granting a private power company a rapid tax amortization certificate?

Rapid tax amortization, as pointed out in the report prepared by the staff of the Joint Committee on Internal Revenue Taxation entitled "A Report on 5-Year Amortization of Emergency Defense Facilities Under Section 168 of the Internal Revenue Code of 1954," "is a form of special Government assistance to private manufacturers, or, bluntly, a subsidy." I would like to illustrate how this subsidy works for a private power company, and also to point out the peculiar fact about the electric utility industry which makes this subsidy so much more lucrative in this industry.

From June 9, 1951, through July 11, 1956, the private sector of the electric utility industry have been issued certificates, under section 124–A of the Internal Revenue Code, permitting accelerated amortization for $3.1 billion worth of plant and equipment. This means that they will be permitted for Federal income-tax purposes to deduct from their gross revenue as expenses the full value of these certificates over a 5-year period—20 percent of the total each year. This is contrasted to the normal average 3 percent depreciation allowed in the electric utility industry for plant and equipment. The private electric utilities therefore will be allowed to retain as net income during the 5-year period the amounts which they otherwise would have had to pay in income taxes on the excess depreciation allowed.

Assuming normal depreciation of 3 percent, the excess depreciation allowed for each of the 5 years is 17 percent. At the end of 5 years the companies will have retained the taxes on 85 percent of the value of the certificates. Therefore, since the present tax rate on the net profits of the private electric utilities is 52 percent, the companies will have an increase in net income, after taxes, amounting to 52 percent of 85 percent of the cost of the facilities.

If we assume a certificate of accelerated amortization of $1 million and a normal depreciation of 3 percent, a company would ordinarily be allowed to deduct as depreciation expense only 3 percent of the $1 million, or $30,000 a year. As a result of granting of an accelerated amortization certificate, however, depreciation expense of $200,000 each year for 5 years. The excess depreciation permitted for each of these years is 17 percent, or $170,000. The tax of $170,000 profits at a rate of 52 percent would be $88,400. The company therefore would have an increase in its net income, over and above the net income it is permitted as a so-called reasonable rate of return, amounting to $88,400 for each of the 5 years.

The peculiar fact I spoke of above is this. The private electric utilities contrary to other private enterprises are, for all practical purposes, guaranteed a rate of return. They operate as a monopoly, and rates can always be adjusted to insure that they receive a "reasonable rate of return." Therefore, the interest-free loan which the Government has made to the private electric utilities through the accelerated amortization program means that they will earn on these deferred taxes, assuming they are only deferred, amounts greater than will be needed to pay any increased taxes in the future, and therefore that will benefit by an amount even greater than the amount of the loan.

It would amount to the same thing if someone were to make a loan to you of a million dollars without interest, and then further provide that repayments should be at the rate of 3 percent of the loan per year. Furthermore, you could then take the million dollars and invest it in absolutely safe securities on which

you would be guaranteed at least 6 percent a year. Obviously, then, you could make the repayments on the loan of $1 million out of the dividends you receive and still have half the dividends left, which you could then reinvest and earn an additional 6 percent. Therefore, at the end of the repayment, 33⅓ years, you would have repaid the loan in full, you would still have left the original amount which was lent you, plus one-half of the earnings for the next 33⅓ years, plus the additional amount you could earn through reinvesting your dividends.

Figured on this basis, the private electric utilities in the United States from June 9, 1951, through July 11, 1956, received interest-free loans amounting to $1.4 billion, which over a period of 33⅓ years would amount to a total estimated subsidy of $4.7 billion.

The enormity of the subsidy being received by the private electric power companies may strike you as fantastic, but let me assure you that we are not biasing the computations, or engaging in spurious reasoning. Ebasco, a subsidy of Electric Bond & Share uses the same procedure in computing the value of accelerated amortization to the private electric utilities.

Taking the suggestion of Ebasco and applying it to a specific instance, we can readily see how lucrative the granting of an accelerated amortization certificate can be. Let me take for illustrative purposes the Roanoke Rapids project owned by the Virginia Electric & Power Co.

The Office of Defense Mobilization granted VEPCO on their Roanoke Rapids project a rapid tax certificate amounting to 65 percent of the cost of the project. The project cost was estimated at $33.1 million. Under the law, VEPCO can depreciate $20,450,000 over a period of 5 years. Therefore, this certification allows for depreciation of $4,302,350 per year for the 5 year period. Let us assume that normal depreciation on this hydro plant averages about 2.5 percent a year. Therefore, excess depreciation per year would amount to $3,764,556 and the "tax savings" for 1 year (52 percent of the excess depreciation allowance) would equal $1,957,569 of a total tax saving for 5 years of $9,787,845.

It is significant to realize that depreciation reserves as far as a utility is concerned (as for any other profit making, taxpaying business) are a cost of doing business, and therefore deductible from gross income. Therefore, by being allowed to accelerate their depreciation, VEPCO is reducing its taxable income. Now, let us assume that after the 5-year amortization period, VEPCO will have to increase its tax payments due to a decrease in their depreciation deductions, and let us also assume that there is no change in the tax laws, VEPCO will still get the benefits of these tax savings or deferrals in the form of an "interest-free loan."

In the utility industry, the rate structure is determined theoretically to result in a reasonable rate of return on a fair valuation of the property. Let us assume a fair rate of return of 6 percent. Then, if we take VEPCO's tax savings of $9,787,845 which in fact become available for investment purposes, and assuming a 6 percent return over the life of the loan compounded annually, we find that VEPCO will receive over the life of the asset a subsidy of $53.7 million—more than one and one-half times the entire estimated cost of the project.

I would like to make one more remark concerning the Virginia Electric & Power Co.'s Roanoke Rapids project. You will recall at the beginning of my statement that I said that it would be quite an assumption to assume that the Office of Defense Mobilization and/or the Defense Electric Power Administration would act in good faith. Rapid tax-amortization certificates, according to the law, are to be issued when the resulting construction will aid in the national defense.

But in the Roanoke Rapids project where a certificate was issued, this obviously was not the case. Please allow me to go into a little detail on this matter, for it is most important.

During the week of August 24, 1953, ODM awarded a rapid tax writeoff certificate to VEPCO for the company's Roanoke Rapids hydroelectric project. However, VEPCO had applied for a license for this project from the FPC as early as October 6, 1948—almost 2 years before the beginning of the Korean war. At this time the company contended that there was a need in the area for the power, obviously a civilian-domestic need, and that the company would begin construction immediately after the issuance of the license.

The actual license for the project was awarded by the FPC on March 17, 1950, still 2 months before the beginning of the Korean war. And, further, the Chief Presiding Examiner, Frank A. Hampton, stated in granting the license that additional generating capacity was then needed to serve the area; that the applicant's system could utilize the capacity and output of the proposed plant;

and that the company would "require no Federal participation or appropriation for its successful completion"; finally that the company "has adequate financial ability to undertake and complete the project proposed in its application * * *."

Eight months later, on November 15, 1950, hearings on this case were reopened and Mr. Hampton issued another decision in which the full Commission concurred. In this decision, issued January 26, 1951, Mr. Hampton stated again that the project would be undertaken by VEPCO "without aid of the Federal Treasury * * *."

With all this obvious evidence proving that the Roanoke Rapids project was planned originally to meet normal civilian growth in demand, ODM went ahead and issued a certificate for rapid tax amortization. Clearly the letter and spirit of the law was violated. It would be interesting to know how many more "Roanoke Rapids incidents" have occurred. We have the same deal with the Idaho Power Co. and its Oxbow and Brownlee projects in the great Hells Canyon. A study of just how many more of these violations of the law would be most interesting and revealing.

Gentlemen, there are other areas of this problem I would like to point out which must be investigated. We all know the original and only purpose of the existing legislation which provided for accelerated amortization was to expedite production essential to the war effort and the national defense. While even its use during wartime might create very serious economic problems, we can still justify such a program in the name of the national defense. However, it is hard to justify such a program under the present peacetime conditions except, at best, in very rare and exceptional cases, and even then the problems that can be created by such a subsidy program may be so serious as to challenge their use.

Some of the more serious problems that could easily be created by the extension of the rapid tax amortization program center around: (1) The creation of unfair competitive situations; (2) damage of existing and newly formed small businesses which cannot take advantage of the rapid tax amortization provisions; (3) the possibility that there may be a false expansion of activities in one or several segments of the economy which could detrimentally distort the entire economic growth of the national economy; and (4) the temporary and possible permanent loss of funds to the United States Treasury. These, to be sure, are not the only problems that could and have arisen, but they are some of the more important ones. I do not feel qualified to comment specifically on any of these points I have listed, but I feel sure subsequent witnesses will.

Mr. Chairman and gentlemen of the committee, I agree with the spirit and purpose of S. 1795. This bill has as its objective the return of "honesty" to the program, rather than permitting the use of "expediency" in future tax amortization certificates.

Not one of us would deprive the agencies of the Government from using every method necessary in the interest of the national defense. And I say it is most regrettable that the present Code 168 has to be changed to better define what "in the interest of national defense" includes. But since that is the case, this bill approaches a reasonable solution to the problem.

It has become necessary that some plan be set up whereby the administering agency for the rapid tax-amortization program does not escape the scrutiny of the Congress, as I believe it has in the past.

Gentlemen, it is the desire of those whom whom I work in the rural electrification program in these three States that the bill be approved by this committee. While we realize that our interest and knowledge lay definitely in the field of electric energy, there are many other fields in which this bill has impact. When it is all wrapped together, the changes which are to be brought about by this bill seem the most logical under the present circumstances, to close loopholes emphasized by acts of expediency.

Thank you for permitting me to appear before your committee, as a representative of small industry, asking that you approve this measure.

The CHAIRMAN. You make such comment as you wish.

Mr. HUDGINS. I am reminded, if I may say, Senator, of the experience—as you know, I have been very much interested in this rapid tax writeoff program.

The CHAIRMAN. I would like to say, Mr. Hudgins has repeatedly discussed the matter with me in the past. He has been very much concerned.

Mr. HUDGINS. I would like to say in my effort to try to get to the bottom of this tax amortization program, that some of my very good friends told me to take it easy and not get so upset, that things could get worse.

I took it easy and it certainly looks like they have gotten worse.

As you know, Senator, I was in your office in July when the first Hells Canyon bill was voted upon, and it was that day, gentlemen, that I called the Senator's attention to this rapid tax writeoff program.

I think he was quite amazed, and he asked that I appear before Mr. Stam's committee and give some of the facts as I saw them in connection with the rapid tax writeoff program.

This I did, and repeatedly I have attempted to call to your attention, and you have listened most attentively, and I think this report that your committee has just issued or issued in December by Mr. Stam, prepared by Mr. Stam, gives the fundamentals of the basis on which this rapid tax writeoff program has been administered.

In my discussion with Mr. Stam, I was very anxious to make it a point that neither I nor any person interested in the rural electrification program would do anything or insist on anything that would hurt the defense program, but we could not help being alarmed by the way this law, as the Secretary has just pointed out, it was a law and still is a law, this law, the way it was being administered.

In my statement I pointed out that the good old-fashioned word "honesty" has, I am afraid, been pushed aside and the modern spelling is expediency.

And so often those who administer our laws are inclined to do what is expedient than what the good old-fashioned word seems to mean to most of us.

Your bill, Mr. Chairman, I think, is designed to put back into this law sufficient controls of the tax amortization program, if it must stay on the books, so that those who administer it will report to Congress what they do in a more effective manner and will be tied down to certain specific objectives rather than to go afield as the Secretary has just pointed out in the Hells Canyon case, that some special circumstances seem to apply in the granting of these tax amortization certificates for Oxbow and Brownlee projects.

You will find in my statement, Mr. Chairman, the details of this type of writeoff.

I need not go into those details, for I am sure most of you are familiar with how the certificates work, but I would call to your attention, Mr. Chairman, that this recent tax amortization certificate issued late last month has so shocked the Rural Electrification people because you, your committee and Congress in general had apparently asked that it be withheld pending this study, has so shocked the Rural Electrification people that we just don't know how to proceed if this kind of action is going to be continued by those officials who are in charge of the rapid tax writeoff program.

It seems to me that this program as set up places the administrative and criteria development in the hands of maybe one of three groups, either the Department of Interior, DEPA, Defense Electric Power Administration, or the Office of Defense Mobilization.

In an effort to try to find out where the responsibility is actually, I am reminded of the magician who has the 3 little cups and the 1 ball and any cup you pick up you just don't seem to find the ball there.

There seems to be a question around as to who has this responsibility. I am sorry I cannot be as charitable to Mr. Gray as the Secretary was. There are some things that I think I should bring to your attention at this point. I hope I may be permitted to be here the day he testifies, but there are some things I think I should bring to your attention at this point about this Oxbow and Brownlee certificates that should get some study prior to his appearance before you.

Just to make sure, Mr. Chairman, that I don't get too far afield from the bill we are speaking of, as Mr. Secretary has pointed out to you, 14 percent of these certificates are in the electric field, a controlled industry, and it looks like the electric field is the one that is going to bring out the points that will help to get this law that you are presenting in your bill passed.

The CHAIRMAN. Mr. Hudgins, just a moment. The 14 percent is the total amortization costs for facilities granted to utilities and sanitary services.

I just wanted to get that clear.

Mr. HUDGINS. Yes, sir; I believe there is a part of that in the sanitary service, sir.

Senator ANDERSON. But a very small part.

Mr. HUDGINS. That is right, sir.

The CHAIRMAN. Still the utilities may be other than power utilities, I imagine, though I am not certain.

Mr. HUDGINS. Well, sir, since you have mentioned that, I stand to be corrected if it is true, but it is amazing to me that one of the greatest utilities in this country, the telephone utilities, have not taken advantage of this law.

It seems to me that if the telephone utilities, which are certainly essential to the defense program, did not find it necessary to take advantage of this law——

The CHAIRMAN. For the purpose of the record, the chairman will endeavor to break that down further as to what kind of utilities and how much of it was sanitary services of the 14 percent.

(The following was later received for the record:)

TREASURY DEPARTMENT,
Washington, D. C., May 10, 1957.

Hon. HARRY F. BYRD,
United States Senate, Washington, D. C.

DEAR SENATOR BYRD: The information you requested on certificates of necessity issued to the "Utilities and sanitary services" industry is given in the enclosed table.

Through the end of December 1956, over 15 percent of the total amortizable cost of facilities was granted to the "utilities and sanitary services" group. Of this amount, 93 percent went to electric utilities and 7 percent to gas utilities. The other utilities represented in the group—telephone, telegraph, and water—received negligible amounts percentagewise.

These data were taken from records available to the public in the Tax Amortization Branch, Office of Defense Mobilization.

Sincerely yours,

DAN THROOP SMITH,
Deputy to the Secretary.

Distribution of outstanding certificates of necessity within the "utilities and sanitary services" group as of Dec. 31, 1956

[Dollar amounts in millions]

	Number of certificates	Cost of facilities	Certified for fast writeoff	
			Amount	Percent of total
Telephone and telegraph	35	$15	$8	(1)
Electric light and power	913	6,652	3,191	93
Gas utilities	132	964	241	7
Electric and gas utilities combined	5	1	(2)	(1)
Water supply	11	11	5	(1)
Total	1,096	7,643	3,445	100

[1] Less than 0.5 percent.
[2] Less than $500,000.

Source: Office of Defense Mobilization.

Mr. HUDGINS. Thank you, sir.

It seems interesting to me, and I am sure to this committee, that the telephone folks have not, apparently, seen fit to make use of benefits of this section 168.

Mr. Chairman, because of the important part that the electric industry plays in this program, I am, of course, as you might guess, confining my remarks to that field.

When I heard of this rapid tax—let me go back for a moment to say that, ever since last July and even before then, you have been following this tax-amortization program, and that is why I happen to be here representing not only the people of Virginia who are interested in the rural electrification program but the people in the entire Nation interested in the rural electrification program.

I have followed this very closely, and I would not be surprised if there is not in the record a great amount of correspondence that has been developed as a result of my visits to your office and the office of Senator Robertson, from Virginia, who is now chairman of the Defense Committee of, I believe, the Appropriations Committee.

I have followed it very closely, and I was quite alarmed when, as you have expressed this morning and we thought in our rural electrification program, I was quite alarmed to find that Mr. Gray had issued these certificates, and as much as it is against my desire to make contact directly with people in the high echelons of the administrative part of the Government, I felt it my responsibility to call Mr. Gray.

I am sorry he is not here today, but I cannot refrain from giving my side of the story, which he may want to comment upon.

I called Mr. Gray from Richmond in connection with these certificates. Mr. Gray told me over the phone that he knew nothing about your correspondence, nor did he know anything about Senator Robertson's correspondence, and that the staff of ODM presented to him the case of the Idaho Power Co., and that, as he put it, "It is evident that I agreed with the staff because I signed the tax-amortization certificates."

Mr. Chairman, I would like to enter in the record a copy of that staff paper, which I happen to have in my possession, which tells

the story of the Idaho Power Co. hydroelectric projects on the Snake River at Oxbow and Brownlee in Idaho and Oregon.

The CHAIRMAN. Without objection, that insertion will be made.

(The paper is as follows:)

STAFF PAPER

IDAHO POWER CO. HYDROELECTRIC PROJECTS ON THE SNAKE RIVER AT OXBOW AND BROWNLEE, OREG. AND IDAHO

I. EXPANSION GOAL NO. 55—ELECTRIC POWER

In 1950 the Defense Electric Power Administration was created in the Department of the Interior to "exercise defense control and expansion functions with respect to the Nation's power industry." Its functions included the "programing of power-supply expansion."

The Defense Electric Power Administration's first major undertaking in cooperation with an Electric Power Advisory Committee appointed by the Administrator of the Defense Production Administration, was a detailed study to determine the probable peak power loads for the years 1951 through 1954 and the generating capacity needed to meet such requirements.

In 1950, after the outbreak of hostilities in Korea, electric power consumption began to increase rapidly, and the peak load in 1950 was 14 percent above the peak of the previous year—by far the largest single-year increase in the history of the industry up to that time. This unprecedented load increase lowered the industry's margin of reserve to 6 percent, considered by the Defense Electric Power Administration to be below that necessary for maintenance and emergency outages of equipment. In December 1941, reserve margins for the country as a whole were 22 percent.

As a result, the Defense Electric Power Administration in 1951 developed a power-expansion program. The objectives of the program were summarized by the Defense Electric Power Administration as follows:

1. To serve the rapidly increasing civilian load without curtailment.
2. To serve the superimposed defense program.
3. To restore an adequate capacity margin for maintenance and emergency outages, and for unscheduled additions to load.

Its study disclosed that the power consumers who planned sharp increases in their requirements were the Atomic Energy Commission and certain industries in the process of major expansion, such as aluminum, steel, chemicals, and various nonferrous metals. The estimated expansion for the Atomic Energy Commission was 1,900,000 kilowatts. For aluminum expansion 1,500,000 kilowatts was needed, of which around 80 percent would be generated by the aluminum industry itself.

As a part of the study, private and public power organizations were asked to report power expansion projected for the years 1950, 1951, and 1952. It was found that, before the outbreak of hostilities in Korea, a 17 million kilowatt expansion program was planned for the 3 years. It was then agreed to by the combined staff of the Defense Electric Power Administration and the Defense Production Administration that a 27 million kilowatt expansion would be needed through 1953. The difference of 10 million kilowatts indicated the increase needed to meet defense requirements and the resulting acceleration of outlays of private capital.

To meet the power demands of defense mobilization and the expanding economy by the end of 1953, a 3-year, 27-million-kilowatt expansion program was considered a minimum by the Defense Electric Power Administration—7 million increase in 1951, 9½ million in 1952, and 10½ million in 1953.

The Defense Electric Power Administration's report dated December 13, 1951, which carried the required expansion through 1954, showed a need for an increase in power facilities of around 30 million kilowatts during 1952, 1953, and 1954 over the anticipated base of 75 million kilowatts at December 31, 1951.

In October 1951, the Defense Production Administrator had appointed the Electric Power Advisory Committee under the chairmanship of Edward W. Morehouse, vice president of the General Public Utilities Corp., to "inquire into the country's requirements for electric power and energy for defense and other purposes."

On December 31, 1951, the Morehouse Committee reported to the Defense Production Administration "the 30 million kilowatts of new capacity now planned by the electric systems of the country to meet these demands (including necessary reserves) is not, in the aggregate, excessive. If anything, the total capacity is too small."

About the same time as the Morehouse Committee was appointed, the Joint Committee on the Congress on Defense Production, headed by Senator Maybank, ordered an investigation of the electric-power program to determine its adequacy to support defense-mobilization needs, and, on January 15, 1952, the Committee reported widespread difficulties regarding allocations of materials for increasing the electric power production capacity.

After careful consideration of the Defense Electric Power Administration and the Morehouse reports, the Defense Production Administration's staff recommended to the Administrator that a goal be set to provide incentive for a 32-million-kilowatt expansion for the 3 years through 1954. This was partially based upon classified information regarding the expansion of the Atomic Energy Commission's plant.

Accordingly, on March 19, 1952, expansion goal No. 55 for electric power was established at 107 million kilowatts by December 31, 1954, an increase of 32 million kilowatts above the December 31, 1951, capacity of 75 million. This action was taken by the Deputy Administrator of the Defense Production Administration for Program and Requirements. The goal called for an expansion of approximately 9 million kilowatts during 1952, 11 million in 1953 and 12 million in 1954.

On August 26, 1952, expansion goal No. 55 was revised to provide for 117 million kilowatts by December 31, 1956, with expansion scheduled as follows:

Year:	*Million kilowatts*
1952	7
1953	10
1954	12
1955	12
1956	1

This revision provided for 42 million kilowatts above the December 31, 1951, capacity of 75 million kilowatts, an expansion of 56 percent in 5 years. This action was also taken by the Deputy Administrator of the Defense Production Administration for Program and Requirements.

From the beginning of the program a major objective was to encourage utilities to install blocks of capacity which would exceed their normal needs, i. e., to build generating capacity in advance of the time required to meet their ordinary load growth patterns, and thus provide a mobilization reserve.

During November of 1953 the electric power program was reviewed by the staff of ODM in conjunction with the staff of the Defense Electric Power Administration. At that time the expansion goal still called for 117 million kilowatts by December 31, 1956. Up to November 1953 certifications for tax amortization under the goal were as follows:

Amount certified	$4, 227, 638, 000
Amount amortized	$1, 902, 150, 000
Capacity in kilowatts	21, 000, 000

The Defense Electric Power Administration reported its belief that the requirements of expansion goal No. 55 as scheduled would be met by the end of 1956 and recommended its closing at that time.

Since the expansion goal covered a period of 3 years in the future—1954, 1955, and 1956—and it was evident that renewed attention should be given to new basic mobilization assumptions and defense requirements resulting therefrom, it was my decision to suspend the goal rather than close it. This action was taken on December 3, 1953, by Defense Mobilization Order VII–6.

After suspension of the goal the staff of ODM worked with the staff of the Interior Department and made a review of the situation. This afforded an opportunity to watch the development of the actual expansion of capacity which was scheduled and certified under the expansion goal prior to its suspension. Agreement was reached with the Department of the Interior on basic assumptions for mobilization readiness and the programing period was extended from the end of 1956 to the end of 1958. This review was completed in early April of 1955. At that time, the capacity for electric power projected to the end of 1958,

taking into account normal growth demand projections and margins for normal operations, amounted to approximately 135 million kilowatts. That projected capacity was not sufficient for mobilization needs. Accordingly, on April 15, 1955, expansion goal No. 55 was reopened and established at 150 million kilowatts by December 31, 1958. The reserve capacity over peak load estimates provided by this full mobilization objective was about 24 percent. This objective was designed to take care of requirements for full mobilization as contrasted with previous efforts to cover only partial mobilization requirements.

On August 11, 1955 expansion goal No. 55 was again suspended under Defense Mobilization Order VII–6, Supplement 1 as part of a general review of all goals. The goal was again reopened on September 29, 1955, with the modification that applications for tax amortization must be filed by December 31, 1955, in order to be eligible for certification. Certifications under the reopened goal are as follows:

Amount certified	$1,198,766,000
Amount amortized	$494,100,000
Capacity in kilowatts	5,990,000

Applications for tax amortization under the electric power goal are subject to the national dispersion policy. Under this policy electric power projects are not eligible for tax amortization unless they are located outside congested urban areas as determined by the Department of Commerce and away from major military installations and key defense industrial facilities as determined by the Department of Defense.

The sole objective of the expansion goal is to encourage the investment of private capital in electric power facilities to increase total capacity by December 31, 1958, to a level sufficient to provide a margin for national defense in the event of mobilization.

II. IDAHO POWER CO. APPLICATIONS

In August 1953 the Idaho Power Co. filed applications TA–26407 and TA–26500 for necessity certificates for two proposed power developments on the Snake River at Oxbow and Brownlee, Oreg.-Idaho. Total cost is estimated at $103,081,970. It has been the practice of the certifying officer to postpone final action on such applications until a license has been issued by the Federal Power Commission.

On August 4, 1955, the Federal Power Commission granted licenses covering the two projects; construction of the Brownlee unit to start within 1 year, and Oxbow within 4 years. After issuance of the licenses by the Federal Power Commission, the applicant requested that final action be taken on the applications. Accordingly, the Department of the Interior was requested to submit its recommendations.

On October 25, 1955, the Department of the Interior recommended to the Office of Defense Mobilization the issuance of necessity certificates on both projects for the following reasons:

"The Oxbow and Brownlee hydro projects of the Idaho Power Co. will contribute to the power supply shortage in the Pacific Northwest. Reserves in the west group are materially lower than what is considered adequate. Under adverse water conditions there are no reserves and the dropping of interruptible loads becomes necesary to met firm load commitments.

"The minimum streamflow of the Columbia and Snake Rivers occur at different times during the year. The reserve water storage at Brownlee and the 230 kilovolt transmission facilities integrating Oxbow with the west group can make a substantial contribution to overcome the indicated deficits in the west group with both direct transfer of power and downstream of storage water from the Brownlee project.

"The Idaho Power Co. has been purchasing capacity from the Utah Power Co. The Utah Power Co. is compelled to withdraw this capacity to Idaho in order to meet their own power requirements.

"The normal load growth and the new power requirements of the Atomic Energy Commission along with the loss of purchased capacity from the Utah Power Co. makes it essential for the Idaho Power Co. to add new generation to their system. This will, in effect, add materially to the capacity needed to meet the requirements of the present defense industries and any new defense loads that might be located in the Pacific Northwest."

In addition to the data contained in the recommendation from the Department of the Interior the following pertinent facts have been established:

(*a*) Both applications were filed within the time limit specified in the goal.

(*b*) Applicant must comply with the provision of the goal that the added capacity to deliver power will be available by December 31, 1958, or the certificate will be invalid.

(*c*) The site of the power development is outside congested urban areas and away from major military installations and key defense industrial facilities.

(*d*) The capacity to be added by these projects fits within the total quantity covered by the goal.

(*e*) Other hydroelectric power developments have been certified in the past when all requirements of the pertinent goal were satisfied.

Accordingly, both applications are certifiable under goal No. 55, electric power.

III. GENERAL OBSERVATION

Opinion No. 264 of the Federal Power Commission issued December 4, 1953, on the matter of "treatment of Federal income taxes as affected by accelerated amortization" contains the following pertinent statement:

"While it is clear to us that Congress, by the enactment of this law, did not intend to make gifts to the customers of the public utilities and natural gas companies which received certificates, it is equally clear that Congress did not intend to provide a temporary fund to these companies which could be diverted to the payment of dividends to their shareholders. Since the possession of necessity certificates is essentially a deferment of tax liability, the accruals for taxes in excess of those actually paid should logically be treated, not as free and unrestricted income, but earmarked to provide for the future of such liability.

"Consequently, we will take all steps necessary to insure that provision is made for meeting the deferred tax liability and the temporary savings produced by the deferral of taxes are not used, directly or indirectly, for the payment of dividends, but are used for the purposes intended; namely, to aid in the construction of the facilities described in the certificate which were deemed by our Government to be necessary to the national defense."

IV. QUESTIONS AND ANSWERS

The following questions have been raised in objection to the issuance of necessity certificates for the two projects:

I. A court suit seeking review of the Federal Power Commission's licensing order makes it doubtful that either of the 2 projects will be constructed within a 5-year period, if at all.

Expansion goal No. 55 requires that projects certified under that goal will be in operation by December 31, 1958. Applications which give no assurance of completion by December 31, 1958 are subject to denial. A condition attached to certificates that are issued may invalidate the certificate if the facilities are not in service by December 31, 1958.

2. The project designs and costs are not known and cannot be presented to ODM with any degree of reliability.

Applications for necessity certificates which are filed with us are based upon estimated costs. Certificates are subject to final revision and amendment when actual costs have been determined. The fact that actual costs are not known by an applicant at the time of filing is no deterrent to the issuance of a necessity certificate.

3. ODM Regulation 1 provides that a facility, to qualify for a necessity certificate, must produce a product required for national defense during the emergency period. These projects were planned to meet normal load growths within its service area.

Expansion goal No. 55 covers power expansion to be undertaken by any Class I utility. Most of the applications filed by such utilities are for the expansion of generatiing capacity, and when favorably recommended by the Department of the Interior as within the purview of the expansion goal, are normally certified by this Office as being in the interest of national defense. To relate the specific contributions of each project to plants which it may supply several years later would be difficult in view of interconnections and the attraction of defense industries to areas of adequate power.

4. You announced on September 23 that you would no longer grant certificates to the steel and aluminum industries. What logic underlies resumption of accelerated amortization for private power and suspension of it for steel and aluminum?

Mobilization readiness requires an overall balance in productive capacity and supply, which must be evaluated individually. There are many industries, necessary for war production, which have been offered no incentive to expand. The review of these three industries, conducted with the aid of the delegate agencies involved and the Defense Mobilization Board, provided the necessary data to determine that the need for expansion in electric power generating capacity is sufficiently urgent to warrant tax amortization as an incentive.

5. If Idaho Power is given 67 percent accelerated amortization on its $103,082,000 expenditure it would result in Federal tax savings of $31,357,000 during the first 5 years of operation of Brownlee and Oxbow which constitutes an interest free loan to Idaho Power.

The company saves interest on deferred tax payments, which amount it might otherwise have to borrow. The Government pays interest on borrowed money to make up for the tax loss. Starting the sixth year the Government gets increased tax revenue because smaller deductions are available to the company and, at the end of the useful life of the facilities, the Government has received the deferred taxes. The net cost to the Government is the difference between the interest it pays on the amount of the "interest free loan" and the interest it saves on the greater tax payments which start with the sixth year.

The CHAIRMAN. It is a seven-page document, dated January 11, 1956. It is too long for us to go into now but I think it is worth your study.

Mr. Gray told me that the staff presented it to him, he approved it and that no one else called it to his attention. It is amazing to me, as I told him, that all this correspondence has been going on that you have pointed out this morning, that you pointed out last Monday a week ago in the Senate, and that we know about for the past 6 months, had not come to his attention through his staff.

Certainly they are the keepers of the record and the ones to have given him this information. I am completely shocked by that kind of administrative ability, and I am sure that his testimony will clear up why the amortization certificates were given.

I might mention, too, Mr. Chairman, that it appears that this certificate or these certificates were signed on the 17th day of April and announced at a press conference on the 24th or the 25th, the 24th, I believe, and that the day before they were announced, Idaho Power Co. got approval from the Federal Power Commission to float a $40 million short-term loan.

I don't know what tax amortization certificate might have effect on credit. I am just not that smart. I am just a country boy up here trying to find out what is going on, trying to find out why these type of certificates are issued and the utilities as 1 segment, who are as you pointed out assured an approximate 6 percent profit on their investment or income, are into the tax amortization program for their own advantage.

Senator ANDERSON. Did you say you didn't see any connection between the granting of the tax amortization and the offering of these $40 million of certificates?

Mr. HUDGINS. Senator, I merely made the statement that I could not understand whether or not there would be a connection.

Senator ANDERSON. Wasn't one to sweeten up the other, or maybe they sweetened each other?

Mr. HUDGINS. Sir, you are saying that.

Senator ANDERSON. I am glad to say it again. Quite obviously, with the Senate Subcommittee on Interior and Reclamation, of which I happen to be chairman, reporting favorably to the full committee a recommendation that the Federal high Hells Canyon Dam be approved, and the full committee subsequently reporting favorably to the Senate, there might have an adverse effect upon these certificates, so they were sweetened by this rapid amortization.

Mr. HUDGINS. I believe those bills were reported out after this.

Senator ANDERSON. Yes, but it was well known that we were going to take that action. We had an agreement that we would meet on a certain day and report them out. I don't know that there is any connection either, but I thought it was awfully strange that they all came together.

Mr. HUDGINS. I think it was probably well known, too, sir, that the tax amortization certificates had been signed, and that to me seems quite strange. It all adds up, Mr. Chairman——

Senator ANDERSON. The Secretary of the Treasury said he didn't know anything about them until he read it in the papers. Quite obviously the people who were going to float the loan heard about it ahead of the Secretary of the Treasury.

Mr. HUDGINS. I think, sir, time will prove that.

Senator ANDERSON. I think so, too.

Mr. HUDGINS. Mr. Chairman, I could go on here for an hour in a discussion of this program. I do not know that I can add too much more to what has already been said.

I believe, sir, that there are probably 2 or 3 items that I would like to call to your attention and then I will be through with my testimony.

I think on the Senate floor you said that you would even like to see this bill that is under discussion here today be made retroactive so that in this particular case the Idaho Power Co. would not enjoy this tremendous interest-free loan.

I don't believe I mentioned how much it is, somewhere in the vicinity of $30 million.

The CHAIRMAN. I said if it was legally possible.

Mr. HUDGINS. Yes, sir.

The CHAIRMAN. We don't intend to do something that is illegal.

Mr. HUDGINS. I do not know whether that is legally possible, Senator, but I do have a suggestion for you, the members of your committee and the great Senate of the United States.

Before you, either this month or early next month, I understand you will have an opportunity to correct the mistake that was made last July and vote again on the High Hells Canyon Dam.

And thank God for such men as Supreme Court Justice Black, who foresaw what was coming and brought about a bond on the Idaho Power Co. to protect the Government in case such a bill were passed, from damages that the Idaho Power Co. might ask of the Government.

I think, Mr. Chairman, that passage of that bill, when it does get on the floor, will be a step in the direction of correcting this very small error in a very big program.

I would conclude my remarks to you by saying, Mr. Chairman, that apparently our program is right and the people in this particular effort certainly appear to have God on their side.

I think you know that the Schoellkopf Curve fell into Niagara, the utility plant up there, and it has helped us in our effort to get power through the Niagara program.

Just recently the floods have come down the Snake River. All of the cofferdams that the Idaho Power Co. had already built have been wiped out and if they do not continue with their program they would have very little damage against the Government if this Hells Canyon bill is passed.

And I say to you, Senator, in your investigation and your study, I think the White House will be unable to stand up and support any such efforts as are being made by the ODM to continue those parts of the rapid tax writeoff program that are so far afield from what defense stands for that your bill would easily be passed in the Senate and become a part of the law to restore that good old-fashioned honesty to the administration of the laws that you pass, and destroy the efforts that are being made in doing these things in an expedient way.

I thank you, Mr. Chairman, for having the privilege of appearing before you.

The CHAIRMAN. Any questions, Senator Anderson?

Senator ANDERSON. I merely wanted to refer to the testimony given before the Senate Interior Committee in which the representative of Morris Knudsen, who had done considerable work in engineering for private dams, was testifying, page 694 of the hearings on S. 1333, in April and May of 1955. He discussed in great detail—I think Mr. Williams was vice president—the work which they had done. He said, "We offer to build the 3 dams for $133 million," and he gave a schedule of them and their uses and told how power from Oxbow could be on the line in 12 months, Brownlee in 24 months, and lower Hells Canyon in a short time thereafter.

Would that have sounded, if you had heard the testimony, as if this was a defense emergency in the Pacific Northwest?

Mr. HUDGINS. No, sir.

Senator ANDERSON. Furthermore, he pointed out that this was intended to benefit the upstream development of the river and not the downstream use of the power.

The downstream use of it refers to those plants out in Portland and Seattle and through the States of Washington and Oregon where the aircraft industry is largely centered, and he stated:

> It is my firm conviction that money spent by the Government for the storage of water should be used for these upstream developments where the floods are caused and where its benefits will be greater.

Would you understand that flood-control upstream would have contributed extra power to the development of the aircraft industry downstream?

Mr. HUDGINS. I shouldn't think so.

Senator ANDERSON. I would think it would not be the purpose at all to use upstream storage if they were trying to develop current downstream. I am merely interested in the defense aspect of it.

The whole testimony here indicates that they would build them for the Idaho Power Co. but that they were not in the slightest interested in the larger development that might have contributed to defense, which makes it difficult for me to understand why it would be done with that as a justification.

Mr. HUDGINS. That type of testimony seems to run through many of these certificates apparently.

Senator ANDERSON. Yes. I am very glad that you are here today to express your surprise at the granting of the certificates.

The CHAIRMAN. Any further questions?

Thank you very much, Mr. Hudgins.

The next witness is Mr. Stuart G. Tipton of the Air Transportation Association of America.

Proceed, Mr. Tipton.

STATEMENT OF STUART G. TIPTON, PRESIDENT, AIR TRANSPORT ASSOCIATION OF AMERICA, ACCOMPANIED BY J. D. DURAND, ASSISTANT GENERAL COUNSEL

Mr. TIPTON. Good morning, Mr. Chairman.

I will read a brief, prepared statement, Mr. Chairman.

Mr. Chairman and members of the committee, my name is Stuart G. Tipton. I am president of the Air Transport Association of America, which is composed of substantially all of the scheduled airlinces of the United States. On behalf of the airline industry I welcome the opportunity to testify before this committee on S. 1795.

The airline industry is opposed to S. 1795 in its present form, since we feel that it would impair the ability of the airlines to meet their national defense obligations to the Nation and to the Government planning authorities concerned. We urge that the bill be amended in the manner I shall indicate in a moment.

The principal purpose of S. 1795 is to limit so-called rapid tax writeoff, authorized by section 168 of the Internal Revenue Code, to facilities used to produce "new defense items," or to provide research, developmental, or experimental services for the Department of Defense or the Atomic Energy Commission, for use in the national defense program, and for the production of which existing productive facilities are unsuitable.

The effect of the bill, as it relates to the airline industry, would be to render ineligible for rapid tax writeoff the new multiengine, long-range jet transport aircraft, which the airlines are planning to acquire and on which the Department of Defense has placed the highest premium for supporting airlift. We believe that this would be a most unwise result.

From the inception of the rapid tax writeoff program, transport aircraft have been recognized to be "emergency facilities" under section 168. This is due to the fact that, with respect to this country's mobilization planning, the airline industry has a unique relationship with the Department of Defense and with the Defense Air Transportation Administration (DATA) of the Department of Commerce.

DATA is the agency which the President, by Executive order, has directed to handle this country's mobilization planning insofar as air transportation is concerned.

As a result of mobilization plans formulated by DATA, working closely with the Department of Defense, on D-day not one aircraft will be left to be operated by an airline on a "business as usual" basis.

Every aircraft in the airline fleet, now over 1,500 multiengine airplanes, will either be assigned to the Military Establishment for oper-

ation under the direct control of the Military Air Transport Service (MATS) or will be placed in a pool and will be assigned by the Civil Aeronautics Board to the airlines and the routes most necessary to the war effort.

The aircraft assigned to MATS, the Civil Reserve Air Fleet—or CRAF—will be the cream of the airline fleet—large, 4-engine, long-range transports. The present requirements of the military on the airlines for the CRAF fleet are for slightly in excess of 300 4-engine aircraft.

This figure can be expected to increase as mobilization plans are revised. For example, the present requirements indicate that the 1959 CRAF will be 48 percent larger than the 1955 CRAF.

Specific aircraft, identified by serial numbers, are assigned to CRAF. Some of them have already been modified to military specifications. Others are in process of being modified. They, and the crews to operate them, will be ready for military duty on 48 hours' notice.

Under the CRAF program the aircraft are purchased by the airlines, and are maintained in a state of readiness, at airline expense.

Crews for the operation of the aircraft, as well as the critical maintenance personnel, and the large physical facilities for major overhaul and maintenance, are provided entirely at airline expense.

The aircraft presently assigned to CRAF would have cost the Government $400 million, plus an annual outlay of $300 million for crew training, maintenance, and supporting facilities. All of these costs are now being borne by the airlines.

On D-day those airline aircraft which are not directly assigned to the military will be placed in a pool and used to operate the war air service pattern (WASP).

These aircraft will be assigned by the Civil Aeronautics Board to the carriers and those routes most necessary to the war effort.

All flight frequencies and points served will be directly controlled by the Civil Aeronautics Board. The entire movement of passengers and cargo over the war air service pattern will be strictly controlled by an air-priorities system.

Only priority traffic will be moved. The Secretaries of Defense and Commerce, with the approval of the Director of ODM, have established an Air Priorities Board combining the priorities authority of the Secretary of Defense over military aircraft, and of the Secretary of Commerce over civil aircraft.

This combined system will be administered in wartime by the Department of Defense. The country is well assured, therefore, that priorities will be determined and administered in accordance with the requirements of a nation at war.

There will be no "business as usual" traffic. The War Air Service Pattern is expected to consist largely of purely military traffic—military personnel in uniform and military shipments.

In the last war, for example, this type of traffic amounted to approximately half of the air priorities moved on the civil system.

In determining the allocations to CRAF, only the barest minimum number of aircraft has been left for these vital WASP operations.

As a result of our work with DATA and the Department of Defense we know that when the airline fleet now in operation and the new

aircraft on order are balanced against the CRAF and the WASP requirements, there is, and will continue to be for the years for which requirements have been projected, a substantial deficit of transport aircraft. As Secretary of Defense Wilson stated to the House Committee on Appropriations:

> A recent study of the essential civil air requirements indicates a sizable deficit will exist in available aircraft capacity. When military requirements are considered, that deficit becomes even greater * * * (Department of Defense Appropriations for 1957, p. 162).

In considering Secretary Wilson's statement, several facts should be borne in mind. In the first place, the military requirements on the airlines are based on the assumption that all airline aircraft will be operational on D-day.

This is not a sound assumption, since when hostilities start, a considerable number of such aircraft will be knocked out of service by enemy action.

In 1956, the airlines participated in a test known as Operation Alert—1956, designated to show the damage to their facilities which would be caused by the bombing pattern assumed for that exercise.

The exercise was limited to the continental United States and Territories, and did not take into account the number of aircraft which would be lost overseas.

The number of aircraft destroyed or damaged in the area covered by the exercise amounted to approximately 12 percent of the airline fleet. As nuclear weapons become more destructive this figure can be expected to increase.

Secondly, it must be borne in mind that with the exception of jet tankers the Department of Defense has no plans for acquiring and operating a fleet of jet transports.

They are relying solely on the airlines for that type of lift. Moreover, as you may have seen recently in the press, the jet-tanker program is being deferred to give added priority to combat-type aircraft.

The fullest possible expansion of the civil air fleet through the acquisition and operation of aircraft by the airlines is the most economical and efficient way for the Federal Government to fill the present and future airlift deficit.

Rapid tax writeoff has been, and will continue to be vital to the airline industry in achieving its fullest expansion.

The presidents of our member airlines have advised me that tax amortization is a factor of primary importance in securing the financing needed to purchase new aircraft.

It enables the airline and its lender to determine in advance the amount of writeoff which will be allowed for tax purposes.

Moreover, by providing a tax deferral, it helps cushion the impact on cash reserves which would otherwise arise if the airline had to meet the heavy costs of expansion and heavy tax payments at the same time.

When tax amortization is compared with the two most widely used methods of flexible depreciation authorized by the new Internal Revenue Code, the results show that tax amortization produces a somewhat larger tax in the first 2 years of depreciable life but results in a substantial deferral during the third, fourth, and fifth years.

The average net tax deferral for each of the 5 years involved is $16,300 per $1 million of investment when tax amortization is com-

pared with depreciation computed on the sum-of-the-digits method, and $15,400 per $1 million of investment when compared with depreciation computed on the declining-balance method.

Pending airline applications for tax amortization, which cover substantially all of the jet aircraft on order by the airlines, amount to approximately $1.4 billion, with delivery dates up to 1961.

When the total tax deferral involved is averaged over the various 5-year periods affected, it results in an estimated average net yearly tax deferral of approximately $23 million.

This is not, of course, tax forgiveness since the amounts deferred will be repaid to the United States Treasury in the sixth and seventh years, assuming no decrease in the tax rate.

If there is a rate increase, the Federal Government will collect not only the amount of the deferral, but also the excess amount produced by the increased rate.

Senator ANDERSON. Have you any figures on interest here? You are talking solely about the amount that is not paid at the particular time. You are not talking about interest that is saved, are you?

Mr. TIPTON. Interest that the airlines save?

Senator ANDERSON. Yes.

Mr. TIPTON. We have computed it in this way, and it has to be rough because as I just indicated we pay more taxes in the first 2 years and less taxes in the last 3 years, but our estimate is, and I think this is on the high side as far as the Government is concerned, that assuming that the Government were to have to borrow the $23 million, which is the average figure, the cost to the Government would be just short of $700,000 annually.

Senator ANDERSON. At what rate are you calculating?

Mr. TIPTON. Three percent.

The CHAIRMAN. The last bond was sold at 3⅝.

Senator ANDERSON. That would increase the $700,000 figure by 14 percent.

Senator BENNETT. Make it $800,000.

Mr. TIPTON. I would make it $800,000.

Senator ANDERSON. What was the statement, under the amortization program you are required to pay more taxes the first 2 years and less the next 3? Will you explain that?

Mr. TIPTON. I think Mr. Durand, the assistant general counsel of the ATA can explain that clearer and quicker than I can.

The CHAIRMAN. Identify yourself for the record, Mr. Durand.

Mr. DURAND. J. D. Durand, assistant general counsel, Air Transport Association.

Senator Anderson, we made a study showing a comparison between the rapid tax writeoff and depreciation on aircraft under the sum-of-the-digits method, one of the new methods authorized by the Internal Revenue Code and a comparison also between rapid tax writeoff and the so-called declining balance method of depreciation, and we found that comparing those two, if an airline used the sum-of-the-digits method, which is a new flexible method of depreciation, actually he took more depreciatin in the first year and therefore got a lower tax if he used that method than if the airline used rapid tax writeoff, but in the second, third, fourth, and fifth years, rapid tax writeoff produced a lower tax; in other words, a tax deferral which would have to be repaid in the sixth and seventh years.

When we compared the rapid tax writeoff, that is the 5-year write-off of aircraft, with the declining balance method of depreciation of aircraft, there was a larger tax in the first year, a somewhat larger tax in the second year produced by rapid tax writeoff, but in the third, fourth, and fifth years there were substantial amounts of tax deferral.

The CHAIRMAN. What is the normal depreciation?

Mr. DURAND. Generally speaking, Senator, it is 7 years with a 15-percent residual value.

Senator ANDERSON. Seven years on an airplane?

Mr. DURAND. Yes, sir.

Senator ANDERSON. How many DC–3's have been written off, all of them?

Mr. DURAND. I think the DC–3 fleet is substantially depreciated.

Senator ANDERSON. And DC–6's? They are pretty well gone by now.

Mr. TIPTON. The DC–6's are not written off yet.

Senator ANDERSON. They are still in the skies and in pretty good shape?

Mr. TIPTON. The DC–3—I am not surprised at all that you are referring to the DC–3 because that is a most unusual airplane.

Senator ANDERSON. It is still flying, isn't it?

Mr. TIPTON. That is right. There are very few of them on the trunk lines of the United States but the local service lines are almost entirely equipped with DC–3's.

Senator ANDERSON. And they are worth more now than they were 4 or 5 years ago?

Mr. TIPTON. Your statement would have been correct a few months ago. The market has slipped a little but not much. That is a very unusual situation which has resulted in passing that airplane down from one operation to another.

Senator ANDERSON. And as rapidly as an airline gets rid of them there is an oil executive ready to take it?

Mr. TIPTON. There is an oil executive ready to buy it and turn it into an executive transport.

The CHAIRMAN. The difference is 2 years between 7 years and 5 years.

Mr. TIPTON. That is right.

The CHAIRMAN. Where are you hurt much on that?

Senator ANDERSON. That was one of my questions, Mr. Chairman. A man comes in and claims he is going to be hit. He has to show ordinarily where he is going to be financially damaged and the extend of the financial damage.

If you are writing them off in 7 years anyhow, how are you so financially damaged?

Mr. TIPTON. As I said, the only way that we can explain that with any degree of clarity is to average the extent of tax deferral, because that is the way we are helped by getting it and hurt by not getting it, and in our case and based upon the fleet of airplanes that we are talking about, which is about 400 airplanes of a value of about $1.4 billion, we get an average tax deferral of $22 million.

The CHAIRMAN. But as a matter of fact under the present law you would get 30 percent off the first year instead of 20; isn't that right?

Mr. DURAND. Yes, sir.

The CHAIRMAN. In other words you double what you now get under the existing law?

Mr. DURAND. That is true in the first year, Senator.

The CHAIRMAN. That declines as it goes on, it is true, but I just cannot see where the airplane industry is hurt at all by taking away the 5-year amortization when you take it off for 7 years now.

As for the first 2 or 3 years, you would actually get a gain in taking off depreciation.

Mr. DURAND. For the first year, Senator, under the sum of the digits and for the first 2 years under the declining balance.

The CHAIRMAN. You have got to select either the digit plan or this other one.

Mr. DURAND. Yes, sir.

The CHAIRMAN. It seems to me you are arguing against yourself to some extent on the rapid writeoff.

Mr. TIPTON. You have to look at it over the whole 7-year period. Here is the reason we are hurt and this is the problem that causes us to come before your committee.

The net worth of the airlines' system right now is about $900 million. Between now and 1961 and 1962 we are committed to come up for new capital acquisitions, equipment and everything that goes with them, of between $2½ billion and $3 billion.

It presents us with a financing problem that is tremendous and about which all airline executives are concerned.

Now under those circumstances what appears to be a relatively small figure begins to loom large. When you have as hard a financing problem as the air-transport industry has, their $22 million gets to be important.

Senator ANDERSON. That is the question. Are you concerned about national defense or is it your own financial budgeting?

Mr. TIPTON. The concern about it is defense because any——

Senator ANDERSON. It sounds like it is your own financial budgeting.

Mr. TIPTON. As I described here, we buy these airplanes and we have the financial obligation of paying for them, but when we get them the Government takes the serial number down and says that "you will deliver that airplane to us on 48 hours' notice with 3½ crews when we call for it in time of emergency."

We are buying airplanes for the Defense Department. We are eliminating the necessity for them to buy a jet transport of their own.

Senator ANDERSON. I am certainly not going to go into the story of how the next war if fought is going to be fought, but are you of the opinion now that if we get into a nuclear war, an allout shooting nuclear war, that the Government is going to be interested in DC–6's, DC–7's, DC–3's, or anything else, after the first 3 days?

Mr. TIPTON. In our computations and in the Government computations, they have shown a very definite, almost an individual interest in any 4-engine airplane at the moment, with a heavy emphasis on improving the quality of our fleet as we go along—for example, we have got a lot of DC–4's in the fleet now. They are in the CRAF. They are assigned to the military on call.

As these jets come in on top of the heap, they are deeply interested in improving the fleet for exactly the reason you mentioned.

A DC–4 now is better than no airplane at all, but it does not compare with the high-capacity, high-speed jet transport which we have been hoping to get rapid writeoff certificates on.

As more modern airplanes come in on top of the CRAF fleet the less modern airplanes go out the bottom.

The CHAIRMAN. Of course, your proposal would open up the whole matter nearly as much as the present bill. It seems to me that you are going to have less cause to complain than most others. I can understand building at only 3 percent makes quite a difference to them but as long as you are now taking off 15 percent a year and these planes are used longer than that time, then you take your repairs off in toto; isn't that true?

Mr. TIPTON. Yes.

The CHAIRMAN. Repairs, rebuilding, and so forth, you can take it off your income tax as an expense.

Your recommendation practically puts it back to where it is. You want the law continued as it is, notwithstanding the fact that we have been at peace since 1953; is that right?

Mr. TIPTON. We have supported the new and tightened recommendations that the ODM has announced and to which the Secretary referred this morning.

The CHAIRMAN. This would bring in freight cars and transportation of every kind. It is not only airplanes.

Mr. TIPTON. To the extent that as a practical factual matter they meet the standard which was set, if you anticipate a deficit on the basis of the meeting of military requirements plus a rockbottom civilian requirement, that is the new policy stated on page 6 of my statement——

The CHAIRMAN. You understand that this was a war measure, don't you? That is the only reason it was passed. It was previously repealed after the war, but it was not repealed after the Korean war. It was entirely a war measure.

This is the first time it was extended after peace was declared. It has been extended for 4 years now.

In other words, you think it ought to be a regular policy of the Government, a regular policy in the future, regardless of war, to continue these rapid writeoffs; is that right?

Mr. TIPTON. The policy that we are here urging is that it is an important factor in the maintenance of a mobilization base as well, not only during the course of a shooting war but also in the unhappy circumstances which this country and the rest of the world is in at the present time, it is a valuable piece of legislation for the maintenance of an adequate mobilization base.

The CHAIRMAN. There is always the prospect of war and always has been. We have been engaged in quite a number of wars, so by your line of reasoning then this should be a permanent part of the tax structure of the country, giving these rapid writeoffs to certain industries and not give them to others on a competitive basis.

Mr. TIPTON. I had regarded our suggestion here of endorsing the current ODM policy which is a very tight one as being a much tighter one than has been.

The CHAIRMAN. I don't see why you say it is a very tight one. It arouses this inquiry today. It has not been a tight one, the way it has been administered. It has been tremendously abused.

Mr. TIPTON. The new policy was put forward in December, Mr. Chairman.

Senator ANDERSON. What policy is that?

Mr. TIPTON. Referring to page 6 of my statement, in December the ODM reviewed the general program of tax amortization, came out with what we have regarded as a very severe restriction on the previous policy. It reads as follows:

> Tax amortization will be granted only to applications directly involving procurement of the Department of Defense and the Atomic Energy Commission or where an expansion goal has been established and publicized because of a clear showing that, under conditions of full mobilization, the military and war-supporting requirements, plus the requirements of a rockbottom civilian economy, would be in excess of the supplies available.

The CHAIRMAN. Do you think then this tax writeoff to the Hells Canyon Dam, that Idaho Power Co. dam, comes under that new policy?

Mr. TIPTON. I wish I could answer your question. I just don't know anything about the Hells Canyon Dam.

The CHAIRMAN. You say it is a much stricter policy that was announced in December, and here on the 17th of April they give to the Idaho Power Co. this writeoff.

What is strict about it?

Mr. TIPTON. I can't answer that question because I don't know any of the circumstances surrounding the Hells Canyon Dam, but it is this policy that the ODM is applying to us. At the present time they have taken under advisement the question as to whether there is and will be a deficit in airlift under these standards, or whether at projected periods in the future or whether they will not be, because as I described in my statement, the mobilization plan for air transport falls directly within this statement, if there is a deficit, an anticipated deficit in airlift.

I have no doubt that they will find that there will be a deficit in substantial amounts.

Senator ANDERSON. How are you financially damaged?

You have already shown that the first 2 years you would be worse off if you took the rapid writeoff than you are under the present program. Then there is a little difference for 3 years and then you have to pay it all in the sixth and seventh years.

Now explain how it hurts you to stay with the law if this law became applicable.

Mr. TIPTON. In the course of acquiring these airplanes, the industry needs all the available cash that it can get in order to be able to finance them and operate them.

The CHAIRMAN. Excuse me. Let's get this straight. The present law gives you 10 percent greater writeoff the first year than you have now.

Mr. TIPTON. That is right.

The CHAIRMAN. And it gives you a greater writeoff the second year.

Mr. TIPTON. Let's assume that we adopt the sum of the digits. We can take the one that is most favorable, that is right.

The CHAIRMAN. There are 2 years when you will gain extra capital, won't you, to the extent of about 11 percent?

Mr. TIPTON. Then there are 3 years that we will have a tax deferral.

The CHAIRMAN. Yes.

Mr. TIPTON. Which in our estimate for this whole fleet will aggregate $22 million annually for the entire 5-year period. That does seem—I must say in listening to some of the figures I had heard, that does seem small, but to us in the circumstances that we are anticipating during that particular period, it is going to make a great deal of difference in the availability of cash.

Senator ANDERSON. On $2 billion worth of orders that you are talking about?

Mr. TIPTON. The ones on which the applications are filed at present are $1.4 billion. The total capital requirements will be over $2 billion.

Senator ANDERSON. And this $22 million is going to be in the third, fourth, and fifth years?

Mr. TIPTON. That is right.

Senator ANDERSON. And what is going to happen in the first and second years?

Mr. DURAND. That is an average, Senator. It is very difficult to do more than average this.

Senator ANDERSON. Don't you pay more the sixth and seventh years?

Mr. DURAND. You do, sir; you have to.

Senator ANDERSON. A lot more. You have to catch it all up, don't you, in the sixth and seventh years?

Mr. TIPTON. Oh, yes, sir.

Senator ANDERSON. So what you are trying to say is that a program which benefits you in the first and second years and benefits you in the sixth and seventh years is offset by what happens to you in the third, fourth, and fifth years.

Mr. TIPTON. I think it is just the opposite of that. A program which makes us pay more taxes in the first and second year——

Senator ANDERSON. I am sorry, it is the opposite of that. You have to admit it has all got to be paid in 7 years; hasn't it?

Mr. TIPTON. That is right; it all has to be paid in 7 years.

Senator ANDERSON. You get a little benefit under the present law; you get a little improvement in the third, fourth, and fifth years, and pay a little more in the first, second, sixth, and seventh.

Mr. TIPTON. That is exactly right.

Senator ANDERSON. Does that destroy the whole aircraft industry?

Mr. TIPTON. I am not arguing here that the whole aircraft industry will be destroyed. I am arguing here that we can buy this equipment and maintain these orders and provide this advanced fleet for the military purposes with the aid of this tax deferral, and even though small under circumstances as they exist now, we think it is important, and $22 million annually is important.

Senator ANDERSON. I was looking last night at the U. S. News of May 10 and on page 40 it has something about this year's mixed-up profits picture. The aircraft industry looks pretty good on that page; doesn't it?

Mr. TIPTON. Those are the manufacturers. Those are the ones from whom we are buying the airplanes. It is no wonder they look good.

Senator ANDERSON. This is not a case where what is good for General Motors is good for the others?

Mr. TIPTON. No.

Senator ANDERSON. It all depends on whose ox is getting gored; doesn't it?

Mr. TIPTON. So often it does.

Senator ANDERSON. The fact is that General Dynamics, which owns Convair, jumped its profits from $4,300,000 to $8,794,000, and is getting along pretty well. Its customers have to be doing well or it could not do that well.

Mr. TIPTON. The customers, of which the air transport industry I guess is a relatively minor one, have to scrounge pretty hard to get the money to buy the airplanes.

The new jet transport is going to cost $5,500,000 apiece. We started with the DC–3 to which Senator Anderson referred, paying $100,000 for the airplane.

The CHAIRMAN. All right, Mr. Tipton.

Mr. TIPTON. Considering the tremendous importance, to the national defense as well as to the commerce of the United States, of having a fleet of 400 of the most advanced transport aircraft in being and in airline operation, the temporary postponement of full tax collection on these new aircraft is truly the best national defense bargain the Government could possibly obtain.

In December 1956, in connection with a general program of closing expansion goals, ODM announced that the transport aircraft goal had been filled and was being closed. Concurrently ODM issued the following policy statement with respect to expansion goals:

> Tax amortization will be granted only to applications directly involving procurement of the Department of Defense and the Atomic Energy Commission or where an expansion goal has been established and publicized because of a clear showing that, under conditions of full mobilization, the military and war-supporting requirements, plus the requirements of a rockbottom civilian economy, would be in excess of the supplies available.

At the time the expansion goal for transport aircraft was closed by ODM there were pending with that agency rapid tax writeoff applications of 17 airlines covering 407 aircraft costing approximately $1.4 billion. Our studies showed that under conditions of full mobilization there would be a serious shortage of transport aircraft when the military requirements and the requirements of a rockbottom civilian economy were considered. Accordingly, we requested reconsideration by ODM of its closing of the aircraft goal, and based our request on the fact that the airline industry came squarely within the policy announced by ODM. Our request for reconsideration was granted, and in connection therewith ODM requested the Department of Defense to update its requirements on the airlines for airlift. That study is now underway in the Department and, of course, ODM necessarily has postponed its decision on the commercial aircraft goal until it receives these new requirements from the Department of Defense.

SUMMARY

The airline industry, the Office of Defense Mobilization, and the Department of Defense share the conviction that transport aircraft are facilities directly connected with the national defense. When the airline fleet now in operation and the new aircraft on order are balanced against the military requirements on the airlines for airlift, and the requirements on the airlines for aircraft to carry priority,

essential, war traffic on civil routes, there is, and will continue to be for the years for which requirements have been projected, a substantial deficit of transport aircraft. The fullest possible expansion of the civil air fleet through the acquisition and operation of aircraft by the airlines is the most economical and efficient way for the Federal Government to fill the present and future airlift deficit. To enable the airlinesto fill that deficit it is vital that the tax amortization program for transport aircraft be continued. Accordingly, we recommend that the committee amend S. 1795 by adding thereto an additional category of facilities eligible for rapid tax writeoff. Specifically, we recommend that the bill be amended to provide that facilities, with respect to which it can be clearly shown that, under conditions of full mobilization, the military, requirements plus the requirements of a rockbottom civilian economy are in excess of the of the transport aircraft goal, in order to provide for rapid writeoff

Senator FLANDERS. I came in late, Mr. Chairman.

I was just trying to understand whether the question of the goal of ODM for transport aircraft is now an open question instead of a closed one.

Mr. TIPTON. On December 31 they closed the goal for transport aircraft, and shortly thereafter we applied in the normal course through the Department of Commerce to the ODM for a reopening of the transport aircraft goal, in order to provide for rapid writeoff of the new transports that I have been describing.

That application is now pending before the ODM and the issue outstanding is whether or not under mobilization circumstances there would be a deficit in airlift when the civilian transports and the military transports are added together, will that result in a deficit?

That is the issue that is now pending before them.

Senator FLANDERS. In your recommendations would you base your request for rapid amortization on the results of such an inquiry as is now in progress, or do you ask for them anyway?

Mr. TIPTON. I am not sure I understand your question, Senator. We have applied for them.

Senator FLANDERS. Do you feel that you are entitled to rapid amortization whether or not the ODM decides on further inquiry that the goal has or has not been finished?

Do you make your case on the decision of the ODM?

Mr. TIPTON. We make our case on the basis of the policy that the ODM has stated as being their guiding policy, which is said to be that under conditions of full mobilization the military and war supporting requirements plus the requirements of a rockbottom civilian economy would be in excess of the supplies available.

We base our case on that, urging that the supply of transport aircraft in the hands of the military and in our hands, when taken with the requirements of the civilian economy, would be found under mobilization circumstances to be inadequate.

Senator FLANDERS. Now if on this further inquiry which I understand is now in progress the ODM decides, still decides as it did in December, that the goal has been reached, what I am trying to find out is then do you feel that you have lost your case?

Mr. TIPTON. I am afraid that we would have. I am afraid that we would have lost our case, because that necessarily would have required

them to find as a matter of fact that there was not any deficit under full mobilization circumstances, in transport aircraft.

I think they would be wrong.

Senator FLANDERS. So you do base your case on the question as to whether or not there is a deficit?

Mr. TIPTON. That is exactly right. I am sorry, I should have caught on to that.

Senator FLANDERS. That is what I wanted to get clear in my mind.

Mr. TIPTON. Yes. We base our case on the conclusion, on a very firmly held conclusion, that under full mobilization circumstances there would be a deficit and a substantial deficit in transport aircraft.

Senator FLANDERS. Thank you. That is all, Mr. Chairman.

The CHAIRMAN. Any further questions?

Thank you very much, Mr. Tipton.

Mr. TIPTON. Thank you, Mr. Chairman, and members of the committee.

The CHAIRMAN. Mr. Clay L. Cochran, Economist of the National Rural Electric Cooperative Association.

Take a seat, Mr. Cochran.

STATEMENT OF CLAY L. COCHRAN, DIRECTOR OF LEGISLATION AND RESEARCH FOR NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION

Mr. COCHRAN. Mr. Chairman and members of the committee, my name is Clay L. Cochran. I am director of legislation and research and staff economist for the National Rural Electric Cooperative Association. This association is the national service organization of the farmers' rural electric systems. Approximately 92 percent of all the rural electrification systems are members of this association.

I am appearing before you, in the name of the association, in favor of S. 1795.

At the annual meting of our association this year, the delegates unanimously endorsed repeal of both sections 167 and 168 of the Internal Revenue Code of 1954. (See exhibit A.)

Your committee has already heard the excellent statement of Mr. Alexander Hudgins, executive secretary of the Virginia Association of Electric Cooperatives, and my statement might be said to be supplemental to his.

Mr. Chairman, as our national resolution states, we are very dubious about the use of the tax system of the United States to extend subsidies to any group whatever. We are particularly dubious of the practice of permitting executive agencies to, in fact, alter the tax system as it applies to particular industries or particular companies.

Nothing is so vital to the unity and patriotism of a people than the widespread belief of tis citizens that the existing tax system is as just as possible in this imperfect world.

The granting of subsidies through the tax system by executive agencies certainly strikes at our whole traditional concept of the right of the Congress—and the Congress alone—to tax, and it invites abuse as under Section 168 of the Internal Revenue Code.

We support S. 1795 and hope that it will pass the Congress as quickly as possible because tightening up on the powers of executive

agencies to grant subsidies through the tax system is a step in the right direction.[1]

We are entirely in accord with the view expressed by Secretary of the Treasury Humphrey in his statement to the Subcommittee on Legal and Monetary Affairs of the House Committee on Government Operations, when he said:

> If, in the wisdom of the Congress, such subsidies or assistance to special communities or for special purposes are desired, then appropriations should be made for the purpose which can be submitted to the Congress through regular channels where the amounts will be well known and where the Congress specifically can vote in favor of or in opposition to special treatment for any group.
>
> Under this program of tax reduction (the rapid tax amortization program) in special cases, our net revenues can be reduced and our deficits increased without formal action or appropriations by the Congress.
>
> This use of the tax laws, where the stimulants are applied by men, not by law, is appropriate only in an emergency or under special conditions under rigid restrictions when usual procedures are inadequate for our protection.

We think that phrase of his statement about "stimulants * * * applied by men, not by law * * *" is particularly pertinent in view of the history of the manner in which the Defense Electric Power Administration, with its staff of about three people, has passed on billions of dollars of proposed and approved applications for certificates, granted a goodly portion of these certificates on the basis of an "electric goal" which nobody in the agency had any definite data to justify.

Such abuses and mishandling as we know of, including the certificate granted on Roanoke Rapids subject, and more recently the certificates granted to the Idaho Power Co. for two of its dams on the Snake River, are adequate evidence of abuses which can occur under a procedure which permits executive agencies to tamper with the tax system.

These certificates were granted to subsidize projects which have no direct connection whatever with the national defense.

There is every evidence that Roanoke Rapids and the two Snake River dams would have been built had the certificates not been granted. If this be true, then what possible justification is there for providing a subsidy incentive. In the case of the Idaho Power Co., a subsidy (over a 50-year period) of approximately $329 million is granted to provide incentive for the construction of projects costing a little over $100 million.[2]

Abuses of section 168:

Thus there has been, in our opinion, outrageous abuses of the authority granted by the Congress under section 168 in the form of grants of certificates not necessitated by defense requirements.

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[1] As we understand this bill, it states plainly that under sec. 168 the Federal Government will subsidize only those activities of industry which relate directly to developmental or experimental research for the Department of Defense or the Atomic Energy Commission during an emergency defense period. Beyond this no accelerated tax certificates will be issued.

Further the bill states that certificates will be issued equal in value only to that portion of a facility directly attributable to the production of new defense items as defined in the bill. In this bill the Atomic Energy Commission is singled out for special treatment but, as we understand the bill, electric utilities constructing atomic reactors could not receive accelerated amortization certificates because such facilities would be used for peacetime purposes.

[2] Exhibit B shows how this subsidy is computed, and exhibit C is an explanation of the theoretical basis on which the calculations are based. Incidentally, our assumptions and computations on this matter are substantially in agreement with those of Ebasco Services, as indicated on p. 742 of the Langer hearings.

In addition, the Federal Power Commission and most of the State commissions have taken the view that the Congress in passing section 168 intended to dictate the granting of a bonanza to the private-power companies, and this view strikes at the whole traditional concept of public-utility regulation.

It is also significant that at least one private-power company, the Washington Water Power Co., has issued what is called tax-free dividends on the basis of ODM tax-subsidy certificates. The company contends that these dividends are a return of capital rather than ordinary return on capital, and, therefore, are not subject to the Federal personal-income tax. This practice not only reduces Federal revenues below normal levels but opens a terrible loophole in the tax laws for a favored few.

The CHAIRMAN. Has that principles been accepted by Internal Revenue?

Mr. COCHRAN. I have not heard a report on that. We just heard the investment houses report that Washington Water Power dividends were being repaid, which was returned capital.

The CHAIRMAN. Washington City?

Mr. COCHRAN. No; this is Washington Water Power in the State of Washington.

The CHAIRMAN. I see. Proceed.

Mr. COCHRAN. We would like to propose three amendments to S. 1795:

First, we would like to urge that, if there is any possible doubt about interpretation, it be made absolutely clear that ODM cannot issue certificates to subdidize the private development of atomic reactors. We are greatly concerned over the possibility of monopolistic control of this very important new source of energy. We believe that it will take public subsidy to move the program ahead, but we think these subsidies should be voted openly by the Congress and not concealed under the mantle of the tax laws.

Senator ANDERSON. May I stop you there just a moment? Do you not have the impression, as I have, that the ODM has already granted to Westinghouse, Duquesne Power & Light Co., and others, amortization on the power reactor?

Mr. COCHRAN. It has done so.

Senator ANDERSON. Why should we lock the door now? Did they not grant them to the Detroit Electric on its reactor that they are getting ready to build at Lagoona Beach?

Mr. COCHRAN. I am not sure, but I think they did or would.

Senator ANDERSON. Do you know of any case that they refused to do it?

Mr. COCHRAN. No; I do not, Senator.

Senator ANDERSON. I think it is fairly well established they are going to keep right on granting them on every one that comes along.

Mr. COCHRAN. That makes our point even stronger. We would hope that this bill, or new language in the bill, would preclude that sort of thing, because we believe that it is going to take public subsidy to do this, but we would like for the Congress to grant these subsidies openly.

Senator ANDERSON. Is it your understanding that this exemption to the Atomic Energy Commission permits the continued granting of these amortizations?

Mr. COCHRAN. The reason I phrased my statement the way I did, Senator Anderson, is that I was going to defer to the experts on the committee as to whether or not it would permit the granting of certificates for the building of commercial atomic reactors.

Senator ANDERSON. I thought that this language was pretty good in here. It says—

which is produced or will be produced for sale to the Department of Defense or component departments of such Department or the Atomic Energy Commission for use in the national defense program.

In the case of the Shippingport reactor, there are certain parts that are being sold to the Atomic Energy Commission. There are other parts that are being sold to the Duquesne Power & Light Co.

I thought this writeoff applied only to the parts being sold to the Atomic Energy Commission. If so, I think it may be all right. If you think this language opens it up to where the Yankee reactor or the one of Consolidated Edison in New York or Commonwealth Edison in Chicago is open to rapid writeoff, then I think we had better take a good look at it.

Mr. COCHRAN. I would hope that the committee would do so, but I would not attempt to say, Senator Anderson, how broad that language is or how much it would cover. We would just hope that subsidies to the atomic-reactor program would be granted by the Congress in the open and not through accelerated amortization.

Senator ANDERSON. I just bring tidings of good cheer. That is what Mr. Cannon was trying to do the other day in the Appropriations Committee, and I think the Joint Committee will shortly be in hearings on this.

The CHAIRMAN. At this point, since Mr. Stam prepared this bill, I would like for him to make a statement on that.

Mr. STAM. I think the effect is about what Senator Anderson said, that if it goes to the Atomic Energy Commission itself it would come within the definition for exemption, otherwise not.

Senator ANDERSON. I so read it, Mr. Stam. I thought it was well drawn.

The CHAIRMAN. We will go into that fully. We do not want any loopholes in it.

Mr. COCHRAN. Thank you, sir.

Secondly, we would like to urge that S. 1795 be amended to specifically preclude all regulated monopolies (or utilities) from receiving certificates under section 168.

It is our view that regulated industries operate virtually as cost-plus industries and that the returns to bondholders and stockholders are sufficiently well protected to assure them against loss without these grants of special privilege.

Moreover, we believe that regulated industries by their very nature have a responsibility to provide adequate service to the community as they are, in fact, performing what is essentially a public service.

We do not think that the community should be compelled to grant subsidies and hold out the promise of special bonanzas to such enterprises for performing functions which the law imposes upon them, and we believe that the granting of such subsidies has already led to widespread violation of what is the intent if not the word of the regulatory acts of both State and Federal Governments.

As Senator Byrd said on the floor of the Senate on April 29, 1957:

* * * A public utility is guaranteed its profits.

Further, as the Senator said:

It is totally indefensible to give a public utility, whose earnings on its investment are guaranteed a writeoff to the extent of $65 million.

(Senator Byrd was referring to the rapid tax writeoff subsidy granted the Idaho Power Co. for its Oxbow and Brownlee projects.)

Senator ANDERSON. Don't you think it is significant that the American Telephone & Telegraph which is certainly a utility but is a very carefully regulated utility in the States has not made application for these writeoffs?

Mr. COCHRAN. We have been very curious as to why they would refrain from asking for certificates whereas the electric industry ask for them wholesale.

Senator ANDERSON. I was giving great credit to the telephone industry in the United States for its rare good judgment and fine public policy.

Mr. COCHRAN. Our third and last suggested amendment was transmitted to your committee earlier as a proposed bill of which a copy is our exhibit D. This bill, if rewritten as an amendment to S. 1795, would require the Office of Defense Mobilization or the appropriate agency to report to the Congress in January of each year the total value of all emergency facilities issued during the previous years by industry and by purpose.

The amendment would further require that the Secretary of the Treasury report to the Congress what the effect of the deduction granted under section 168 will have upon the income-tax revenues of the United States.

Such an amendment would give the Congress the necessary information needed to either approve or disapprove any future proposed goals of the administering agency.

Given such a law the Congress could determine whether it is in the interest of the country to issue additional certificates; whether unfair competitive situations are being created; what effects the issuance of these certificates have on small business; and whether the economic growth of the economy is being distorted by granting these certificates.

Senator ANDERSON. Could I ask you at this point if you think there is any advantage in an amendment that would require that these certificates do not become effective until 30 days after being submitted to the Ways and Means Committee of the House and the Senate Finance Committee?

What I am getting at is that you may recall in one of the Atomic Energy Acts, the one of1954, there was a requirement with reference to certain licenses that might be granted for plants, and provision was made that the item had to come before the committee for 30 days.

It seems to me that if on a sizeable power writeoff there had been a 30-day period during which either committee, the Ways and Means Committee of the House, or the Finance Committee of the Senate, could have interposed an objection and effectively held it up, that the speech made by the chairman of this committee on the floor of the Senate might so forcibly have called it to the attention of the Senate Finance Committee that action would not have been taken on it.

Now there is a question in everybody's minds whether any action taken would be effective. I am sure either of those committees might have delayed the effectiveness of the order and I am just wondering if you do not think that might be useful in view of what we found out.

Mr. COCHRAN. I would certainly agree, Senator Anderson, because in my opinion the grants to the Idaho Power Co. would never have been made had they known that such grants would have to lay before a congressional committee for 30 days.

Senator ANDERSON. And there was full power of review?

Mr. COCHRAN. Yes, sir.

Senator ANDERSON. I agree with you. They would never have been made under those circumstances.

Mr. COCHRAN. These are important questions. At the present time, in our opinion, neither the Congress nor citizens have the requisite information on which to base informed opinion.

Surely there would be no objection to having the results of section 168 from past operations, and the planned activities under that section in the future made available to the Congress and the public.

Senator ANDERSON. You say "and the planned activities under that section made available to the Congress."

That is what I am trying to get at. If they are planning to issue a certificate, if that fact were communicated to the Congress and the Congress had 30 days for either House to disapprove it or either committee or House to approve or disapprove, then there certainly would be a deterrent on the planned activities that you mentioned?

Mr. COCHRAN. I think this would be an excellent provision.

In conclusion, Mr. Chairman, I would repeat, we would like to see S. 1795 passed. We hope that these amendments can be added, and I would certainly incorporate Senator Anderson's suggestion with ours, but we would like to see the present bill passed if that is the only alternative, because it is a good bill and a long step in the right direction.

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

(The exhibits previously referred to follow:)

EXHIBIT A

RESOLUTION ADOPTED BY THE NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION AT ITS ANNUAL MEETING MARCH 7, 1957, CHICAGO, ILL.

From: Legislative committee.
Approved by: Resolutions committee.
Subject: Tax laws and subsidiaries to power companies.

Whereas under sections 167 and 168 of the Internal Revenue Act of 1954, power companies are receiving billions of dollars in interest-free loans and, under rulings by the Federal Power Commission, stand to collect immense subsidies: Now, therefore, be it

Resolved, That sections 167 and 168 be repealed; and be it further

Resolved, That the Federal Power Act be amended to compel the Federal Power Commission to require power companies to use the same depreciation figures for ratemaking purposes as for corporation income taxes; and be it further

Resolved, That the practice of providing subsidies to industry and utilities through the tax laws be abandoned, and that all subsidies considered necessary by the Congress be provided in direct, regular appropriations rather than being concealed in tax laws.

EXHIBIT B

Estimated benefits accruing to Idaho Power Co. by virtue of accelerated tax amortization certificates issued on Brownlee and Oxbow

	Brownlee	Oxbow	Total
Total value of certificates	$43,639,700	$21,559,200	$65,198,900
Depreciation allowance per year, based on certificates	8,727,940	4,311,840	13,039,780
Less normal 2-percent depreciation (assuming average 50-year life of facilities)	872,794	431,184	1,303,978
Excess depreciation per year	7,855,146	3,880,656	11,735,802
Tax savings for 1 year (52 percent of excess depreciation)	4,084,676	2,017,941	6,102,617
Total tax savings for 5 years	20,423,380	10,089,705	30,513,085
Plus 6-percent interest compounded over 50-year life of facilities	220,406,145	108,886,637	329,292,782
Less deferred taxes (assumed payable over 45 years)	20,423,380	10,089,705	30,513,085
Net benefits accruing to Idaho Power Co. over 50-year period	220,406,145	108,886,637	329,292,782

Source: National Rural Electric Cooperative Association.

EXHIBIT C

EXPLANATION OF TAX SUBSIDIES RECEIVED UNDER THE DEFENSE ACCELERATED AMORTIZATION (DEPRECIATION) PROGRAM

DEAR SIR: Reference is made to a telegram received by one of our State editors stating that the figures we have produced showing interest-free loans and subsidies to the private power companies under the accelerated depreciation certificates issued by the Office of Defense Mobilization "have been challenged" on the ground that the practice of accelerating depreciation for Federal income tax purposes actually results in a delay in payment—or a deferral—of Federal income taxes rather than a subsidy.

Attached are two tables which are the basis for the computations I have made. Table 1 shows the summary figures on the amount of "interest-free loans" available to a power company under a $1 million certificate and the total subsidy available to the same company under the same certificate. Let us explain this table.

In the first place, we take a $1 million certificate as a round figure on which to base our analysis. This certificate may be the total cost of a facility, but, as a rule, ODM certifies only a part of the total cost of a facility for rapid depreciation. This certification of only a part of the total cost is the result of two factors: (1) Such costs as the cost of land for the site of the plant is not depreciable and therefore would not be included; (2) ODM (via its subsidiary agency the Defense Electric Power Administration (DEPA) which is under the control of Mr. Fred G. Aandahl, Assistant Secretary of Interior) has a set of rules and procedures which affect the percentage of the total investment subject to accelerated depreciation—the basic item being that when the utility is adding capacity faster than the average rate of expansion over a long period of years this added capacity is assumed to be for defense purposes. This assumption is usually absurd, but they nevertheless make it. So, we assume that a utility company has been granted a certificate for $1 million—meaning that it can accelerate depreciation on that $1 million plant.

Under the certificate, the utility can depreciate the total cost of this property for tax purposes over a 5-year period—or, at the rate of $200,000 per year—which accounts for the second item in table 1. But, the utility would be able to depreciate the plant at a normal rate without the certificate, so we assume that it would be entitled to $30,000 in depreciation without certificate and we subtract this normal figure from the $200,000 total, leaving $170,000 in "excess depreciation."

Now the most significant thing about depreciation to a utility is that any earnings of the company which can be labeled "depreciation" are automatically tax-free as far as Federal income tax purposes are concerned. Therefore, this

certificate makes its possible for the company to claim $170,000 in excess depreciation over and above its normal legal right. With Federal income taxes at a 52 percent rate on profits, this means a tax saving, tax deferral, or interest free loan to the company of $88,400 per year for each of 5 years or a total of $442,000 over the 5-year period of the certificate. We use the terms "tax saving," "tax deferral," and "interest free loan" because various people use various terms, but they all refer to the same money—money which has been collected from rate payers on the justification that the company will use it to pay Federal income taxes, but which is not used for that purpose because of the accelerated depreciation certificate. Instead of paying the money to the Treasury, the utility is permitted to keep it.

If you will refer to column 4 of table 2 (or col. 4 of table 51, p. 89 of the NRECA Power Facts Handbook) you will see the annual savings for 5 years set forth there. So far as I know, nobody has, can or will challenge the fact that a company with a $1-million certificate would be entitled to withhold these taxes under the certificate because that is the whole purpose of the certificate.

Another assumption on which there is general agreement is that once the 5-year period is past, the company will be able to claim no further depreciation on the depreciated plant or portion of the plant for income tax purposes, and, as a result, the company will have to pay more taxes out of a given income than they would have had to pay had they used normal depreciation rates. If you will look at column 5 of table 2, you will find that we assume that the company will repay these taxes over a period of 28⅓ years after the privileges granted by the certificate have been exhausted. (If Federal income tax rates rise in the future, the company will have to pay more than is shown. If income tax rates are decreased, the company will enjoy a flat profit windfall over and above anything we have shown anywhere. And the odds are overwhelmingly on the side of a Federal corporation tax reduction rather than an increase.)

Columns 4 and 5 of table 2 indicate that the company will defer $442,000 per $1-million certificate and will ultimately repay the same amount—assuming no change in the tax laws. But, and this is the heart of the matter on these challenges of our figures, in the meantime, the corporation gets the benefit of the interest free loan of its deferred taxes. It gets the use of those deferred taxes in varying amounts over a long period of time. I quote from Opinion 264 of the Federal Power Commission, issued December 4, 1953:

"Thus, the recipient of a certificate of necessity obtains substantial deductions against net income for income tax purposes during each of the first 5 years, and much smaller deductions therefrom during the remainder of the normal amortization period. If the income tax rates remained the same during the entire life of the facilities, the same amount of taxes ultimately would be paid under either accelerated or normal amortization. By the enactment of this law, Congress did not forgive the payment of any income taxes; it merely allowed payment of some of them to be deferred. This has the precise effect of a grant by our Government to a certificate holder of an interest-free loan."

In giving this opinion, the Federal Power Commission adopted NRECA's "interest-free loan" in describing the nature of this tax deferral.

Now the question is: If a power company gets a $442,000 interest-free loan on each $1 million of certified property—what is this interest-free loan worth to the company? In a competitive industry where profits and returns vary sharply, the answer would be indeterminate, but in the electric utility industry the value of such an interest free loan is pretty definite. The value of the certificate could be placed as the return which the company would pay on common stock, but this would shoot the resulting subsidy sky high because utility common stocks (including both the cash dividends and the stock dividends) frequently range well above 6 percent. We have taken the conservative course and have assumed that the private company will earn 6 percent on its investment—and have made this $442,000 a part of that investment which it in fact is. On this assumption the total benefit or subsidy to the utility is 6 percent of the interest free loan over the life of the loan—compounded annually.

It might be easier to visualize our reasoning if you assumed that a utility had only one consumer. This consumer is compelled to pay for the taxes which the utility withholds, but we credit the benefits to the company at its regular

earning rate, and since those earnings are not turned over to the consumer, we compound them to show the total subsidy involved.

The columns in table 2 show the method of computing such subsidies. We were very careful to show that the utility does not have the entire $442,000 for the full 33⅓ years—but only varying amounts depending upon the rate of accumulation, the compound interest, and the repayment of the loan.

In effect, the net subsidy to the company over the life of a $1 million facility is $1,502,564—and, in our opinion, this is a very conservative estimate because it (1) disregards the very real chance of a future reduction in Federal corporate income taxes; (2) omits any cost to the company of raising comparable amounts of money in the money market; (3) assumes that the company will not make in excess of 6 percent; and (4) assumes that the interest-free loan is entitled to only the average rate of return instead of the rate of return on common stocks or other securities which always earn a rate of 6 percent and more—usually more.

If there are any further points we have not cleared up, please let us know. We know these figures will be challenged—always on the assumption that the person confronted with the challenge will not be able to handle the computations. The power companies have to challenge these figures because they have spent no one knows how many millions of dollars attacking rural electrification and Federal power as subsidized, only to find that someone has caught them ransacking the Treasury of an estimated $4 billion. All of the figures are not available, but several months ago they had already secured certificates entitling them to $1.4 billion in interest-free loans and almost $4 billion in subsidies.

Sincerely,

CLAY L. COCHRAN,
Director, Legislation, Research and Management Department.

TABLE 1.—*Estimated benefits accruing to a commercial electric corporation under accelerated tax amortization certificates*

Assumptions: Investment, $2,000,000. Total period of amortization and depreciation, 33⅓ years. Amount subject to 5-year amortization (50 percent), $1,000,000.

Total value of certificates issued	$1,000,000
Depreciation allowance per year based on certificate	200,000
Less normal 3-percent depreciation (assumes average life of facilities of 33⅓ years)	30,000
Excess depreciation per year	170,000
Tax savings for 1 year (52 percent of excess depreciation allowance)	88,400
Total tax savings for 5 years	442,000
Plus 6 percent interest compounded over estimated 33⅓ year life of facilities	[1] 1,502,564
Less deferred taxes assumed to be payable (payable over 28⅓-year period)	442,000
Net benefits accruing to the corporation over a 33⅓-year period	1,502,564

[1] See table II for computations.

NOTE.—A short method for computing the amount of interest free loan is to multiple 0.442 times the amount amortized, and a similar way to compute the total subsidy is to take 1.502564 times the amount amortized.

TABLE II.—*Computation of total benefits derived by commercial electric corporations for an accelerated amortization certificate of $1,000,000*

Year	Cumulative total benefits	6 percent interest per annum	Interest free loan [1]	Deferred taxes paid [2]	Net benefits each year
1			$88,400		$88,400
2	$88,400	$5,304	88,400		93,704
3	182,104	10,926	88,400		99,326
4	281,430	16,886	88,400		105,286
5	386,716	23,203	88,400		111,603
6	498,319	29,899		$15,600	14,299
7	512,618	30,757		15,600	15,157
8	527,775	31,666		15,600	16,066
9	543,841	32,630		15,600	17,030
10	560,871	33,652		15,600	18,052
11	578,923	34,735		15,600	19,135
12	598,058	35,883		15,600	20,283
13	618,341	37,100		15,600	21,500
14	639,841	38,390		15,600	22,790
15	662,631	39,758		15,600	24,158
16	686,789	41,207		15,600	25,607
17	712,396	42,744		15,600	27,144
18	739,540	44,372		15,600	28,772
19	768,312	46,099		15,600	30,499
20	798,811	47,929		15,600	32,329
21	831,140	49,868		15,600	34,268
22	865,408	51,924		15,600	36,324
23	901,732	54,104		15,600	38,504
24	940,236	56,414		15,600	40,814
25	981,050	58,863		15,600	43,263
26	1,024,313	61,459		15,600	45,859
27	1,070,172	64,210		15,600	48,610
28	1,118,782	67,127		15,600	51,527
29	1,170,309	70,219		15,600	54,619
30	1,224,928	73,496		15,600	57,896
31	1,282,824	76,969		15,600	61,369
32	1,344,193	80,652		15,600	65,052
33	1,409,245	84,555		15,600	68,955
34 [3]	1,478,200	29,564		5,200	24,364
Total	1,502,564	1,502,564	442,000	442,000	1,502,564

[1] Federal corporation income taxes deferred.
[2] Deferred taxes assumed to be payable after facilities have been depreciated 100 percent.
[3] On assumption of 33⅓ years as average life of facilities, interest, taxes and net annual benefits are reduced to ⅓ for 34th year.

A BILL To amend section 168 of the Internal Revenue Code of 1954 to provide that certain reports and estimates shall be furnished annually to the Congress on matters relating to accelerated amortization

EXHIBIT D

A PROPOSED BILL

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That Section 168 of the Internal Revenue Code of 1954 is amended by redesignating subsection (i) as subsection (j), and by inserting immediately after subsection (h) the following new subsection:

"(i) REPORTS TO CONGRESS—

"(1) REPORTS BY CERTIFYING AUTHORITY.—The certifying authority designated under subsection (e) shall report to the Congress in January of each year on its activities under this section. Such report shall show the total dollar cost of all emergency facilities with respect to which certifications were made under this section during the preceding calendar year and during the preceding five calendar years, and shall show the total dollar cost of emergency facilities of each of the classes of industries with respect to which such certifications were made during such year and during the preceding five calendar years.

"(2) REPORTS BY SECRETARY OF TREASURY.—The Secretary of the Treasury shall report to the Congress in January of each year concerning the effect of the deduction granted under this section upon the income tax revenues of the United States. Such report shall state the total of the deductions granted under this section during the preceding five calendar years. The report shall also contain an estimate of the total increased revenue from income taxes which would have been obtained for the pre-

ceding calendar year, and for the preceding five calendar years if this section had not been enacted. Such report shall also contain such other information as the Secretary of the Treasury may deem necessary in order properly to inform the Congress of the effect of this section and operations of the United States and private citizens under it."

Senator FLANDERS. Mr. Chairman, I would like to ask a question of the witness if I may.

Without prejudice to the position that you have stated, as set forth in this document, I would like to be clear in my own mind as to the tax liabilities of the REA, which are members of your cooperative association.

What is the nature of the tax liabilities to which your members are subjected?

Mr. COCHRAN. In virtually all of the States, Senator Flanders, their taxes are the same as that of the ordinary commercial utility under State and local laws.

The exception is that as nonprofit cooperatives and in some cases public utility districts, they are not subject to the Federal corporation income tax.

Senator FLANDERS. Then the Federal cooperative income tax is in some way determined by local legislation?

Mr. COCHRAN. No, sir. I was only saying that in terms of State and local tax laws in most of the States they are treated the same as a commercial power company.

Senator FLANDERS. Yes.

Mr. COCHRAN. The difference between the taxes of a commercial power company and our cooperatives or public utilities districts is that being nonprofit, the latter are not subject to the Federal corporation income tax.

This is the result of Congress' action, not State or local.

Senator FLANDERS. So not having any profit, you have no profit tax?

Mr. COCHRAN. Yes, sir.

Senator FLANDERS. That is all, Mr. Chairman.

The CHAIRMAN. Thank you very much.

Mr. COCHRAN. Thank you, sir.

(Whereupon, at 12 noon, the committee was adjourned, to reconvene at 10 a. m., Thursday, May 9, 1957.)

RAPID AMORTIZATION OF EMERGENCY FACILITIES

THURSDAY, MAY 9, 1957

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

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

Present: Senators Byrd (chairman), Kerr, Frear, Long, Smathers, Gore, Martin, Williams, Flanders, Malone, Carlson, Bennett, Jenner.

Also present: Colin F. Stam, Chief of Staff, Joint Committee on Internal Revenue Taxation.

The CHAIRMAN. The committee will come to order.

The witness today will be Mr. Gordon Gray, Director, Office of Defense Mobilization.

Mr. Gray, will you please come forward.

Senator GORE. Mr. Chairman, before we start with Mr. Gray, I wonder if it would be in order for me to request that the staff call the Treasury and get certain information?

As you know, the option expired yesterday for the holders of 1⅝ bonds. There was some rumor in financial circles, also, yesterday, that more than a billion dollars of those must be redeemed in cash.

I would like to know the extent to which holders exercised their option to exchange the 1⅝s issued 3 years ago for the 3⅝s, and also the cash balance of the Treasury.

The CHAIRMAN. Mr. Stam, will you take a memorandum and get the information?

(The material referred to follows:)

Total bonds	$4,155,000,000
Total converted	2,351,000,000
Notes	647,000,000
Not converted	[1] 1,156,000,000

[1] A total of 28 percent were not converted.

Mr. KERR. I assume you are testifying on the pending bill, your testimony is directed to the bill, S. 1759.

Mr. Chairman, I would like to state that I am happy to be here this morning when Mr. Gray is here. I think he is one of the ablest men we have in our executive branch, and I think that the information he gives us will be very worthwhile.

Mr. GRAY. Thank you, sir.

The CHAIRMAN. Go ahead, Mr. Gray.

STATEMENT OF GORDON GRAY, DIRECTOR, OFFICE OF DEFENSE MOBILIZATION

Mr. GRAY. Mr. Chairman, gentlemen, the bill with respect to which this hearing is being held is taking place——

Mr. KERR. May I ask if he is in possession of a copy of your statement?

Mr. GRAY. I have no prepared statement, Senator.

It has to do with restricting very substantially the authority to grant tax amortization certificates under the internal revenue legislation.

As perhaps the members of the committee know, the program of administering these tax amortization certificates has been progressively narrowed and restricted over a period of time until at the present time we only have 8 expansion goals open of which 5, as I have recently announced, are under very serious current study, looking forward to a closing of them at the earliest possible date.

Senator BENNETT. Mr. Gray, would you give us those 8 and those 5?

Mr. GRAY. Yes, sir; I will. I have a great sheaf of papers here.

The five which are under serious immediate study cover: Nickel, mica substitutes, steam turbines, steel castings, roll-on roll-off ships.

Senator KERR. The last one is what?

Mr. GRAY. Roll-on, roll-off ships.

That is a type of vessel which is built so that large equipment can be rolled on, and rolled off, and not loaded aboard by crane and offloaded by other methods.

The other three are: Research and development labs; liquid oxygen and liquid nitrogen for defense use; and production facilities for military and Atomic Energy Commission procurement.

Now, I take it that——

Senator KERR. That last is what?

Mr. GRAY. Production facilities for military and Atomic Energy Commission procurement.

Now, if I understand Senator Byrd's bill, the intent of it would be to permit, where justified, the continued tax amortization in the fields of military and AEC procurement and in research and development.

I believe that it would not permit an open goal for liquid oxygen and liquid nitrogen facilities, so that administratively we have moved toward a practical situation which would result from Senator Byrd's bill. However, we, as I say, cannot say that these five goals under study are actually closed yet.

I would expect them to be closed relatively soon.

Therefore, I suppose one thing we are dealing with is a practical question.

Let me say particularly with regard to the legislation, if it is to be adopted by the Congress, I would hope that some technical amendments could be made which would make it clear that procurement for defense and AEC purposes was fully covered.

I think there is some question about it as the language of the bill now stands, and I would certainly hope that there would be an amendment which would take care of such a problem as liquid oxygen for defense uses.

Senator KERR. At that point, Mr. Gray, what use is made of liquid oxygen and liquid nitrogen?

Mr. GRAY. Very important uses in the missile program.

Senator KERR. What relation, if any, to that is the use of helium?

Mr. GRAY. Senator, you are getting me into a technical field.

Senator KERR. I didn't want to.

Mr. GRAY. I am not sure that I understand the question.

Of course, one important commercial byproduct at the present time of liquid oxygen production is argon gas which has not only military but important civilian uses today.

As you probably know, as far as the civilian economy is concerned, because of strikes, partially, and I guess generally limited production facilities in existence, argon gas has been a problem. There has not been enough to go around.

I am afraid that I am unable to relate helium specifically to this. I will be glad to get any information for the record if the committee is interested in it.

Senator KERR. I would like to have you do that for us.

(Mr. Gray subsequently submitted the following:)

In regard to the need for helium by the military services and the AEC, the information we have received from the Air Force is that helium is required in their ballastic and guided-missile programs. The specific use and names of the missiles have been classified "Secret" by the Air Force. We will be pleased to make the information available, if desired, to authorized persons. The AEC informs us that they would be unable to meet their production program levels if the delivery to them of adequate supplies of helium were in any way curtailed.

We also have recent estimates from the Air Force, the AEC, and the Navy with regard to helium requirements. This information too is classified. It can be released only with proper precautions and if necessary.

Mr. GRAY. All right.

Senator GORE. May I ask a question along that line?

Senator BYRD. Certainly.

Senator GORE. Mr. Gray, why, in your opinion, do you think it is necessary to permit rapid depreciation of facilities involved in atomic-energy procurement? What kind of procurement do you have in mind?

Mr. GRAY. At the present time, in the administration of the program of certification under this open goal, we are not now certifying, as I understand it, for any commercial or so-called peaceful uses of atomic energy, but only as it relates to Atomic Energy Commission requirements for the Defense Establishment. It is in the interest of defense.

Senator GORE. We should be—I wish you would be a little more specific. Just what kind of procurement do you have in mind for defense purposes for which rapid depreciation may be necessary?

Senator BENNETT. May I suggest the specific question which may help?

Does this rapid amortization cover the erection of mills for the benefitiation of low-grade uranium ores?

Mr. GRAY. Mr. Chairman, I have members of my staff who are specifically familiar with the operation of this particular expansion goal. May I ask——

The CHAIRMAN. Ask them to come forward and identify themselves.

Mr. WYCKOFF. Mr. Chairman, my name is J. B. Wyckoff, Chief of the Tax Amortization Branch, the Office of Defense Mobilization.

Mr. GRAY. Would you respond to the question? What kind of Atomic Energy Commission facilities would be permitted for rapid tax amortization under our open expansion goal?

Mr. WYCKOFF. The applications that we have received have mainly been for the mining and smelting of uranium, and all of the work which is done on zirconium and hafnium, new products.

Senator GORE. You say work done on. Does that involve research?

Mr. WYCKOFF. Then we have had many applications for research and development in the atomic-energy field which involves all of those products and others.

Senator FREAR. We are only talking about facilities.

Mr. WYCKOFF. Production facilities, including——

Senator KERR. And research expansion.

Senator FREAR. Do you capitalize research expense?

Mr. WYCKOFF. No, applications cover the buildings, all of the equipment, and everything which is involved in the capital investment preparatory to research and development work in the atomic-energy field.

Senator FREAR. I see.

Senator GORE. Mr. Chairman, it so happens that I have the privilege of serving as chairman of the Raw Resources Subcommittee of the Joint Committee on Atomic Energy. From my experience in that capacity I know that the AEC enters into negotiated contracts with mills and concerns for the mining and smelting and processing of uranium ores.

There is, as of now, an unlimited market and will be for many years, for any foreseeable year in the future. It does seem to me that if there is to be a subsidization of this industry, which is now moving into a stabilized and greatly improved industry, that the subsidy should be clearly recognized and not camouflaged in tax amortization.

The Joint Committee ought to be able to exercise surveillance over the execution of these contracts with the clear knowledge of the amount of subsidy involved.

I do not know why the subsidy itself should be diversified.

Senator BENNETT. May I ask the Senator a question?

Doesn't the present law regarding incentives for the production and smelting of uranium end in 1966?

Senator GORE. I am unable to answer you.

Senator BENNETT. I think it does, and on that basis, the responsibility of erecting plants and then depreciating them over the normal life of an ordinary industrial plant, 20 to 30 years, would carry them far beyond the point where the present Government-purchase program might end.

Senator KERR. The Senator from Utah is correct. The basic program of purchasing ends in 1962 under an order issued by the Atomic Energy Commission. There is an extension of the program beyond that to 1966. But on a basis considerably limited as compared to the one which ends in 1962.

Senator BENNETT. So this might be a field where the privilege of more rapid amortization might be justified because the opportunity to use those facilities beyond at least 1966 might be restricted.

Senator GORE. Senator, I doubt if that is very material, except to the extent of the legal expiration of the purchase program. I remind you that the atomic-power program of the Government is not expected to really come into fruition until the middle sixties, at which time the demand for unanium is expected to greatly increase. There is no foreseeable end to the demand for uranium, even though there is a cutoff date within the law.

Senator BENNETT. It is presumed that, after the cutoff date arrives, the incentives which former partial subsidies gave to the industry may be conceivably eliminated. Many of these plants might have to close down in the face of a price that might exist beyond that point. We are after uranium now at any price. When the industry is forced to compete in the open market, a lot of producers and probably a lot of smelters would find it difficult to continue.

Senator GORE. I must take exception to the statement that we are after uranium at any price. The recent experiences have shown a very encouraging reduction in the cost of mining and processing uranium.

Senator BENNETT. That is an exaggerated statement, but we certainly have had a liberal subsidization program and a liberal price structure for uranium for defense, which presumably might end after 1966.

Senator GORE. My point, Mr. Chairman, is that it seems to me that the matter should be considered by the Congress as a whole and that there should not be splintering of subsidy. If there is to be a subsidy, and in some cases subsidy is necessary, then it should be clearly recognized and so treated by the Congress.

The CHAIRMAN. Proceed, Mr. Gray.

ONE MAN JUDGE OF WHO BENEFITS FROM SHORT AMORTIZATION PERIODS

Senator MALONE. May I ask, is this so-called shortened plan optional with you as Chairman of the Board; you can give it or withhold it? Is that right?

Mr. GRAY. Yes; within the framework of the legislation, the responsibility is in the Office of Defense Mobilization.

Senator MALONE. What is the framework of the legislation? Would you explain it?

Mr. GRAY. The basic legislation is the Internal Revenue Code, as amended, I believe, in 1954, which permits the granting of accelerated depreciation in the interest of the mobilization requirements of the country. As I have indicated, through administrative action, the breadth of this program has been very substantially narrowed. There were a great many expansion goals which have been closed, and I am not sure that you were here, sir, when I indicated this is down to 8 areas now, of which 5 are under urgent consideration, I think, looking toward closing them, so that, as I have stated, substantially——

Senator MALONE. Closing such areas to short amortization periods for industry within that area?

Mr. GRAY. It means that no application in that area will be received and acted upon.

Senator MALONE. Specifically, my question was: "It is discretionary with you as Chairman of the Board; you can withhold or grant it; is that right?"

Mr. GRAY. That's right, sir.

Senator MALONE. Then I join with Senator Gore that that is too much power to place in the hands of one man over whom Congress has no control. How much money does it amount to now? What is the amount involved in the short amortization periods that have been granted since the passage of the act?

Mr. GRAY. Since the beginning?

Senator KERR. Investments to which the principle of accelerated depreciation has applied?

Senator MALONE. Has applied; that is true. How much is it?

Mr. GRAY. Over the period of the entire program?

Senator MALONE. The entire period.

Mr. GRAY. The number of applications runs into the thousands.

Senator MALONE. It isn't applications I asked about. How many did you grant?

Senator KERR. Total investments.

The CHAIRMAN. Mr. Humphrey gave that information.

Mr. GRAY. Yes; Mr. Humphrey gave it.

The CHAIRMAN. From November 1950 to March 1957, there were 22,000 certificates issued. Under the 5-year amortization program, the total cost of these projects was almost $39 billion. Almost $23 billion, or about 60 percent, was made eligible for a 5-year writeoff. Mr. Humphrey further stated that the Government has lost $3 billion by reason of necessity of paying interest on borrowed money.

Senator MALONE. Now, Mr. Chairman, $40 billion approximately, then, has been granted by this Board, this Board of which now you are the sole deciding member; is that right?

Mr. GRAY. Tax-amortization certificates have been issued for almost $23 billion.

Senator MALONE. For 4 or 5 years, tax-amortization periods.

Mr. GRAY. That's right, sir.

Senator MALONE. I say, again, that there might have been some justification for it when it was first passed, but it is too much power for you to have. It is simply the judgment of one man, then, and one man is not big enough to judge all of the factors set in motion by such decisions—there is too much chance of favoritism without intention on your part.

I believe, with Senator Gore, that this committee should severely limit your power, if not abolish it altogether.

I think it has been abused, without question—probably not with any intention on the part of the Chairman. The Chairman who preceded you is a highly respected man and a very intelligent and capable man, but there is no one who can write off $3 billion worth of taxation in this country and understand the effect on the tax structure of the Nation.

It is simply too much responsibility to place in one man over which Congress has no control at all.

Senator WILLIAMS. If I understand correctly, you suggested that this bill be amended to cover those facilities for procurement for defense; is that correct?

Mr. GRAY. That is correct, sir.

Senator WILLIAMS. Would it not be possible to almost cover any type of facility under that category?

Mr. GRAY. I don't think so, sir. This would be direct procurement for defense.

Senator WILLIAMS. Steel is for defense, isn't it?

Mr. GRAY. Well, this would be procurement of defense items; items used by the military as a product, as an example.

The CHAIRMAN. Isn't that what the present law is supposed to be? The present law is supposed to be confined to defense plants. Am I correct?

Mr. GRAY. No, sir; I think the present law is much broader than that.

The CHAIRMAN. Would you mind, just so that we can understand it, to read the present law, that clause that gives you the power to grant accelerated amortization?

Mr. GRAY. In determining, for the purposes of subsection——

The CHAIRMAN. Read the specific section that gives you the power to do this, what it is, upon what conditions can you do it.

Mr. GRAY (reading):

> There shall be included only so much of the amount of the adjusted basis of such facility as is properly attributable to such construction, reconstruction, erection, installation, or acquisition, after December 31, 1949, as a certifying authority—

that is, Office of Defense Mobilization—

> designated by the President, by Executive order, as certified as necessary in the interest of national defense during the emergency period.

In the interest of national defense.

The CHAIRMAN. It is all based on national defense.

Senator WILLIAMS. If we amend this bill in line with the suggestions you have made, we would just as well leave the existing law as it stands because you have almost unlimited authority to interpret any type of facilities, as you have done, in the interest of national defense.

Senator KERR. Will the Senator yield there?

As I understood Mr. Gray, he made that classification, or limited his recommendation only to those facilities having to do, one with research in certain fields, two, production of liquid oxygen and nitrogen; three, production facilities for military and Atomic Energy Commission procurement.

In other words, he was not talking about a broad classification for all matters of national defense, but only those three classifications for national defense.

Senator WILLIAMS. I understood him to give those as examples, but if those are the examples and only three, why not spell them out?

Senator KERR. He did.

Senator WILLIAMS. Why the broad language?

Mr. GRAY. I think, Senator, if the bill should be amended in that respect, that the concern you have, would be taken care of by my interpretation of it.

It certainly would not include tax amortization for steel expansion.

Senator WILLIAMS. I just used that as an example.

You say you have 8 facilities that you are listing and 5 of which are in process of being studied and perhaps dropped?

When was this last of eight made up?

Mr. GRAY. It was reduced down to 8—well, let me say when I took over this responsibility in March, there were 12 open goals. Four have been closed since the 14th of March.

Senator WILLIAMS. Under which of those categories would you find the classification for this amortization certificate for Idaho Power?

Mr. GRAY. The power goal is not involved in these eight.

Senator WILLIAMS. You have some more besides these eight?

Mr. GRAY. The electric power goal was closed in December 1955.

No new applications, were acted upon which were received after December 1955 with respect to power; this was an application which had been filed in 1953 at the time this goal was open.

But there is no——

Senator WILLIAMS. Had it been turned down before?

Mr. GRAY. No, sir.

Senator WILLIAMS. How many more pending do you have?

Mr. GRAY. In power, I think not any.

Senator WILLIAMS. You don't have any more pending in any of these other categories?

Mr. GRAY. In other categories, we do. I would like to give you the figures of what is now pending.

Senator WILLIAMS. Do I understand correctly that anyone who has his application in before you suspended, before you declare your goal completed, is eligible for consideration, and those who have not filed prior thereto would not be eligible?

Mr. GRAY. That is correct.

Senator FREAR. December 1955?

Mr. GRAY. That is correct.

Senator WILLIAMS. Would that not lend itself to the suggestion that everybody who thinks he may at some future date want to be eligible to rush in with an application and load you with a lot of applications just in the event he wants to get under the deadline?

Mr. GRAY. I don't think that happens, Senator, and as soon as there are sufficient applications to meet the goal which has been established, then, and when the goal is closed, there are no new applications received.

If, before the goal is closed, there are applications which exceed the goal established, then certain criteria apply to the selection of those which shall be granted involving such things as dispersion and other matters.

The CHAIRMAN. Are these goals you mention simply the policy of this particular department?

Mr. GRAY. That's right.

The CHAIRMAN. That is not the law.

If the Idaho Power Co. is entitled to this from the standpoint of national defense, why are not other power companies entitled to it?

Senator WILLIAMS. Would it not be possible in that line that after you have closed your date for applications, or as I understand it, 1955, that in the latter part of 1956 or even earlier part of 1957, you would get an application from a company which would be much more strategically located and which would be, if you were going to grant 30 or 40, would be much better from the interest of national defense than one that would be—would be better than that one; yet, do I understand that you have precluded yourself from even considering that which

you would know would be better and just because you had a date shut off a couple of years ago?

Do you operate under that basis?

Mr. GRAY. I am saying that on the basis of a very careful consideration, not just in the Office of Defense Mobilization, but with the agencies involved, and knowledgeable in the area which is under consideration, certain target goals were set for capacity in whatever the area involved was, and once this very carefully considered goal was met, the goal was closed and applications that came in subsequent to that are not eligible for consideration.

Senator WILLIAMS. Even though that in the opinion of you and the rest of the Board would be unanimous that one of these later applications would be much more strategically located and would be better in the interest of national defense and all other factors involved, you still would not consider it?

Mr. GRAY. We do not withdraw a tax amortization certification once it has been granted.

Senator WILLIAMS. I am not speaking of that, but I am speaking of the fact that you wouldn't even consider an application coming in from another party for facilities which would be much more strategically located and better for all concerned—you would reject it in its entirety because it was not filed in time, is that correct?

Mr. GRAY. Because the goal for which the facility was requested had already been met.

There would be no reason for granting tax amortization to a new facility to get a productive capacity which had already, in the judgment of those who had considered it, been taken care of.

Senator WILLIAMS. How would you know that the goal had been met solely on the basis of these applications because conceivably you could decide against all of these applications?

Conceivably, you could have decided against the Idaho Power and many other applications in which event you maybe would not have met your goal.

Is your goal set on applications only, or is it set on facilities after they are approved?

Mr. GRAY. No, the goal is set without regard to applications.

As a matter of fact, we have had some goals where we felt that capacity should be expanded, where there have been no applications under the goal.

Senator WILLIAMS. But your goal is set on the basis of finished facilities, is that correct?

Mr. GRAY. The goal is set on the basis of what is required in this particular area.

Senator WILLIAMS. In the form of completed facilities?

Mr. GRAY. That is right, sir.

Senator WILLIAMS. If you shut off your applications back in 1955, on the basis that you had all the facilities applied for that you needed, you were operating on the assumption at that time that you were going to approve the facilities at some future date, is that correct?

Senator BENNETT. I wonder if it would help the committee if we could ask Mr. Gray: Isn't it true that your goal is set on the basis of estimated need at a future time, total need over a future period rather than need as of the current time?

Mr. GRAY. That is correct, Senator. It is our presently identifiable need against the mobilization requirements of the economy against an emergency.

Now, I would like to respond, if I may, to the suggestion that, which I think, the suggestion that one man makes the entire decision with respect to this program.

The steps involved in the development of the expansion goals which have been discussed is that the delegate agencies, for example, if we were talking about a military item, the Department of Defense, working with the ODM staff, would identify these deficiencies in productive capacity and recommend an expansion goal or goals.

The Office of Defense Mobilization then reviews and evaluates these deficiencies, publishes the goals.

Then the Defense Department would establish control records on the goals and recommend projects thereunder for certification.

The certification is recommended by the delegate agency in each case which is concerned with the area involved in the expansion goal.

Then the progress under the expansion goal is monitored by the Office of Defense Mobilization.

ONE-MAN CONTROL

Senator MALONE. Mr. Chairman, my question went to the heart of the subject, and that is: Who is the final judge?

Mr. GRAY. Well, under——

Senator MALONE. As to who gets the short amortization periods?

Mr. GRAY. Well, Senator——

Senator MALONE. The accelerated amortization periods.

Mr. GRAY. As it operates at the present time, the responsibility is that of the Office of Defense Mobilization. Final responsibility——

Senator MALONE. Your first answer was correct, and that is that you, as Chairman of the Board—how many are members of the Board?

Mr. GRAY. Senator, I don't know whether you have reference to the Defense Mobilization Board, but it itself does not pass upon the individual applications.

Senator MALONE. What is the Board of which you are Chairman?

Mr. GRAY. Well, one board of which I am Chairman is the Defense Mobilization Board.

Senator MALONE. What is the other one?

Mr. GRAY. There are various committees in Government, but there is no board as such that passes on these individual applications.

Senator MALONE. Then you are the sole judge?

Mr. GRAY. It is my responsibility as it now operates.

Senator MALONE. Then I just want this short answer:

After you receive recommendations, you may ask a Senator for recommendations—you may ask a governor for recommendations—you may ask all of the Cabinet members for recommendations—but after you receive all these recommendations, you are the sole judge as to who may be designated for the accelerated amortization payments in all fields included in the legislation?. You are the sole judge?

Mr. GRAY. I would repeat that the basis upon which applications are considered is a process in which other Government agencies have an important and serious responsibility.

There are limitations in terms, quantitative limitations on the number of, or the capacity created by the applications to be filed.

But when these applications are filed and have been processed, it is my responsibility, if they are granted or not granted.

Senator MALONE. Could you just answer my question "Yes" or "No"?

After all the evidence is in, after all the recommendations come in to you which you have requested, then you are the sole judge as to who shall receive the accelerated amortization advance?

Mr. GRAY. Well, I have said, sir, it is my responsibility.

Senator MALONE. I understand what you have said, but you make the decision yourself?

Mr. GRAY. That's right, sir.

Senator MALONE. That is all we need.

I say to you, I think it is too much responsibility to allow any one man to take because I don't think any one man or group of men can think through the ramifications and the economic factors set in motion by such actions.

Now, you yourself, call in your advisers. You have advisers in various fields?

Mr. GRAY. That's right.

Senator MALONE. Some are a part of your staff; they are under you; they do what you tell them to do, do they not? That is, if you have the information and knowledge to direct it, and when they bring in a recommendation just like a Senator's staff, he is the final judge. Isn't that right?

Mr. GRAY. That's right.

Senator MALONE. I think it is too much responsibility, Mr. Chairman, for any one man to have.

I think it has been amply demonstrated over the years through the reckless use of the "short" amortization period concessions.

The CHAIRMAN. Mr. Gray, I would like to ask this question specifically directed at the Idaho Power Co.:

Did you make a survey that would indicate that additional power was needed in that particular area for defense purposes?

Mr. GRAY. I did not personally make a survey.

The CHAIRMAN. Did your organization do it before you granted the certificate?

Mr. GRAY. The processes under which the expansion goal was originally established; yes, sir; did involve a survey of power requirements throughout the country and when there was established in September, I think, of 1955, a goal of 150 million kilowatts of power——

The CHAIRMAN. In that particular area?

Mr. GRAY. No, this was for the Nation.

The CHAIRMAN. Was there any investigation made that would indicate that the construction of this particular utility was necessary for the defense needs of that area?

Mr. GRAY. It was considered, the expansion goal was considered necessary to meet the defense needs of the Nation.

The CHAIRMAN. But the Nation is one thing and that particular area is another.

These are power companies, and supply power over the Nation. You must think there is a need in that particular area that is to be served by this particular company?

Mr. GRAY. I think it was clear that there was and is a need for increased power in that particular area.

The CHAIRMAN. For what purposes? Defense purposes? You wouldn't have any right to grant them for any other purposes.

Mr. GRAY. That's right, sir, for the requirements not only of defense industry, but what would be the defense requirements if we became involved in an emergency.

The CHAIRMAN. Could you furnish the committee with a statement of the defense plants in that area which required this additional power to be furnished by the Idaho Power Co.?

Mr. GRAY. I will furnish the committee with a statement of defense considerations.

The CHAIRMAN. I am surprised to know that that investigation was not made before this particular amortization was granted.

Mr. GRAY. The investigation was made, Senator.

The CHAIRMAN. On a nationwide basis, as I understand you, we know that a single power company doesn't serve the whole Nation. It serves an area.

Mr. GRAY. That is correct, sir.

The CHAIRMAN. So we wanted to break it down to that particular area.

Now, Mr. Gray, did you take into consideration that a power company, a public utility, is guaranteed a reasonable return on their investment?

Mr. GRAY. Senator, may I speak to that Idaho Power case, and I think I will cover the question you have?

The CHAIRMAN. I would like for you to cover these particular questions.

I want you to cover the question as to whether a power company needs a subsidy from the Government. This is a subsidy; you will admit that?

Mr. GRAY. I wouldn't so characterize it as a subsidy.

The CHAIRMAN. I wouldn't know why you wouldn't so characterize it, because you charge off the cost of your plant in 5 years and thereby get the use of tax money that otherwise would have gone to the Government. Mr. Humphrey testified that the Government has lost $3 billion.

Senator MARTIN. The interest.

The CHAIRMAN. The interest was lost.

Senator KERR. Would the chairman yield for one suggestion there?

The distinguished chairman has referred to the witness as having made no investigation.

I believe Mr. Gray didn't go into his position until March of this year.

The CHAIRMAN. I was speaking, Senator, of the organization. I realize Mr. Gray has just come in, but this is a continuing organization.

Mr. GRAY. Yes, sir.

The CHAIRMAN. I understand that you based your actions on something that was done before you came in and I want to know whether

anybody made such an investigation as to whether the area covered by the Idaho Power Co. required additional power for defense needs.

I should think that you would admit that unless such a condition existed, it was not justifiable under the law to make this concession.

Now, I want you to explain why you think when a company is permitted to deduct taxes in a manner not accorded other companies, and thereby gets the use of that money, it is not a subsidy.

Who is benefited? Three billion dollars that the Federal Government has lost in interest.

Mr. GRAY. I don't know about the $3 billion; $3 billion is not my figure.

The CHAIRMAN. You say it is not a subsidy. You contend that these rapid amortizations are not subsidies in the sense that they are special benefits, that they give special benefits to special industries?

Mr. GRAY. I would certainly agree that they are an inducement because otherwise there would be no value in the program whatsoever.

The CHAIRMAN. I don't know the difference between inducement and subsidy. Somebody has gotten advantage of the Government to the extent of $3 billion in interest.

Mr. Humphrey testified to that. Somebody has gotten the benefit of that. The Government has lost it, lost it forever. There is no question about that.

Mr. GRAY. I am not competent to challenge Mr. Humphrey's figures. I don't say that they are wrong but I do point out, Senator, that after 5 years when the depreciation has been completed accelerated and amortized, then the taxes paid are higher than they are during the 5-year period and are higher than they would be under a long amortization period.

The CHAIRMAN. That is true, Mr. Gray, but the company gets the advantage of it to begin with. It gets the use of the money. The Government loses the use of the money. There is no question about that at all.

Senator MARTIN. Would you yield a moment, Mr. Chairman?

The amount of that, it is not necessary for, we will say, a utility company to go to the public for that amount of financing. They can just deduct that amount of financing. It saves them that much.

The CHAIRMAN. Another question. Did you take into consideration the fact that this construction has been going on for 6 months before you granted this subsidy or whatever you call it? Did this company contend it was necessary to get this particular concession in order to finance this project or not?

Mr. GRAY. I don't think they did make that contention.

The CHAIRMAN. How did the company contend it was entitled to this concession? If you don't like the word subsidy—we will call it a concession.

Senator GORE. May I interject there?

The CHAIRMAN. What was the basis of the application? Don't they make an application in detail and give some justification for this benefit?

Mr. GRAY. That's correct, sir.

These applications were originally filed in 1953.

Senator GORE. Mr. Gray, may I point out there just this: That the Federal Power Commission did not grant permission until 1955, so you acted according to that, you acted upon an application that was filed some 2 years before the company could legally engage in the development of this project?

Mr. GRAY. It was filed properly under an expansion goal which was open at the time, Senator. When the expansion goal was reopened, in 1955, these applications were taken into account in determining the total expansion goal which would have to be met, and were figured into the expansion goal and against its closing when it was closed.

Senator GORE. You took into consideration, even though it was filed before the company had a license to develop the project?

Senator KERR. I think the license had been granted before it was regarded as a part of that, that it was adequate, whereupon the classification was closed; wasn't it?

Mr. GRAY. The classification was closed when the goal was met. These two applications had been figured in toward the total of meeting the goal, and the application was not granted until, oh, a couple of weeks, 3 weeks ago.

Senator KERR. But the license for the project had been granted prior to the date that you accepted it as being a viable and therefore to be regarded in the matter of keeping open or closing the applications for that particular classification.

Mr. GRAY. That is correct, Senator.

Then, as you will recall, there was litigation involving the construction of these projects, or the licensing of these projects, which was not terminated until, I think, April 1 of this year.

It was not completed until the first of this year, when the Supreme Court declined to review the case. Therefore, the legal questions had been disposed of.

When that came to my attention, this was a pending application which had not been acted upon. Since it was the only remaining one under electric power generation, and since it had been considered in filling the expansion goal, and since the application had been filed in the appropriate time, and since it met the conditions which were imposed by the goal, and since over 900 similar applications had been granted in the period of the program—all having met these requirements, I saw no basis on which a certification should be withheld.

Senator GORE. Then, am I to understand that you granted this great benefit because you thought that they were entitled to it for the reason that other concerns had obtained it, and not because such a benefit, concession, or subsidy, was necessary to bring about the development of the project?

Mr. GRAY. The determination had been made that there was a need for power expansion.

Senator GORE. We understand that, but this expansion was already underway 6 months before you granted this benefit.

Mr. GRAY. That's right.

There have been many certificates granted, Senator, in this program after construction has been started.

In part, that has been due to the need for urgency for development of these facilities. You have to remember that when this program was conceived, and was a very large operation, we had quite a different kind of atmosphere than we have today.

This is one reason why administratively this program has been so sharply narrowed and curtailed.

But you cannot look at this expansion goal and need for it as of May 1957 without taking into consideration all of the factors and circumstances existing at the time that the Federal Government indicated that it wished power expansion to take place.

Senator GORE. To ask you a specific question, did you grant this certificate on equitable consideration, or because, in your considered opinion, it was necessary to bring about the development of this project?

Mr. GRAY. I would say that I was largely motivated by equitable considerations.

Senator GORE. Going back to the question asked earlier, that this company is entitled to this great benefit, just as all other power companies were entitled to it.

Senator, there could be no other power company now entitled to it because there is no program for the expansion of electric power.

Senator KERR. No applications have been eligible since a certain time in 1955, have they?

Mr. GRAY. No applications could have been considered after December 1955.

Senator KERR. That is, no application filed subsequent to that date?

Mr. GRAY. That's right, sir.

The CHAIRMAN. But the law is the law.

Mr. GRAY. Yes.

The CHAIRMAN. The law today is as it was in 1955.

What you are talking about is some policy that was established by your agency?

Mr. GRAY. Under the law.

The CHAIRMAN. The question is whether that policy is a just one when it denies these same privileges to other power companies.

I am not opposed to it at all—don't misunderstand me. There may have been other power companies with legitimate reason to get this rapid amortization on account of some defense plants in their vicinity, which apparently this policy of yours completely ignores.

Was this plant required to produce power needed for additional defense requirements in that locality?

Mr. GRAY. The decision was made, Senator, that the expansion of power was needed for defense purposes, and these two applications were specifically figured in to the meeting of the goal which was established and which has been closed.

The CHAIRMAN. I asked you to furnish the committee specifically the defense industries that required this additional power.

Senator MARTIN. Mr. Chairman, if you would yield there, could you also include the posts, stations, camps, and so forth of the Army, Navy, and Air Force that might require additional power?

(The following was later received for the record:)

Because of the unprecedented increase in the demand for electric power after the outbreak of hostilities in Korea in 1950, the Defense Electric Power Administration in the Department of the Interior developed in 1951 a power-expansion program. The three objectives of the program were summarized by the Defense Electric Power Administration as follows:

1. To serve the superimposed defense requirements.
2. To serve the rapidly increasing civilian load without curtailment.
3. To restore an adequate capacity margin for maintenance and emergency outages and for unscheduled additions.

The study disclosed that the power consumers who were planning sharp increases in their requirements were the Atomic Energy Commission and certain

industries in the process of major expansion, such as aluminum, steel, chemicals, and various nonferrous metals. The estimated expansion for the Atomic Energy Commission was 1,900,000 kilowatts. For aluminum expansion 1,500,000 kilowatts was needed.

On December 31, 1951, the overall power capacity of the country was 75 million kilowatts. At that time the Joint Committee on Defense Production ordered an investigation of the electric power program to determine its adequacy to support defense mobilization needs, and an Electric Power Advisory Committee was appointed by the Defense Production Administration to "inquire into the country's requirements for electric power and energy for defense and other purposes."

As a result of these studies, expansion goal No. 55 was established in March 1952 calling for an increase of 32 million kilowatts by December 31, 1954, above the December 31, 1951, national capacity of 75 million kilowatts.

Under final revision, on April 15, 1955, the goal was increased to 150 million kilowatts to be available by December 31, 1958; double the power capacity of the country 7 years earlier. Applications filed after December 31, 1955, were not eligible for certification.

Because of interconnections in the power grid system that covers the Nation, regional shortages such as were reported in all the studies that preceded the goal—the northwest area in particular—were not given preferential consideration. This was based upon a Department of the Interior position that powerplants in any area are equally valuable for defense.

Idaho Power Co.'s system is an integral part of the interconnected Northwest power pool, the resources of which now include the systems of Idaho Power Co., Utah Power & Light Co., the Montana Power & Light Co., Pacific Power & Light Co., Washington Power Co., Puget Sound Power & Light Co., Portland General Electric Co., together with the municipal systems of the cities of Seattle and Tacoma, Wash., and the Bonneville-Grand Coulee system of the United States of America.

The Brownlee and Oxbow projects of the Idaho Power Co. will serve major electric loads in the Pacific Northwest, including military posts, Atomic Energy Commission installations and defense plants. (See attached list.)

The major contribution of Idaho Power Co. to the Northwest Power Pool will commence immediately upon completion of the Oxbow and Brownlee projects, presently frecast for the end of 1958. The table below (taken from information submitted by company) shows both the peaking or emergency contribution of the certified facilities for the years 1959 through 1963 and average or continuing contribution from these two projects to the overall power supply of the Northwest:

Year	Peaking or emergency contribution	Average or continuing contribution
	Kilowatts	*Kilowatts*
1959	464,000	288,000
1960	369,000	202,000
1961	304,000	137,000
1962	284,000	114,000
1963	237,000	80,000

The Northwest power pool, having 90 percent of the total power generation in the Northwest, operates virtually as a single system in its service of electric energy to the consumers of its area. Its operations are so interdependent upon the various company systems within the pool that an adverse condition in one section is shared throughout the entire area, and vice versa.

When the bulk of the Northwest pool is low on both water and energy, the Idaho Power Co. will be in a position to supply the total amount of its peaking surplus to the pool (which is the major amount shown above) and at the time when most needed. The certified installations of Idaho Power Co. are the only major generating facilities in the entire area which have any surplus to supply during the critical winter period of the pool system.

Conditions experienced this past winter have served to illustrate the above. On January 27, 1957, Bonneville Power Administration was forced to discontinue service entirely to all interruptible industrial loads aggregating approximately 490,000 kilowatts, resulting in the loss of 7 aluminum potlines in the area, as well as thousands of kilowatts to other interruptible power consumers. Had

the Brownlee and Oxbow plants been in operation at that time the bulk of this power could have been made up by the Idaho Power Co., thus in effect making the interruptible power of the Northwest firm.

EXECUTIVE OFFICE OF THE PRESIDENT, OFFICE OF DEFENSE MOBILIZATION

Defense plants and military installations served by Idaho Power Co. and the Northwest power pool

Company	Location	Product
Navy Ordnance Plant	Pocatello, Idaho	
Mountain Home Air Force Base	Boise, Idaho	
National Metallurgical Corp	Springfield, Oreg	Silicon and aluminum-silicon.
Buffalo Electro Chemical Co	Vancouver, Wash	Hydrogen peroxide.
Larson Air Force Base	Ephrata, Wash	Air Force Base.
Boeing Aircraft Co	Moses Lake, Wash	Aircraft testing.
Do	Everett, Wash	Aircraft tooling.
Do	Seattle, Wash	Aircraft construction.
Allied Chemical Co	Kennewick, Wash	Nitric acid.
Howe Sound Co	Holden, Wash	Copper and Zinc Concentrating.
Radar Station	Neah Bay, Wash	
Salt Lake Pipe Line Co	Pasco, Wash	Transportation of petroleum products
Tidewater Terminal Co	East Pasco, Wash	Tank farm.
Nike installation No. F-37	Medical Lake, Wash	
Pend Oreille Mines & Metals	Metaline Falls, Wash	Lead and zinc.
Snohomish Co. Airport (Paine Field).	Everett, Wash	Aircraft overhaul.
Standard Oil Co	Richmond Beach, Wash	Petroleum products.
Umatilla Ordnance Depot	Ordnance, Oreg	
American Zinc, Lead and Smelting Co.	Metaline Falls, Wash	Lead and zinc.
U. S. Naval Station	Tongue Point, Astoria, Oreg	
U. S. Naval Radio Station	Oso, Wash	
Naval Supply Depot (Velox)	Spokane, Wash	
Maritime Administration	Vancouver, Wash	Shipyard.
Fairchild Airbase	Fairchild, Wash	
Aluminum Company of America	Vancouver, Wash	Aluminum.
Do	Wenatchee, Wash	Do.
Anaconda Aluminum Co	Columbia Falls, Mont	Do.
Kaiser Aluminum & Chemical Co	Spokane, Wash	Do.
Kaiser Aluminum & Chemical Co (rolling mill).	do	Do.
Kaiser Aluminum & Chemical Co	Tacoma, Wash	Do.
Reynolds Metals Co	Longview, Wash	Do.
Do	Troutdale, Oreg	Do.
Carborundum Co	Vancouver, Wash	Abrasives.
Electro-Metallurgical Co	Portland, Oreg	Ferroalloys. Calcium Carbide.
Hanna Nickel Smelting Co	Riddle, Oreg	Ferronickel.
Keokuk Electro Metals Co	Rock Island, Wash	Ferrosilicon.
Pacific Carbide & Alloys Co	Portland, Oreg	Calcium carbide.
Pacific Northwest Alloys Co	Spokane, Wash	Ferrochromium.
Pacific Salt Manufacturing Co	Portland, Oreg	Chlorine, caustic, chlorates.
Victor Chemical Co	Silver Bow, Mont	Phosphorus.
Atomic Energy Commission	Hanford, Wash	
Camp Hanford	do	
Anaconda Copper Co	Anaconda, Mont	Ferroalloys, zinc.
Do	Great Falls, Mont	Copper.
Fort Lewis	Tacoma, Wash	
McChord Field	do	
Portland Army Airbase	Portland, Oreg	
Ohio Ferro-Alloys	Tacoma, Wash	Ferroalloys.
Hooker Electrochemical Co	do	Chlorine, caustic soda.
Bethlehem Steel Corp	Seattle, Wash	Steel.
Electric Steel Foundry	Portland, Oreg	
Willamette Iron & Steel	do	Shipbuilding.
Tacoma Smelter	Tacoma, Wash	
Westvaco Chemical	Pocatello, Idaho	Phosphates.
Bunker Hill & Sullivan	Kellogg, Idaho	Zinc and lead.
Rohr Aircraft Co	Everett, Wash	Parts for airplanes.
Iron Fireman	Portland, Oreg	Electronic equipment.
Tektronix, Inc	do	Do.
General Petroleum Corp	Ferndale, Wash	Petroleum refinery.
Shell Oil Co	Anacortes, Wash	Do.
Puget Sound Navy Yard	Bremerton, Wash	
Pacific Car & Foundry	Renton, Wash	
Pacific Salt Manufacturing Co	Tacoma, Wash	Chlorine, caustic soda.
Monsanto Chemical	Soda Springs, Idaho	Phosphates.
Atomic Energy Commission	Arco, Idaho	

The CHAIRMAN. That is defense, all of it is defense.

Senator FREAR. One question, may I ask, Mr. Chairman, that I think is important.

I am not sure that I am sufficiently well acquainted with this. You have the power—you, as the Chairman of ODM—you have the power, do you not, not only to say that this is the goal today, but you can say that in some future date power may be needed in this area for which you have granted a certificate to the Idaho Power Co. It doesn't have to be on paper today, according to what I understood you to say earlier, but you have authority for future expansion and you can say that in this area of Idaho Power & Light, or whatever it is, that in the next 10 years there will be need for the national defense in that area. There may not be today.

Do you have that power or do you not?

Mr. GRAY. I think the legislation is probably broad enough, Senator, to enable such a decision, but you have to recall that under this legislation, I am acting under delegated authority, but I would also remind the committee, I think it is true, that all these considerations—I shouldn't say were debated in this committee, because I was not here or familiar with the program—but many of these considerations which we are discussing existed in 1950 when the present law under which we are operating was passed by the Congress.

So, this isn't something that——

The CHAIRMAN. Mr. Gray, I would like to interrupt you there. When that law was passed, I thought it was intended completely and solely for defense purposes, but now you tell me that you act on some kind of a nationwide goal basis that does not take specific plants into consideration.

Mr. GRAY. Senator, the expansion under this program for the total mobilization base involved a great many areas, including electric power which, in time of emergency, is clearly, certainly, one of the greatest needs for defense purposes.

I would point out to you that in order to meet an emergency, there are many things you can stockpile. We have stockpiled billions of dollars worth of critical materials. You cannot stockpile electric power.

This becomes very vital; in fact, the economy of the country would not be viable at all in time of emergency with an inadequate amount of electric power. It cannot be said that every one of the tax certificates which has been granted in this program over a period of years is producing a specific item for the use of the military. Nevertheless, in terms of the total defense of the country this goal was a part of a large program which was very useful, I think, in the Korean emergency.

The CHAIRMAN. Let me interrupt you again, sir. The history of this rapid amortization is this: In World War I, we had it. It was repealed immediately after.

In World War II it was again in operation. It was repealed immediately after that.

This is the first time that it has extended for practically 3 years in times of peace.

This has never occurred before in this country.

When you say it has been greatly curtailed, I want to give you these figures.

Since 1953, when the Korean war ended, there has been 6,000 certificates of necessity issued covering investments of $13 billion and tax writeoffs of $7 billion. That is in time of peace.

Now, that is contained in the report by the staff of the Joint Committee on Internal Revenue Taxation. I am sorry you have not read this report. I was surprised when you came to see me in my office the other day that you had not seen it.

There is also correspondence about this matter. There is correspondence with Mr. Flemming in which as chairman of the Finance Committee, I requested him to hold up these matters pending investigation. The joint committee staff report was submitted to the Congress on December 31. I have a letter from Mr. Flemming giving me to understand these matters would be held up. They were not.

I am much concerned about this because I think in time of peace a great deal more caution should be used about giving special benefits to special industry. So, when you say the program has been curtailed considerably, the fact is, use of the program in peacetime is new, and 6,000 certificates have been issued with tax writeoffs of $7 billion.

Senator GORE. Mr. Chairman, I would like to ask a question of the chairman.

It may be that my memory is faulty. I am sure the memory of the chairman is much better.

Does the chairman recall that at any time in the debate or discussion of this legislation, this law, that one of the goals of it would be the granting of benefits on equitable considerations?

The CHAIRMAN. No, sir, completely on the question of national defense.

Senator CARLSON. Mr. Gray, did you not give, or that is, your Office, Defense Mobilization, give consideration to tax amortization or accelerated depreciation to companies that would move into areas with large unemployment and, if so, how many during this period?

Mr. WYCKOFF. We are given a list by the Labor Department of the labor surplus areas and we have offered within the expansion goals that were then open to give a premium at the request of the Labor Department for any applications that were eligible for certification.

Senator KERR. In that area.

Mr. WYCKOFF. In any chronic labor surplus area.

A number of certificates have been issued for such areas at premium percentages as an inducement.

The CHAIRMAN. On the basis of defense?

Mr. WYCKOFF. Always within an expansion goal.

Senator FREAR. But expansion goals have been reopened. I mean your goals haven't been closed all the time. You have reopened your goals and reconsidered them and made different goals; have you not?

Mr. WYCKOFF. We have never reopened an expansion goal that was closed.

Senator CARLSON. May I inquire further, Mr. Chairman, along the same line.

Do I understand from Mr. Gray's statement or Mr. Gray, do I understand you now that in view of your recent statement there would be no certificates of tax amortization granted even though there were labor unemployment areas unless it met these particular 5 or 8 projects for which the goals are open now?

Mr. GRAY. Senator, I am not sure about the depressed area.

Mr. Wycoff, would we grant one on a depressed area basis, that was out of an open goal?

Mr. WCKOFF. Never, that I know of.

Mr. GRAY. I think the answer—I am sorry, Mr. Chairman, you have asked me a lot of questions which go back in the history of the program which I have to frankly confess I am not altogether familiar with, but I should like, if I may, to respond to this suggestion that the debate did not authorize the granting of a certificate purely on equitable considerations.

I believe that the use of the word "equitable" was involved in the question which was put to me in regard to various considerations that went into the granting of these certificates.

I should like to repeat that these certificates were properly filed. They met the goal established. They were the only ones involved, which had not been granted to people similarly situated.

It was partially on the basis of these pending applications that the goal was closed. Under all these considerations, including those of an equitable nature, they were going to meet the advance date of furnishing the extra power which was required; that is, by December 1958, that they were properly dispersed, and a number of other considerations—they met the requirements for granting the certificates.

I said that equitable considerations entered into it on the basis that nobody else who met these criteria, which were clearly established and published had been denied.

I don't think that, frankly, the Idaho Power certificates can be considered alone out of the context of the whole electric-power expansion program.

Now, whether electric power companies should have been involved in this program is quite a different matter. It was determined a good long time ago that this would be a basis for the granting of tax amortization and these certificates met the considerations which had been applied.

So I feel that I am entitled to say that this was not simply an equitable decision. It was a consideration of equity along with all of these other considerations of requirements which these certificates had met.

Senator FREAR. Mr. Chairman, I hate to follow this, but the gentleman here, the staff member, said that you had never reopened an expansion goal; is that right?

Mr. WYCKOFF. We never have reopened an expansion goal which had been closed.

Senator FREAR. Have you ever had a suspension of goals, then?

Mr. WYCKOFF. Yes.

Senator FREAR. What happened in that case? Couldn't you use it the same as a determination for expanding the goal?

Mr. WYCKOFF. The power goal was suspended for a period of time while it was under study and then it was reopened, but it had not been closed.

Senator FREAR. Then it gave you——

Mr. WYCKOFF. I think it was one of the very few that was ever suspended.

Senator FREAR. It may have been, but it accomplished the purpose for which we are trying to find an answer here now.

What would happen, Mr. Gray, if, in your decision, you decided that a particular area—I don't like to use this Idaho Power because I think there are other examples, but we will use it as long as it is here before us now, and you decided, and I think you had the authority to—I am frank to admit—that you could say in this area out here, "We need a new aluminum plant; we need a new steel plant out there, because it is out of the area somewhere, not in the bombing target of the enemy"—there are many different reasons you could give, and it is within your power to say that within the next 10 years we can profitably locate in this area, so therefore you have the authority to grant this rapid amortization because, in the future, you may think this area would be in the interest of national defense a place for a steel or aluminum plant, even a jet engine plant. Is that true?

Mr. GRAY. I think that in the administration of this program there has never been a time when individual applications were considered without regard to a study of the needs of the country for defense purposes, for the facilities in whatever area it would be. I cannot conceive of a situation where I would unilaterally determine that a company was entitled to a rapid tax amortization and just grant a certificate offhand in that way.

Senator FREAR. You may not utilize it, but you say it is within your power, your authority?

Mr. GRAY. To give a legal opinion on that, I would like to call the lawyers, but it never occurred to me that there was such power because I don't think anybody would ever seek to use it, sir. I hadn't addressed myself to this question.

Senator KERR. Mr. Gray, let me see if I can——

Senator FREAR. You think a certificate should be a certificate of rapid amortization, it should be made available to any facility, anywhere—that, for instance, the jet engine, an experiment in jet engines, and certainly that would be classified as national defense as far as you were concerned, and this committee, too, I think. Would think a certificate should be available for a facility to meet a subcontract on a jet engine basis, for jet engines.

That is, a research in a new jet engine, let us say.

Mr. GRAY. I think that would be permitted under Senator Byrd's bill.

The CHAIRMAN. You are mistaken about that, Mr. Gray. It says "new defense items." That is not new. This may be to produce new defense items or component parts of new defense items.

Mr. GRAY. I don't know how you define what is new in defense, Senator. This is one of the technical matters, amendments, which I would hope you would give us an opportunity to discuss with you.

The CHAIRMAN. Maybe we had better consider this a little, if you say jet engines are new. They have been in operation for some time.

Mr. GRAY. I would say this, Senator, to this question: If we had a military requirement for vastly increased numbers of a particular military item, let us say it is a jet bomber, and if there were not adequate facilities to meet this defense requirement, I would think that it would be well to be in a position to encourage the development of industrial facilities for that item. Now——

The CHAIRMAN. Jet planes are used for private purposes peacetime, too.

Mr. GRAY. I am talking about a particular military plane, sir. If we had legislation which said that because jet planes are not new, and therefore we could not increase the expansion of a plant which was solely for the purpose of selling, furnishing to the military department, this particular item—that is, a jet bomber—then I think it would be too bad not to have the authority not to grant the tax amorization.

The CHAIRMAN. Isn't it true, though, Mr. Gray, that these new methods, weapons, and so forth, are built on a cost-plus basis? There is no risk involved. There is no risk to those who build these new planes. They are all built on a cost-plus basis by the Government.

Senator KERR. That is the building program, though, Mr. Chairman. I think the witness is talking about a research project.

The CHAIRMAN. The bill provides for research.

Senator KERR. That would be used to find an improved way to produce that which is being produced, or an improved facility better than those being produced.

I think that is what the witness said.

Mr. GRAY. Or a facility which would meet direct defense requirements in procurement of military end items, for example.

Mr. Chairman, I would like to——

Senator GORE. Before we leave that, I know of no program in the Government that is more subject to cost-plus contractual relationship than research contracts.

Mr. GRAY. I would point out that some of these programs, Mr. Chairman, especially in defense procurement, may involve the procurement of items which potentially have an expectancy of obsolescence. Technological progress is such that weapons that we thought were good weapons in World War II are not even in use any more.

One reason, it seems to me, for encouraging or giving an inducement to a plant to get into the production of a particular item of that sort is that there isn't any long-range foreseeable demand for it.

Senator GORE. Mr. Gray, what more inducement does the concern have in a facility or need to get it into an activity than to have a cost-plus-fixed-fee contract with the Government?

What additional inducement, what additional subsidy, what additional benefits would a company require?

Mr. GRAY. If a company has a present plant capacity and enters into a cost-plus contract, I would agree that if the capacity is there to meet procurement requirements, there isn't any point in talking about a further inducement. What we are talking about is a facility needed for production.

Senator KERR. Which is not built under a cost-plus arrangement. That is what you are talking about?

Mr. GRAY. That's right, sir.

Senator GORE. I understood you to be talking about research contracts.

Mr. GRAY. I thought we were talking about procurement for military purposes. Research and development is another area in which I feel that there should be continued authority to grant tax amortization when it is for military purposes.

Senator MALONE. Mr. Chairman, I would just like to say before I ask this next question that I think this Board, of which Mr. Gray is the present head, is the greatest centralization of power in the history of this Nation.

It is a question, then, whether it should be all centered in one board.

Now, I wanted to ask Mr. Gray:

Aren't you, as Chairman of this Board, or whatever it is, the sole judge of the goals that are set in each area?

Mr. GRAY. No, these goals are set only on recommendation of the delegated agency affected, Senator.

Senator MALONE. But I will ask you again. You make the decision on the evidence that you obtain?

Mr. GRAY. Yes, sir.

Senator MALONE. But you make the decision and you are the sole judge of the evidence?

Mr. GRAY. Well, I come back to my earlier answer to you. It is my responsibility, but in the exercise of that responsibility there is a participation by the portion of the executive branch of the Government which has a responsibility in the area under consideration.

As I pointed out, the Defense Department——

Senator MALONE. I asked the question once more and to save time, I wish you would answer it.

After you have secured all the advice that you care to ask for, among your Cabinet officers, then you are the sole judge, you make the final decision after you have secured all of the evidence from the Cabinet officers you can get?

Mr. GRAY. Subject to the procedures and regulation by the President, it is my responsibility.

Senator MALONE. What are those regulations?

Mr. GRAY. They are the procedures which we have, under which various steps are taken in the process of identifying deficiencies, establishing goals, establishing criteria, and finally, granting the application.

Senator MALONE. Is there any written rule or anything that you have not so far furnished this committee that would prevent you from making the final decision?

Mr. GRAY. I don't know any rule that would prevent me from making final decisions, but the regulations which I referred to I shall be glad to submit for the committee.

(The following was later furnished for the record:)

[Reprint from the Federal Register of February 9, 1954]

TITLE 32A—NATIONAL DEFENSE, APPENDIX

Chapter I—Office of Defense Mobilization

[ODM Regulation 1]

ODM REG. 1—ISSUANCE OF NECESSITY CERTIFICATES UNDER SECTION 124A OF THE INTERNAL REVENUE CODE

The following regulations are hereby prescribed by the Office of Defense Mobilization with the approval of the President pursuant to the authority contained in Executive Order 10480, dated August 14, 1953, and section 124A of the Internal Revenue Code.

Sec.

1. Definitions.
2. Criteria for determination of necessity.
3. Criteria for determination of portion of the adjusted basis attributable to defense purposes for computing the amortization deduction.
4. Procedures and responsibilities.
5. Exercise of powers of Certifying Authority.

AUTHORITY: Sections 1 to 5 issued under sec. 216, 64 Stat. 939; 26 U. S. C. Sup. 124A; E. O. 10480, Aug. 14, 1953, 8 F. R. 4939.

SECTION 1. *Definitions.* As used throughout this regulation:

(a) "Emergency facility" means any facility, land, building, machinery or equipment, or any part thereof, the construction, reconstruction, erection, installation or acquisition of which was completed after December 31, 1949, and with respect to which a Necessity Certificate has been made.

(b) "Emergency period" means the period beginning January 1, 1950, and ending on the date on which the President proclaims that the utilization of a substantial portion of the emergency facilities with respect to which Necessity Certificates have been made is no longer required in the interest of national defense.

(c) "Certifying Authority" means the Director of the Office of Defense Mobilization.

(d) "Necessity Certificate" means a certificate made by the Certifying Authority pursuant to section 124A (e) of the Internal Revenue Code, certifying that the construction, reconstruction, erection, installation or acquisition of the facilities referred to in the certificate is necessary in whole or in part in the interest of national defense during the emergency period, and stating the portion of the adjusted basis thereof which has been determined to be attributable to defense purposes within the meaning of such section 124A (e) for computing the amortization deduction under section 124A (a).

(e) "Material" means raw materials, articles, commodities, products, supplies, components, technical information and processes.

SEC. 2. *Criteria for determination of necessity.* Determination will be made by the Certifying Authority as to whether the construction, reconstruction, erection, installation or acquisition of the facility (in whole or in part) is necessary in the interest of national defense during the emergency period.

(a) *Material or service required for national defense.* In making the determination of necessity, a determination will be made that the material or service to be produced with the proposed facility is required in whole or in part in the interest of national defense during the emergency period. A material or service will not be found to be so required unless it is directly required for the Armed Services of the United States or auxiliary personnel, for civil defense, for the Atomic Energy Commission, or for any operations or activities in connection with the Mutual Defense Assistance Act of 1949, as amended; or unless it is necessary for the production of a material or service directly required in the interest of national defense during the emergency period; or unless it is otherwise necessary in the interest of national defense.

(b) *Shortage of facilities for the production of material or service required for national defense.* In making the determination of necessity, a determination will be made that at the time of the beginning of construction, reconstruction, erection, installation or acquisition of the facility, there was or is an existing or prospective overall shortage of facilities for the production of the material or service produced or to be produced by the facility sought to be certified. Consideration will be given to the necessity for and adequacy of facilities for the production of a material or service in a particular region, the necessity for stand-by capacity, and any other factors contributing to or threatening a shortage of facilities for producing such material or service. A shortage will be found to exist only with respect to facilities required to meet expansion goals determined by the Office of Defense Mobilization.

(c) *Other considerations.* In making the determination of necessity, consideration will also be given to other factors such as: new or improved technology; assurance of a fair opportunity for participation by small business; the promotion of competitive enterprise; the competence, performance record and other factors bearing upon the ability of the applicant to construct or acquire, and manage the proposed facility; location of the facility with due regard to military security and dispersion criteria and standards; the degree to which the facility will alleviate the shortage of production; other forms of financial assistance provided by the Government; and the availability of manpower, housing, community facilities, transportation and other factors of production. An existing or prospective shortage of facilities for the production of a material or service necessary in the interest of national defense will not be considered alleviated by:

(1) The acquisition of the productive assets of a going concern or secondhand facilities unless:

(i) Clear prospect of a substantial increase in the usefulness of such facilities for national defense exists and such increase cannot be obtained by other practical means; or

(ii) Substantial loss of usefulness for national defense would probably result in the absence of such acquisition.

(2) The construction, reconstruction, erection, installation or acquisition of that part of a facility which is or will be used in lieu of existing facilities, except to the extent considered extraordinary and necessitated by reason of the emergency.

SEC. 3. *Criteria for determination of portion of the adjusted basis attributable to defense purposes for computing the amortization deduction.* Determination will be made by the Certifying Authority as to the portion of the adjusted basis upon which the amortization deduction under section 124A (a) shall be computed.

(a) In determining the portion to be certified, the Certifying Authority will consider the probable economic usefulness of the facility after five years and the additional incentives to the minimum amount deemed necessary to secure the expansion of industrial capacity in the interest of national defense during the emergency period. For this purpose, consideration will be given to such factors as the character of the business, including the source, amount and nature of the materials required for the expansion and the material or service to be produced; the manufacturing or servicing processes involved; normal depreciation rates; expansion in competitive fields: the extent of risk assumed, including the amount and source of capital employed; the potentiality of recovering capital or retiring debt through tax savings or pricing; the relative expansion needed; the economic consequences of the location of the facility due to security or other emergency factors; increased costs due to expedited construction or emergency conditions; the historical background of the industry; the extent to which the facility is being or will be used in lieu of existing facilities; assistance to small business and the promotion of competitive enterprise; compliance wth Government policies, e. g., manpower and dispersion: and other relevant factors. Land will not ordinarily be certified. The percentage certified shall be closely related to the provision of other financial incentives provided by the Government to encourage the construction of facilities, such as direct Government loans, guarantees and contractual arrangements, so that these incentives separately or in combination will secure the needed expansion at minimum cost to the Treasury. Where percentage certification patterns for individual industries are established, adjustments upward or downward may be made for special factors.

SEC. 4. *Procedures and responsibilities*—(a) *Application form.* Formal application shall conform to the standard form prescribed by the Certifying Authority and shall be executed in the manner and by the person prescribed by the form. The standard form of application for a Necessity Certificate may be obtained from the Office of Defense Mobilization, Washington 25, D. C., or from Department of Commerce field offices.

(b) *Classified information.* If the application or its filing would involve the disclosure of information which has a security classification, the applicant shall, prior to the filing of his application, request instruction from the Government agency with which he has classified contract relations.

(c) *Filing of application.* All applications for Necessity Certificates shall be filed with the Office of Defense Mobilization in Washington, D. C., and shall be deemed to be filed when received by that agency.

(d) *Time of filing applications, and cases in which determination of necessity must be made before beginning of construction.* (1) Application for a Necessity Certificate for facilities the construction, reconstruction, erection or installation of which was begun or which were acquired prior to March 1, 1952, or for facilities acquired on or subsequent to March 1, 1952, must be filed before the expiration of six months after the beginning of such construction, reconstruction, erection or installation, or the date of such acquisition.

(2) (i) Applications for Necessity Certificates for any building, structure or other real property, or for the installation of facilities which will become an integral and permanent part of any building, structure or other real property the construction, reconstruction, erection or installation of which is begun on or after March 1, 1952, must be filed prior to the beginning of such construction, reconstruction, erection or installation, except that,

(ii) An application for a Necessity Certificate for any building, structure or other real property or for the installation of facilities which will become an integral and permanent part of any building, structure or other real property the construction, reconstruction, erection or installation of which is begun subsequent to the closing of an expansion goal and prior to the reopening of such

expansion goal, must be filed before the expiration of 30 days after the reopening of such expansion goal. Certification in such cases may be made for only that part of any facility which is constructed, reconstructed, erected, installed, or acquired not earlier than six months prior to the date of filing of such application.

(3) (i) Facilities at any one location involving the construction, reconstruction or erection of any building, structure or other real property, or the installation of facilities which will become an integral and permanent part of any building, structure or other real property, and which are estimated by the applicant to cost $100,000 or more, excluding the cost of land, the construction, reconstruction, erection or installation of which is begun on or after March 1, 1952, and prior to December 3, 1953, will not be eligible for certification within the meaning of this regulation unless a determination of necessity is made by the Certifying Authority as evidenced by the issuance of a Necessity Certificate or a Letter of Predetermination prior to the beginning of such construction, reconstruction, erection or installation.

(ii) The term "Letter of Predetermination" shall mean a written communication to the applicant from the Certifying Authority stating that there is a shortage of the facilities for which certification is requested, that the material or service to be produced thereby is necessary in the interest of national defense, and that thereafter the beginning of construction, reconstruction, erection or installation of the facilities for which certification is requested will not in itself prejudice the applicant's eligibility for a Necessity Certificate.

(4) For purposes of subparagraphs (1), (2) (i) and (ii), and (3) (i) and (ii) of this paragraph, the following definition shall apply: Construction, reconstruction, erection or installation is deemed to begin with the incorporation in place on the site by the applicant or by any other person pursuant to any contract, understanding or arrangement, directly or indirectly for or with the applicant, of physical materials as an integral and permanent part of any building, structure or other real property (for example, the pouring or placing of footings or other foundations). Acquisition of land; engineering; contracting for construction; preparation of site; building of access roads; excavation; demolition; installation of service utilities required for construction; the fabrication, production or processing of building materials or building equipment; or the acquisition of personal property to be installed in the building, structure or other real property does not constitute beginning of construction, reconstruction, erection or installation.

(e) *Modification of regulations.* The provisions of this regulation concerning the filing of applications for Necessity Certificates may be changed by the Certifying Authority. Such change shall be made effective not less than 15 days after publication in the FEDERAL REGISTER.

(f) *Referral of applications.* Each application, after acknowledgement, will be referred to that agency or officer of the Government according to its respective assigned responsibilities under the Defense Production Act of 1950, as amended. The military department or other Government agency directly interested in the production of the material or service involved in the application for a Necessity Certificate shall on request of any agency or officer to whom the application has been referred, and may in any case, supply such information and advice as may aid the agency or officer in making his report and recommendation to the Certifying Authority.

(g) *Responsibilities of agencies and officers other than Certifying Authority.* Delegate agencies or officers of the Government to which an application is referred, shall be responsible for making a report and recommendation for specific action to the Certifying Authority regarding each application. Such report and recommendation shall be based upon a thorough examination and investigation conducted by the delegate agency or officer or by other competent Government agencies or officers. Such reports shall conform to instructions issued by the Certifying Authority.

(h) *Action by the Certifying Authority.* After consideration of relevant factors, including but not limited to the reports of the delegate agencies and officers of the Government, the Certifying Authority will take action upon the application.

(i) *Necessity Certificates.* Upon approval of an application, a Necessity Certificate will be forwarded to the Commissioner of Internal Revenue and will constitute conclusive evidence of certification by the Certifying Authority that the facilities therein described are necessary in the interest of national defense and of the portion of the adjusted basis upon which the amortization deduction under section 124A (a) shall be computed. The Certifying Authority will not certify the accuracy of the cost of any facility nor of any date relative to the

construction, reconstruction, erection, installation or acquisition thereof. It will be incumbent upon taxpayers electing to take the amortization deduction to establish to the satisfaction of the Commissioner of Internal Revenue the identities of the facilities, the costs thereof, and the dates relative thereto.

(*j*) *Further description after certification.* (1) Where the actual description or cost of a certified facility varies or will vary so materially from the description or cost in the application for a Necessity Certificate as to put in question the identity of the facility, the taxpayer may request an amendment of the certificate by filing a statement with the Certifying Authority setting forth the revised description or cost.

(2) The statement should consist of four copies of an amended Appendix A setting forth all of the emergency facilities certified with their revised descriptions or costs in the same order in which such emergency facilities were listed on the original Appendix A. However, where the original Appendix is lengthy and only a few variations or changes are involved, the four copies of the amended Appendix A may list only the facilities changed. In all instances, the amended descriptions or costs should be identified, by item and page number, with the descriptions or costs contained in the original Appendix A and should be accompanied by a letter explaining all changes with the reasons therefor.

(3) If the Certifying Authority is of the opinion that the varied or changed costs or descriptions are within the scope of the original certification, the amended Appendix A will be forwarded by the Certifying Authority to the Commissioner of Internal Revenue for substitution for the original Appendix A attached to the original certificate to have the effect of an amendment thereof. A copy of the amendment will be transmitted to the taxpayer.

(4) Although reasonable substitutions for facilities previously certified may be determined to be within the scope of the original certification, additional facilities, as a general rule, will not be considered to be within the scope of the original certification and will require a separate new application which may be subject to the provisions of paragraph (d) (3) (i) of this section. The Certifying Authority may, however, afford a filing date for such separate application which will correspond to the date on which the application for amendment was filed for the facilities found to be outside the scope of the original certification.

(k) *Cancellation or amendment of Necessity Certificate.* The Certifying Authority may (1) cancel any Necessity Certificate where it has been obtained by fraud or misrepresentation or has been issued through error or inadvertence, or (2) amend any Necessity Certificate for sufficient cause.

SEC. 5. *Exercise of powers of Certifying Authority.* (a) Any actions taken in exercise of the powers and authority vested in the Director of the Office of Defense Mobilization, by Executive Order 10480, dated August 14, 1953, under section 124A (e) of the Internal Revenue Code may be taken in the name of the Office of Defense Mobilization by the Director's authorized representative.

(b) The Director may for good and sufficient reason in the interest of national defense make exceptions to the requirements for filing in section 4 (d) (2) (i) and (ii) and the requirements of section 4 (d) (3) (i).

DPA Regulation No. 1, as amended, dated February 14, 1952, is hereby superseded.

Effective date: December 3, 1953.

ARTHUR S. FLEMMING,
Director of the Office of Defense Mobilization.

Approved: February 2, 1954.

DWIGHT D. EISENHOWER,
The White House.

[F. R. Doc. 54-906; Filed, Feb. 8, 1954; 8:51 a. m.]

Senator MALONE. What do they say, just roughly, and then will you furnish those regulations for the record, but what do they say in this regard?

I will be happy to yield. I would just like to know if he is not the final judge after all the evidence is in?

The CHAIRMAN. I think he has admitted that.

Senator JENNER. He said he was.

Senator KERR. Not only admitted it——

The CHAIRMAN. He has admitted it time and time again.

Senator KERR. Under the law he has to be. He didn't pass the law; he is just the captive of it.

Senator MALONE. I didn't say who passed the law. Are you the sole judge?

Mr. GRAY. Senator, under the law——

Senator MALONE. Which we passed, you are the sole judge, are you not?

Mr. GRAY. I have already said that it is my responsibility; yes, sir.

Senator MALONE. You are the sole judge, have the sole responsibility?

The CHAIRMAN. Let the witness say that he is the sole judge. Are you the sole judge or not, Mr. Gray?

Senator KERR. May I remind the committee that this witness has the right to answer the question on the basis of what he thinks the facts are?

Senator MALONE. I will keep on asking him. If the chairman would like to get it terminated—that under the law you are the sole judge, so to speak—you are the man who makes the final decision; is that correct or wrong?

Mr. GRAY. Under the law, and the delegations under the law, yes, sir.

Senator MALONE. You are the one that makes the final decision?

Mr. GRAY. Yes, sir.

Senator MALONE. You can laugh as long as you want to, but you are going to answer the question.

Mr. GRAY. Yes, sir.

Senator MALONE. I have another question, and I hope it doesn't take as long. You could, under your authority, at any time, expand these goals, I think?

Mr. GRAY. I think that is right.

Senator MALONE. Then the power of the entire Cabinet, including the Administrator of National Defense, the Department of the Interior, and all other power that formerly rested in those positions, in the matter of purchase, we will say, of critical materials for stockpile, you are the judge, the sole judge, after all the evidence is in, as to what should be purchased of critical materials for a stockpile. For example——

Mr. GRAY. Well, the Office of Defense Mobilization has the responsibility of determining the amount of critical materials which should be stockpiled.

Senator MALONE. Then you do, after receiving all the advice for which you asked from the Cabinet officers, then you make the final decision?

Mr. GRAY. That is right, sir.

Senator MALONE. That is better. We are improving as we go along. You mentioned 150 million of power. Does that mean in this particular area, or all over the United States?

Mr. GRAY. That was the general expansion goal for electric power.

Senator MALONE. Throughout the United States?

Mr. GRAY. Yes.

Senator MALONE. From what date?

Mr. GRAY. I think, Senator, that the date of this expansion goal which we have been discussing, of 150 million kilowatts was in August or September of 1955. I can get the date for the record, if you wish.

Senator MALONE. 1955. You are sure it was kilowatts?

Mr. GRAY. I think so.

Senator MALONE. You are to expand from 1955 in the United States, and in this field you could give short amortization periods to any companies participating in this expansion.

Mr. GRAY. To those which met the criteria established under the expansion goal, which, among other things, was to have the increased power called for available by the end of 1958.

Senator MALONE. It seems, Mr. Chairman, that that is a good deal of power. It would be about 150 Hoover Dams. There is 1,000 kilowatt-hours in a kilowatt. I just wanted the witness to be sure it was kilowatts he was talking about. We need, then, about, you need that many new Hoover Dams.

Mr. GRAY. The expansion goal of the 150 million kilowatts was established on April 15, 1955, Senator. I was in error about the date. Those who participated in the expansion under this goal ultimately had to make the expanded capacity available by December of 1958. This was the result of a review in which the Interior Department participated. The goal was agreed upon in consultation with the Department of the Interior in April 1955.

Senator MALONE. And it is 150 million kilowatts.

Mr. GRAY. That is right, sir.

Senator MALONE. How much of that has been allocated since that time?

Mr. GRAY. That goal was met, and there are no further applications for power eligible for consideration.

Senator MALONE. We have had an expansion of 150 million kilowatts of power since 1955?

Mr. GRAY. I will have to find out what the actual expansion has been and furnish that for the record, Senator. I do not know what the total expansion is.

Senator MALONE. But you are giving no further short amortization periods or encouragement to further plants in the United States?

Mr. GRAY. No, sir. That is right, sir.

Senator MALONE. Then you must have issued certificates for the 150 million kilowatts, if that was your goal, or you have reduced the goal. Which is it?

Mr. GRAY. Do you know exactly how much has been generated under the expansion?

Mr. WYCKOFF. At the time the original goal was established, I know there was less than 100 million kilowatts available of productive capacity in the United States.

Senator MALONE. So your goal was to more than double the capacity in the United States.

Mr. WYCKOFF. The 150 million kilowatts is an increase of something over 50 million kilowatts over what was available at the beginning of the program.

Senator MALONE. This 150 million kilowatts included.

Mr. GRAY. That is the total capacity.

Senator MALONE. Then you wanted 50 million kilowatts more?

Mr. WYCKOFF. More than 50.

Senator MALONE. How many kilowatts do you get on this Idaho Power amortization?

Mr. WYCKOFF. We will have to furnish that.

Senator MALONE. Then, Mr. Gray, would you furnish for the record not only the amount of kilowatts that you will secure in this latest amortization period that you granted Idaho Power Co., and you understand, Mr. Chairman, I do not understand thoroughly what part it is going to play in the national defense. Therefore, I am not criticizing that grant at all, but I would like the record to show the amount of kilowatts that you secured there, the amount of kilowatts that you secured since April 1955, in short amortization periods, and termination of the program.

Mr. GRAY. We will be glad to furnish that.

(The following was later furnished for the record:)

Since April 15, 1955, when the electric power goal was reopened and expanded to 150 million kilowatts, 13,131,300 kilowatts of productive capacity have been certified, including 512,100 kilowatts in the Brownlee and Oxbow projects of Idaho Power Co.

Senator MALONE. Mr. Chairman, I would like to say for the record that I think it is too much power to concentrate in any one board or one man, and from the witness' own statements, he is the sole judge of when you buy critical materials and to what amount, and the size of the stockpile, and it is something that, in my opinion, should be given back to the Cabinet officials and make them responsible for it, that understand the program.

This power is all centered in one man. We knew it was going to be. Some of us criticized it at the time when it was first passed and I think it was little understood, even by the Congress, and certainly not understood by the country, that one man in the White House could say when a critical material would be purchased and when it would not be purchased and to set goals, and then to choose between the companies as to who would get the short amortization periods to carry out the program.

Centainly not understood by the country and I think very little by the Congress.

Senator BENNETT. Mr. Chairman, may I ask the witness a question?

The CHAIRMAN. Certainly.

Senator BENNETT. I am sorry I had to be out of the room and you may have answered the question to someone else.

You talked earlier about the overall power goal of 150 million kilowatts.

Was that broken down in terms of regional goals or was it handled entirely as an overall total?

Mr. WYCKOFF. It was an overall total.

Mr. GRAY. This was a total capacity goal of 150 million kilowatts and was handled as an overall total, Senator.

Senator BENNETT. That was the question I wanted to get clear for the record.

Mr. GRAY. Mr. Chairman, may I just make, with respect to the bill itself—I had not finished saying what I would like to say about that—we got off into a discussion——

The CHAIRMAN. Sorry we interrupted you so much.

Mr. GRAY. First, the question as to whether this program has been curtailed or not, I think the record ought to show that there have been

in the history of this program 229 goals under which certificates were granted.

I have indicated that there are only eight open at the present time. I would like the committee to know how much is outstanding and eligible now.

Under the open goals, there is a backlog of 257 applications estimated to cost a total of $688 million; 243 of these 257 are eligible under the goals which I have described here earlier.

Senator BENNETT. They are eligible under the 8 or the 3.

Mr. GRAY. They are eligible under the 8. The great majority in dollar volume of these applications would be under these three goals which I have referred to.

Because Senator Byrd inserted in the Congressional Record a statement which I think, I am sure, had been furnished him by my predecessor, showing the outstanding eligible certificate and because of the format of the way that was printed—and I am not critical——

The CHAIRMAN. October 17, 1956, so stated in the Congressional Record.

Mr. GRAY. I understand that, Senator, but the Record seems to indicate that there were outstanding some $4 billion in eligible certificates. Actually that table showed something over $900 million.

I don't have in mind the exact figure which has now been reduced through the operation of the program to the $680 million figure.

The CHAIRMAN. Excuse me. Has that been reduced by granting the applications or by——

Mr. GRAY. Some granted and some rejected. Actually, since January 1 ODM has rejected applications which were estimated to have cost over $4 billion so that eligible for consideration now are only 257 applications estimated to cost $688 million.

Senator WILLIAMS. How many have you granted since January 1?

Mr. GRAY. How many individual certificates?

Senator WILLIAMS. Yes, sir. You told us how many you had rejected. How many have you granted?

Mr. GRAY. May I furnish that for you?

(The following was later received for the record:)

EXECUTIVE OFFICE OF THE PRESIDENT, OFFICE OF DEFENSE MOBILIZATION

Certificates of necessity for accelerated tax amortization have been issued during the period Jan. 1, 1957, through May 10, 1957, as follows

Expansion goal	Number of certificates issued	Amount amortized
		Thousands
No. 224: Production facilities for military and atomic energy procurement	129	$73,743
No. 206: Facilities for research and development	23	48,037
No. 27: Oceangoing tankers	26	186,950
No. 181: Steel castings	12	3,987
No. 227: Roll-on, roll-off ships	2	73,200
No. 65: Oil-refining facilities	10	20,085
No. 82: Glycerin facilities	1	6,405
No. 74: Steam-turbine facilities	3	10,658
No. 76: Steam-boiler facilities	1	1,400
No. 226: Oil-storage facilities for the armed services	10	39,213
No. 225: Electric power transmission and interconnection facilities	13	45,495
No. 55: Electric power generating facilities (Idaho Power Co.)	2	65,199
No. 223: Titanium-processing facilities	3	6,841
Total	235	581,213

Senator WILLIAMS. While you are furnishing it, can you furnish all that have been granted in the last 12 months and along with a specific breakdown by certification, industry type, who got it, and the percentage of the total amount of investment?

Mr. GRAY. We would be glad to do so.

Senator WILLIAMS. Would it be too much trouble to give it on the past 3 years which would cover this study that we had here?

Mr. GRAY. I think we can give it to you in category, that is, types.

Senator WILLIAMS. Don't you have it broken down?

Mr. GRAY. We can give you the whole list.

Mr. WYCKOFF. We can give them the whole list much easier.

Mr. GRAY. Would it satisfy you to have the whole list, Senator?

Senator WILLIAMS. Do you have the list?

Mr. GRAY. Yes.

Senator WILLIAMS. Just send the list up. That would show the type of industry and everything.

Mr. GRAY. Yes, sir.

(The material referred to is on file with the committee.)

The CHAIRMAN. Now, Mr. Gray, do you favor the bill or do you not favor it? Would you make clear your position on it?

Mr. GRAY. I will be glad to.

My position on the bill, Senator, is first, as I have said, if the bill is passed—adopted by the Congress—I would hope that the amendments that I have referred to could be worked out.

I myself, as the officer in Government primarily charged with mobilization preparedness am very reluctant to urge the elimination of a tool which, in the past, has been, I think, useful, and especially in the Korean emergency to help meet mobilization requirements of our economy. So I am not urging the adoption of this amendment.

However, I must say that as a practical matter, since we are administratively moving very rapidly toward what I think you are seeking to accomplish with your bill, I could not say that as of the present time the authority which your bill would eliminate is needed.

However, I wish to repeat that in my position as one responsible for thinking about defense-mobilization preparedness, I would not feel comfortable about urging the elimination of any available tool which might become necessary in the event another emergency arose.

The CHAIRMAN. Do I understand you favor the bill but you want to suggest certain amendments; am I correct?

Mr. GRAY. I am not urging the adoption of the bill.

The CHAIRMAN. I understand that, but the bill is before you.

Are you opposing it or do you favor it? That is what we want your advice about.

Mr. GRAY. Well, I think that what you are seeking to do we would do and have been doing administratively.

The CHAIRMAN. If you do it administratively, shouldn't then the Congress authorize it because, after all, Congress is supposed to make the laws which govern this country, not the bureaus, except to such extent that we give them power.

So, if you were doing this administratively, what is the objection to writing it into law, and then, if some emergency arises, requiring rapid amortizations, as they have in the past we will meet it. This is the only time we have had it for a period of 3 years in time of peace. As you know, it has gone far beyond what we have discussed

today. The steel plants have gotten enormous amortization privileges out of it going into the billions of dollars. And they raised the price of steel on top of that.

It cannot be overlooked that steel companies got these tremendous benefits and then raised the price of steel and this was the base for raising prices of many other products in the country.

As you know, the railroads which have gotten 16 percent of these, also have been granted an increase in fares, and under the law they are assured a fair return on their investment.

We have to watch the United States Treasury a little and $3 billion has been lost. Mr. Humphrey said it has been lost and he must be correct. He is Secretary of the Treasury.

In other words, we have had to borrow money to make up for this loss of revenue and it has cost us $3 billion in interest to do it.

It is quite a substantial amount.

One billion of that has resulted from permits that were granted in peacetime. That is $1 billion lost to the Treasury.

Mr. GRAY. Senator, I am saying that I am not now urging that there be any tax amortization certificates for areas other than these three that we have been talking about.

I hope that that will be true soon with respect to the open goals other than these three that are still open.

The CHAIRMAN. Do you have any serious objection to the bill as it now stands?

Mr. GRAY. My objection to it is this, Senator, that whereas I say that I see no present need to have authority which could go beyond your bill, I cannot predict that we will not get into another emergency which will require more authority.

The CHAIRMAN. In emergency the Congress is in session constantly? Can't you get authority from Congress?

My experience has been that it is a mistake for Congress to grant this kind of authority except in emergency.

I am not criticizing your action except I do think that a mistake was made in the Idaho Power Co.

But these departments of the Government usually use the power that is given to them.

If another emergency occurs, that is no reason to think we will not do as we have done in the past.

Certainly, Congress must exercise some control over such extraordinary things of giving tremendous tax reductions to certain industries and not giving them to others. Among other reasons is the fact that from a competitive standpoint within industries, a bad situation is created.

I would like to get clearly your views. Are you opposed to it strongly, or are you opposed to it mildly; what is your position on the bill?

Mr. GRAY. Senator, there are two questions here. If you refer to the present bill as it stands, I am opposed to the bill unless it could be amended to take care of things which I believe that you and I would agree needed to be taken care of.

That is, defense matters.

The CHAIRMAN. Then you have suggested amendments. We have confidence in you, and we want to give full consideration to your judgment. But we want to know what your judgment is.

As I understand it, you are not opposed to the bill if it has certain amendments that you will suggest, is that correct?

Mr. GRAY. I am not violently opposed to it, if that is your question.

The CHAIRMAN. You are not violently for it and you are not violently opposed to it, but after all, you will admit that Congress in matters of this kind should have a controlling voice?

Mr. GRAY. I admit that the Congress has responsibility to address itself to this question.

The CHAIRMAN. If another emergency comes, we can take it up.

Mr. Stam suggests the question: Should a certificate be available for a facility to meet a subcontract for the engine in a new kind of jet plane?

Should it be available for a specific facility to meet a subcontract for aluminum to go into the plane? If not, how do you draw the line? The aluminum goes eventually into Air Force procurement and so does steel?

Mr. GRAY. I would like very much, Senator, if we can talk with Mr. Stam about these particular amendments and not try to write them here.

The CHAIRMAN. You might just take these.

If you will suggest, Mr. Gray, your amendments, I will assure you the committee would give the fullest consideration to them.

I do not guarantee that we will adopt them but we will give them fullest consideration.

(The material referred to is on file with the committee.)

Senator LONG. Mr. Gray, with regard to these fast tax writeoffs, when these are given to a large corporation, for example, any of the major corporations that produce more than just one item. If the Government should decide to quit ordering one item or found it was no longer needed, would not there be other procedures whereby the corporation could recoup the loss?

In other words, couldn't it take, by obsolescence, for example, what it might otherwise fail to get in terms of depreciation as a tax matter?

Mr. GRAY. I am not sure I know the answer to that question, Senator.

Senator LONG. The point I had in mind is that we enter into a contract with someone to produce a modern-type engine that may be obsolete by the time the engine is coming off the production line and the Government may see fit to cancel that contract before the manufacturer has depreciated the machinery that he is using to manufacture it.

But assuming the corporation is in business year after year and they have many other items that they are producing, it would seem to me that they could probably recoup by just taking obsolescence on that machinery to the extent the rapid tax writeoff might not be available.

Senator BENNETT. May I suggest to the Senator there is no such legitimate deduction as obsolescence. It is depreciated rate or fast rate.

The only way you can clear yourself out of the situation you describe is to abandon the project and sell it off on the liquidation basis.

There is no other way.

Senator LONG. Even in that case, what the Senator is telling me, I would imagine if a man had a machine which cost $1 million and because the Government made a change in its programing the machine was no longer useful, it would seem to me that he could probably sell the machine and based on the difference between that amount he had depreciated it and the amount which he had paid, he could take that as a loss.

Senator BENNETT. That would be true on any basis of depreciation.

Senator LONG. In that event, though, he could recoup that which he did not get by his inability to depreciate it at a more rapid rate at the time he sold it. Is that correct?

Mr. GRAY. You would have to write it off against income. He couldn't just write it off against nothing.

Senator LONG. That is correct. That is the assumption on which we are proceeding, that this would be a corporation of sufficient magnitude that it has income year after year. I could quite agree if it were a small corporation and had no other item to produce, that the loss would be there and you couldn't get the tax writeoff.

Mr. GRAY. But as far as the administration of this kind of thing is concerned, it would be between the corporation and the Treasury. My office would not be involved.

Senator LONG. Does the Government also have procedures where a determination of the Government contract would provide for reimbursing the producer, the manufacturer, for what he lost by tooling up to produce an item that the Government decided it was going to discontinue?

In other words, supposing you go to produce some particular type of atomic machine or something of that sort, atomic reactor or anything else.

You decide later you don't need that type. Some new development or some new discovery makes it a worthless machine so far as modern-day operations are concerned.

You want something better and some more advanced than that.

Do not most of your contracts provide that the Government would adjust with that person or provide some protection for the manufacturer in the case like that?

Senator BENNETT. If the Government canceled the contract there would be a legal adjudication of its responsibility.

Senator LONG. Let the witness answer that.

Mr. GRAY. You are asking me a question about defense procurement which is not my responsibility, Senator. I have really very little recent knowledge about it. But I think such provisions as you refer to could, as a matter of contract, be entered into. Whether as a matter of practice they are, I do not know.

Mr. LONG. The only thing I would want to know about, because I voted for this rapid amortization, I voted for the accelerated depreciation in the tax law, but I wouldn't want to terminate it if meant that there were no other remedies available to persons who might be injured by it, if they had a good case.

Mr. GRAY. Of course, this is not so much of a remedy as an inducement to bring in facilities quickly. But one of the justifications, as I have indicated, is that whereas the manufacturer might be willing to bring into being facilities for procurement which he thinks are

going to be existing over a long period of time, he hesitates where defense is concerned, because of the high rate of change in military technology. Sometimes these things are very useful in inducing him to at least get into production for procurement which is foreseeable, foreseeably available.

Now, as to what the Treasury regulations are with respect to obsolescence, I am not equipped to answer that for you, sir.

Senator BENNETT. May I ask the witness just 1 or 2 questions?

The basis of your operation is a series of predetermined goals; am I right in that?

Mr. GRAY. That's right.

Senator BENNETT. Of the various agencies involved, to determine the series of goals in a series of areas which they consider to be vital to the national defense.

Mr. GRAY. That is correct.

Senator BENNETT. Your issuance of these certificates is not related to these goals?

Mr. GRAY. And within them.

Senator BENNETT. And within the goals.

So it could be assumed that if the agencies had taken the trouble and time to determine specific goals, they would not be inclined to declare obsolete or cancel contracts or their interest in products produced under these goals.

The goals, I assume, are projected for a reasonable period of time into the future and are sufficiently basic so that they do not turn on a change in the design of a carburetor. They represent a long-time, well-considered appraisal of the needs of the defense effort.

Mr. GRAY. Well, it is very difficult to generalize.

For example, the one goal that has been the subject of a good deal of discussion here this morning has been a power goal.

We do not think in terms of power becoming obsolete. It is an ever-present requirement. But I think the point that you are trying to make is, if the Defense Department has participated in the development of an expansion goal, would it therefore feel estopped from ceasing to procure under this goal? I don't think that would be true, sir.

Senator BENNETT. I was trying to indicate there is a responsible analysis of the situation made before any certificates are authorized.

Mr. GRAY. A very careful and responsible analysis is made by those people expert in the field of defense needs under consideration.

Senator BENNETT. So that there is not much chance—I wanted to say there is no chance, but there is not much chance that products developed by an industry under a certificate within the goal would be suddenly wiped out as being obsolete or unnecessary?

Mr. GRAY. I think that it is unlikely that that would be the case.

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

(By direction of the chairman, the following is made a part of the record:)

STATEMENT BY AMERICAN PUBLIC POWER ASSOCIATION TO SENATE FINANCE COMMITTEE

This statement is submitted on behalf of the American Public Power Association, 1025 Connecticut Avenue NW., Washington, D. C., in support of S. 1795, a bill by Senator Byrd of Virginia, to amend section 168 of the Internal Revenue Code of 1954 so as to restrict the issuance of certificates for rapid tax amortization.

The American Public Power Association is a trade organization representing more than 800 local publicly owned nonprofit electric utility systems, most of them municipally owned utilities, in 40 States, Alaska, and Puerto Rico.

In our opinion, S. 1795 is a good bill and properly confines the authority to grant fast tax-amortization certificates. This opinion reflects our interpretation of the bill, considering the statements made by Senator Byrd on the floor of the Senate on April 29, as precluding any certificates for any privately owned utility, since through regulation they are guaranteed a fair rate of return.

For a number of reasons, the members of this association have a direct interest in the program providing for fast tax writeoffs on facilities of the privately owned utilities. Many of our member systems purchase power from privately owned utilities which have received fast tax-amortization certificates. Although the resulting subsidies have benefited the utilities, no benefits have been passed on to the consumers, including our members which purchase power at wholesale. We consistently have opposed the fast tax-amortization program but believe that, since it nevertheless was carried out, the power consumers should have received the benefits.

Rather than going to the consumers, the benefits of fast tax amortization have enriched the power companies. The additional income is one reason why they are able to spend millions of dollars on advertising, propaganda, and other activities designed to discredit and ultimately put out of business the local consumer-owned nonprofit systems, thereby leaving the privately owned companies with a nationwide monopoly over power distribution.

In short, as taxpayers, the individual consumers served by our members have had to help bear the cost of the fast tax-amortization program; they have been denied any benefit from this program in the form of lower power rates, where they use power purchased from a utility receiving fast tax-amortization subsidies; and, consequently, they are actually forced to help subsidize the attacks by the private power industry on their own local systems.

The opposition of this association to the operation of the rapid-amortization program as it relates to electric utilities has been expressed in resolutions adopted by the association at its annual conventions for the past 4 years. The most recent expression on this subject, resolution No. 12, adopted at the 13th annual convention of the American Public Power Association in Los Angeles, Calif., April 26, 1956, is appended to this statement.

I have referred to fast tax amortization as a subsidy because this is what it is. The way in which it operates to subsidize the receiving corporation is most lucidly explained in the report by the staff of the Joint Committee on Internal Revenue Taxation of December 1956.

Government subsidies to business are not uncommon in the United States but they should be necessary to the accomplishment of some public purpose, they should be understandable or at least explainable to the general public, and they should be subject to control by normal processes of democratic government. As far as the electric utility industry is concerned, the fast tax-amortization program meets none of these requirements.

As the chairman of this committee, Senator Byrd, stated in his speech in the Senate on April 29 that the awarding of fast tax writeoffs to an electric utility "is totally indefensible."

Although the law states that facilities must be "certified as necessary in the interest of national defense," in order to qualify for fast tax writeoffs, the Office of Defense Mobilization has made almost no attempt to relate its actions on utility certificates to national defense needs as the staff report of the Joint Committee on Internal Revenue Taxation states: "In a period in which the electric power expansion goal is open there appears to be only one cause for outright rejection of a specific application, namely, location too close to a possible target area."

In a letter of January 18, 1956, to Senator Kefauver, Mr. Arthur Fleming, then director of ODM, confirmed this conclusion. He said that "in most instances it is not feasible to associate individual electric power facilities directly with specific defense activities." He went on to say that the ODM goals rather were measured against total current and prospective demand for electric power and certificates issued in order to prevent any prospective shortage for defense purposes. However, as the staff report makes evident, the formula adopted by ODM is a joke.

In an industry growing as rapidly as the electric power industry, in which projected demands repeatedly prove too conservative, how does one measure abnormal expansion and subsidize it so as to provide an abnormal margin of

excess capacity to cover emergency defense needs? In the electric industry, it is virtually impossible to do this, as ODM discovered. The agency issued certificates in order to reach a goal of 117 million kilowatts by 1956 but the industry actually reached a capacity of 122 million kilowatts. However, the staff report observes, "the demand for electric power is running higher also and the extra capacity is not as large as was planned." In other words, despite pumping enormous subsidies into the power industry, ODM ended up with greater total capacity but less margin for emergency defense needs than it planned. This result could have been predicted by anyone with a knowledge of the industry. To quote Electrical World magazine, it is "a fight to keep up with demand."

The staff report points out that ODM's 1955 experience also was instructive. The tax-writeoff program designed to bring in new capacity by the end of 1954 actually achieved an excess capacity of 20.5 percent over peak load, the objective of the ODM program. However, by the end of 1956 the excess apparently was back down to the normal margin of 15 percent. As the report says, "the fact that the program of increasing electric capacity must be long continued is not itself a criticism of the objective. It does emphasize the fact that the objective is not cheap."

I would add that the report shows quite clearly that the program is fruitless, if its objective is to maintain standby excess capacity for emergency defense demands. Unless a subsidy program so massive as to be economically unacceptable were adopted, the result will continue to be one of subsidizing capacity which would have been built anyway to meet normal demands. To asume anything else is, as ODM has found, an expensive delusion.

To illustrate how far from the national defense criterion and, in fact, any real principles at all, ODM has wandered in granting fast tax-writeoff subsidies, I would like to cite a few examples:

1. Fast tax-writeoff certificates were approved on April 25, 1957, for Brownlee Dam and Oxbow Dam, both projects of the Idaho Power Co., amounting to a total of $65,206,094. There has been no showing that these projects will contribute to the defense effort nor, apparently, did ODM ask for any showing. On the contrary, what findings are in the record point in the other direction. Thus, the Federal Power Commission presiding examiner in his opinion on the Idaho Power Co. application for licenses for these projects pointed out that there is "a crying need for firm power in the Northwest" and, he said, "One of the seemingly attractive aspects of the Idaho Power proposal and one which has been exploited and publicized was that Idaho Power would *without cost to the taxpayer* relieve this need to a substantial extent. * * * Whether power costing 6.6 mills is marketable on a firm basis is open to serious question *in spite of the power deficiency in prospect;* 6.6-mill power is fancy-priced power in the Northwestern area. * * * [Italics supplied.]

Thus, the examiner doubted whether the projects would help meet a deficit due to *normal* demands, let alone provide salable extra capacity for emergency defense needs.

A letter of August 4, 1955, from FPC Chairman Kuykendall to Senators sponsoring Federal Hells Canyon legislation in fact made it quite clear that the purpose of the projects was "to assure consumers in the (company service) areas of an adequate power supply." He made no mention of national defense needs or extra capacity.

ODM nevertheless approved fast tax-writeoff certificates for these projects. The projects were already underway and would have been completed with the same rate of speed if ODM had not approved the certificates for fast tax amortization. The ODM action was a plain and simple gift by the American taxpayer for which neither the taxpayers nor the power consumers will receive any benefit. This action was bad enough; it was particularly offensive when taken in the face of requests by Members of the Senate that such actions be held up pending study by Senate committees concerned.

There is general agreement that the tax amortization certificates represent interest-free loans and are therefore Government subsidies. In my opinion, it is fair to compute the benefit derived from these subsidies using the method used by the manager of the tax department of Ebasco Services, Inc., as outlined by him in a letter of June 10, 1954, to the Mississippi Power & Light Co. This method takes into acount the benefit to a utility of keeping one set of books for tax purposes and another set for rate-setting purposes. The taxes are paid on a fast tax-writeoff basis but the rates assume taxes are paid on the straight-line depreciation basis over the life of the plant.

Using the Ebasco formula, and assuming a 50-year life for Oxbow and Brownlee Dams, we find that the net benefits to the Idaho Power Co. of these certificates will be $329.3 million. This is more than twice the cost of the projects and about the cost of the high Hells Canyon Dam.

We urge that this or some other committee of the Congress inquire as to exactly why ODM took this action. It was not for national defense purposes.

This action discloses more clearly than any other action the fallacy of the so-called "partnership" policy on comprehensive river-basin development. Here is a case where a high dam, which only the Federal Government appears able to finance, would provide 3,880,000 acre-feet of usable flood storage and 1,124,000 kilowatts of prime power capacity and thus truly serve the objective of increased use of natural resources for peace and war. More than that, the power investment would be self-liquidating. The Federal Treasury would be paid back every cent of the power investment plus interest. At the end of 50 years the Government would own a debt-free income-producing asset with at least another 50 years of useful life.

In place of this, we are asked to believe that it is somehow cheaper to build some small dams with substantially less flood storage and substantially less power capacity which will produce power so expensive that it will not be marketable outside the area in which the power company has a legal monopoly. We are told that this in fact is so much wiser economically that the Government should contribute toward this undertaking an interest-free loan of $30.5 million. Somehow, it is supposed to be better business management to settle for a loan which will be paid back without interest, a development which will produce only slightly more than half as much prime power and about one-fourth as much flood storage, and an arrangement which leaves the Government with no asset or equity whatsoever, than to make a self-liquidating investment which will provide maximum flood storage and maximum low-cost power production. ODM cooperates in this undertaking in the name of national defense—an action which undoubtedly will be recorded as one of the most disgraceful blunders in our history.

2. Another example of the curious way this program has been administered is the fast tax amortization certificate awarded in 1955 to the Duquesne Light Co. for 75 percent of its investment of $14 million in the $125 million atomic power plant being built by AEC in partnership with Duquesne at Shippingport, Pa. This was another outright gift from the American taxpayer bestowed by ODM.

Acceptance of Duquesne as the partner in this project was based on "bids" received by AEC in response to its request to any and all utilities to submit proposals indicating the financial contribution they would make toward the project. AEC received a number of proposals and on March 14, 1954, announced that Duquesne's had been accepted as the one most favorable to the Government.

When AEC accepted the proposal, there was no mention and presumably no understanding that fast tax amortization of the Duquesne investment would be any part of the arrangement. The final contract was signed on November 3, 1954. Although in September Duquesne had applied for a fast tax writeoff, it was not mentioned as a condition in the firm contract. Nevertheless, Duquesne's certificate was approved by ODM several months later. In other words, Duquesne's going ahead with the project was in no way dependent upon getting a fast tax writeoff, nor was the tax certificate supposed to affect the speed with which the project would be undertaken. If the certificate had been denied, the status of this project today would be precisely the same except that Duquesne's net investment would be what it originally agreed to make instead of a great deal less.

The fast tax writeoff given to Duquesne represents a benefit to Duquesne of $8.2 million, well over half its investment, if one assumes that its investment in the reactor actually will depreciate to zero in 5 years and its investment in the conventional turbine-generator will depreciate in the normal period of 33⅓ years. The reactor investment probably will be good for more than 5 years so this figure is conservative. This calculation again is made using the Ebasco formula.

The net effect of this ODM action, in which AEC concurred, was to give Duquesne a gift for which the Government received no quid pro quo. If this action had been part of the Duquesne proposal, it is possible that it would have been less attractive than some other proposal. Having accepted the proposal on one set of terms, the Government then, more than 9 months later, suddenly made the terms much more favorable with no reason given and no reconsideration of the other bids.

Oddly enough, although ODM agreed to a 5-year writeoff for tax purposes, AEC has agreed to pay Duquesne rental for its investment, after the first 5 years, based on normal straight-line depreciation over a much longer period.

To top it off, the ODM action was taken in respect to a project which, while extremely important, is not a national defense project. Equally ironical, it was a subsidy granted to support construction of an atomic powerplant in the heart of the coal country where now, according to Congressman Van Zandt, unemployment in the coal-mining industry is a serious problem. It is difficult to imagine a rational basis for this action by ODM.

The Roanoke Rapids project of the Virginia Electric & Power Co. is another example of where ODM granted tax amortization subsidies for a project which the company had planned to build anyway to meet its normal requirements, quite apart from any special defense program.

On October 6, 1948, almost 2 years before the beginning of the Korean hostilities, the company applied to the Federal Power Commission for a license for the project, stating that there was a need in the area for the power which would be produced by the proposed project. On March 17, 1950, more than 2 months before the outbreak of fighting in Korea, a Federal Power Commission presiding examiner recommended that a license be issued for the project and stated as his first finding:

"1. Additional generating capacity is needed now and will be required in the future in the area to be served by the Roanoke Rapids project. The applicant's system can utilize the capacity and output of the plant on the basis it proposes."

Clearly, the record shows that this was neither a defense nor defense-related project and that there existed no need for an incentive in the form of tax assistance to induce the company to construct the project. Yet in August 1953, the Office of Defense Mobilization issued a certificate of necessity to Virginia Electric & Power Co. for rapid amortization of 65 percent of $33,095,000 of the cost of the Roanoke Rapids project.

4. As a further example of the irrelevant justifications given for the fast tax amortization program in the public utility field, I should like to cite from a letter of January 18, 1956, from Mr. Arthur Flemming, then Director of ODM, to Senator Kefauver. In this letter Mr. Flemming refers to the power needs of the Atomic Energy Commission as partial justification for the 1951 tax amortization program and, again, for the 1954 program. As is well known, almost all of AEC's massive power requirements are met by TVA, Bonneville Power Administration, Electric Energy Inc., and the Ohio Valley Electric Co. Obviously, fast tax amortization is not the way to expand the capacity of TVA and BPA but the ODM letter did not mention this.

EEI and OVEC are private corporations set up especially to serve the AEC loads in the Paducah, Ky., and Portsmouth, Ohio, areas. The contracts with these firms are drawn so that AEC, like any other power consumer, pays the Federal taxes assessed. The construction of these plants and the speed with which they were started was in no way dependent upon or affected by rapid tax amortization. The formation of the corporations and the construction of the facilities were wholly dependent upon the conclusion of mutually satisfactory contracts with the AEC. Whether they got fast tax amortization or not could not matter to the private corporations because AEC pays all Federal taxes through its power rates anyway.

Both companies, strangely enough, did apply for fast tax writeoff certificates but subsequently withdrew or suspended them. Possibly AEC objected to getting the same treatment other power consumers get, namely, to paying rates based on normal depreciation while the company pays taxes based on fast depreciation.

In any event, to use AEC power needs as a justification for setting goals for a fast tax amortization program makes exactly as much sense as to say that we must give subsidies to Consolidated Edison of New York because TVA needs more capacity. It is hard to believe that the ODM staff was ignorant of AEC power supply arrangements at the time Mr. Flemming wrote his letter to Senator Kefauver.

There are doubtless other examples of the gross misuse of the fast tax amortization provisions in the law. In fact, I am confident that a thorough-going investigation would disclose that for most of the certificates granted to the privately owned utilities, neither the Government, the taxpayers nor the consumers received anything in return for the subsidies tendered.

ODM's regulations did not require that they receive any return. Mr. Flemming has stated that the only requirements for "favorable consideration" were

that "applications for tax amortization must be filed before December 31, 1955 and the generating facility covered thereby must be located outside a congested urban area and scheduled for completion by December 31, 1958." Note that even in respect to one of the two criteria only a statement of intent is required. It does not have to be completed by any given date, but only "scheduled for completion." Mr. Flemming said, in effect, "Come and get it", and of course the utilities responded. Apparently, Mr. Gray is carrying on in the same tradition.

Finally, I should like to mention that the privately owned electric utilities through their nationwide electric companies advertising program have been advertising for years that they are ready, willing and able to finance all of the power capacity which America needs. In view of this declaration, there should be no need for Government subsiides to them of any type at all.

The cost of this program must be very large. On July 18, 1955, Secretary of the Treasury Humphrey, in urging an end to the program, said the loss in taxes to the Treasury in the then current fiscal year alone would be $880 million. The total tax postponement, according to the joint committee staff report will be about $5 billion and of course the benefits to the corporations affected are many times this figure. In the electric power field, as Senator Byrd has said, such subsidies are "utterly indefensible."

There is little need to expand on the point that this is a subsidy program which the citizens and taxpayers find extremely hard to understand. It is so complex that it is hard to explain even when one understands its mechanics. In our view any subsidy program should be simple enough to allow sufficient public understanding so that the voter can have an opinion on it.

The subsidies of course are completely out from under congressional control. The authority to appropriate billions of dollars of tax revenues has been delegated to the executive branch with such a wide degree of discretion that it can approve subsidies in the interest of national defense for projects which make no identifiable contribution to national defense.

We endorse S. 1797, because we believe that it eliminates the abuse of section 168 of the Internal Revenue Act of 1954 arising from the issuance of rapid amortization certificates to electric utilities. It is, however, only a partial answer to the problem of tax subsidies to electric utilities. We believe that either through amendments to S. 1797 or through separate legislation, Congress also should prohibit the application of section 167, relating to liberalized depreciation, to public utilities.

To electric utilities, the benefits which can be realized from section 167 are similar to and comparable to those received under the certificates for rapid amortization authorized in section 168. Although the intent of the two sections may have been entirely different, the principal differences to electric utilities are that the benefits of section 167 may be claimed without special certification or limitation and section 167 requires no showing, however indirect, of defense interest.

The Federal Power Commission has ruled that benefits to utilities under section 167 are to be treated in the same fashion for accounting purposes as those under section 168, explaining that, "We can find no legal difference" between the effects of the two sections of the Internal Revenue Code (*Amere Gas Utilities Co., et al.*, Docket G–6358, order issued June 30, 1956). This decision, as the Commission's action on the certificates of necessity for rapid amortization (Opinion No. 264, Docket R–126, adopted Dec. 3, 1953), prevents the benefits to the utilities from being shared with consumers.

In commenting upon the issuance of a rapid writeoff certificate to Idaho Power Co. for its proposed dams in the Hells Canyon reach of the Snake River, Senator Byrd very appropriately pointed out that "a public utility is guaranteed its profits." I cannot believe that Congress had regulated public utilities in mind when it approved section 167, but these utilities will realize tax benefits far exceeding those under section 168 unless Congress acts to plug this loophole.

For the reasons indicated, we recommend:

1. That S. 1795 be interpreted to preclude any fast tax amortization certificates for electric utility facilities of all kinds. I assume that this is the intent of the author of the bill and urge that there be adequate legislative history on this point to make it unmistakably clear, even to the ODM. S. 1795 should be erected as a roadblock to stop what a congressional committee once described as "the biggest bonanza that ever came down the Government pike."

2. That the instant case of high Hells Canyon Dam, which will soon be before the Senate, be considered on a hard-headed dollars-and-cents basis. If it is considered on this basis, and the emotions aroused by the public versus private power

issue are set aside, it will be clear that the high Hells Canyon Dam is by far the best investment of the public's money.

We are willing to support this statement with whatever degree of detail may be desired. A high Hells Canyon Dam will provide large amounts of power to the Idaho Power Co. but not through an interest-free loan. The company and the other power purchasers will repay the Government's investment with interest.

3. That legislation be introduced and enacted to exempt regulated public utilities from the provisions of section 167 of the Internal Revenue Act of 1954.

RESOLUTION NO. 12.—OPPOSING FAST TAX WRITEOFFS FOR PRIVATE UTILITIES

Whereas certificates of necessity for rapid amortization for tax purposes of new facilities issued to private power companies have, in effect, resulted in interest-free loans to private monopoly electric corporations exceeding $1.2 billion with ultimate benefits to these corporations in excess of $4 billion; and

Whereas these certificates issued under section 124A of the Internal Revenue Code of 1951 and under section 168 of the Internal Revenue Code of 1954 will result in benefits to the private monopoly electric corporations exceeding all Federal investment in power dams, an investment which will be repaid together with interest to the United States Treasury; and

Whereas the benefits of these certificates under Opinion 264 of the Federal Power Commission adopted in December 1953, and under similar decisions of various State regulatory commissions, flow almost entirely to stockholders of privately owned utilities; and

Whereas similar and comparable benefits to private power monopolies can result from the liberalized depreciation provisions of section 167 of the Internal Revenue Code of 1954; and

Whereas the presiding examiner of the Federal Power Commission in a recommended decision filed February 28 in the matters of Amere Gas Utilities Co. and others (Docket No. G–6358) has held relying in part upon aforementioned Opinion No. 264, that utilities may treat the benefits of liberalized depreciation in a similar manner to those resulting from rapid amortization; and

Whereas if this decision is adopted by the Commission and its findings and conclusions are made applicable to electric utilities, private power companies will be able to enjoy benefits from liberalized depreciation such as those they now receive from rapid amortization without either applying for certificates or being limited to a specified percentage of the costs of projects: Now, therefore, be it

Resolved, That the American Public Power Association:

1. Recommends that the Congress amend the Internal Revenue Act of 1954 to provide that section 167 relating to liberalized depreciation and section 168 relating to accelerated amortization shall not apply to regulated utility monopolies; and

2. Urges the Federal Power Commission to reconsider and reverse Opinion No. 264 relating to treatment of benefits received by electric utilities under certificates of necessity for rapid amortization; and

3. Asks the Federal Power Commission to deny and reverse the recommended decision of the presiding examiner in the matters of Amere Gas Utilities Co. and others (Docket No. G–6358) filed February 28, especially as the findings and conclusions of said decision might be related to electric utilities; and

4. Urges the Federal Power Commission and all State regulatory commissions having jurisdiction over electric utilities to prescribe procedures to insure that the benefits accruing to private power companies under certificates of necessity for rapid amortization or from the use of liberalized depreciation will be passed on to electric consumers.

NORTHWEST PUBLIC POWER ASSOCIATION, INC.,
Vancouver, Wash., April 23, 1957.

Re repeal of accelerated amortization.

Hon. HARRY F. BYRD,
Chairman, Senate Finance Committee,
Senate Office Building, Washington, D. C.

DEAR SENATOR BYRD: By resolution our 101 member consumer-owned electric systems of Washington, Oregon, Idaho, Montana, and Alaska have repeatedly urged the repeal of section 168 of the Revenue Code of 1954 which permits acceler-

ated amortization of plant investment including normal peacetime additions made to electric utility plant. We also favor the repeal of the Defense Production Act.

Our basic objections to both of these laws are on the constitutional grounds that they constitute appropriations by subterfuge; they are a method for taking money out of the United States Treasury before the money is put in; that they constitute a method of bypassing the Congress and thus bypassing the constitutionally required controls over the expenditure of Federal funds.

It is our view that any expenditures for the national defense should be set forth in the annual budget and enacted into law by means of appropriations bills. This subterfuge reaches extremely serious dimensions when it is applied to hydroelectric projects. These projects have long life. Accelerated amortization in practical effect grants to a private utility an interest-free loan for the construction of utility plant on which said company may earn and demand the right to earn a 6-percent rate of return. The compound interest impact of this financial manipulation was recognized as early as 1942 in a report submitted by a committee headed by Judge Healy, then Chairman of the Securities and Exchange Commission, who was chairman of this committee of the National Association of Railway and Utility Commissioners. I make reference to Judge Healy's report and also provide a case study of the unjust operation of accelerated amortization in a paper presented to the American Public Power Association at Boston, Mass., on May 14, 1953, entitled "Accelerated Amortization—Biggest Bonanza That Ever Came Down the Government Pike."

A copy of this paper is enclosed and it is respectfuly requested that this letter and the enclosed paper may be entered into the record of the hearings.

Aside from the gross injustice of this particular subterfuge and financial manipulation I wish to urge the committee's action to repeal section 168 of the Revenue Code of 1954 on the broader ground that undue and unwarranted complexity of public business tends to undermine the democracy.

It has been extremely difficult to explain the injustice of the fast writeoff activity to the general public. Therefore, for the further reason that the public business should be simplified and clarified, we respectfully urge the repeal of section 168 of the Internal Revenue Code.

Sincerely,

GUS NORWOOD, *Executive Secretary.*

ACCELERATED AMORTIZATION—"BIGGEST BONANZA THAT EVER CAME DOWN THE GOVERNMENT PIKE"

By Gus Norwood, Executive Secretary, Northwest Public Power Association

(Address at the annual convention of the American Public Power Association, May 14, 1953, at Boston, Mass.)

The Massachusetts constitution, adopted 1780, contains in its bill of rights this important principle:

"No man, nor corporation, or association of men, have any other title to obtain advantages, or particular and exclusive privileges, distinct from those of the community than what arises from the consideration of services rendered to the public. Government is instituted for the common good, for the protection, safety, prosperity, and happiness of the people and not for the profit, honor or private interest of any one man, family, or class of men."

This is the familiar principle of equality before the law. It is in the light of this principle that I wish to discuss the subject of accelerated amortization. As the story unfolds I ask you to reflect, whether the operation of accelerated amortization in the electric utility industry during the Korean war does not contravene this principle stated in the Massachusetts constitution, which is also the guiding principle of all high-minded government.

My discussion is organized under four headings, first, what is the origin and nature of accelerated amortization, second, how does it work in an actual example, third, what are the public-policy implications, and fourth, what are the conclusions to be drawn from this study.

ITS ORIGIN AND NATURE

On May 14, 1940, Hitler invaded France. One month and eight days later France surrendered. The German air armadas had won the blitzkrieg. President Roosevelt reacted promptly by asking Congress in his urgent messages of May 16 and June 13 for funds to build 4,000 planes. Congress approved the funds.

Two months later only 33 planes were on order. Companies refused to expand plans except on a basis of higher than normal profits. Meanwhile Germany was producing 1,500 planes a month. In desperation the Secretaries of War, Navy, and Treasury appeared in August 1940 before the joint hearings of the House Committee on Ways and Means and the Senate Committee on Finance. They recommended special income-tax treatment for companies which would build defense plants. The result was the enactment of section 124 of the Internal Revenue Code on October 10, 1940.

Thus was eliminated almost from the start the noble ideal of the Vinson-Trammell Act which proposed to take the profit out of war.

The new law permitted the defense agencies to grant certificates of necessity which entitled the holder thereof to amortize for tax purposes his new plant investment over a 5-year period at the rate of 20 percent a year. As Senator Magnuson told the Federal Power Commission on March 18, 1953, it was the intent of Congress to provide a means whereby a corporation could write off the investments in plants which would have little, if any, use after the defense emergency had passed. No industry would end up with a white elephant on its hands. Congress had socialized the risk.

Two years after the enactment of section 124 the National Association of Railroad and Utilities Commissioners at the 1942 convention received an important recommendation from Commissioner Robert E. Healy, Securities and Exchange Commission, and acting chairman of the NARUC Committee on Corporate Finance. In a brilliant report Judge Healy puts his finger on the central issue of accelerated amortization by pointing out the compound interest advantage. He concludes in favor of passing that advantage to the utility consumer by urging the removal of amortized plant from the rate base of the utilities.

Judge Healy's recommendation for strict adherence to net investment rate base was observed in a number of jurisdictions and was upheld in a clear case in the Michigan courts. The World War II utility record with certificates was fairly good because of restraint in granting them, because of OPA pressure to keep rates down and because of the influence of outstanding regulatory men, notably Leland Olds, chairman of the Federal Power Commission, Judge Healy, Beamish, Jourolmon, Fitzhugh, and Tom Buchanan. They are now all gone.

Nevertheless regarding the program as it applied to all industries the Brewster Committee of the 80th Congress reported that the certificate of necessity program in World War II gave rise to "legal profiteering."

With the start of the Korean War the Congress again enacted the rapid tax write-off method as section 124A of the Revenue Act of September 23, 1950. This time there was virtually no restraint as certificates were issued at the rate of a billion dollars worth a month. A preliminary investigation of the first $1,800 million in certificates and covering chiefly just the steel industry was made by the House Committee on Expenditures in the Executive Departments. In its report dated May 28, 1951, the committee concluded:

"The certificate of necessity program is the biggest bonanza that ever came down the Government pike."

During World War II the certificates reached $7.3 billion of which witnesses before the Brewster Committee suggested $3 billion was unwarranted. However, the Korean war has already passed the $26 billion mark or more than 3 times as much as was necessary to defeat Germany, Italy, and Japan in a 6-year war. Nor is the end in sight.

Especially eager to obtain certificates of necessity have been the private electric utility corporations. As of March 24, 1953, they have received certification of 592 projects involving a total cost of $3.7 billion of which $1.66 billion or 45 percent has been assumed to be investment incurred for national defense.

How does the defense agency determine what percentage of a plant is to be written off for national defense? The original National Securities Resources Board criteria read, "the major factor controlling the percentage of the certifi-

cate should be the probably economic usefulness of the facility for other than defense purposes after 5 years." Under this criteria the electric systems would have received virtually no certification.

Apparently the rule of the Defense Electric Power Administration was to regard the normal historical growth of the utility as peacetime investment and anything above that amount as defense. Under this logic the Pacific Power & Light Co. received a 75-percent write-off on the $26,170,000 Yale Dam and the Washington Water Power Co. received a 65-percent write-off on the $34,425,000 Cabinet Gorge Dam although both projects were urgently needed to alleviate the Pacific Northwest power shortage. It is hardly necessary to add that the DEPA staff was made up largely of private utility executives on loan from their companies.

Another incident in this history is the introduction of H. R. 426 on January 3, 1953, by Congressman Dondero to make accelerated amortization available retroactively to December 31, 1939. The House Committee on Ways and Means has held no hearings on the bill, but the Northwest Public Power Association has filed a letter in opposition.

This brings the story up to date to the Federal Power Commission hearings on Docket No. R–126 on proposed rulemaking for treatment of Federal income taxes as affected by accelerated amortization. The issue is whether the tax benefits should be given to the stockholders as windfall profits or be passed on to the consumer in the form of cheaper power rates.

The utilities testified at length in favor of placing the tax savings in newly set up deferred accounts, instead of passing on the savings to consumers. This type of accounting had been authorized by many State commissions and in view of that fact the utilities felt the best solution was for the Federal Power Commission not to make any rule at all.

In favor of passing the benefits on to the consumer was Mr. Francis J. Walsh of the FPC staff who made a very able case. Statements were likewise submitted by Senators Magnuson and Jackson, Congressman Don Magnuson, the National Rural Electric Cooperative Association, the Northwest Public Power Association, and the American Public Power Association.

The utilities' contention that no rule should be made by the Federal Power Commission brings to mind the remarks of Maryland's Governor McKeldin recently wherein he discussed the man who professes impartiality: "By looking with benign tolerance equally upon what is good and what is bad, he really allies himself with evil, like the policeman who takes no sides between the robber and his victim. * * *"

If I may borrow from Governor McKeldin's simile I should say that if the Federal Power Commission regards the arguments of the utility managements with benign tolerance, we may end up with the American consumer in the role of victim.

THE CABINET GORGE DAM

As a result of this program of noncollection of Federal income and excess profits taxes from the electric utilities, the Federal Government will have an investment in the companies of about $1,700 million. This is an interest-free loan on which the companies did not have to pay any financing or underwriting fees or bond discount. Theoretically the companies must repay the principal amount of this money unless they can duck out by one of the following four methods: First, they can avoid the repayment by showing a very low net income for any year. Second, they will save money if there is any reduction in the corporate income tax rate or they may have to pay a little more if the rate goes above the present 52-percent level. Third, they may utilize a subterfuge such as the method of composite depreciation rates as is practiced in Oregon. Finally, the company can duck the repayment by selling the amortized plant to a public body at any time after the fifth year.

The Federal Government is the junior stockholder in the electric utility business. The United States Treasury puts up some $1,700 million on the basis of no interest or dividends and expecting repayment of principal only if the companies enjoy uninterrupted prosperity. The Federal lien is junior to that of all other bondholders, preferred-stock holders, common-stock holders, or any other present or future creditors of these companies. Thus accelerated amortization

becomes a halo around the gilt edges of utility bonds. This great amount of junior equity money has already enabled the utilities to obtain bond money cheaply without the necessity of issuing additional common stock.

Over and above all these benefits is the interest-free feature which shows up most dramatically in the case of a plant with a long life if the amortized investment is included in the rate base of the utility.

On February 18, 1952, the Washington Water Power Co. obtained a certificate of necessity for the 200,000-kilowatt Cabinet Gorge Dam on the Clark Fork River in Idaho with a permissible writeoff of 65 percent on $34,425,000. The Idaho and Washington regulatory commissions have granted orders permitting tax deferral accounting over a 40-year period. Actually the project obviously has an average useful life of more than 40 years. What is the value of the accelerated amortization benefit to the company for this dam? The answer is $55,809,119. Even if the corporate income tax rate remains as high as 52 percent and even if the company obtains a rate of return of only 6 percent, the compound interest gain over the 40-year period is $55,809.119 or more than 5 times the amount of the original tax deferral of $10,181,195. The computations are shown in table 1.

Applying the same criteria to all electric utilities but reducing the normal plant life to 30 years shows in table 2 an unearned windfall profit for utility stockholders of $1,901,009,000 over the 30-year period. All these benefits, furthermore, will go to stockholders not as income but as capital gains.

Please note also table 3, which shows that the national debt will be at least $418,916,000 higher 30 years from now, just to reflect the interest cost on the deferred taxes. This figure is an absolute minimum and is based on 2½ percent interest compounded whereas present interest on Federal bonds is over 2.8 percent. This amount of almost half a billion dollars is the additional out-of-pocket cost to all other Federal taxpayers in order to subsidize the electric utility corporations.

TABLE 1

WASHINGTON WATER POWER CO.—CABINET GORGE HYDROELECTRIC PROJECT

Investment subject to rapid amortization (65 percent on $34,425,000)	$22, 376, 250
Annual depreciation accrual on a straight line basis:	
5-year rapid amortization	4, 475, 250
40-year normal life	559, 406
Balance transferred to earned surplus	3, 915, 844
Federal tax, 52 percent	2, 036, 239

Effect of rapid amortization of Cabinet Gorge project for income-tax purposes, assuming company earns a return of 6 percent on its invested capital

Year	Cumulative amount deposited in special earned surplus account	Annual charges			
		Interest at 6 percent per annum	Annual amount transferred to earned surplus account	Annual amount deducted from earned surplus account	Total
1			2,036,239		2,036,239
2	2,036,239	122,174	2,036,239		2,158,413
3	4,194,652	251,679	2,036,239		2,287,918
4	6,482,570	388,954	2,036,239		2,425,193
5	8,907,763	534,466	2,036,239		2,570,705
6	11,478,468	688,708		290,891	397,817
7	11,876,285	712,577		290,891	421,686
8	12,297,971	737,878		290,891	446,987
9	12,744,958	764,697		290,891	473,806
10	13,218,764	793,126		290,891	502,235
11	13,720,999	823,260		290,891	532,369
12	14,253,368	855,202		290,891	564,311
13	14,817,679	889,061		290,891	598,170
14	15,415,849	924,951		290,891	634,060
15	16,049,909	962,995		290,891	672,104
16	16,722,013	1,003,321		290,891	712,430
17	17,434,443	1,046,067		290,891	755,176
18	18,189,619	1,091,377		290,891	800,486
19	18,990,105	1,139,406		290,891	848,515
20	19,838,620	1,190,317		290,891	899,426
21	20,738,046	1,244,283		290,891	953,392
22	21,691,438	1,301,489		290,891	1,010,598
23	22,702,036	1,362,122		290,891	1,071,231
24	23,773,267	1,426,396		290,891	1,135,505
25	24,908,772	1,494,526		290,891	1,203,635
26	26,112,407	1,566,744		290,891	1,275,853
27	27,388,260	1,643,296		290,891	1,352,405
28	28,740,665	1,724,440		290,891	1,433,549
29	30,174,214	1,810,453		290,891	1,519,562
30	31,693,776	1,901,627		290,891	1,610,736
31	33,304,512	1,998,271		290,891	1,707,379
32	35,011,891	2,100,713		290,892	1,809,821
33	36,821,712	2,209,303		290,892	1,918,411
34	38,740,123	2,324,407		290,892	2,033,515
35	40,773,638	2,446,418		290,892	2,155,526
36	42,929,164	2,575,750		290,892	2,284,858
37	45,214,022	2,712,841		290,892	2,421,949
38	47,635,971	2,858,158		290,892	2,567,266
39	50,203,237	3,012,194		290,892	2,721,302
40	52,924,539	3,175,472		290,892	2,834,580
Total	55,809,119	55,809,119	10,181,195	10,181,195	55,809,119

TABLE 2

Estimated annual tax savings of the electric utility industry due to rapid amortization for income tax purposes assuming average life of projects is 30 years.

Total estimated cost of 592 projects which have received tax amortization certificates as of March 24, 1953	$3,692,726,899
Investment subject to rapid amortization	1,659,113,149
Annual depreciation accrual on a straight line basis:	
5-year rapid amortization	331,822,629
30-year normal life	55,303,772
Balance transferred to earned surplus	276,518,857
Federal tax 52 percent	143,789,806

Effect of rapid amortization for income-tax purposes, assuming companies earn a 6 percent return on tax savings which are placed in a special earned-surplus account

[In thousands]

Year	Cumulative amount deposited in special earned-surplus account	Annual charges			
		Interest at 6 percent per annum	Annual amount transferred to earned-surplus account	Annual amount deducted from earned-surplus account	Total
1			143,790		143,790
2	143,790	8,627	143,790		152,417
3	296,207	17,772	143,790		161,562
4	457,769	27,466	143,790		171,256
5	629,025	37,742	143,790		181,532
6	810,557	48,633		28,758	19,875
7	830,432	49,826		28,758	21,068
8	851,500	51,090		28,758	22,332
9	873,832	52,430		28,758	23,672
10	897,504	53,850		28,758	25,092
11	922,596	55,356		28,758	26,598
12	949,149	56,952		28,758	28,194
13	977,388	58,643		28,758	29,885
14	1,007,273	60,436		28,758	31,678
15	1,038,951	62,337		28,758	33,579
16	1,072,530	64,352		28,758	35,594
17	1,108,124	66,487		28,758	37,729
18	1,145,853	68,751		28,758	39,993
19	1,185,846	71,151		28,758	42,393
20	1,228,239	73,694		28,758	44,936
21	1,273,175	76,390		28,758	47,632
22	1,320,807	79,248		28,758	50,490
23	1,371,297	82,278		28,758	53,520
24	1,424,817	85,489		28,758	56,731
25	1,481,548	88,893		27,758	60,135
26	1,541,683	92,501		28,758	63,743
27	1,605,426	96,326		28,758	67,658
28	1,672,994	100,380		28,758	71,622
29	1,774,616	104,677		28,758	75,919
30	1,820,535	109,232		28,758	80,474
Total	1,901,009	1,901,009	718,950	718,950	1,901,009

TABLE 3

Effect of rapid amortization for income-tax purposes on Federal tax income, assuming that Government loses interest compounded at 2½ percent on the deferred amount

[In thousands]

Year	Cumulative amount deposited in special earned surplus account	Annual charges			Total
		Interest at 2½ percent per annum	Annual amount transferred to earned surplus account	Annual amount deducted from earned surplus account	
1			143, 790		143, 790
2	143, 790	3, 595	143, 790		147, 385
3	291, 175	7, 279	143, 790		151, 069
4	442, 244	11, 056	143, 790		154, 846
5	597, 090	14, 927	143, 790		158, 717
6	755, 807	18, 895		28, 758	9, 863
7	745, 944	18, 649		28, 758	10, 109
8	735, 835	18, 396		28, 758	10, 362
9	725, 473	18, 137		28, 758	10, 621
10	714, 852	17, 871		28, 758	10, 887
11	703, 965	17, 599		28, 758	11, 159
12	692, 806	17, 320		28, 758	11, 438
13	681, 368	17, 034		28, 758	11, 724
14	669, 644	16, 741		28, 758	12, 017
15	657, 627	16, 441		28, 758	12, 315
16	645, 310	16, 133		28, 758	12, 625
17	632, 685	15, 817		28, 758	12, 941
18	619, 744	15, 494		28, 758	13, 264
19	606, 480	15, 162		28, 758	13, 596
20	592, 884	14, 822		28, 758	13, 936
21	578, 948	14, 474		28, 758	14, 284
22	564, 664	14, 117		28, 758	14, 641
23	550, 023	13, 751		28, 758	15, 007
24	535, 016	13, 374		28, 758	15, 384
25	519, 632	12, 991		28, 758	15, 767
26	503, 865	12, 597		28, 758	16, 161
27	487, 704	12, 193		28, 758	16, 565
28	471, 139	11, 778		28, 758	16, 980
29	454, 159	11, 354		28, 758	17, 404
30	436, 755	10, 919		28, 758	17, 839
Total	418, 916	418, 916	718, 950	718, 950	418, 916

PUBLIC POLICY IMPLICATIONS

To analyze the public policy implications of accelerated amortization is to trace the pathology of a bad law. Step by step it is not unlike the morbid progress of a disease.

The starting point is the issue before the Federal Power Commission as pointed out by Healy in 1942, namely, will the compound interest benefit go to the stockholdrs as windfall profits or to the consumers as cheaper power rates. The utility stock speculator want to use accelerated amortization as a booster pump to transfer more money from the consumers to the stockholders. The economic effect would be regressive, making the poor poorer and the rich richer. One utility man from Texas even testified it would be inflationary to let the consumers have cheaper electric rates.

This conspiracy of utility executives and stock speculators against the consumers would not be at issue before FPC but for the breakdown of regulation at the State level. Here is a prime example of hypocrisy. The record shows 17 State commissions each parading under the flag of the consumer while in fact permitting the consumer to be exploited. On some of the blackest pages of American government is recorded the repeated betrayal of the consumer at the hands of his publicly paid guardian and protector, the public service commissioner.

The second stop in this pathological pilgrimage is the defense agency where an army of corporation executives temporarily dressed as policemen are passing out tickets, $26 billion worth of tickets. This is a case of making the fox the custodian of the chicken coop. Three congresisonal committees have now complained in strong language. Most recently the Dawson committee in 1951 said,

"* * * administration * * * has been unsound and detrimental to the public interest. In the first place, the established regulations and procedures have not been followed. There are instances of outright disregard for the safeguards which were designed to protect these most vulnerable functions from abuse. The need for prompt action to meet the national emergency was construed as justifying a 'shovel in the barrel' approach to the certificate of necessity program as early as 10 days after it got underway." These congressional reports cite numerous examples of reckless and irresponsible administration.

The Secretary of Interior likewise protested frequently regarding the high percentage granted in the certificates but he was overruled by Defense Mobilizer Charles Wilson.

Thirdly, the law itself invites maladministration. The committee found "the criteria it sets out for determining the certifiable portions are ambiguous and vague, to say the least." For example the term "necessary in the interest of national defense" was construed very broadly "to encompass all expansion necessary to satisfy military needs together with all expansion necessary to keep civilian suplies at as close to normal levels as possible during the emergeny." Another train of evils followed from the law's vague terminology, "attributable to defense purposes".

Fourthly, the conception or theory of the law is inconsistent with the traditions of this country. As the war clouds were gathering in 1940 the National Association of Railroad and Utilities Commissioners committee on progress in public utility regulation observed:

"It has been the avowed purpose of Congress, through a legislative policy which antedates the depression and goes back to the period immediately following the First World War, to control war profits in any future war in which the United States might become involved, and to prevent the creation of new war millionaires. It was the general concensus that this should be effected by the imposition of income and excess-profit taxes. Accordingly, the Vinson-Trammell Act was passed, its provisions including a limitation upon the profits from the construction or manufacture of naval vessels and Army and Navy aircraft. The express purpose of this act was to take the profit out of war."

If indeed government is instituted for the common good and not for the profit or private interest of the select few, if indeed there is to be equality in the enjoyment of benefits before the law, then there must also be equality of scarifice under the law in time of war.

War requires a basic partnership between producing industries at home and fighting forces at the front. Yet to achieve this partnership we use on the one hand the mercenary method and on the other hand the compulsory draft. The Korean war has cost 130,000 American casualties and $26 billion in accelerated amortization certificates. Refined in terms of actual profiteering from tax writeoffs, the Korean war has produced 1 new war millionaire, or his equivalent in profits, for every 20 casualties.

The experience with accelerated amortization casts doubt on the sincerity of utility executives in their protestations that they are loyal to their country. Instead of patriotism and a proper regard for the duties of citizenship there is found an exploitation of the national defense emergency as an opportunity for unwarranted legal profiteering. The national defense has been used as a subterfuge and excuse to demand and obtain huge Federal subsidies, paid by you and me, to get the electric corporations to perform their normal and simple public utility responsibilities. Having received these subsidies, they now have the unmitigated gall to demand the right to incorporate these Federal subsidies in their rate base and to exact from their consumers a 6 percent rate of return thereon. From 1937 to 1950 as a result of many hearings and court cases the utilities were required to wring out over $1.5 billion of water from their capital structure. Now they propose to put at least as much back.

This has been a study in sophism, of attempts to make black appear white, of counterfeiting truth, of using the appearance of logic and a claim of reasonableness to camouflage error. This has also been a study in the breakdown of the fundamental morality and ethical standards of American public life. Good State regulations would have stopped this raid on the consumer. Good Federal administrators would not have issued the certificates. Patriotic utility executives would not have demanded them. A wise Congress would have thought twice before enacting the law. An aroused public would not tolerate war profiteering. Whatever it is that "is rotten in Denmark" is rotten five times. Life has become more complex since the days of Hamlet. This pyramid of demoralization brings to mind the words of Oliver Goldsmith, "Laws grind the poor, and rich men rule the law."

A PROGRAM FOR ACTION

In conclusion there are certain measures which the members of this association can support in order to restore the principle that excessive profits should not be drained from the people during a period of national sacrifice.

First, we should all support the efforts of the Federal Power Commission to formulate rules which will guard and protect the consumer. This the Commission can do by purging the utility rate base of the plant investment which has been amortized through the tax-certificate process.

Second, we should all oppose H. R. 426, a bill introduced by Congressman Dondero, advocate of the utility corporations, whereby accelerated amortization might be applied retroactively to 1939.

Third, we can all work for the repeal of section 124A of the Internal Revenue Code—a law which has carried many evil consequences in its train.

If we can succeed in these three endeavors we will not only have served the interests of the electric consumers, but we will also have repaired the moral standards of the utility industry and established principles which cannot fail to strengthen our system of American democracy in its struggle against totalitarianism.

When we wipe out the opportunity of using a period of warfare as a means of making profiteers we return to the conception that democracy was once something for which men fought, and that it must continue to represent a belief in the moral equality of men and a ceaseless struggle to create a society in which such equality will be a living reality.

These problems are not new. The same concern was ably expressed by the committee on progress in public utility regulations in language which was adopted by the 1940 convention of the National Association of Railroad and Utilities Commissioners in Miami, Fla.:

"If the time should come for an all-out showdown between the United States and the totalitarian powers, there is but one thing that can defeat this country. That is the deep-rooted love of private pecuniary gain. Freed of this spirit of greed, democracy as it has traditionally flourished in this country is invincible."

AMERICAN FARM BUREAU FEDERATION,
Washington, D. C., May 6, 1957.

Senator HARRY F. BYRD,
Chairman, Senate Committee on Finance,
United States Senate, Washington, D. C.

DEAR SENATOR BYRD: Since December 1954 the American Farm Bureau Federation has favored termination of the authority provided in section 168 of the Internal Revenue Code of 1954 (and prior acts) which provides that a part of the cost of certain defense facilities may be charged off against taxable income in a period of 5 years without regard to the expected life of the facility, otherwise known as the accelerated amortization program. The basis for this position lies in the fact that the program appears largely to have served its purpose of encouraging a rapid expansion of our productive capacity for defense. As a long-time policy, any encouragement that may be found necessary to bring out the construction of new facilities should be provided through generally applicable provisions of law rather than by programs which require that the Government certify individual projects.

During recent years the repeal of the excess-profits tax and the incorporation of new and more liberal depreciation options in the Revenue Code of 1954 offer strong justification for the termination of this permissive authority.

The phase of the accelerated amortization program which requires special certification, in the light of the liberal depreciation policy now outstanding, has outlived its usefulness and we feel is not now a suitable or desirable authority during an era of peacetime.

We respectfully request that our views be made a part of the hearing record with respect to S. 1795.

Sincerely yours,

JOHN C. LYNN,
Legislative Director.

(Whereupon, at 12 o'clock meridian, the committee adjourned.)

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