
THE REVENUE BILL OF 1940

JUNE 10, 1940.—Committed to the Committee of the Whole House on the state of the Union and ordered to be printed

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

REPORT

[To accompany H. R. 10039]

The Committee on Ways and Means, to whom was referred the bill (H. R. 10039) to provide for the expenses of national preparedness by raising revenue and issuing bonds, to provide a method for paying for such bonds, and for other purposes, having considered the same, report favorably thereon without amendment and recommend that the bill do pass.

NEED FOR THE LEGISLATION

There is a growing concern regarding the state of our national defense. Recent developments in the European War have reminded us forcefully of the inadequacy of our means of defense against modern weapons of aggression. This need has been pointed out by the President upon several occasions; particularly, in his message to the Congress of May 16, 1940.

In this message, and in other requests, the President has requested defense funds for the fiscal year 1941 totaling \$3,250,000,000. This sum includes the amounts carried in the Budget for 1941, and the supplementary requests made since January 3, 1940, the date of the Budget message.

As outlined in the President's message of May 16, 1940, the four primary purposes for which the additional appropriations are to be used, are—

First. To procure the essential equipment of all kinds for a larger and thoroughly rounded-out Army;

Second. To replace or modernize all old Army and Navy equipment with the latest type of equipment;

Third. To increase production facilities for everything needed for the Army and Navy for national defense. We require the ability to turn out quickly infinitely greater supplies;

Fourth. To speed up to a 24-hour basis all new contracts to be awarded.

The urgent need for the speedy and effective undertaking and completion of this program cannot be doubted.

THE FISCAL SITUATION

The working balance of the Treasury is at present about \$1,300,000,000. The gross public debt is \$42,787,000,000, and the face amount of obligations which the Secretary of the Treasury may issue under the limitation of \$45,000,000,000 specified in section 21 of the Second Liberty Bond Act, as amended, is \$1,973,000,000.

The present deficit will be \$260,000,000 less on June 30, 1940, than was estimated on January 1, 1940. The national defense expenditures, including public works for the Army and Navy, were estimated in the Budget submitted to Congress last January, at \$1,940,000,000 and they are now estimated on the basis of the program submitted to the Congress up to and including June 10 at \$3,250,000,000.

These greatly increased necessary expenditures for national defense would, thus, result in the large deficit indicated, except for this tax bill which is designed to raise the revenue to pay for the national-defense program.

From these estimates it will be seen that it is highly desirable that Congress take some action at this session to provide the Treasury with the additional taxes levied in the bill and to provide it with the additional borrowing power set forth therein. This will give the Treasury that flexibility in its financing which so necessary for the effective management of the public finances in times like these and thus obviate the payment of higher interest rates.

THE FISCAL PROGRAM

Section 21 of the Second Liberty Bond Act, as amended, provides that the face amount of bonds, certificates of indebtedness, Treasury bills and notes issued under that act, as amended, shall not exceed \$45,000,000,000 outstanding at any one time. Section 302 of the bill amends this provision to permit the Treasury to issue, within the framework of current statutes relating to the public debt, \$4,000,000,000 of short-term public-debt obligations with maturities not exceeding 5 years, to be designated "National Defense Series". These obligations will be in addition to the \$45,000,000,000 face amount of securities authorized under existing law.

The tax increases provided under the bill are estimated to yield additional revenue of approximately \$1,004,000,000 for each full year of operation. The increased taxes may be divided into two categories. Those contained in title I are permanent in nature and will yield about \$322,000,000 annually. Those contained in title II are temporary in nature, being applicable only for the 5-year period, 1940-45, and will yield about \$682,000,000, annually.

The increased revenue attributable to title II, with certain minor exceptions, will be placed in a special fund which shall be available only for the retirement of the "National Defense Series" obligations. Because of the difficulty of segregating the additional revenue attributable to the permanent increases contained in title I, this amount cannot be earmarked for this special purpose. However, the total additional revenue attributable to both titles I and II is intended to

insure the retirement of these special obligations issued during the 5-year period for which the temporary taxes are to be effective.

STUDIES OF EXCESS-PROFITS TAXES AND SPECIAL AMORTIZATION

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

REVENUE ESTIMATES

The following table, prepared by the Treasury Department, shows the additional revenue under the taxing provisions of the bill:

Estimated additional revenue¹ attributable to the proposed Revenue Act of 1940²

<i>Source of revenue</i>		
Title I:		
Income tax:		<i>Millions of dollars</i>
Corporation income tax	-----	70
Individual income tax	-----	252
	Total increase, title I	322
Title II:		
Corporation super income tax	-----	135
Individual super income tax	-----	123
Capital stock and excess-profits taxes	-----	12
Estate tax	-----	29
Gift tax	-----	3
Alcoholic-beverage taxes:		
Distilled spirits	-----	76
Fermented malt liquors	-----	46
Other	-----	3
	Total increase, alcoholic-beverage taxes	125
Tobacco taxes:		
Cigarettes	-----	67
Other	-----	12
	Total increase, tobacco taxes	79
Stamp taxes	-----	7

¹ Excluding (a) the nonrecurring collections of floor taxes on alcoholic beverages and tobacco, estimated for fiscal year 1941 at \$26,000,000 and (b) revenues resulting from the extension of certain excise taxes as provided in title II, "Section 209. Continuation of Excise Taxes", but including the super-tax on such excise taxes.

² As introduced by Mr. Doughton, June 10, 1940.

prevent the rate in the higher brackets from being confiscatory, a cushion is inserted which prevents such increase from being greater than 10 percent of the net income in excess of the tax computed under existing law, as amended by title I. This cushion begins to operate where the tax so computed is in excess of 50 percent of the net income, which in the case of a married person is around \$200,000. The following examples will show the result of the operation of the tax and the cushion:

Net income	Tax under existing law as amended by title I	Super-tax	Net income	Tax under existing law as amended by title I	Super-tax
\$3,000.....	\$28	\$2.80	\$100,000.....	\$39,524	\$3,952.40
\$5,000.....	100	10.00	\$300,000.....	169,364	13,063.60
\$10,000.....	480	48.00	\$1,000,000.....	686,204	31,370.60

It will be seen from the above examples that in the case of a married man without dependents with \$5,000 net income, the supertax is determined by increasing the ordinary tax of \$100 by 10 percent, or \$10, making a total tax of \$110. The cushion will not operate in this case because the ordinary tax is not in excess of 50 percent of the net income. In the case of a married man with \$300,000 net income the 10 percent supertax if applied without the cushion, would amount to \$16,936.40, but since the ordinary tax is in excess of 50 percent of the net income the cushion applies. Accordingly, the supertax in this last example is computed by applying the 10 percent against \$130,636 (the amount of the net income less ordinary tax) instead of against the tax of \$169,364. This makes the supertax \$13,063.60 instead of \$16,936.40.

(2) EXCESS-PROFITS TAX

The amount of the excess-profits tax payable for any taxable year ending after June 30, 1940, and before July 1, 1945, is increased by 10 percent. Thus, a corporation with an excess-profits-tax year ending July 31, 1940, will be subject to the 10-percent increase. If the excess-profits tax payable is \$1,000, the supertax will be \$100, and the corporation will pay a total excess-profits tax of \$1,100.

(3) CAPITAL-STOCK TAX

The capital-stock tax is increased for the year ending June 30, 1940, and for the 4 succeeding years ending June 30, from \$1 per thousand of adjusted declared value to \$1.10 per thousand of adjusted declared value.

(4) ESTATE TAX

In the case of a decedent dying after the enactment of this bill and before the expiration of 5 years after such date, the estate tax payable (after application of the credits provided for State death taxes and Federal gift taxes), is increased by 10 percent.

(5) GIFT TAX

The gift tax is also increased by 10 percent, effective for the calendar year 1940 and subsequent calendar years up to and including the calendar year 1945.

For the calendar year 1940, the increase is in effect applied only to gifts made after the date of the enactment of this bill. This is accomplished by determining the gift tax for the entire year at the existing rates and adding thereto an amount which bears the same ratio to 10 percent of the tax so computed as the amount of gifts made after the enactment of the bill bears to the total amount of gifts made during the year.

(6) TRANSFERS TO AVOID INCOME TAX

Under the existing law, an excise is imposed upon the transfer of stock or securities by a citizen or resident of the United States, or by a domestic corporation or partnership, or by a trust which is not a foreign trust, to a foreign corporation as paid in surplus or as a contribution to capital. The rate under existing law is 25 percent and this has been increased to 27½ percent in the case of any transfer made during the period after the date of the enactment of this bill and before July 1, 1945.

(7) TOBACCO TAXES

The bill makes the following changes in the taxes on tobacco and tobacco products:

Tobacco, snuff, cigars, and cigarettes

Description of tax	Old rate	New rate	Percentage of increase
Snuff and snuff flour.....	18 cents.....	21 cents.....	16¾%
Tobacco, except chewing tobacco.....	do.....	do.....	16¾%
Cigars.....	75 cents.....	87½ cents.....	16¾%
Do.....	\$2.....	\$2.33½.....	16¾%
Do.....	\$3.....	\$3.50.....	16¾%
Do.....	\$5.....	\$5.83½.....	16¾%
Do.....	\$10.50.....	\$12.25.....	15¾%
Cigarettes.....	\$3.....	\$3.50.....	16¾%
Do.....	\$7.20.....	\$8.40.....	16¾%
Cigarette paper.....	¼ cent.....	½ cent.....	16¾%
Do.....	1 cent.....	1½ cents.....	16¾%

A floor-stocks tax is imposed upon all the products listed above to which the increased rates apply, with the exception of cigarette papers. This tax is equal to the difference between the old rate and the new rate and is imposed with respect to such products held by any person for sale otherwise than in retail stock. The tax on chewing tobacco was not increased, due to the declining consumption of this product and the small amount of revenue involved.

DISTILLED SPIRITS

Your committee increased the taxes on distilled spirits at the following rates:

Distilled spirits	Old rates	New rates	Percentage of increase
Distilled spirits generally.....	2.25	3.00	33¾%
Brandy.....	2.00	2.75	37½%
Imported perfumes.....	2.25	3.00	33¾%

(b) Title I of the bill also increases permanently the surtax rates with respect to taxable years beginning after December 31, 1939. The normal tax rate, which is 4 percent under existing law, is not changed in the bill. The following table shows the surtax rates under the existing law and under the bill:

TABLE I.—Comparison of surtax rates, existing law, and proposed bill

Amount of surtax net income		Existing law rate	Proposed bill rate	Amount of rate increase
Exceeding	Not exceeding			
		Percent	Percent	Percent
\$4,000	\$6,000	4	4	0
6,000	8,000	5	6	1
8,000	10,000	6	8	2
10,000	12,000	7	10	3
12,000	14,000	8	12	4
14,000	16,000	9	15	6
16,000	18,000	11	18	7
18,000	20,000	13	21	8
20,000	22,000	15	24	9
22,000	26,000	17	27	10
26,000	32,000	19	30	11
32,000	38,000	21	33	12
38,000	44,000	24	40	13
44,000	50,000	27	44	13
50,000	56,000	31	44	9
56,000	60,000	35	47	12
60,000	62,000	35	47	8
62,000	68,000	39	47	4
68,000	70,000	43	50	7
70,000	74,000	43	50	3
74,000	80,000	47	53	2
80,000	90,000	51	56	1
90,000	100,000	55	58	0
100,000	150,000	60	60	0
150,000	200,000	62	62	0
200,000	250,000	64	64	0
250,000	300,000	66	66	0
300,000	400,000	68	68	0
400,000	800,000	70	70	0
500,000	750,000	72	72	0
750,000	1,000,000	73	73	0
1,000,000	2,000,000	74	74	0
2,000,000	5,000,000	75	75	0
5,000,000 and up		75	75	0

(c) Total income-tax burden.—(1) Permanent increases: In order to secure a complete picture of the total income-tax burden, the following tables are included with respect to a married man with no dependents. Table II shows the increased normal and surtax rates on a married man with no dependents under existing law and under the bill. While there is no change in the normal tax rate over that of existing law, the normal tax itself is increased by reason of the lowering of the exemptions to \$800 for single persons and to \$2,000 for married persons.

TABLE II.—Comparison of normal and surtax, existing law and proposed bill, married person, no dependents, all income earned

Net income	Normal tax		Surtax		Surtax increase
	Present law	Proposed bill	Present law	Proposed bill	
\$2,000	0	0	0	0	0
\$2,500	0	\$10	0	0	0
\$3,000	\$8	28	0	0	0
\$4,000	44	64	0	0	0
\$5,000	80	100	0	0	0
\$6,000	116	136	0	0	0
\$7,000	152	172	\$20	\$40	\$20
\$8,000	188	208	60	80	20
\$9,000	224	244	105	140	35
\$10,000	260	280	155	200	45
\$11,000	296	316	210	280	70
\$12,000	332	352	270	360	90
\$13,000	368	388	335	460	125
\$14,000	404	424	405	560	155
\$15,000	444	464	480	680	200
\$20,000	644	664	645	1,460	815
\$25,000	844	864	1,645	2,830	985
\$30,000	1,044	1,064	2,525	4,040	1,515
\$40,000	1,444	1,464	4,535	7,220	2,685
\$50,000	1,844	1,864	7,025	10,980	3,955
\$60,000	2,244	2,264	10,985	15,300	5,215
\$70,000	2,644	2,664	13,805	19,940	6,135
\$80,000	3,044	3,064	18,225	24,880	6,655
\$90,000	3,444	3,464	23,225	30,120	6,895
\$100,000	3,844	3,864	28,625	35,600	7,035
\$150,000	5,844	5,864	57,550	64,020	7,070
\$200,000	7,844	7,864	87,500	94,580	7,080
\$250,000	9,844	9,864	118,460	125,540	7,090
\$300,000	11,844	11,864	150,400	157,500	7,100
\$400,000	15,844	15,864	216,350	223,460	7,110
\$500,000	19,844	19,864	284,300	291,420	7,120
\$750,000	29,844	29,864	459,250	460,380	7,130
\$1,000,000	39,844	39,864	639,200	640,340	7,140
\$2,000,000	79,844	79,864	1,369,175	1,370,320	7,145
\$5,000,000	199,844	199,864	3,589,150	3,590,300	7,150

It will be noted that a married person with a net income of \$2,500 pays no tax under existing law. However, under the bill he will pay a normal tax of \$10 for each taxable year beginning after December 31, 1939. The same person with a net income of \$3,000 will pay for each such taxable year a normal tax of \$28. No surtax is imposed either under the bill or under the existing law until the net income of a married man exceeds \$6,500 under the present law and \$6,000 under the bill. In the case of a single person, no surtax is imposed until the net income exceeds \$5,000 under the present law and \$4,800 under the bill. The largest increase in the surtax rate over existing law is with respect to married persons with net incomes between \$46,000 and \$58,000, where the rate is increased 13 percent. In the case of a single person, the largest increase is with respect to net incomes from \$45,000 to \$57,000, where the rate is also increased 13 percent.

(2) Temporary increase: In addition to the permanent increases caused by the change in the exemptions and the surtax rates, title II of the bill imposes a 10 percent supertax with respect to taxable years beginning after December 31, 1939 and before January 1, 1945. This is shown in the following table:

