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REPORT
No. 617

REVENUE BILL OF 1918.

DECEMBER 6, 1918.—Ordered to be printed.

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

REPORT.

[To accompany H. R. 12863.]

The Committee on Finance, to whom was referred the bill (H. R. 12863) to provide revenue, and for other purposes, having had the same under consideration, report it back with sundry amendments and recommend that the bill as amended do pass.

The revenue bill as passed by the House—which is fully explained in the appended copy of the report which accompanied its introduction into the House—was so framed as to yield in the first 12 months of the full operation of its several titles an estimated revenue of \$8,182,492,000. This is possibly the largest tax budget ever voted by any legislative chamber in the history of the world, and the committee approached the task of its revision in a spirit appropriate to the gravity of the task before it: By securing through careful investigation and numerous hearings the advice not only of those who would be most vitally affected by the new law, but of those who by study and administrative experience were in position to offer helpful suggestions. These hearings fill a printed volume of over 650 pages which, with similar hearings of the Committee on Ways and Means, constitute a reference library of great value upon the entire subject.

Since the formulation of the House bill the scope and character of the prospective revenue act have been profoundly affected by two events of controlling importance. First, in order of time, was the adoption of regulations and legislation restricting the production and sale of alcoholic beverages. Beverage taxes under the House bill were estimated to yield for the first 12 months of their operation \$1,137,600,000, and approximately \$850,000,000 for the fiscal year 1919. At the present time, under the changed conditions, it is possible to count upon only \$500,000,000 for the fiscal year 1918-19, and \$93,000,000 for the fiscal year 1919-20, from this source. At

the very beginning of its labors, therefore, the committee was called upon to face a loss or reduction in the beverage taxes of approximately \$350,000,000 for the fiscal year 1918-19, and of more than \$1,000,000,000 for the fiscal year 1919-20.

When the committee had nearly completed its original task of revising and perfecting the House bill, came the sudden and dramatic victory of the allied arms. The task of financing the operations of a great war gave way to the task of financing the Government through a period of reconstruction and demobilization. The two problems are not the same, and the tax legislation appropriate to the one is not wholly appropriate to the other. Taxes which can be easily borne amid the feverish activity and patriotic fervor of war times, are neither so welcome nor so easily sustained amid the uncertainties, the depreciating inventories, and the falling markets which are apt to mark the approach of peace. Repressive taxes which in time of war are justified for the very reason that they diminish the demand for labor, capital, and raw material, are for the very same reason obnoxious and undesirable in times of peace. The cessation of war, therefore, brought with it not only the opportunity but the necessity of reducing the large tax budget which the House had voted.

This interpretation of the financial significance of the cessation of war was promptly confirmed in a letter addressed by the Secretary of the Treasury to the chairman of the committee under date of November 14, 1918, in which Secretary McAdoo announced that "the collapse of our enemies necessitates instant reconsideration of the financial plans before the Government," and added, "The prompt enactment of a revenue bill is imperative. The existing law is not satisfactory to the country nor to the Treasury. On the other hand, the revenue bill which passed the House is more stringent than the changed situation will justify." At the same time the Secretary expressed his belief that the actual expenditures of the Government during the fiscal year ending June 30, 1919, would be in the neighborhood of \$18,000,000,000, and recommended—

That the pending revenue bill be revised with a view to yielding \$6,000,000,000 payable during the calendar year 1919, and not less than \$4,000,000,000 during the calendar year 1920.

This recommendation of the Secretary has been accepted by the committee and the necessary changes made to give it full effect. The House bill as originally passed, as heretofore stated, was expected to yield about \$8,100,000,000 for the first year of its operation, but a part of this was lost by reason of the shrinkage in the prospective yield of the beverage taxes. It is now estimated that the House bill would produce for the fiscal year 1919 \$7,405,390,000. Because of the changed conditions resulting from the signing of the armistice Secretary McAdoo recommends that a tax levy of \$6,000,000,000 is all that is now necessary or justifiable, and the changes recommended by your committee, it is estimated, will reduce the revenue to this amount.

A clear idea of the effect of the committee's recommendations upon the yield of the several schedules or titles may be gathered from the brief statistical summary which follows herewith:

Title.	Present law, fiscal year 1919.	House bill, fis- cal year 1919.	Senate com- mittee bill, fis- cal year 1919.	Reduction, committee bill from House bill, fiscal year 1919.
II. Income tax.....	\$1,488,500,000	\$2,378,188,000	\$2,207,000,000	\$169,188,000
III. War excess-profits tax.....	1,791,000,000	3,368,000,000	2,480,000,000	800,000,000
IV. Estate or inheritance tax.....	100,000,000	100,000,000	100,000,000
V. Tax on transportation and other facilities.....	230,000,000	281,000,000	220,000,000	2,000,000
VI. Tax on beverages.....	400,000,000	500,000,000	450,000,000	50,000,000
VII. Tax on cigars and tobacco.....	300,000,000	341,204,000	240,800,000	100,404,000
VIII. Admissions and dues.....	54,000,000	81,000,000	54,000,000	27,000,000
IX. Excise taxes.....	76,000,000	207,000,000	123,000,000	174,000,000
X. Special taxes.....	28,617,000	97,000,000	73,868,000	23,134,000
XI. Stamp taxes.....	32,000,000	32,000,000	31,000,000	1,000,000
Floor taxes.....	150,600,000	70,000,000	80,000,000
Total.....	4,870,117,000	7,405,300,000	5,978,466,000	1,426,834,000

FISCAL YEAR 1919-20.

The committee was of the opinion that provision should be made in the present bill for the termination, after 1919, of the war-profits tax and for the reduction of the excess-profits tax. The country has a right to know how soon and in what degree the burden of war taxes can prudently be reduced. During this period of reconstruction, however, business (particularly new business) is entitled to go forward without the burden of an 80 per cent tax upon profits. In time of peace the existence of an 80 per cent profits tax would be a positive evil, for the perpetuation or continuance of which no sufficient reason has or could be given. The reasons for this decision are well set forth in the following statement by Secretary McAdoo:

Nor can I overemphasize the importance of determining now the basis of taxation which will apply to the calendar year 1920 as well as to the calendar year 1919. Business and industry and individual initiative and enterprise are entitled to know in advance the basis of taxation upon which all the activities of the Nation must be conducted. Prosperity can not be maintained if business is kept in uncertainty as to taxation. It is always unfortunate to be compelled to enact a tax bill at the end of the calendar year, with retroactive effect, instead of in advance of the calendar year, which would permit contracts and business arrangements generally to be entered into with certainty as to the burden of taxation to be borne. This is a gross injustice to business and to all forms of enterprise. It is costly to the people at large, as they are required to pay higher prices for their necessities, because producers, in order to be on the safe side, fix prices on the assumption that taxes may be higher than they subsequently turn out to be. Definiteness and certainty as to the basis of taxation should be given in the pending bill, not alone as to the calendar year 1918 but as to the calendar year 1919. This will enable business and enterprise to proceed with confidence and courage.

For the year 1920, therefore, the committee recommends that the war-profits tax or bracket be abolished; and that the rates of the excess-profits tax be substantially lowered; and that the rate of normal tax be reduced by one-third; i. e., in the case of corporations from 12 per cent to 8 per cent and in case of individuals from 12 and 6 per cent to 8 and 4 per cent. It is estimated that these changes would reduce the revenue for 1920 as compared with 1919 by approximately \$1,400,000,000; and that there would be a net reduction from other miscellaneous sources of about \$500,000,000 attributable chiefly to shrinkage in the yield of the beverage taxes. With respect to taxes

other than income and profits taxes, the committee recommends no change in rates for the fiscal year 1920.

The main outline of the program proposed by the committee thus becomes clear. For the fiscal year 1919 it is planned to raise nearly \$4,600,000,000 from income and profits taxes, and something like \$1,400,000,000 from other sources; for the fiscal year 1920 it is planned to raise somewhat less than \$3,000,000,000 from income and profits taxes, and about \$1,000,000,000 from other sources. About the general wisdom of such a program we entertain no serious doubt. It is imperative that profits and income for the year 1918 be heavily taxed. This is not only necessary but it is equitable and in accordance with sound public policy. The profits realized during the year 1918 are in large part war profits; they are now in the pocket of the taxpayer; they should contribute heavily before they have been dissipated or reinvested toward the payment of the expenses of the war to which in large measure they are attributable.

But it is equally important that these special taxes should be reduced as the occasion which inspired and justifies them recedes into the past. To fail adequately to tax the war profits of 1918 would constitute a manifest miscarriage of fiscal justice. Not to provide now for the reduction of the war-profits tax would be equally inexcusable.

TITLE II.—INCOME TAX.

SURTAX RATES.

The committee has adopted a more equitable schedule of surtax rates (sec. 211). The rates in the House bill start at 2 per cent and advance by steps, varying from 1 to 7 per cent, until the maximum of 65 per cent is reached upon incomes in excess of \$5,000,000. These steps bear no fixed relation to each other. For example, income between \$20,000 and \$30,000 would pay 8 per cent more tax than income between \$10,000 and \$15,000, while income between \$90,000 and \$100,000 would pay only 2 per cent more than income between \$80,000 and \$90,000.

The surtax rates approved by the committee begin with 1 per cent upon incomes in excess of \$5,000 and not in excess of \$6,000 and advance to a rate of 48 per cent upon incomes in excess of \$98,000 and not in excess of \$100,000. This advance is uniform with an additional 1 per cent of tax for each additional \$2,000 of income until the income of \$100,000 is reached. From that point the rate of increase is reduced so as to reach the maximum rate of 65 per cent after passing \$1,000,000. The effect of these changes is slightly to reduce the tax upon incomes of \$200,000 or less, while upon incomes in excess of \$200,000 the tax is somewhat increased. The estimated revenue to be derived from surtaxes under the provisions of the House bill is \$1,068,186,000, while under the bill as amended the amount as estimated upon the same basis is \$1,045,069,000.

RATES FOR CORPORATIONS.

The committee has provided for a uniform tax upon the net incomes of corporations, this rate being 12 per cent for the 1918 taxable year and 8 per cent for succeeding years (sec. 230). Under the House bill

the 12 per cent rate applied only to so much of the net income as was distributed in dividends, or paid in the discharge of interest-bearing obligations, or in the purchase of liberty bonds issued after September 1, 1918, and on the balance the rate was 18 per cent. While certain essential uses of earnings for purposes other than distribution were recognized, many other such uses of earnings equally essential, such as for additions to plant for purposes of further production, were not recognized. Failure to permit without penalty all legitimate uses of earnings for financing corporations seemed inconsistent with the policy which has in the past been actually followed by well-managed corporations and which has been urged by the War Finance Corporation and the Capital Issues Committee. To retain the differential rate while exempting from the extra tax all income used by the corporation for legitimate purposes other than distribution would, however, make the law difficult of administration, because it would involve review by the Treasury Department of too many detailed questions of the administrative policy of individual corporations. These and other considerations, among which was the fact that corporations are subject to the war excess-profits tax, to which individuals and partnerships are not subject, moved the committee to restore a flat-rate system.

INCOME OF CERTAIN CORPORATIONS TAXABLE TO STOCKHOLDERS.

It was believed that the incentive to withhold from distribution as dividends earnings not required for legitimate business uses exists chiefly in the case of certain corporations the stock of which is very closely held, and that the encouragement of distribution sought to be accomplished by the differential rate on corporations in the House bill could be better accomplished by changes in the provision dealing with such closely held corporations (sec. 220). The section of the present law, incorporated in the House bill, providing that undistributed profits of a corporation may in certain cases be treated as part of the income of its stockholders subject to surtax, has proved to be of little value, because it was necessary to its application that intended fraud on the revenue be established in each case. The committee has done away with this requirement and has provided that in the case of any corporation formed or availed of for the purpose of permitting gains or profits to accumulate instead of being divided the income shall be taxed to the stockholders in the same way that partnership earnings are taxed to partners.

BASIS FOR DETERMINING GAIN OR LOSS (SEC. 202B).

A provision was inserted designed to establish the rule for determining taxable gains in the case of exchanges of property and to negative the assertion of tax in the case of certain purely paper transactions. The substance of this provision is that when property is exchanged for other property the property received in exchange shall be treated as the equivalent of cash to the amount of its fair market value, but when in connection with the reorganization or consolidation of a corporation a person receives in place of stock or securities owned by him new stock or securities of no greater aggregate par value, or when a person receives in place of property stock of a cor-

poration formed to take over such property, no gain or loss shall be deemed to occur from the exchange.

GAINS DERIVED FROM PROSPECTING, EXPLORATION, OR DISCOVERY.

The prospector for mines or oil and gas frequently expends many years and much money in fruitless search. When he does locate a productive property and comes to settle it seems unwise and unfair that his profit be taxed at the maximum rate as if it were ordinary income attributable to the normal activities of a single year. To stimulate prospecting and exploration, the committee has limited the surtax to 20 per cent of the selling price in the case of a bona fide sale of mines, oil or gas wells where the principal value was demonstrated by prospecting, exploring, or discovery work done by the taxpayer (sec. 211b, p. 18). A similar limitation has been imposed by the war excess-profits tax applicable to gains derived by a corporation from the bona fide sale of such mines, oil or gas wells (sec. 337, p. 107). Special provision is also made for increased depletion allowance in the case of such properties (sec. 214 (10), p. 28; and sec. 234 (9), p. 58).

TAXABLE AND NONTAXABLE INCOME.

The committee amended section 213a so as to require that any gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, and so on, be subject to income tax, leaving the constitutional question as to the authority of Congress to tax certain salaries to be settled by the courts in any case in which the question may be raised.

The proceeds of life insurance policies paid upon the death of the insured are, under the House bill, exempt from taxation only when paid to individual beneficiaries or to the estate of the insured (sec. 213b, 1). This limitation has been removed so as to place all beneficiaries (individual, corporate, or otherwise) on the same footing.

The exemption of soldiers' and sailors' salaries (sec. 213b, 8) has been modified by removing the \$3,500 limitation, but its operation has been restricted to the duration of the war, and it is made to apply only to those in active service.

The provision (sec. 213b, 4) subjecting the interest on new issues of State and municipal bonds to taxation as income was also stricken out. Apart from the constitutional question, it seemed unwise for Congress to attempt to impose this tax upon the obligations of States and municipalities as long as the States are not free to tax in a similar manner the obligations of the United States.

Bonds issued by the War Finance Corporation have been added to the list of obligations the interest on which is exempt from the tax (sec. 213b, 4). These bonds were issued under the same terms as the liberty bonds issued under the original act of September 24, 1917, with respect to exemption from taxation, and it is felt that no discrimination ought to be made in the income-tax law.

DEDUCTIONS.

The interest deduction (sec. 214a, 2, and sec. 234a, 2) has been amended so as not to permit a deduction for interest on indebtedness incurred or continued to purchase or carry tax-free securities other

than obligations of the United States issued after September 24, 1917. This limitation is substantially the same as the one contained in the present law. The provision of the House bill which allows a deduction for interest on all indebtedness permits the taxpayer to make loans for purchases of wholly exempt securities and then deduct the interest paid on such loans from his otherwise taxable income, thereby reducing his tax. The limitation suggested above would operate to discourage this practice except in the case of the later issue of liberty bonds.

Under the present law and under the bill as passed by the House a nonresident alien individual or a foreign corporation is not allowed to deduct any taxes paid to a foreign country. Many such taxpayers are, however, subject to taxation abroad upon property or business which is producing income subject to taxation in the United States. It seems only fair that such taxes paid to a foreign country should be deducted in computing net income subject to taxation in the United States, and provision for such deduction has been inserted (sec. 214a, 3, and sec. 234a, 3).

NET LOSSES.

One of the most important provisions inserted by the committee is quite new to our tax laws. At the present time no recognition is given to net losses; that is, if in any year the losses and expenses of a taxpayer exceed his gross income the excess (or in other words, the net loss) can not be carried over into the next year. For purposes of taxation the settlement must be made upon the basis of each year's business by itself. The chief merit of the present plan is its simplicity of administration. But it does not adequately recognize the exigencies of business, and, under our present high rates of taxation, may often result in grave injustice. The committee has accordingly incorporated an amendment (sec. 204) which provides that under certain limitations net losses sustained in 1917 or in 1918 may be deducted in computing the net income of the taxpayer for the succeeding taxable year; that a net loss sustained in the future may be deducted from the net income of the preceding taxable year, and if it is in excess of the net income for such preceding taxable year, that such excess may be allowed as a deduction in computing the net income for the succeeding taxable year. Provision is made for the necessary adjustment of the taxes for the years involved, and for crediting or refunding to the taxpayer any amounts found due under such adjustment.

AMORTIZATION.

In the paragraph relating to amortization allowances (sec. 214a, 9, and sec. 234a, 8) it was feared that the language was not broad enough to include vessels devoted to war purposes, and provision has therefore been made for the amortization allowance in the case of vessels constructed or acquired on or after April 6, 1917, for the transportation of articles or men contributing to the prosecution of the present war. The clause limiting the amortization deduction of 25 per cent of the net income has been stricken out. The amount of the amortization allowance to which a taxpayer may fairly be entitled

has little or no logical connection with the amount of his net income; and as a matter of fact the taxpayer is likely to need the full allowance most when his net income is small.

DEPLETION.

For the purpose of depletion allowance in the case of properties acquired prior to March 1, 1913, the provision of the present law, omitted in the House bill, has been restored by the committee, so that in the case of such properties the basis for the depletion allowance shall be the March 1, 1913, valuation; but a proviso has been added that where mines or oil and gas wells have been discovered by the taxpayer on or after March 1, 1913, and not acquired as a result of the purchase of a proven tract or lease, and where the fair market value is materially disproportionate to the cost, the depletion allowance shall be based upon the fair market value of the property at the date of the discovery or within 12 months thereafter (sec. 214a, 10, and sec. 234a, 9).

SHRINKAGE IN INVENTORIES.

The matter of anticipated losses through the shrinkage in value of inventories from the present high level received much attention from the committee. It was believed that the provision in regard to net losses above referred to might afford relief in certain cases. In order, however, to afford more prompt relief in case it should be discovered within a relatively short time after the close of a taxable year that a loss had been sustained resulting from a material reduction of the value of the inventory, or other similar cause, provision was made that the amount of the loss then discovered may be deducted from the net income of the preceding taxable year, any amount of tax thus found to have been overpaid to be promptly refunded (sec. 214a, 12, p. 29, and sec. 231a, 13, p. 60).

In the case of nonresident alien individuals and foreign corporations, expenses, losses, debts, depreciation, amortization, and depletion are, under the language of the House bill, allowed only to the extent that they are connected with a trade or business carried on within the United States, and the depreciation, amortization, and depletion deductions are allowed only with respect to property within the United States. In many cases, however, property outside of the United States is directly concerned in the production of income taxable in the United States. Accordingly, the limitation with respect to nonresident aliens and foreign corporations has been modified so that the specified deductions shall be allowed to the extent that they are connected with income arising from a source within the United States (sec. 214b and sec. 234b).

CONSOLIDATED RETURNS.

Provision has been made in section 240 for a consolidated return, in the case of affiliated corporations, for purposes both of income and profits taxes. A year's trial of the consolidated return under the existing law demonstrated the advisability of conferring upon the commissioner explicit authority to require such returns.

So far as its immediate effect is concerned consolidation increases the tax in some cases and reduces it in other cases, but its general and permanent effect is to prevent evasion which can not be successfully blocked in any other way. Among affiliated corporations it frequently happens that the accepted intercompany accounting assigns too much income or invested capital to company A and not enough to company B. This may make the total tax for the corporation too much or too little. If the former, the company hastens to change its accounting method; if the latter, there is every inducement to retain the old accounting procedure, which benefits the affiliated interests, even though such procedure was not originally adopted for the purpose of evading taxation. As a general rule, therefore, improper arrangements which increase the tax will be discontinued, while those which reduce the tax will be retained.

Moreover, a law which contains no requirement for consolidation puts an almost irresistible premium on a segregation or a separate incorporation of activities which would normally be carried as branches of one concern. Increasing evidence has come to light demonstrating that the possibilities of evading taxation in these and allied ways are becoming familiar to the taxpayers of the country. While the committee is convinced that the consolidated return tends to conserve, not to reduce, the revenue, the committee recommends its adoption not primarily because it operates to prevent evasion of taxes or because of its effect upon the revenue, but because the principle of taxing as a business unit what in reality is a business unit is sound and equitable and convenient both to the taxpayer and to the Government.

LIFE INSURANCE COMPANIES.

A new basis is recommended for the taxation of life insurance companies (Pt. IV, secs. 245, 246, 247). The tax is in form an income tax, but is imposed upon a net income defined with special reference to the peculiar conditions of the business of life insurance. Roughly, it consists of the gross income from interest, dividends, and rents less tax-free interest, investment expenses, and taxes and other expenses paid exclusively in connection with real estate owned by the company. In the case of a domestic life insurance company there is also a specific deduction of \$2,000. Thus the tax falls upon the true income of the company; that is, its income from investments; and the rate is so fixed that this tax takes the place of the income tax, war excess-profits tax, capital-stock tax, and the tax on the issuance of policies. It will yield considerably more revenue than the taxes which it is designed to replace, and has the great merit of simplicity and certainty. Above all, it avoids the almost insuperable difficulty of defining the invested capital of a life insurance company for purposes of the war excess-profits tax.

PAYMENT OF TAXES.

The installment plan for payment of taxes adopted in the House bill has been retained; but, in accordance with the recommendation of the Secretary of the Treasury, in place of three installments at intervals of two months there have been provided four installments at intervals of three months. The provision relating to extensions has

been changed so that an extension of time for filing the returns serves automatically to extend the time for the payment of installments. Where the payment of any installment is postponed because of such extension, interest is charged at the rate of one-half of 1 per cent a month. No interest, however, will be charged if the whole amount of the tax is paid on or before the time the third installment would have been due if no extension has been granted.

The language of the House bill requires notice and demand by the collector before a penalty accrues for failure to pay the tax on time. In order to avoid the necessity of a personal notice to every taxpayer, a proviso has been added to the effect that in the case of the first installment the instructions printed on the return shall be deemed sufficient notice of the date when the tax is due and sufficient demand.

Authority is given to the commissioner to take summary proceedings for the collection of the tax in cases where there is evidence that the taxpayer designs to evade the tax by a sudden departure from the United States or by removal or concealment of his property (sec. 250g).

REFUND.

Under the House bill the Government has five years within which to determine and assess the tax. In section 252, as amended by the committee, the two-year limitation upon the right of the taxpayer to obtain a credit or refund has been removed, so that the taxpayer's right shall not be prejudiced by any delay on the part of the Government in discovering that he has made an overpayment. Under the section, as amended, the limitation upon the taxpayer is the same as that upon the Government.

INFORMATION AT SOURCE.

Provision is made in section 256 for returns of information in the case of payments, which are at the rate of \$1,000 or more a year, as well as in the case of actual payments of \$1,000 or over; but in order not to burden taxpayers with the labor and expense of furnishing useless information, returns of information are to be made only to such extent as may be prescribed by the commissioner with the approval of the Secretary. This is especially important on account of the present scarcity of clerical labor both inside and outside of the department.

ACCESS TO RETURNS AS PUBLIC RECORDS.

Access to returns of corporations is extended to the proper officers of any State without limitation as to whether such State imposes an income tax (sec. 257), and also to all bona fide stockholders of record holding at least 1 per cent or more of the stock of any corporation.

RETURNS OF INDIVIDUALS.

As an aid in assuring the full enforcement of a tax, section 228 requiring returns of individuals having net incomes in excess of certain specified amounts has been changed so as to require returns in the case of persons having gross incomes of specified amounts.

TITLE III.—WAR EXCESS-PROFITS TAX.

Before directing attention to the changes in the war excess-profits tax, which the committee does recommend, it may be helpful to explain why the committee does not indorse certain proposed changes which have been advocated by some.

In the first place, the committee does not recommend that individuals and partnerships be brought under the war excess-profits tax, but follows the provisions of the House bill in this respect. Individuals and partnerships pay the heavy surtaxes upon all net income, whether left in the business or not, while corporations and their stockholders are relieved from surtaxes upon the portion of the earnings which is not distributed. This inequality is more than compensated for by the fact that the corporation is—while the individual and partnership are not—subject to the war excess-profits tax. The situation as between the different forms of business organization having been thus brought into approximate balance, it was deemed proper to relieve the corporation from the 6 per cent differential income tax provided by the House bill.

The committee proposes that personal-service corporations (those whose earnings are to be ascribed primarily to the activities of the principal owners or stockholders) be exempted from the profits tax and be treated as partnerships; i. e., that the stockholders, like partners, be subject both to normal tax and surtaxes upon the entire earnings of the corporation, whether distributed or not. When the undivided shares of such earnings are large the additional surtaxes will more than make up for the loss of the profits tax. The war excess-profits tax, moreover, can not be applied to personal-service corporations, because such corporations have, as a rule, very little invested capital, and the tax, if computed in the ordinary way, would be excessive. The committee thus solves the old problem of dealing with the close corporation, which is used as a medium of avoiding payment of surtaxes.

INVESTED CAPITAL.

The committee refrains also from recommending any radical change in the method of computing invested capital, although a number of important improvements are suggested in this connection. Speaking generally, assets are valued, for the purpose of determining invested capital, at the price paid in acquiring them without recognition of subsequent appreciation. Weighty arguments have been presented in favor of abandoning this rule and valuing property acquired before March 1, 1913, as of that date. But the committee believes that such a method would be impracticable; that it would impose upon the Treasury Department the impossible task of valuing nearly all of the durable property of the country as of a date nearly six years in the past. The present statutory rule works well in a large majority of cases. The remaining cases, in which it works injustice, can and should be cared for by adequate relief provisions which the committee has carefully formulated and recommends. The committee therefore indorses the general rule expressed by the House bill in paragraph (8) of subdivision (a) of section 326, but believes that in certain

exceptional cases inability to recognize appreciation furnishes just ground for relief, and in order that such relief may not be imperiled by overemphasis upon the general principle recommends that the explicit denial of the right to include any increase in the value of assets above original cost be stricken from section 326.

RATES OF THE WAR EXCESS-PROFITS TAX.

The House bill provides, in effect, alternative war-profits and excess-profits taxes, the taxpayer to pay whichever is the higher. To this plan grave objection was made on constitutional grounds and because the scheme was troublesome to the taxpayer. The plan was also criticized as conferring undue discretion on the Treasury Department.

In place of this alternative scheme the committee recommends a single war excess-profits tax, which is mathematically equivalent to an alternative plan at the same rates. It unifies the two taxes by the simple device of including the war-profits tax as an additional bracket of the rate schedule.

The committee has also simplified and reduced the rates of the excess-profits tax adopted by the House. The rates imposed in the House bill were 35 per cent of the net income in excess of the excess-profits credit (\$3,000 plus 8 per cent of the invested capital) and not in excess of 15 per cent of the invested capital; 50 per cent of the net income in excess of 15 per cent and not in excess of 20 per cent of the invested capital; and 70 per cent of the net income in excess of 20 per cent of the invested capital. The committee proposes in lieu of the House brackets of 35, 50, and 70 per cent two brackets of 30 and 60 per cent, with no change in the deduction or "excess-profits credit." The third bracket of the committee plan is, as stated before, simply the war-profits tax of 80 per cent.

The preceding rates are applicable only to taxes payable in 1919 covering income for the year 1918. For the year 1920 and thereafter, the war-profits tax (or bracket) is repealed, and the excess-profits rates are reduced from 30 and 60 per cent to 20 and 40 per cent.

LIMITATION ON TAX OF SMALL CORPORATIONS.

Experience with the existing excess-profits tax proves beyond doubt that the tax discriminates against small corporations. Some limitation of the tax upon small corporations is thus required. The method of limiting the tax adopted in the House bill is, however, open both to economic and possible legal objections. A few dollars difference in the income or invested capital might, under the House bill, make thousands of dollars difference in the tax. Your committee accordingly recommends the adoption of a limit so fixed that the tax can in no case be more than 30 per cent of the net income in excess of \$3,000 and not in excess of \$20,000, plus 80 per cent of the net income in excess of \$20,000. Thus, the tax of a corporation with profits of \$20,000 or less can not exceed 30 per cent of such profits less \$3,000. To the very large corporation this limitation will obviously not afford any substantial reduction of the tax. To the small corporation it will mean a great deal. For the year 1920 the limit has been adjusted (to correspond with the change made in the rates of the excess-profits

tax) so that the tax can in no case be more than 20 per cent of the net income in excess of \$3,000 and not in excess of \$20,000 plus 40 per cent of the net income in excess of \$20,000.

WAR-PROFITS CREDIT FOR CORPORATIONS ORGANIZED SINCE THE PREWAR PERIOD (SEC. 311C, P. 90).

The House bill defines the war-profits credit for the new corporation—i. e., the corporation organized since the prewar period—as the sum of \$3,000 plus 10 per cent of the invested capital for the taxable year. This places the new corporation in a trade or business whose normal profits for the prewar period were above 10 per cent at a great disadvantage as compared with corporations which happened to be in existence during the prewar period. A majority of the older corporations might enjoy a deduction of from 12 to 15 per cent, because their profits in the prewar period were that high, but the new corporation under the House bill would be restricted to a deduction of 10 per cent.

The committee accordingly recommends that the new corporation be placed on an equality with the old corporation in this respect by granting to the new corporation a percentage deduction equal to same per cent of its invested capital as was earned on the average, during the prewar period, by representative corporations engaged in a trade or business of the same general class as that conducted by the new corporation in question.

INVESTED CAPITAL—TANGIBLE PROPERTY PAID IN FOR STOCK OR SHARES.

In its definition of invested capital the House bill provides that tangible property paid in for stock or shares may in no case exceed the par value of the original stock or shares specifically issued therefor. Such a limitation would work grave injustice in case of highly conservative corporations which have acquired property for stock or shares, the par value of which was (at the date of acquisition) materially less than the actual value of the tangible property acquired. The committee recommends, therefore, that where the actual cash value of such tangible property is shown to the satisfaction of the Commissioner of Internal Revenue to have been clearly and substantially in excess of the par value of the stock or shares paid therefor, such excess shall be treated as paid-in surplus.

This amendment seeks to enact into law the substance of a regulation of the Treasury Department, which has worked well and which has not led either to abuse or the filing of an excessive number of claims. It is highly important that this regulation be placed on a statutory basis and continued.

THE "20 PER CENT LIMITATION" UPON INTANGIBLE PROPERTY.

The existing law and the House bill as well provide that intangible property paid in for stock or shares prior to March 3, 1917, may not be included in invested capital at a value in excess of 20 per cent of the par value of the total stock or shares of the corporation outstanding on March 3, 1917. While this figure—20 per cent—has not been

changed, the definition of intangible property has been greatly enlarged. Under the existing law, however, patents and copyrights are not defined as "intangible property," and they are not subject to the 20 per cent limitation; while under the proposed bill the definition of intangible property has been extended to include patents and copyrights. Because of this increase in the scope and content of the term "intangible property," the 20 per cent limit impresses the committee as obviously too low, and we recommend accordingly that it be increased to 30 per cent.

INTANGIBLE PROPERTY PAID IN FOR STOCK OR SHARES ON OR AFTER
MARCH 3, 1917.

The House bill provides flatly that intangible property (other than patents and copyrights) paid in for stock or shares on or after March 3, 1917, shall not be included in invested capital; but that patents and copyrights paid in after that date may be included in invested capital under certain specified conditions. This discrimination between patents or copyrights and other intangible property impresses the committee as unwarranted. Patents and copyrights give rise to as much abuse in connection with overcapitalization as other forms of intangible property. Moreover, sufficient protection against abuse would seem to be provided in the provision that intangible property can not be included in invested capital at an amount in excess of the actual cash value of such property at the time paid in. It is recommended therefore that all intangible property acquired for stock on or after March 3, 1917, be permitted to count as invested capital, under the conditions and safeguards applicable to patents and copyrights.

RELIEF PROVISIONS.

No part of Title III is as important as the so-called relief provisions. The business world is apprehensive about the operation of the war excess-profits tax, and it is true that the ordinary method of computing invested capital would in certain exceptional cases work great hardship. There is a measure of truth, for instance, in the the current criticism that the war excess-profits tax places a heavy penalty on conservative financing and a corresponding premium on overcapitalization.

The committee therefore believes it necessary to provide a special method of determining the tax for those cases in which the ordinary method of assessment would result in grave hardship or serious inequality. To do this is not to confer an arbitrary discretion upon the administrative authorities; it is merely an exercise of the legislative power of reasonable classification. Indeed without such classification the constitutionality of the whole tax might, because of its unequal operation, be open to serious question.

The committee has materially increased the number of cases for which the House bill grants relief. It is not necessary here to enumerate these cases. It is sufficient to say that they represent the principal classes of cases which a year's experience with the excess-profits tax prove to be in need of special treatment. The committee moreover

believes that these relief powers should not be hidden under vague and general phraseology. The business world is apprehensive of the operation of a war excess-profits tax at the high rates which war exigencies make necessary. It is entitled to be reassured, explicitly and frankly, by the enactment of carefully safeguarded provisions for the relief or prevention of injustice and inequality.

TITLE IV.—INHERITANCE TAX.

SUBSTITUTION OF INHERITANCE TAX FOR ESTATE TAX.

The committee has substituted for the estate tax provided in the House bill, which is a modification of the existing estate-tax provisions with very greatly increased rates, an inheritance tax. Under the estate-tax plan the progressive rates are graded in accordance with the size of the net estate as a whole, without regard to the amount of the shares of individual legatees or heirs. According to this method a beneficiary receiving a legacy of any given sum, say \$100,000 from an estate of \$1,000,000, may have that share diminished by a much greater amount of tax than a beneficiary who receives the same sum from a smaller estate. The method of taxation employed in practically all of the States is that of an inheritance tax in which the rate of tax is based upon the size of the individual share. It was the opinion of the committee that the inheritance-tax plan is fairer and more equitable in its operation than the estate-tax plan.

The general scheme embodied in the amendment which appears on pages 111 to 128 of the bill is accordingly that of a progressive inheritance tax classified on the basis of the size of the inheritances. No difference in the rate is made because of the relationship of the beneficiary, but it is provided that no tax shall apply on transfers by reason of the death of a decedent dying during the continuance of the present war while serving in the military or naval forces of the United States, or dying within one year after the termination of the war from injuries received or disease contracted in such service. Provision is also made for exemption from the tax of transfers for public or for religious, charitable, scientific, or literary purposes.

The method of collection provided in the estate tax act is retained; that is, the executor is made liable for the payment of the tax and the property of the estate is subject to a lien for it, but provisions are added rendering the ultimate beneficiaries liable to the executor for taxes upon their respective interests.

The difficult feature of the plan, as in all inheritance laws, was to provide for the tax upon contingent future interest. This difficulty has been handled by providing for the application of the tax to the separate determinable interests, present or future, in the net estate, and the treatment of the remainder of the net estate as to which the ultimate disposition can not be presently determined as a single share or interest. This method is provided for in section 4-3. The matter of valuing annuities and remainders is covered in the customary way in section 404.

Provision is made that inheritance taxes assessed by the various States may be deducted in determining the net estate, while under the House bill they are not permitted to be taken into account.

So far as possible, subject to the change in method which was adopted, the structure of the statute follows that of the estate tax provisions (secs. 400-415, pp. 120-136).

TITLE V.

The provisions of this title are retained without substantial change, except the striking out of the tax on the issue of life insurance policies necessitated by reason of the new plan adopted for the taxation of such companies.

TITLE VI.—TAX ON BEVERAGES.

RATES (SEC. 600.)

The committee saw no sound reason for increasing the tax on non-beverage alcohol above the present rate of \$2.20 on each proof gallon. This alcohol is largely used for medicines and medicinal preparations and for household necessities, such as flavoring extracts, the cost of which has already become very high. The tax on distilled spirits withdrawn for beverage purposes was reduced from \$8 to \$6.40, this being double the present rate, with the belief that more revenue would be secured at this rate than at the higher rate.

DISTILLED SPIRITS LEFT IN BOND AFTER PROHIBITION.

It seemed necessary to make provision as to the treatment of distilled spirits which may be left in bond after the effective date of prohibition, and such a provision appears in subsection (b) of section 600 (pp. 137-139). This subsection provides essentially (1) that no tax shall become payable in respect of any such spirits after the effective date of prohibition; (2) that all bonds previously executed to secure the payment of tax shall be canceled as of the date prohibition takes effect; (3) that distillers having spirits in bond on that date shall execute a bond to keep in good condition the bonded warehouses and the spirits in them, and not to remove or suffer to be removed contrary to law any such spirits; (4) that the distiller may have the option to leave in bond distilled spirits upon which the tax would become due at the new rates in the interval before the effective date of prohibition; and (5) that on removal of prohibition additional allowance may be made for loss in the spirits by reason of their longer storage in the warehouse. Provision was also made for distilled spirits and wines held in customs bonds (sec. 600b).

To prevent the total loss owing to prohibition, of vineyards developed through many years for the production of wine, it was provided that under proper regulations wines may be produced and existing stocks of wine may be utilized for the making of nonbeverage spirits and nonalcoholic wines (sec. 618b).

TITLE VII.—TAX ON CIGARS, TOBACCO, AND MANUFACTURERS THEREOF.

REPEAL OF "FREE LEAF" ACT.

Aside from changes in rates, the only change of importance made in the tobacco provisions is the addition of section 704. By this new section the so-called "free-leaf act" appearing in section 35 of the

act of August 5, 1909, is repealed. That section permitted the carrying on of a retail business in leaf tobacco without tax liability. Apparently this right has not been extensively used. It is feared that owing to the largely increased rates upon manufactured tobacco, untaxed leaf tobacco might under this provision be brought into substantial competition with the tax-paid product. It is therefore provided as was the case previous to the act of August 5, 1909, that buyers of leaf tobacco may make shipments only to other dealers in leaf tobacco or to registered manufacturers or for export. No restriction is, however, placed upon the farmer or grower of tobacco in respect of leaf tobacco produced by him.

The amendment of section 3360 of the Revised Statutes provided for in this section is designed to enable the Internal Revenue Bureau to secure better records of the disposition and handling of leaf tobacco. It is also provided that upon such tobacco sold or removed or shipped otherwise than in accordance with law, there shall be a tax equivalent to the tax upon manufactured tobacco.

TITLE VIII.—TAX ON ADMISSIONS AND DUES.

The rate of tax on admissions and dues was changed from the general rate of 20 per cent to the general rate of 10 per cent provided in the existing law.

The provision making the dues tax applicable to dues paid to produce exchanges, boards of trade, and other similar organizations was stricken out.

TITLE IX.—EXCISE TAXES.

In section 900 certain rates were reduced and some of the proposed new taxes were omitted.

The tax in respect of motion-picture films was changed into a license tax of 5 per cent upon the total rentals earned from each lease or license, as it was believed that this rate is equitable and that this method of taxation will insure collection upon all taxable gross revenue arising from the rental of motion-picture films (sec. 905, p. 204).

The tax on gasoline provided for in section 902 of the House bill was stricken out.

Section 905, levying taxes in respect of the excess of certain arbitrary amounts paid for various articles in common use, was stricken out.

SALES FOR EXPORT.

Provision was made that the excise taxes levied by this title should not apply in respect of articles sold or leased for export and in due course so exported (sec. 907, p. 207).

TITLE X.—SPECIAL TAXES.

The House bill provided for the continuance of the capital stock tax on the basis of the fair average value of the capital stock of the corporation for the preceding year. The determination of fair

average value has proved in administration to be very difficult. The committee has accordingly provided that the basis of the tax shall be the amount of the net assets of the corporation as shown by its books. It is believed that this basis of levying the tax is just and that the change will not lead to any reduction of the revenue from this source.

Certain changes in rates were made, and the proposed tax on the use of automobiles was stricken out.

TITLE XI.—STAMP TAXES.

No changes of importance were made in this title, except that a provision was made for a special tax of 5 cents on each dollar of premium charged under each policy of insurance or its equivalent issued to or for a domestic corporation, partnership, or individual by any foreign corporation, partnership, or individual when such policy or instrument is not signed or countersigned by an officer or agent of the insurer in a State, Territory, or District of the United States in which the insurer is authorized to do business (sec. 1107 (15), p. 241).

TITLE XII.—CHILD LABOR.

The committee proposes the insertion of a new title imposing an excise tax of 10 per centum on the net profits upon the operation of (a) any mine or quarry situated in the United States in which children under the age of 16 years have been employed or permitted to work during any portion of the taxable year; or (b) any mill, cannery, workshop, factory, or manufacturing establishment situated in the United States in which children under the age of 14 years have been employed or permitted to work, or children between the ages of 14 and 16 have been employed or permitted to work more than eight hours in any day or more than six days in any week, or after the hour of 7 o'clock post meridian, or before the hour of 6 o'clock a. m. during any portion of the taxable year.

Such tax is not to apply in the case of an employer relying in good faith upon an employment certificate issued under regulations prescribed by a board composed of the Secretary of the Treasury, the Secretary of Labor, and the Commissioner of Internal Revenue; nor in the case of an employer who satisfies the Secretary of the Treasury that his employment of a child under the prescribed ages was due to an honest mistake of fact as to the age of such child.

TITLE XIII.—GENERAL ADMINISTRATIVE PROVISIONS.

GENERAL PENALTY PROVISION.

The provision making general provision for penalties appearing in the House bill was found to involve possible duplication of penalties for the same offense. The section was redrawn to make clear the precise offense to which it applies and to avoid conflict with or duplication of other provisions (sec. 1308, p. 256). Changes have also been made elsewhere in the bill to prevent a duplication of penalties under specific and general provisions of the statute, and the amounts of some of the assessable penalties have been changed.

APPLICATION OF SALES TAX IN THE CASE OF PREEXISTING CONTRACTS.

The provision in the House bill with reference to the situation arising by reason of the application of a tax in respect of a sale effected under a contract made prior to any notice of the tax, and which does not permit the passing on of the tax, was limited to the case of such contract between a manufacturer and a dealer. Where such contract was made with a person other than a dealer covering any article in respect to which a corresponding tax was imposed by the revenue act of 1917, your committee changed the House provision so that such person should pay the tax under the act of 1917, and no further tax should be imposed. Otherwise the House provision has not been changed.

TITLE XIV.—GENERAL PROVISIONS.

Your committee has substituted for the general repeal in the House bill of "any provisions of any act inconsistent with any provisions of this act" a specific repeal of all those titles and sections of the revenue act of September 8, 1916, the act of March 3, 1917, and the revenue act of October 3, 1917, which are covered by the bill. It is believed that this will make it easier for the taxpayer and the Treasury Department to know exactly what provisions of law are expressly repealed.

POSTAL RATES.

A new section (sec. 1401) has been inserted by the committee, repealing, as of July 1, 1919, the increase of postage on letters and post cards provided by section 1100 of the revenue act of 1917.

Another new section (sec. 1402) repeals the provisions of section 1101 of the revenue act of 1917, which establish a zone system for second-class mail matter (newspapers and periodicals), and substitutes therefor a provision that on and after July 1, 1919, the rate on such class of mail matter shall be 1 cent a pound for delivery within the first and second zones (150 miles) and 1½ cents a pound for all other zones.

The report of the Ways and Means Committee of the House is hereto attached. It is as follows:

REVENUE BILL OF 1918.

SEPTEMBER 3, 1918.—Committed to the Committee of the Whole House on the state of the Union and ordered to be printed.

Mr. KITCHIN, from the Committee on Ways and Means, submitted the following

REPORT.

[To accompany H. R. 12863.]

The Committee on Ways and Means, to whom was referred the bill (H. R. 12863) to provide revenue, and for other purposes, having had the same under consideration, reports it back to the House without amendment and recommends that the bill do pass.

THE FIRST PROBLEM IN DETERMINING OUR FISCAL POLICY TO FINANCE THIS WAR.

In determining our fiscal policy for financing the war the first question that must be determined is, what per cent of our total expenditures shall be financed by taxation and what per cent by bonds? Your committee has determined the proportion of the cost of the war that should be financed by taxation and by bonds not upon the basis of previous experience, for there is no analogy in history, but upon a careful consideration of the effect of the fiscal policy upon the morale of the people, upon the inflation of prices, upon production, and with reference to the relative ability of the people to pay taxes now and after the war.

On June 5 the Secretary of the Treasury advised your committee that the probable expenditures for the fiscal year ending June 30, 1919, would be about \$24,000,000,000 and recommended that one-third of this amount be raised in taxes, or \$8,000,000,000. On July 15 Mr. Sherley, chairman of the Appropriations Committee of the House, confirmed the estimate of the Secretary of the Treasury and set out in detail the appropriations for this fiscal year, the total of which amount to \$24,328,561,427.67, exclusive of contract authorizations.

PREPARATION OF THE MEASURE.

On May 27, 1918, the President addressed the Congress in joint session and recommended that the Congress set to work immediately to draft the new revenue measure and recommended that the necessary additional taxes be secured from war profits, incomes, and luxuries. The Ways and Means Committee immediately began the preparation of the new measure, and on May 29, 1918, the chairman, after conference with the Ways and Means Committee, gave out the following statement relative to hearings on the proposed new revenue bill:

The Committee on Ways and Means announce to all concerned that it will hold public hearings at Washington, D. C., beginning June 6, 1918.

It is deemed necessary largely to increase the revenue from taxation. It seems to the committee that it will be necessary to raise the necessary increased revenue chiefly from taxes upon incomes, excess of war profits, luxuries, and semiluxuries.

In the preparation of the new tax measure the committee will give careful consideration to all suggestions with reference to the measure, together with suggestions of other revenue sources.

Your committee sat in daily hearings from June 7 to July 17, and since that time has been in continual daily session engaged in the preparation of the measure.

At the beginning of the preparation of the new measure your committee accepted the fiscal policy, suggested by the Secretary, as sound, and determined to prepare a new revenue bill that would raise during a 12-month period \$8,000,000,000. In making the decision to recommend that one-third of the expenditures for the current fiscal year be raised by taxes and two-thirds from the sale of bonds, your committee has been guided by conditions existing at the present time. While your committee makes this recommendation for the current year, it realizes that no fixed policy as to the relation of taxes to bonds for the future can be determined at this time and that the amount that should be raised by taxation in any given year must necessarily be determined after due consideration is given to business and financial conditions existing in such year. Your committee further adopted the policy that so far as practicable the \$8,000,000,000 should be raised from taxes on incomes, excess and war profits, and luxuries and semiluxuries.

Throughout the preparation of the measure your committee has endeavored to distribute equitably the new tax burden and to levy the taxes in such a way that the burden should be met by those most able to pay. Your committee has endeavored to wipe out all inequalities in the operation of existing law and recommends the repeal of the major portions of the revenue acts of 1916 and 1917 in order that the existing internal-revenue laws so far as deemed practicable will be in one act and therefore more readily accessible to the taxpayer. A law of so great magnitude as this with the necessary exemptions and similar provisions in the interest of quality and justice must of necessity be more or less complicated, but your committee has striven to make this bill as simple and clear as possible in every particular.

THE NEW MEASURE.

The bill is divided into 14 titles, as follows:

- Title I. General definitions.
- Title II. Income tax.
- Title III. War profits and excess profits tax.
- Title IV. Estate tax.
- Title V. Tax on transportation and other facilities and on insurance.
- Title VI. Tax on beverages.
- Title VII. Tax on cigars, tobacco, and manufactures thereof.
- Title VIII. Tax on admissions and dues.
- Title IX. Excise taxes.
- Title X. Special taxes.
- Title XI. Stamp taxes.
- Title XII. Advisory Tax Board.
- Title XIII. General administrative provisions.
- Title XIV. General provisions.

TITLE I. GENERAL DEFINITIONS.

This title contains definitions applicable to the entire bill. The following terms are defined in this title: Person, corporation, domestic, foreign, United States, Secretary, commissioner, collector, revenue act of 1916, revenue act of 1917, taxpayer, and Government contract.

TITLE II. INCOME TAX.

Part I. GENERAL PROVISIONS.

DEFINITIONS.

Part I of Title II contains the definitions applicable to the income tax only. In this part (sec. 200) the following terms are defined: Taxable year, fiscal year, fiduciary, withholding agent, and dividend. This part (secs. 201 and 202) also states the basis for determining gain or loss and for taking inventories.

The dividend provision makes any distribution made by a corporation out of its earnings or profits accrued since February 28, 1913, and payable to its shareholders or members, whether in cash or in other property or in stock of the corporation, subject to tax in the hands of the shareholder, the same as under the present law. It also provides that any distribution made in 1918 or subsequent years shall be deemed to have been made from earnings or profits accrued since February 28, 1913. The present law provides that dividends distributed to the stockholder shall be taxable to the individual at the income-tax rates in effect in the year in which the dividend is received, unless the corporation distributes more than its earnings for the taxable year, in which case the additional amounts so distributed are taxable in the hands of the individual at the rates in effect during the year in which the corporation earned the same. Under the proposed bill all distribution of earnings accrued since February 28, 1913, will be taxable in the hands of the stockholder according to the rates in effect during the year in which the dividend

is received. The proposed bill, like the present law, provides that earnings or profits accrued prior to March 1, 1913, may be distributed in stock dividends or otherwise exempt from tax after the earnings and profits accrued since February 28, 1913, have been distributed.

Under court decisions an addition to surplus through reappraisal of assets is not made out of earnings or profits, and therefore a distribution of the amount so added to surplus would not be a taxable dividend, since not made out of earnings or profits. In order to prevent tax evasion by this method, it is provided by the proposed bill that any distribution made shall be deemed to have been made from earnings or profits unless all earnings and profits have first been distributed.

BASIS FOR DETERMINING GAIN OR LOSS.

In determining gain or loss from the sale or disposition of property, real, personal, or mixed, the bill provides that the basis shall be as follows:

In the case of property acquired before March 1, 1913, the fair market price or value of such property as of that date; and in the case of property acquired on or after that date, (1) the cost thereof, or (2) the inventory value, if the inventory is made in accordance with the rules and regulations to be prescribed by the Commissioner of Internal Revenue in order that the inventory may clearly reflect the income.

INVENTORY.

In many cases the only way that the net income can be determined is through the proper use of inventories. This is largely true in the case of manufacturing and merchandise concerns. The bill authorizes the commissioner to require inventories whenever in his opinion the same is necessary in order clearly to reflect the income of the taxpayer.

Part II. INDIVIDUALS.

NORMAL TAX.

Under existing law a normal tax of 2 per cent is levied under the revenue act of 1916, upon the amount of the net income of a head of a family or married person in excess of \$4,000 and upon the amount of the net income of a single person in excess of \$3,000. A like normal tax of 2 per cent is also levied under the revenue act of 1917 upon the amount of the net income of a married person or head of a family in excess of \$2,000 and in the case of a single person in excess of \$1,000. In lieu of the rates now in effect the proposed bill (sec. 210) levies upon citizens or residents of the United States a normal tax of 12 per cent upon the amount of the net income in excess of credits provided in section 216, but provides that upon the first \$4,000 of this amount the rate shall be only 6 per cent.

UNEARNED INCOME.

The committee gave careful consideration to the advisability of making a differential between earned and unearned income, but finally determined that a flat normal tax was advisable in view of the

difficulty experienced by the committee in finding a satisfactory method of distinguishing between earned and unearned income (a difficulty also experienced by the Treasury Department) and in view of the almost insuperable difficulties in the administration of such a differential and the added complications in the law which would be necessitated thereby. The Treasury Department also gave careful consideration to this question and reached the same conclusion as the committee.

CREDITS.

In determining the amount of net income for the purpose of the normal tax only the following credits are allowed (sec. 216): (1) The amount received as dividends from a corporation. (2) Any amount received as interest upon obligations of the United States, any State, Territory, any political subdivision thereof, or the District of Columbia, if the same has been included in gross income. (3) In the case of a single person, an exemption of \$1,000 or in the case of a head of a family or a married person living with husband or wife, a personal exemption of \$2,000. A husband and wife living together are entitled to but one personal exemption of \$2,000. If a husband and wife make separate returns either one may take credit for the \$2,000 or they may divide the same between them. (4) An additional credit of \$200 is allowed a taxpayer for each dependent receiving his chief support from the taxpayer if the dependent is under 18 years of age or incapable of self-support because mentally or physically defective.

The only changes in the credit provisions are as follows:

For the purpose of the normal tax levied under the act of 1916, a single person was entitled to a personal credit of \$3,000 and a married person or head of a family to \$4,000. The proposed bill reduces this exemption to the exemption provided under the revenue act of 1917, namely, \$1,000 in the case of single persons and \$2,000 in the case of heads of families or married persons. Under the revenue act of 1917 a credit of \$200 was allowed a taxpayer for each dependent child under the age of eighteen years. The proposed bill allows the same exemption for dependent children under eighteen years of age, but extends the \$200 exemption to cover persons receiving their chief support from the taxpayer who are incapable of self-support because mentally or physically defective.

NONRESIDENT ALIENS.

Under existing law a nonresident alien is not entitled to a personal exemption, but is only subject to a 2 per cent normal tax. The bill provides that the normal tax upon nonresident aliens be made the same as in the case of citizens or residents, namely, 12 per cent of the net income in excess of the credits provided in section 216 (but without any reduction to 6 per cent on the first \$4,000) and that nonresident aliens be entitled (sec. 217) to the same deductions and credits as citizens of the United States if they file or cause to be filed with the collector a true and accurate return of their total income received from all sources corporate or otherwise in the United States, and include therein all the information which the commissioner may deem necessary for the calculation of such

deductions and credits. Provision is made in the bill (sec. 217) to allow the commissioner in his discretion to permit nonresident aliens to file a claim for the personal exemption with the withholding agent in cases where the income is withheld at the source.

The bill also provides (sec. 216 (e)) that if the nonresident alien is a citizen or subject of a country which imposes an income tax the personal exemption shall be allowed only if such country allows a similar exemption to United States citizens residing in such country.

SURTAX.

The following table shows the surtaxes levied under existing law and the proposed bill:

Table showing surtaxes levied under existing law and under the proposed bill.

Income.		Surtax rates under—	
		Existing law (per cent).	Proposed bill (per cent).
\$5,000—	\$7,500.....	1	2
7,500—	10,000.....	2	3
10,000—	12,500.....	3	7
12,500—	15,000.....	4	7
15,000—	20,000.....	5	10
20,000—	30,000.....	8	15
30,000—	40,000.....	8	20
40,000—	50,000.....	12	25
50,000—	60,000.....	12	32
60,000—	70,000.....	17	38
70,000—	80,000.....	17	42
80,000—	90,000.....	22	46
90,000—	100,000.....	22	48
100,000—	150,000.....	27	50
150,000—	200,000.....	31	50
200,000—	250,000.....	37	52
250,000—	300,000.....	42	52
300,000—	500,000.....	46	54
500,000—	750,000.....	50	58
750,000—	1,000,000.....	55	58
1,000,000—	1,500,000.....	61	60
1,500,000—	2,000,000.....	62	60
2,000,000—	5,000,000.....	63	60
Over 5,000,000.....		63	66

The following table shows the income tax levied under existing law and under the proposed bill for specified incomes:

Table showing the income tax levied under existing law and levied under the proposed bill for specified incomes of married persons without dependents and without dividends from corporations or interest from tax-free securities.

Incomes.	Tax under—		Per cent of tax to net net income.	
	Existing law.	Proposed bill.	Existing law (per cent).	Proposed bill (per cent).
\$2,500.....	\$10	\$30	0.40	1.20
3,000.....	20	60	.67	2.00
3,500.....	30	90	.86	2.67
4,000.....	40	120	1.00	3.00
4,500.....	60	150	1.33	3.33
5,000.....	80	180	1.60	3.60
5,500.....	105	220	1.91	4.00
6,000.....	130	260	2.16	4.33
6,500.....	155	330	2.38	5.06
7,000.....	180	400	2.57	5.71
7,500.....	205	470	2.73	6.27
8,000.....	235	545	2.98	6.81
8,500.....	265	620	3.12	7.29
9,000.....	295	695	3.28	7.72
9,500.....	325	770	3.42	8.11
10,000.....	355	845	3.55	8.45
12,500.....	530	1,320	4.24	10.56
15,000.....	730	1,795	4.87	11.97
20,000.....	1,180	2,895	5.90	14.48
25,000.....	1,780	4,245	7.12	16.98
30,000.....	2,380	5,595	7.93	18.65
35,000.....	2,980	7,195	8.51	20.53
40,000.....	3,580	8,795	8.95	21.99
45,000.....	4,280	10,645	9.73	23.66
50,000.....	5,180	12,495	10.36	24.99
55,000.....	5,980	14,695	10.87	26.72
60,000.....	6,780	16,895	11.30	28.16
70,000.....	8,880	21,895	12.69	31.26
80,000.....	10,980	27,295	13.73	34.12
100,000.....	16,180	39,095	16.18	39.10
150,000.....	31,680	70,095	21.12	46.73
200,000.....	49,180	101,095	24.59	50.55
300,000.....	92,680	168,095	30.89	55.03
500,000.....	182,680	297,095	38.54	59.42
1,000,000.....	475,180	647,095	47.52	64.71
5,000,000.....	3,140,180	3,527,095	62.80	70.54

The following table shows the income taxes imposed in the United States, United Kingdom, Canada, and France.

Income taxes upon specified incomes of married persons or heads of families with no dependents levied in the United States, United Kingdom, Canada, and France.

Income of married persons or heads of families.	United States tax under—				United Kingdom tax.				Canada.		France.	
	Existing law.		Proposed bill.		Amount.		Rate (per cent.)		Amount.	Rate (per cent.)	Amount.	Rate (per cent.)
	Amount.	Rate (per cent.)	Amount.	Rate (per cent.)	Unearned.	Earned.	Un-earned.	Earned.				
\$2,500	\$10	0.40	\$30	1.20	\$281.25	\$210.94	11.25	8.44	\$10.00	0.40	\$31.25	1.25
3,000	20	.67	60	2.00	445.31	356.25	14.84	11.87	20.00	.67	50.00	1.67
3,500	30	.86	90	2.57	568.44	453.75	16.24	12.96	40.00	1.14	72.50	2.07
4,000	45	1.00	120	3.00	726.56	581.25	18.16	14.53	60.00	1.50	97.50	2.44
4,500	60	1.33	150	3.33	843.75	675.00	18.75	15.00	80.00	1.78	128.75	2.86
5,000	80	1.60	180	3.60	937.50	750.00	18.75	15.00	100.00	2.00	160.00	3.20
5,500	106	1.91	220	4.00	1,237.50	1,031.25	22.50	18.75	120.00	2.18	191.25	3.48
6,000	130	2.16	260	4.33	1,350.00	1,125.00	22.60	18.75	140.00	2.33	222.50	3.71
6,500	155	2.38	330	5.08	1,462.50	1,218.75	22.60	18.75	171.50	2.64	253.75	3.90
7,000	180	2.67	400	5.71	1,575.00	1,312.50	22.50	18.75	203.00	2.90	285.00	4.07
7,500	205	2.73	470	6.27	1,687.50	1,408.25	22.50	18.75	234.50	3.13	316.25	4.21
8,000	235	2.98	545	6.81	2,100.00	1,800.00	26.25	22.50	266.00	3.33	347.50	4.34
8,500	265	3.12	620	7.29	2,231.25	1,912.50	26.25	22.50	297.50	3.50	385.00	4.58
9,000	295	3.28	695	7.72	2,362.50	2,025.00	26.25	22.50	329.00	3.66	422.50	4.69
9,500	325	3.42	770	8.11	2,493.75	2,137.50	26.25	22.50	360.50	3.79	460.00	4.84
10,000	355	3.55	845	8.45	2,625.00	2,250.00	26.25	22.50	392.00	3.92	497.50	4.96
12,500	530	4.24	1,320	10.56	3,750.00	3,281.25	30.00	26.25	639.50	5.12	691.25	5.53
15,000	730	4.87	1,795	11.97	4,812.50	4,812.50	32.08	32.08	887.00	5.91	910.00	6.07
1,180	1,180	5.90	2,895	14.48	6,812.50	6,812.50	34.06	34.06	1,382.00	6.91	1,997.50	6.99
26,000	1,730	7.12	4,245	18.98	8,937.50	8,937.50	35.75	35.75	2,042.00	8.17	1,960.00	7.84
30,000	2,380	7.93	5,595	18.65	11,187.50	11,187.50	37.29	37.29	2,702.00	9.01	2,522.50	8.41
35,000	2,980	8.51	7,195	20.56	13,562.50	13,562.50	38.75	38.75	3,472.00	9.92	3,147.50	8.99
40,000	3,580	8.95	8,795	21.99	15,937.50	15,937.50	39.84	39.84	4,242.00	10.60	3,772.50	9.43
45,000	4,380	9.73	10,645	23.66	18,437.50	18,437.50	40.97	40.97	5,012.00	11.14	4,397.50	9.77
50,000	5,180	10.36	12,495	24.99	20,937.50	20,937.50	41.88	41.88	5,782.00	11.56	5,022.50	10.05
55,000	5,980	10.57	14,695	26.72	23,562.50	23,562.50	42.84	42.84	6,627.00	12.41	5,647.50	10.27
60,000	6,780	11.30	16,895	28.16	26,187.50	26,187.50	43.66	43.66	7,572.00	13.12	6,272.50	10.45
70,000	8,880	12.69	21,895	31.26	31,437.50	31,437.50	44.91	44.91	9,962.00	14.23	7,772.50	10.75
80,000	10,980	13.72	27,295	34.13	36,687.50	36,687.50	45.86	45.86	12,327.00	15.41	8,772.50	10.96
100,000	16,180	16.18	39,095	39.10	47,187.50	47,187.50	47.19	47.19	17,607.00	17.61	11,272.50	11.27
150,000	31,680	21.12	70,095	46.73	73,437.50	73,437.50	48.96	48.96	34,262.00	22.55	17,522.50	11.65
200,000	49,130	24.59	101,095	50.55	99,687.50	99,687.50	49.84	49.84	50,967.00	25.48	23,772.50	11.89
300,000	92,680	30.89	165,095	55.03	152,187.50	152,187.50	50.73	50.73	96,857.00	32.28	36,272.50	12.09
500,000	192,680	38.54	297,095	59.42	257,187.50	257,187.50	51.44	51.44	196,407.00	39.08	61,272.50	12.26
1,000,000	475,180	47.52	647,095	64.71	519,687.50	519,687.50	51.97	51.97	499,157.00	49.92	123,772.50	12.28
5,000,000	3,140,180	62.80	3,527,095	70.54	2,619,687.50	2,619,687.50	52.39	52.39	3,415,157.00	68.30	623,772.50	12.48

NET INCOME DEFINED.

The bill (sec. 212) defines net income to mean the gross income as defined in section 213 less the deductions allowed by section 214. Gross income will include the same items of income as are included under the present law, with the following exceptions:

(1) The bill includes in gross income the interest from obligations of States, Territories, political subdivisions thereof, or the District of Columbia, issued after the passage of this act, unless authorized by law prior to the passage of this act or unless issued for the purpose of funding or refunding interest-bearing indebtedness outstanding at the time of the passage of this act or for the performance of a contract entered into prior to the passage of the act. The committee was of the opinion that, although there is doubt as to the constitutionality of including the interest on these obligations, justice requires that at least in time of war the holders of these securities should share the burdens equally with the holders of Liberty bonds. The bill places these bonds and Liberty bonds upon the same basis, exempting the holder of not more than \$5,000 of them from all income, war profits, and excess profits taxes, and exempting him from normal income tax on the interest received from the total amount held by him, and subjecting him to surtax and war profits or excess profits tax on the interest received from such bonds the aggregate principal of which exceeds \$5,000.

(2) The compensation of the President of the United States and of the judges of the Supreme and inferior courts of the United States and all other officers and employees of any State, Territory, or political subdivision thereof or the District of Columbia, is made subject to income tax. The compensation of these officials under existing law is not subject to income tax. Your committee realizes that there is a great difference of opinion among the best legal talent with reference to the constitutionality of this provision, but feels that in all equity and justice such officials should be subject to income taxes and that, if necessary, this matter should be definitely decided by the courts.

(3) The bill also excludes from gross income amounts not in excess of \$3,500 received by persons in the military or naval forces of the United States as salary or compensation in any form from the United States for services abroad or at sea in such forces.

(4) The present law excludes from gross income the proceeds of life insurance policies paid upon the death of the insured to individual beneficiaries. The proposed bill also excludes the proceeds of such policies paid to the estate of the insured.

(5) Under the present law it is not necessary to include in gross income the income of foreign governments received from investments in the United States in stocks, bonds, or other domestic securities owned by such foreign governments, or from interest on deposits in banks of the United States of moneys belonging to such foreign governments. The proposed bill, in addition to providing that the aforementioned income shall not be included in gross income, provides that income of foreign governments from any other source within the United States shall not be so included.

(6) Under the present law it is doubtful whether amounts received through accident or health insurance, or under workmen's compen-

sation acts, as compensation for personal injury or sickness, and damages received on account of such injuries or sickness, are required to be included in gross income. The proposed bill provides that such amounts shall not be included in gross income.

DEDUCTIONS.

Sec. 214 of the bill allows the same deductions from gross income as under existing law, with the following exceptions:

(1) The present law allows the deduction of interest paid, except on indebtedness incurred for the purchase of tax-free obligations or securities. This is difficult of administration, for in many cases it is impossible to tell for what purpose indebtedness is incurred. A man, for example, may have a mortgage on his house and have \$1,000 in bank. He borrows \$1,000 and buys a Liberty bond and makes a payment on his mortgage. For what purpose was the \$1,000 borrowed? The proposed bill allows the deduction of all interest paid in excess of the amount of interest received free from income tax. This is easy of administration and carries out the general purpose of the existing law.

(2) The present law allows as a deduction the whole amount of taxes paid to a foreign government. The proposed bill, since it allows (sec. 222) the amount of income and excess profits taxes paid to foreign countries upon income received from sources therein as a credit against the income tax payable to the United States, does not allow the same amount over again as a deduction in computing net income.

(3) Under existing law, in transactions entered into for profit but not connected with the taxpayer's business or trade, only the losses actually sustained therein during the year to an amount not exceeding the profits arising therefrom can be deducted. The proposed bill changes the provision of existing law to allow the entire loss in such transaction to be deducted.

(4) Due to the necessity for erecting buildings and building machinery for war purposes many buildings and much machinery have been erected that will be of little value after the war. Under existing law it is impossible for the Treasury Department to allow deductions other than for the ordinary exhaustion, wear and tear, and depletion of such property. A provision is incorporated in this bill to allow the Treasury Department in such cases to allow special amounts for amortization, according to the peculiar condition in each case, but such amounts can not exceed in any year 25 per cent of the net income. At any time within three years the allowance may be reexamined, and if found incorrect the taxes will be readjusted, and any overpayment refunded or any underpayment collected from the taxpayer.

(5) The depletion provision of existing law does not grant an allowance for cost of development. In the case of mines, oil and gas wells such an allowance seems only equitable and fair and the bill provides that a reasonable allowance in such cases be allowed for depreciation of improvements. The bill also corrects an inequality of the present law by providing for an equitable apportionment of the depletion allowance between lessor and lessee.

PARTNERS.

Under the proposed bill the partners will be liable to income tax the same as under existing law. The partnership as such is not liable to income tax, but each partner will pay his income tax upon his share of the partnership profits whether the same are distributed or not.

CREDIT FOR FOREIGN TAXES.

Under existing law a citizen of the United States can only deduct income war or excess profits taxes paid to a foreign country from gross income in computing net income. With the corresponding high rates imposed by certain foreign countries the taxes levied in such countries in addition to the taxes levied in the United States upon citizens of the United States place a very severe burden upon such citizens. The bill provides that a credit against the income tax imposed in the United States be allowed a citizen of the United States subject to income and war or excess profits taxes in a foreign country of an amount equal to the tax paid in such country upon income that is received from sources within such country. The bill further provides that, in the case of an alien resident of the United States who is a citizen or subject of a country which imposes income, war profits, or excess profits taxes, a like credit shall be allowed if such country allows a similar credit to citizens of the United States resident in such country.

INDIVIDUAL INCOME-TAX RETURNS.

Under existing law only persons of lawful age have to make returns. A minor's income is either included in the income-tax return of the parent or a return is made for the minor by his guardian. Single persons of lawful age and having a net income of \$1,000 or over and married persons having incomes of \$2,000 or over are required to make returns under existing law. The proposed bill requires every person, whether of lawful age or not, having a net income for the taxable year of \$1,000 or over, if single, or if married and not living with husband or wife, to make a return, and requires all married persons living with husband or wife having a net income of \$2,000 or over to make returns. It is deemed advisable to allow persons under 21 years of age to make their own return and pay their own tax separate from their parents if they are making their own living or are emancipated. It is believed that there are a considerable number of young men and women under the age of 21 now earning more than \$1,000 per year.

INDIVIDUAL INCOME TAX ESTIMATES.

The income-tax estimates are based upon the returns for the calendar year 1917, as near as the Treasury Department can determine the details of such returns at this time.

These figures show that there were about 615,000 individuals with an income of over \$4,000 per annum, and 2,440,000 with taxable incomes of \$4,000 or less.

The total taxable income is given as \$7,400,000,000 and of income subject to normal tax \$4,700,000,000, the difference being due to the

fact that in computing the normal tax a credit is given for the personal exemption and for dividends received from corporations.

It is assumed, in these estimates, that the grouping of incomes of taxpayers for 1918 will correspond to the grouping in 1916. That is, that the incomes in any one bracket in 1918 will bear the same proportion to the total income that the incomes in the like bracket in 1916 bore to the total income for 1916. It was necessary to use the 1916 groupings of income for the basis of the estimates because the 1917 compilation of returns is not yet complete in this respect.

It is estimated that the individual normal income tax will yield \$414,000,000 and the surtaxes \$1,068,186,000, making the total individual income tax for the current taxable year, \$1,482,186,000.

Part III. CORPORATIONS.

Under the revenue act of 1916 a corporation tax of 2 per cent is levied upon the net income of all corporations and under that act dividends received by one corporation from another are not allowed to be deducted in arriving at net income. The revenue act of 1917 levies an additional corporation income tax of 4 per cent upon the net income of all corporations but for the purpose of such additional tax allows a corporation to deduct dividends received by it from other corporations in arriving at its net income. The proposed bill allows a deduction of all dividends received by one corporation from another in computing net income and levies (sec. 230) a corporation tax of 18 per cent upon the amount of the net income in excess of the credits allowed in section 236, but provides that the rate shall be 12 per centum upon so much of this amount as does not exceed the sum of (1) the dividends paid during the taxable year, plus (2) the amount paid during the taxable year out of earnings or profits in discharge of bonds and other interest-bearing obligations outstanding prior to the beginning of such year.

An example will make clear the effect of this tax. Suppose the amount of the net income of a corporation in excess of its credits is \$100,000. Suppose it has paid out during the year \$50,000 in dividends, and discharged \$10,000 worth of bonds. Its tax would then be 12 per cent of \$60,000, and 18 per cent of \$40,000.

The committee believes that the reduction of the rate to 12 per cent on an amount equal to the amount of dividends paid will have a wholesome effect in many cases in stimulating the payment of dividends, which will be subject to surtax in the hands of the stockholders.

The bill makes no change in the corporations exempt from income tax.

DEDUCTIONS.

Section 234 of the bill allows corporations the same deductions from gross income as under existing law, with the following exceptions:

(1) Under existing law the interest deduction is limited to interest on an amount of indebtedness not in excess of the sum of the paid-in capital stock plus one-half of the interest-bearing indebtedness. Since borrowed money is not allowed to be included in computing invested capital for the purpose of the war profits and excess profits tax, it seems only fair to allow as a deduction in computing net

income the whole amount of the interest paid during the year. This is done in the bill, which, however, contains the same limitation in respect to the tax-free interest received by the corporation which is applied in the case of an individual. This matter is discussed under the heading "Deductions," under the portion of this report relating to the individual income tax.

(2) Existing law allows as a deduction the whole amount of taxes paid to a foreign Government. The proposed bill, since it allows (sec. 238) the amount of income and excess-profits taxes paid to foreign countries upon income received from sources therein as a credit against the income tax payable to the United States, does not allow the same amount over again as a deduction in computing net income.

(3) A new amortization provision applicable to corporations has been added to the deduction provisions. This amortization provision as applied to corporations is exactly the same as the amortization provision applicable to individuals, which is explained at an earlier page of this report.

(4) The depletion provision of existing law has been changed in the same manner as in the case of an individual. For a statement in regard thereto, see paragraph (5) on an earlier page of this report.

CREDITS ALLOWED.

In computing net income for the corporation tax the following credits are allowed:

(1) The amount received as interest upon obligations of the United States, any State, Territory, or political subdivision thereof, or the District of Columbia, which is included in gross income.

(2) The amount of any war or excess profits taxes imposed by act of Congress for the same taxable year.

(3) In the case of a domestic corporation, \$2,000.

CORPORATION RETURNS.

Like existing law, the proposed bill provides that every corporation not specially exempt shall make a return. The exempt corporations are specified in section 231. The return will be required to show the items of gross income and the deductions and credits allowed, in a manner similar to that now required under existing law. The returns will be required to be filed with the collector of the district in which is located the principal place of business or principal office or agency of the corporation, the same as under existing law.

CORPORATE NET INCOME.

The following table shows the corporate net income from 1909 to date:

Corporate net income, 1909 to 1918.

Year.	Net income.	Year.	Net income.
1909.....	\$3,500,000,000	1914.....	\$3,940,000,000
1910.....	3,761,000,000	1915.....	5,310,000,000
1911.....	3,503,000,000	1916.....	8,765,900,000
1912.....	4,151,000,000	1917 (estimated).....	10,500,000,000
1913.....	4,714,000,000	1918 (estimated).....	10,000,000,000

CORPORATION INCOME TAX.

The net income of corporations for the current taxable year has been estimated by the Treasury Department at \$10,000,000,000.

After deducting from this amount the credits allowed (1) \$2,000 exemption allowed each corporation, estimated to amount to \$500,000,000, and (2) the estimated excess and war profits taxes amounting to \$3,200,000,000, the income subject to the corporation taxes will be \$6,300,000,000. It is estimated that of this amount \$4,000,000,000 will represent amounts distributed in dividends and indebtedness paid off during the taxable year and at the 12 per cent rate will yield \$480,000,000. The remaining \$2,300,000,000 will be subject to the 18 per cent rate and will yield \$414,000,000 revenue, thus making a total revenue of \$894,000,000 from the corporation income taxes.

Part IV. ADMINISTRATIVE PROVISIONS.

PAYMENT OF TAXES.

Under existing law all corporations having an accounting period ending with the close of the calendar year and all individuals are required to make their return on the following March 1 and to pay their tax on or before June 15. Under the present law corporations having a fiscal year other than the calendar year are required to make return on the 1st day of the third month following the close of the fiscal year. In order to harmonize the payment dates of business concerns and Government transactions, with a view to distributing the burden upon the banks to the best advantage, it is deemed preferable to change the time for filing the return of such corporations to the 15th day of the third month after the close of the calendar or fiscal year. A like period is also provided for individuals having accounting periods for a fiscal year other than the calendar year and also for those having an accounting period closing at the end of the calendar year. In order not to have the large payment of income and excess profits taxes come upon one date, the bill provides that these taxes be paid in three installments, one-third to be paid at the time of the filing of the return, one-third on the 15th day of the second month thereafter, and the remaining one-third on the 15th day of the fourth month after the time fixed by law for filing the return. In other words, the tax payment dates of individuals and corporations whose accounting period is on the basis of the calendar year will be March 15, May 15, and July 15. The commissioner is authorized to extend the time for making the return, whenever in his judgment good cause exists, for a period not to exceed two months, except in the case of taxpayers who are abroad. In the case of taxpayers who are abroad the commissioner has discretionary authority to extend the time for such period as he deems necessary. Except in the case of a taxpayer who is abroad, taxpayers securing such extension of time must pay the first installment of taxes upon the expiration of the period of extension, and the second and third installments will become due as in the case of all other taxpayers and as above stated. In the case of any taxpayer who is abroad the commissioner may extend the time for pay-

ment of the second and third installments by not more than four months after the expiration of the period of any extension of time for filing his return.

REFUNDS.

A new provision is incorporated in the bill providing that if upon examination of any return of income made pursuant to the income-tax provisions of the revenue act of August 5, 1909, or October 3, 1913, or the revenue acts of 1916 and 1917 or this act it appears that an amount of income, war profits, or excess-profits tax has been paid in excess of that properly due the amount of the excess so paid shall be credited against any income, war profits, or excess-profits taxes or installments thereof then due from the taxpayer under any other return and that any balance of such excess shall be immediately refunded to the taxpayer. It is believed that this provision will materially assist in the settlement of transactions between the taxpayer and the Government.

INFORMATION AT THE SOURCE.

The revenue act of 1917 abolished collection at the source and substituted information at the source in lieu thereof, and provided that all individuals, corporations, and partnerships, including lessees or mortgagors of real or personal property, fiduciaries, and employers making payment to another individual, corporation, or partnership of any fixed or determinable annual or periodical sum in excess of \$800 should report this information to the commissioner in order that he might use the same as a check upon the returns of the respective taxpayers. The proposed bill retains the system of information at the source, but only requires information of income payments made in excess of \$1,000 or more in any taxable year.

COLLECTION AT THE SOURCE.

The proposed bill, as under existing law, only requires the withholding of income in the case of payments by individuals, corporations, and partnerships of fixed and determinable annual or periodical gains, profits, and income to nonresident alien individuals or nonresident corporations. In the case of nonresident aliens the normal tax will be withheld at the rate of 12 per cent.

In the case of tax-free covenant bonds the obligor will be required to deduct and withhold a tax equal to 2 per cent of the interest upon such bonds and similar obligations the same as under existing law.

TITLE III. WAR PROFITS AND EXCESS PROFITS TAX.

In the interest of clearness this title has been divided into eight parts, as follows:

- Part I. General Definitions.
- Part II. Imposition of Tax.
- Part III. War Profits Method.
- Part IV. Excess Profits Method.
- Part V. Net Income.
- Part VI. Invested Capital.
- Part VII. Reorganizations.
- Part VIII. Miscellaneous.

Part I. GENERAL DEFINITIONS.

In this part it is provided that the terms "taxable year," "fiscal year," and "dividends" shall have the same meaning for the purpose of the excess profits tax and war profits tax title as is provided for the purpose of the income tax in section 200, and that the "first taxable year" for the purpose of this title shall be the same as the "first taxable year" for the purpose of the income tax.

Part II. IMPOSITION OF TAX.

In lieu of the excess profits tax imposed by Title II of the revenue act of 1917 and in addition to the other taxes imposed by this act, a tax is levied for each taxable year upon the net income of every corporation, computed according to which ever of the two following methods will yield the higher amount of taxes: (1) The war profits method or (2) the excess profits method.

In view of the increased individual normal and surtax rates upon the income of individuals and partnerships which in most cases will make the taxes paid by such individuals as high as the income and excess or war profits taxes paid by corporations engaged in similar business and in view of the difficulty in administering an excess profits tax applicable to individuals, the bill provides that the war and excess profits taxes shall apply to corporations only.

CORPORATIONS WHOSE INVESTED CAPITAL IS LESS THAN \$50,000.

In view of the fact that in many cases it has been the experience under the present excess profits tax law that the excess profits tax has borne more heavily upon many small corporations with capital of less than \$50,000 than upon the larger corporations, because of the fact that the smaller corporations are in most instances capitalized on a different basis, and the income of such smaller corporations is in most cases largely attributable to the personal activities of the stockholders rather than to the capital invested, in order to more equally distribute the tax burden the bill provides that in the case of a corporation having an invested capital of not more than \$25,000 the excess or war profits tax levy shall in no case exceed 35 per cent of the amount of its net income for the taxable year in excess of \$3,000, and that in the case of corporations having more than \$25,000 but not more than \$50,000 invested capital, the excess or war profits tax levy shall in no case be more than 40 per cent of the amount of its net income for the taxable year in excess of \$3,000. This provision, however, will not apply to corporations whose net income exceeds \$50,000.

CORPORATIONS IN WHICH INVESTED CAPITAL IS NOT A MATERIAL INCOME-PRODUCING FACTOR.

In certain instances the experience under the existing excess-profits tax law has been that there are certain classes of corporations the earnings of which are to be ascribed primarily to the activities of the principal owners or stockholders and in which capital is not directly or indirectly a material income-producing factor. In such cases the excess-profits tax would bear too heavily upon such corporation, as practically all or by far the greater portion of the income

would be subject to the rate provided in the highest excess-profits bracket. In order to equalize this situation the bill provides in section 303 that in the case of such a corporation, in lieu of the tax imposed by the excess-profits tax provision of the Revenue Act of 1917 and in lieu of the tax imposed by section 301 of the proposed bill, and in addition to all other taxes imposed by such bill, a tax of 20 per cent upon the amount of the net income of such corporation for the taxable year in excess of \$3,000. It is provided, however, that no corporation shall be taxable under this provision if 50 per cent or more of its gross income consists of gains or profits derived from purchase or sale, or of gains, profits, or commissions derived from Government contracts, or if the invested capital of such corporation is more than \$100,000. Such corporations will be taxable under section 301 under the excess-profits method or the war-profits method, whichever will yield the higher tax.

EXEMPT CORPORATIONS.

All corporations exempt under the income-tax title will be exempt from the excess-profits or war-profits tax. A list of these corporations will be found in section 231.

Part III. WAR-PROFITS METHOD.

This part fixes the prewar period as the calendar years 1911, 1912, and 1913, or, if a corporation was not in existence during the whole of such period, then as many of such years during the whole of which the corporation was in existence. The bill provides a tax of 80 per cent upon the amount of the net income in excess of the war-profits credit. The war-profits credit will be determined in the following way: Every corporation will be allowed a specific exemption of \$3,000 and in addition its average prewar earnings for the prewar period 1911, 1912, and 1913. In the case of corporations who have increased their capital since the prewar period, the bill provides that an additional amount be allowed equal to 10 per cent of the additional invested capital employed during the taxable year. If the corporation has reduced its capital since the prewar period, the allowance must be decreased by an amount equal to 10 per cent of the invested capital withdrawn. If a corporation was not in existence during the whole of any one calendar year during the prewar period, or if it had no net income for the prewar period, or if its prewar earnings were less than 10 per cent of its invested capital for the taxable year, it will be entitled to a specific exemption of \$3,000 and an additional amount equal to 10 per cent of the invested capital for the taxable year. The proposed bill, like the present excess-profits tax law, specifically provides that a foreign corporation shall in no case be entitled to the specific exemption of \$3,000.

The war profits tax is not distinctly a war profits tax, since a minimum exemption of 10 per cent is allowed in all cases. In view of the high rate of tax imposed by this method and in view of the fact that owing to a serious depression in many industries, many corporations were making very small profits during the prewar period, your committee believes that it is only equitable and fair to allow such corporations a minimum exemption of 10 per cent and that such an

exemption is necessary to allow such corporations a sufficient return upon their investment in order to assure them a reasonable profit and at the same time to enable them to maintain their plants as going concerns.

Part IV. EXCESS PROFITS METHOD.

The bill provides that for the purpose of determining the excess profits tax the credit shall consist of a specific exemption of \$3,000 plus an amount equal to 8 per cent of the invested capital of the corporation for the taxable year. The tax under the excess profits tax method will be computed upon the following basis: Thirty-five per cent of the amount of the net income in excess of the excess profits credit (of 8 per cent of the invested capital plus \$3,000) and not in excess of 15 per cent of the invested capital for the taxable year; 50 per cent of the amount of the net income in excess of 15 per cent of the invested capital and not in excess of 20 per cent of such capital; and 70 per cent of the amount of the net income in excess of 20 per cent of such capital. Even with the increased excess profits tax rates, it is probable that many corporations whose tax will be computed under this method will not have their taxes increased to so great an extent over their excess profits taxes of last year as many corporations whose taxes will be computed under the war profits tax method.

Under existing law it is found that some corporations of small capital would not be able to take their entire credit out under the first bracket. The bill provides that in such cases where the full amount of the credit can not be allowed in the first bracket by reason of the fact that such credit is in excess of 15 per cent of the invested capital the part not so allowed shall be deducted from the amount in the next succeeding bracket, and if not then fully allowed the remaining part shall be deducted in the last bracket. As under existing law, in computing the excess-profits tax a foreign corporation will not be entitled to a specific exemption of \$3,000 in computing the excess-profits tax under the proposed bill.

Part V. NET INCOME.

The net income of corporations for the prewar period 1911, 1912, and 1913 will be computed exactly as under the existing excess-profits tax law and will be comparatively easy to ascertain, since the returns are already on file in the Treasury Department. The net income for the taxable year will be computed upon the same basis and in the same manner as is provided for computing the corporate income under Title II of the proposed bill.

The average net income for the prewar period will be determined by dividing the number of years within that period during the whole of which the corporation was in existence into the sum of the net income for such years, even though there may have been no net income for one or more of such years.

Part VI. INVESTED CAPITAL.

The definition of invested capital in the existing law, while rewritten in the proposed bill in the interest of clearness and while changed slightly in order to apply a more liberal rule in a few cases

where the existing law has in operation been found to produce certain inequalities, has not been changed in any important particular.

In order to simplify the definition of invested capital it has been deemed advisable to define certain terms, such as "intangible property," "tangible property," "borrowed capital," and "inadmissible assets." These definitions will be found in section 325 of the bill.

In the case of certain investment banking houses whose business is almost entirely confined to tax-exempt securities, such as municipal and State bonds, a very difficult question arises as to what should be the invested capital of such corporation. Although the definition of invested capital in existing law specifically states that the amount invested in such securities shall not be included in invested capital if the interest income from the same is not subject to income, excess and war profits taxes, the income from the gain upon the sale of these bonds, however, is subject to all the aforementioned taxes. The bill therefore allows such a corporation to add to its invested capital an amount equal to the same proportion of the amount invested in such tax-free securities as the profit from the sale of such securities bears to the total net income derived from the sale thereof and the interest thereon.

It also has been the experience of the Treasury Department that the excess profits tax places a very heavy burden upon investment houses and similar corporations whose business is largely confined to dealing in tax-free securities, because such corporations cannot include in invested capital either such securities or borrowed money. In order more nearly to equalize this burden, the bill provides that in such cases a corporation shall be entitled to include in invested capital an amount invested in such tax-free securities not in excess of the borrowed capital of such corporation (other than indebtedness maturing within one year of its creation, all accounts payable and current liabilities) for such year, if it includes in its net income for excess profits tax purpose the interest and dividends from the bonds and stocks included in computing invested capital.

CONSTRUCTIVE CAPITAL.

The existing excess profits act provides that in cases where the Secretary of the Treasury is unable to determine satisfactorily the invested capital of a corporation he may construct the same upon the basis of representative concerns. The bill provides that the Commissioner of Internal Revenue be given this same discretion under the proposed excess profits tax method and adds a provision in section 327 for the construction of capital in two additional specified cases: (1) Where the mixed aggregate of tangible property and intangible property has been paid in for stock or for stock and bonds and the commissioner is unable satisfactorily to determine the representative values of the several classes of property at the time of payment or to distinguish the classes of property paid in for stock and for bonds, respectively, or (2) where capital is a material income producing factor but where, because of the fact that the capital employed is in large part borrowed, there is no invested capital, or the invested capital is materially disproportionate to the net income as compared with representative concerns engaged in a like or similar trade or business. This section is not, however, to

apply to any corporation 50 per cent or more of whose gross income is derived from Government contracts.

The bill provides in section 328 that in determining invested capital in the above cases the commissioner shall compare the taxpayer only with representative corporations whose invested capital can be satisfactorily determined and which are as nearly as may be similarly circumstanced with respect to gross income, net income, profits per unit of business transacted and capital employed, the amount and rate of war or excess profits, and all other relevant facts and circumstances.

Section 328 also provides that the commissioner shall keep a record of all cases in which invested capital is constructed under section 327 and that the Senate or House of Representatives may call for a copy of such record or information regarding any such cases without regard to the restrictions contained in section 257 with reference to publicity of income tax returns.

Part VII. REORGANIZATIONS.

In the case of the reorganization, consolidation, or change of ownership after January 1, 1911, of a trade or business now carried on by a corporation, for the purpose of determining the net income and invested capital for the prewar period, the corporation shall be deemed to have been in existence prior to that date, and the net income and invested capital of the predecessor trade or business for all or any part of the prewar period prior to the organization of the corporation shall be deemed to have been the net income and invested capital of the corporation.

In the case of the reorganization, consolidation, or change of ownership of a trade or business after March 3, 1917, if an interest or control in such trade or business of 50 per cent or more remains in the same persons or any of them, in such case no asset transferred or received from the predecessor trade or business shall, in computing invested capital, be allowed a greater value than would have been allowed in computing the invested capital of the prior trade or business if such asset had not been so transferred or received.

Part VIII. MISCELLANEOUS.

In the case of corporations having a fiscal year ending during 1918 the income will be divided into two parts: The income falling in the year 1917 will be subject to the excess-profits tax rates provided under existing law in the revenue act of 1917, and the income falling in the period from January 1, 1918, to the close of the fiscal year will be taxable at the war-profits rate or excess-profits rate, whichever is higher, provided in this bill.

CORPORATION RETURNS FOR EXCESS OR WAR PROFITS TAXES.

No returns for excess or war profits tax purposes will be required of any corporation not having a net income of \$3,000 or over for the taxable year. Corporations subject to tax under this title will make return and pay their taxes at the same times and places and in the same manner and subject to the same conditions as is required of corporations in making their return for income-tax purposes.

EXCESS PROFITS AND WAR PROFITS ESTIMATE.

The basis of the estimate for the excess profits taxes is as follows:

It is assumed that the net income of corporations for the current taxable year will be \$10,000,000,000. This is less than the net income for the last taxable year, which is estimated by the Treasury Department at \$10,500,000,000, and it is estimated that these earnings will be reduced to the above figure for 1918.

As a basis for applying the rates provided in this bill the returns of about 11,500 corporations for 1917, selected at random, were tabulated. It is assumed that the returns for the current year will be similar to these known corporations reporting for last year, the total net income, of course, being estimated at \$10,000,000,000. It is estimated that the revenue from these taxes will be about \$3,200,000,000.

TITLE IV. ESTATE TAX.

Congress for the first time, by the revenue act of September 8, 1916, levied a tax (a graduated tax) upon the transfer of the net estate of a decedent. In determining the net estate an exemption of \$50,000 is allowed.

This form of taxation has now been in operation for about two years and sufficient opportunity has been afforded those engaged in administering the law to observe and report to Congress the effect of the existing law and suggestions for amendments which will bring out more clearly the intention which Congress desired to prevail at the time of the original imposition of an estate tax.

The present bill provides for the imposition of a tax which will take the place of that imposed by Title II of the revenue act of 1916 as amended March 3, 1917, and the tax imposed by Title IX of the revenue act of 1917.

Section 402 of this bill, which takes the place of section 202 of the original act, has been revised so as to contain a provision specifically including in the gross estate dower, curtesy, or any estate created in lieu of dower or curtesy. The distinction between dower and curtesy interest and property passing to wife or husband by will or intestate succession is technical rather than real, at least in the consideration of the question as to whether they should be subject to estate tax. The proposed amendment is for the purpose of making it clear that such interests are to be included.

It was the intention of the framers of the original act that dower, curtesy, and estates created in lieu of dower or curtesy should be included in the gross estate, and your committee believes that the Treasury Department has correctly ruled in requiring them to be so included. Since a dispute has arisen with reference to this question, your committee deems it advisable to provide specifically that these estates shall be included in the gross estate.

There has also been included in the gross estate the value of property passing under a general power of appointment. This amendment as well as that preceding is for the purpose of clarifying rather than extending the existing statute. A person having a general power of appointment is, with respect to disposition of the property at his death, in a position not unlike that of its owner. The possessor of the power has full authority to dispose of the property at

his death, and there seems to be no reason why the privilege which he exercises should not be taxed in the same degree as other property over which he exercises the same authority. The absence of a provision including property transferred by power of appointment makes it possible, by resorting to the creation of such a power, to effect two transfers of an estate with the payment of only one tax.

The gross estate section has been amended to specifically include (1) insurance receivable by the executor under policies taken out by the decedent upon his own life and (2) insurance in excess of \$40,000 receivable by all specific beneficiaries under policies taken out by the decedent upon his own life. (1) Insurance payable to the executor or to the estate is now regarded as falling within section 202 (a) of the existing statute and this construction of the existing statute is now written into the new bill for the sake of clearness. The amendment will serve the further purpose of putting on notice those who acquaint themselves with the statute for the purpose of making more definite plans for the disposition of their property. (2) The provision with respect to specific beneficiaries has been included for the reason that insurance payable to such beneficiaries usually passes under a contract to which the insurance company and the individual beneficiary are the parties in interest and over which the executor exercises no control. Amounts passing in this way are not liable for expenses of administration or debts of the decedent and therefore do not fall within the existing provisions defining the gross estate. It has been brought to the attention of the Committee that wealthy persons have and now anticipate resorting to this method of defeating the estate tax. Agents of insurance companies have openly urged persons of wealth to take out additional insurance payable to specific beneficiaries for the reason that such insurance would not be included in the gross estate. A liberal exemption of \$40,000 has been included and it seems not unreasonable to require the inclusion of amounts in excess of this sum.

Section 403, which takes the place of section 203 of the original act defining the deductions for the purpose of arriving at the net estate, inserts a provision that income taxes upon income received after the death of the decedent, and estate, succession, legacy, or inheritance taxes, are not to be deducted. Obviously, income taxes should not be deducted, for the reason that they are payable from and on account of income which is not included in the gross estate. Inheritance taxes payable to States are payable in respect to the benefits derived by individual legatees and beneficiaries. They are computed upon the basis of the amount which passes to such beneficiaries and are not known until estate taxes have been ascertained. These provisions are in conformity with existing rulings in the administration of the law, which rulings the committee thinks are in accordance with the statute, and are now included for the sake of clarification, as in the case of additions made to section 402 mentioned above.

An additional subdivision has been added to section 403 which will grant a deduction of amounts which have been received by the decedent as a share in the estate of any person who died within five years prior to the death of the decedent. It has come to the attention of the committee that persons closely related have died within such a short space of time that the same estate passing within a short period

of time has been subjected to the estate tax and thereby diminished unreasonably because of the short period within which the two levies have been made. For example, a husband dies leaving a large amount of property to his wife, an elderly woman, who dies within a few weeks after her husband's death. Under existing law the entire estate is taxed on the transfer from husband to wife and on the transfer from wife to other beneficiaries. The proposed amendment grants an interval of five years within which the deduction may be taken.

Section 404 includes a provision that returns shall be made in all cases where the gross estate exceeds \$50,000 instead of \$60,000, as provided under existing law. In the administration of the present law it has been found that representatives of the estates almost uniformly report local tax assessments as the value of property for measuring estate tax. The act levies this tax on the actual value of property at the time of the decedent's death. It was therefore necessary to require a return on estates of \$50,000 or more even though there is a specific exemption of \$50,000, in order that the department may have the opportunity of verifying the true value of the property included in estates which are near the line of exemption.

A provision has been included in section 406 which will enable the commissioner to grant relief in the form of an extension of time for the payment of the tax not to exceed two years from the due date, where the requirement for immediate payment of the tax will impose undue hardship upon the estate. In the case of those estates where the holdings of the decedent are largely in lands and other property for which there is no ready market, it has been found in practice that a forced collection of the tax results in enormous sacrifice to the beneficiaries. This is due not so much to the amount of the tax as to the lack of a market for certain kinds of property. It is believed that in levying taxes of this character the estate should be given every opportunity, consistent with safe and proper enforcement of the law, to raise the money with which to pay the taxes without sacrificing the true value of the property of the decedent.

The rate of interest chargeable on taxes not paid within a year and a half after the decedent's death has been changed from 10 per cent to 6 per cent per annum in the belief that this rate is a fair rate as interest and that penalties should preferably be imposed as penalties and not in the form of penal rates of interest.

Minor changes in verbiage and slight modifications in procedure have been made for the sake of insuring more equitable, uniform, and efficient administration of the law. Instances of these are the extension of time for filing notice, the extension of the due date, the change in the rate of interest on account of delayed payment, authorization to release the lien on specific property when the tax has been paid, the limitation of deductions in the case of non residents to 10 per cent of the value of the gross estate situated in the United States for administering the estate, and the giving to the executor a right of contribution from the specific beneficiary under policies of insurance.

The following table compares the estate-tax rates imposed by existing law and the proposed bill:

Amount of net estate (an exemption of \$50,000 is allowed estates of residents of the United States, in computing the value of net estate).	Rates on net estates under—	
	Existing law.	Proposed bill.
	<i>Per cent.</i>	<i>Per cent.</i>
Not exceeding \$50,000.....	2	3
Exceeding \$50,000 and not exceeding \$150,000.....	4	6
Exceeding \$150,000 and not exceeding \$250,000.....	6	9
Exceeding \$250,000 and not exceeding \$450,000.....	8	12
Exceeding \$450,000 and not exceeding \$1,000,000.....	10	15
Exceeding \$1,000,000 and not exceeding \$2,000,000.....	12	18
Exceeding \$2,000,000 and not exceeding \$3,000,000.....	14	21
Exceeding \$3,000,000 and not exceeding \$4,000,000.....	16	24
Exceeding \$4,000,000 and not exceeding \$5,000,000.....	18	27
Exceeding \$5,000,000 and not exceeding \$8,000,000.....	20	30
Exceeding \$8,000,000 and not exceeding \$10,000,000.....	22	35
Exceeding \$10,000,000.....	25	40

ESTATE TAX ESTIMATE.

It is estimated that the estate tax will yield during the fiscal year 1920 \$110,000,000, and that when the bill is in full operation the annual yield will be \$140,000,000. For the fiscal year 1919 it is estimated that the estate tax yield will be about \$80,000,000.

TITLE V. TAX ON TRANSPORTATION AND OTHER FACILITIES AND ON INSURANCE.

FREIGHT.

The proposed bill does not increase the present rate of 3 per cent upon the amount paid for transportation of freight. It does provide, however, that in the case of freight transported from a point without the United States to a point within the United States, a tax of 3 per cent shall be paid upon the amount paid for transportation of such freight within the United States.

The receipts from the freight tax during the period it was in operation during the fiscal year ended June 30, 1918, amounted to \$30,000,000. It is estimated that this tax will yield \$75,000,000 during the first 12 months' period the bill is in operation.

EXPRESS.

The proposed bill does not increase the rate of 1 cent for each 20 cents or fraction thereof of the amount paid for transportation by express. It does, however, as in the case of the freight provision, provide that a tax shall be paid upon express transported from a point without the United States to a point within the United States, and levies a tax of 1 cent for each 20 cents or fraction thereof upon the amount paid for such transportation within the United States.

During the period that the express tax provision was in operation during the fiscal year ending June 30, 1918, the express tax receipts amounted to \$6,459,000. It is estimated that this tax will yield \$20,000,000 during the first 12 months' period the bill is in operation.

TRANSPORTATION OF PERSONS.

The proposed bill levies a tax of 8 per cent upon the amount paid for transportation of persons, the same as under existing law.

During the period that this tax was in operation during the fiscal year ended June 30, 1918, the tax yielded \$24,306,000. It is estimated that during the first 12-month period this bill is in operation the receipts from this tax will amount to \$60,000,000.

PULLMAN ACCOMMODATIONS.

Under existing law the tax upon Pullman accommodations is an amount equivalent to 10 per cent of the amount paid for seats, berths, and staterooms in parlor cars, sleeping cars, or on vessels. The proposed bill reduces this rate to 8 per cent. This reduction is recommended because the Director General of Railroads contemplates issuing in the very near future a ticket combining the regular fare and Pullman accommodation charge, and therefore in order to most expeditiously conduct the sale of such tickets and to avoid making a separate computation of tax for each railway and Pullman transportation charge, it is deemed advisable that the rate for both such charges be the same.

The receipts from seats and berths during the period that the tax upon Pullman accommodations was in effect during the fiscal year ended June 30, 1918, amounted to \$2,237,000. It is estimated that this tax will yield, during the first 12-months period this bill is in operation \$5,000,000.

TRANSPORTATION OF OIL BY PIPE LINE.

In view of the fact that freight charges have been increased 25 per cent and that there has been no similar increase in the transportation charge on oil by pipe line, your committee deems it fair to make an increase in the tax on the amount paid for the transportation of oil by pipe line of approximately 25 per cent. The present rate is 5 per cent of the amount paid for such transportation and the bill provides that the rate be increased to 6½ per cent of the amount so paid.

During the period of the fiscal year 1918 that the oil tax provision was in operation the receipts from this source amounted to \$1,453,000. It is estimated that the receipts from the increased tax during the first 12 months this bill is in operation will amount to \$4,550,000.

TELEGRAPH AND TELEPHONE MESSAGES, ETC.

Under existing law a tax of 5 cents is levied upon each telegraph, telephone, or radio dispatch, message, or conversation in which the charge for the transmission is 15 cents or more. The bill provides the following taxes upon the transmission of such messages: A tax of 5 cents for each message on which the charge is more than 14 cents and not more than 50 cents, and a tax of 10 cents upon all such messages when the charge is more than 50 cents.

The bill provides a new tax upon the amount paid to any telegraph or telephone company for any leased wire or talking circuit special service equivalent to 10 per cent of the amount so

paid. It is provided, however, that this tax shall not apply to the amount paid for so much of such service as is utilized (1) in the collection and dissemination of news through the public press or (2) in the conduct by a common carrier or telegraph or telephone company of its business as such.

The receipts for the period the tax upon telegraph and telephone and similar messages was in effect during the fiscal year 1918 amounted to \$6,299,000. It is estimated that at the increased rates, the tax, together with the tax upon talking circuit and leased wire charges, will amount to \$16,000,000 during the first 12 months this bill is in operation.

LIFE INSURANCE.

A tax equivalent to 8 cents, on each \$100 or fractional part thereof of the amount for which any life is insured, is levied under existing law, and this same tax is retained in the proposed bill. It is found that some industrial insurance is written on the monthly payment plan. A new provision is proposed in such cases to harmonize more nearly the tax upon such insurance with the tax upon industrial policies issued on the weekly payment plan providing that in the case of industrial insurance upon policies by which a life is insured not in excess of \$500 issued on the monthly payment plan, the tax shall be 20 per cent of the amount of the first monthly premium. This bill also provides that in the case of such policies issued on the weekly premium plan the tax shall be 40 per cent of the amount paid for the first weekly premium, the same as under existing law. The bill contains a new provision in the case of group life insurance covering groups of not less than 25 lives in the employ of the same person for the benefit of persons other than the employer, providing that the tax shall be equivalent to 4 cents on each \$100 of the aggregate amount for which the group policy is issued and of any net increase in the amount of insurance under such policies.

MARINE, INLAND, AND FIRE INSURANCE.

The bill re-enacts the tax of 1 cent on each dollar or fractional part thereof of the premium charged under each policy of such insurance without change.

CASUALTY INSURANCE.

Under existing law a tax is levied equivalent to 1 cent on each dollar or fractional part thereof of the premium charged under each casualty-insurance policy. No change is made in this provision except that in the case of industrial-insurance policies when issued on the monthly payment plan, a tax equivalent to 20 per cent of the amount of the first monthly premium is imposed; and when issued on the weekly payment plan a tax of 40 per cent of the amount paid for the first weekly premium is imposed, so that the tax levied upon such casualty-insurance policies will correspond to the tax levied upon similar life-insurance policies.

INSURANCE-TAX ESTIMATE.

During the period the insurance provisions were in operation during the fiscal year 1918 the revenue receipts from insurance amounted to \$6,492,000. It is estimated that the receipts from insurance during the first 12 months this bill is in operation will amount to \$12,000,000.

TITLE VI. TAX ON BEVERAGES.

In fixing the rates upon beverages your committee, in the preparation of this bill, has endeavored to fix the maximum revenue-producing rate, and therefore the bill provides in the case of distilled spirits for beverage purposes for an increase in the rate from \$3.20 to \$8 per gallon and in the case of beverages to be used for manufacturing purposes for an increase in the rate from \$2.20 to \$4.40 per gallon. In the case of imported perfume containing distilled spirits, the bill provides for an increase in the rate from \$1.10 to \$3.30 per gallon, in order to place the imported perfume upon the same tax basis as domestic perfume.

In the case of all other beverages, other than soft drinks, the rates under existing law are doubled.

The present law levies the tax upon soft drinks upon the basis of the gallon and the present tax only applies to soft drinks sold by the manufacturer, producer, or importer. As a considerable portion of the soft drinks sold are compounded at the soda fountain, and not reached under existing law, the taxes levied under existing law are not great revenue producers. In order to secure a greater revenue from soft drinks the bill provides that a tax of 30 per cent be levied upon the manufacturer's, producer's, or importer's selling price of cereal beverages, and that a tax of 20 per cent be levied upon the manufacturer's, producer's, or importer's selling price of all other soft drinks.

In the case of soft drinks, compounded or mixed at the soda fountain, ice-cream parlor, or other similar places of business, and ice cream, ice-cream sodas, sundaes, or other similar articles of food or drink when sold for consumption in or in proximity to such places of business, the bill levies a tax of 2 cents for each 10 cents or fraction thereof of the selling price to be collected from the consumer by the proprietor of the soda fountain or similar place of business and returned to the Government. In the case of sales amounting to 7 cents or less the tax will only be 1 cent.

The following table shows the beverage rates under existing law and under the proposed bill.

Beverages.

Distilled spirits, rectified spirits, fermented liquors and wines, etc.	Existing law.	Proposed bill.
Distilled spirits, per proof gallon or wine gallon if below proof.....	\$3.20	\$8.00
If withdrawn for other than beverage purposes.....	2.20	4.40
Perfume imported containing distilled spirits, per wine gallon (to be collected by collector of customs).....	1.10	3.30
Grape brandy or wine spirits (to be assessed):		
Used in the fortification of sweet wines, per proof gallon.....	.30	.60
In sweet wines held for sale by the producer, per proof gallon.....	.10	.20
Withdrawn for fortifying wine and not used, per proof gallon.....	.20	.30
Distilled spirits, stock on hand, held and intended for sale, a tax equal to the additional taxes imposed:		
Rectified spirits (with certain exceptions), per proof gallon.....	.15	.30
Rectified spirits, floor tax, per gallon.....		.15
Fermented liquors, per barrel, containing not more than 31 gallons (and a proportionate rate for any other quantity or for fractional parts of a barrel authorized by law).....	3.00	6.00
WINES.		
Still wines, including vermouth, and artificial or imitation wines and compounds sold as wine containing:		
Not more than 14 per cent absolute alcohol per wine gallon.....	.08	.16
Over 14 per cent but not over 21 per cent alcohol per wine gallon.....	.20	.40
Over 21 per cent but not over 24 per cent alcohol per wine gallon.....	.50	1.00
Over 24 per cent (classed as distilled spirits) per wine gallon.....	3.20	8.00
Champagne or other sparkling wines, per one-half pint or fraction thereof.....	.06	.12
Artificially carbonated wine, per one-half pint or fraction thereof.....	.03	.06
Liqueurs, cordials, or similar compounds, containing sweet wine, fortified with grape brandy, or wine spirits, per one-half pint or fraction thereof.....	.03	.06
Other liqueurs, cordials, and similar compounds.....		.06
Floor tax on tax-paid wines, vermouth, and artificial or imitation wines and compounds sold as wine, held and intended for sale, a tax equal to additional taxes imposed.....		
Upon all prepared sirups or extracts used in the manufacture of soft drinks:	Rate per gallon.	Per cent.
If sold for not more than \$1.30 per gallon.....	\$0.05	
If sold for more than \$1.30 and not more than \$2 per gallon.....	.08	
If sold for more than \$2 and not more than \$3 per gallon.....	.10	
If sold for more than \$3 and not more than \$4 per gallon.....	.15	
If sold for not more than \$4 per gallon.....	.20	
Upon all unfermented grape juice, soft drinks, or artificial mineral waters (not carbonated) sold by manufacturer, producer, or importer, in bottles or closed containers.....	.01	20
Upon beverages derived wholly or in part from cereals or substitutes therefor, containing less than one-half per cent of alcohol.....	.01	30
Upon all ginger ale, root beer, sarsaparilla, pop, and all other carbonated waters or beverages manufactured and sold by the manufacturer, producer, or importer of the carbonic-acid gas used in carbonating the same.....	.01	20
Upon all natural mineral waters or table waters sold by the producer, bottler, or importer thereof, in bottles or other closed containers, at over 10 cents per gallon..	.01	(1)
Upon all carbonic-acid gas in drums or other containers (intended for use in the manufacture or production of carbonated water or other drinks), sold by the manufacturer, producer, or importer thereof..... per pound..	.05	
Soft drinks compounded or mixed at a soda fountain, ice-cream parlor, for other similar place of business, ice-cream, ice-cream sodas, sundaes, or other similar articles of food or drink, when sold for consumption in or in proximity to such place of business.....		(2)

¹2 cents per gallon.
²2 cents for each 10 cents or fraction thereof of the amount paid. Where the charge is 7 cents or less the tax will be 1 cent.

Many of the special provisions relating to beverages which are now found in the revenue acts of 1916 and 1917 are carried into this bill without material change in order that the provisions of the revenue acts of 1916 and 1917 relating to beverages may all be incorporated in this bill.

The following new legislation is contained in the bill:

(1) By section 602 the commissioner, with the approval of the Secretary, may permit distillers of ethyl alcohol for use in the production of munitions of war or other nonbeverage purposes to empty their fermenting tubs as often as in his judgment it may be deemed expedient, the provisions of existing law to the contrary notwith-

standing. This legislation is in the interest of expediting the manufacture of munitions and in order to provide for getting the maximum use out of each fermenting tub.

(2) By section 603 the commissioner, with the approval of the Secretary, may permit ethyl alcohol of not less than 180 degrees proof produced at central distilling and denaturing plants to be removed before or after denaturation from such plant or from denaturing bonded warehouses free of tax for the use of the United States or for shipment to any nation engaged in the present war with the Imperial German Government. This legislation is also suggested as a war measure.

(3) In order to enable the Internal Revenue Bureau to keep a more accurate check upon all wine producers, section 616 of the bill requires all producers of wine to be duly registered.

(4) A floor tax of 15 cents per proof gallon is levied upon rectified spirits.

(5) Liqueurs, cordials, or similar compounds are not taxable as such under existing law unless they contain sweet wine fortified with grape brandy. The tax in the bill of 6 cents on each one-half pint or fraction thereof applies to all liqueurs, cordials, or similar compounds.

(6) Under existing law the producer of fortified wines is allowed six months to pay the tax upon grape brandy used in fortifying sweet wines. Because of doubling the rate upon grape brandy, and the fact that the producer of such wines has to hold the wines for a considerable period before sale, the producers of these wines are given 10 months to pay the tax.

(7) Under the present law retail liquor dealers were allowed to hold 50 gallons of distilled spirits and 25 gallons of wines free from the floor tax. The bill eliminates every exemption of this nature because it is believed the revenue needs require it.

(8) Due to the levy of a tax on soft drinks sold at the soda fountain, the bill does not include the provision in existing law levying a tax upon carbonic-acid gas, since the theory upon which the tax upon carbonic-acid gas was levied was that by placing the tax upon the gas used at the soda fountain a tax was indirectly levied upon the drink sold at the soda fountain. The tax in this bill will be a greater revenue producer and a more satisfactory basis for levying the tax.

BEVERAGE TAX ESTIMATES.

The following table shows the estimated revenue collections from the beverage taxes during the first 12 months period the law is in operation, disregarding the effect of any prohibition legislation:

Spirits:	
For beverage use.....	\$760,000,000
For other use.....	35,200,000
Rectified.....	11,400,000
Fermented liquors.....	240,000,000
Wines, etc.....	20,000,000
Cereal beverages.....	24,000,000
Other soft drinks, sold by the manufacturer, producer, or importer....	10,000,000
Soft drinks, ice cream, etc., sold at soda fountains.....	37,000,000
Total.....	<u>1,137,600,000</u>

TITLE VII. TAX ON CIGARS, TOBACCO, AND MANUFACTURES THEREOF.

Your committee, after making a careful study of the tobacco of England and the monopoly receipts from tobacco and products of France and Italy, and the revenues raised there in proportion to population as compared with the United States, concluded that the proposed taxes are approximately the revenue-producing rates that can safely be levied in the States at this time in the interest of a continuous flow of revenue to the Treasury and without greatly reduced consumption of tobacco and manufactures thereof. Under the revenue act of 1917 dealers were allowed to hold not to exceed 100 pounds of manufactured tobacco and snuff and not to exceed 1,000 cigars or cigarettes free from the floor taxes levied under that act. It has been the purpose of your committee in framing this bill to eliminate all such exemptions as far as possible and in this particular case no similar exemption is provided in this bill.

The revenue act of 1917 only levied one-half of the additional tax imposed by that act upon cigars, cigarettes, and manufactured tobacco and snuff held by retail dealers upon the passage of the act. This bill provides that the entire additional taxes imposed by that act be levied upon all stocks held and intended for sale by any person upon the passage of this act.

The following table shows the rates under existing law and the rates proposed by this bill upon cigars, cigarettes, and manufactures of tobacco and snuff:

Tobacco, snuff, cigars, and cigarettes.

Item.	Existing law.
Cigars weighing not more than 3 pounds per 1,000, per thousand.....	\$1.00
Cigars weighing more than 3 pounds per 1,000, if manufactured or imported to retail at—	
Less than 4 cents each, per thousand.....	3.00
4 cents or more each and not more than 5 cents each, per thousand.....	4.00
More than 5 cents each and not more than 7 cents each, per thousand.....	4.00
More than 7 cents each and not more than 8 cents each, per thousand.....	6.00
More than 8 cents each and not more than 15 cents each, per thousand.....	6.00
More than 15 cents each and not more than 20 cents each, per thousand.....	8.00
More than 20 cents each, per thousand.....	10.00
Cigarettes weighing not more than 3 pounds per thousand, if manufactured or imported to retail at—	
Less than 2 cents each, per thousand.....	2.05
2 cents or more each, per thousand.....	2.05
Cigarettes weighing more than 3 pounds per thousand, per thousand.....	4.80
Tobacco, however prepared, manufactured or imported, and sold, or removed for consumption or sale, per pound.....	.13
Snuff, however prepared, manufactured or imported, and sold, or removed for consumption or sale, per pound.....	.13
Cigarette papers, on each package, book, or set, containing—	
More than 25 but not more than 50 papers.....	.004
More than 50 but not more than 100 papers.....	.01
Over 100 papers, for each 100 or fraction thereof.....	.01
Cigarette tubes, for each 100 or fraction thereof.....	.02
Floor stock tax on cigars, cigarettes, manufactured tobacco and snuff, equal to the difference between the tax paid under existing law and the tax imposed under proposed bill.	

ESTIMATES.

The following table shows the revenue collected from cigars, tobacco, snuff, and cigarette papers and tubes during the fiscal year 1918 and the estimated revenue therefrom for the fiscal year 1919.

year 1919 under existing law and for the first twelve-month period under the proposed bill:

Items.	Fiscal year 1918.	Fiscal year 1919 under existing law (estimated).	For 12-month period under proposed bill.
Cigars.....	\$30,909,000	\$41,700,000	\$41,364,000
Cigarettes.....	66,000,000	100,000,000	165,240,000
Tobacco.....	48,000,000	63,700,000	104,000,000
Snuff, etc.....	10,000,000	6,000,000	9,100,000
Papers and tubes.....	325,000	750,000	1,500,000
Totals.....	155,234,000	212,150,000	341,204,000

TITLE VIII. TAX ON ADMISSIONS AND DUES.

ADMISSIONS.

Under existing law the tax upon the amount paid for admission to any place of amusement is 1 cent for each 10 cents or fraction thereof of the amount paid for such admission. The bill increases this tax to 2 cents for each 10 cents or fraction thereof of the amount paid for such admission. Under existing law and under the proposed bill in the case of children under 12 years of age the tax upon such admission will be 1 cent regardless of the amount paid for the admission.

Under existing law there is no tax levied upon admission to any place the maximum charge for admission to which is 5 cents or in the case of shows, rides, and other amusements (the maximum charge for admission to which is 10 cents) within outdoor general amusement parks or in the case of admission to such parks. The proposed bill provides in lieu of this provision that in cases where the charge for admission is 7 cents or less the tax shall be 1 cent.

In the case of persons (except bona fide employees, municipal officers on official business, and children under 12) admitted free to any place at a time when and under circumstances under which an admission charge is made to other persons, a tax of 1 cent for each 10 cents or fraction thereof of the price charged such other persons for the same or similar accommodations is required to be paid by the person so admitted under existing law. The proposed bill proposes to increase this tax to 2 cents for each 10 cents or fraction thereof of the price so charged and also proposes to exempt from the payment of the admission tax persons in the military or naval service of the United States when in uniform, admitted free by the proprietor. In the case of persons receiving reduced rates of admission to any place, a tax of 2 cents for each 10 cents or fraction thereof of the price charged to other persons for the same or similar accommodations is levied.

TAX ON TICKETS SOLD AT OTHER THAN THEATERS, OPERAS, AND PLACES OF AMUSEMENT.

The following new taxes upon the amount paid for admissions are levied:

In the case of tickets or cards of admission to theaters, operas, and other places of amusement, sold at news stands, hotels, and places

other than ticket offices at not to exceed 50 cents in excess of the sum of the established price therefor at the ticket office plus the amount of the admission tax, the bill imposes a tax equivalent to 5 per cent of the amount of such excess, and if such tickets are sold for more than 50 cents in excess of the established price plus the amount of the regular admission tax an additional tax equivalent to 30 per cent of the whole amount of such excess. If a proprietor, manager, or employee of an opera house, theater, or other place of amusement sells or disposes of tickets or cards of admission in excess of the regular established price or charge therefor a tax equivalent to 50 per cent of the excess so charged is imposed.

Under existing law in case of persons having permanent use of a box or seat in an opera house or any place of amusement or a lease for the use of a similar box or seat a tax equivalent to 10 per cent of the amount for which such box or seat is sold for a performance or exhibition is required to be paid by the person enjoying such privilege. The bill increases this tax to an amount equivalent to 25 per cent of the amount for which similar boxes or seats are sold.

The revenue act of 1917 levied a tax of 1 cent for each 10 cents or fraction thereof paid for admission to any public performance for profit at any cabaret or other similar entertainment and in case the amount charged for admission was included in the price paid for refreshment, service or merchandise, left the amount so included for admission to be determined by the commissioner. Under this provision the Treasury Department determined that a general rule could be laid down to the effect that 20 per cent of the amount paid for refreshment, service and merchandise represented approximately the amount covered by the total price paid which could be attributable to the admission charge, and upon the basis of this ruling collected the tax levied under existing law. A provision of the bill contains this Treasury ruling as a basis for determining the tax upon the admission where the admission charge is included in the price charged for refreshments. The tax upon admission to roof gardens, cabarets, and other similar entertainments is increased from 1 cent for each 10 cents or fraction thereof to 2 cents for each 10 cents or fraction thereof of the amount paid.

TAX UPON DUES.

The revenue act of 1917 levied a tax of 10 per cent upon the amount paid as dues or membership fees (including initiation fees) to any social, athletic, or sporting club or organization where such dues or fees are in excess of \$12 per year. This tax is increased to 20 per cent of the amount paid where the dues or fees of an active resident annual member are in excess of \$10 per year, and a like tax is imposed upon dues or membership fees of stock and produce exchanges. Under existing law if the dues or fees including initiation fees amounted to \$12 a tax of 10 per cent was collected, although the dues or fees exclusive of the initiation fees might be less than \$12. The present law is changed by the bill so that a tax of 20 per cent will be levied upon the dues or membership fees where such dues or fees are in excess of \$10 per year and upon initiation fees if such fees amount to more than \$10

ADMISSION AND DUES TAX ESTIMATES.

Your committee believes that the doubling of the rates on admissions and dues will result in doubling the revenue from these sources and that these taxes can be easily borne by the taxpayers.

During the period of the fiscal year 1918 that the present admission and dues taxes were in effect, the revenue yield therefrom amounted to \$26,357,000. It is estimated that during a 12-month period the present rates on admissions and dues will yield \$50,000,000 and the proposed rates \$100,000,000.

TITLE IX. EXCISE TAXES.

In recommending excise taxes in the proposed bill your committee has endeavored to select articles that fall within two classes: (1) Articles that are more or less a luxury because of their nature and (2) articles that become in the nature of a luxury when sold for more than a fixed price. The purpose of the committee in recommending these taxes is twofold: (1) To provide revenue and (2) to reduce extravagance.

So far as practicable the committee has placed these taxes upon the manufacturer, producer, or importer. In the second group of articles that are regarded as a luxury when sold over a fixed price your committee believes that these taxes should be paid by the consumer and collected by the retailer and by him returned to the Government, and the bill so provides.

Under existing law the tax upon jewelry is based upon the manufacturer's selling price. The jewelry definition has been materially extended in the interest of securing more revenue from this source and because of this extension your committee is of the opinion that this provision can be better administered by placing the tax upon the basis of the retail sales.

A floor tax is levied upon all articles specified in section 900 equal to the difference between the tax that has been paid upon such articles and the tax provided by this bill, or if no tax has heretofore been levied upon any article specified in this section a tax equal to the tax imposed by this bill.

Section 905 levies a tax of 20 per cent upon the amount paid in excess of a fixed price upon articles upon which this tax is imposed because regarded as a luxury when sold for an amount in excess of the fixed price.

Section 907 imposes a tax of 10 per cent, in addition to the tax on retail sales of jewelry, on the amount paid for all jewelry composed in whole or in part of platinum. Such tax is to be collected by the vendor from the purchaser and paid over by him to the United States, together with the name and address of the purchaser and a description of the article sold.

It is estimated that the revenue from the excise taxes during the first 12 months this bill is in operation will amount to \$517,305,000.

The following tables show the excise taxes levied under existing law and the proposed bill except those specified in section 905 of the bill which are fully set out therein.

REVENUE BILL OF 1918.

Excise taxes on manufacturer, producer, or importer.

	Present law (per cent of price for which sold).	Proposed bill (per cent of price for which sold).
Automobile trucks, automobile wagons.....	3	3
Automobiles or motorcycles.....	3	10
Piano players, graphophones, phonographs, talking machines and records used in connection with any musical instrument, etc.....	3	10
Moving picture films (which have not been exposed) per linear foot.....	¹ / ₂	10
Positive moving picture films, per linear foot.....	¹ / ₂	10
Jewelry, real or imitation, on price for which sold by manufacturer, producer, or importer on retail price.....	3	10
Sporting goods.....	3	10
Chewing gum or substitutes therefor.....	2	6
Cameras.....	3	10
Perfumes, essences, extracts, cosmetics, toilet soaps, etc., of price for which sold by manufacturer, producer, or importer.....	2	
Of price paid by consumer for each 10 cents or fraction thereof paid.....		¹ / ₂
Pills, tablets, powders, etc. (proprietary medicines, etc.), of price for which sold by manufacturer, producer, or importer.....	2	
Of price paid by consumer for each 10 cents or fraction thereof paid.....		¹ / ₂
Floor stock tax: To be paid by the person holding any of the following articles for sale upon which the tax under the revenue act of 1917 has been paid (not applicable to second-hand articles):		
Automobile trucks and wagons.....		2
Automobiles and motorcycles.....		7
Piano players, graphophones, phonographs, talking machines and records used in connection with any musical instruments, etc.....		7
Positive moving picture films.....		¹ / ₂ 10
Sporting goods.....		7
Chewing gum.....		4
Cameras.....		7

¹ Cent.² Less ¹/₂ cent per linear foot.

NEW EXCISE TAXES.

On manufacturer, producer, or importer.

	Per cent of price when sold or leased.
Automobile trailers or tractors, including tires, inner tubes, parts, accessories.....	5
Automobile tires, tubes, parts, accessories, sold on or in connection with:	
Trucks and automobile wagons.....	5
Automobiles or motorcycles.....	10
Tires, tubes, parts or accessories, sold to any person other than a manufacturer or producer of automobiles, etc.....	10
Pianos and pipe organs.....	10
Clocks, opera glasses, lorgnettes, marine glasses, and binoculars.....	10
Photographic films and plates, other than moving-picture films.....	10
Candy.....	10
Firearms, shells, and cartridges:	
Pistols and revolvers.....	25
All other firearms and shells and cartridges.....	10
Dirk knives, bowie knives, daggers, sword canes, stiletos, and brass or metallic knuckles.....	100
Electric fans.....	10
Thermos and thermostatic bottles, etc.....	10
Tapestries and textiles for furniture coverings or hangings in interior decoration.....	10
Cigar or cigarette holders and pipes, meerschauum or amber, humidors, and smoking stands.....	10
Photographs, productions or reproductions.....	10
Duplicating machines.....	10
Cash registers.....	10
Adding machines.....	10
Automatic slot-device weighing or vending machines.....	10
Liveries and livery boots and hats.....	10
Hunting garments and riding habits.....	10
Bathing suits.....	10
Articles, made from any of the following furs: Seal, Hudson seal, Russian or Hudson Bay, sable, ermine, silver fox, natural black fox, natural blue fox, natural American mink, fisher, otter, kolin/ky, squirrel, skunk, or mole.....	10
Yachts and motor boats; and pleasure boats and canoes if sold for more than \$15 each.....	10
Gasoline, per gallon.....	¹ / ₂
Sculpture, paintings, and statuary, sold by other than the artist, upon the purchaser for consumption.....	10
Platinum jewelry, on amount by consumer, an additional.....	10

¹ Cents.

Of amount paid.

TITLE X. SPECIAL TAXES.

After considering all the special tax sources suggested to your committee it has endeavored to select such special taxes as would yield considerable revenue and at the same time well distribute the burden of taxation and be capable of satisfactory administration by the Treasury Department. It is believed that the special taxes recommended in the proposed bill will yield about \$165,000,000 annually.

The following table shows the special taxes levied under existing law and the proposed bill:

Special taxes.

Item.	Existing law.	Proposed bill.
Corporations, for each \$1,000 of value of capital stock--		
Exceeding \$99,000.....	\$0.50
Exceeding \$5,000.....		\$1.00
Brokers.....	3.00	100.00
If a broker is a member of any stock exchange, or if he is a member of any produce exchange, board of trade, or similar organization, where produce or merchandise is sold and if the average value during the preceding year ending June 30, of a seat or membership in such exchange or organization was--		
Not more than \$2,000, an additional.....		50.00
More than \$2,000 and not more than \$5,000, an additional.....		100.00
More than \$5,000, an additional.....		150.00
Pawnbrokers.....	50.00	100.00
Ship brokers.....	20.00	50.00
Customhouse brokers.....	10.00	50.00
Theaters, museums, and concert halls:		
Seating capacity not exceeding 250.....	25.00	50.00
Seating capacity over 250 and not exceeding 500.....	50.00	100.00
Seating capacity over 500 and not exceeding 800.....	75.00	150.00
Seating capacity exceeding 800.....	100.00	200.00
Theaters, museums, and concert halls (cities, towns, or villages of 5,000 population or less), according to seating capacity, one-half of that above stated.....	12.50	25.00
to.....	50.00	100.00
Circuses (one special tax for exhibition within any one State, Territory, or District) Exhibitions not otherwise provided for (one special tax for exhibitions within any one State, Territory, or District).....	100.00	200.00
Aggregation of entertainments, known as "a street fair" (maximum).....	100.00	200.00
Bowling alleys and billiard rooms, for each alley or table.....	5.00	10.00
Shooting galleries.....		20.00
Riding academies.....		100.00
Sight-seeing automobiles, on the basis of the gross receipts during the preceding year ending June 30, from the operation of each such automobile having a seating capacity of more than seven.....		10
Business of operating for hire of three or more passenger automobiles (other than sight-seeing automobiles having a seating capacity of more than seven), on the basis of gross receipts during the preceding year ending June 30, from the operation of each such automobile.....		15
Carrying on the business of a brewer, distiller, wholesale liquor dealer, retail liquor dealer, wholesale dealer in malt liquor, or manufacture of stills, contrary to the laws of any State, Territory, or District, in any place in which carrying on such business is prohibited by local or municipal law, in addition to all other taxes.....		1,000.00
Proprietors of any trade, business, or profession, the gross receipts of which for the year ending June 30 exceed \$2,000.....		10.00
If such gross receipts from sources other than sales directly to the consumer exceed \$100,000, the proprietor shall pay, additional.....		15.00
SPECIAL TAXES ON MANUFACTURERS OF TOBACCO, COARS, AND CIGARETTES.		
Manufacturers of tobacco:		
Annual sales not over 50,000 pounds.....	3.00	6.00
Annual sales over 50,000 and not over 100,000 pounds.....	6.00	12.00
Annual sales over 100,000 and not over 200,000 pounds.....	12.00	24.00
Annual sales over 200,000 pounds, per 1,000 pounds or fraction.....	.08	.16
Manufacturers of cigars:		
Annual sales not over 50,000 cigars.....	2.00	4.00
Annual sales over 50,000 and not over 100,000 cigars.....	3.00	6.00
Annual sales over 100,000 and not over 200,000 cigars.....	6.00	12.00
Annual sales over 200,000 and not over 400,000 cigars.....	12.00	24.00
Annual sales over 400,000 cigars, per 1,000 or fraction.....	.05	.10
Manufacturers of cigarettes, including small cigars weighing not more than 3 pounds per thousand: Per 10,000 cigarettes, including small cigars, or fraction thereof..		
Upon the use of all yachts, pleasure boats, power boats, motor boats with fixed engines, and sailing boats, of over 5 net tons, length--		
Not over 50 feet, for each foot.....	.50	1.00
Over 50 feet and not over 100 feet, per foot.....	1.00	2.00
Over 100 feet, per foot.....	2.00	4.00

1 Per cent.

Special taxes—Continued.

Item.	Existing law.	Proposed bill.
SPECIAL TAXES ON MANUFACTURERS OF TOBACCO, CIGARS, AND CIGARETTES—CON.		
Manufacturers of cigars—Continued.		
Motor boats of not over 5 net tons with fixed engines.....	\$5.00	\$10.00
Businesses consisting of the retailing of merchandise through or upon orders received by mail, on the basis of the retail sales during the preceding year ending June 30, on the gross amount in excess of \$100,000.....		(1)
Use of motorcycles.....		5.00
Use of automobiles:		
(Other than electric) 23 horsepower or less.....		10.00
More than 23 horsepower and not more than 30 horsepower.....		20.00
More than 30 horsepower and not more than 40 horsepower.....		30.00
More than 40 horsepower.....		50.00
Use of electric automobiles.....		(?)
Manufacturer of automatic vending or weighing machines who operate such machines, on the basis of the gross amount received by him from such operation during the preceding year ending June 30.....		(2)

11 per cent.

\$5 per horsepower and 50 cents for each 100 pounds of weight.

5 per cent.

AMENDMENT OF HARRISON NARCOTIC ACT.

The decision of the Supreme Court in the *Jim Fuy Moy* case (June 5, 1916) has made it very difficult to enforce the act of December 17, 1914, known as the Harrison Narcotic Act. Under that decision it is impossible to hold criminally liable a person having in his possession any amount of the habit-forming drugs included within that act, unless such person is a dealer therein. The proposed bill in section 1008 amends that act so as to place an internal revenue tax, payable by stamp, upon such drugs, and provides that the possession of an unstamped package shall be *prima facie* evidence of a violation of the act.

Section 6 of the Harrison Narcotic Act exempts from the operation of the act preparations containing only a small proportion of narcotics. In the administration of the act it has been found that the exemption has made the adequate enforcement of the act almost impossible, and that many preparations are marketed which contain a lawful amount of the drugs, but which are of great harm to the consumer. The bill therefore provides in section 1009 for the amendment of section 6 so as to make the Harrison Narcotic Act apply to all habit-forming drugs.

Under the present law only prepared smoking opium seized by the United States Government from any person violating the acts of October 1, 1890, as amended by the acts of March 3, 1898, February 9, 1909, and January 7, 1914, may be sold to the highest bidder, pursuant to the provisions of section 3460 of the Revised Statutes of the United States. The Secretary of the Treasury does not have any authority to dispose of coca leaves, their salts, and derivatives, or compounds, or opium, except smoking opium, in any manner whatever, when seized for violation of any of the above acts, or when seized under the act of December 17, 1914. Neither are the courts authorized by any statute to dispose of coca leaves, their salts and derivatives or compounds, or any opium, except smoking opium.

At the present time, the Federal Government has in its possession, at the present market value, about \$100,000 worth of opium salts and alkaloids, and salts and derivatives of coca leaves seized by it from persons violating the acts aforementioned.

Section 1010 of the bill permits the Federal Government to deliver this amount of opium salts and alkaloids, and salts and derivatives of coca leaves, and any such salts and alkaloids, hereafter taken to any department, bureau, or agency of the United States Government for use for medicinal or scientific purposes.

TITLE XI. STAMP TAXES.

The bill reenacts the stamp tax provision of the revenue act of 1917 without changing the rates except in one instance. In the case of playing cards an increase from 7 cents to 8 cents per package is recommended. The following table shows the articles subject to stamp tax and the rates proposed upon the same.

Stamp taxes—Schedule A.

	Rate.
1. Bonds, debentures, or certificates of indebtedness issued by any person, corporation, partnership, or association, on each \$100 of face value or fraction thereof.....	\$0. 05
2. Indemnity and surety bonds.....	. 50
Where premium is charged for the execution of such bond, on each dollar or fractional part thereof, 1 per cent.	
3. Capital stock issue: On each original issue of certificates of stock, whether on organization or reorganization, on each \$100 of face value or fraction thereof.....	. 05
Capital stock issued without face value, on each \$100 of actual value or fraction thereof, per share.....	. 05
4. Capital stock sales or transfers: On all sales, or agreements to sell, or memoranda of sales, or deliveries of or transfers of legal title to shares or certificates of stock of any association, company, or corporation, on each \$100 of actual or face value or fraction thereof.....	. 02
5. Produce, sales of, on exchange: Upon each sale, agreement of sale, or agreement to sell any products or merchandise at any exchange or board of trade or similar place for future delivery, for each \$100 in value of the merchandise covered.....	. 02
And for each additional \$100 or fraction thereof.....	. 02
6. Drafts or checks (payable otherwise than at sight or on demand) upon their acceptance or delivery within the United States whichever is prior, promissory notes, except bank notes issued for circulation, and for each renewal of the same, for a sum not exceeding \$100 (except obligations secured by pledge of bonds or obligations of United States).....	. 02
And for each additional \$100 or fraction thereof.....	. 02
7. Conveyances: Deeds, instrument, or writing conveying lands, tenements, or other realty sold, etc., value over \$100 and not exceeding \$500.....	. 50
For each additional \$500 or fractional part thereof.....	. 50
8. Entry of goods, wares, or merchandise at any customhouse, not exceeding \$100 in value.....	\$0. 25
Exceeding \$100 and not exceeding \$500 in value.....	. 50
Exceeding \$500 in value.....	1. 00
9. Entry for the withdrawal of goods or merchandise from custom-bonded warehouses.....	. 50
10. Passage tickets, one way or round trip, for each passenger, sold or issued in the United States for passage by vessel to places not in the United States, Canada, or Mexico, costing not exceeding \$30.....	1. 00
More than \$30 and not exceeding \$60.....	3. 00
More than \$60.....	5. 00
(Passage tickets costing \$10 or less exempt.)	
11. Proxy for voting at any election of officers of any incorporated company or association, except religious, charitable, fraternal, or literary societies, or public cemeteries.....	. 10
12. Power of attorney.....	. 25
(Exemption: Papers used in the collection of claims for pensions, back pay or bounty, or for property lost in the military or naval service, or in bankruptcy cases.)	
13. Playing cards: Upon every pack containing not more than 54 cards.....	. 08
14. Parcel-post packages, where the postage amounts to 25 cents or more, for each 25 cents or fractional part thereof.....	. 01

During the period of the fiscal year 1918 that the stamp taxes were in effect the revenue yield therefrom amounted to \$18,815,000. It is estimated that these taxes will yield \$32,000,000 during a 12-month period.

TITLE XII. ADVISORY TAX BOARD.

Because of the large number of difficult cases that arise under the internal-revenue laws by reason of the great scope of the same, the amount of revenue involved in the collection of the same, and to assure fair and adequate consideration of every case arising under the internal-revenue laws, the bill provides for the creation of a board of tax advisors to be known as the "Advisory tax board," to pass upon all cases referred to them by the Secretary of the Treasury or Commissioner of Internal Revenue or to consider any case in which the taxpayer shall request that the board consider. The board is to consist of five members to be appointed by the President of the United States by and with the advice and consent of the Senate. The bill provides that the board shall remain in existence during the continuance of the present war with the Imperial German Government and for a period of one year after the termination of such war. The salary provided for each member of the board is \$9,000 per year and is deemed to be the lowest salary advisable in view of the class of men that it is desired shall be secured for this board.

TITLE XIII. GENERAL ADMINISTRATIVE PROVISIONS.

The salary of the Commissioner of Internal Revenue is increased by the bill to \$10,000 a year. Such a salary is small enough compensation for one qualified, as the present commissioner concededly is, to fill the position of Commissioner of Internal Revenue with its onerous duties and vast responsibilities.

APPROPRIATION TO CARRY THIS ACT INTO EFFECT FOR THE FISCAL YEAR 1919.

The Commissioner of Internal Revenue appeared before your committee on August 15 and fully set forth the plans of his bureau for collecting the internal revenue under the new bill during the fiscal year ending June 30, 1919, and the estimated cost of collecting the same. His statement has been printed as Hearings No. 29 and sets forth in detail the estimated cost of maintaining the Internal Revenue Bureau and the estimated additional employees required. Your committee believes that the sum requested by the Commissioner of Internal Revenue of \$7,500,000 additional is a reasonable estimate and recommends that this amount be appropriated. This additional appropriation for this fiscal year will make the appropriation for the Internal Revenue Department for this fiscal year amount to approximately \$25,000,000.

Because of the additional responsibility and the great amount of additional work placed upon the collectors of internal revenue, the bill provides that the commissioner, subject to the approval of the Secretary, be allowed to readjust and increase the salary of the collectors of internal revenue upon the basis of the responsibility and internal revenue collections but that in no case shall any collector of internal revenue receive a salary in excess of \$6,000 a year.

Section 301 of the bill authorizes in lieu of the deputy commissioners, whose salaries are now fixed by law, the employment of five deputy commissioners and an assistant to the commissioner at a salary each of \$5,000 a year. The present law provides for three deputy commissioners, two at a salary of \$4,000 per year and one at \$3,600 per year. Due to the increased scope of the internal revenue laws and the greatly increased problems to be met under the same, your committee believes that the recommendation of the commissioner is advisable and in the interest of the better administration of the department, and, therefore, incorporated in the bill such recommendation.

LEGISLATIVE DRAFTING SERVICE.

The bill provides in section 1303 for the creation of a legislative drafting service, under the direction of two draftsmen, one to be appointed by the President of the Senate and one by the Speaker of the House, at a salary of \$5,000 each, the appointments to be made without regard to political affiliation and solely with regard to fitness for the duties of the office. This drafting service would aid in the drafting of public bills on the request of any committee of either House, and would be under the general supervision of the Joint Committee on the Library. For the remainder of the current fiscal year an appropriation of \$25,000 is provided to pay the salaries of the two draftsmen and their necessary assistants and clerks and to provide for the purchase of necessary furniture and supplies.

Your committee during the past two years has received valuable volunteer assistance from expert legislative draftsmen, and is informed that other committees of both Houses have made use of such services, including the Finance Committee of the Senate and the Merchant Marine and Fisheries and the Judiciary Committees of the House, as well as numerous individual Representatives and Senators. The experience of your committee convinces it that the establishment of such a service, on a nonpartisan and permanent basis, will prove of great value in the framing of bills, particularly at this time, when the complexity and wide scope of war legislation with the constantly increasing necessity of dealing with problems never heretofore within the limits of congressional action, render it imperative that all acts of Congress be drawn with the greatest possible clearness and precision.

The remainder of the general provisions carry forward into this bill the general administrative provisions of the revenue acts of 1916 and 1917, which are repealed by this bill. Section 1318 and section 1319 are new sections added to the general administrative provisions. Section 1318 provides that whoever in connection with the sale or lease, or offer for sale or lease, of any article, or for the purpose of making such sale or lease, makes any statement, written or oral, (1) intended or calculated to lead any person to believe that any part of the price at which such article is sold or leased, or offered for sale or lease, consists of a tax imposed under the authority of the United States, or (2) ascribing a particular part of such price to a tax imposed under the authority of the United States, knowing that such statement is false or that the tax is not so great as the portion of such price ascribed to such tax, shall be guilty of a misdemeanor and upon conviction thereof shall be fined not more than \$1,000.

LIBERTY-LOAN BONDS MAY BE USED IN LIEU OF SURETY BONDS.

Section 1319 provides that wherever by the laws of the United States or regulations made pursuant thereto, any person is required to furnish surety or sureties on any bond, such person may, in lieu of surety or sureties, and under regulations prescribed by the Secretary, deposit with the United States an amount of bonds of the United States issued after April 24, 1917, equal to the amount of such bond, together with an agreement authorizing the United States to sell such bonds in case of any default in payment of the bond. As soon as the bond becomes void and of no effect such bonds shall be returned to the depositor.

Your committee is unanimous in recommending the passage of this bill.

RECAPITULATION.

Revenue receipts during the fiscal year 1918 and estimated receipts during the fiscal year 1919 under existing law and under the proposed bill.

	Revenue receipts.		
	Fiscal year 1918.	Fiscal year 1919 under existing law (estimated).	For 12-month period under proposed bill.
Income tax:			
Individual.....	\$930,000,000	\$930,000,000	\$1,482,186,000
Corporation.....	1 528,500,000	528,500,000	894,000,000
Excess-profits tax.....	1 1,791,000,000	1,791,000,000	3,200,000,000
Estate tax.....	47,453,000	75,000,000	110,000,000
Transportation:			
Freight.....	30,000,000	75,000,000	75,000,000
Express.....	6,459,000	20,000,000	20,000,000
Persons.....	24,306,000	60,000,000	60,000,000
Oil by pipe lines.....	1,453,000	3,500,000	4,550,000
Seats and berths.....	2,237,000	5,000,000	5,000,000
Telegraph and telephone.....	6,299,000	14,000,000	16,000,000
Insurance.....	6,492,000	12,000,000	12,000,000
Admissions.....	26,357,000	50,000,000	100,000,000
Club dues.....	2,259,000	4,500,000	9,000,000
Excise taxes:			
Automobiles, etc.....	23,981,000	41,000,000	123,750,000
Jewelry, sporting goods, etc.....	13,000,000	35,000,000	80,000,000
Other taxes on luxuries, at 10 per cent.....			88,790,000
Other taxes on luxuries, at 20 per cent.....			184,795,000
Gasoline.....			40,000,000
Yachts and pleasure boats.....			1,000,000
Beverages.....	300,000,000	500,000,000	1,137,600,000
Stamp taxes.....	18,815,000	32,000,000	32,000,000
Tobacco:			
Cigars.....	30,909,000	41,700,000	61,364,000
Cigarettes.....	66,000,000	100,000,000	165,240,000
Tobacco.....	48,000,000	63,700,000	104,000,000
Snuff, etc.....	10,000,000	6,000,000	9,100,000
Papers and tubes.....	325,000	760,000	1,500,000
Special taxes:			
Capital stock.....	24,996,000	25,000,000	70,000,000
Brokers.....	333,000	850,000	1,765,000
Theaters, etc.....	865,000	1,070,000	2,143,000
Mail order sales.....			5,000,000
Bowling alleys, billiard and pool tables.....	1,086,000	1,100,000	2,200,000
Shooting galleries.....			400,000
Riding academies.....			50,000
Business license tax.....			10,000,000
Manufacturers of tobacco.....		37,000	69,000
Manufacturers of cigars.....	538,000	440,000	850,000
Manufacturers of cigarettes.....		120,000	240,000
Use of automobiles and motorcycles.....			72,930,000
Total.....	3,941,663,000	4,417,267,000	8,182,492,000

¹ Assessed but not collected in 1918.

Income tax based on total individual income of (taxable)..... \$7,400,000,000
 Corporation excess profits and income tax on net income of..... 10,000,000,000

Calendar No. 563.

65th CONGRESS, }
3d Session. }

SENATE.

{ REPT. 617,
Part 2. }

REVENUE BILL OF 1918.

DECEMBER 6, 1918.—Ordered to be printed.

Mr. THOMAS (for himself), from the Committee on Finance, submitted the following

VIEWS OF A MINORITY.

[To accompany H. R. 12863.]

The Finance Committee has, after a long and anxious consideration of the revenue bill reported it to the Senate. I do not think that it is wholly satisfactory either as to rates or subject matter to a single member. It is probably, however, as nearly so as discussion and compromise can make it, and very much more so than would have been the case had the sum to be produced by it remained at \$8,000,000,000. The reduction of this estimate by 25 per cent and the consequent elimination of some of its most objectionable features has gone far towards bringing a majority of the committee to an understanding as to the remainder of the bill.

But while in accord with the committee as to its general structure and rates, I am unable to accept its action relating to what are known as the excess-profits tax. This feature of the bill has been condemned, and justly so, by the President and the Secretary of the Treasury in terms with which the Senate is familiar, and I think by a majority of those who are familiar with its character and operation as embodied in existing law. I opposed it at all times in Committee and am compelled to continue my opposition to it here.

It is proposed to levy this tax upon practically all corporate profits in excess of 8 per cent of the invested capital as defined in the bill, less a deduction of \$3,000; and this without regard to earnings in the prewar period or to the character of the business in which the corporation is engaged. Such a basis of taxation is, in my judgment, arbitrary, unjust, and indefensible. If other objections are needed, they are furnished by that provision which makes the tax an alternative one with the war-profits tax, the commissioner being required to apply that one of the two which in the given case will produce the greater revenue.

Eight per cent profit on invested capital is a just allowance in many cases. In many others, it is too much; in others, far too little. Business pursuits involving practically no hazard may well be content with 6 per cent. Those involving some hazard can be stimulated with 8 per cent. Those involving considerable or very great hazard must have much more to induce capital to risk investment in them. To make a hard-and-fast rule for all business alike is as statesmanlike as to prescribe one punishment for all offenses, or one wage for all workmen, or one rate of levy for all incomes.

Such a method of taxation bears some analogy to the German levies of fines and contributions. It is not so harsh nor so arbitrary, but it embodies the same idea. It sets aside a certain allotment for all concerns and then appropriates the bulk of the remainder. It is a tithing system multiplied by eight. The only justification for it which I have heard is that due to their large antewar profits some corporations would pay no tax at all beyond those imposed by the income-tax schedule. But that is only to say that such corporations have made no war profits and therefore pay no war-profits tax.

This basis for the excess-profits tax, which would penalize all profit over 8 per cent for the sake of reaching a very few of them, is easily removed by the substitute for this title of the bill which I proposed to the committee and which treats as war profits all profits in excess of the profits of representative corporations for the prewar period. Such a provision accomplishes the purpose without doing injustice to all corporations, and without sensibly diminishing the sum total of the estimated revenues.

The tax on war profits, that is to say upon profits due to the existence of the war and in excess of the profits of the prewar period, is a legitimate one and can be made to yield a very large revenue without disturbing or dislocating business and commercial conditions. With the disappearance of the profit the tax will disappear, while the so-called excess-profits tax will not be affected a particle by the return of peace, save as the profit may for that reason tend to decrease in volume. Yet no one would have had the temerity to propose such a tax in any other than times of war. It should, and I trust will be, eliminated from the bill.

In my judgment the so-called estate tax should be stricken from the bill. Apart from the fact that an estate tax is no tax at all, but a condition of inheritance, and that all conditions of inheritance are matters strictly of State concern, with which the Government has nothing to do, thus presenting the question of the validity of such an assessment, is the consideration that estates are a source of State revenue. State sources of taxation are restricted. They consist largely of real estate, licenses, and estates. With the ratification of the eighteenth amendment, State revenues from licenses will be more than cut in half. The expense of State and municipal administration like everything else is increasing. The States have need of all the money they can raise and the imposition of Federal taxes on estates will require the States to increase their levies on real property and their rates of license, both of which are now higher than ever before and likely to remain so. And we may be sure that the State inheritance taxes will be graduated in time quite as high as, if not much higher, than those provided for in the pending bill.

In this connection, we should not overlook the fact that the national debt, which will be not less than \$35,000,000,000, represents that amount of investment of American capital, wholly exempt from State taxation of any sort, and which but for the exigencies of the war would be subject to State assessment. The Government would swiftly resent any intrusion of the States upon its taxing powers. It should be equally considerate of those still remaining to them.

C. S. THOMAS.



Calendar No. 563.

65th CONGRESS, }
3d Session. }

SENATE.

{ REPORT 617
PART 3.

REVENUE BILL OF 1918.

DECEMBER 6, 1918.—Ordered to be printed.

Mr. PENROSE (for himself, Mr. LODGE, Mr. McCUMBER, Mr. SMOOT, Mr. TOWNSEND, and Mr. DILLINGHAM), from the Committee on Finance, submitted the following

VIEWS OF A MINORITY.

[To accompany H. R. 12863.]

The undersigned minority members of the Committee on Finance feel constrained to withhold their support from the provisions recommended by the majority having for their purpose the arbitrary fixing of rates for taxes to be collected mainly in 1920 to the estimated extent of \$4,250,000,000.

With respect to those provisions of the bill as amended by the committee, which it is estimated will produce \$6,000,000,000 revenue for a full 12-months' period, we are generally in accord. These provisions are the result of months of painstaking deliberation and are based upon as accurate and reliable expert information as it was possible to obtain through every agency, official and other. They reflect actual business, industrial, and economic conditions now believed to exist, taking into consideration the rapid transition during the year from the maximum war-needs production to the sudden cessation of hostilities and the arrest of war industry.

Difficult as was the committee's task its conclusions as to just and proper bases of taxation upon current year conditions were, at least, approximately definite and consonant with known facts. We, therefore, were enabled by patient consideration to apply the new and increased taxes in a way to harmonize, so far as practicable, with existing economic, financial, and industrial conditions, and at the same time to provide all the revenue that revised estimates of the Treasury Department indicated as necessary in view of the signing of the armistice, namely, \$6,000,000,000, or \$2,000,000,000 less than was estimated the bill carried when it came to the Senate. The fact that rapidly changing conditions, while the bill was under consideration in the Committee on Finance, enabled the committee to reduce the amount of taxes \$2,000,000,000, furnishes a forcible illustration of the importance of legislating on the subject of taxation, so vital to the country, with the utmost care and in the light of ascertained con-

ditions. It further demonstrates how unwise is the policy of haste and the anticipation of future needs at a time when radical changes in domestic and world conditions render to-day's conclusions perhaps worthless to-morrow.

We recall that it was insisted in July and August, last, that the revenue bill, not even then prepared, should become a law not later than September 28. Disaster to the fourth Liberty loan was predicted, and apprehension was expressed as to the inability of the Secretary of the Treasury to market short-time certificates if the bill were not on the statute books by that date. These predictions, fortunately, were unfulfilled. The Secretary experienced no difficulty in placing short-time certificates, and the fourth Liberty loan was oversubscribed. The country was not affected by lack of knowledge in advance as to the extent and methods of taxation, but went ahead and met each situation as it arose.

Who now will claim that Congress was not justified or lacked wisdom in deliberating upon this, the greatest of all tax bills in history. The fact alone that changed conditions made possible a reduction of \$2,000,000,000 in the interest of the taxpayers justifies the care and scrutiny given the bill by those charged with the constitutional duty of framing it.

In the light, therefore, of this recent valuable experience and object lesson it would be entirely without justification to attempt to prescribe for the American people what amount of taxes they shall be called upon to pay in the year 1920. We can not fail to be impressed with the many difficulties encountered, even with every possible aid, in levying just taxes for the current year; and to undertake to project ourselves into the future, so filled with portentous changes, and arbitrarily and rigidly to fix taxes for the year 1920, is in violation of every sound principle of legislative procedure, and economically is fallacious and unsound.

No one can foresee the full course of events which will crowd the intervening months, and no one with any degree of definiteness can estimate the Government's needs or the country's industrial prosperity. Sources of revenue not now tapped may be made to yield a just portion, thus relieving other sources from onerous taxation. Who can foresee clearly results from the readjustment and reconstruction program inevitably impending and bound to follow the return of peace? Both capital and labor are vitally interested in these readjustments, and will be affected by them in a way that can not be foretold. The problem of the high cost of living is not the least of those awaiting attention, and a wise and carefully considered economic policy must be framed at the proper time with full information as to the facts. Care must be exercised not to disarrange our industrial system in a way which will render either capital or labor less employed in profitable pursuits than at the present time. A sound policy demands that no legislation shall be enacted which will suddenly or unwisely disturb values and prices. Vast governmental undertakings and agencies, made necessary by the war, must come in for a large share of consideration as to the policy to be adopted with respect to those activities in the future, thus presenting the most difficult domestic problems ever confronted by this Nation.

No program for the near or even distant future has been evolved—nothing but the merest outlines, suggestions, and preliminaries—and yet, on the threshold of these nebulous conditions, it is proposed to lay down a hard and fast scheme of taxation for the future. The only argument advanced in behalf of this extraordinary proposition to fix arbitrarily the rates of taxation in the present bill for the year 1920 is, that the taxpayers are entitled to know the amount of reduction in taxes and the character of the taxes for that year. It does not seem to the minority that this argument furnishes any justification for violating the methods of orderly legislative procedure. Every taxpayer in the country knows that taxes will be reduced after this year as the inevitable result of a reduction in governmental needs following the declaration of peace. Every business man knows the next Congress can enact a revenue measure, based on accurate information as to the then existing conditions, which will reduce the burdens of taxation so far as the requirements of the Government will permit. Why, then, attempt to do so in this bill with no knowledge of future conditions and needs?

As a 1918 measure the undersigned minority members of the committee concur in the reporting of the bill, but the measure should stand essentially as a 1918 measure, and the many changes which will be necessary to adapt the tax law to conditions found to obtain in 1919, and subsequent years, should follow and be made at one time and in the light of as full information as it will be possible to obtain.

BOIES PENROSE,
H. C. LODGE,
P. J. McCUMBER,
REED SMOOT,
CHAS. E. TOWNSEND,
WM. P. DILLINGHAM.



Calendar No. 563.

65th CONGRESS, }
3d Session. }

SENATE.

{ REPT. 617,
Part 4. }

REVENUE BILL OF 1918.

DECEMBER 6, 1918.—Ordered to be printed.

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

ADDITIONAL VIEWS.

[To accompany H. R. 12863.]

Differing materially from the plan of taxation imposed by H. R. 12863, as reported to the Senate, I avail myself of the privilege of expressing my personal views, in a separate report, of the provisions of the bill that I believe should never be enacted into law. The unworkable, unscientific, and discriminatory provisions of the act of October 3, 1917, have not been eliminated by H. R. 12863, the pending revenue bill. In some respects they have been modified, but in others increased. If I could have framed the pending revenue bill, I would have made it very simple and so plain that any ordinary business man or individual could have understood it and would have had no trouble in making out a tax return.

Every individual, whether in business as such or as a member of a partnership, would have been treated alike. Every corporation would have been taxed upon the same basis, and the question of capital invested, watered stock, and bonded indebtedness would not have entered into the question of the amount of tax to be imposed, with the single exception of a few corporations with a capital stock of over \$1,000,000, and making undue profits during the prewar period. I would have provided a separate provision for taxing these few corporations. I would have provided for a straight war-profits tax, following the principles outlined in my amendment that I offered on January 5, 1918, to House Joint Resolution 195, with certain modifications, to meet to-day's changed conditions.

I believe that there should be eliminated from the bill all the harassing, nagging taxes—all of which are consumption taxes—and substituted for them a 1 per cent sale tax on all goods sold for consumption or use. A tax of that character would in no way embarrass the producer or the consumer and would yield a revenue of over \$1,000,000,000.

In addition to the 1 per cent sale tax, and a straight war-profits tax, as above referred to, I would include in the bill, title 2, income tax; title 5, tax on transportation, with certain modifications; title 6, tax on beverages, only so far as it affects alcohol, beer, wine, and the floor tax on the same; title 7, tax on cigars, tobacco, and manufactures thereof, with increased rates; title 9, the tax to be limited on automobiles, and on leases for exhibition of any positive motion-picture film; title 10, tax upon capital stock, brokers, manufacturers of tobacco, cigars, and cigarettes, and on pleasure boats. All other items found in any of the above titles should be eliminated.

If this plan were adopted, the bill would provide a larger revenue for the Government than will be received under the provisions of the pending bill, and unjust and discriminatory taxation would be avoided.

That part of the pending bill that deals with the imposition of a tax for the calendar year 1919 I disapprove of and agree with the statement made in the minority report upon this subject. The majority base their action of including in the pending bill provisions for the collection of taxes for the year 1920 upon the recommendations of the Secretary of the Treasury and the indorsement of that plan by the President. I call attention to the fact that the majority have not followed the plan of taxation as recommended by the Secretary of the Treasury, but maintains the unjust and discriminatory plan of taxation on so-called excess profits, as provided in existing law and the pending bill. The Secretary of the Treasury recommended that a flat normal tax be imposed upon all net profits (less certain exemptions) in place of the discriminatory excess-profits tax, in which is involved the questions of watered stock, borrowed money—over and under capitalization—and the definition of invested capital; questions that if incorporated in a revenue bill can not result in anything but the collection of a discriminatory and unjust tax. I much prefer the Secretary's plan than the one proposed in the pending bill.

I call the attention of the country to the fact that the requirements of the Government for the fiscal year ending June 30, 1920, will approximate \$10,000,000,000, which I will explain in detail when I discuss the bill in the Senate. This estimate of \$10,000,000,000 does not take into consideration future estimates that may be sent to Congress that will be included in deficiency appropriation bills. The \$10,000,000,000, with the amount of deficiency appropriations added, will be reduced by whatever amount is received as salvage from the sale of war material paid for and not now needed, either in this country or Europe. There are many relief provisions incorporated in the bill, and I frankly admit as to some of them I do not know what effect they will have upon the revenues to be collected, but that will greatly depend upon the construction that will be placed upon them by the Commissioner of Internal Revenue.

Respectfully submitted.

REED SMOOT.

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3d Session. }

SENATE.

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REVENUE BILL OF 1918.

DECEMBER 6, 1918.—Ordered to be printed.

Mr. LA FOLLETTE, from the Committee on Finance, submitted the following

VIEWS OF A MINORITY.

[To accompany H. R. 12863.]

I concur fully with the minority report of the Committee on Finance in withholding support from the provisions recommended by the majority, having for their purpose the arbitrary fixing of rates of taxation to be collected in 1920. In the confusion and chaos resulting from the sudden termination of the war, neither the needs of the Government nor the sources of its income for 1920 can be more than wildly approximated at this time, and in my opinion, no sound reason for this proposed legislation has ever been given.

I dissent, however, from so much of the report of the minority members of the Finance Committee as concurs with the majority in proposing to raise by taxation under this bill only \$6,000,000,000 or even less than that amount, for the taxable year, and which in consequence permits war profits and excessive incomes to escape fair and reasonable taxation.

I am also of the opinion that the proposed taxes on occupations, amusements, particularly of the cheaper kind, taxes upon freight, express and passenger rates, upon telegraph and telephone messages, and consumption taxes generally, should be eliminated from the bill, and that a heavy tax should be imposed on luxuries.

As is well known, the bill as passed by the House proposed to raise upward of \$8,000,000,000 by taxation. A shrinkage in the beverage tax, among other things, has caused a revision of that estimate. It is now claimed the House bill would, if enacted into law, produce a little more than \$7,400,000,000.

The estimate of the Secretary of the Treasury is that the expenditures of the Government for the fiscal year ending June 30, 1919, will be about \$18,000,000,000. This figure is purely speculative. It is a reduction of \$6,000,000,000 below the estimates made by the Secretary of the Treasury at the time the House bill was framed and prior to the introduction and passage of deficiency appropriation bills covering many billions of dollars additional to such estimate. It

rests upon vague conjectures as to the amount of saving which will result from the termination of the war.

But assuming that the expenditures will be but \$18,000,000,000 for the fiscal year ending June 30, 1919, I contend that sound principles of taxation applied at this time require that at least one-half of this amount should be raised by taxation and not leave more than one-half thereof to be raised by further bond sales.

The Senate bill proposes to decrease the revenue to be derived from incomes and war profits compared with the House bill by about \$1,000,000,000. To be exact the estimates given in the report of the majority of the committee, on page 3, reduces the income tax from that proposed by the House bill \$169,186,000, and reduces what the report terms the "war excess-profits" tax \$800,000,000. The House rates, in my opinion, on these sources of income were too low and instead of being decreased, as this bill proposes, should be increased.

The argument that the war is over and that taxation should therefore be immediately decreased has little or no weight when applied to these two sources of income. This bill when it becomes a law will tax incomes received during the calendar year 1918 and also tax excess and war profits made during the same period. Until practically the day of the signing of the armistice on the 11th of November, we all supposed that the war would continue for many months. Whatever war profits would have been made for the calendar year 1918, if the war had continued until the end of the year, will substantially, so far as anyone can estimate, still be made during that year. Nor will the immediate expenditures of the Government be materially reduced by reason of the cessation of hostilities. The Government needs the money; the war profits will have been made, and the incomes received during the taxable year, and there is no reason why the sudden and unexpected cessation of hostilities should cause us to fix the rates of taxation on these sources of income below what we would have levied if the war had continued.

If we accept the estimates given in the House committee report, and apparently adopted in the majority report, that the net income of corporations for the current taxable year will be \$10,000,000,000 and deduct therefrom \$5,000,000,000, the largest estimate of peace time net income that can be reasonably made for the taxable year, it leaves substantially \$5,000,000,000 of profits made from the war, of which it is proposed to take by taxation under this bill \$2,400,000,000, or about 48 per cent. That is what the bill really proposes to do, although it has been widely heralded throughout the country as a bill which will levy an 80 per cent tax on war profits.

The first year that corporations made income-tax returns to the Federal Government was 1909. The following table shows the corporate net income from 1909 to date:

Corporate net income, 1909 to 1918.

Year.	Net income.	Year.	Net income.
1909.....	\$3,500,000,000	1914.....	\$3,940,000,000
1910.....	3,761,000,000	1915.....	5,310,000,000
1911.....	3,603,000,000	1916.....	8,765,900,000
1912.....	4,151,000,000	1917 ¹	10,500,000,000
1913.....	4,714,000,000	1918 ¹	10,000,000,000

¹ Estimated.

The above estimates for 1917 and 1918 are made by the Treasury Department and can be safely relied on as not being too high. That the estimate of \$5,000,000,000 war profits made by corporations during the taxable year is a reasonable estimate is asserted by the Treasury expert and also appears from a comparison of the net income of corporations during the war with their prewar net income.

The total net income for the three years 1911, 1912, and 1913, adopted as the prewar years, of all corporations was \$12,368,000,000. The average annual net income for the three years was therefore \$4,122,666,000. This deducted from the \$10,000,000,000 net income of corporations for 1918 leaves \$5,877,334,000 over that of the peacetime income for the average of the three prewar years. Making allowance for the normal net income of new corporations—corporations that were not in existence during any of the prewar period—it is plain that the war profits must still account for at least \$5,000,000,000 of the net income of \$10,000,000,000 for 1918.

It is to be remembered also that the above table takes no account of the vast sums made by individuals and partnerships out of the war.

I shall not dwell upon the inequitable features of this bill as between corporations. That is pointed out in the minority report submitted by the Senator from Colorado (Mr. Thomas). But I do protest that it is a gross injustice to the people to take by taxation an amount which must be admitted to be less than one-half of the war profits of the corporations.

This bill is misleading in the rates which it apparently proposes. Passed in its present form it will, for example, produce far less than an 80 per cent tax on war profits. The bill carries many provisions which will accomplish that result. For example:

(1) There is a deduction from the net profits—profits determined by deducting every expense that can possibly be passed as a cost of the business—a minimum of 10 per cent of the total invested capital. This minimum deduction can be as great as was the prewar profits of the concern, possibly one or even many hundred per cent of the prewar capital. This minimum of 10 per cent of the invested capital may be a much larger percentage than it is of the net income. For example, if the profits are 10 per cent of the capital, this deduction becomes 100 per cent of the income.

(2) \$3,000 flat deduction.

(3) Numerous other deductions which appear in many places in the bill, providing for depletion, amortization, or even for limiting the amount of the tax itself.

But this bill has other features that call for further examination in order to ascertain the real rates of taxation under its provisions.

In working out the application of its complex rules the investigator is lead from paragraph to paragraph, back and forth, to provisions which modify and reduce the high rates which catch the eye on first reading.

They have been called "relief provisions" or "cushion provisions."

They should be called "trap-door provisions," as they will prove a ready and convenient exit for disappearing revenues and serve to facilitate the escape of the corporations from just taxation.

They found favor with the committee in a desire to afford relief to a limited number of corporations which appeared to suffer hardship in the application of the general rule. But in an effort to pro-

vide relief for these exceptional cases, which do not constitute one-tenth of 1 per cent of the total number, the grave error has been committed of opening the way for the loss of a vast amount of revenue and the escape of a large number of corporations from just taxation.

The net result of all these deductions is that instead of this tax being an 80 per cent tax, it will average not more than 48 per cent of the net income of corporations, and most likely even less than this.

The principle that should guide us in framing this bill is that no man should be allowed to retain a dollar of profits made out of this war, when thousands of our people have been called upon to give everything, including their lives, for its prosecution, and millions must suffer great hardships on account of it, and generations must sweat and toil to pay its cost. It is intolerable that a favored few should be allowed to amass immense fortunes by reason of this war.

This is the last opportunity to tax war profits. Last year we took less than one-third of such profits. This year's tax bill proposes to take less than one-half, and with the passage of this law the opportunity to reach this war-made wealth by a war profits-tax will disappear forever. The billions saved from taxation through the injustices of this bill, if it becomes a law, will create many millionaires and require further sacrifice and entail greater suffering upon the many millions of our people who have reaped no profit but have suffered hardship and loss as a result of the war.

Senator Thomas in the minority report above referred to, estimates that our debt as the result of this war will not be less than \$35,000,000,000.

Everything that we do not raise by taxation upon war profits at this time, we will be compelled to raise hereafter by bond sales. This will carry with it through years to come further taxation that will greatly increase the cost of living and impose an interest burden which is certain to prove intolerable.

The mass protest against every form of injustice and oppression which is sweeping over the world should admonish us at this time not to go too far with this lopsided system of war finance which deals so tenderly with the taxation of wealth and especially with that form of wealth which has made huge profits out of war.

The Senator from Utah (Mr. Smoot) in his minority report calls attention to the fact that the requirements for the fiscal year ending June 30, 1920, will approximate \$10,000,000,000. This amount will be further increased, he says by the deficiency appropriations, and the total reduced by whatever amount the Government receives as salvage in the sale of war material. If you omit from this bill for 1920 the estimated war-profits tax of \$2,400,000,000 the other taxes proposed will only raise approximately three and a half billion dollars. Of course, the war-profits tax will be a diminishing amount in the fiscal year of 1920 as a means of raising revenue. Where then is the money coming from to meet the estimated expenses of \$10,000,000,000? Even if the present rates of taxation proposed in this bill are maintained at that rate, omitting, of course, the war-profits tax, it would only raise \$4,000,000,000 of the necessary ten billion. Consequently there must be a great increase in taxation or a continuation of this policy of borrowing billions upon billions of dollars long after the war is over. As it becomes increasingly difficult to borrow we must

give greater inducements to the purchasers of the bonds by raising the interest rate and exempting the bonds from taxation. These bonds are certain to soon find their way into the hands of the owners of great wealth, because their exemption from taxation makes them of far greater value to those of large incomes than to those with moderate incomes. The result must be that for years and generations to come a small and favored class will draw their tax-exempt incomes from the earnings of the poor.

I submit that this is an unjust system of war finance.

It secured its first victory when the first war-revenue bill was passed in 1917. The profiteers were allowed to escape at that time with a tax of less than 33 per cent.

England was then taxing war profits 80 per cent. She still imposes that tax on war profits.

This bill taxes corporations less than 50 per cent on their war profits.

It favors the rich and grinds the poor.

The war-tax bill of 1917 was the initial step. If we pass this bill as reported we shall, I submit, write into our statutes the consummation of a great wrong.

Respectfully submitted.

ROBERT M. LA FOLLETTE.

