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THE COMMITTEE STAFF

FOR THE

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LETTERS OF TRANSMITTAL

To the Members of the Joint Economic Committee:

Transmitted herewith for the use of the Joint Economic Committee and other Members of Congress is a staff report, "The Federal Tax System: Facts and Problems." This report, which is a revision of an earlier staff study, reflects the provisions of the Revenue Act of 1964.

PAUL H. DOUGLAS,
Chairman, Joint Economic Committee.

Hon. PAUL H. DOUGLAS,
Chairman, Joint Economic Committee,
U.S. Congress, Washington, D.C.

DEAR SENATOR DOUGLAS: Transmitted herewith is a staff report, "The Federal Tax System: Facts and Problems." The report provides a brief description of Federal tax law, as amended by the Revenue Act of 1964, and outlines in an objective manner the issues and arguments which have arisen over the various features of the law. The present report is a revision of materials originally prepared in 1955 and last revised in 1961.

The subcommittee appreciates the cooperation afforded its staff by the Federal executive departments and independent agencies and by individuals outside the Government. Materials in this report do not necessarily reflect the views of the subcommittee or of its individual members.

MARTHA W. GRIFFITHS,
Chairman, Subcommittee on Fiscal Policy.

Hon. MARTHA W. GRIFFITHS,
Chairman, Subcommittee on Fiscal Policy,
Joint Economic Committee,
U.S. Congress, Washington, D.C.

DEAR MRS. GRIFFITHS: Transmitted herewith is a staff report, "The Federal Tax System: Facts and Problems."

The report consists of information and statistics about the major elements of the Federal tax structure. Each section of the report presents a brief statement of present statutory provisons regarding a segment of that structure, supplemented in some cases by a short account of the legislative history of these provisions. In addition, each section contains a brief statement of major current issues in the related area of tax law and outlines the principal arguments advanced with respect to these issues in the light of recent changes and proposals. A final section of the report presents some of the most recent statistics which bear on the operation of the Federal tax system.

Every effort has been made to maintain complete objectivity in preparing this report. No attempt has been made to evaluate the various arguments offered on any side of the issues discussed. The purpose has been to provide as accurate, up-to-date a statement as possible of the issues and arguments, leaving appraisal of their validity to the reader.

This report is substantially a revision of materials originally prepared at the request of the Subcommittee on Tax Policy for its use in connection with the December 1955 hearings on Federal tax policy for economic growth and stability. Those materials were revised and reissued in 1959 and 1961 under the title, "The Federal Revenue System: Facts and Problems." Along with the fact that these earlier studies are out of print, occasion for this revision is necessitated by important changes in the Internal Revenue Code enacted since the revision in 1961, particularly those contained in the recently enacted Revenue Act of 1964.

The report was prepared by Dr. Alan P. Murray, staff economist for the Subcommittee on Fiscal Policy. Mr. Gregory Guroff of the committee staff provided assistance in the preparation of the statistical data. Grateful acknowledgment is made for the suggestions and comments of Mr. Norman B. Ture, Director of Tax Studies, National Bureau of Economic Research, who prepared the first three editions of this report while on the Joint Economic Committee staff. Valuable suggestions were also received from Dr. Joseph A. Pechman, Dr. Richard Goode, and Dr. Lawrence B. Krause of the Brookings Institution, and Dr. Arthur S. Fefferman, Director of Economic Analysis, American Life Convention.

The staff is also grateful for the assistance of those on the staff of the Joint Committee on Internal Revenue Taxation, those in the Office of Tax Analysis and the Tax Legislative Counsel of the Treasury Department, and those in other executive departments and independent agencies who reviewed the report for accuracy. The cooperation and assistance of the Statistics Division of the Internal Revenue Service and the Office of Tax Analysis of the Treasury Department in the collection of statistical material were, as on prior occasions, invaluable. This report, of course, does not necessarily reflect the views of those who rendered assistance.

JAMES W. KNOWLES,
Executive Director, Joint Economic Committee.

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CHAPTER 1

THE TAX STRUCTURE

The revenues of the Federal Government are derived from a wide array of sources which include the receipts of public enterprises such as the Post Office, the sale of Government assets, rents, dividends, fees, fines, royalties, and interest.[1] The prime source of Federal revenue is, however, the tax structure. The importance of Federal taxation has increased during the present century as a consequence of a rise in the level of Federal expenditures. The weight of Federal tax receipts, which in 1963 were equal to roughly 19 percent of the Nation's gross national product, has intensified debates over the composition of the tax structure and over provisions of the separate taxes within that structure. Issues of this nature, which exist apart from controversy over the proper level of Federal taxes, are discussed in this volume.

I. Characteristics of the Tax Structure

A. THE LEVEL OF FEDERAL TAX COLLECTIONS

1. *Concepts of measurement*

Federal taxes are measured in a variety of ways, no one of which is superior for all purposes. The conventional administrative budget covers Federal receipts said to be "owned" by the Government. It thus excludes receipts received by funds which are merely held in trust. The consolidated cash statement, the so-called cash budget, is designed to indicate the magnitude of the flow of financial transactions between the public and the Government. From the receipts standpoint the cash budget differs from the administrative budget chiefly in that it includes trust fund receipts, such as the taxes collected under the old-age, survivors, and disability insurance program. In both the administrative and cash budgets the receipts of public enterprises, such as the Post Office, are recorded on a net basis after the deduction of expenditures from gross receipts. Both budgets are presented on a fiscal-year basis.[2]

In the national income accounts, Federal receipts are examined from the standpoint of their impact on the flow of national income and output. Thus trust fund receipts are included and receipts are generally estimated on an accrual basis as opposed to the collections basis employed in the administrative and cash budgets.[3] Accrual account-

[1] In Federal budget accounting nontax revenues are often shown as net figures after the subtraction of related expenditures. These net totals appear on the expenditure side of the accounts. Conventional budget accounting then does not provide a measure of gross Federal receipts or expenditures. Gross receipts are estimated to have totaled $134 billion in fiscal 1963, and gross expenditures, $138 billion. For a discussion of the relation between gross receipts and standard budget totals see Roy E. Moor, "The Federal Budget as an Economic Document," Subcommittee on Economic Statistics of the Joint Economic Committee, joint committee print, 1962, ch. 4. For a discussion of gross expenditures of Government-administered funds in the fiscal years 1963, 1964, and 1965, see "The Budget of the U.S. Government, 1965," pp. 337-346.

[2] For a further description see the annual budget document.

[3] In addition, transfers involving the exchange of financial claims and exchanges of existing assets are excluded.

ing is employed in the national income accounts because it is judged that accruals rather than cash collections more accurately describe the economic impact of Government receipts. In regard to taxes, this adjustment affects primarily estimates of corporate income tax receipts, since collections currently lag accruals under this tax by 6 months or more. National income totals are available on both a calendar-year and fiscal-year basis.[4]

The Bureau of the Census compiles data on Federal tax receipts in connection with its periodic reports on governmental finances. The Bureau classifies Federal receipts in a manner that facilitates comparison with the receipts of States and localities. While the Bureau's concept of Federal tax receipts differs in some respects from the three concepts discussed previously, it most closely resembles the cash budget. Census Bureau figures are presented on a fiscal-year basis and are not generally available until sometime after the close of the fiscal year.[5]

Aggregate tax revenues are not explicitly separated from nontax revenues in the administrative and cash budgets, although receipts under the major taxes are identified. In the national income and Census Bureau presentations, on the other hand, tax revenues are distinguished from nontax revenues. Trust fund receipts are shown separately, however, and are not classified as either taxes or nontaxes. Federal tax receipts under the four definitions are presented in table 1 for the fiscal years 1963 and 1964.

TABLE 1.—*Federal receipts and tax receipts, four measures, 1963–64*

[Fiscal years; in billions of dollars]

Receipts classification	1963	1964 [4]
The administrative budget:		
Total receipts	86.4	89.4
Receipts, major specified taxes [1]	82.5	86.0
The consolidated cash budget:		
Total receipts	109.7	115.4
Receipts, major specified taxes [1] other than employment taxes	85.7	89.5
Employment taxes [2]	17.9	19.9
National income accounts:		
Total receipts	109.3	114.0
Tax receipts	87.2	(5)
Social insurance contributions [3]	20.9	(5)
Bureau of the Census:		
Revenue from own sources	[4] 114.5	(5)
Tax receipts	86.8	(5)
Insurance trust revenue [6]	16.4	(5)

[1] Individual and corporate income, excise, estate, and gift taxes, and customs duties.
[2] Includes contributions for the old-age and survivors, disability, and unemployment trust funds, the Railroad Retirement account, and deposits to the unemployment trust fund by the States.
[3] Includes contributions to funds listed in footnote 2 plus contributions to the Federal civilian retirement system and premiums paid for Government life insurance.
[4] Preliminary.
[5] Not available.
[6] Includes Federal unemployment compensation tax, exclusive of deposits by States, and contributions to old-age, survivors, and disability insurance, the Federal employee retirement fund, veterans' life insurance, and the railroad retirement fund.

Source: Bureau of the Budget, Office of Business Economics of the Department of Commerce, and the Bureau of the Census.

[4] For further information see the Department of Commerce, Office of Business Economics, the Survey of Current Business, and supplements.
[5] Detail on the Census Bureau concept is found in the Bureau's annual report on governmental finances.

2. Federal taxes and the economy

The Federal tax structure has a significant impact on the level of economic activity and occupies a dominant position in the Nation's system of Federal-State-local taxes. In 1963, Federal tax receipts, as identified in the national income accounts and including social insurance contributions, exceeded $100 billion and were equal to 19 percent of the value of the Nation's total output of goods and services. In dollar terms, Federal tax receipts have increased substantially relative to earlier levels, including those reached during World War II (when large amounts of revenue were raised through borrowing) and the Korean emergency. As a percentage of gross national product, Federal tax receipts in 1963 were at roughly the same level as those reached in the two defense emergencies.

While the Federal Government is but one of the jurisdictions that levies and collects taxes, its revenues are substantially greater than those of all other governments combined. For example, in fiscal 1962 the Federal share of the tax revenues of all governments, exclusive of employment tax receipts, was nearly twice as large as the share of State and local governments. This relation is essentially unchanged when trust fund receipts such as contributions for old-age, survivors, and disability insurance, Federal and State unemployment compensation, and railroad retirement benefits, are included.[6]

At the turn of the century, the Federal share of all government tax revenues was less than 40 percent. By 1913 this share had fallen to less than 30 percent. Federal tax revenues expanded rapidly as a result of World War I, then subsequently declined relative to State and local collections. In the mid-1930's Federal revenues once again began to rise in relation to State and local receipts. The high-water mark was reached in 1944, when Federal tax receipts comprised 82 percent of all the taxes collected. In recent years State and local tax collections have risen relative to Federal tax collections. Federal, State, and local tax collections in the years 1954 to 1963 and their relation to gross national product are shown in table 2.

[6] Bureau of the Census.

TABLE 2.—*Federal, State, and local tax collections, 1954–63, and their relation to gross national product*

Calendar year	Gross national product (billions)	Tax receipts [1]		Tax receipts as a percent of GNP	
		Federal (billions)	State-local (billions)	Federal (percent)	State-local (percent)
1954	$363.1	$63.2	$23.8	17.4	6.6
1955	397.5	72.1	26.1	18.1	6.6
1956	419.2	76.9	29.1	18.3	6.9
1957	442.8	81.0	31.4	18.3	7.1
1958	444.5	77.8	33.1	17.5	7.4
1959	482.7	89.4	36.1	18.5	7.5
1960	502.6	95.6	40.1	19.0	8.0
1961	518.7	97.4	42.8	18.8	8.2
1962	556.2	105.3	46.4	18.9	8.3
1963 [2]	583.9	112.7	49.7	19.3	8.5

[1] Includes personal tax receipts, corporate tax accruals, indirect business tax accruals, and contributions for social insurance, less refunds.

[2] The Revenue Act of 1964 reduced Federal tax liabilities at 1963 levels of income by an estimated $11,500,000,000. Such a reduction would have reduced 1963 Federal tax receipts to $101,200,000,000 or 17.3 percent of gross national product.

Source: Department of Commerce, Survey of Current Business.

Debate over a given tax or tax structure typically concerns conflicting opinions as to the equity of the distribution of tax liabilities and frequently gives rise to disputes over effects on resource allocation. Issues of this nature pervade controversy over the Federal tax structure and underlie many proposals for the revision of that structure. Current issues in tax policy are not limited to these traditional areas, however, but encompass as well broad problems of fiscal policy. Federal tax receipts are equivalent to such a significant portion of national income that the tax structure's contribution to the attainment of such goals as full employment, price level stability, satisfactory economic growth, and balance-of-payments equilibrium has inevitably become a matter of speculation. While a thorough exposition of issues of the latter type is outside the scope of this volume, a brief summary is appropriate since these issues, too, pervade debates over specific tax provisions and proposals.

Several characteristics of the Federal tax structure have received attention in discussions of the relation between that structure and the performance of the economy. Firstly, it has been pointed out that because of the progressive nature of the most important Federal taxes, tax revenues tend to increase at a more rapid rate than the Nation's economy expands. In the absence of discretionary changes in tax rates, therefore, Federal tax revenues tend to increase as a share of gross national product. This tendency is evident in table 2. Tax receipts increased from 17.4 percent of gross national product in 1954, and 18.1 percent in 1955, to 19.3 percent in 1963. Tax reductions carried out in 1964 will serve initially to reduce this percentage to roughly its 1954 level. The basic character of the tax structure remains unchanged, however, and the tendency for Federal tax receipts to increase in proportion to gross national product is expected to persist.

It is argued that the tendency for tax receipts to increase at a more rapid rate than gross national product may act to retard the progress of the economy unless it is offset by an increase in the level of Federal expenditures or corrected periodically through tax reduction. Controversy has arisen primarily over the selection of the proper policies needed to insure that Federal revenues do not become so burdensome as to serve as a check to economic expansion. Briefly, some observers argue that Federal revenues should be adjusted to regulate the level of aggregate demand in the economy in such a manner that actual Federal revenues and expenditures would balance only at full employment levels of activity. Others argue that economic growth would best be promoted by maintaining a tight rein over the level of Federal expenditures and adhering to a policy of matching revenues and expenditures, at least over the business cycle.

A second characteristic of the Federal tax structure which has stimulated recent discussion concerns the relatively heavy weight given to so-called direct taxes, such as income taxes, in contrast to indirect taxes, exemplified by sales taxes. Critics of the present distribution argue that if the system were revised to give more weight to indirect and less to direct taxes, its contribution to rapid economic growth would be enhanced as the result of favorable effects on the level of saving, investment, and individual effort. Those opposed to this proposal contend that its acceptance would make it more difficult to maintain full employment, the most important requisite to rapid growth. Moreover, it is contended that there would be a loss in tax equity as a result of such a revision which would outweigh any other benefits likely to be derived from it. These arguments are presented in greater detail in chapters 3 and 9.

It is generally recognized that the Federal tax structure tends to promote economic stability. This attribute stems from the fact that tax revenues respond automatically to changes in national income in a manner which tends to counteract such changes. In periods of recession the fall in tax revenues helps to maintain disposable incomes while in periods of inflation the increase in tax liabilities tends to check the growth of disposable incomes and thus dampen down inflationary pressures. There is relatively little disagreement over the desirability of this feature of the tax structure, but there is frequently some difference of opinion as to the rank which should be given to this attribute in the hierarchy of tax policy goals. Thus, for example, while a restructuring of tax rates and exemptions might serve to increase the tax structure's sensitivity to changes in income, such a revision would in all likelihood disturb the present distribution of tax liabilities and raise tax equity questions.

It is evident from table 2 that State and local tax revenues have been increasing in recent years relative to the revenues of the Federal tax system. The States and localities rely on types of taxes which differ markedly from those which produce the major share of Federal revenue. The changing relation between Federal and State-local tax systems adds an important dimension to current discussions over Federal tax policy. Broad questions of equity, resource allocation, economic growth, and stability concern the combined tax systems of all levels of government. Judgments concerning specific questions raised by Federal taxes, therefore, may be influenced by the character of State and local tax systems.

B. THE COMPOSITION OF THE FEDERAL TAX STRUCTURE

1. *Types of taxes*

Taxes on individual and corporate income are the mainstays of the Federal tax system. In combination, these taxes accounted for 67 percent of cash budget tax receipts in the fiscal year 1963. Despite the rate reductions enacted in 1964, these taxes will remain the largest revenue producers in the Federal tax structure.

Of the two taxes, the individual income tax produces roughly two times as much revenue as the corporate income tax. The relative importance of these taxes will not be substantially changed as a consequence of the Revenue Acts of 1962 and 1964. Individual and corporate tax liabilities were reduced approximately in proportion as a result of the combined revenue acts, apart from the relatively minor, transitional impact of the shift in the payment timetable required with respect to that portion of corporate liabilities expected to exceed $100,000.

After the income taxes, employment taxes and excise taxes are the most important sources of Federal tax revenue. Employment tax receipts accounted for 14 percent of 1963 cash budget tax receipts. Employment tax collections are credited to the various trust funds from which social security, railroad retirement, and unemployment compensation benefits are paid. Because of the existence of the trust fund arrangement, employment taxes are often viewed as distinct from other forms of tax. Nevertheless, a surplus of trust fund collections over disbursements, because it is invested in Government securities, is available to finance current Government expenditures. By the same token, a temporary excess of payments over collections, while paid from trust fund accounts through the redemption of Federal securities, must be financed from other current Federal receipts.

Federal old-age and survivors' insurance trust fund receipts, which include employee contributions withheld from wages, matching contributions by employers, and tax payments by the self-employed, comprise the greatest part of Federal employment tax receipts. Other employment taxes include those levied to support the disability insurance trust fund, the railroad retirement account, and the unemployment trust fund.[7] Contributions for the latter are divided between the States and the Federal Government. Since State unemployment tax collections are deposited with the Federal Government until drawn to finance unemployment compensation benefits, they are listed as receipts in the cash budget. Increases in the contribution rates under the old-age, survivors, and disability insurance program and the Railroad Retirement Act scheduled for 1966 and 1968 will increase the relative importance of employment tax collections.

Federal excise taxes accounted for 13 percent of cash budget tax receipts in 1963. While excises are levied on a wide variety of specific items, the taxes on alcohol and tobacco products, gasoline, and automobiles, trucks, automobile parts, tires, and tubes are responsible for more than 75 percent of excise tax revenues.

Estate and gift taxes and customs duties are relatively minor contributors of Federal tax revenue. The estate tax, which affects only a small percentage of the estates transferred each year, provides roughly 2 percent of cash budget tax receipts. Customs duties, which provided the major share of Federal revenue throughout the 19th century, are currently the least important source of Federal tax revenue.

[7] In addition, contributions to the Federal Government retirement system and veterans' life insurance premiums are classed as trust receipts.

The distribution of tax receipts by type of tax under the administrative, cash, and national income accounts budget classifications is presented in table 3 for the fiscal year 1963.

TABLE 3.—*Distribution of tax receipts by type of tax under administrative, consolidated cash, and national income budgets, fiscal year 1963*

Type of tax	Administrative budget	Consolidated cash budget	National income accounts budget
	Billions	*Billions*	*Billions*
Individual income taxes	$47.6	$47.6	$47.4
Corporation income taxes	21.6	21.6	21.6
Employment taxes		14.9	15.5
Unemployment tax deposits by States		3.0	3.0
Excise taxes	9.9	13.2	13.2
Estate and gift taxes	2.2	2.2	2.2
Customs duties	1.2	1.2	1.3
Other taxes [1]			3.9
Total	82.5	103.7	108.1
	Percentage distribution		
Individual income taxes	57.7	45.9	43.8
Corporation income taxes	26.2	20.8	20.0
Employment taxes		14.4	14.3
Unemployment tax deposits by States		2.9	2.8
Excise taxes	12.0	12.7	12.2
Estate and gift taxes	2.7	2.1	2.0
Customs duties	1.5	1.2	1.2
Other taxes [1]			3.6
Total	100.0	100.0	100.0

[1] Includes employee and employer contributions to the Federal retirement system, veterans life insurance premiums, and miscellaneous taxes.

Source: Bureau of the Budget and the Department of Commerce.

2. The distribution between direct and indirect taxes: The United States and eight foreign countries [8]

The distinction between a "direct" tax and an "indirect" tax raises conceptual difficulties in many instances, but is nonetheless often made. In recent years the distinction has been the subject of renewed interest because of discussions involving the relative merits of tax structures weighted more heavily with direct or indirect taxes.[9]

Indirect taxes are generally regarded as those incurred as the result of consumption, while direct taxes are considered to be those based upon income or wealth. Commonly accepted examples of indirect taxes are excises and customs duties, while examples of direct taxes are the individual and corporate income taxes. More controversial is the classification of property and social security taxes. A 1964 Treasury Department survey classifies property taxes and employer contributions to social security programs as indirect taxes and employee contributions to social security programs as direct taxes.[10] On this basis, the Federal Government derived 79 percent of its 1961 tax revenue from direct taxes.

[8] Much of this discussion is based upon J. A. Stockfisch, U.S. Treasury Department, "International Comparisons on Direct and Indirect Taxes," Excise Tax Compendium, Compendium of Papers on Excise Tax Structure submitted to the Committee on Ways and Means, 1964, pt. I (hereinafter referred to as Excise Tax Compendium) pp. 109–181.

[9] For discussion of these issues see ch. 3, "Corporate Income Taxation" and ch. 9, "Federal Excise Taxation."

[10] J. A. Stockfisch, op. cit., pp. 110-113.

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In evaluating the economic significance of this distribution, a number of additional considerations are relevant. The Federal Government's reliance on income taxes is partially offset by the predominance of sales and property taxes in the tax structures of the States and localities. In the Nation as a whole, direct taxes accounted for 57 percent of fiscal 1961 tax receipts. The distribution of tax revenues of Federal, State, and local governments by types of tax is shown in table 4 for 1961.

TABLE 4.—*Federal, State, and local government tax revenues by source, 1961* [1]

[In millions of dollars]

	Federal	State	Local	Total
Direct taxes:				
Individual income tax	41,338	2,355	258	43,951
Corporation income tax	20,954	1,266		22,220
Death and gift taxes	1,896	501		2,397
Social insurance contributions of employees [2]	7,886	1,261		9,147
Insurance premium taxes		585		585
Total direct taxes	72,074	5,968	258	78,300
Indirect taxes: Excise taxes, sales taxes, and customs duties:				
Excises: [3]				
Alcoholic beverages	3,192	688	25	3,905
Tobacco products	1,978	1,001	76	3,055
Manufacturers' excises (excluding gasoline)	2,510			2,510
Retailers' excises	396			396
Miscellaneous excises (telephone, telegraph, admissions)	1,489			1,489
Severance taxes [4]		451		451
Motor fuels	2,355	3,431	34	5,820
Public utilities		401	298	699
License taxes		2,624	113	2,737
Liquor store revenues		1,260		1,260
Other		416	78	494
Total excises	11,920	10,272	624	22,816
General sales tax		4,510	921	5,431
Total excises and general sales tax	11,920	14,782	1,545	28,247
Customs duties	1,008			1,008
Total excises, sales taxes, and customs duties	12,928	14,782	1,545	29,255
Property taxes		631	17,370	18,001
Other taxes		197	631	828
Social insurance contributions of private employers [2]	6,061	4,184		10,245
Total indirect taxes	18,989	19,794	19,546	58,329
Total all taxes	91,063	25,762	19,804	136,629

[1] Fiscal year ended June 30, 1961, for Federal Government and all but 4 of the State governments. A considerable number of local governments operate in terms of a fiscal year ending Dec. 31.

[2] Estimated by the International Social Security Branch, Division of Research and Statistics, Department of Health, Education, and Welfare, Social Security Administration.

[3] Federal excises from Annual Report of the Secretary of the Treasury, tables 4 and 19, adjusted for refunds. State and local government excises from Governmental Finances in 1961, U.S. Department of Commerce.

[4] Taxes imposed distinctively on removal of natural products; e.g., oil, gas, minerals, timber, etc., and measured by value or quantity of products removed or sold.

Source: Compiled by Treasury Department, Office of Tax Analysis, from Annual Report of the Secretary of the Treasury, fiscal year ended June 30, 1962, tables 4 and 19; Governmental Finances in 1961, U.S. Department of Commerce, Bureau of Census, Oct. 26, 1962; Detail of State Tax Collections in 1963, U.S. Department of Commerce, Bureau of Census, November 1963; Compendium of State Government Finances in 1961, U.S. Department of Commerce, Bureau of Census, 1962.

Compared with other industrialized countries, and considering all levels of government combined, the United States is among those nations which rely to a relatively large extent on direct as opposed to indirect taxes. Among eight foreign countries examined by the Treasury Department in 1964, Italy and France were shown to have collected less than 30 percent of their 1961 tax revenues from direct taxes and Canada 43 percent, as compared to 57 percent for the United States. In Germany, Japan, and the United Kingdom, direct taxes composed 50 percent or more of the total yield, and in the Netherlands and Sweden the direct tax percentage exceeded that of the United States.

The division of revenue yield between direct and indirect taxes may have little significance of itself if overall tax burdens are low. To take the level as well as the type of tax into account, it is useful to express tax revenues as a percent of some measure of economic activity. Considered in relation to gross national product, the level of direct taxes in the United States, 15.3 percent of GNP in 1961, was higher than corresponding levels in Canada, France, Italy, and Japan, but lower than in West Germany, the Netherlands and Sweden, and roughly equal to that of the United Kingdom. The overall level of taxes, both direct and indirect, as a percent of GNP was lower in the United States than in all but two of the countries studied, Japan and Canada. Relative tax levels varied from 20.8 percent of GNP in Japan to 34.9 percent of GNP in Germany. The United States occupied an intermediate position in the range with a tax to GNP ratio of 26.8 percent. Six of the other eight nations had ratios exceeding 30 percent. These relationships are summarized in table 5.

TABLE 5.—*Direct and indirect taxes of nine countries related to gross national product and total tax yield, 1961* [1]

	United States		Canada		France		Germany		Italy	
	Percent of yield	Percent of GNP	Percent of yield	Percent of GNP	Percent of yield	Percent of GNP	Percent of yield	Percent of GNP	Percent of yield	Percent of GNP
Direct taxes:										
Individual income tax	32.2	8.6	19.5	5.0	14.7	4.8	19.7	6.9	11.3	3.4
Corporate income tax	16.3	4.4	16.1	4.1	6.0	2.0	6.9	2.4	2.1	.6
Death and gift taxes	1.8	.5	1.5	.4	.7	.2	.2	.1	.7	.2
Social insurance contributions of employees	6.7	1.8	4.9	1.3	6.9	2.3	13.5	4.7	6.3	1.9
Net wealth tax	------	------	------	------	------	------	1.3	.5	1.4	.4
Taxes on investment income	------	------	------	------	1.1	.4	.9	.3	------	------
Taxes on land and buildings	------	------	------	------	------	------	------	------	2.0	.6
Municipal trade tax	------	------	------	------	------	------	7.5	2.6	------	------
Other direct taxes	.4	.1	1.2	.3	.4	.1	------	------	1.5	.5
Total, direct taxes	57.3	15.3	43.2	11.1	29.8	9.7	50.1	17.5	25.2	7.6
Indirect taxes: Excise taxes, sales taxes, and customs duties:										
Excises:										
Alcoholic beverages (spirits, wine, beer, etc.)	3.8	1.0	2.2	.6	1.8	.6	1.7	.6	.6	.2
Tobacco products and matches	2.2	.6	4.1	1.1	2.3	.8	3.6	1.3	6.8	2.1
Manufacturers' excises	1.8	.5	.2	.1	------	------	1.6	.5	.9	.3
Retailers' excises	.3	.1	------	------	------	------	------	------	------	------
Motor fuels (mineral oils, gasoline, hydrocarbon, etc.)	4.3	1.1	4.2	1.1	------	------	3.1	1.1	7.2	2.2
Public utilities (gas and electrical energy)	.5	.1	------	------	------	------	------	------	.4	.1
Radio, television, phonographs, etc	------	------	.1	(2)	------	------	------	------	.7	.2
Stamp duties, registration and transfer taxes, etc	2.0	.5	5.8	1.5	3.8	1.2	1.0	.3	5.4	1.6
Coffee, tea, and cocoa	------	------	------	------	.2	.1	.7	.2	.8	.2
Sugar	------	------	------	------	------	------	.2	.1	1.0	.3
Betting and gambling enterprises	------	------	------	------	------	------	.3	.2	1.4	.4
Admissions, entertainment and amusements	------	------	1.3	.3	------	------	------	------	------	------
Other	1.8	.5	.3	.1	2.9	1.0	1.3	.5	.9	.3
Total, excises	16.7	4.5	18.4	4.7	11.1	3.6	13.3	4.6	26.1	7.9

General sales taxes	4.0	1.1	14.3	3.7	25.0	8.1	16.5	5.8	16.7	5.1
Total excises and general sales taxes	20.7	5.5	32.6	8.4	36.1	11.8	29.8	10.4	42.8	13.0
Customs duties	.7	.2	5.6	1.5	8.7	2.8	2.9	1.0	3.7	1.1
Total excises, sales taxes, and customs duties	21.4	5.7	38.3	9.9	44.8	14.6	32.7	11.4	46.6	14.1
Property taxes	13.2	3.5	14.2	3.6	1.0	.3	1.6	.6	----------	----------
Social insurance contributions of private employers	7.5	2.0	4.1	1.1	19.3	6.3	13.7	4.8	27.1	8.2
Other indirect taxes	.6	.2	.3	.1	5.1	1.7	1.9	.7	1.2	.4
Total, indirect taxes	42.7	11.4	56.8	14.6	70.2	22.9	49.9	17.4	74.8	22.7
Total, all taxes	100.0	26.8	100.0	25.8	100.0	32.6	100.0	34.9	100.0	30.3

Footnotes at end of table, p. 13.

TABLE 5.—*Direct and indirect taxes of nine countries related to gross national product and total tax yield, 1961* [1]—Continued

	Japan		Netherlands		Sweden		United Kingdom	
	Percent of yield	Percent of GNP	Percent of yield	Percent of GNP	Percent of yield	Percent of GNP	Percent of yield	Percent of GNP
Direct taxes:								
Individual income tax	20.3	4.2	27.4	8.9	52.8	17.9	35.5	10.9
Corporation income tax	26.8	5.6	10.4	3.4			4.0	1.2
Death and gift taxes	.5	.1	1.2	.4	.5	.2	3.2	1.0
Social insurance contributions of employees	6.4	1.3	16.2	5.2	7.4	2.5	7.3	2.3
Net wealth tax			1.2	.4				
Taxes on investment income			.9	.3	[2]			
Taxes on land and buildings			1.9	.6				
Municipal trade tax								
Other direct taxes	[2]	[2]	.2	.1	.4	.1	[2]	[2]
Total, direct taxes	54.0	11.2	59.3	19.2	61.2	20.7	50.0	15.4
Indirect taxes: Excise taxes, sales taxes, and customs duties:								
Excises:								
Alcoholic beverages (spirits, wine, beer, etc.)	8.3	1.7	1.6	.5	6.7	2.3	5.3	1.6
Tobacco products and matches	6.5	1.4	3.6	1.2	4.1	1.4	10.5	3.2
Manufacturers' excises	3.7	.7	1.2	.4	.9	.3	1.7	.5
Retailers' excises								
Motor fuels (mineral oils, gasoline, hydrocarbon, etc.)	4.6	1.0			3.3	1.1	6.1	1.9
Public utilities (gas and electrical energy) radio, television, phonographs, etc.	1.3	.3			2.3	.8		
Stamp duties, registration and transfer taxes, etc.	2.0	.4	1.6	.5	2.4	.8	1.6	.5
Coffee, tea, and cocoa					.1	[2]		
Sugar	.9	.2	.6	.2				
Betting and gambling enterprises							.5	.1
Admissions, entertainment and amusements	.5	.1	.2	.1	.2	.1	.1	[2]
Other	1.4	.3			1.8	.6	.6	.2
Total, excises	29.2	6.1	8.9	2.9	21.8	7.4	26.5	8.1

General sales taxes			13.1	4.3	8.3	2.8	6.3	1.9
Total excises and general sales taxes	29.2	6.1	22.0	7.1	30.1	10.2	32.8	10.1
Customs duties	3.9	.8	7.3	2.4	3.7	1.2	1.8	.6
Total excises, sales taxes, and customs duties	33.1	6.9	29.3	9.5	33.8	11.4	34.6	10.6
Property taxes	5.7	1.2	.5	.2			9.5	2.9
Social insurance contributions of private employers	6.0	1.3	10.9	3.5	4.9	1.7	5.9	1.8
Other indirect taxes	1.2	.3			.2	.1		
Total indirect taxes	46.0	9.6	40.7	13.2	38.8	13.1	50.0	15.3
Total, all taxes	100.0	20.8	100.0	32.4	100.0	33.8	100.0	30.7

[1] Percentages based on GNP totals adjusted to conform to fiscal periods wherever necessary.
[2] Less than 0.05 percent.

Source: Treasury Department, Office of Tax Analysis.

II. Historical Development

The present composition of the Federal tax system represents a relatively recent development in the fiscal history of the Federal Government. Indicative of this is the fact that customs duties, which today account for only 1 percent of total Federal tax revenues, accounted for more revenue than all other Federal taxes combined in most of the years between the founding of the Republic and the start of the First World War.

The growth in Federal tax revenues has been the product of the addition of new taxes to the Federal tax structure, increases in the effective rates of these taxes, and the growth of the economy. To a large extent new taxes have been added to the Federal tax structure and rates under existing taxes raised in response to the fiscal requirements of national defense emergencies. The principal exception to this rule occurred in the depression decade of the 1930's. Economic growth has been largely responsible for increases in Federal tax receipts in times of peace.

Prior to the Civil War customs duties were nearly the exclusive source of Federal tax revenue. Excise taxes were imposed during two periods, however, from 1791–1802 and during the emergency surrounding the War of 1812. No income tax was levied until the Civil War period.

The Nation's first income tax was enacted on August 5, 1861. Before the collection machinery was set up, however, this act was superseded by the act passed on July 1, 1862. Thus the first income tax revenues were collected under the 1862 act. This tax was subsequently revised in response to the changing revenue needs of the Federal Government; it was allowed to expire in 1872. During the period 1863–73 a total of $376 million was collected from the tax (with small amounts collected also in 1874 and 1876). The largest amount collected in any one year was the $73 million collected in 1866, which equaled about 15 percent of total Federal taxes that year.

During the Civil War excise taxes were revived and an inheritance tax was introduced. The excises were imposed on a long list of commodities, including alcoholic beverages and tobacco. During the postwar period most of the excises and the inheritance tax were repealed. The taxes on alcoholic beverages and tobacco were continued, however, and steadily increased in importance.

In 1894 a second income tax law was enacted, which was declared unconstitutional in 1895. In the short time in which the tax was in effect, some $77,000 was collected under it.

New miscellaneous excise taxes and an inheritance tax were levied to help finance the Spanish-American War. The excises were largely repealed by 1902. The inheritance tax, which yielded little revenue, was repealed a few years later.

In 1909 a corporate excise tax was levied on the net income of corporations. Ratification of the 16th amendment in 1913 paved the way for the introduction of the modern income tax. A tax which applied to both corporations and individuals was enacted as an amendment to the Tariff Act of 1913. It superseded the 1909 Corporate Excise Tax Act and provided for a tax at progressive rates on the income of individuals.

The income tax achieved sudden revenue importance during the period of the First World War. The traditional 19th century revenue sources were inadequate to finance the greatly expanded Federal defense and war expenditure needs of the period. The maximum rate of the individual income tax, which was 7 percent in the years 1913–15, was increased to 77 percent by 1918. The corporate income tax rate also rose sharply during the war, rising from an initial level of 1 percent in 1913–15 to 12 percent by 1918. Income taxes thus rapidly became the most significant source of Federal revenue. By 1917 income tax collections surpassed customs revenues and by 1920 accounted for about two-thirds of total Federal tax revenues.

Additional wartime revenues were derived from newly imposed estate, capital stock, and excess profits taxes.

During the prosperous decade of the 1920's, four tax reduction acts were enacted. The corporate income tax rate was slightly higher at the end of the decade than at the beginning, but corporate tax burdens were reduced as a result of an increase in the surtax exemption and the repeal of the wartime excess profits and capital stock taxes. Although annual income tax receipts during the decade were below the 1920 level, they represented the major part of total tax receipts.

During this decade most of the excise taxes were either repealed or greatly reduced. The only important excise tax in existence at the end of the decade was the tax on tobacco. The alcoholic beverage tax, which produced nearly a half billion dollars of revenue in 1919, remained in effect, but produced little revenue during the period of prohibition.

In an attempt to maintain Federal revenues in the 1930's in the face of falling income levels, the rates of various existing taxes were increased and some new taxes were imposed. In spite of income tax rate increases and lower personal exemptions, revenues from these taxes fell both absolutely and as a share of total tax collections during the decade. Income tax revenues declined from a level of \$2.4 billion in 1930—which represented about two-thirds of total tax revenues—to less than \$750 million by 1933. In 1940 they amounted to about \$2.1 billion, less than two-fifths of tax revenues.

Federal tax receipts rose in the latter half of the decade and by 1940 had reached \$5.7 billion or about \$2 billion more than the 1930 level. A significant part of the increase was due to increased excise tax revenues, particularly, following the repeal of prohibition, from the tax on alcoholic beverages. Estate tax (imposed in 1916) and gift tax (imposed in 1932) revenues increased substantially, reaching their peak revenue importance during this decade. They accounted for nearly 10 percent of total tax revenues in several years. A capital stock tax and a supplementary declared value excess profits tax were imposed. And in the late 1930's employment taxes were introduced to finance the old-age social security, unemployment insurance, and railroad retirement programs. During this decade several short-lived taxes were also imposed under the undistributed profits and agricultural adjustment acts.

Under the pressure of increased demands for additional revenues to finance World War II programs, the overriding importance of the individual and corporate income taxes in the Federal structure was established. Sharp increases in tax rates, reductions in personal exemptions, and the introduction of the excess profits tax coincided with a rapid expansion of income and profits to raise income (and profits) tax revenues from a 1940 level of $2 billion to over $35 billion in 1945.

The individual income tax, which had applied to only a small percentage of the population prior to the 1940's, was broadened to cover most of the working population. The withholding system was introduced to facilitate payment and collection. In the years 1944–45 individual income rates ranged from 23 to 94 percent—a historic high.

Major tax reductions were enacted in 1945 and 1948. The 1945 act reduced individual income tax rates, repealed the excess profits tax, capital stock and declared value excess profits taxes, and reduced corporate income taxes slightly. The 1948 act reduced individual rates further and introduced the split income provision. By 1950 income (and profits) tax revenues had declined to $28 billion from the $35 billion level of 1945.

Faced with the problem of financing the Korean emergency, Congress enacted three major revenue acts between September 1950 and October 1951. As a result of these acts, individual and corporate income tax rates were increased and an excess profits tax was reimposed. By 1953 income (and profits) tax revenues amounted to $54 billion.

In 1954, individual income tax rates were reduced to the levels existing prior to the Revenue Act of 1951, and the excess profits tax was allowed to expire. An excise tax reduction act was also enacted.

Major income tax reductions were next provided in the Revenue Act of 1964. Individual income tax rates, which ranged between 20 and 91 percent, were reduced to a range of 16 to 77 percent, effective in 1964, and to 14 to 70 percent in 1965 when the reductions will be fully effective. Corporate tax rates, which were 30 percent on the first $25,000 of taxable income and 52 percent on taxable income over $25,000, were reduced to 22 and 50 percent, respectively, in 1964, and to 22 and 48 percent in 1965.

CHAPTER 2

THE INDIVIDUAL INCOME TAX

I. Present Law

A. THE DETERMINATION OF TAXABLE INCOME

In the statutory sense, there are three principal categories of adjustments made in determining the amount of a taxpayer's income on which tax liability accrues. These are the adjustments which (1) exclude certain types of personal receipts from the taxpayer's gross income, (2) provide deductions from gross income for certain expenses, typically trade and business expenses, in determining adjusted gross income, and (3) provide for the deduction from adjusted gross income of certain other expenses, typically nonbusiness expense items (including the deduction for personal exemptions), in arriving at taxable income.

1. Exclusions from gross income

The Internal Revenue Code of 1954 defines "gross income" as "* * * all income from whatever source derived. * * *"[1] Notwithstanding this all-inclusive statutory concept, specific exemptions have been made, in the statute, by court decision, and by administrative ruling, to exclude a wide range of personal receipts. The major income items explicitly excluded from gross income are:

(*a*) Government transfer payments, death benefits, compensation for injury, etc.:

Social Security Act benefits, unemployment compensation,[2] and relief payments.

Railroad Retirement Act payments.[3]

Veterans' pensions (exclusive of retirement pay based on age or length of service).[4]

Workmen's compensation, damages for injury or illness, payments from accident and health insurance.[5]

Employer-financed payments in lieu of wages during periods of injury or sickness (i) up to $75 a week, subject to certain limitations, during the first 30 days of continuous absence if "sick pay" is 75 percent or less of regular weekly pay, and (ii) up to $100 a week after 30 continuous days of absence.[6]

Life insurance payments made by reason of death.[7]

Death benefits, up to $5,000, paid by an employer to an employee's beneficiary by reason of the death of the employee.[8]

[1] Sec. 61(a). All footnote citations of sections and of chapters when accompanied by a chapter title refer to the Internal Revenue Code of 1954 unless explicitly noted to the contrary.

[2] IT 3194, 1938-1 CB 114, IT 3447, 1941-1 CB 191, IT 3229, 1938-2 CB 136 in the case of Social Security Act benefits and IT 3230, 1938-2 CB 136, Rev. Rul. 56-652, 1955-2 CB 21 in the case of unemployment compensation.

[3] Sec. 12, Railroad Retirement Act of 1937 (50 Stat. 307), IT 3662, 1944 CB 72.

[4] Sec. 1001, Public Law 85-56, 85th Cong.

[5] Sec. 104.

[6] Sec. 105.

[7] Sec. 101(a).

[8] Sec. 101(b).

Employer contributions to qualified employee pension, annuity, accident, or health plans.[9]

Premiums paid on behalf of employees by an employer for up to $50,000 of group term life insurance coverage.[10]

(b) Other employee benefits:

Meals or lodging furnished on premises by and for convenience of employer.[11]

Rental value of dwelling or rental allowance of clergyman.[12]

Subsistence and rental allowance of members of the Armed Forces.[13]

Combat and mustering-out pay of members of the Armed Forces.[14]

Reimbursed moving expenses of existing employees.[15]

(c) Other:

Gifts and inheritances.[16]

Scholarship and fellowship grants (subject to limitations).[17]

Interest paid on obligations issued by State and local governments.[18]

Income earned abroad, up to $20,000 for a taxpayer living abroad for 17 out of 18 months and $25,000 for a bona fide resident abroad for 3 years or more.[19]

Income from discharge of indebtedness incurred in connection with property used in trade or business.[20]

Recovery of previously deducted bad debts, prior taxes, etc., when deduction did not result in tax benefit.[21]

Improvements by lessee on lessor's property (unless made in lieu of rent).[22]

Dividends received from domestic corporations, up to $100 per year per taxpayer.[23]

Any gain attributable to the first $20,000 of the sales price of a personal residence in the case of an individual aged 65 or over who owned and lived in the residence for at least 5 of the 8 years preceding the sale.[24]

In addition, certain types of income, particularly certain types of income in kind, while not explicitly excluded from gross income have never been construed in practice as included in this concept. Chief among these are the rental value of owner-occupied residences and certain types of goods and services produced for consumption by the taxpayer and his family; e.g., farm produce and merchandise inventory items.

Many of the items excluded from the statutory concept of gross income represent sizable amounts of personal income. For example, total imputed net rental income from owner-occupied houses in 1962 was estimated by the Department of Commerce at $6.9 billion, while

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9 Secs. 106, 402, and 403.
10 Sec. 79.
11 Sec. 119.
12 Sec. 107.
13 *Clifford Jones* v. *United States*, 60 Court of Claims 552 (1 USTC, par. 129).
14 Secs. 112, 113.
15 Rev. Rul. 54-429, 1954-2 CB 53.
16 Sec. 102.
17 Sec. 117.
18 Sec. 103.
19 Sec. 911. See ch. 8, "Taxation of Income from Foreign Sources."
20 Sec. 108.
21 Sec. 111.
22 Sec. 109.
23 Sec. 116.
24 Sec. 121.

food and fuel produced and consumed on farms was valued at $1.1 billion.[25] Federal Government transfer payments, including benefits from social insurance funds, military pensions, and veterans benefits amounted to $26.7 billion. Tax exempt interest totaled an estimated $900 million. In the aggregate, exclusions from gross income are estimated at $78 billion in 1962. This estimate includes those items of personal income, as defined by the Department of Commerce, which are deductible from gross income but does not include transfers of wealth by gift or inheritance.

2. Deductions from gross income

Gross income less certain deductions, which consist primarily of expenses connected with a trade or business and the excluded portion of long-term capital gains, determine adjusted gross income. Deductions from gross income include: [26]

All "ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business," except in the performance of services as an employee.[27] Examples are wages and salaries, depreciation, depletion, taxes, interest.

In the case of employees, expenses incurred on behalf of an employer (1) as an outside salesman, (2) for travel while away from home, (3) for transportation, and (4) for which he is reimbursed.

One-half of the excess of net long-term capital gains over net short-term capital losses.

Net losses realized from the sale or exchange of capital assets used in the production of income, up to $1,000.[28] Net losses in excess of $1,000 may be carried over to future years until exhausted.[29]

Expenses attributable to the production of rent and royalty income.

Certain deductions of life tenants and income beneficiaries of property.

Allowable deductions of self-employed individuals for pension, profit sharing, annuity, and bond purchase plans.[30]

Moving expenses incurred by new or continuing employees in connection with a change in job location, subject to certain limits and conditions.[31]

3. Deductions from adjusted gross income

The following expenses, generally of a nonbusiness or personal nature, may be deducted from adjusted gross income if itemized by the taxpayer:

(*a*) Interest on indebtedness, with certain exceptions relating to amounts paid in connection with insurance, endowment, or annuity contracts, tax-exempt income, carrying charges chargeable to capital accounts, and transactions between related taxpayers.[32]

[25] Department of Commerce, Survey of Current Business, July 1963, p. 39.
[26] Unless otherwise noted, these deductions are found in sec. 62.
[27] Sec. 162(a).
[28] Sec. 1211.
[29] Sec. 1212.
[30] Secs. 401(c)(1), 404, 405(c).
[31] Sec. 217.
[32] Sec. 163.

(*b*) The following taxes paid: State and local personal property, real property, income, war profits, excess profits, general sales, and gasoline taxes, and foreign real property, income, war profits, and excess profits taxes.[33] Prior to 1964 State and local taxes on tobacco products, alcoholic beverages, admissions, and occupancy were also deductible under certain conditions, as were poll taxes and auto license and driver registration fees.

(*c*) An amount equal to the excess over $100 of each loss due to fire, theft, or other casualty to the extent not compensated by insurance.[34]

(*d*) Contributions to certain nonprofit institutions, such as religious, educational, scientific, and charitable organizations.[35] In general, the deduction may not exceed 20 percent of adjusted gross income plus an additional amount, not to exceed 10 percent of adjusted gross income, for donations to charitable organizations which normally receive a substantial portion of their support from the general public or a governmental institution. If contributions to organizations of the latter type exceed 30 percent of adjusted gross income in any one year, however, they may be carried forward by the taxpayer for as many as 5 years.

A taxpayer may deduct without limit contributions to publicly supported charitable organizations and certain "operating" and "conduit" private foundations if such contributions and his income tax payments in the taxable year and 8 out of the last 10 taxable years have equaled 90 percent of his taxable income computed without regard to personal exemptions, operating loss carryovers, or deductible contributions.[36]

(*e*) Certain expenses associated with the taxpayer's occupation as an employee such as union dues, professional association membership fees and journal subscriptions, uniforms and other types of special work apparel, and educational expenses incurred to maintain or improve skills required in the taxpayer's employment, trade or business, or to meet the requirements of the taxpayer's employer.[37]

(*f*) Medical expenses incurred on behalf of the taxpayer, his wife, and dependents, if not reimbursed by insurance, to the extent such expenses exceed 3 percent of his adjusted gross income.[38] In computing medical expenses, outlays for drugs and medicines can be included only to the extent they exceed 1 percent of adjusted gross income. Neither the 3- nor the 1-percent limit applies to expenses incurred for the taxpayer or his spouse if either is 65 or over or to expenses for a dependent parent of the taxpayer who is 65 or over. Unless the taxpayer or his spouse is 65 or over and disabled, the deduction may not exceed $10,000 on the return of a single person or married person filing separately and may not exceed $20,000 on a joint return or the return of a head of household.

(*g*) Expenses incurred by a woman, a widower, a divorced or legally separated person, or the husband of an incapacitated wife for the care of certain dependents to enable the taxpayer to be gainfully employed.[39] The deduction is limited to $600 if there is one depend-

[33] Sec. 164.
[34] Sec. 165.
[35] Sec. 170.
[36] Secs. 170(b)(1)(C), 170(g).
[37] Sec. 212.
[38] Sec. 213.
[39] Sec. 214.

ent and to $900 if there are two or more dependents. The deduction is reduced in the case of a working wife, other than a deserted wife or the wife of an incapacitated husband, and in the case of a husband with an incapacitated wife if she was not institutionalized for at least 90 days, by the amount by which the combined income of husband and wife exceeds $6,000. The dependent for whom the expenses are incurred must be under 13 or an individual who is unable to care for himself because of physical or mental disability.

(*h*) Alimony and separate maintenance payments to the extent these amounts are includable in the gross income of the recipient.[40]

In lieu of the itemized deductions listed above, a taxpayer may claim the standard deduction.[41] In the case of single persons and married couples filing joint returns, the standard deduction is the greater of 10 percent of adjusted gross income or an amount equal to $200 plus $100 times the number of claimed exemptions, including those for age and blindness. The standard deduction in this case may not exceed $1,000. For married persons filing separate returns, the standard deduction is equal to the greater of 10 percent of adjusted gross income or an amount equal to $100 plus $100 times the number of claimed exemptions and may not exceed $500.

Deductions were itemized on 41 percent of the individual income tax returns filed for the year 1961. Total itemized deductions of $38.4 billion included an estimated $9.3 billion for interest, $11.8 billion for taxes paid,[42] $7.1 billion for contributions, and $5.6 billion for medical expenses. The standard deduction was claimed on 59 percent of the returns filed and totaled $12.9 billion.

4. Personal exemptions

The taxpayer is permitted to deduct an exemption of $600 for himself and an additional exemption of $600 for his spouse and for each dependent. To qualify for the exemption, the dependent must (1) be related to the taxpayer in a manner specified in the statute or be a member of the taxpayer's household, (2) receive less than $600 gross income, except in the case of the taxpayer's child who is under 19 or if 19 or over, who is a student, (3) receive over half his support from the taxpayer, except where a multiple-support agreement is effected, (4) be a U.S. citizen, with certain exceptions, and (5) not have filed a joint return with another taxpayer.[43]

Additional $600 exemptions are provided for a taxpayer aged 65 or over, for his spouse if 65 years of age or over, for a blind taxpayer, and for a blind spouse.[44]

The present per capita exemption system was first provided for the taxable year 1944. Prior to that time, differential amounts were allowed as exemptions for single and married persons and for dependents. The following table summarizes in broad outline the history of personal exemptions in the Federal income tax:

[40] Sec. 215.
[41] Secs. 141–145.
[42] Includes an estimated $1,300,000,000 for taxes not deductible in 1964 and later years.
[43] Secs. 151–153.
[44] Sec. 151 (c) and (d).

TABLE 6.—*Personal exemptions in the Federal income tax, 1913–64*

Year	Single	Married	Dependents
1913–16	$3,000	$4,000	0
1917–20	1,000	2,000	$200
1921–24	1,000	2,500	400
1925–31	1,500	3,500	400
1932–39	1,000	2,500	400
1940	800	2,000	400
1941	750	1,500	400
1942–43	500	1,200	350
1944–47	500	1,000	500
1948 to date	600	1,200	600

Amounts claimed by individuals as deductions for personal exemptions substantially exceed all other deductions combined. In 1961, exemptions totaled $106.5 billion, $82.5 billion on taxable returns and $24 billion on nontaxable returns.

5. Personal income and taxable income

Under present law, the statutory definition of taxable income differs markedly from the concept of personal income employed in national income accounting.[45] In recent years taxable income has comprised less than half of personal income. The divergence reflects both differences in the legal and economic definitions of income and the effect of the deductions and exemptions provided in the tax law. The relative importance of the adjustments necessary to reconcile taxable income with personal income can be illustrated with reference to data for 1961. Personal income in that year was $417.4 billion, as estimated by the Department of Commerce. Taxable income on the taxable returns filed for that year totaled $181.6 billion, or 43.5 percent of personal income. Explicit and implicit statutory exclusions from gross income amounted to $75 billion while receipts included in gross income but excluded from personal income totaled $20.5 billion. The net adjustment for conceptual differences, $55.6 billion, was equal to 13.3 percent of personal income. Nonreported adjusted gross income, in large part attributable to persons not required to file tax returns, and adjusted gross income on nontaxable returns aggregated $51.6 billion, or 12.4 percent of personal income. Deductions and exemptions claimed on taxable returns accounted for the remaining differences between personal and taxable income. Personal exemptions of $82.5 billion comprised the largest component in the

[45] Personal income is defined by the Department of Commerce as the current income received by persons from all sources, including transfers from government and business but excluding transfers among persons. It is measured as the sum of wage and salary disbursements, other labor income, proprietor's and rental income, interest, dividends and transfer payments, minus personal contributiohs for social insurance. Cf. U.S. Department of Commerce, Office of Business Economics, National Income Supplement to the Survey of Current Business, 1954, p. 58.

latter category. Details of the reconciliation are presented in the following table:

TABLE 7.—*Reconciliation of personal income with adjusted gross income, and derivation of the income tax base and tax, calendar years 1961 and 1962* [1]

	1961	1962
	Billions	*Billions*
Personal income	$417.4	$442.1
Deduct:		
Transfer payments (except fees and military retirement pay)	32.9	34.1
Other labor income (except pay of military reservists)	10.7	11.4
Imputed interest	11.6	11.6
Imputed rent	7.0	6.9
Nontaxable military pay	2.0	2.0
Income in kind [2]	3.2	3.2
All other deductions [3]	7.6	8.7
Total deductions	75.0	77.9
Add:		
Employee contributions for social insurance	9.5	10.2
Net gains from sale of assets [4]	8.3	6.4
All other additions [5]	2.7	3.5
Total additions	20.5	20.1
Personal income adjusted	362.9	384.3
Income not reported on tax returns [6]	33.0	35.8
Adjusted gross income reported on tax returns [7]	329.9	348.5
Adjusted gross income, nontaxable returns [7]	18.6	18.0
Adjusted gross income, taxable returns	311.3	330.5
Deduct:		
Standard deduction	11.6	11.9
Itemized deductions	35.6	38.7
Personal exemptions	82.5	85.3
Taxable income of individuals	181.6	194.6
Taxable income of fiduciaries [8]	1.1	1.1
Total taxable income	182.7	195.7
	Percent	*Percent*
Effective tax rate [9]	23.2	23.0
	Billions	*Billions*
Tax liability of individuals, Statistics of Income basis	$42.2	$44.7
Tax liability of fiduciaries [8]	.4	.4
Adjustment to collections basis [10]	1.4	1.5
Tax liability, collections basis	44.0	46.6

[1] 1962 is based on preliminary data and may be subject to significant changes.
[2] Including food and fuel consumed on farms.
[3] Tax exempt interest and savings bond accruals, inventory items, excludable dividends and sick pay, undistributed fiduciary income, and income of pension funds and tax-exempt organizations, etc.
[4] Net gains and losses on capital and other assets reported on individual and fiduciary returns.
[5] Pensions and annuities, and some miscellaneous reported income.
[6] Income of persons not required to file, income disclosed by audit, income of tax evaders, income of fiduciaries, estimating errors in personal income, sampling errors in Statistics of Income, etc.
[7] Adjusted gross income less deficit, individual returns.
[8] Estimate based on recent years.
[9] Effective rate on taxable income of individuals, after tax credits.
[10] Includes tax adjustments, interest and penalties arising from income of earlier years.

Source: Office of the Secretary of the Treasury, Office of Tax Analysis.

B. TAX RATES AND CREDITS

1. *Tax rates*

Once taxable income is determined tax liability is computed by applying the applicable rates from a schedule of rates graduated by taxable income brackets. The basic rate schedule is set forth in section 1(a) of the Tax Code. The rates in this schedule actually apply, however, only to single persons not the head of a household and to married persons who file separate returns. Married couples who file joint returns and heads of households are taxed under modified procedures discussed below. Section 1 tax rate schedules for the taxable years 1954–63, 1964, and 1965 are as follows:

TABLE 8.—*Tax rate schedules, 1954–63, 1964, 1965*

	Tax rates (percentages)				Tax rates (percentages)		
	1954–63	1964	1965		1954–63	1964	1965
Taxable income bracket (thousands):				Taxable income bracket (thousands)—Con.			
0 to $0.5	20	16.0	14	$22 to $26	59	53.5	50
$0.5 to $1.0	20	16.5	15	$26 to $32	62	56.0	53
$1.0 to $1.5	20	17.5	16	$32 to $38	65	58.5	55
$1.5 to $2.0	20	18.0	17	$38 to $44	69	61.0	58
$2 to $4	22	20.0	19	$44 to $50	72	63.5	60
$4 to $6	26	23.5	22	$50 to $60	75	66.0	62
$6 to $8	30	27.0	25	$60 to $70	78	68.5	64
$8 to $10	34	30.5	28	$70 to $80	81	71.0	66
$10 to $12	38	34.0	32	$80 to $90	84	73.5	68
$12 to $14	43	37.5	36	$90 to $100	87	75.0	69
$14 to $16	47	41.0	39	$100 to $150	89	76.5	70
$16 to $18	50	44.5	42	$150 to $200	90	76.5	70
$18 to $20	53	47.5	45	$200 and over	91	77.0	70
$20 to $22	56	50.5	48				

An alternative method of tax computation may be used with respect to any excess of net long-term capital gains over net short-term capital losses. The alternative tax is 25 percent of such amounts.[46] As a rule, this option is employed only by taxpayers whose marginal tax rate on the taxable portion of long-term gains would otherwise exceed 50 percent.

2. Income splitting

In addition to exclusions and deductions from income, the structure of the individual income tax is significantly affected by the provision for income splitting. Married persons who file a joint return compute their joint liability by applying the statutory rates to one-half their combined taxable income and multiplying the result by two.[47] Because the tax rates are graduated, the provision for income splitting generally results in a lower overall tax liability than that on separate returns whenever the taxable income of either spouse exceeds the amount of taxable income in the first rate bracket. Single persons who meet the statutory qualifications for a head of household compute their liabilities from a separate rate schedule which accords approximately one-half of the tax benefits of income splitting.[48] In general, a head of household is defined as an unmarried person who supports a dependent in his home or maintains a residence for a dependent parent.

Provision for income splitting was made in the Revenue Act of 1948 as a means of equalizing the tax treatment of married couples in community property and noncommunity property States. Under the community property doctrine, the income of a married couple is regarded as earned equally by the two. Prior to 1948, court interpretations of the tax law permitted couples in community property States to file separate income tax returns upon which each reported one-half of the community income. A married couple in a noncommunity property State could report on separate returns only the actual income received by each spouse. In the latter case, where all

[46] Sec. 1201.
[47] Sec. 2.
[48] Sec. 1(b).

or most of the combined income was received by one spouse, the filing of separate returns frequently resulted in a greater combined tax liability than the couple would have incurred in a community property State. Permitting all married couples to split their combined taxable income for the purposes of tax computation, therefore, was proposed as a means of insuring that married couples in noncommunity property States would receive the same treatment as those in community property States.

3. Tax credits

Individual income tax liabilities may be affected by one or more of the following tax credits:

(*a*) A credit for tax withheld at source.[49]

(*b*) A credit for foreign income taxes paid, subject to certain limitations, provided that a deduction is not elected.[50]

(*c*) For the taxable years 1954 through 1963, a credit based on 4 percent of the dividends received from domestic corporations, after exclusion, provided such credit does not exceed 4 percent of taxable income.[51] The rate at which the credit is computed is reduced to 2 percent for the taxable year 1964 and the dividend credit provision is repealed for taxable years beginning with 1965.

(*d*) A credit for partially tax-exempt interest on certain Federal Government bonds. The credit may not exceed 3 percent of taxable income.[52]

(*e*) A retirement income credit, under certain conditions, for persons 65 or over and for those under 65 who are retired under a public retirement system.[53] The credit is equal to 15 percent (17 percent in 1964) of up to $1,524 of retirement income in the case of a single person and up to $2,286 of a married couple's retirement income if both are 65 or over. If both husband and wife have retirement income each may take a credit based on up to $1,524 of their individual retirement income provided they both meet the other qualifications for the credit. In the case of persons aged 65 or over, retirement income is defined as pensions, annuities, rents, interest, and dividends. In the case of persons under 65, retirement income is limited to pensions or annuities received under a public retirement system. The maximum amount of retirement income upon which the credit may be based is reduced by (i) the amount of pensions or annuities received which are exempt from tax, such as Social Security and Railroad Retirement Act pensions, and (ii) earned income in excess of $900 for a person under 62 and, for a person aged 62 but under 72, one-half of earned income between $1,200 and $1,700 plus all earned income in excess of $1,700.

(*f*) A credit equal to 7 percent of qualified investment in depreciable personal property placed in service during the tax year.[54] This investment credit is subject to certain limits but excess credits may be carried over to later years. In general, personal property is not depreciable for tax purposes unless used in connection with a trade or business.

[49] Sec. 31.
[50] Secs. 33 and 901. See ch. 8, "Taxation of Income from Foreign Sources."
[51] Sec. 34.
[52] Sec. 35.
[53] Sec. 37.
[54] Sec. 38. See ch. 5, "Depreciation and the Investment Credit."

With the exception of the credit for taxes withheld at source, the sum of allowable tax credits cannot exceed tax liability. Excess credits for foreign taxes and qualified investment may be carried over, however, and applied to liabilities incurred in future years.

4. Averaging

In the absence of a provision for averaging, an individual might, because of graduated tax rates, pay substantially more in tax if his income fluctuated widely than he would if his income were spread evenly over the years. Recognition of this problem has given rise to a number of provisions in the tax law designed to introduce some measure of averaging. For example, special rules for long-term capital gains furnish a rough approximation to averaging in certain cases where a gain that has accrued over many years is realized in 1 year.[55]

Prior to 1964, the tax law did not contain a general provision for the related problem that occurs when career earnings or earnings that are the result of an extended period of effort and preparation are received over a relatively short span of time. A number of special rules had been introduced, however, dealing with the special problems of authors and inventors and with such matters as backpay and damages received in lawsuits. The Revenue Act of 1964 replaced these scattered provisions with an averaging device of general applicability which does not require the recomputation of taxes paid in prior years. In general, the amount of taxable income in the computation year which exceeds four-thirds of the average taxable income of the preceding 4 years, if it amounts to at least $3,000, is taxed at five times the rate otherwise applied to one-fifth of the averagable income.[56] Net long-term capital gains, the income from previous gifts, and wagering gains are excluded from the benefits of this provision. Furthermore, averaging is not available to those who were nonresident aliens at any time during the 5-year period or who were not members of the labor force throughout that period.

C. UNINCORPORATED BUSINESSES AND FIDUCIARIES

1. Sole proprietorships and partnerships

Under the provisions of the Internal Revenue Code, the tax treatment of the profits of a trade or business depends to an extent on the form of business organization. Businesses organized as sole proprietorships or partnerships are not taxed as separate entities.[57] Taxable profits, whether or not actually distributed, are included on the individual returns of the proprietors or partners. In such cases personal exemptions and deductions may be set off against business income, and business losses can be set off against other sources of personal income. On the other hand, businesses organized as corporations are taxed as separate entities at tax rates which are intermediate between the highest and lowest rates applied to individual income. In general, corporate shareholders include on their individual returns only that portion of corporate net income distributed as dividends.

While in most important respects business taxable income is defined in the same manner regardless of the form of organization, certain

[55] See ch. 4, "Capital Gains Taxation."
[56] Secs. 1301–1305.
[57] Unless they constitute associations taxable as corporations under sec. 7701(a)(3).

deductions are available only to corporations.[58] Chief among these is the deduction for intercorporate dividends.

Although its income is fully taxable to the partners, a partnership is required to file a return for informational purposes, indicating its income and the distributive share of each partner.[59] Each partner must take into account, separately, his distributive share of the various types of income received by the concern and of its deductible expenses.[60] Distributions in excess of the income of a partnership are not taxable to a partner unless they exceed his adjusted basis in the concern. The adjusted basis, in general, is equal to the partner's contribution to capital plus any of his distributive share of income not withdrawn from the firm, less any of his distributive share of partnership losses previously deducted and the amount of any distributions in excess of income. A partner may deduct his share of partnership losses only to the extent of his adjusted basis in the firm. Excess losses may be deducted in future years, however, if the partner subsequently increases his basis in the partnership.

The Internal Revenue Code contains a number of provisions which deal with problems peculiar to partnerships, such as reorganizations, dissolutions, membership changes, the sale or transfer of partnership interests, and the allocation of basis in capital assets. Other provisions are designed to prevent tax avoidance through the use of family partnerships or member dealings with the concern.

Under certain conditions, unincorporated businesses may elect to be taxed as corporations.[61] To qualify, the business cannot have more than 50 individual owners and must be one in which either capital is an income-producing factor or at least 50 percent of gross income is derived from trading. Once made, the election is irrevocable unless there is a major change in the composition of business ownership.

Sole proprietorships, which include the activities of many farmers and self-employed professional men, comprise the bulk of the Nation's business firms, but corporations account for the largest share of total business receipts, profits, and depreciation. In 1961, the 11.4 million business units that filed tax returns were composed of 9.2 million proprietorships, 0.9 million partnerships, and 1.2 million corporations. Unincorporated businesses received 23 percent of the $1.07 trillion of total business receipts, 41 percent of the total net profits of $77 billion, and claimed 28 percent of total depreciation deductions.

2. Estates and trusts

Estates and trusts are taxed as separate entities, at the rates applicable to single individuals not the head of a household. The fiduciary who manages the estate or trust (not the grantor or the beneficiaries) must file the necessary tax returns and pay any tax due.[62]

The gross income of a trust or estate is defined in the same manner as the gross income of individuals.[63] In addition to the deductions allowed individuals a further deduction is allowed for distributions

58 Secs. 241–248.
59 Sec. 6031.
60 Ch. 1, subch. K.
61 Sec. 1361.
62 Sec. 6012(b)(4).
63 Sec. 641(b).

to beneficiaries, however, so that an estate or trust is only taxed on undistributed income.[64] Estates are entitled to an exemption of $600, simple trusts to an exemption of $300, and complex trusts to an exemption of $100.[65] In general, credits against tax are permitted as in the case of individuals.

Beneficiaries must include in their gross incomes not only distributions received from a trust or estate but also income required to be distributed to them. Distributions in excess of the net income of the trust or estate, however, are not includible in the gross income of the beneficiary. Special rules govern distributions of previously accumulated undistributed net income of trusts (but not estates) to prevent tax avoidance which would otherwise occur if the income of many years were distributed in 1 year so that the excess over the trust's distributable net income in the year of distribution would be untaxed to the beneficiary.[66] If the grantor of a trust retains certain rights in, or control of, the property, the income of the trust must be included in his gross income.[67] Other provisions of the law deal with employee trusts, [68] multiple beneficiaries, [69] and adjustments when the trust or estate cannot use all of its available credits or exclusions.[70]

In 1960, tax returns were filed for 425,424 trusts and 154,236 estates. Over half of the trusts and estates were nontaxable, primarily because of distributions to beneficiaries. The distribution of taxable income among fiduciaries was skewed sharply. Trusts and estates with total incomes of $25,000 or more comprised 6.6 percent of the fiduciary returns filed in 1960, yet received 55 percent of total income and paid 71 percent of the tax after credits.

D. METHOD OF TAXPAYMENT

While the final tax return for a calendar year need not be filed before the following April 15, provisional taxpayments are normally required during the course of the tax year. The principal of current payment, established by the Current Payment Tax Act of 1943, is implemented by a system of wage withholding supplemented by declarations and quarterly payments of estimated tax. In general, the latter are only required when the full tax liability is expected to exceed withheld tax by more than $40. The taxpayer credits amounts withheld from wages and any estimated taxpayments against his final liability. If there is remaining tax due, it must be paid when the final return is submitted. If the provisional payments have exceeded the final liability, the excess may, at the taxpayer's option, be refunded, applied toward the purchase of Federal savings bonds, or applied as a credit against the following year's tax.

1. *Wage withholding*

Employers are required to deduct provisional income tax payments before wages and salaries are paid out to employees. The tax withheld is equal to 14 percent of the excess of wages for the pay period over the proportionate share of the employee's annual, claimed with-

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[64] Secs. 651, 661.
[65] Sec. 642(b).
[66] Secs. 665–668.
[67] Secs. 671–677.
[68] Secs. 401, 501.
[69] Secs. 652, 662, 663(c).
[70] Sec. 642(b).

holding exemptions allotted to the pay period. Withholding exemptions have an annual value of $667; the $600 personal exemption is "grossed up" to reflect the standard deduction. The withholding rate is equal to the average of the statutory rates applicable, in 1965, to the income in the first four tax brackets (15.5 percent) reduced to reflect the standard deduction. Wage bracket tables are provided to facilitate the computations.[71] Amounts withheld must be deposited by the employer, usually each month, in a designated depository.

The withholding rate has fluctuated between 22.5 and 14 percent, reflecting changes in the statutory rates. From January 1, 1945, to May 1, 1948, a two-rate, graduated scale of withholding tax rates was in effect. An outline of the history of withholding tax rates follows:

TABLE 9.—*Withholding tax rates, 1943–64*

Dates:	*Percentage rate*
July 1, 1943, through 1944	20
1945	[1] 20.7, 22.5
1946–47	[1] 17, 19
1948 through Sept. 30, 1950	15
Oct. 1, 1950, through Oct. 31, 1951	18
Nov. 1, 1951, through 1953	20
1954 through Mar. 4, 1964	18
Mar. 5, 1964, to date	14

[1] The lower rate applied to surtax net income, at annual rates, of $2,000 or less.

Withholding is also required with respect to all fixed or determinable annual or periodic income payments made to nonresident aliens. The withholding rate in this case is 30 percent unless a lower rate is specified by a tax treaty in effect between the United States and the country in which the alien resides or of which he is a citizen.

2. Payments of estimated tax

Single persons who can reasonably expect their gross income to exceed $5,000 and married couples or heads of households who can reasonably expect their gross income to exceed $10,000 must file a declaration of estimated tax not later than April 15 of the current year. Declarations are also required of any person whose gross income can reasonably be expected to include more than $200 of income not subject to withholding. No declaration is required, however, if after the deduction of anticipated withholding and other credits against tax the estimated tax is less than $40.[72] Payments of estimated tax are made in equal quarterly installments, due on or before April 15, July 15, September 15, and January 15 for calendar year taxpayers. If the taxpayer's financial outlook changes, amended declarations must be filed, and estimated taxpayments adjusted. The January estimated tax payment may be omitted if the final return is filed by January 31. Farmers and fishermen have until January 15 of the following year to file a declaration and may omit it entirely if they file their final return by February 15.[73]

Penalties are assessed for the underpayment of estimated tax if the cumulative amount of tax paid is less than 70 percent of the tax due in any one quarter. No penalty is assessed, however, if the esti-

[71] Sec. 3402.
[72] Sec. 6015.
[73] Sec. 6073.

mated tax installments are based on either the preceding year's tax or taxable income, and under certain other conditions.[74]

3. Characteristics of the current payment system

Current payment procedures spread the payment of tax liabilities evenly over the year and insure a relatively steady flow of funds to the Treasury. Of the 61.5 million individual returns filed in 1961, 51.6 million recorded a credit for withheld tax. These credits totaled $34.4 billion. Credits for quarterly payments of estimated tax were taken on 5.2 million returns and totaled $9 billion. Provisional taxpayments were thus roughly equal to total individual tax liabilities for the year.

Current payment methods are provisional; the amounts withheld and paid quarterly rarely equal a taxpayer's exact final liability. In 1961, 38.4 million tax refunds were made and 1.6 million credits were extended toward 1962 liabilities as a result of overpayments totaling nearly $6 billion (the option of purchasing savings bonds was not available until 1963). Nearly 90 percent of the overpayment was accounted for by overwithholding. On the other hand, 18.6 million 1961 returns indicated tax due at the time of filing, which totaled $5.7 billion.

II. Issues and Proposals

The structural features of the individual income tax have been a major source of controversy since the inception of the tax. Questions currently at issue include the impact of the graduated rate structure on incentives to work and invest, the size of the tax base relative to total personal income, the fairness with which tax burdens are distributed, the effects of the tax on the allocation of resources, and the need for simplified procedures.

A. THE IMPACT OF THE RATE STRUCTURE ON INDIVIDUAL INCENTIVES

The tax rate reductions enacted in 1964 notwithstanding, some observers feel the degree of rate graduation in the income tax may be excessive.[75] This is reflected in the fact that the new rate structure falls far short of many of the proposals for rate revision that have been made in recent years, including proposals for a constitutional amendment.[76] Some of the widely publicized proposals, for example, call for restricting the spread between the lowest and highest marginal rates to 15 or 25 percentage points.

One of the principal arguments in support of such proposals is that steep income tax progression has a seriously adverse effect on personal incentives to provide labor services and, in particular, managerial services. It is argued that additional efforts involve costs to the individual in terms of leisure and recreational activities which must be foregone and often in terms of the physical and psychological strains which must be undergone. The greater the proportion of additional income which must go to pay taxes, the less the incentive to provide additional effort or assume added responsi-

[74] Sec. 6654.

[75] See, for example, the statement of C. Lowell Harriss, in the Revenue Act 1963, hearings before the Committee on Finance on H.R. 8363, 88th Cong., 1st sess., pt. 3, pp. 1455–1473.

[76] For a discussion of some of the proposals, see "Constitutional Limitation on Federal Income, Estate, and Gift Tax Rates," Joint Economic Committee print, 82d Cong., 2d sess., and "The Proposed 23d Amendment to the Constitution To Repeal the 16th Amendment to the Constitution Which Provides That Congress Shall Have Power To Collect Taxes on Incomes," S. Doc. 5, 87th Cong., 1st sess.

bility. This argument is said to have particular relevance to the position of talented young men and women with the opportunity to advance in a business or profession. The extent to which the overall rise in tax rates is concentrated in the middle taxable income brackets is said to discourage the exertion of maximum effort by the enterprising people whose work has special significance to the economic progress of the country.

Steeply progressive rates are also said to discourage investment in high-risk ventures. The possibility of large rewards is necessary to compensate individuals for the assumption of large risks, it is argued, yet the greater the reward under the present tax system, the heavier the effective rate of tax. It is contended that investments which carry high risks are often the ones which lead to the breakthroughs in the discovery of new products or processes which are of great significance to rapid economic growth. Steep progressive rates are also said to limit the amount of savings available to implement investment projects, particularly the savings of those most likely to support risky ventures.

Those who defend the progressive rate structure point out that there is neither conclusive argument nor empirical evidence to demonstate that present tax rates, in the aggregate, inhibit individual effort or risk taking. On analytical grounds, it is contended that the loss of income occasioned by the tax may induce an individual to work harder, offsetting any adverse incentive effect of higher tax rates on marginal earnings. As a practical matter it is contended that nonfinancial motives, such as power or prestige, are often the most important sources of individual motivation. It is also pointed out that various studies have failed to discover evidence of the supposed disincentive effects of steeply progressive tax rates.[77] Furthermore, it is contended that observed decreases in general hours of work and the labor force participation rate are fully accounted for by long-term institutional factors.

As regards risk taking, it is pointed out that the deductibility of losses for tax purposes reduces an investor's actual risk if he has other sources of income. The fact that the Government will, in a sense, share potential losses, may be as important to an investor as the fact that it will share in any rewards.[78] Those who accept this argument concede, however, that a provision for loss deduction may be immaterial if there is little or no other income to set against the loss. Furthermore, present law limits the deductibility of net long-term capital losses.

It is also argued that the statutory rate structure suggests a great deal more progression in the income tax than in fact exists. It is pointed out that, contrary to widespread impression, progression in the rate structure applies only to a very limited amount of income. In the first place, total individual income actually subject to tax is

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[77] Cf. Butters, Thompson and Bollinger, "Effects of Taxation on Investments by Individuals," and Sanders "Effects of Taxation on Executives," Harvard Business School series, Effects of Taxation, 1953 and 1951; Long, "Impact of Federal Income Tax on Labor Force Participation" and Break, "Effects of Taxation on Work Incentives" in Federal Tax Policy for Economic Growth and Stability, papers submitted by panelists appearing before the Subcommittee on Tax Policy, Joint Committee on Economic Report, 84th Cong., 1st sess., Nov. 9, 1955 (hereafter cited "Tax Compendium"), pp. 153–166 and 192–199; and Break's papers "Income Taxes and Incentives To Work: An Empirical Study," American Economic Review, September 1957, pp. 529–549, and "Income Tax Rates and Incentives To Work and To Invest," Tax Revision Compendium, Compendium of Papers on Broadening the Tax Base submitted to the Committee on Ways and Means, committee print, 1959 (hereinafter cited as "Ways and Means Compendium") pp. 2247–2255.

[78] See Evsey D. Domar, and R. A. Musgrave, "Proportional Income Taxation and Risk-taking," Quarterly Journal of Economics, May 1944, pp. 387–422.

less than half of total personal income. Second, two-thirds of the income subject to tax at ordinary income tax rates, it is estimated, fell within the first tax bracket in the years prior to 1964. Moreover, in 1961 total individual tax liabilities before credits, $42.7 billion, exceeded 20 percent of taxable income by only $6.3 billion, indicating that the marginal tax rates that exceeded the first bracket rate of 20 percent accounted for only 15 percent of individual income tax liabilities. Finally, when measured against adjusted gross income, the overall effective rate of tax, after credits, was only 12.8 percent in 1961.

It is also pointed out that at very high income levels, where presumably high marginal rates in the income tax have a maximum impact, effective tax rates are considerably less than statutory rates might suggest. In 1961, for example, tax after credits represented 47 percent of the adjusted gross income of all persons with incomes of $1 million or more. Moreover, it is pointed out that the tax represented only 29.5 percent of the total of adjusted gross income and the excluded half of capital gains. This suggests that the supply of venture capital has not been as sharply curtailed by the progressive tax rates as some have supposed.

Those who hold that criticisms of the present rate structure are unconvincing point out that the record since the end of World War II has not, in the main, indicated that progressive tax rates have slowed the economy's performance. It is argued that any lag in the Nation's rate of growth in the late 1950's and early 1960's, if, indeed, it occurred, was due to a lack of overall demand attributable more to the heavy weight of taxes in general than to the character of the rate structure. The repressive effect has been lifted, it is argued, by the 1964 rate reductions.

As regards the rate at which the overall progression is attained, it is pointed out that the level of tax rates and not the rapidity with which they increase is apt to be of greater significance to incentives. In this sense, it is argued, the reduction in rates carried out in 1964 is more important than the concentration of progression in certain taxable income tax brackets. Furthermore, use of the rate scale as a measure of progression does not take into account capital gains provisions, income splitting, deductions, and other factors which affect effective tax rate progression.

B. THE SIZE OF THE TAX BASE RELATIVE TO PERSONAL INCOME

In recent years increasing attention has been devoted to the structural features of the individual income tax which affect the manner in which various types of receipts and expenditures are treated in determining taxable income. Many of these features, it is contended, keep substantial amounts of income out of the tax base on grounds only haphazardly, if at all, related to the taxpaying ability of the recipient. By contracting the tax base relative to actual income, these structural features necessitate excessively high tax rates in order to meet present revenue demands. Numerous proposals have been made for increasing the revenue potential of the income tax by eliminating or modifying base-eroding features. Restoration of the tax base, it is contended, would make possible substantial reductions in tax rates without a loss in revenue.

The relative importance of the various adjustments which account for the difference between personal income as defined by the Department of Commerce and taxable income has been noted.[79] As a result of exclusions, deductions, exemptions, and definitional differences, taxable income in 1962 was equal to 44 percent of personal income.

The ratio of taxable income to personal income has risen gradually since 1945. The individual income tax base increased from $52.3 billion in 1945 to an estimated $210 billion in 1963,[80] or by roughly 300 percent. In the same period, personal income increased from $171.2 to $463 billion, or by 170 percent. In 1945, the income to which statutory rates were applied in computing tax liabilities represented 30.5 percent of personal income while in 1963 taxable income was an estimated 45.2 percent of personal income. The major factor in this rise has been the continued expansion of personal income which has increased the relative amount of taxable income despite legislation which has tended to narrow the tax base.

Nevertheless, despite the growth in the tax base relative to personal income, the absolute difference between personal income and taxable income has increased substantially, from $118.9 billion in 1945 to an estimated $253.5 billion in 1963. Although statutory changes in the postwar period, particularly those provided by the Revenue Acts of 1948 and 1954, contributed significantly to the increase in the gap between personal income and the tax base, a substantial part is accounted for by longer standing provisions of the law. While many of these provisions involved quite modest contractions of the tax base at the time they were enacted, the amount of income removed from the tax base by these provisions has tended to increase as the economy expands.

While few dispute that the magnitude of the difference between personal and taxable income is a matter of considerable concern for tax policy, there are divergent views about the extent to which additional revenue can be provided by diminishing this difference. Those who favor eliminating tax provisions which wholly or partially exclude various types of income from the tax base contend that this is the most feasible way in which tax rates can be significantly reduced in view of present and foreseeable trends in Federal expenditures. Even relatively modest success in expanding the taxable income base at any given level of personal income, it is pointed out, would make possible a substantial reduction in individual income tax rates without a loss in revenue. For example, if only one-tenth or $25 billion of the estimated difference between personal and taxable income in 1962 had been restored to the taxable income base, individual income tax rates could have been reduced on the average by about 12 percent.[81]

On the other hand, it is pointed out that most of the difference between personal and taxable income is accounted for by items which either cannot be included in taxable income on the basis of practical administration and compliance considerations, or which should not be included if other basic objectives of public policy are to be adequately served. Even granting that in theory income in kind and imputed rent and interest income, for example, are properly subject to tax, the practical difficulties of taxing these items under a self-

[79] See above, table 7, p. 23.
[80] Department of Commerce, Survey of Current Business, March 1964, pp. 3-5. Excludes fiduciaries.
[81] For an interesting analysis of the possibilities in this regard, cf. Joseph A. Pechman, "What Would a Comprehensive Individual Income Tax Yield?" Ways and Means Compendium, pp. 251-281.

assessed income tax would be formidable. These items accounted for $21.7 billion of the estimated difference between personal and taxable income in 1962. Moreover, it is pointed out that the largest single difference between the two income concepts is the personal exemption which aggregated $85.3 billion on taxable returns in 1962. An additional $34.1 billion represented transfer payments, such as unemployment compensation benefits and social security benefits. The sum of these items represents over half of the difference between personal and taxable income. Including them in taxable income, it is contended, would have severe repercussions on low-income and retired individuals which could not be adequately offset by any feasible changes in tax rates. Viewed in the perspective of these constraints, therefore, opportunities for broadening the tax base are not as great as an unqualified comparison of personal and taxable income data might suggest. Moreover, these illustrations point up the fact that a significant change in the distribution of income tax burdens might well result from broadening the base and reducing tax rates. The resulting distribution might differ materially from that widely regarded as desirable.

C. EQUITY CONSIDERATIONS

At the heart of much of the controversy over the structural features of the individual income tax are disagreements over the appropriate distribution of the burden of the tax. Numerous proposals have been made in recent years to expand the tax base and provide the revenues needed to offset the loss occasioned by a revision in the rate structure or an increase in personal exemptions. Some of these proposals would eliminate specific provisions the benefits of which presumably accrue largely to upper income individuals. Other proposals are concerned with eliminating inequitable differences in tax liabilities between individuals with the same income. While the two approaches are distinct in principle, they are interrelated in debates over particular issues. Within recent years, the impact of special provisions has generated as much if not more controversy than the structure of tax rates.

1. *The concept of income*

A difficulty that lies behind much of the debate over equity issues is the lack of a consensus on the proper definition of income. The Internal Revenue Code does not define income directly but arrives at the statutory concept, by and large, by specifying the manner in which various types of receipts and expenditures are to be treated. As a consequence, it is contended, the principle of the uniform application of standard rules has been sacrificed as differential provisions have been proliferated through the law. Numerous illustrations are cited. Thus, it is pointed out that while interest income is generally included in taxable income, an exception is made for interest paid on State and local government obligations. Differential treatment is afforded various types of arrangements for providing retirement income. The extra personal exemption extends blind taxpayers preferential tax treatment as compared with those who suffer from other disabling physical handicaps.

The proliferation of differential tax provisions, it is argued, is the result of a continuing process of attempting to provide special tax adjustments for special types of situations. The basic difficulty, it is pointed out, is in the fact that forsaking a general rule in any one case gives rise to demands for similar concessions in others. The result is an income tax system which places a premium on tax avoidance devices and increases the relative tax burdens of those who are unable or unwilling to take advantage of the special provisions.[82] Those who hold this view argue that a major objective of tax policy should be to reduce the number of special provisions in the income tax. To this end, it is maintained, it is necessary to achieve acceptance of a meaningful and practical concept of taxable income.

For many economists, the best definition of income for tax purposes is the algebraic sum of an individual's consumption expenditures and the change in his net worth during a given period of time.[83] According to this definition, neither the source of the income, the conditions under which it is received, nor the manner in which it is disposed of should be regarded as pertinent in determining the extent to which it is subjected to tax. Adherence to this definition would require that income, including unrealized capital gains, be taxed on the basis of its accrual, rather than on the basis of actual realization.

As a practical approximation to this definition, it has been suggested that taxable income should be defined as gross receipts less the expenses necessarily incurred in obtaining these receipts, including depreciation. In addition, deductions would be allowed for liens on the taxpayer's income, such as the income taxes of another jurisdiction and alimony payments. Proponents of this concept concede that it is not ideal. Nevertheless, it is maintained that some such standard, rigorously applied, is necessary if the erosion of the tax base is to be arrested. Moreover, it is argued, any adverse effects on the fairness of the tax structure resulting from close adherence to this type of standard would be far less substantial than those which have resulted from a multiplicity of special provisions. Furthermore, the expansion of the tax base which would result from following the proposal would permit major reductions in tax rates which would greatly mitigate any adverse effects of base expansion.

On the other hand, it is pointed out that a truly uniform tax system might often impose severe financial hardships on taxpayers whose special situation would not be adequately reflected in a general tax statute. Carefully designed tax allowances in such cases, it is argued, serve to equalize comparative tax burdens among persons in varied circumstances. Moreover, the tax law must recognize that certain types of desirable economic activity are peculiarly sensitive to the deterrent effect of income taxation. Other provisions in the law, it is pointed out, reflect deliberate public policy to encourage worthwhile activities. Furthermore, the full taxation of income when realized would impose hardships when income earned over several years was realized in 1 year and might thus discourage certain investments.

2. The level of exemptions

It is frequently proposed that the value of the exemptions be altered to effect desired changes in the distribution of tax burdens. Some of those who believe that the tax burden on low income indi-

[82] Cf. Blum, "Effects of Special Provisions in the Income Tax on Taxpayer Morale"; Cary, "Pressure Groups and the Increasing Erosion of the Revenue Laws"; and Paul, "Erosion of the Tax Base and Rate Structure," in Tax Compendium, pp. 251-275 and 297-311.
[83] Henry C. Simons, "Personal Income Taxation," Univ. of Chicago Press, 1938, p. 50.

viduals should be eased have called for an increase in the value of the personal exemption. They contend that such an increase is required to make adequate allowance for the substantial increase in the cost of living that has occurred since the present $600 personal exemption was adopted. In addition, it is maintained that tax legislation since the end of the Korean emergency has afforded relief primarily to middle and upper income taxpayers while increases in old age and survivors insurance contribution rates and State and local government tax assessments have actually added to the burdens on individuals at the lower end of the income distribution. Tax reduction for the low income taxpayer, it is contended, is required in order to restore the appropriate overall distribution of income tax burdens.

Those opposed to an increase in the exemption, or in an equivalent tax credit, point out that such proposals would result in a significant decrease in the tax base and in the number of individuals who contribute to the financial base of the Government through the income tax. It is estimated that a $100 increase in the exemption, for example, would remove about 3.5 million taxpayers, who now file 2 million taxable returns, from the income tax rolls and reduce tax revenue by about $2.7 billion.

Moreover, it is argued, the present income tax structure places undue importance on the size of a taxpayer's family. An increase in the value of the exemption, it is pointed out, would exaggerate this relationship.

Some of those who favor tax reduction for lower income individuals point out that the benefits of an increase in the personal exemption would not be limited to such taxpayers. On the contrary, the reduction in tax liability would actually be greater the greater the amount of the taxpayer's income, since the amount of the tax savings conferred by an exemption depends on the marginal tax rate to which the taxpayer is subject. Accordingly, in order to limit the benefits and, therefore, the expense in terms of lost revenue, it has been proposed that a flat credit be allowed against an individual's tax liability, based on the number of exemptions the taxpayer claims.

Alternatively, it is contended that the minimum standard deduction enacted in the Revenue Act of 1964 provides a more suitable method of extending relief to low-income individuals than a direct increase in the value of the personal exemption. It is pointed out that the value of the minimum standard deduction diminishes as the taxpayer's income increases and vanishes entirely when adjusted gross income exceeds 10 times the minimum deduction or $10,000. This provision effectively supplements personal exemptions for taxpayers with low incomes without extending tax benefits to those with relatively large incomes. Proponents of a larger personal exemption point out, however, that the benefits of the minimum standard deduction are available only to low-income taxpayers who do not itemize their deductions. Those low income persons with heavy deductible expenses, such as medical expenses, are not likely to benefit greatly, if at all, from the minimum deduction.

It is also contended that relative to an increase in the exemption, the four-way split in the former first income tax bracket enacted as a part of the Revenue Act of 1964 is a superior method for providing relief to low income taxpayers. This feature, it is pointed out, will not decrease the number of taxpayers or the size of the tax base. Moreover, it introduces rate progression for a large number of taxpayers who under former law were subject only to the first bracket tax rate. The new rate brackets, it is maintained, afford a proper differentiation in tax liabilities among low income individuals.

On the other hand, it is pointed out that the personal exemption provides a substantial degree of effective progression. The exemption represents, in effect, a zero rate bracket; although each dollar of income in the first statutory bracket is taxable at the same marginal rate, the effective rate of tax, i.e., tax liability divided by adjusted gross income, increases as income increases. For example, a single individual with no dependents, claiming the standard deduction, would have no tax liability at 1965 rates on an adjusted gross income of $900. With an adjusted gross income of $1,200, his tax liability would be $42, an effective rate of 3.5 percent. At $1,399 of adjusted gross income, his tax would be $70 or 5 percent of his adjusted gross income. The marginal tax rate at all three levels would be 14 percent.

3. The importance of family status

Some observers contend that tax burdens, particularly at low- and middle-income levels, are unduly effected by family status. Under present law much of the progression in effective rates of tax results from the exemption system and, therefore, progression depends to an undue extent on family size rather than family income. It is pointed out, for example, that a single taxpayer with an income of $1,000 is subject to the same bracket rate of tax as a married person with three children earning $4,500, or four and one-half times as much. Prior to 1964, a married person with three children could have earned over 10 times as much as a single person and still have paid tax at the same bracket rate.

In addition, it is argued that income splitting on joint returns of married taxpayers unduly favors the married individual as compared with a single person and substantially vitiates rate progression, particularly for certain upper bracket taxpayers. Moreover, it is pointed out that the benefits of income splitting vary with income in a manner which provides no benefit for those in the very highest or lowest tax brackets and the maximum benefit for those with incomes in the middle taxable income brackets. To offset these consequences without reintroducing the inequality between community and noncommunity property States which existed prior to 1948, it has been suggested that married taxpayers be required to use a separate rate schedule with taxable income brackets one-half the width of the present statutory brackets.[84]

Those who support the present provisions regarding family status argue that favorable tax treatment of the family is socially desirable and conforms to reasonable criteria of ability to pay. To tax families and single persons under the same progressive rate schedule would impose a financial penalty on marriages in which both parties have separate incomes. Furthermore, it is said, families with children typically have greatly expanded needs for space, food, and services, such as health and education, which justify differential tax treatment.

[84] Pechman, "Individual Income Tax Provisions of the 1954 Code," National Tax Journal, March 1955, p. 129.

4. Tenants and homeowners

Those who argue that equity would be served by sharply restricting the scope of the present deductions and exclusions often call attention to the tax treatment of tenants as opposed to persons who own and occupy their residences. The fact that the imputed rental value of owner-occupied residences is not included in gross income results in a lower tax liability for the homeowning taxpayer than for a person who rents his residence and receives the same amount of income, all explicit, from other sources.[85] Moreover, the differential tax treatment of many homeowners is further enhanced by the deductibility of property taxes and interest payments on mortgage and home improvement loans. To restore tax equity, it is argued, imputed rental income should be taxable or, as a practical alternative, the deductions for property taxes and mortgage interest payments should be denied.

Those in favor of retaining present tax provisions argue that taxing imputed income would be difficult if not impossible as a practical matter. On the other hand, to deny a deduction for mortgage interest would, it is contended, lessen the differential favoring homeowners over tenants at the expense of imposing a new differential between those with a large equity in their home and those with little equity. Furthermore, it is contended, such a major change in the law would be unfair to those who purchased homes under prior conditions. If, on the other hand, the revised law applied only to newly purchased homes it would provide a new source of tax discrimination and disrupt the housing market.

It is also pointed out that the present tax treatment has been in effect over a relatively long period and, therefore, the supply of rental and owner-occupied housing has been adjusted to take into account any differential originally created by the tax law. In this view, while the tax law may have been responsible for an allocation for resources which varies from what some regard as optimal, relative prices have been adjusted in a manner which offsets the differential in the tax law. It is also pointed out that tenants often employ the standard deduction in lieu of itemized deductions for interest and taxes. While this deduction may not be as great as the itemized deductions which would arise from the ownership of a similar accommodation, it normally exceeds expenditures of a deductible nature actually made.

Finally it is contended that the promotion of widespread homeownership serves an important social objective. Homeownership is said to be beneficial to the community and the individual. Furthermore, a vigorous residential construction industry is said to be important to the maintenance of full employment.

5. The tax treatment of the aged

The tax law contains a number of special provisions designed to grant special relief to the aged (those aged 65 or over), including a double personal exemption, the retirement income credit, exemption from the floor on the medical expense deduction, and others. In addition, Treasury ruling exempts social security and railroad retirement benefits from tax. Justification for these special provisions is found in the problems of the retired aged, whose incomes are said to

[85] Cf. White, "Deductions for Nonbusiness Expenses and an Economic Concept of Net Income," in Tax Compendium, pp. 357–360.

be typically much reduced after retirement. As lifespans increase, retirement ages decline, medical costs increase, and price levels rise, the financial problems of the aged, it is said, become ever more difficult.

Objections to the present provisions have been made on the grounds that they give little relief to the really needy aged while the wealthy, a proportionately large number of whom are in the 65 and over age bracket, derive significant benefits. Furthermore, present provisions, it is said, unduly complicate the tax law and discriminate against aged persons who continue in employment. The age of 65 is held to be a purely arbitrary dividing line which bears no direct relation to taxpaying ability. Moreover, it is contended that while medical costs are typically higher for the aged, other costs are generally lower.

6. A credit or deduction for educational expenses

Considerable support has been generated in recent years in favor of a deduction or tax credit for the expenses of financing higher education.[86] Proponents argue that support for education is in the national interest. They further argue that the use of the tax system is an expedient which would avoid disputes involving aid to religious schools and other issues engendered by expenditure proposals designed to achieve the same result. They argue that a deduction or credit for educational expenses would not influence students in the selection of schools or courses of study yet grant them material relief with respect to the ever-increasing costs of higher education. The deduction or credit can, it is argued, be tailored to prevent the value of the tax concession from varying directly with tuition and other costs.

Those who oppose this deduction contend that the tax system is an inefficient device for promoting this social objective. While desirable in itself the objective is only one of many worthwhile purposes which could be implemented through the tax structure. If this particular allowance were permitted, it would be difficult to deny others. The overall result would be a serious loss of tax revenue.

Moreover, a tax deduction or credit would, it is contended, be of benefit primarily to those who could afford to finance a higher education in any case. The real objective, it is argued, is to supply a higher education for those otherwise not able to provide it from their own or their family's resources. In this sense, a credit or deduction for all taxpayers is a costly method for providing support to a few. Furthermore, it is not likely to help the really needy, since they have little or no taxable income in any case. The credit or deduction, it is argued, can only provide marginal relief, since to cover the full cost of higher education would be too costly to the Treasury. It is also pointed out that the low tuition levels maintained by many State colleges and universities for State residents would preclude the parents of many of the students at these institutions from benefiting from a credit or deduction based on tuition. Finally, some institutions might simply raise their tuition charges to absorb the relief provided by a credit or deduction.

7. The degree of progression

Some observers feel that the present tax law is excessively progressive in impact and have advanced proposals for easing the present

[86] Cf. S. 1567, introduced by Senator Ribicoff in the 88th Cong., 1st sess.

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burden on middle or upper income taxpayers. It is contended that such tax reduction is necessary to increase the overall rate of saving and capital formation out of any given level of total income. The potential improvement in real living standards of low-income indiivduals resulting from more rapid economic growth, it is maintained, substantially exceeds that from any practicable redistribution of tax burdens.[87]

Others voice the opinion that the progression in the tax rate structure is more apparent than real. They point out that in 1959, among the 1,002 returns listing adjusted gross incomes of $500,000 or more, there were 20 returns on which there was no tax liability and 73 returns with effective tax rates of under 30 percent. Furthermore, adjusted gross income excludes one-half of capital gains. Measuring tax against adjusted gross income augmented by the excluded portion of capital gains, the median effective tax rate on these returns was only 28 percent.[88] Moreover, since these returns were selected on the basis of adjusted gross income, they do not include the returns of some persons with large incomes from tax-exempt interest or with income from mineral production that was offset by depletion deductions. On the basis of these considerations, it is argued, the degree of actual progression in the tax system should be strengthened, not reduced.

D. EFFECT ON RESOURCE ALLOCATION

Many of the differential provisions in the income tax which serve to contract the tax base were originally justified as necessary or desirable to achieve some specific economic or social objective. These efforts to use the tax law as a means of encouraging particular types of economic activity or personal expenditure have been criticized on the ground that they may result in a serious misallocation of resources and, therefore, prevent optimum development of the economy.

It is argued, for example—

> that if, because of tax differentials, a dollar invested in activity A will produce 20 cents before tax and 10 cents after tax, while a dollar invested in activity B will produce 15 cents before tax but 11 cents after tax, commonsense will induce any taxpayer to put his dollar in B rather than A. But since it is the pretax return which measures the relative value accorded by the economy as a whole to each of these investments, the tax law operates to produce a lower real value of product. While this argument is expressed in terms of investment activity, it applies equally well with respect to other types of economic activity.
>
> A common characteristic of preferential tax provisions, therefore, is that they tend to * * * result in resource use different from that which would otherwise be determined by the operation of the price mechanism in free markets. But since a fundamental philosophical and analytical assumption underlying a free market economy is that the operation of the impersonal market mechanism will result in the best allocation of resources, tax provisions which interfere with such allocations must necessarily involve a cost in terms of a lower total real value product for the economy as a whole.[89]

On the other hand, it is contended that the market mechanism does not always operate to produce socially optimum results. Monopoly elements and other limitations on the mobility of resources may prevent the market mechanism from directing resources into their

[87] Cf. Wallich, "Conservative Economic Policy," Yale Review, Autumn 1956.
[88] The Revenue Act of 1963, hearings before the Senate Committee on Finance, on H.R. 8363, 88th Cong. 1st Sess., pt. 1, pp. 278–282.
[89] Norman Ture, "The Costs of Income Tax Mitigation," proceedings of the 49th Annual Conference on Taxation sponsored by the National Tax Association, 1956, pp. 59–60.

most productive uses, or may undervalue some activities relative to others because of various structural or institutional limitations. Use of the taxing power to provide incentives for these activities to a greater extent than afforded by the market, it is maintained, does not impede but enhances economic progress.

Accordingly, it is contended that if the tax law is to be an effective instrument of public policy, it must be kept flexible in order to adjust to changes in economic conditions and priorities in public policy objectives. A rigidly uniform tax system might provide greater equity but would do so at the cost of other important objectives of public policy.

E. SIMPLIFICATION

Tax simplification is widely acknowledged as an important objective of tax reform, yet the revenue acts of recent years have generally added to rather than diminished the size and complexity of the tax code.[90] In part, this is the result of legislative compromises worked out over proposals for simplification which involved relatively large revenue losses or the realinement of individual tax burdens. In part, it is the result of a concern for assuring an equitable distribution of tax liabilities by modifying the law to take account of special situations.

The need for simplification is said to lie in the broad-based nature of the individual income tax and the fact that its efficient operation depends upon a general willingness of taxpayers to comply with the law by filing complete, timely tax returns. While existing enforcement procedures deal effectively with the relatively small number of deliberate evasion cases which presently occur, they would not be adequate if taxpayers in general were unable or unwilling to file competently prepared returns.

Furthermore, undue complexity is said to produce a misallocation of human resources. On the one hand, individual taxpayers must devote time to the preparation of their returns. On the other hand, talented individuals are engaged in the profession of tax return preparation. Only an expert, it is contended, can be sure to take account of all the relevant factors. From society's point of view, however, the time devoted to tax work on the part of highly trained individuals is a less than optimum use of available human resources.

Opposition to simplification generally arises over specific proposals made in that direction. Often such proposals would establish a degree of standardization which would conflict with widely accepted views of tax equity. Thus, it has proved virtually impossible to devise a simplified tax structure that would preserve the existing distribution of tax burdens and yet substantially maintain existing revenues.

A currently discussed simplification proposal would establish an alternative tax rate schedule for taxpayers who elect to forego special credits, exclusions, and deductions. One suggestion calls for a tax rate of 40 percent on the first $50,000 of "simplified" taxable income and a rate of 50 percent on any such income in excess of $50,000. Simplified taxable income is, with certain exceptions, the same as adjusted gross income. Such a proposal was considered and rejected

[90] The Individual Income Tax Act of 1944, which introduced the standard deduction, the uniform exemption, and other features, is a notable exception.

by the Senate Finance Committee during its deliberations on the Revenue Act of 1964.

Proponents argue that taxpayers electing this method would have little difficulty computing their tax since simplified taxable income would not take account of deductions and the like. The proposal was expected to appeal to high-income taxpayers for whom the individual savings afforded by simplified procedures would be most significant. Those skeptical of the proposal's benefits point out that some taxpayers would have to compute their tax under both the regular and alternative methods to discover which was most advantageous. Such a result would aggravate, not reduce, the problems of tax compliance. It is also argued that such an option would enable some high-income persons to reduce their tax burdens substantially with a resulting loss in tax equity. Finally, it is argued that the real need for simplicity exists at low-income levels where individuals tend to be less well informed and less able to employ others to prepare their returns. The proposal in question, it is pointed out, would not affect low-income taxpayers.

CHAPTER 3

CORPORATE INCOME TAXATION

I. Present Law

A. THE TAX BASE

The taxable income of a corporation is a statutory concept derived, in general, by deducting from gross income the expenses incurred in securing that income. To be deductible, expenses must be "ordinary and necessary" to the conduct of a trade or business.[1] Such expenses include wages and salaries, the compensation of executives, rents, repairs, bad debts, the cost of materials, casualty losses, taxes, advertising expenses, and interest payments. In addition, net operating losses may be deducted, subject to certain stipulations.[2] As a rule, the full cost of fixed capital equipment is not deductible in the year of acquisition but must be spread out as depreciation over the useful life of the asset in accordance with the methods specified in the law.[3] Corporations cannot deduct amounts paid out as dividends to shareholders, with the exception of certain dividends on the preferred stock of public utilities.[4] Since payments for interest, rent, royalties and the like are deductible, the corporate tax base, therefore, consists of the return to equity capital.

Corporations may, like individuals, deduct contributions to charitable institutions.[5] Deductible contributions may not exceed 5 percent of net income, but excess deductions in any one year may be carried over and applied against taxable income in each of the 5 succeeding years, if necessary. Contributions to profit-sharing plans and pension funds are deductible corporate expenses, subject to certain limits, if the plans are nondiscriminatory as regards the employees eligible to participate in them.[6]

Entertainment expenses are not deductible unless they meet certain requirements in addition to the "ordinary and necessary" criteria.[7] With the exception of certain expressly enumerated situations only that portion of entertainment expenses directly related to the active conduct of business is deductible. Lavish and extravagant expenditures may be disallowed as deductions. Deductions for business gifts are limited to $25 per individual per year. In any case, entertainment expenses must be substantiated by the taxpayer by means of fairly detailed records.[8]

The corporate tax base is affected by a number of provisions in addition to the general rules outlined above. These provisions include those which govern the tax treatment of certain special types

[1] Sec. 162.
[2] Sec. 172.
[3] Sec. 167. See cha 5, "Depreciation and the Investment Credit."
[4] Sec. 247.
[5] Sec. 170.
[6] Sec. 404.
[7] Sec. 274.
[8] Reg. 1.274-5.

of corporations and those which provide special treatment for certain types of income or expenditures. In most cases the latter are not restricted to corporations but apply to all businesses. Corporations, however, because of their predominant position in the economy, account for the largest share of the income affected by these provisions.

1. Special classes of corporations

(a) Tax-exempt organizations

Federal tax law exempts from tax a variety of corporations which qualify as nonprofit companies.[9] Such companies include those organized for charitable, religious, scientific, literary and educational purposes provided no part of net earnings inures to the benefit of any individual and the organization neither substantially engages in propaganda nor participates in political campaigns. Also exempt are labor and agricultural organizations, business leagues and chambers of commerce, voluntary employees' benefit societies, credit unions, recreational clubs, fraternal organizations, and local benevolent life insurance companies which are nonprofit in nature. Certain smaller mutual life insurance companies and farmers' producer cooperatives may also be exempt under certain circumstances.

Within recent years, provision has been made for the partial taxation of otherwise tax-exempt organizations which engage in profitmaking business operations which are not substantially related to their basic purpose.[10] Educational and charitable organizations, for example, are taxed on any unrelated business income.

(b) Insurance companies, mutual financial institutions, cooperatives, and regulated investment companies

Under the Life Insurance Company Income Tax Act of 1959 major changes were adopted in the taxation of life insurance companies which were previously taxed only on a portion of their net investment income.[11] A major feature of the 1959 act is a provision for taxing one-half of underwriting income when earned and the other half when distributed. In addition, investment income is now taxed under a new formula which measures the taxable margin of investment earnings on an individual company basis. Capital gains of these companies are also now subject to tax.

The Revenue Act of 1962 modified the tax treatment of mutual fire and casualty insurance companies. These companies are now taxed at regular corporate rates on their underwriting income as well as their investment income, with provision for deducting certain additions to a protection against losses account.[12] Mutual fire and casualty insurance companies with total annual receipts of less than $150,000 are tax exempt, however, and those with receipts of more than $150,000 but less than $500,000 may be taxed only on their investment income. Prior to 1962 all these companies were taxed on the greater of their investment income or 1 percent of their gross receipts.

[9] Sec. 501.
[10] Secs. 511–515.
[11] Secs. 801–820
[12] Secs. 821–826.

Insurance companies other than life or mutual companies are taxed at regular rates on their taxable income, as computed under special rules.[13]

Mutual and cooperative savings banks and mutual building and loan associations may deduct amounts paid or credited to the accounts of depositors. Prior to 1962 such institutions were virtually free of tax because they could also deduct additions to bad-debt reserves as long as the total of such reserves did not exceed 12 percent of the amount of total reserves plus surplus and undivided profits. The Revenue Act of 1962 restricted deductions by these institutions for additions to bad-debt reserves to amounts determined on the basis of experience to be a reasonable addition to a reserve against losses on loans, subject to certain limitations.[14]

Cooperatives may deduct dividends allocated to patrons provided at least 20 percent of the face value of such dividends is paid in cash. Patrons are taxable on dividends so distributed, and cooperatives are taxed on undistributed income.[15]

Regulated investment companies which meet certain specific requirements are treated as "conduits" of income and are taxed only on their undistributed earnings. To qualify for this treatment, the company must derive at least 90 percent of its gross income from dividends, interest, or gain from the sale of stock or securities. In general, at least 50 percent of the company's portfolio must consist of holdings no one which exceeds 10 percent of the voting securities of the issue or 5 percent of the assets of the regulated investment company. Exception is made to permit regulated investment companies furnishing capital for so-called development companies to hold more than 10 percent of the voting stock of such companies. No more than 25 percent of the value of the total assets of the regulated investment company may be invested in any one company or group of associated companies under the investment company's control. Finally, the investment company must distribute at least 90 percent of its ordinary income to its shareholders.[16]

Beginning in 1961, conduit treatment modeled after that for regulated investment companies is also provided for real estate investment trusts which meet certain tests as to sources of income, diversification of portfolio, and the provision of services to tenants of property owned by the trusts.[17]

2. Exclusions and special deductions

Eighty-five percent of the dividends received from a domestic corporation may be deducted from a corporation's gross income provided the total deduction does not exceed 85 percent of taxable income computed without regard to the deduction.[18] Complete exemption is provided under certain conditions for dividends received from another member of an affiliated group of corporations and for dividends received by a small business investment company. In the former case, the members of the affiliated group must forego the use of multiple surtax exemptions, make the same foreign tax elections, and comply with certain other regulations.

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13 Secs. 831–832.
14 Secs. 591–594.
15 Ch. 1, subch. T.
16 Secs. 851–855.
17 Secs. 856–858.
18 Secs. 243–246.

Special provisions also apply with respect to the income derived by a corporation from foreign sources.[19] Under certain conditions, tax on the income of foreign subsidiaries may be deferred until such income is remitted to the domestic parent company. A special deduction is granted to Western Hemisphere trade corporations, as defined in sections 921 and 922.

Corporations, like individual income-tax payers, may exclude from gross income the interest received on debt issues of States and localities.[20] Corporate receipts of such tax-exempt interest totaled $1.14 billion in 1961.

Businesses operating in the extractive industries may select one of two alternative methods for recovering capital costs. The cost of initial investment in a depletable property may be written off over the useful life of the mineral deposit or, alternatively, the deduction may be computed as a specified percentage of the gross income derived from the property, not to exceed 50 percent of the taxable income from the property computed without regard to depletion.[21] In the latter case percentage depletion allowances are not limited to the taxpayer's investment in the property, but may be claimed as long as the property produces income. In 1961, corporate deductions for percentage depletion totaled $3.6 billion.

Special treatment is also accorded certain capital costs incurred in exploring for or developing mineral properties. Such costs may be deducted either as current expenses or ratably as the minerals are sold, subject to certain limitations in the case of exploration expenditures.

3. Statutory and national income concepts of corporate net income

The concept of corporate profits employed in national income accounting differs in important respects from the statutory definition of taxable income. For the former purpose, corporate profits are, briefly, the earnings of corporations organized for profit which accrue to residents of the Nation, before Federal and State profits taxes. There is no allowance for depletion and capital gains and losses are not taken into account. Furthermore, the national income concept does not incorporate the earnings of certain mutual financial intermediaries, which are allocated to personal income as interest payments to individuals.

Whereas statutory corporate taxable income includes net long-term capital gains and losses, the profits of mutual financial intermediaries, and certain foreign earnings of U.S. firms, items not included in the national income definition, it also reflects certain deductions which do not measure costs in a strict accounting sense and excludes certain sources of income. A reconciliation of the two concepts is presented in the following table.

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[19] See ch. 8, "Taxation of Income From Foreign Sources."
[20] Sec. 103.
[21] Secs. 611–616. See ch. 6, "Taxation of Income From Natural Resources."

TABLE 10.—*Reconciliation of profits before taxes, U.S. Department of Commerce, with compiled net profit as tabulated by the Internal Revenue Service and taxable income as derived from the IRS tabulations, 1959–61*

[In millions of dollars]

	1959	1960	1961 (preliminary)
Profits before taxes, Department of Commerce	47,657	44,261	44,187
Add: Tax-return measures of:			
Profits of mutual financial intermediaries	829	899	896
Gains, net of losses, from sale of property	2,403	2,245	4,771
Domestic dividends received	2,948	3,084	3,276
Income received by U.S. corporations with respect to equities in foreign corporations and branches	2,854	3,063	3,852
Less: Income received from such equities by all U.S. residents, including individuals, net of corresponding outflows	1,793	1,880	2,321
Deduct:			
Post tabulation amendments and revisions, including allowance for audit profits	2,058	1,415	1,931
Depletion (tax deductible)	3,239	3,523	3,587
State income taxes on corporations	1,204	1,285	1,329
Profits of Federal Reserve banks	742	950	780
Equals: Compiled net profit, IRS, all active corporations	47,655	44,499	47,034
Add: Compiled net loss, IRS	4,805	6,828	6,445
Equals: Compiled net profit, IRS, all active corporations with net income	52,460	51,327	53,479
Deduct:			
Wholly tax exempt interest received	808	945	1,078
Dividends received deduction	3,399	2,020	2,147
Net operating loss deduction		1,286	1,497
Western Hemisphere deduction	214	213	215
Taxable income, subchapter S corporations (see p. 50, text)	605	678	904
Regulated investment company income	1,028	966	1,325
Add:			
Mutual insurance company income taxed at 1 percent rate	1,288	2,095	1,690
Errors and omissions	−46	−67	−65
Equals: Taxable income, Treasury Department	47,648	47,247	47,938

NOTE.—Reconciliation between Commerce profits and IRS compiled net profit, U.S. Department of Commerce; all other figures from IRS tabulations.

Source: Treasury Department, Office of Tax Analysis.

4. *Characteristics of the corporate tax base*

One of the most significant characteristics of the corporation income tax base is its volatility. While the total number of corporation income tax returns has increased substantially from year to year in the post-World War II period, short-run changes in total corporate income have been quite large and have tended to be greater than variations in national income. This variability in the corporate tax base is shown in the following table:

TABLE 11.—*Corporation income tax returns and net income, 1946–61*

[Dollar amounts in billions]

Year	Total number of returns [1]	Returns with net income [2]		National income	Total net income reported [3]	
		Number	Percent of total returns		Amount	Percent of national income
1946	491,152	359,310	73.2	$180.9	$25.2	13.9
1947	551,807	382,531	69.3	198.2	31.4	15.8
1948	594,243	395,860	66.6	223.5	34.4	15.4
1949	614,842	384,772	62.6	217.7	28.2	13.0
1950	629,314	426,283	67.7	241.9	42.6	17.6
1951	652,376	439,047	67.3	279.3	43.5	15.6
1952	672,071	442,577	65.9	292.2	38.5	13.2
1953	697,975	441,767	63.3	305.6	39.5	12.9
1954	722,805	441,177	61.0	301.8	36.3	12.0
1955	807,303	513,270	63.6	330.2	47.5	14.4
1956	885,747	559,710	63.2	350.8	46.9	13.4
1957	940,147	572,936	60.9	366.9	44.5	12.1
1958 [4]	990,381	611,131	61.7	367.4	38.5	10.5
1959 [4]	1,074,120	670,581	62.4	400.5	46.8	11.7
1960 [4]	1,140,574	670,239	58.8	414.5	43.5	10.5
1961 [4]	1,190,286	715,589	60.1	426.9	45.9	10.8

[1] Active corporations only.
[2] Before net operating loss deduction.
[3] All returns. Amount shown is total net income less total net deficit.
[4] Data include returns of subchapter S corporations.

Source: Internal Revenue Service: Statistics of Income, Corporation Income Tax Returns; Department of Commerce, Office of Business Economics.

Some smoothing of the fluctuations in the corporate income tax base results from the loss carryover provisions in the tax law. Losses may be carried back and offset against the taxable income of the preceding 3 years and carried forward as offsets against the taxable income of the succeeding 5 years. In effect, therefore, corporate income and losses may be averaged over a 9-year period.[22]

As shown in the following table, the bulk of taxable corporate income is concentrated in a relatively few large corporations. Of the 715,589 corporate returns with net income in 1961, 82.2 percent reported taxable incomes under $25,000. These corporations accounted, however, for only 6.8 percent of the aggregate net income reported. On the other hand, 4,238 companies with incomes above $1 million, or 0.6 percent of all corporations with net income, accounted for 71.0 percent of total corporate income. The volatility of the corporate income tax base is, therefore, attributable largely to changes in the profits of larger companies.

TABLE 12.—*Corporate returns and net income, by net income classes, 1961*

Net income classes	Returns with net income		Net income	
	Number	Percent of total (cumulative)	Amount (thousands)	Percent of total (cumulative)
Under $25,000	588,202	82.2	$3,550,564	6.8
$25,000 under $50,000	65,357	91.3	2,162,890	10.9
$50,000 under $100,000	29,629	95.5	2,044,684	14.8
$100,000 under $250,000	18,232	98.0	2,799,558	20.1
$250,000 under $500,000	6,516	98.9	2,267,590	24.4
$500,000 under $1,000,000	3,415	99.4	2,377,039	29.0
$1,000,000 and over	4,238	100.0	37,199,003	100.0
Total	715,589		52,401,331	

Source: U.S. Internal Revenue Service: Statistics of Income—1960–61, U.S. Business Tax Returns.

[22] Sec. 172.

B. TAX RATES AND TAX CREDITS

1. Normal and surtax rates

In general, the corporate income tax consists of a normal tax on the full amount of taxable income and a surtax on the amount of taxable income in excess of a $25,000 surtax exemption.[23] In 1964 and later years the normal tax rate is 22 percent. The surtax rate is 28 percent in 1964 and 26 percent in later years, for a combined rate of 50 percent in 1964 and 48 percent in later years. For the calendar years 1952 through 1963, the normal tax rate was 30 percent and the surtax rate was 22 percent, for a combined rate of 52 percent on corporate taxable income in excess of $25,000. Effective tax rates at various taxable income levels are shown in the following table for the years 1954–65.

TABLE 13.—*Effective corporation tax rates at various taxable income levels, 1954–65*

Taxable income	Effective rate of tax (percent)			Taxable income	Effective rate of tax (percent)		
	1954–63	1964	1965		1954–63	1964	1965
$5,000	30.00	22.00	22.00	$250,000	49.80	47.20	45.40
$10,000	30.00	22.00	22.00	$500,000	50.90	48.60	46.70
$25,000	30.00	22.00	22.00	$1,000,000	51.45	49.30	47.35
$50,000	41.00	36.00	35.00	$10,000,000	51.95	49.93	47.94
$75,000	44.67	40.67	39.33	$100,000,000	51.99	49.99	47.99
$100,000	46.50	43.00	41.50				

The rate reductions provided by the Revenue Act of 1964 interrupt a previously evident general upward trend in corporate tax rates. Following the 1913 law, corporate tax rates were increased gradually to 12 percent in 1918 and ranged from 10 to 13½ percent during the 1920's. In 1936 graduated rates were introduced, ranging from 8 to 15 percent and supplemented by a surtax on undistributed profits ranging from 7 to 27 percent. The undistributed profits tax was repealed in 1938 and graduation in rates was limited to corporations with net incomes of $25,000 or less.

Tax rates ranging from 25 to 40 percent were imposed throughout most of World War II. These were supplemented by an excess profits tax which for the income years 1943–45 brought the maximum combined effective tax rate to 80 percent. In the years 1946–49, effective rates ranged from 21 to 38 percent.

Beginning with the income year 1950, the system of graduated rates for corporations with taxable incomes of less than $25,000 was replaced with a single normal tax rate applicable to the full amount of taxable income and a surtax applicable to taxable income in excess of a specific $25,000 surtax exemption. Under the impetus of the revenue requirements of the Korean emergency, normal and surtax rates were increased and were supplemented by an excess profits tax of 30 percent, subject to an overall effective rate ceiling of 70 percent. The excess profits tax expired on December 31, 1953.

2. Long-term capital gains

Long-term capital gains realized by corporations may be taxed at the alternative rate of 25 percent.[24] By statutory definition such

[23] Sec. 11.
[24] Sec. 1201.

gains arise from the sale or exchange of capital assets held by the taxpayer for more than 6 months. Capital assets are defined as any property held by the taxpayer except such assets as merchandise and depreciable and real property used in the trade or business.[25]

Capital gains tax treatment has been extended to special types of income not otherwise defined as gains arising from the sale of capital assets. Such income includes profits, in certain cases, from the sale of depreciable and real property, profits from the sale of certain draft, breeding, or dairy livestock, coal and iron ore royalties, income from timber cutting operations, and profits arising from the sale of unharvested crops on land sold or exchanged, subject to certain limitations. Any net losses realized in connection with these sources of income are deductible in full against other sources of taxable income. Net gains from these special sources of income are estimated to have totaled $2.2 billion in 1960.

3. Tax credits

A major feature of the Revenue Act of 1962 was a credit against income tax liability based on expenditures for depreciable machinery and equipment used in a trade or business located in the United States.[26] The credit is equal to 7 percent of qualified investment (3 percent of such investment in the case of public utilities).

Corporations with income derived from foreign operations may, under certain conditions, credit foreign taxes paid against their U.S. tax liability.[27]

4. Subchapter S corporations

Certain corporations, under subchapter S of chapter 1 of the Internal Revenue Code, may avoid the payment of the corporation income tax if all shareholders consent to the taxation of the corporation's income at the shareholder level. To qualify for this treatment, a corporation must be a domestic corporation with no more than 10 shareholders, each of whom must be an individual (or an estate) and no one of whom may be a nonresident alien. The corporation must have only one class of stock and may not be a member of an affiliated group eligible to file a consolidated return. The corporation may not receive more than 20 percent of its gross receipts from rents, royalties, dividends, interest, annuities, and gains from sale or exchange of stocks and securities, nor may it receive more than 80 percent of its gross receipts from sources outside the United States.

5. Corporations assessed additional taxes

Special provisions have been enacted in an effort to prevent tax avoidance through the use of the corporate form. In the absence of these provisions, high bracket individual taxpayers, and some corporations, might be able to avoid paying tax at the higher rates which would normally apply to their income by channeling income into, and accumulating income in, controlled corporations.

A corporation that accumulates earnings in excess of the "reasonably anticipated" needs of the business may be required to pay tax on such excess, in addition to the regular normal and surtax, at a rate of 27½ percent on the first $100,000 of accumulated taxable income

[25] Ch. 1, subch. P. See ch. 4, "Capital Gains Taxation."
[26] Sec. 38. See ch. 5, "Depreciation and the Investment Credit."
[27] See ch. 8, "Taxation of Income from Foreign Sources."

and at a rate of 38½ percent on any such income remaining. Accumulated taxable income is taxable income adjusted, primarily, to allow deductions for dividends paid to shareholders and for Federal income and excess profits taxes paid, and to disallow any deduction for dividends received. A credit is allowed for the amount of earnings and profits retained to meet the reasonable needs of the business. The penalty tax is not imposed, however, unless the accumulated surplus exceeds $100,000. The Commissioner of Internal Revenue generally bears the burden of proof regarding improper accumulations.[28]

A tax at the rate of 70 percent is imposed on the undistributed income of companies defined under the law as personal holding companies. In general, a corporation is adjudged a personal holding company if its personal holding company income—dividends, interest, royalties reduced for depletion deductions, rents reduced by depreciation, taxes and interest, and certain other types of income—equals 60 percent of more of its gross income reduced by the amount of deductions for depreciation, depletion, interest and taxes.[29] Furthermore, the corporation must be controlled by not more than five individuals. Certain types of corporations, such as life insurance companies and finance companies, are exempt from these provisions.

Shareholders in foreign personal holding companies, as defined by law, are required to include the undistributed as well as distributed income from such corporations in their individual taxable incomes.[30]

C. CORPORATE REORGANIZATIONS

Gains arising out of corporate reorganizations are treated under special provisions intended to minimize tax barriers to normal business adjustments which involve transactions that do not basically alter the continuity of an economic interest. The relevant provisions of the taxing statute, contained in chapter 1, subchapter C of the code, provide detailed rules for a series of specified transactions which may be completed without tax hindrance.

1. *Corporate organizations*

A person (or persons) may form a corporation without immediate tax consequences by transferring property to the newly organized corporation and receiving its stock in exchange, provided the person (or persons) transferring the property owns 80 percent of the stock of the new company. This provision provides the vehicle under which the typical sole proprietorship or partnership is incorporated.

2. *Corporate reorganizations—recapitalizations*

A corporation may, without any immediate tax consequences, readjust its financial structure through a recapitalization. Typical tax-free recapitalizations include the exchange of existing preferred stock for new common stock, one class of common for another class of common, and existing bonds for new bonds. It is necessary, however, that a business purpose germane to the conduct of the corporate enterprise form the basis for the transaction. If no business purpose underlies the transaction and it in fact masks a device by which a disguised dividend is distributed, it will be treated in accordance with its true nature. For example, the exchange of existing

[28] Secs. 531–537.
[29] Secs. 541–547.
[30] Secs. 551–558.

common stock for new common stock and bonds would be treated, to the extent of the fair market value of the bonds, as the distribution of a corporate dividend, since the shareholders control the corporation before and after the transaction. Similarly the distribution of a preferred stock dividend or the emergence of preferred stock in a recapitalization together with a sale of such preferred and its redemption, i.e., the so-called preferred stock bailout, is taxed as if the corporation had declared a dividend to its shareholders.

3. Corporate reorganizations—mergers and consolidations

The law permits shareholders of one corporation, as part of a merger or acquisition, to exchange without tax consequences their shares for shares of a new corporation which has acquired the assets or stock of the corporation of which they were shareholders. Similarly two corporations may consolidate by pooling their assets and issuing to the shareholders of both of the old corporations stock in the new company.

In order to assure that the foregoing transactions are treated in a tax-free manner, two requirements, based on judicial interpretation, must be met:

(1) The transaction must have a business purpose as its basis; and

(2) The shareholders of the corporation which disappeared by reason of the merger or consolidation must have a continuity of interest in the corporation which survives.

The so-called continuity of interest test insures that a purchase and sale of corporate assets will not be disguised in the form of a corporate reorganization. Thus, if all of the shareholders of a corporation exchange their stock solely for bonds of the acquiring company, the continuity of interest requirement will not be met for, in effect, they have "sold" their interest to the new company. Under these circumstances, tax is imposed at the time of the exchange.

4. Corporate reorganizations—corporate separations

It is also possible to divide a corporation into two or more of its functiong economic components without any immediate tax effects. For example, a corporation engaged in two separate active businesses may separate into two corporations by separately incorporating one of its businesses and distributing the stock of the new company to its shareholders. Similarly, a corporation which owns a subsidiary engaged in business with the general public may distribute the stock of that subsidiary to its shareholders.

In order to accomplish a tax-free corporate separation, a multitude of complex statutory requirements must be met, involving the nature of the businesses, the manner of stock distribution, etc. Under certain circumstances, the law permits the division of existing corporations through the divestiture of their subsidiaries or businesses for bona fide corporate reasons. Such a transaction may result in removal of corporate earnings at the capital gains rate through the distribution of stock and the later sale of that stock.

5. Corporate liquidations

The statute also provides special rules governing the termination of a corporation through liquidation. Unlike the corporate organization and reorganization provisions, these rules provide for taxation to the shareholder at the time of liquidation. Thus, when the shareholder surrenders his shares for cancellation or retirement and receives corporate assets in exchange, taxes are payable at capital gains rates, generally, on the difference between the value of the assets received by the shareholder and the cost to him of the stock surrendered. Other special rules, however, permit the simplification of the corporate structure by allowing the tax-free liquidation of a subsidiary into its parent.

D. TAXPAYMENT

Prior to 1950, corporate income tax liabilities were paid in four equal installments in the 3d, 6th, 9th, and 12th months following the close of the tax year. This payment timetable has been gradually advanced under later revenue acts so that by 1970 that portion of a corporation's estimated liability in excess of $100,000 will be paid in four quarterly installments during the taxable year.

The Revenue Act of 1950 provided for the payment of corporate liabilities in two installments in the first two quarters of the year following the tax year. The transition to this timetable was accomplished in stages over a 5-year period. Under the Revenue Act of 1954 corporations were required to pay half of their estimated liabilities in excess of $100,000 in the last half of the current year and the remaining liability in two installments in the first 6 months of the succeeding year. Again, the transition was accomplished in a 5-year period.

The Revenue Act of 1964 contains a provision designed to place corporations on a payments basis which is more akin to that of individuals. That portion of a corporation's estimated liability which exceeds $100,000 will, when the 7-year transition period is completed, be paid in equal quarterly installments during the tax year.[31] The following table illustrates the manner in which the transition will be accomplished. Any tax due at the time of filing the corporate tax return (March 15 for a corporation with a calendar year accounting period) is due in two installments in the third and sixth months following the close of the tax year.

TABLE 14.—*Corporate taxpayment schedule for estimated tax in excess of $100,000 a year, 1964–70*

	Percent of estimated tax to be paid on the 15th day of the—				Percent of tax to be paid on the 15th day of—	
	4th month	6th month	9th month	12th month	3d month	6th month
	of the year of liability				of the year following the year of liability	
1964	1	1	25	25	24	24
1965	4	4	25	25	21	21
1966	9	9	25	25	16	16
1967	14	14	25	25	11	11
1968	19	19	25	25	6	6
1969	22	22	25	25	3	3
1970 and any subsequent year	25	25	25	25	(1)	(1)

1 Payments will still be due on these 2 dates with respect to the first $100,000 of tax liability and with respect to any underestimated income.

Source: Treasury Department, Office of Tax Analysis.

31 Sec. 6154.

II. Issues

A. THE INCIDENCE OF THE CORPORATE INCOME TAX

The debate over the proper place of the corporate income tax in the revenue system is complicated by disagreements over who actually bears the final burden of the tax. According to one view, corporations are able to shift a substantial share of the tax onto other sectors of the economy. Proponents of this view generally maintain that most of the tax is shifted forward onto consumers by means of upward price adjustments, while much of the remaining burden is shifted backward in the form of lower payments to the factors of production. From this standpoint, the corporate income tax is essentially a sales or wages tax.

A second view holds that the tax is not shifted to any significant extent, at least in the short run. It is argued that the determination of the most profitable price and output levels in the short run is not affected by variations in the rate of tax on profits. This conclusion follows directly from the analysis of price determination presented in conventional economic theory. This analysis demonstrates that the most profitable level of output for a firm is the one at which the incremental cost of the last unit produced is just equal to the addition to revenue which the sale of that unit brings about. Since profits are not an element of the incremental cost, in this analysis, the determination of the proper level of output is unaffected by a tax on profits. Proponents of this view generally concede, however, that over the long run the corporate income tax may tend to curtail the amount of corporate equity investment and, therefore, to affect the price structure.

Those who believe the tax is shifted point out that many businessmen have stated that they look upon the tax in the same manner as their other costs of doing business. Proponents of this view also cite studies which have indicated that the after-tax rate of return on invested capital has remained fairly constant since the 1920's. The stability of this measure, it is argued, over a period in which corporate income tax rates were sharply increased suggests that the tax was shifted. On the other hand, those who doubt that corporations are able to avoid the burden of the tax point out that other studies have shown that the ratio of before-tax profits to the gross national product originating in the corporate sector has remained stable during the same period of time. If the tax had been shifted, it is argued, this ratio would have increased as corporate tax rates were increased. While the divergence between the two measures can be explained by changes in capital-output ratios, the tax incidence problem is left unresolved.[32] Nor have recent studies employing econometric techniques settled the question.[33]

Many observers have taken an intermediate position. For example, it has been contended that the extent to which the tax is or is not shifted varies among different business firms depending on such factors as the degree of competition in the industry, price policies,

[32] See Richard E. Slitor, "The Enigma of Corporate Tax Incidence," Public Finance, XVIII, 1963, pp. 330, 348-349.

[33] Compare Marian Krzyzaniak and Richard A. Musgrave, "The Shifting of the Corporation Income Tax, an Empirical Study of its Short-Run Effect Upon the Rate of Return," the Johns Hopkins Press, Baltimore, 1963, with Challis Hall, "Direct Shifting of the Corporation Income Tax in Manufacturing," the Papers and Proceedings of the Annual Meeting of the American Economic Association, Dec. 27-29, 1963, pp. 258-271.

and the general business situation. The only general conclusion possible in this view is that the tax falls to some extent on consumers and to some extent on corporate shareholders.[34]

B. RELATIVE EMPHASIS ON CORPORATE INCOME TAXATION

The proper role of the corporate income tax in the Federal revenue system has long been a subject of debate among students of taxation. Currently this debate is focused on the proposal that the corporation income tax be replaced in whole or in part by a manufacturers' sales tax of the value added type; that is, by a tax based upon the gross receipts of a business less the cost of materials used in production. Proponents argue that such a proposal would improve the efficiency of resource allocation, promote an increase in the economy's rate of growth, and lead to an improvement in the balance of payments. Opponents dispute these claims and counter that acceptance of the proposal would have seriously adverse effects on tax equity.

With regard to resource allocation, it is contended that the corporation income tax is in essence an excise tax on corporate equity capital.[35] It is pointed out that the burden of the tax does not fall on the return to debt capital used by corporations or on the return to capital invested by unincorporated businesses. Rather, the tax is absorbed by the return to corporate equity capital. As a result, it is argued, the tax promotes adjustments in the ratio of capital and labor used in various firms and in the relative prices of the products of these firms. The extent of these adjustments depends on the nature of the demand for the products of the relatively heavily taxed and relatively lightly taxed firms and the ease with which resources can be shifted between such firms. The final result, it is contended, is the equalization of after-tax rates of return to equity capital in all industries. Pretax rates of return, however, tend to be higher in those firms which employ relatively large amounts of corporate equity capital than in those firms which employ little or no corporate equity capital. Investment in industries where unincorporated firms predominate, as in agriculture, and in industries where debt-laden capital structures are typical is said to be greater, and investment in industries which require large amounts of corporate equity capital less, than it would be in the absence of the corporation income tax or in the presence of a tax whose base encompassed the return to all business capital. It is contended that such a distribution of investment and consumption differs from the optimal distribution which would otherwise exist. The result of the present tax, it is contended, is a net loss in productive efficiency which was estimated to total $1.5 billion annually in the period 1953–55.

In reply to this argument, it has been pointed out that the analysis assumes that the burden of the corporation income tax is not shifted. To the extent that this assumption is at variance with actual experience, the conclusions must be modified. Moreover, any estimate of the magnitude of the resource allocation effects is held to be highly conjectural.

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34 Dan Throop Smith, "Federal Tax Reform," McGraw-Hill, New York, 1961, pp. 191 ff.

35 Arnold C. Harberger, "The Corporation Income Tax: An Empirical Appraisal," Ways and Means Compendium, pp. 231–250.

Those who are opposed to a substantial reduction in the role of the corporation income tax contend that even if the present tax does result in a loss of productive efficiency, this consideration is outweighed by questions of tax equity. It is argued that the corporation income tax must remain an essential component of the Federal revenue system as long as capital gains are taxable to individuals only as they are realized. It is pointed out that the increase in the market value of corporate stocks reflects, in part, the acccumulation of retained earnings. For individual taxpayers subject to marginal tax rates higher than 48 percent, the corporation provides a partial tax shelter. If the corporation income tax were removed, this shelter, it is contended, would become a tax-free sanctuary for individual stockholders.

A second argument in support of proposals to substitute a value-added tax for the corporation income tax concerns effects on economic growth. Central to this argument is the view that more rapid growth requires the diversion of a larger share of current output to capital formation and the conclusion that this requires an increase in the national savings rate. A shift from the tax on corporate profits to a sales tax, it is contended, would lead to an increase in saving, release a larger share of current output from the production of consumption goods, and promote the expanded production of capital goods. In answer to those who argue that a sales tax capable of producing as much revenue as the corporate income tax would of necessity fall as heavily on aggregate community saving as an income tax, proponents contend that reducing the tax on corporate savings would encourage the expansion of the more efficient firms since retained earnings are a major source of the capital for expansion.

In recent years the major argument advanced by opponents of such proposals involves the effect they would have on the level of employment and production. This argument is centered on the opinion that the performance of the economy in much of the period since 1957 has demonstrated a deficiency in the aggregate demand for goods and services. Substitution of a sales tax for an income tax, it is contended, is likely to reduce the demand for consumer goods and impede the attainment and maintenance of full employment. Those who accept this argument contend that the business community has ample resources to finance new investment, partly as a result of such developments as depreciation reform and the investment tax credit. It is argued that greater investment would be encouraged more by evidence of the existence of an active market for the products which would be produced by expanded capacity than by an increase in the supply of investable funds.

This argument rests on the further conclusion that the economy contains sufficient unused capacity to permit an increase in the output of capital goods without a reduction in the output of consumption goods. This assumption has been challenged by observers who point out that a large proportion of the capital resources said to be idle are obsolete while much of the available idle manpower is unfit for the demanding requirements of the modern labor force. Thus it is said statistics on unemployment and capital utilization are often misleading; a substantial increase in the production of capital goods will lead to inflation unless consumption levels are restrained.

It is also argued that the sensitivity of the corporate income tax yield to changes in economic conditions makes it an important element in countercyclical fiscal policy. The appraisal of proposals for basic changes in the role of corporate income taxation, therefore, must consider their likely impact on the overall effectiveness of the tax system's contribution to stability and growth. Finally, it is argued that any adverse effects which may be created by the present corporation income tax could be eliminated by structural reforms such as the investment tax credit. To justify a reduced role for the corporation income tax and the introduction of a broad-based sales tax, it is contended, proponents must demonstrate that it is the very basis of the tax and not its particular features that produce any detrimental economic effects.

Support for proposals favoring the substitution of a value-added tax for the corporation income tax has also been engendered by concern over the balance-of-payments position of the United States. It is pointed out that under the terms of the General Agreement on Tariffs and Trade, to which the United States is a signatory, indirect taxes on exported items may be rebated and compensating taxes may be imposed on imported items. No such adjustments, however, may be made with respect to corporate income taxes. The rebate on exported items enables foreign exporters, it is argued, to sell goods in foreign markets below domestic prices while the equalization tax on imports serves to raise the price of U.S. goods sold in foreign markets. Some of those who feel that the present situation discriminates against our exports urge that we meet the situation by adopting a tax structure similar to those of our international competitors.

Central to the issue is a decision on the manner in which the burdens of a corporate income tax and a sales tax are distributed, and, therefore, the effects of the separate taxes on prices and resource allocation. The GATT position assumes, at least implicitly, that sales taxes are fully passed on, in the form of higher prices, to consumers of the taxed products while income taxes are entirely absorbed by corporate shareholders. Whereas the GATT position has been criticized for assuming 100 percent shifting in the case of a sales tax and zero shifting in the case of an income tax, no consensus can be said to exist on the proper assumption which should be made. In the absence of such a consensus, there are wide differences regarding the extent to which a shift to indirect taxes would affect the price of U.S. exports.

Apart from questions on the degree to which existing taxes are reflected in the prices of products traded, there is debate on the effect that tax measures would have on the balance of payments. It is pointed out that exports of U.S. goods and services have regularly exceeded imports throughout the postwar period. Balance-of-payments deficits, it is said, are traceable to capital flows and to Government operations. It is contended, therefore, that efforts to redress balance-of-payments deficits should concentrate on these transactions and not on the flow of trade. Others argue, on the other hand, that a further widening in the favorable trade balance would grant U.S. investors greater freedom to invest capital abroad and the Government greater flexibility in the pursuit of foreign policy objectives.

C. SPECIFIC PROBLEMS IN CORPORATE INCOME TAXATION

1. *Dividend distributions*

The proper treatment of dividend distributions is a longstanding issue of corporate income taxation. The provisions of existing law are frequently said to impose a double tax burden on dividends. They are also said to discourage equity financing by corporations and to promote debt financing and the retention of earnings by such enterprises.

(*a*) *The double taxation of dividends.*—It is contended that the present tax treatment of dividends is inequitable because the tax law imposes a severe double tax on this form of income. According to this view, the individual stockholder's share of corporate income is taxed twice, once in the hands of the corporation and again when distributed as a dividend. Moreover, in the absence of relief provisions, the burden of double taxation is particularly heavy for low-income dividend recipients. For example, the combined corporate and individual income tax on a dollar of corporate income (at 1965 rates and disregarding the dividend exclusion) is about 84 cents for a top-bracket individual—about 14 cents above his individual liability alone—and nearly 55 cents for a first-bracket shareholder—about 41 cents greater than the tax payable on a dollar of his wage income.

Opponents of special relief for dividend income argue that the extent of alleged double taxation is greatly exaggerated. On the one hand, it appears likely that the burden of the tax, or at least a substantial portion of it, is passed on to consumers or wage earners in the form of higher prices and lower wages, in which case no double tax problem exists. Furthermore, even if the tax is not passed on, stockholders, it is claimed, do not base their decisions with respect to stock purchases on pretax corporate earnings per share, but rather on after-tax earnings available for distribution. Accordingly, it is argued, shareholders take full account of the corporate income tax in determining the price they will offer for a corporation's stock. Having discounted the corporate tax in the purchase price of the stock, shareholders are subject only to the individual tax on distributed corporate earnings. The added burden of the corporate tax, therefore, is limited to those who purchased stock before an increase in taxes. Because of the high turnover in corporate shares, this double tax burden tends to be concentrated among older shareholders with inactive portfolios. Even in such cases, however, this burden may be mitigated by the fact that taxes tend to be increased under inflationary conditions which tend to drive stock prices up and thus offset, at least in part, the fall in stock prices which otherwise would result from discounting the increased corporate tax.

(*b*) *Effect on equity financing.*—The present tax treatment of dividends has also been criticized as imposing a bias against equity financing by corporate enterprise. This bias is said to exist because dividend payments to stockholders are not deductible by the corporation while interest payments on borrowed capital are deductible. This situation, it is argued, induces an undue concentration on debt financing which may significantly circumscribe a company's willingness to undertake new and relatively risky ventures and limit its ability to adjust readily to changing business conditions. Thus, at a time of adverse business conditions, the heavily debt-laden corporation may find the required adjustments particularly difficult, or even impossible.

In reply to this argument, it is contended that tax considerations generally are not dominant in determining the form of financing sought by corporate enterprise. It is argued that one of the principal limitations on equity financing stems from the desire on the part of existing shareholders to avoid the dilution of their interest through additional equity issues. Furthermore, it is maintained that the character of the market for the supply of capital funds is another important factor in determining the form of corporate financing. This market, it is claimed, is dominated by institutional investors such as commercial banks, savings banks, insurance companies, and trusts which are generally restricted, either by legal requirements or by traditional investment practice, to low-risk securities. It is also asserted that the adverse effects of debt financing on the willingness of corporations to undertake risky investments allegedly induced by tax considerations are greatly exaggerated. In this connection, it is pointed out that many of the most highly speculative ventures are financed with very thin equity and that, indeed, it is the prospect of realizing substantial net returns on this equity through the leverage afforded by debt financing which primarily impels this type of investment.

It is also pointed out that a large proportion of the capital funds raised by corporations is secured through the retention of earnings. Taking such funds into account, it is argued, no significant overemphasis on debt issues is observable in the typical corporate financial structure. Critics of the present treatment of dividend income contend, however, that this observation does not refute their views. The existence of double taxation encourages the retention of earnings as well as debt financing, and therefore the relationship between these two types of financing is irrelevant. The important consideration is the ratio between equity financing and other types of financing. Furthermore, the existing composition of corporate financing does not indicate the heavy weight given to the existence of double taxation when methods for financing new ventures are considered.

Developments in corporate financing since the end of World War II do not offer convincing evidence with respect to the impact of income taxation on corporate financial policy. In 1946 corporations obtained $22 billion in new funds and in 1962, $58 billion. Internal sources, retained profits and depreciation, accounted for 52 percent of these funds in 1946 and 60 percent in 1962. The sale of corporate stock accounted for 6 percent of the funds in 1946 and 4 percent in 1962. Debt issues, including bonds, accounted for 13 percent of the funds obtained in 1946 and 14 percent in 1962. Year-to-year changes in the composition of corporate funds, indicated in appendix table 47, do not appear to be systematically related to changes in corporate tax rates or to changes in or the enactment of important tax provisions, such as the dividend credit and exclusion. It is pointed out, however, that this may be due to the relatively small amount of relief provided from the so-called double taxation of dividends by the law up to this time.

(*c*) *Proposals*.—Some relief from the double taxation of dividends was provided from 1913 to 1936 due to the fact that dividends were not subject to the normal tax assessed individuals. Between 1936 and 1954, no such relief was provided. The Internal Revenue Code of 1954 revised this position by introducing the dividend credit and exclusion. From 1954 to 1963 dividend recipients were permitted to exclude the first $50 of dividends from their gross income and to credit against tax liability an amount equal to 4 percent of dividends not excluded. The Revenue Act of 1964 provided for the repeal of the dividend credit and increased the exclusior to $100 per taxpayer ($200 for a married couple).

Proponents of the dividend credit and exclusion provisions contend that they provided partial relief from the double taxation of dividends in an administratively feasible manner. In combination, the two features provided proportionately greater relief to low-income investors than to dividend recipients at high-income levels. It was pointed out, for example, that individual income tax liabilities on dividend income were completely eliminated for taxpayers who received an amount of dividend income equal to or less than the exclusion while the reduction in tax was limited to 4 percentage points with regard to dividend income in excess of the exclusion, regardless of the total income of the recipient. It was also argued that, to the extent the corporate income tax is shifted forward to consumers, the provisions constituted a measure of relief from what is, in effect, a sales tax. Finally, the provisions, it is contended, removed a measure of the bias against corporate equity financing caused by the double taxation of dividends.

Critics of the dividend credit and exclusion argue that, even if the stockholders share of corporate savings are subject to double taxation, the dividend-received credit was an inequitable method for providing relief. The credit, it was pointed out, limited the combined corporate and individual income tax on a dollar of corporate earnings to 93.76 percent at 1963 rates, for a top bracket taxpayer, or only 2.76 percentage points more than his liability on a dollar of salary income. In the case of the first-bracket taxpayer, however, the credit left a combined tax of 59.68 percent on a dollar of corporate earnings, as compared with a 20-percent tax on income from other sources. In effect, therefore, apart from the dividend exclusion, the dividends-received credit removed 41 percent of the alleged double tax for the taxpayer in the highest bracket but only 4.6 percent of the double tax for a first-bracket taxpayer. Supporters of the provision point out, however, that the above criticism is based on one manner of viewing the credit. From another standpoint, the credit can be viewed as granting the same dollar relief from double taxation for a given amount of dividends at all taxable income levels. Furthermore, it is argued that any undesirable features of the credit could have been corrected; outright repeal was not required.

Critics also contend that the credit and exclusion were ineffective as offsets to any bias created against equity financing. It is pointed out that the provisions did little to alter the attractiveness of various methods of raising capital from the corporation's standpoint. In the latter connection the crucial factor is that interest may be deducted as a corporate expense while dividend distributions are not deductible for tax purposes.

Aside from the dividend exclusion and credit provisions, two basic alternative proposals have been offered for revision of the tax treatment of dividends. The first of these is based on the concept of the public corporation as a separate economic entity rather than merely an agency for its stockholders. Under this concept, the form of the contract by which the corporation acquires financial resources is not relevant in determining the tax treatment of payments made for these resources. Since the tax law permits deductions for virtually all resource payments, a deduction should also be allowed for payments which take the form of dividend distributions. Allowing a deduction for dividends paid, it is argued, would eliminate an illogical bias (however significant it may be in practice) against the acquisition of external financial resources through the issue of new stock. Moreover, it would impel more liberal dividend distribution policies and, therefore, increase the dependence of corporate enterprise on external funds for financing growth and new ventures. Such dependence should be encouraged, it is contended, to secure more frequent and more objective appraisals of the relative value of alternative investment programs and, therefore, to assure the best possible allocation of investable resources.

This proposal has been opposed as representing an undue interference by the tax system in the financial policies of corporations. Since allowing a deduction for dividends would mean that the corporation would pay a tax only on retained earnings, the corporate income tax would be converted into an undistributed profits tax. As such, it would impose heavy pressure on management to distribute earnings without due reference to the corporation's financial requirements. It would, moreover, result in a shift in the distribution of the total corporate income tax burden to small and new companies whose dependence on retained earnings is relatively great.

In answer to these arguments, it is pointed out that the deductibility of dividends would permit an increase in both the amount of dividend distributions and the volume of retained earnings out of any given amount of corporate profits with the present tax rate. Moreover, the relative shift in corporate tax burden to small and new companies might be avoided or limited by increasing the surtax exemption or by effecting some equivalent revision.

The second basic alternative is modeled after the treatment of dividends in the United Kingdom. Under this approach, the corporate tax, or a portion thereof, would be regarded as the shareholder's individual income tax liability withheld at source on his share of corporate earnings. On the individual's personal return the actual amount of dividends received would be "grossed up" to account for the tax withheld at the corporate level, tax liability would be computed on the basis of this gross amount, and a credit would be taken against the individual's tax for the tax paid by the corporation. For example, if 20 percentage points of the present corporate tax were regarded as individual income tax withheld at source, a dividend receipt of $100 would be grossed up by the recipient to $125. The individual's liability would be computed on the basis of the $125 and a $25 credit against the final tax would be allowed.

Proponents of this approach urge that it would substantially overcome the tax bias against equity financing. The grossing up feature would preclude an individual credit in excess of the double tax involved and would remove the same proportion of the double tax on dividends, regardless of the size of the withholding percentage or the tax bracket of the dividend recipient. On the other hand, it is argued, this approach is unduly complicated, would potentially involve a large revenue loss, and is only remotely related to the basic discrimination at the corporate level against equity financing.

2. Taxation of small and new business

A continuing issue in corporate income taxation concerns the relative impact of the tax on small and new businesses as compared with large and established firms. It is generally conceded that vigorous small business enterprises are vitally important to a healthy, competitive economy. Of particular importance is the rate at which new businesses are formed and their ability to survive and to become established as successful business units.

In general, the basic problems associated with small and new businesses are thought to stem from their difficulty in securing the financial resources required for growth and development. In the case of the new business, the principal difficulty, it is alleged, lies in securing the capital needed to tide the company over the formative and development stages to the point at which profitable operations begin. In the case of the established small business, the major problem, it is contended, is to obtain a supply of capital adequate at least to maintain the company's position in its industry and at terms favorable enough to permit it to resist the inducements offered for absorption into larger business units. The sources of these difficulties are generally identified as the inaccessibility of the market for equity funds, the differentially burdensome terms upon which credit (particularly long term) may be obtained, and the inadequacy of retained earnings and capital recovery allowances.

The Federal tax structure has been criticized as failing to make a positive contribution to the promotion of new and small business and even as contributing to a decline in the relative importance of small business in recent years. These criticisms have embraced virtually the entire Federal revenue system but have been directed with particular emphasis against the tax treatment of capital gains and losses, estate and gift taxes, and the corporation income tax. Particularly with respect to the latter, numerous proposals have been made either to provide deliberate tax advantages to small and new business as an offset to some of their nontax disadvantages or to remove what are regarded as inherent discriminations in the law.

An opposing view holds that the requirements of small and new businesses can best be met by general improvements in the economic climate rather than by special tax treatment. According to this view, general fiscal and monetary policies contributing to a steady and strong growth in total demand, while avoiding inflationary excesses, are more likely to provide the conditions under which new business opportunities are abundant than would any differential tax treatment consistent with the basic standards of a good tax system. More vigorous and extensive enforcement of the Federal antitrust laws would also improve economic opportunities for new and small enterprises.

The corporate income tax rate structure has been characterized as disproportionately burdensome on new and small corporations. In partial recognition of this position, the Revenue Act of 1964 reversed prior normal and surtax rates. In 1963 the normal tax rate, which applies to all corporate net income, was 30 percent and the surtax rate was 22 percent. Beginning in 1964, the normal tax rate is reduced to 22 percent while the surtax rate is increased. Thus while the combined normal and surtax rate is reduced by 2 percentage points in 1964 and 4 percentage points in 1965, the tax rate on the first $25,000 of corporate net income is reduced immediately in 1964 by 8 percentage points.

Proponents of this revision point out that it serves to increase the effective tax rate differential between large and small corporations in a simple, direct manner. Others contend that as long as the surtax exemption remains $25,000, the reversal cannot provide a really significant reduction in tax. They point out that while the percentage reduction in the tax rate because of this change is as high as 27 percent, the absolute reduction, at maximum, is only $2,000.

Other proposals advanced to provide relief to small and new businesses include (*a*) complete exemption of the first, say, $25,000 of net earnings of new companies for a limited period of time, e.g., 3 years; (*b*) restoration of the type of limited rate graduation in effect prior to 1950; (*c*) introduction of full rate graduation for all corporations regardless of the amount of their taxable income; and (*d*) an increase in the surtax exemption.

(*a*) *Full exemption of a limited amount of earnings of new companies.*—This proposal would seek to offer positive encouragement to the formation of new businesses. It recognizes that a relatively rapid rate of capital accumulation frequently is essential during the early years of the life of an enterprise and that this requires a relatively heavy net inflow of funds both from external and internal sources. In addition to increasing potential retained earnings, it is said, the proposal would facilitate external financing since the Government would, in effect, underwrite the new company's equity or debt issues, at least for the first few years.

Several objections have been raised to this proposal. In the first place it would significantly discriminate against unincorporated new businesses unless similar tax benefits were provided in the individual income tax, where very troublesome equity and enforcement problems would have to be surmounted. Secondly, providing special tax treatment of this character for a limited group of taxpayers would tend to set up pressures for extension of the preferential treatment to other taxpayers with perhaps equally pressing, though dissimilar, financial problems. Finally, the inducements to tax avoidance afforded by this proposal would be difficult to control.

(*b*) *Restoration of limited rate graduation.*—Under the system of limited graduation in effect prior to 1950, graduated rates were applied only in the case of a corporation whose income did not exceed some designated amount. In the case of corporations with incomes in excess of this amount, a single tax rate was applied to the full amount of taxable income. For example, for the income years 1946 through 1949, the following normal and surtax rate schedules were applicable:

TABLE 15.—*Corporate normal and surtax rate schedules, 1946 through 1949*

Taxable income	Normal tax rate	Surtax rate	Combined marginal rate
Incomes in total amount—			
Not over $50,000:			
1st $5,000	15	6	21
Next $15,000	17		23
Next $5,000	19		25
Next $25,000	31	22	53
Over $50,000	[1] 24	[1] 14	[1] 38

[1] Of entire income.

Combined rates ranged from 21 percent on $5,000 or less of taxable income to 38 percent on incomes over $50,000. In the range between $25,000 and $50,000 of taxable income, a marginal or "notch" rate of 53 percent was imposed.

This high "notch" rate was required in order to provide a relatively smooth progression of effective rates on incomes up to $50,000 in view of the fact that both the marginal and effective rate on the full amount of taxable income was 38 percent where taxable incomes exceeded $50,000. Effective rates under this graduated rate schedule were as follows:

TABLE 16.—*Effective rates under graduated rate schedule for corporation income tax, 1946–49*

Taxable income	Amount of tax	Effective rate (percent)
$5,000	$1,050	21.00
$20,000	4,500	22.50
$25,000	5,750	23.00
$30,000	8,400	28.00
$40,000	13,700	34.25
$50,000	19,000	38.00
Over $50,000		38.00

Proponents of this type of rate structure contend that it best meets the objective of differential taxation of small and large companies since the benefits of the lower graduated rates are confined to companies with relatively low incomes.

On the other hand, because of its dependence on a high "notch" rate, this system of graduation was severely criticized when it was in effect. The 53-percent "notch" rate was regarded as imposing a heavy penalty on corporations with incomes between $25,000 and $50,000 since it absorbed a larger share of additional earnings in this range than was taken by the 38-percent rate on additional earnings in excess of $50,000.

Moreover, this method of graduation made it extremely difficult to change the alinement of rates in order to increase the spread between the preferential rate on small companies and the standard rate. In order to do so, it was necessary either to increase the "notch" rate, further aggravating the problem described above, or to provide a disproportionately large increase in the effective rate of tax as soon as income reached the $25,000 level.

(*c*) *Full rate graduation.*—Under this method a graduated rate structure similar to the individual income tax would be provided for all corporations regardless of the amount of their total income. Proponents of this system point out that it would provide increasing tax liabilities to reflect progressively increasing Government benefits as corporate income increases. Tax benefits, moreover, would tend to vary directly with the need for the internal financing of growth, which is most pronounced in the case of small companies.

Critics of this proposal point out that full graduation would impose a relatively heavy penalty on risky businesses with fluctuating incomes as compared with less venturesome enterprises with the same total income over a period of years. It would also apply different tax burdens to different industries depending on the characteristic size of business units in each industry, with possibly adverse effects on resource allocation and tax equity. In addition, full graduation would provide greater inducements for corporate splitups than prevail under the present law. Whatever the arguments for or against such reorganizations on the basis of nontax considerations, it is maintained that they should not result in preferential tax treatment so long as a community of ownership and managerial control persists. Finally, it is contended that it would be virtually impossible to determine the appropriate income brackets and the degree of graduation, since the generally accepted notions of intertaxpayer relationship which may be used in determining rate graduation in the individual income tax are not applicable in the case of corporations.

(*d*) *Increase in the surtax exemption.*—Proponents of an increase in the surtax exemption contend that it would serve the objective of providing differential relief for small firms without the major conceptual and practical difficulties involved in proposals for rate graduation. Thus, it is argued that increasing the surtax exemption would effectively decrease the amount of income of small companies subject to the full corporate tax rate without unduly aggravating the penalty on risky business and without greatly enhancing inducements for corporate splitups afforded by rate progression.

On the other hand, those opposed to an increase in the surtax exemption point out that in addition to the sizable revenue loss involved, the benefits of the increased surtax exemption would be lost on companies with taxable incomes under $25,000, even though these companies, on the basis of 1961 returns, comprise about 82 percent of all corporations with net income. While the effective rate reductions for large companies would be small, these companies would nevertheless obtain a disproportionately large share of the total reduction in tax liabilities. On the basis of 1965 tax rates, a $100,000 surtax exemption would result in tax reductions aggregating $975 million, of which corporations with incomes over $100,000 would obtain about 60 percent.

CHAPTER 4

CAPITAL GAINS TAXATION

I. Present Law

A. GENERAL PROVISIONS

Under present law, gains accruing on capital assets are taxed only at the time when realized through the sale or exchange of the property.[1] The term "capital assets" as defined in section 1221 of the Internal Revenue Code includes all property held by the taxpayer except certain specified classes: (*a*) stock in trade or property of a kind includible in inventory; (*b*) property held primarily for sale to customers in the ordinary course of the taxpayer's trade or business; (*c*) property used in trade or business and subject to an allowance for depreciation; (*d*) real property used in trade or business; (*e*) a copyright, literary, artistic, or musical composition which is the product of the taxpayer's personal efforts; (*f*) accounts or notes receivable acquired in the ordinary course of trade or business; and (*g*) certain Government obligations sold at a discount. Although depreciable and real properties used in a trade or business are specifically excluded from the capital asset category, net gains realized on their sale or exchange are taxable at the alternative capital gains rate. Net losses, however, are treated as ordinary losses.[2]

In a number of situations capital gains treatment hinges not only on the definition of a capital asset but also on the definition of a sale or exchange. The latter has led to considerable litigation and has required the adoption of various statutory provisions which deem certain transactions, such as the redemption of a bond, to be a sale or exchange.

Gains realized on the sale or exchange of capital assets held less than 6 months are treated as ordinary income and are fully taxable. Special treatment, however, is afforded gains realized on capital assets held more than 6 months. For individuals, this is effected by including in adjusted gross income only 50 percent of the excess of net long-term capital gains over net short-term capital losses. The tax is then computed at regular rates on the taxpayer's adjusted gross income, with the result that the capital gain is taxed at half the marginal rate applied to ordinary income. Alternatively, if it results in a lower tax liability, a tax at regular rates may be computed on all income excluding capital gains and this amount increased by 50 percent of the gains taken into account (i.e., 25 percent of the excess of net long-term gains over net short-term losses).[3] In effect, the maximum rate at which long-term capital gains are taxed is 25 percent. The following table illustrates the effect of this limitation in the case of a joint return at various levels of taxable income at 1965 tax rates.

[1] Secs. 1201, 1222.
[2] Sec. 1231.
[3] Secs. 1201, 1202.

TABLE 17.—*Comparison of effective rates of tax on ordinary income and net long-term capital gains, joint return, 1965 tax rates*

Taxable income (joint return)	Tax on 1 additional dollar of—		Capital gains rate as a percent of regular rate
	Ordinary income	Net long-term capital gains	
	Percent	*Percent*	
$1,000	14.0	7.0	50.0
$5,000	19.0	9.5	50.0
$10,000	22.0	11.0	50.0
$25,000	36.0	18.0	50.0
$45,000	50.0	25.0	50.0
$101,000	62.0	25.0	40.3
$401,000	70.0	25.0	35.7

A somewhat similar alternative tax computation limits the corporation income tax on net long-term capital gains to 25 percent.[4]

Losses sustained by individuals on the sale or exchange of property are recognized only if the property was held for the production of income,[5] although gains arising from the sale of property are taxable even if the property is not held for the production of income. Individuals may offset losses sustained in capital transactions against capital gains realized in the same year and then against up to $1,000 of other current income.[6] Capital losses in excess of the deductible amounts may be carried over until exhausted. Losses carried over are treated as short- or long-term capital losses depending on the nature of the sale in which they originated.[7]

Capital losses of corporations may be offset against capital gains.[8] Any excess of capital losses over capital gains cannot be set against other income, however, and can only be carried over, as a short-term capital loss, for 5 years.[9]

B. SPECIAL PROVISIONS

In general, a conceptual distinction is felt to exist between capital gains, as those gains which arise from increases in the market value of investment properties, and profits which result from the sale of the goods or services which are the end product of the taxpayer's economic activity. The statute provides, in keeping with this distinction, that gains which arise from the sale or exchange of a capital asset may be accorded the differentially favorable capital gains tax treatment. Under the general rule, gains which accrue without a sale or exchange or from a source not a capital asset, as defined under law, are considered ordinary income. The conceptual distinction notwithstanding, however, numerous exceptions have been made to the general rule.

In some cases, capital gains treatment has been accorded as a convenient way of providing relief to certain types of income regarded, for one reason or another, as incapable of bearing the full burden of ordinary income taxation. In others, capital gains treatment has been provided in lieu of an explicit averaging technique. In still other

[4] Sec. 1201.
[5] Sec. 165(c), Reg. 1.165-2 and 1.165-9.
[6] Sec. 1211(b).
[7] Sec. 1212(b).
[8] Sec. 1211(a).
[9] Sec. 1212(a).

cases, the capital gains option has been made available as an incentive device. As a result, the differential tax treatment accorded capital gains has been extended to certain types of income representing compensation for personal services, to income arising from sales of assets representing the taxpayer's stock in trade, and to amounts representing the accelerated receipt of future income. Some of the major exceptions to the general statutory rules are described in the following pages.

1. Real property used in the taxpayer's trade or business

A major change in the capital asset concept was made in the Revenue Act of 1938, which excluded from the capital asset category depreciable property used in the taxpayer's trade or business. Land continued to be a capital asset. The purpose of this provision was to eliminate the limitation on the deductibility of losses realized on the sale or exchange of depreciable property. It had been observed that the capital loss limitation was an inducement to retain in use obsolete and inefficient property or to abandon it, rather than sell it on the open market.

Since the exclusion from capital assets of depreciable property applied to real estate improvements but not to the land on which the improvements were erected, a problem of allocation of basis and receipts between the improvement and the land existed. This problem was in part resolved by legislation in 1939 which made long-term capital losses of corporations fully deductible.

While the exclusion of depreciable property from the statutory concept of capital assets afforded the taxpayer favorable treatment in the event of losses on sales or exchanges or such property, it made gains fully subject to tax. It was recognized that this might have adverse effects on replacement practices in periods of rising prices. Sales of real and depreciable property at gains became more frequent under wartime circumstances, and at the same time involuntary conversions, particularly shipping losses, increased.

The tax treatment of depreciable property was completely revised by the 1942 act in the light of these considerations. Section 117(j) of the 1939 code was introduced, at first, to cover only the involuntary conversion situation. The section provided that where total gains with respect to involuntary conversions exceeded total losses, the net gains were to be regarded as capital gains. Where total losses exceeded total gains, ordinary loss treatment was to be accorded the net losses. In the development of the act, the provision was extended to include all sales of all real and personal property, whether depreciable or not, used in the taxpayer's trade or business.[10]

Prior to 1962, the full difference between the sales price and the adjusted basis of a depreciable asset was treated as a capital gain. It was argued that individuals were therefore able, in certain cases, effectively to convert ordinary income into capital gains when the rate of depreciation exceeded the actual decline in the value of an asset. In such cases depreciation deductions were set against ordinary income while the gain which eventually arose because of the corresponding reduction in the adjusted basis of the asset was later taxed as a capital gain. Furthermore, once sold the asset could be redepreciated in the hands of the new owner. The issuance of Revenue

[10] Sec. 1231.

Procedure 62–21 in 1962, which set forth guidelines for the selection of tax lives for depreciation purposes substantially shorter than those previously set forth in Bulletin F, promised to aggravate the problem.

The Revenue Act of 1962 therefore provided that gains arising from the sale of certain depreciable property would be taxed as ordinary income to the extent of depreciation taken after 1961. The application of this provision was restricted to depreciable property, other than buildings or their structural components, used in a trade or business or for the production of income.[11] Depreciable real estate was treated by the 1964 Revenue Act.[12] In this case, however, only "excessive" depreciation is taxed at ordinary income tax rates. Excessive depreciation is defined as any depreciation taken on an item of depreciable real estate disposed of within 1 year. When the asset is held longer than 1 year excessive depreciation is a percentage of the excess of actual depreciation over straight line depreciation. The percentage is 100 percent of the excess for an asset held for 12 to 20 months, and is reduced by 1 percentage point for each month over 20 the asset is held. Thus after 10 years none of the excess depreciation, if any, is taxed as ordinary income.

2. Timber

The Revenue Act of 1943 extended section 117(j) treatment to income from the cutting or other disposition of timber. It had been observed that, under the 1942 legislation, a taxpayer might obtain capital gains treatment for gains realized on the sale of timber sold outright as a stand, although he would receive ordinary income tax treatment on income derived from cutting the timber. Moreover, gain from the sale of timber, however disposed of, was regarded as accruing over a relatively long period during which the trees matured and, therefore, as not properly taxable in full in the single year in which the gain was realized.

To eliminate the discrimination against the taxpayer who sold his timber under a cutting contract and to provide averaging for this bunched income, the Revenue Act of 1943 amended section 117 by adding subsection (k), which permitted taxpayers owning timber or having the contract right to cut timber from the property of another to treat the net proceeds as a long-term capital gain. The same treatment was accorded to a timber owner who disposed of timber under a contract in which he retained an economic interest in it. As in section 117(j), if losses exceeded any gains from disposition of the timber, the net losses are treated as ordinary losses.[13]

In 1954 the election to treat the income from timber operations as a long-term capital gain was extended to income from the sale of Christmas trees at least 6 years old when cut.

3. Livestock

The treatment provided in section 117(j) was specifically denied to property held for sale to customers in the ordinary course of business or to property included in inventory. This limitation raised a question in the case of livestock. The Treasury Department ruled that section 117(j) applied only to unusual livestock sales such as those which would reduce the normal size of the herd. Ordinary income

[11] Sec. 1245.
[12] Sec. 1250.
[13] Secs. 631, 1231.

treatment was prescribed for other sales. In 1949, however, a court decision held that animals used for breeding, whether or not sold as culls in the ordinary course of business, constituted property to which section 117(j) was applicable.

Subsequent case history and rulings by the Bureau of Internal Revenue created considerable uncertainty. The latter was largely resolved by the Revenue Act of 1951 which held that property used in a trade or business, and therefore eligible for section 117(j) treatment, included livestock, regardless of age, used by the taxpayer for draft, breeding, or dairy purposes if owned by him for 12 months or more.[14]

4. Unharvested crops

The 1951 legislation also resolved a question which had arisen as to the treatment of gains on the sale of land with unharvested crops. The Bureau of Internal Revenue had ruled that unharvested crops constitute property held primarily for sale to customers in the ordinary course of the taxpayer's trade or business and, therefore, any gain on the sale of the unharvested crops was to be treated as ordinary income. Subsequent court decisions reached conflicting positions. The 1951 act resolved the issue by providing that section 117(j) treatment would be applicable to the full amount of the gains or losses realized on the sale of land with unharvested crops. The cost of producing the unharvested crop is not deductible as a current expense.

5. Coal royalties

The Revenue Act of 1951 extended section 117(j) treatment to coal royalties. It was argued that since most coal property leases are long term with fixed royalty payments in terms of so many cents per ton, the lessor receives no automatic adjustment in royalties as price changes occur. It was also observed that since so many coal leases were negotiated well in the past, royalty payments had declined in value relative to other types of income. Furthermore, it was contended that capital gains treatment for coal royalties was necessary to remove the discrimination against coal lessors as compared with timber owners who lease their timberland.[15]

6. Iron ore royalties

Capital gains tax treatment was extended by the Revenue Act of 1964 to royalties derived from leasing domestic iron ore deposits. It was argued that iron ore royalties should be given the same tax treatment as coal royalties as a matter of equity and also to encourage leasing at a time when domestic iron ore production was decreasing. Capital gains treatment was also expected to improve the competitive position of domestic ore production relative to foreign production. As in the case of coal, where the ore has been held for more than 6 months and is sold under a contract in which the owner retains an economic interest, the excess of royalty payments over the adjusted depletion basis of the ore may be treated as a long-term capital gain in 1964 and later years.[16] Further depletion deductions are disallowed once this option is made.

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14 Sec. 1231.
15 Secs. 631, 1231.
16 Secs. 631, 1231.

7. Lump-sum distributions from retirement plans

Since 1942, lump-sum distributions to employees from qualified pension trusts have been treated as long-term capital gains if the distributions are made as a result of, and paid within 1 taxable year from, the date of the employee's death or other separation from service. Capital gains treatment for such distributions apparently was intended as a substitute for a specific averaging device thought to be required in view of the bunched character of the distribution. The Internal Revenue Code of 1954 extended capital gains treatment to lump-sum distributions from insured retirement plans.[17]

8. Employee stock options

Prior to 1945, if the grant to an employee of an option to purchase company stock at a favorable price was found to be a reward for services, the difference between the market price and the option price was held to be compensation taxable as ordinary income at the time the option was exercised. If the transfer was found to be merely for investment purposes, this difference was taxable as a capital gain when the stock was sold. In 1945, however, the Supreme Court ruled that the value of any option should be taxed as ordinary income at the time of exercise.

The Revenue Act of 1950 provided capital gains tax treatment for certain "restricted" stock options in recognition of the use of such options as an incentive device for important employees. An employee who received a restricted stock option, in general, only paid tax if he sold the stock, and then at capital gains tax rates if he had held the stock at least 6 months, on the difference between the option price and the sales price. This basic treatment has remained, but the Revenue Act of 1964 established more stringent qualifying rules with respect to options granted key employees after December 31, 1963.[18] Such options, now referred to as "qualified" stock options, cannot be granted at less than the stock's then existing market price, cannot be reset below the original option price, and cannot be granted to substantial shareholders of a corporation. The stock must be held for 3 years or more after exercise before gains on its sale are eligible for long-term capital gains tax treatment and the option must be exercised within 5 years after grant. In addition, option plans must be approved by shareholders within 12 months of the date they go into effect. If options to key employees do not meet these stipulations, the difference between the option price and the market price will be taxed as ordinary income when the option is exercised.

The 1964 act preserves, in effect, the former rules regarding restricted stock options for stock purchased under nondiscriminatory employee stock purchase plans. If the employee purchase price is 95 percent or more of the fair market value at the time of grant, no taxable gain is recognized when the stock is purchased. Subsequent sale or exchange of the stock, if more than 2 years after grant and 6 months after purchase, produces a long-term capital gain or loss. If the employee purchase price is less than 95 percent but not less than 85 percent of market price, the difference between the market price at the time of grant and the purchase price is taxed as ordinary income when the stock is sold or exchanged.

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[17] Sec. 402.
[18] Secs. 421-425.

34-435—64——6

9. Patents, copyrights, and literary, musical, or artistic compositions

Prior to the Revenue Act of 1950, the tax treatment of income from patents, copyrights, and literary, musical, or artistic compositions depended largely on the surrounding facts, including the manner in which the taxpayer developing these items disposed of them. Royalties from copyrights and other artistic works were in all cases treated as ordinary income. Ordinary income treatment was also accorded the sale of royalty rights by professional writers or artists whose works were regarded as held primarily for sale to customers in the ordinary course of a trade or business and, therefore, not capital assets. In the case of an amateur, case history had resulted in the treatment of royalties as ordinary income, but proceeds from the sale of royalty rights on the book or other artistic work if held for more than 6 months after completion were regarded as the proceeds from the sale of a capital asset. The Revenue Act of 1950 specifically excluded from the statutory definition of capital assets all such copyrights, and literary, musical, and artistic compositions for amateurs as well as professionals, regardless of the manner of their disposition.[19]

In the patent area, case history had also developed a confusing set of rules. With respect to patents developed by professional inventors, the courts had ruled that these were the inventor's stock in trade, the proceeds from the sale of which, therefore, were taxable as ordinary income. In the case of the amateur inventor, however, whether capital gain or ordinary income treatment was applicable turned on the legal form of the transfer of the patent. Where a lump-sum payment was received upon disposition of the patent, capital-gains treatment was generally applied. Capital-gains treatment was also generally allowed for a series of payments if the taxpayer was able to establish that such payments were merely installments on the sales price. Where the installments were found to be royalties, because the taxpayer retained a legal interest in the patent, the royalties received ordinary income treatment. Where, however, the taxpayer retained no legal interest, such royalties were frequently treated as capital gains even though the taxpayer retained an economic interest in the patent's use.

The Internal Revenue Code of 1954 clarified the treatment of income received with respect to patents by providing that all proceeds from the sale of a patent by the inventor or a financial contributor in the early stages of its development are to be regarded as long-term capital gains regardless of the form in which the purchase price is received.[20]

10. Oil royalties and in-oil payments

Oil royalties and in-oil payments are both ordinary income to the recipient. Gain on the sale or disposition of such rights may be a capital gain, however, depending on the circumstances.

A royalty payment covers the entire life of the property while an in-oil payment is limited in time, money, or barrels of production. The sale of an oil royalty is generally subject to capital-gains treatment on the theory that it represents the sale of a fractional share of a capital asset. The sale of an in-oil payment, on the other hand, has generally been treated as an assignment of future income, thus giving

[19] Sec. 1221.
[20] Sec. 1235. Patents held by taxpayers other than the inventor and used by them in their trade or business are depreciable business property subject to capital gain, ordinary loss treatment under sec. 1221.

rise to ordinary income. In the past, case history cast doubt on the ordinary income character of such gains by upholding the taxpayer's right to capital-gains treatment with respect to proceeds realized from limited-period assignments of royalty interests.[21] More recently, however, the Supreme Court has upheld the position of the Internal Revenue Service which calls for the ordinary income treatment with respect to sales of in-oil payments if the seller retains an interest in the property.[22]

11. Life interests in estates

Under court rulings, the sale of a right to income for life from a trust or estate has been treated as the sale of a capital asset, subject to the capital gains provisions.[23] This permits the realization as a capital gain of the present value of a stream of future payments which would be taxable as ordinary income when received.

12. Losses on certain small business securities

The Technical Amendments Act of 1958 and the Small Business Tax Revision Act of 1958 provide capital gains-ordinary loss treatment with respect to gains and losses realized on certain types of securities. Losses realized on stock in a small business investment company operating under the Small Business Investment Act of 1958 are treated as ordinary losses, while gains receive capital gain treatment.[24] Similarly, losses sustained by a small business investment company operating under the act on convertible debentures are treated as ordinary rather than capital losses.[25] Finally, up to $25,000 ($50,000 in the case of a husband and wife filing a joint return) a year of losses realized on the stock of a small business corporation, as defined in the law, may be treated as ordinary losses.[26]

13. Gain on the sale of a personal residence

Payment of tax on any gain realized at the time of the sale of a principal personal residence may be deferred if a new residence is purchased within 1 year of the date of the sale (4 years for members of the Armed Forces and longer in the case of involuntary conversions).[27] A gain is currently recognized only to the extent that the adjusted sales price of the old residence exceeds the cost of the new residence. The cost basis of the old residence is carried over and applied to the new home to provide for the eventual taxation of the gain. Part or all of such gain may eventually be exempt from tax, however, if the taxpayer sells his last personal residence after he has attained the age of 65. The 1964 Revenue Act excludes from gross income the gain attributable to the first $20,000 of the sales price of a personal residence sold by a taxpayer age 65 or more after December 31, 1963.[28]

14. Other special provisions

(*a*) *Deferral of tax on capital gains.*—Under existing law, certain property under specified conditions may be sold or exchanged without current recognition of gain. This is accomplished by carrying over

[21] Nordan, 22 T.C. 137: John D. Hawn, 239 T.C. 4.
[22] P.G. Lake, Inc. 356 U.S. 260, 58-1 U.S.T.C. and I.T. 4004, 1950-1 C.B. 10.
[23] *McAllister* v. *Commissioner*, 157 Fed. (2d) 235.
[24] Sec. 1242.
[25] Sec. 1243.
[26] Sec. 1244.
[27] Sec. 1034.
[28] Sec. 121.

the basis of the property sold to new property acquired and deferring recognition of gain until the disposition of the new property in a taxable transaction. This "rollover" area includes, in addition to personal residences, (1) the exchange of property held for productive use or investment for property of a like kind, the gain, if any, being currently recognized only to the extent of cash or other "unlike" property received in the transaction; [29] (2) an involuntary conversion, where the property is replaced with similar property within a specified period; [30] and (3) certain other nontaxable exchanges of stock for property in the organization of a corporation, the exchange of stock for stock of the same corporation in a recapitalization, the exchange of stock of one corporation for stock of another corporation in a merger or reorganization, and certain exchanges of insurance policies.[31]

(b) *Other provisions.*—Special rules are provided to determine the taxability of gains and losses in a number of situations. These include the specific provisions dealing with investment accounts of security dealers,[32] sales of subdivided real estate,[33] life insurance annuities and endowments,[34] bond retirements,[35] bond losses of banks,[36] cancellation of leases or distributorships,[37] short sales,[38] options,[39] commodity futures,[40] and corporate distributions and liquidations.[41]

C. HISTORY OF CHANGES IN THE LAW

The method of taxing capital gains and allowing deductions for capital losses has been altered many times since 1913.

Prior to 1922, capital assets were not explicitly defined in the law. Gains from the sale of all assets were taxable in full as ordinary income, both to individuals and to corporations. This treatment continued until 1942 for gains realized by corporations. The latter had the right to full deduction of losses on the sale of assets until 1933. For individuals, however, losses were not deductible at all between 1913 and 1915, were deductible to the extent of gains during 1916 and 1917, and in full from 1918 to 1921.

Capital assets were first defined in the Revenue Act of 1921, and special treatment provided for gains on sales by individuals. From 1921 until 1933, capital assets were defined as property held for more than 2 years (whether or not connected with a trade or business), but excluding stock in trade or property included in inventory. Property held for the personal use or consumption of the taxpayer or his family was given capital asset status after 1923. During the period 1922–33, the full amount of gains and losses was taken into account, although individuals could elect to be taxed at the alternative rate of 12.5 percent on net capital gains. This ceiling remained in effect until 1933. Long-term capital losses were deductible in full in 1922 and 1923, but between 1924 and 1933 the allowance was limited to a tax

[29] Sec. 1031.
[30] Sec. 1033.
[31] Secs. 251, 354, 361, 1032, and 1035–1036.
[32] Sec. 1236.
[33] Sec. 1237.
[34] Sec. 1035.
[35] Sec. 1232.
[36] Sec. 582(e).
[37] Sec. 1241.
[38] Sec. 1233.
[39] Sec. 1234.
[40] Sec. 1233.
[41] Secs. 301–346.

credit equal to 12.5 percent of such losses. Short-term capital losses were deductible in full against ordinary income.

The Revenue Act of 1934 redefined capital assets to include all property, whether or not connected with a trade or business, regardless of the length of time held, except stock in trade or other property included in inventory, and property held primarily for sale to customers. One of the purposes of this new definition was to deny to professional traders and speculators in securities and commodities the right to deduct trading losses in full as ordinary losses. The 1934 law repealed the 12.5-percent ceiling rate for individuals and substituted a sliding scale under which 30 to 100 percent of capital gains or losses were to be taken into account, depending on the length of time the assets had been held. Corporation gains continued to be recognized in full. Net gains of individuals and corporations, to the extent included in income, were taxable at the regular income tax rates. Up to $2,000 of net capital losses could be deducted from ordinary income.

The Revenue Act of 1938 continued the 1934 definition of capital assets with the further exception of property used in a trade or business. This permitted individuals and corporations to charge off against ordinary income the full amount of loss on the sale of buildings, machinery, and other depreciable assets, although deductible losses on land sales continued to be limited to $2,000 plus capital gains. The act also changed the five-step schedule for recognizing various percentages of gain or loss of individuals to a three-step schedule. Gains or losses from assets held 18 months or less were called short-term and those from assets held more than 18 months were called long-term. The full amount of gains and losses was recognized for corporations, while, for individuals, 100 percent was taken into account if the gain was short-term, 66⅔ percent if long term but from the sale of an asset held less than 24 months, and 50 percent if the gain was from an asset held more than 24 months. The regular rates for both individuals and corporations were then applied, although individuals could elect to be taxed on the taxable portion of their long-term capital gains at the rate of 30 percent, i.e., at an effective rate of 20 percent on gains from the sale of assets held 18 to 24 months and at a rate of 15 percent on gains from the sale of assets held more than 24 months. Long-term capital losses (according to the percentages recognized) could be deducted by individuals from other income, or 30 percent of the recognized loss could be credited against the tax on other income.

During 1940 and 1941 corporations could deduct their long-term losses in full, but neither individuals nor corporations could deduct their net short-term losses; these could, however, be carried forward and set off against the short-term gains of the immediately following year.

The Revenue Act of 1942 continued the definition of capital assets but excepted therefrom real property used in the trade or business of the taxpayer, introducing the special provisions for what came to be known as section 117(j) transactions. The law divided capital assets into long and short term, depending on whether held for more than 6 months. Short-term capital gains of individuals and long- and short-term capital gains of corporations were included in income but only 50 percent of the long-term capital gains of individuals were taken into account. The regular individual and corporate rates were then applied but both individuals and corporations could elect to be taxed at an effective rate of not more than 25 percent on their long-term capital gains. In determining net capital losses, all capital gains and losses (long term and short term) were considered together. Individuals were permitted to deduct net capital losses against up to $1,000 of other ordinary income and carry forward any balance of capital loss to be applied against capital gains and $1,000 of ordinary income in each of the succeeding 5 years. Corporations could also carry forward net capital losses for 5 years, but could not apply such losses against ordinary income.

The Revenue Act of 1951 temporarily increased the alternative tax rate on capital gains to 26 percent. In addition, the 2-for-1 offset of short-term loss against long-term gain was eliminated. The 1951 act also provided section 117(j) treatment for sales of land with unharvested crops if held more than 6 months, sales of livestock held for draft, breeding, or dairy purposes if held for 12 months, and for coal held for more than 6 months before being mined.

The Internal Revenue Code of 1954 made numerous changes, mostly of a technical and definitional character. The principal substantive changes made were provisions for capital gain treatment for patent royalties and for proceeds from the sale of subdivided real estate, subject to certain qualifications.

The Revenue Acts of 1962 and 1964 restricted somewhat the amount of gain eligible for long-term capital gains tax treatment in the case of depreciable property. The 1964 act contained more stringent rules regarding qualified stock options and extended capital gains treatment to iron ore royalties. The act further provided for the unlimited carryover of capital losses suffered by individuals. Although individual and corporation tax rates were reduced by the 1964 act, neither the 50-percent exclusion ratio nor the alternative tax rate on net long-term capital gains was changed.

Many major revisions in capital gains taxation were proposed by the President in 1963, but were not enacted.[42] They included a suggested reduction from 50 to 30 percent in the percentage of net long-term capital gains included in the adjusted gross income of individuals, a reduction from 25 to 22 percent in the rate of tax on corporate long-term capital gains, and an increase from 6 months to 1 year in the holding period required before an asset can be sold for a long-term capital gain. Also proposed was the income taxation of the unrealized capital gains accrued on assets transferred by reason of death or gift. Furthermore, proposed definitional changes would have: taxed as ordinary income at the time of exercise the difference between the value of option stock at the time of grant and its value at the time of exercise; removed capital gains treatment from the income derived from timber operations to the extent it exceeded $5,000 a year; taxed as ordinary income gain on the sale of mineral properties to the extent of cost depletion previously taken; and taxed as ordinary income lump-sum pension and profit-sharing distributions. Other proposals related to gains derived from the sale of livestock, citrus groves, and similar farm property, patents, various types of royalties, installment sales, and life estates.

[42] The President's 1963 Tax Message, hearings before the Committee on Ways and Means, 88th Cong., 1st sess., on the tax recommendations of the President contained in his message transmitted to the Congress, Jan. 24, 1963 (hereafter cited as the "President's 1963 Tax Message"), pp. 23–26, and 52-59. For a discussion of the proposals by witnesses appearing before the committee, see vols. 2 through 7 of the hearings.

II. Issues and Proposals

The tax treatment of capital gains and losses has been subject to criticism on both economic and equity grounds. Proponents of more liberal treatment argue that the present system imposes a significant barrier to the mobility of investable funds. Moreover, they maintain that the present treatment is inequitable in that it fails to make a large enough distinction between capital gains and losses and ordinary income and losses. On the other hand, those favoring elimination or reduction of the present preferential treatment of capital gains point out that the differences between capital gains and ordinary income do not warrant such treatment. They further argue that the problem of capital mobility is exaggerated and, to the extent it does exist, could be substantially eliminated by amending the present law to tax gains on assets transferred at death or by gift.

A. ECONOMIC ISSUES

The basic economic problem in the taxation of capital gains stems from the realization principle underlying the present law. Capital gains are taxable, not as they accrue, but only when the capital asset is sold or exchanged. The timing of the sale or exchange and therefore realization of the gain is at the discretion of the taxpayer. Whether or not the gain is realized depends on the taxpayer's choice between (*a*) obtaining a larger expected income from the asset in the future, of (*b*) immediately obtaining the present value of this future income. In the case of ordinary income, on the other hand, no such choice is generally open to the taxpayer. As a rule the benefits of ordinary income can be enjoyed only when the income is actually realized, and such realization gives rise to tax liability.[43]

The imposition of tax on realized capital gains has the effect of reducing the present value of the future income; i.e., the capital sum realized. Accordingly, the tax tends to weigh the taxpayer's choice in favor of retaining the asset and enjoying its enhanced future returns.

The weight of the tax factor in this choice between realization or nonrealization of accrued capital gains varies considerably among investors. Very often, factors other than tax considerations are determinant. All other things being equal, however, the holder of an appreciated capital asset will not sell or exchange it and realize the gain unless (*a*) he has found an alternative investment sufficiently preferable to the present holding to offset the tax and other costs of the exchange, or (*b*) he anticipates a decline in the market value of his present holding at least equal to the reduction in proceeds from the sale which will result from the tax.

This tax consideration may be illustrated in the case of an investor with 100 shares of corporation X bought at $50 and now selling at $80 per share. Assume that the X stock is now yielding 6 percent on the basis of its current price and the taxpayer is considering a shift to another stock yielding 7 percent on the basis of its current price. At the present tax rate of 25 percent, the net proceeds after the tax from

[43] The Senate Finance Committee observed in its report on the revenue bill of 1938, that "There is an essential difference between income derived from salaries, wages, interest, and rents and income derived from capital gains. It is always to the advantage of the taxpayer to receive the first class of income no matter what the rate of tax as long as it is less than 100 percent. On the other hand, the tax in respect to capital gains is optional—the taxpayer is not obliged to pay any tax unless he *realized* a gain by the *sale* of the asset * * *." [Italic added.] (S. Rept. 1567, 75th Cong., 3d sess., p. 6.)

the sale of the X stock would be $7,250 ($8,000 minus 25 percent of $3,000) which, if invested in the new stock, would yield more than the yield in the securities sold ($507.50 compared with $480). The switch would therefore be justified. It would also be justified if the taxpayer expected his present holdings to remain at their present price while the new stock was expected to rise in price by 10.3 percent or more. Similarly, sale of the present holdings would be justified if their price were expected to decline by $7.50 or more per share (from $80 to $72.50 or less).[44]

It is evident that the higher the rate of tax, the greater will be the deterrent effect of tax considerations on investment transfers. Accordingly, proponents of more liberal tax treatment of capital gains argue that a reduction in the rate would serve to "unlock" a substantial volume of investable funds which have been "frozen" into investments by the capital gains tax.

This problem of frozen investments is alleged to be particularly acute today in view of the substantial increase in property values which has occurred over the past 25 years. This rise reflects both a general rise in prices and the continuing increase in the level of business activity. Accordingly, sales or exchanges of capital assets are likely to involve the realization of very large capital gains measured in money terms and, consequently, very heavy capital gains tax liabilities. Many of the investors whose funds are "locked in" these appreciated assets, it is argued, would be willing and able to assume the risks involved in financing the high-risk ventures which are so important in sustaining the dynamic quality of the economy. More liberal capital gains treatment, it is maintained, would encourage such investors to transfer their investable funds in this manner. In addition, it would offer inducements to potential investors in the broad middle-income range to increase their holdings of corporate securities, particularly the relatively low-risk issues which would become available as present investments shifted to riskier outlets.[45]

Finally, those in favor of liberalizing capital gains treatment argue that the present system serves to promote economic instability.[46] In times of rising prices, investors tend to set a higher reservation price in order to recoup the tax paid to the Government as a necessary cost of transferring from one investment to another. Capital assets, therefore, tend to be withheld from the market, thereby restricting the supply offered for sale and forcing prices to rise still further. The reverse occurs when prices are falling, the net effect being to accentuate price swings of capital assets.

Opponents of the preferential treatment for capital gains argue that the lock-in effect of the present tax system has been greatly exaggerated. In the first place it is maintained that tax considerations are only one of a large number of considerations which enter into decisions with respect to asset transfers. It is pointed out that analytical investigations and available statistical data tend to confirm the conclusion that the lock-in effect is not great.[47]

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[44] Cf. Heller, "Investors' Decisions, Equity, and the Capital Gains Tax," Tax Compendium, pp. 381-394 particularly pp. 384-385.

[45] Cf. Jonathan A. Brown, "The Locked-In Problem," Tax Compendium, pp. 367-381.

[46] Cf. Somers, "Reconsideration of the Capital Gains Tax," National Tax Journal, December 1960, pp. 289-309.

[47] Cf. Holt and Shelton, "The Lock-In Effect of the Capital Gains Tax," the National Tax Journal, December 1962, pp. 337-352.

On the other hand, it is argued that a major factor contributing to any lock-in problem that does exist is the fact that capital gains are not subject to income tax at the time assets are transferred through gifts or by reason of death.[48] Furthermore, the basis of inherited assets in the hands of the heirs when they subsequently dispose of them is the value at the time transferred. The realization that gains accrued over a lifetime will never be subject to income tax if held until death is thought to be a serious deterrent to the sale of existing assets, particularly by older taxpayers. From this standpoint the lock-in problem could be substantially eliminated, it is argued, if provision were made for the taxation of unrealized capital gains at the time of death or gift, or alternatively for the carryover of the decedent's basis to the heir, as is presently the case with regard to gifts.

Moreover, it is argued that the impact of capital gains taxation on investment decisions has been misconstrued by proponents of more liberal treatment. To analyze this impact, it is necessary to recognize that individual investors may be classified, broadly speaking, into two groups. The first includes those who are income- and security-minded, who tend to balance the current income yield of their investments against the risk of capital loss and who are little concerned with capital appreciation potentials of their investments. For this group, obviously, the specific tax treatment of capital gains is of little consequence in investment decisions, although the capital loss provisions may be quite significant. The second group consists of those who are primarily motivated by the desire for appreciation in the value of their investments. For such individuals, the present preferential treatment of long-term capital gains is an important tax consideration which serves to encourage shifting out of conservative types of investments into more speculative ventures. Accordingly, it is maintained that the present provisions do not deter the mobility of venture capital. Moreover, a substantial mitigation of the present liberality in capital gains taxation would not significantly affect the transferability of investments for the latter group of taxpayers.[49]

It is also claimed that any significant effect of further liberalizing the capital gains provisions on the amount of capital assets offered for sale would be of short duration. Any given reduction in the tax rate, it is argued, might at first free some investments for which transfers now are marginal, but once these transfers were made, a further increase in the level of capital asset transactions would be minor, unless further rate reduction were provided. The "unlocking" effect, therefore, would be largely "one shot." A more substantial one-shot effect, it is claimed, would result from announcing a substantial increase in the tax rate to take effect, say, in 6 months.

B. EQUITY ISSUES

Proponents of preferentital income-tax treatment for capital gains maintain that gains derived from the disposition of property differ in a number of fundmental respects from ordinary income. These differences are such that capital gains cannot be expected to bear the full weight of progressive income taxation.

[48] Heller, op. cit.

[49] Cf. Butters, "Effects of Taxation on the Investment Capacities and Policies of Individuals," Tax Compendium, pp. 126-135, particularly pp. 130-133.

In the first place, it is argued that a capital gain is the increment in market value of a capital asset which reflects an increase in the present value of the future income stream produced by the asset. Regardless of the factors which produce this increase in value, the imposition of a tax on the realization of the gain represents a capital levy, since the tax liability precludes replacing the asset with an equally valuable asset unless funds are diverted from other sources. While it may be true that the gains would have entered the taxpayer's taxable income as they accrued were it not for the "realization" principle in the law, they have nevertheless been incorporated in the taxpayer's capital by the time of realization.

It is also argued that capital gains typically accrue over more than one income-tax accounting period. It is obviously unfair, therefore, to tax such gains at progressive rates in the year of realization. To do so might often result in a greater total tax liability than if the gains had been subject to tax each year as they accrued.

It is also argued that in view of the fact that capital gains are generally realized only incidentally to transfers of investment funds from one capital asset to another, such gains are not available to finance consumption expenditures in the same way or to the same extent as income from wages, salaries, rents, or dividends. Accordingly, they represent less ability to pay taxes than the latter types of income.

Moreover, it is maintained that capital gains do not represent an increase in the real product or income of the community. Such gains reflect merely relative changes in the market valuation of assets rather than additions in real terms to the total amount of goods and services currently available for consumption or investment purposes. Accordingly, taxes on such gains represent a transfer from the private to the Government sector of the economy, not of claims to the economy's current product (income) but of claims to its future product (capital).

Finally, it is pointed out that capital gains frequently reflect only general increases in prices. Such gains are "illusory" in that they do not measure real changes in the taxpayer's economic position. As such, therefore, they represent no addition to the taxpayer's ability to pay taxes. Recognition of the fact is found in section 1034 of the Internal Revenue Code of 1954 which permits the tax-free transfer of gains from the sale of a personal residence into another residence.

Opposed to this view is the contention that the concept of income upon which income taxation should be based permits no distinction between capital gains and other types of income. Income, it is argued, is properly defined as "* * * the money value of the net accretion to one's economic power between two points of time." [50] Another way of expressing this concept is that income is "the algebraic sum of the individual's consumption and the change in value of his property rights during a period." [51] These definitions specifically include appreciation in capital assets.

Moreover, it is argued capital gains represent as much ability to pay taxes as equal amounts of income from other sources. Any income, it is pointed out, may be regarded as a fund which the recipient may allocate between current consumption and personal investment as he sees fit. In this sense, any tax reduces the taxpayer's net

[50] R. M. Haig, "The Federal Income Tax," New York, 1921, p. 7.
[51] Henry C. Simons, "Personal Income Taxation," University of Chicago Press, 1938, p. 125.

wealth position when it is collected, regardless of the type of income he receives. The fact that income from some types of property transactions typically is reinvested by the recipient reflects merely a pattern of behavior but not a lack of taxpaying ability.

Many opponents of preferential treatment of capital gains would concede that where the gains have accrued over a number of years it is not appropriate to tax them as if they had in fact accrued only within the current income period. They maintain, however, that the present preferential rate treatment is an unsatisfactory approach to this problem of "bunching," since any specific rate; e.g., the present 25 percent, bears no necessary relationship to that which would have been applicable had the gain been taxed as it accrued. Furthermore, it is pointed out that an averaging scheme should take into account the fact that the realization principle permits the postponement of taxes on which no interest is charged. The absence of interest is a clear gain to the taxpayer. If taxpayers were permitted to spread their gains back over the period of accrual, but charged interest on the taxes deferred, it is contended, the result would be more tax in many cases than is now paid.

The "illusory" character of capital gains arising from changes in price levels, it is contended, is not an adequate basis for preferential treatment of this type of income. Incomes from nonproperty sources frequently reflect price level changes rather than real changes in the recipient's economic status. To accord more favorable treatment to capital gains than to other income on this basis, it is maintained, is manifestly unjust.

It is also contended that the fact that capital gains in the aggregate do not measure an increase in the economy's total product is not relevant in determining the taxability of these gains in the hands of their recipients. Income taxation is based on the principle of ability to pay, which in the case of any one taxpayer is enhanced by the realization of a capital gain.

Opponents of the preferential treatment of capital gains point out that capital gains realizations are concentrated among those with the highest incomes. The latter will therefore receive disproportionate benefits from existing law. It is pointed out that in 1959 net long-term capital gains comprised 63 percent of the realized income of taxpayers with adjusted gross incomes of $500,000 or more. At the same time such gains were less than 4 percent of the realized incomes of those with adjusted gross incomes of less than $15,000. (Realized income equals adjusted gross income plus the half of net long-term capital gains excluded from adjusted gross income.) It is further pointed out that taxpayers with incomes of $10,000 or more realized 71 percent of all net long-term gains in 1959. On returns with adjusted gross incomes of $1 million or more the average net long-term gain exceeded $1 million.

In this connection it is pointed out that the popularity of "growth" as opposed to "income" corporate stocks is based largely on the tax treatment of the income from these stocks. Growth stocks emphasize capital appreciation through earnings retention and are stressed as good investments for those in high tax brackets. The same income received as dividends would be much more heavily taxed.

Others point out, however, that the fact that annual statistics disclose that capital gains compose a large proportion of the income listed on upper income returns reflects, to a significant extent, realizations of gains accumulated over many years. These large gains, it is said, are nonrecurring in contrast to other sources of income and often represent a shift in investment portfolios. The relative income position of the recipient is likely to be overstated in the year gains are realized, since it is typically far above his average position during the years over which the gain accrued.

Finally, it is maintained that preferential taxation of capital gains creates a powerful incentive for converting ordinary income into capital gains. The opportunity to do so, however, is almost nonexistent for ordinary wage and salary earners who comprise the bulk of the taxpayers. Business people and high-income taxpayers, on the other hand, have been able to devise a wide array of income arrangements to take advantage of the capital gains provisions. As a result, some argue that capital gains treatment has become one of the most impressive loopholes in the Federal revenue structure.[52]

C. PROPOSALS FOR REVISION OF CAPITAL GAINS TAXATION

The problems noted in the taxation of capital gains have called forth a wide range of proposals for revision. Some are primarily addressed to mitigating the adverse economic consequences of the present system and some are concerned with making it more equitable. In addition to proposals calling for major substantive revision, a number of suggestions have been made for more limited modification of specific aspects of the present system. Only the former proposals are described below.

1. Downward revision of rate and holding period

Apart from proposals for complete exemption of capital gains, perhaps the most frequently advocated revision is a decrease in the present tax rate and the holding period requirement for long-term gain treatment. A 10- to 15-percent rate coupled with a 3-month holding period, it is argued, would significantly increase the volume of capital transactions, particularly in corporate securities.

This proposal is opposed on the grounds that it would further increase the unfairness of the present system, increase the incentive for conversion of ordinary income into capital gains, and result in a significant loss in revenue which would have to be made up by additional taxes on other sources of income. Moreover, it is argued, the proposal would not result in a significant continuing increase in the level of transactions but would have only an important initial impact on freeing immobilized funds.

2. Step-scale reduction in tax rate

Another frequently offered proposal is to provide for graduated reduction of the tax rate applicable to realized capital gains according to the length of time the asset is held before realization. This proposal, it is held, would mitigate the impetus toward converting ordinary income into capital gains, since most devices for so doing can be effectively employed only over relatively short periods of time. Assets distributed through the liquidation of a collapsible corporation, for example, would have to be held for a relatively long period of

[52] Cf. Surrey, "Definitional Problems in Capital Gains Taxation," Tax Compendium, pp. 404-418.

time if maximum benefits from this proposal were to be obtained. Such assets, however, are generally realized promptly.

On the other hand, it is pointed out that this proposal would offer increasing incentives to hold capital assets and would therefore serve to decrease the mobility of venture capital. Moreover, the proposal would greatly complicate tax computation. The proper allocation of basis, for example, in the case of the disposition of corporate stock acquired over an extended period in which such events as stock splits, the issuance of stock dividends, and distributions resulting from a corporate reorganization had occurred would, it is contended, be particularly burdensome.

3. Taxation of gains on assets transferred at death

The income-tax law has been criticized for failing to tax unrealized capital gains on assets transferred from a decedent's estate to his heirs. Under present law, gains so transferred are not subject to income tax because actual realization does not occur and constructive realization is not required. Furthermore, the heirs receive a step-up in basis; that is, they may treat the value of the asset at the time transferred as their basis for computing gain or loss in a subsequent sale. The latter treatment is in contrast to the treatment of assets transferred by gift in which the basis to the recipient is the donor's basis, adjusted to reflect any gift tax paid, provided the basis does not exceed the fair market value of the property at the time the gift is made.

In February 1963 the President proposed that the law be revised to provide for the income taxation of accrued gains on assets transferred by gift or death provided the recipient was not a nonprofit institution contributions to which would be deductible under section 170.[53] Numerous exemptions and limiting provisions were included in an effort to prevent possible hardships. Combined with proposals for a lower effective tax rate on long-term capital gains, the revision was supported on the grounds that it would unlock a substantial volume of assets now frozen because of tax considerations. Others held the proposal to be a major advance in tax equity, since it would in part remove an income-tax exemption particularly beneficial to high-income taxpayers from an important source of increased wealth. A large volume of gains, estimated to be as much as $12 or $13 billion, is said presently to pass untaxed between generations each year.[54]

The proposal was opposed on the grounds that it would subject estates to severe tax burdens and deny heirs the usual discretionary realization privilege with respect to capital gains. The added tax burden, it was argued, would be particularly burdensome for families with closely held businesses. The owners of many family businesses, it was contended, would be induced to dispose of their interests. It was also pointed out that since capital assets are taken at their fair market value at the time of death or shortly thereafter for estate and gift tax purposes, the proposal would constitute a double tax.

As an alternative to the President's proposal, the Ways and Means Committee discussed a provision for the carryover of a decedent's basis to his heirs. In this case, an heir would compute capital gains on the sale of inherited assets on the basis of their cost to the decedent

[53] President's 1963 tax message, p. 24.
[54] Senate Finance Committee, hearings on the Revenue Act of 1963, 88th Cong., 1st sess., p. 307.

adjusted for any estate tax paid on the appreciation in value during the decedent's lifetime. Proponents argued that while this proposal would eliminate the tax free step-up in basis provided by present law, it would avoid many of the objections raised over the constructive realization proposal. On the other hand, the carryover proposal, it was said, would aggravate lock-in effects and would prove too complicated from a technical standpoint.

4. "Rationalization" of the capital gains area

A proposal which has gained wide acceptance calls for a careful review of the entire area of capital gains taxation in the present law for the purpose of eliminating those transactions and receipts which are not true capital gains. Preferential treatment under the capital gains provisions, accordingly, would be confined to gains realized on the sale or exchange of a much narrower category of assets than at present, principally corporate securities. Other types of income currently receiving capital gains treatment, such as those representing compensation for personal service (distributions from retirement plans, stock options, patent royalties), gains from transactions involving inventory-type assets (coal royalties, cutting of timber, livestock), and anticipation of future income (in oil payments, life interests in estates) would be subject to ordinary income treatment or whatever preferential treatment specifically accorded with the special circumstances attendant on such receipts.

The principal objection raised to this proposal is that it would be virtually impossible, as a practical matter, to draw a line distinguishing the so-called true capital gains from the wide range of other income now receiving capital gains treatment. The concept of a capital gain as different from ordinary income, it is maintained, is fuzzy, pertaining not so much to the kind of income as to the circumstances under which the income is received. Even strict adherence to the general qualifying rule in the present law, the capital asset sale or exchange rule, would offer only a partial guide in making the required determination, since it would still leave open the question of what assets were to be included as capital assets. Nevertheless, proponents of this approach argue that many items now treated as capital gains are clearly outside the scope originally intended for preferential treatment and that a good beginning would be to remove these from the capital gains list.

5. The "rollover" approach

Proposals have been made to provide for tax-deferred exchanges of nonbusiness capital assets held in an individual's personal investment account in a manner similar to that now provided for gains on the sale of personal residences.[55] Taxation of gains would be deferred until final disposition of the assets, either by diversion of the proceeds to consumption or to investments of an entirely different character. Realization would also be provided for at the transfer of the property by gift or at death, or even at the election of the taxpayer. In general, an investor would not be taxed if the gains on the sale of an eligible asset were reinvested in similar assets within the same income period. A tax would be imposed, at ordinary income rates, on that portion of the gains not so reinvested. Capital losses could be carried over without limit for offset against capital gains.

[55] See Dan Throop Smith, op. cit., pp. 151-155.

This proposal, it is maintained, would completely eliminate the deterrent of current taxation on transfers of investable funds. Moreover, though it would afford some benefits to taxpayers reinvesting gains by virtue of deferral of tax, it would nevertheless provide for utlimate and complete taxability as ordinary income of all gains realized by the taxpayer.

This proposal is criticized as favoring those with very large income-producing investments while falling more harshly on those who might inadvertently be forced to convert their assets into income to be used for consumption. Thus, for example, it is pointed out that an older couple who sold an investment which had appreciated in value in order to obtain funds to support them in their retirement years would be subject to tax, as would an investor who sold some of his assets following a severe loss, while a more fortunate person would not be faced with the necessity of converting his capital into income for consumption expenditures. If attempts were made to provide special provisions for hardship cases, the law would become quite complex and the end result could be a virtual tax exemption for capital gains.

6. Averaging

It is contended by some that the major justification for special tax treatment of capital gains is the fact that they accrue over more than one income period. Realization of capital gains, therefore, may often result in a "bunching" within 1 taxable year of income which accrued over several taxable years. If capital gains were taxable as ordinary income, this bunching would result in their being taxed at a higher rate of tax than if they bad been taxable as they accrued. Accordingly, the only appropriate special provision, it is argued, is some sort of averaging device.

A wide variety of averaging proposals have been made. The principal objection raised against such proposals is the practical one of administrative and compliance difficulties. The taxpayer would be required to maintain detailed records and undertake complicated calculations. On the administrative side, the Internal Revenue Service would experience a significant increase in audit work. These difficulties, it is maintained, would arise under virtually any averaging proposal which attempted to determine tax liability on realized gains as if realization had occurred as the gains accrued.

Proponents of averaging argue, however, that the additional administrative and compliance burdens would be a small price to pay for more equitable and economically appropriate treatment of capital gains and losses, and other income items accruing over more than one income period.

A further objection is that for those taxpayers realizing the bulk of capital gains in any year, averaging would be of little help. These taxpayers, it is claimed, are mostly at the upper end of the income scale, where the statutory tax brackets, particularly for joint returns, are quite wide. Averaging, it is contended, would not necessarily serve to spread the bunched income into lower brackets and would not, therefore, necessarily produce results materially different from those which would obtain if capital gains were subject to ordinary tax treatment.

7. Taxation of capital gains on an accrual basis

Since the realization principle in the present law has been generally identified as the principal source of difficulty in capital gains taxation, the taxation of gains on an accrual basis has been proposed as an ideal solution. Under this proposal, taxable income would include the net change in the value of the property owned between the beginning and end of the taxable year, whether or not realized. Tax at ordinary income tax rates would be applied to such changes in value. Where net capital losses accrued over the year, they would be deducted in full from ordinary income. This approach would also eliminate problems resulting from the lack in the present law of a provision for constructive realization on transfers by gift or at death.

Numerous objections are raised against this proposal. In addition to the difficulties attendant upon establishing reliable values for property in the absence of a sale or exchange, the proposal would also frequently result in forced realizations in order to provide the means for payment of the tax. Moreover, this treatment would eliminate the present tax bias in favor of so-called growth investments as compared with safer income investments, and would, in fact, introduce an opposite bias.

D. THE TAX TREATMENT OF GAINS AND LOSSES REALIZED UPON THE DISPOSITION OF DEPRECIABLE PROPERTY

The proper treatment of gains and losses realized upon the sale of depreciable property has been the subject of renewed controversy since the allowance of more rapid depreciation beginning in 1954. At that time the difference between the adjusted basis of a capital asset and its sales price was treated as a capital gain. The 1962 and 1964 Revenue Acts amended the law, however, to provide that gains arising from the sale of depreciable property other than buildings and structural components would be taxed as ordinary income to the extent of depreciation taken since 1961, while gains on the sale of depreciable real estate would be taxed as ordinary income to the extent of any excess depreciation taken, as defined by law. If capital losses exceed gains, ordinary loss treatment (i.e., deduction in full from ordinary income) is provided.

Capital-gains treatment for gains realized upon the disposition of depreciable property cannot be permitted, it is argued, if the provisions for accelerated depreciation are to remain in the law. The pre-1962 provisions, it is contended, afforded a substantial tax advantage to taxpayers making extensive use of depreciable property in the production of their income as compared with those whose income-producing activities involved little dependence on such facilities. This advantage arose from the fact that depreciation deductions are chargeable against income taxed at ordinary income tax rates, while upon disposition of the property, the gains, which may have been nothing more than the result of accelerated reduction of the asset's basis for tax purposes, were taken into income as capital gains, taxable at a maximum rate of 25 percent.

Those who favor the former treatment maintain that it is necessary if prompt replacement of obsolete facilities is not to be deterred. In view of the persistent rise in capital costs, it is argued, dispositions of depreciable facilities are likely to give rise to gains, regardless of the method of depreciation employed. When such gains are fully taxable as ordinary income, it is argued, it pays the taxpayer in many cases to retain the property and continue to claim depreciation deductions on it, or in the case of unit accounting for depreciation, to discard it and claim an abandonment loss.

One proposal aimed at composing these differences would provide ordinary gain-ordinary loss treatment for dispositions of depreciable property but would permit deferral of tax on gains. This would be achieved by reducing the basis of new or existing facilities by an amount equal to the gain realized upon those sold or exchanged. The tax would be recouped through the resulting reduction in the amount of depreciation allowable on the facilities remaining in the taxpayer's depreciable asset account (including additions thereto). By virtue of the accelerated depreciation methods, a substantial portion of the recoupment would be achieved fairly promptly.

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CHAPTER 5

DEPRECIATION AND THE INVESTMENT CREDIT

I. Present Law

Business expenditures for plant, machinery, equipment, and other capital assets cannot ordinarily be deducted in full in the year in which such an item is acquired. Rather the deduction must be apportioned over the estimated useful life of the asset. The income of each year's operation is thus charged with a proportion of the cost of the capital asset until the full amount, less any salvage value, has been deducted. Depreciation allowances can only be taken with respect to property used in a trade or business or otherwise held for the production of income and cannot exceed the original cost of the asset.

In an economic sense, a capital asset declines in value gradually as it is used, through wear and tear and obsolescence. Since the rate of a future decline in value cannot be measured accurately in advance, it must be estimated or recognition of the decline must be deferred until it is measurable, which may not be until the asset is retired from use. An estimate entails a judgment concerning the likely useful life of the property, the proper method of depreciation, and the amount of any eventual salvage value. While variations in such judgments will in no case permit the amount of depreciation to exceed the cost of the asset, they may have important tax consequences. Tax liabilities can be deferred, in effect, by lumping depreciation deductions in the early years of an asset's useful life, a result of particular consequence to rapidly growing firms.

The statute specifies several of the methods of computing depreciation which are permitted. While a taxpayer may use any estimated useful life for tax purposes consistent with his retirement practices, guidelines are provided in Revenue Procedure 62–21. This document also contains an objective test which will be used to determine whether estimated lives for tax purposes (tax lives) conform to actual useful lives (service lives).

A major feature of the Revenue Act of 1962 was a provision for a credit against tax liability based on expenditures for depreciable machinery and equipment used for business purposes within the United States. The credit was enacted to encourage increased investment in such property.

A. METHODS OF COMPUTING DEPRECIATION ALLOWANCES

The present law [1] sets out three methods of computing depreciation (including a reasonable allowance for obsolescence) as follows:

(1) The straight-line method;

(2) The declining-balance method at not exceeding twice the straight-line rates; and

(3) The sum of the years-digits method.

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[1] Sec. 167.

The law also allows any other consistent method, provided the deductions at the end of each year during the first two-thirds of the useful life of the property do not result in accumulated allowances greater than those permitted by the double declining-balance method.

Straight-line depreciation allowances are computed by applying the depreciation rate (equal to the estimated useful life of the property divided into 1) to the cost of the asset less its salvage value. As indicated by the name of this method, the amount of the allowance is the same each year over the asset's useful life.

Under the declining-balance method, a uniform rate (which may be as much as twice the straight-line rate) is applied to the unrecovered basis of the asset. Since the basis is always reduced by prior depreciation, the rate is applied to a continually declining basis. Salvage value is not considered under this method.

Under the sum of the years-digits method, the annual allowance is computed by applying a changing fraction to the cost of the property reduced by estimated salvage value. The denominator of the fraction is the sum of the numbers representing the successive years in the estimated life of the asset and the numerator is the number of years, including the current year, remaining in its useful life. In the case of a 5-year property, for example, the allowance in the first year is computed by applying to the depreciable value of the asset the fraction $\frac{5}{15}=\left(\frac{5}{(1+2+3+4+5)}\right)$. In the second year, the allowance would be four-fifteenths of the original cost of the asset, less salvage.

The straight-line method is available to all types of depreciable property whether acquired new or secondhand, and no matter when or how acquired. The declining-balance method at not more than twice the straight-line rate and the sum of the years-digits method are available only with respect to assets with a useful life of 3 years or more constructed or acquired by the taxpayer after December 31, 1953; neither method is available for used or secondhand property. The declining-balance method at 150 percent of the straight-line rate may be applied, however, to used property acquired after December 31, 1953. A taxpayer may switch to the straight-line method from the declining-balance method, basing future allowances on the unrecovered cost of the asset and its remaining life at the time of the change. This option insures that the asset can be fully depreciated.

The operation of each of these methods is shown in the following table, which assumes an asset costing $10,000 with an estimated useful life of 10 years and insignificant salvage value:

TABLE 18.—*Comparison of straight-line, declining-balance, and sum of the years-digits methods of depreciation*

Year	Straight-line		200 percent declining balance		Sum of the years-digits	
	Annual charge	Cumulative charges	Annual charge	Cumulative charges	Annual charge	Cumulative charges
1	$1,000	$1,000	$2,000	$2,000	$1,818	$1,818
2	1,000	2,000	1,600	3,600	1,636	3,454
3	1,000	3,000	1,280	4,880	1,455	4,909
4	1,000	4,000	1,024	5,904	1,273	6,182
5	1,000	5,000	819	6,723	1,091	7,273
6	1,000	6,000	655	7,378	909	8,182
7	1,000	7,000	[1] 655	8,033	727	8,909
8	1,000	8,000	655	8,688	545	9,454
9	1,000	9,000	655	9,343	364	9,818
10	1,000	10,000	655	9,998	182	10,000

[1] Switch to straight-line for years 7 through 10 authorized so that total depreciation will equal the cost of the asset. Cumulative charges do not add to $10,000 because of rounding.

As the table indicates, use of the declining-balance method at twice the straight-line rate results in the writeoff of about two-thirds of the cost of the asset over the first half of its life. The sum of the years-digits method permits recovery of almost three-fourths of the asset's cost over the same period. Under all three methods, full recovery of cost is spread over the entire useful life of the asset.

In computing depreciation on personal property the taxpayer may ignore that portion of the estimated salvage value of an asset purchased after October 16, 1962, which does not exceed 10 percent of its cost, provided the asset has an estimated useful life of 3 years or more.[2] This provision was enacted in the Revenue Act of 1962 and was related to a provision for the taxation at ordinary income tax rates of gains on the sale of depreciable assets other than buildings to the extent of depreciation previously taken. Salvage value can be ignored entirely when computing depreciation under the declining-balance method.

B. THE GUIDELINES AND THE RESERVE RATIO TEST

Neither the law nor accompanying regulations specify the useful lives to be used in computing depreciation allowances. Prior to 1962, the Internal Revenue Service published in Bulletin F a list of suggested useful lives for a large number of specific depreciable assets. By the early 1960's, there was widespread agreement that these suggested lives were, in general, longer than actual experience warranted. While the suggested lives were not binding on taxpayers, they were said to constitute a bias in favor of the use of tax lives longer than justified by actual experience. Since these lives had remained unchanged for over two decades, a searching review of their pertinence was undertaken by the Treasury Department in 1961.

In July 1962, the Treasury Department issued Revenue Procedure 62–21, superseding Bulletin F and substantially revising the basic approach to the determination of useful lives. Use of this procedure is elective. The taxpayer may continue to follow former guidelines if he wishes.

[2] Sec. 167(f).

1. Guideline lives

The new procedure provides suggested useful lives by industry grouping rather than on the item-by-item basis employed in Bulletin F. One guideline life applies to all the assets in each of the less than 100 specified asset classes. Normally a single industry guideline covers all the productive equipment and machinery used in that industry. Certain assets in general use, such as office equipment, are covered by guideline classes that cross industry lines. The guidelines may be applied to existing facilities as well as to those acquired in 1962 and later years.

A taxpayer may employ the useful lives suggested in the guidelines without question for tax purposes for an initial period of 3 years. Thereafter he may continue to use them only if they conform with, or are longer than, actual service lives as demonstrated by retirement practice. A taxpayer may, however, use shorter useful lives than those specified by the guidelines if his replacement practice warrants or if their use is established upon the basis of all relevant facts and circumstances.

The useful lives suggested by Revenue Procedure 62–21 are on the average 30 to 40 percent shorter than those suggested in Bulletin F and 15 percent shorter, on the average, than the useful lives actually being used at the time the new procedure was released.

2. The reserve ratio test

The new procedure contains a reserve ratio test which is intended to provide an objective basis for appraising the correctness of the useful lives claimed for tax purposes. Under the test, the criterion for determining proper useful lives is the speed with which a firm replaces assets in a given class, rather than the physical or other properties of the assets themselves.

The first step in the application of the test is the computation of the actual reserve ratio for each guideline class. The ratio is equal to total depreciation allowances claimed to date on all property in the class, including fully depreciated property still in use, divided by the cost of such property. Other things equal, the ratio will normally be higher for a firm that is slow to replace assets than for a firm that replaces them rapidly.

The actual ratio is then compared with a range of test ratios furnished in tables provided in Revenue Procedure 62–21. The selection of the applicable test ratio for each guideline class depends on the method of depreciation used and the annual average rate of growth in the size of the asset class over the last class life cycle as well as the class life claimed. If the actual ratio falls within the range of test values, the class life used by the taxpayer will be accepted as compatible with his replacement practices. If the actual ratio is below the range of test values, the taxpayer may consider using a shorter class life. On the other hand, if the actual ratio exceeds the upper limit to the range of test values, it suggests the taxpayer has not replaced assets at a rate fast enough to justify the class life he is using. As indicated, the test does not apply during an initial 3-year period. Moreover, during a further transition period no adjustment in useful lives will be required if the gap between the actual ratio and the upper limit of the range of test values in any one year is less than the same gap in any of the three previous years. Even if the class life used by the taxpayer must be lengthened, no penalty will be assessed for the years in which he based his depreciation deductions on too short a class life. Nor are the results of the reserve ratio test necessarily binding. The taxpayer may establish the reasonableness of his depreciation deductions in other ways.

C. SPECIAL DEPRECIATION

1. *Additional first-year depreciation*

The Small Business Tax Revision Act of 1958 provides a limited amount of additional first-year depreciation. The allowance is limited to 20 percent of the cost of tangible personal property, whether new or used, acquired by the taxpayer after December 31, 1957, for use in a trade or business or for the production of income. The property must have a useful life of at least 6 years. The 20 percent allowance may be claimed with respect to not more than $10,000 of such property ($20,000 in the case of a husband and wife filing a joint return) in any taxable year. This additional allowance is computed without reference to salvage value, but together with salvage value must be deducted from the basis of the property for purposes of computing the ordinary depreciation allowable.[3]

2. *Rapid amortization*

Until 1960, special provision was made for emergency facilities certified as necessary in the national defense by a certifying agency designated by the President. Such facilities could be written off on a straight-line basis over a 5-year period, without reference to the customary useful life.[4] Statutory authorization for further issuance of certificates expired on December 31, 1959. Grain storage facilities constructed after December 31, 1952, and before January 1, 1957, could also be amortized over a 5-year period instead of being depreciated over their useful life.[5]

D. THE INVESTMENT TAX CREDIT

A major feature of the Revenue Act of 1962 was a credit against income tax liability based on expenditures for depreciable machinery and equipment used in a trade or business located in the United States.[6] The credit is equal to 7 percent of qualified investment (3 percent of such investment in the case of public utilities).[7] In any 1 year the credit taken may not exceed the first $25,000 of tax liability plus one-fourth of any remaining tax liability. Any unused credit may be first carried back to the 3 preceding tax years and, if not exhausted, then carried forward for as many as 5 of the succeeding years.

The determination of qualified investment depends both on the nature of the property and its estimated useful life in the hands of the taxpayer. In general, the credit is limited to new or used section 38 property. Section 38 property consists of tangible personal property, and other depreciable property, but not a building, used as an integral part of manufacturing, production, extraction, transportation,

[3] Sec. 179.
[4] Sec. 168.
[5] Sec. 169.
[6] Sec. 38.
[7] Secs. 46–48.

communications, electrical energy production, gas or water transmission, or sewage disposal.

Section 38 property must have a useful life of at least 4 years before it can become the basis for a credit. Qualified investment in either new or used section 38 property is limited to 33⅓ percent of the cost of such property that has a useful life of more than 4 years but less than 6 years and to 66⅔ percent of the cost of property with a useful life of 6 years but less than 8 years. If it has an estimated useful life of 8 years or more the full cost of the equipment qualifies as the basis for a credit. Qualified investment in used section 38 property is limited to $50,000 a year.

For taxable years 1962 and 1963, in computing allowable depreciation, the basis of qualified investment property had to be reduced by the amount of the credit which could be taken. This stipulation was repealed effective for taxable years beginning after December 31, 1963. Taxpayers who placed qualified investment property in service before January 1, 1964, may increase the depreciable basis of such property by the amount of the credit taken and base future depreciation allowances on this augmented basis.

Provision is made for the recovery of excess tax credits when a taxpayer disposes of the property before its original estimated useful life. Further provisions govern the allocation of the investment tax credit in cases involving leased property.

It is estimated that investment credits totaling $1 billion were claimed by corporations in 1962.

E. HISTORY OF CHANGES IN THE LAW

The history of depreciation policy may be divided into four parts: 1913 to 1933, 1934 to 1954, 1954 to 1962, and since 1962. Before 1934, taxpayers could generally determine over what period and at what rate they would write off their assets. These deductions were permitted to stand unless the Bureau of Internal Revenue could show by clear and convincing evidence that they were unreasonable.

In 1933, a subcommittee of the Committee on Ways and Means recommended, as a means of increasing tax revenues, that for the next 3 years depreciation allowances be reduced by one-fourth. The Treasury suggested as an alternative that it be permitted to tighten up its practices in a way which might prove more equitable than a flat reduction for everybody. This was agreed to, and the Treasury adopted Treasury Decision 4422 which paved the way for redetermining the period over which assets should be written off, and shifted to the taxpayer the burden of proof as to the correctness of deductions. The Bureau subsequently issued Bulletin F containing estimates of the useful lives of many items of property.

From 1934 to 1954, Treasury and congressional attitudes on depreciation allowances were under constant attack by industry. Depreciation problems constituted a major source of conflict and occasioned many controversies between taxpayers and the Bureau of Internal Revenue. The issue generally involved the suggested tax lives for assets provided in Bulletin F, which were alleged to be unrealistically long. Taxpayers claimed that they could not recover their investments with sufficient speed. It was frequently argued that the situation was a deterrent to new investment. As a result of numerous controversies involving depreciation, the Internal Revenue Service in 1953 issued Revenue Ruling 90 which instructed revenue agents not to adjust tax lives used by taxpayers unless there was a clear and convincing basis for a change. This did not, however, stem criticism of depreciation tax policy.

The only important legislative departures from general policy in this period were the adoption in 1940 and 1950 of provisions for accelerated amortization of defense facilities constructed during World War II and the Korean emergency.

Prior to 1954, permissible methods of computing depreciation for income tax purposes were not specified. The straight-line method was the one most frequently used although others such as the unit-of-production method and the declining balance method were permitted. In 1946 the Bureau liberalized the availability of the declining balance method but limited the rate to 150 percent of the corresponding straight-line rate. Subject to this limitation, the method was rarely used.

The Internal Revenue Code of 1954 specifically authorized the use of the more liberal 200-percent or "double" declining balance and sum of the years-digits methods of depreciation. It did not, however, authorize any changes with respect to the determination of the useful lives over which assets might be written off, nor any change in the historic cost basis for depreciation allowances.

In 1962, following a review of depreciation rules and methods and a survey of existing practices, the Treasury superseded Bulletin F with Revenue Procedure 62–21 which substantially reduced suggested tax lives, explicitly provided for the computation of depreciation allowances on a class rather than an item basis, and set forth an objective procedure for testing the acceptability of depreciation allowances.

An investment tax credit was proposed by the President in his message on the Federal tax system delivered in April 1961.[8] The credit proposed was to be based on the amount of investment in excess of 50 percent of current depreciation allowances. The intent was to encourage net additions to the stock of business plant and equipment. An investment credit was enacted in 1962 equal to 7 percent of all qualified investment in depreciable machinery and equipment. As originally enacted, the depreciation basis of assets eligible for the credit was required to be reduced by the amount of the credit which could be taken. This provision was repealed by the Revenue Act of 1964. The depreciation basis on assets purchased after December 31, 1963, is equal to full cost. The depreciation basis of assets purchased in the taxable years 1963 and 1964 can be increased by the amount of any investment credit taken.

II. Issues

Within recent years depreciation provisions have been revised to permit the more rapid writeoff of the cost of business assets and a tax credit proportionate to investment in machinery and equipment has been enacted. The Revenue Act of 1954 authorized the use of the double declining balance and sum of the years-digits methods of depreciation and the Revenue Act of 1958, under certain conditions,

[8] H. Doc. 140, 87th Cong., 1st sess., Apr. 20, 1961.

permitted additional first year depreciation. In 1962 the Treasury replaced Bulletin F with revised, shorter guideline lives for depreciable assets other than buildings. Also in 1962 an investment tax credit was enacted to stimulate greater outlays on machinery and equipment. The nature of these provisions and their effect on the volume of investment in new plant and equipment have been matters of debate. In addition, an issue of long standing concerns the appropriate capital sum to be recovered through depreciation.

A. ACCELERATED DEPRECIATION IN THE 1954 INTERNAL REVENUE CODE

The use of methods which provide for larger depreciation deductions in the early years of an asset's useful life than the straight-line method allows have been supported as more realistic in a modern setting. It is contended that in general the value of a piece of equipment or machinery decreases at a decreasing rate, the loss in value being most pronounced in the early years of the asset's life. Automotive equipment is cited as a prime illustration of this problem. Accordingly, it is argued, depreciation charges for tax purposes should be permitted to reflect this pattern, which is closely approximated both by the declining balance method, using a rate twice the straight-line rate, and by the sum of the year-digits method. Failure to permit tax deductions according to this pattern, it is maintained, involves a forced loan of tax funds from the taxpayer which he can recoup only in the later years of the asset's life. Considering the total amount of assets acquired in recent years, these forced loans would, in the absence of the accelerated methods, amount to a very considerable sum. Moreover, the resulting misstatement of income would have adverse effects on management considerations with respect to investment policies.

In answer to this argument, critics of the 1954 depreciation provisions maintain that no single pattern of depreciation can be safely generalized for all types of depreciable property. While it may well be true that automobiles frequently exhaust a disproportionate amount of their serviceability in their first year or two, this is a result primarily of changes in demand resulting from style changes. It does not follow, however, that the same pattern of value loss is applicable, say, to an electric power-generating facility, which has a substantially longer useful life and which is not generally subject to the changes in market condition which affect automobile values.

Moreover, it is contended that according to traditional accounting concepts, depreciation is a device for measuring the annual conversion of the prepaid expense represented by the asset into cost as the asset is exhausted over its service life. In this context, the depreciation allowance is not intended to measure the change in the market value of the asset, since a large number of factors which may have little or no bearing on the taxpayer's use of the asset influence the volume and direction of that change. Ideally, according to this view, annual depreciation deductions should be taken in proportion to the decrease in the asset's contribution to the taxpayer's income. Since with reasonable maintenance and repair expenditures, which are deductible for tax purposes, the exhaustion of serviceability generally accelerates in the later years of the asset's use, the most appropriate measure of true depreciation would be afforded by a method, such as the annuity or sinking fund method, under which depreciation allowances would increase in each successive year.

With regard to the latter view, it is argued in reply that depreciation for tax purposes need not and in some cases, should not be tied to a realistic appraisal of the actual extent of capital erosion which occurred in the past. It is contended that national economic policy makes it desirable to stimulate increased investment expenditures by providing for accelerated depreciation. Such a policy objective, it is said, should be predominant.

Proponents of tax depreciation which accurately measures the cost of capital exhaustion contend that any deviation from this standard carries important equity consequences. When a large proportion of the total cost of an asset can be written off in the early years of that asset's useful life, tax payments are, in effect, postponed. This phenomenon is said to produce inequitable results because firms differ as to the volume of depreciable assets they employ and in respect to the rate at which they replace similar assets. Accelerated depreciation, it is argued, involves a redistribution of tax burdens from firms which are in a position to make extensive use of the provisions to firms which are not. Moreover, as long as new assets are purchased before the accelerated depreciation on a previously purchased asset is recouped through lower depreciation allowances in the later years of the asset's life, the firm will continue to enjoy tax postponement benefits. In a rapidly growing firm the volume of postponed taxes will actually increase over time.

B. THE 1962 GUIDELINES AND THE RESERVE RATIO TEST

The revised depreciation guidelines issued in 1962 contain three major features. The publication of guideline lives substantially shorter, on the average, than those in superseded Bulletin F met with wide approval. The shorter lives were held to reflect on a more realistic appraisal of the average life of productive assets, at least those in the hands of progressive, more efficient firms The substitution of broad classes for item-by-item depreciation has been well received and conforms to what was previously often done in practice. The reserve ratio test, on the other hand, has become the center of considerable controversy.

In general, critics of the reserve ratio test contend that the new guideline lives should be made available for tax purposes as a matter of right. On the one hand, this contention is based on the conclusion that no single, objective test can be devised to cover the great preponderance of possible depreciation situations. In this view, it is better to forgo the use of an objective test rather than to rely on one which might produce unsatisfactory results in many cases. On the other hand, a more fundamental objection to the proposed test is based on the argument that no essential purpose is served by requiring that depreciation deductions for tax purposes be related to replacement practice.

Criticism of the adequacy of the reserve ratio test has been directed at the tabular form of the test as published in Revenue Procedure 62–21. It is pointed out that the test ratios were derived on the basis of a "stabilized" depreciation account; that is, one in which the average

age of the assets in a given class does not fluctuate from year to year.[9] The test itself, therefore, is adequate only when individual depreciation accounts resemble this special case, which is said to be far from typical since it would have to be built up over time through a smooth flow of acquisitions with similar service lives. More likely are cases in which asset purchases are made unevenly over time and the individual assets within a class differ widely in service life. In such cases, it is contended, the actual reserve ratio will fluctuate above and below the range of test ratios during a class life cycle even though the tax lives used by the taxpayer conform to actual service lives. It is also pointed out that depreciation deductions with respect to a new asset should properly be based on an expectation of the length of future service life. The reasonableness of this expectation cannot be satisfactorily appraised on the basis of the useful life of assets acquired in the past. Finally, it is argued that because depreciation is limited to cost, tax liabilities are only deferred, not reduced, by provisions for more rapid depreciation. Therefore, it is argued that no serious inequity would be involved if taxpayers were allowed to use the guidelines as matter of right.

Those who support the use of the reserve ratio test point out that to grant the use of the guideline lives as a matter of right would result in an appreciable revenue loss to the Treasury and significant inequities in the distribution of tax burdens between taxpayers. Those taxpayers whose service lives exceeded the tax lives permitted by the guidelines would be able to defer tax payments. Other things equal, tax deferral will be greatest for firms with the greatest differential between tax and service lives. Firms whose retirement practice conforms service lives with tax lives would, on the other hand, receive relatively little benefit from tax deferral.

It is also pointed out that section 167 of the Internal Revenue Code stipulates that depreciation deductions should be "reasonable." This requirement would not be met, it is argued, if the taxpayer could use the guidelines as a matter of right. The section is said to require the use of some test to assure that tax lives are reasonable in terms of the service lives of the assets concerned.

It is also pointed out that the lack of such a test would weaken the effectiveness of a policy designed to encourage a higher level of investment in plant and equipment by allowing the use of shorter tax lives for such assets. If firms could use shorter tax lives without in fact conforming their retirement practice to these lives, the provision of shorter tax lives would encourage little actual change in business operations.

In defense of the present reserve ratio test, it is contended that while there may be weaknesses in its present tabular form as contained in the regulations, such weaknesses could be eliminated if an alternative form of the test were used. The essence of the test, it is contended, is the reserve ratio formula. The tables are merely illustrations of the use of the formula under certain restrictive conditions. Efforts should therefore be directed to improving the application of the reserve ratio test.

Moreover, it is pointed out that the results of the test are not binding; the taxpayer may as an alternative justify tax lives on the basis

[9] See George Terborgh, "The Reserve Ratio Test of Tax Depreciation Lives," in The President's 1963 Tax Message, pp. 2459–2489.

of all relevant facts and circumstances. Nor must the test be applied in all situations. For example, new businesses are permitted to apply the guidelines during the first-class life cycle without reference to the reserve ratio test. Finally, it is pointed out that the test is a significant administrative improvement over the pre-1962 situation. At that time the absence of such a test resulted in a lack of uniformity in depreciation adjustments made by the Internal Revenue Service in its negotiations with taxpayers. The reserve ratio test guarantees greater equity and fairness to all taxpayers by serving as an objective and uniform standard. As such, it is said to be applicable to the great majority of those cases which were previously contested; namely, to large well-established firms with mature, growing group asset accounts.

C. DEPRECIATION POLICY AND CAPITAL OUTLAYS

A major argument raised in support of provisions for more liberal depreciation, either through shorter tax lives or accelerated depreciation methods, concerns the effect of such provisions in stimulating the rate of private capital formation. Those who are critical of the possible effect of more liberal depreciation on increasing outlays for new investment contend that changes in the volume of capital outlays are attributable primarily to changes in the rate of expansion of total demand. They maintain that plant and equipment expenditures since 1954 have followed the pattern of the business cycle, just as in previous periods. Moreover, they point out that despite the accelerated depreciation provisions in the 1954 Code, plant and equipment expenditures represent a smaller share of gross national product, on the average, for the years since 1954 than for the prior postwar years. This they attribute to the slower rate of expansion of gross national product since 1954.

Others maintain, however, that regardless of the immediate impetus for expanding outlays on plant and equipment, the extent of the increase would have been less in the absence of the accelerated depreciation allowances afforded by the 1954 Code. Furthermore, it is pointed out that expenditures on new plant and equipment have risen significantly since the 1962 guideline revisions and the enactment of the investment tax credit.

The data currently available neither substantiate nor refute either position. From 1954 to 1963 expenditures for new plant and equipment increased by 50 percent. At the same time, however, such expenditures fluctuated in a manner which appears to be correlated to movements in the business cycle. These developments are indicated in the following table:

TABLE 19.—*Expenditures for new plant and equipment (excluding agriculture), seasonally adjusted quarterly totals at annual rates, in current prices and constant (1954) dollars, 1947–64*

Year and quarter	Weighted price deflator [1]	Expenditures for new plant and equipment (billions of dollars): Current prices	Expenditures for new plant and equipment (billions of dollars): Constant (1954) dollars
1947:			
1st	73.7	$19.7	$26.7
2d	75.5	20.3	26.9
3d	77.0	21.0	27.3
4th	78.3	21.3	27.2
Total	76.1	20.6	27.1
1948:			
1st	80.5	22.4	27.8
2d	81.6	21.8	26.7
3d	84.5	21.9	26.0
4th	85.7	22.3	26.0
Total	83.1	22.1	26.5
1949:			
1st	86.2	21.1	24.4
2d	86.2	19.7	22.8
3d	85.0	18.9	22.2
4th	84.7	17.9	21.0
Total	85.5	19.3	22.6
1950:			
1st	85.3	18.4	21.6
2d	85.7	19.2	22.4
3d	88.5	21.0	23.8
4th	90.7	23.3	25.7
Total	87.7	20.6	23.5
1951:			
1st	94.3	23.7	25.2
2d	95.8	25.5	26.6
3d	95.9	26.5	27.6
4th	96.2	26.6	27.6
Total	95.6	25.6	26.8
1952:			
1st	96.9	27.0	27.9
2d	97.5	26.6	27.3
3d	97.1	25.7	26.4
4th	97.1	26.7	27.5
Total	97.2	26.5	27.3
1953:			
1st	97.7	27.8	28.5
2d	99.5	28.1	28.2
3d	99.8	28.8	28.9
4th	99.0	28.5	28.8
Total	99.0	28.3	28.6
1954:			
1st	99.5	27.5	27.6
2d	100.2	26.9	26.9
3d	100.1	26.8	26.8
4th	100.2	26.2	26.1
Total	100.0	26.8	26.8
1955:			
1st	101.2	25.7	25.4
2d	102.2	27.2	26.6
3d	103.0	29.7	28.8
4th	104.6	31.5	30.0
Total	103.1	28.7	27.8
1956:			
1st	106.5	$32.8	$30.8
2d	108.8	34.5	31.7
3d	110.2	35.9	32.6
4th	112.6	36.5	32.4
Total	109.6	35.1	32.0
1957:			
1st	114.0	36.9	32.4
2d	115.5	37.0	32.0
3d	116.4	37.8	32.5
4th	116.8	36.2	31.0
Total	115.7	37.0	31.9
1958:			
1st	117.7	32.4	27.5
2d	118.4	30.3	25.6
3d	118.6	29.6	25.0
4th	119.2	30.0	25.2
Total	118.5	30.5	25.6
1959:			
1st	120.2	30.6	25.5
2d	120.9	32.5	26.9
3d	121.6	33.4	27.5
4th	121.1	33.6	27.7
Total	121.0	32.5	26.9
1960:			
1st	121.2	35.2	29.0
2d	121.7	36.3	29.8
3d	121.9	35.9	29.5
4th	121.6	35.5	29.2
Total	121.6	35.7	29.4
1961:			
1st	122.3	33.9	27.7
2d	122.2	33.5	27.4
3d	122.2	34.7	28.4
4th	122.1	35.4	29.0
Total	122.1	34.4	28.2
1962:			
1st	122.2	35.7	29.2
2d	122.8	37.0	30.1
3d	123.1	38.4	31.2
4th	122.4	38.0	31.0
Total	122.6	37.3	30.4
1963:			
1st	122.9	37.0	30.1
2d	123.5	38.1	30.9
3d	124.0	40.0	32.3
4th	124.2	41.2	33.2
Total	123.7	39.2	31.7
1964:			
1st	----------	41.3	----------
2d	----------	42.7	----------

[1] Derived (by Joint Economic Committee staff) by weighting the implicit price deflator for gross national product for producers' durable equipment and new construction (other than residential nonfarm) with weights of ⅔ and ⅓, respectively.

Source: Securities and Exchange Commission, and Department of Commerce.

The following table suggests that an increasing proportion of the depreciable facilities acquired in the years 1954 through 1960 is being written off for tax purposes under the accelerated methods afforded in the 1954 code. In 1954, 89 percent of total depreciation deductions claimed on active corporation returns were computed by the straight-line method and only 7 percent were computed by the accelerated methods. In 1960, the proportions had changed to 58 and 39 percent, respectively.[10]

TABLE 20.—*Percentage distribution of the amount of depreciation claimed by depreciation method, 1954–60*

Taxable year	Depreciation method (percent)			
	Straight line	Declining balance	Sum of the years-digits	Other
1954	89	5	2	4
1955	81	10	6	3
1956	74	12	9	5
1957	70	16	11	3
1958	61	17	16	6
1959	58	22	16	4
1960	58	24	15	3

Source: 1954–59: Internal Revenue Service: Statistics of Income, 1959–60, Corporate Income Tax Returns, p. 7; 1960: Statistics Division, Internal Revenue Service.

As yet, little data are available concerning the response to the 1962 depreciation revisions. A survey of corporations conducted by the Office of Business Economics of the Department of Commerce disclosed that corporations accounting for about 55 percent of corporate depreciation allowances adopted the new guidelines in 1962. The additional depreciation taken as a result totaled $2.4 billion and is estimated to have reduced 1962 corporate income tax liabilities by $1.23 billion. In 27 percent of the cases in which the guidelines were not used, management indicated that existing procedures were already in line with the guidelines.[11]

Those who contend that liberalized depreciation provisions contribute to increasing the level of investment in depreciable property attribute this result in part to the fact that even though the total depreciation which may be charged with respect to an asset is unaffected, a larger proportion of this charge may be made sooner. This serves to increase the present value of the total amount of depreciation allowances at the time an asset is purchased. This, in turn, means that the present value of the after-tax return on an asset is greater than it would be under straight-line depreciation, even though the absolute amount of charges over the life of the asset is the same. This increase in profitability serves to stimulate demand for depreciable property.

This effect, it is argued, is most pronounced in the case of long-lived property. Such property includes basic steel and other metal capacity, refineries, public-utility installations, and other facilities

[10] These data are suggestive but not conclusive. Since the accelerated methods "bunch" depreciation deductions in the early years of the asset's life whereas the straight-line method spreads the deductions evenly through the asset's early life, the change in the annual volume of deductions under either type of method is not necessarily proportionate to the change in the volume of assets depreciated under either type of method.

[11] The Department of Commerce, Survey of Current Business, July 1963, pp. 3–9. See appendix tables 37 and 38.

which represent a basic source of the economy's growth. The stimulus to capital outlays provided by more rapid depreciation, therefore, is regarded as particularly desirable in an economy in which growth is so essential.

In addition, it is maintained that accelerated depreciation methods and shorter tax lives stimulate increased investment through their effect on the risks involved. Particularly in the case of long-lived assets, it is argued, the difficulty of foreseeing the duration of usefulness results in management's setting a relatively brief period over which the asset must pay for itself. The greater the portion of the asset's cost which may be recouped through depreciation allowances within this "payoff period," the less is the risk incurred in the asset's acquisition. Use of the 200-percent declining balance and sum of the years-digits methods and shorter tax lives therefore contribute materially to reducing the risk deterrents to plant and equipment expenditures, provided the firm expects to earn profits sufficient to absorb tax depreciation deductions. Finally, it is maintained that provisions for more liberal depreciation help substantially to reduce the working capital barriers to the acquisition of fixed assets. The annual volume of corporate funds from all sources increased by an estimated $24.4 billion between 1953 and 1963. The increase in depreciation and amortization allowances during this period was $17.6 billion. Moreover, depreciation represented 54 percent of total sources of corporate funds in 1963, compared with 39.3 percent in 1953.[12] Provision for more rapid depreciation is held to be potentially of particular help to small and new businesses, whose internal funds are frequently inadequate to finance capital programs and who have access to credit only on relatively unfavorable terms. Accelerated depreciation reduces cash outflows for taxes in the early years after the acquisition of depreciable property and thus facilitates the repayment of any loan which may be required to finance such an acquisition.

The extent to which more rapid depreciation for tax purposes will increase outlays on investment goods depends on the degree to which the demand for such goods responds to given changes in profitability rates, risk differentials, and cash flow.[13] It is pointed out that little is known concerning such responses.

Those who are critical of the stimulating effectiveness of accelerated depreciation methods contend that their effectiveness in offsetting risk is overstated. If risk is measured by the rate at which the taxpayer discounts future receipts, it will be found that as the discount rate rises, the benefits from acceleration do indeed increase, but only up to a point. Beyond this point, i.e., at very high rates of discount reflecting very risky investments, the benefits from acceleration fall off markedly. Moreover, the benefits are often greater in absolute amounts (though not in relative terms) for short-lived assets than for long-lived properties.[14] Since it is the latter to which the greater risk is attributed, accelerated depreciation may actually operate perversely in encouraging relatively greater investment in relatively safe assets.

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[12] January 1964 Economic Report of the President, p. 285.

[13] Cf. Norman Ture, "Tax Reform: Depreciation Problems," Papers and Proceedings of the annual meeting of the American Economic Association, Dec. 27–29, 1962, p. 340.

[14] Cf. E. Cary Brown, "Weaknesses of Accelerated Depreciation as an Investment Stimulus," Tax Compendium, pp. 495–504.

In addition, it is pointed out that the effectiveness of accelerated depreciation methods and shorter service lives in improving the working capital position of taxpayers depends on their having adequate income to absorb the increased depreciation charges in the early years of an asset's life. While this may present little difficulty in the case of large, established firms, it is argued that the situation is not so certain in the case of small or new companies. The latter, particularly, may derive little benefit from acceleration despite loss carryover provisions since very often the profits in the early years of operation are quite meager.

It is further argued by critics of the newer depreciation provisions that the limited incentives afforded are at the expense of a substantial revenue loss to the Federal Government. Shortly prior to enactment of the 1954 Revenue Code, one estimate, assuming constant levels of plant and equipment outlays, showed the loss attributable to accelerated depreciation methods rising from about $375 million in fiscal 1955 to $2.2 billion in fiscal 1960, falling thereafter until 1969 for a cumulative loss of $19 billion. A more recent estimate shows a revenue loss of about $1.1 billion with respect to the taxable year 1959.[15] The revenue cost of the 1962 guideline revisions was estimated at $1.5 billion for 1962. An early survey showed this estimate to be substantially correct.[16] If an increasing rate of capital outlays were projected, the revenue loss would not decline absolutely so long as outlays increased. Thus, it is pointed out that while the revenue loss may be only temporary with respect to any given item of depreciable property, in the aggregate the new depreciation provisions permit the indefinite postponement of substantial amounts of tax.

In rebuttal to these analyses of cost, it is pointed out that they disregard the possible revenue repercussions of the higher level of investment induced by more liberal depreciation. Revenues will be increased as a byproduct of the higher level of economic activity stemming from a favorable response to the provision of more rapid depreciation. It is pointed out that the initial revenue loss can be completely offset by a relatively slight attendant increase in gross national product.

Finally, it is argued that the accelerated depreciation provisions may well serve to accentuate fluctuations in levels of economic activity and impose a greater burden on the other fiscal and monetary stabilization devices. These provisions, it is maintained, have little effect on plant and equipment outlays during a business downturn but may be counted on to provide some stimulus for such expenditures when boom conditions develop; i.e., at the very time when total spending should be damped to prevent inflation.

D. CAPITAL COST RECOVERABLE THROUGH DEPRECIATION

As a general rule, under present law total depreciation deductions over the life of a property may not exceed its original cost less estimated salvage value. This historic cost or adjusted basis limitation on depreciation allowances reflects the traditional accounting concept which regards the cost of a fixed asset as a prepaid expense.

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15 William F. Hellmuth, "The Corporate Income Tax Base," Ways and Means Compendium, pp. 293, 313, and 316.

16 See appendix table 38 and Department of Commerce, Survey of Current Business, July 1963, pp. 3–6.

This prepaid expense is gradually converted into cost as the property is exhausted over its service life. Since, under this view, the purpose of depreciation charges is to measure the annual conversion of asset into cost in order to determine the net profit from the asset's use, total depreciation charges cannot exceed the original cost (or adjusted basis) to the taxpayer. Depreciation is said to be a problem of allocation rather than evaluation.

The historic cost limitation on recoverable capital value is frequently criticized as producing an inaccurate measure of taxable income in an economy characterized by fluctuations in asset prices. This criticism is based on the concept of depreciation as a measure of the loss in the capital value of plant and equipment sustained over the course of the accounting period, regardless of the factors responsible for this value loss. According to this concept, the purpose of depreciation allowances is to provide an adequate fund out of current income for the replacement of the fixed capital employed in the production of that income. Where prices are rising over the course of an asset's life, it is argued, limiting depreciation allowances to historic cost will result in an inadequate tax-free reserve for replacement of the asset. The income tax, therefore, will have taxed away some portion of the capital invested as well as the income produced by the investment.

Numerous objections have been raised against proposals for substituting replacement cost for historic cost as the basis for limiting cumulative depreciation charges. It is pointed out that the contention that historic cost depreciation results in an inadequate replacement fund is valid only under certain unlikely assumptions. In the general case of an expanding company, it is argued, cumulative depreciation charges will more than adequately meet replacement needs unless replacements are made according to a grossly discontinuous pattern [17] or unless asset prices increase at a greater rate than the rate of increase, in real terms, of total facilities.

A second objection raised is that consistency would require the use of a concept similar to that underlying replacement cost depreciation in measuring taxable income from all sources, not merely from depreciable facilities. Thus, changes in price levels would have to be taken into account in measuring gains and losses on capital assets. Similarly, if property income were to be measured in "real" terms for tax purposes, a similar measurement would have to be employed for wages and salaries. The practical difficulties in such an approach to income taxation would, of course, be formidable. Yet, in the absence of a general system of real income measurement, special provisions to this effect for a limited number of income categories would probably produce undesirable shifts in tax-burden distribution during periods of general price movements.

A final objection is that replacement cost depreciation would operate counter to the stabilization devices in the revenue system. Thus, in a period of falling prices, characterizing a business downturn, depreciation allowances would be cut back at the very time when stabilization policy would call for an increase in internal funds for business. By the same token, when boom conditions resulted in rising prices,

[17] To take an extreme example, if a company acquiring one 20-year asset per year for 20 years replaced all 20 of the assets in the 20th year.

depreciation allowances would increase and tax liabilities would fall just when increased tax revenues were called for.

E. THE INVESTMENT TAX CREDIT

The investment credit provided in the Revenue Act of 1962 was intended as a device for stimulating increased business investment in machinery and equipment. Proponents of this provision argued that by intentionally favoring this form of business expenditure the then lagging rate of business investment in new capacity would be stepped up, to the benefit of the entire economy.

Those opposed to the measure argued that it is an inefficient if not ineffective means of achieving the objective desired and that preferable alternatives are available. On the one hand, some critics contended that a straightforward reduction in corporate tax rates or the provision of more liberal depreciation would be more effective since they would raise the expected profitability of new investment while avoiding the uncertainty likely to be created by a provision generally regarded as a "tax gimmick". On the other hand, other critics took the view that the credit provided simply a windfall to business firms, particularly large businesses with substantial capital replacement needs. It was argued that the most effective incentive for business investment is an increase in the level of aggregate demand, which creates active markets for increased output. In this view, business investment at a time such as the one in which the credit was debated is more likely to increase if tax reduction is concentrated among low- and middle-income consumers than if it is given directly to business firms.

In addition to general debate over the credit, controversy arose over its structural features, including the nature of credit, its relation to depreciation, and the status of public utilities.

1. Nature of the credit

The present 7-percent credit was the outgrowth of congressional consideration of a proposal set forth in a Presidential message delivered on April 20, 1961.[18] The credit proposed by the President was to be based largely on net new investment; that is, that portion of business investment in new plant and equipment which exceeded current depreciation charges. The credit proposed was to equal 15 percent of the amount of investment in excess of current depreciation changes plus 6 percent of expenditures below this level but in excess of 50 percent of current depreciation. In no case, however, was the credit to be less than 10 percent of the first $5,000 of new investment.

Proponents of this form of credit argued that the objective of the investment credit was to bring about an increase in the stock of productive capital and not simply to encourage the replacement of wornout or obsolete units in that stock. Net additions to plant and equipment, it was contended, have the greater impact on the general level of activity in the economy. Furthermore, they argued that a credit based on net new investment would exert a maximum impact on business investment decisions for a given loss of revenue.

Those who criticized the proposed type of credit were generally of the opinion that the modernization of existing capital was as important

[18] H. Doc. 140, 87th Cong., 1st sess. For further discussion see the President's 1961 Tax Recommendations, hearings before the committee on Ways and Means on the tax recommendations of the President contained in his message of Apr. 20, 1961, 87th Cong., 1st sess.

to the economy and, in particular, to our international competitive position as an increase in the total stock of capital. Therefore, they tended to favor a flat credit for all qualified investment. It was also contended that the proposed credit was too complicated and would encourage tax avoidance maneuvers. It was further argued that the proposed credit would tend to favor small, rapidly growing firms and discriminate against older firms with large stocks of accumulated depreciable assets. It was pointed out that the credit would tend to become less important over time since a firm could only increase the credit it received by accelerating its rate of growth. It was argued that a firm could not accelerate growth indefinitely and, therefore, would have to anticipate a lesser credit in a future period of stable growth. Finally it was argued that the proposed credit might intensify future business cycles.

2. Relation to depreciation

As first enacted, the investment credit was accompanied by a provision which required that the depreciation basis of an asset be reduced by the amount of the credit taken. In support of this provision it was argued that depreciation should be based on asset cost and that the 7-percent credit effectively reduced the cost of an asset. To permit full depreciation in addition to the credit, it was contended, was to permit depreciation in excess of cost.

Opposition developed to this provision, largely on the grounds of the inconvenience caused taxpayers, some of whom were required to keep separate sets of books for Federal and State income tax purposes. It was also pointed out that the credit did not affect the cost of an asset but rather tax liability, and that the effect of the depreciation provision was to reduce the value of the 7-percent credit by nearly 50 percent. The disputed provision was repealed in the 1964 Revenue Act.

3. Public utilities

The proper treatment of regulated public utilities under the investment credit has been the subject of considerable controversy. On the one hand, some have argued that the basic rationale for the credit does not apply to such companies and, therefore, its benefits should be denied them. Rate regulation, it is contended, assures utilities of a specified return on new investment. Thus these companies are not subject to the uncertainties faced by firms in more competitive industries. These uncertainties, it is contended, are the root cause of the need for an investment incentive. On the other hand, it has been argued that public utilities should receive the same incentive to new investment as other firms, and to exclude them from its benefits would be discriminatory and would discourage utilities from expanding their facilities. Investment capital might, it is pointed out, be diverted into fields eligible for the credit.

A related issue concerns the manner in which Federal regulatory agencies treat the investment credit for ratemaking purposes. The Revenue Act of 1964 prevents Federal regulatory agencies from immediately passing on the benefits of the credit to consumers through lower utility rates. In the case of natural gas pipelines, railroads, airplanes, trucks and buses, and other equipment used by public carriers on which a 7-percent investment credit may be taken, regulatory agencies are not allowed to take into account any reduction in taxes arising from the credit in their ratemaking calculations unless prior consent is received from the taxpayer. Agencies regulating utilities with assets eligible for only the 3-percent credit may adjust costs for ratemaking purposes, but not immediately by the full amount of the credit. Rather, they can take into account a proportionate part of the 3-percent credit during each year of the asset's useful life. Utility property for this latter purpose includes the assets of electric, gas, water, telephone, and telegraph companies.

Those who support the present provision regarding regulatory agencies argue that public utilities should not have to face the possibility that Federal agencies will, in effect, force them to forgo the benefits of the credit by requiring a corresponding reduction in utility rates. The so-called 7-percent utilities, it is contended, are in competition with nonregulated carriers and must receive the full credit to maintain a competitive footing. The 3-percent utilities, it is pointed out, are already denied much of the benefit of the credit by the lower rate which they must use. The provision protects the credit remaining to them.

Opponents argue that Federal regulatory agencies should not be required to base utility rates on taxes that were never paid. Furthermore, they contend that present practice discriminates between 7-percent and 3-percent utility properties on grounds which are not justified by the economic position of the companies involved. Finally, it is pointed out that the credit would raise the aftertax earnings of regulated utilities even if they received no direct credit. Since the credit would raise rates of return in nonregulated industries, regulatory agencies would raise the target rate of return taken into account in adjusting rates. The present treatment, it is argued, places public utilities in a better position in some cases than firms in more competitive industries where the investment credit will be at least partially reflected in a reduction in product prices.

CHAPTER 6

TAXATION OF INCOME FROM NATURAL RESOURCES

I. Present Law

The tax law contains several special provisions for the treatment of income derived from natural resources. Owners of such resources are accorded a number of optional provisions with respect to their capital costs. In recognition of the wasting character of mineral deposits, a special deduction, known as percentage depletion, is allowed which need bear no relation to actual development costs. Mineral producers may elect to recoup certain capital costs currently rather than deduct them over the life of the asset, as in the case of ordinary depreciable assets. Timber producers and coal and iron lessors may treat much of their profits as capital gains rather than ordinary income.

A. DEPLETION ALLOWANCES

Capital sums invested in the development of natural resource properties may be recovered through depletion allowances. These, like depreciation allowances, are deducted over the productive life of the property. In the case of mineral properties, depletion allowances are computed by either the cost depletion or percentage depletion method, whichever provides greater deductions.[1] Under the cost depletion method, which must be used with respect to timber, the adjusted basis of the property is divided by the total number of units estimated to remain in the deposit or property (i.e., barrels of oil, tons of ore, board feet of lumber, etc.) and the result is multiplied by the number of units sold during the year.[2] Cost depletion deductions cease when the adjusted basis of the property is reduced to zero.

Under the percentage method, depletion is computed as a specific percentage of the annual gross income from the property, but cannot exceed 50 percent of the net income therefrom.[3] Although allowable percentage depletion serves to reduce the basis of the property for the purpose of determining gain or loss at the time of sale, exhaustion of basis or the absence of any original basis does not preclude further percentage depletion allowances since these are related to the income from the property rather than to actual investment costs. Accordingly, percentage depletion allowances may be claimed with respect to the income from a property the basis of which has been completely written off through prior depletion allowances.

The percentage depletion rates prescribed by the law are as follows: [4]

(1) 27.5 percent, oil and gas wells.

(2) 23 percent, sulfur and uranium, and, if mined in the United States, asbestos, bauxite, and the ores of the metals cobalt, lead,

[1] Secs. 611-613.
[2] Reg. 1.611-2.
[3] Sec. 613.
[4] Sec. 613(b).

manganese, mercury, nickel, platinum, thorium, tin, titanium, tungsten, zinc, and 23 other strategic minerals.

(3) 15 percent, certain clays, asphalt, vermiculite, and metals not covered by (2) above.

(4) 10 percent, asbestos (if not covered by (2) above), coal, lignite, salt, and three other minerals.

(5) 5 percent, brick and tile clay, gravel, sand, clam and oyster shells, peat, pumice, sand, scoria, shale, rough stone, and certain brine well products.

(6) 15 percent, all other minerals except soil, sod, dirt, turf, water, or mosses, or minerals from sea water, the air, or similar inexhaustible sources.

Two exceptions are made for this last group Some of these minerals may be listed in (2) above if produced in the United States All of these minerals, in addition, are subject to a use test, i.e., they are restricted to the 5-percent rate, whether or not domestically produced, when used for purposes comparable to common sand, gravel, or rough stone.

Depletion allowances are generally available to every person who has an economic interest in and receives income from the exhaustion of a natural resource, the total allowances being apportioned among the various parties in interest. Such allowances, however, may not be claimed by taxpayers whose economic interests in depletable properties are indirect, such as shareholders or creditors of a corporation which owns the mineral properties.

The 1913 income tax legislation provided a reasonable allowance for depletion, not to exceed 5 percent of gross income, for wasting mineral assets. This was later changed to a more specific allowance for depletion based on the cost or 1913 value of the property. Allowances in excess of cost depletion were granted, in the form of discovery depletion, in 1918 to stimulate mineral exploration for war purposes and to lessen tax burdens on small-scale prospectors who made discoveries after years of fruitless search. Discovery depletion deductions allowed the discoverer of any new mineral deposit to recoup not only his costs but also the materially larger appreciated value of the property at the time its profitability was established. In 1921, disturbed by the extent to which large discovery depletion deductions were being used to offset other income, the Congress limited annual discovery depletion to the amount of net income from the mineral property. In 1924, it further lowered this limitation to 50 percent of net income.

Discovery depletion was eliminated for oil and gas properties in 1926, and for metals, sulfur, and coal in 1932, by substituting allowances based on a percentage of gross income. The 50 percent of net income limitation was retained. Percentage depletion was gradually substituted for discovery depletion on other minerals, until, in 1954, discovery depletion was eliminated altogether. The original percentage depletion rates for oil and gas and metals were, in general, fixed at levels designed to afford these industries approximately the same total annual depletion which they had been allowed under discovery depletion. The percentage depletion rates on coal, sulfur, and other nonmetallics were not based on industry experience under prior discovery depletion allowances but were selected to provide tax relief and incentives deemed suitable by the Congress in view of the rates accorded oil and gas and metals. Subsequent legislation increased these rates in numerous cases.

B. EXPLORATION AND DEVELOPMENT COSTS

In addition to depletion allowances, the tax law also provides special treatment for certain capital expenditures incurred in bringing mineral properties into production. Section 615 of the Internal Revenue Code permits a taxpayer either to write off as incurred the costs of exploring for mineral deposits (except oil and gas wells) or to set these up as deferred expenses to be deducted ratably as the deposit is exhausted. Included in exploration expenses are expenditures to ascertain the existence, location, extent, or quality of mineral deposits. Deductions for exploration expenditures are limited to $100,000 per year and a total of $400,000.

Section 616 of the Internal Revenue Code permits a taxpayer either to write off as incurred the costs of developing a mineral deposit (except oil and gas wells) or to set these up as deferred expenses to be deducted ratably as the deposit is exhausted. Development expenses include expenditures for mine shafts, tunnels, and stripping which are incurred after the presence of minerals in sufficient quantity and quality to justify commercial exploitation has been ascertained. If the expenditures are incurred during the development stage of a mine, the election to treat the expenditures as a deferred expense only applies to the excess of the expenditures over the net proceeds from the mine during the year the expenses were incurred; if the expenditures are incurred during the production stage of a mine the full amount of the expenditure may be treated as a deferred expense. There is no dollar limitation imposed on deductions for development costs.

Section 263(c) of the Revenue Code grants oil and gas operators the option of either capitalizing or charging as a current expense so-called intangible drilling and development costs of wells. The expenses currently deductible include those for labor, fuel and power, materials and supplies, tool rental, repairs of drilling equipment, and nonrecoverable materials used in drilling, if incurred while drilling a well or preparing it for production. There is no limit to the amount of such outlays which may be deducted.

The current expensing deductions for mine development expenditures and exploration costs were first granted in the Revenue Act of 1951, which limited the annual deduction for exploration expenses to $75,000 in each of any 4 years; the 1954 code raised this limit to $100,000. In 1960, the 4-year limitation was replaced by a total limitation of $400,000 which may be spread over any number of years. The privilege of expensing the intagible drilling and development costs of oil and gas wells has existed since an administrative ruling under the Revenue Act of 1916; a concurrent resolution of Congress in 1945 assured its continuance, and finally an express statutory provision was incorporated in the Internal Revenue Code of 1954.

To some extent, exploration costs of oil and gas wells are also currently expensed through loss deductions which are allowed by the regulations governing the treatment of the cost of exploration projects that prove unsuccessful and are dropped (such as dry wells and surrendered leases). However, geological and geophysical expenditures resulting in the acquisition or retention of properties are not deductible as ordinary expenses but must be capitalized.[5]

When currently expensed, the capital costs incurred in the exploration and development of mineral properties are not included in the adjusted basis of the properties, which determines the sum to be recovered through cost depletion. Broadly speaking, these deductions are in lieu of cost-depletion deductions. On the other hand, the expensing of such costs does not serve to reduce percentage-depletion allowances, which are based on the income from the property.

C. OTHER SPECIAL TAX PROVISIONS

A number of other specific provisions afford special tax treatment to taxpayers in the extractive industries. For example, recipients of grants from the United States for the encouragement of exploration, development, or mining of critical and strategic minerals or metals for national defense may exclude such grants from taxable income.[6]

Special treatment is also accorded income arising from certain types of timber cutting and iron and coal mining operations. A taxpayer owning timber or the contract right to cut timber for a 6-month period prior to the beginning of the taxable year may elect to treat the proceeds from cutting the timber as a long-term capital gain.[7] A taxpayer owning timber, coal or iron ore for a period of 6 months before its disposal who retains an economic interest following such a disposal is permitted to treat the royalties received as long-term capital gains. If the net result is a loss, however, it may be treated as an ordinary loss.[8] This provision as applicable to timber was added in 1943, extended to coal in 1951, and extended to iron ore in 1964. In 1954, the election to treat income from timber as a capital gain was extended to producers of Christmas trees which are more than 6 years old when cut.[9]

In 1954 mineral operators were permitted to aggregate producing properties in the same "operating unit" for the purposes of computing gross income and the depletion allowance. An operating unit proved difficult to define in the case of oil and gas wells and operators in this industry were able, in certain cases, effectively to circumvent the 50 percent of net income percentage depletion limitation by grouping high-cost and low-cost properties from widely scattered geographical areas. The Revenue Act of 1964 eliminated the operating unit rule with respect to the oil and gas industry and restored pre-1954 administrative practice, which generally confines aggregations to operating interests in a single tract or parcel of land.[10]

II. Issues

It is generally agreed that mineral resources, because of their wasting nature and their importance in an industrial economy, are an appropriate concern of public policy. Issues that have arisen concerning the taxation of income from the extractive industries include effects

[5] I.T. 4006, 1950-51 C.B. 48.
[6] Sec. 621.
[7] Sec. 631(a). The purpose of this provision is to give the taxpayer the benefit of the capital gain rate which he would get if he sold the timber for cutting rather than cutting it himself.
[8] Sec. 631(b)(c).
[9] Sec. 631(a).
[10] Sec. 614.

on the allocation of resources, tax equity and revenue, national defense, and prices.

A. THE ALLOCATION OF RESOURCES

One of the major criticisms directed against the present tax treatment of income from the extractive industries is that it encourages serious misallocation of resources.[11] It is contended that the present preferential tax provisions induce a level of investment in these industries at which the pretax rate of return is substantially below that prevailing, on the average, elsewhere in the economy, although the after-tax rate of return, by virtue of tax preferences, is about the same. Present tax provisions, in other words, encourage investors to commit to the development of mineral deposits resources which would produce a greater, more valuable product, judged by the preferences expressed in the market, in other lines of activity. Preferential tax provisions, therefore, are said to be in fact a subsidy which promotes overinvestment and the development of excess capacity in the extractive industries.

In further development of this argument, it is pointed out that in a fully employed economy, efforts to increase the level of activity in any one industrial area must necessarily be at the expense of output in other sectors of the economy, at least in the short run. Tax policy which affords special privileges with respect to particular types of business activity, therefore, should be based not only on the absolute level of demand in the economy for the output of the affected industry, but also upon careful and explicit consideration of relative priorities. If tax treatment were neutral in the sense that all industries were taxed alike, the relative priority of mineral output would be expressed through the market mechanism in the price of such output as compared to that of other industries. Thus, if users of mineral products anticipated an increased demand, this would be reflected in a relative increase in the prices of the affected minerals which would serve to attract additional resources to these industries and away from those for which anticipated demand was either falling, stable, or increasing at a lesser rate. With preferential tax treatment only indirectly related to the pricing process, however, economic priorities in mineral industries are not accurately measurable. As a corollary, the real costs of these tax incentives, in terms of the loss of the alternative products of the extra resources in extractive industries, has not been determined.

In rebuttal, however, it has been argued that income taxation at uniform rates is not neutral because of differences in the degree of risk and the intensity of capital investment between industries. In the extractive industries, it is contended, large capital outlays must often be made in connection with extremely risky ventures, particularly those connected with the discovery of new deposits. In the absence of special tax provisions investment would tend to flow into industries where investments were less risky and required less of an initial capital outlay. Present special provisions then provide an offset to the allocation effects of a uniform tax on investment profits.[12]

[11] See Harberger, "The Taxation of Minteral Industries," Tax Compendium, pp. 439–449, and "Federal Tax Policy for Economic Growth and Stability," hearings before the Subcommittee on Tax Policy of the Joint Committee on the Economic Report, 84th Cong., 1st sess. (hereinafter cited as hearings), pp. 355–356 and 364 ff. See also Steiner, "Percentage Depletion and Resource Allocation," Ways and Means Compendium, pp. 949–966.

[12] See Stephen L. McDonald, "Federal Tax Treatment of Income From Oil and Gas," the Brookings Institution, 1963, ch. III.

In support of this contention it is pointed out that if present tax provisions had encouraged overinvestment in the minerals industries, existing reserves would be much larger than they are. Present reserves, it is argued, are not large relative to likely future demand and in view of the long leadtime required to bring in and develop new deposits.

Some critics question whether the degree of risk in the extractive industries is significantly greater than in other industries. They point out, for example, that the ratio of unproductive drillings to producing wells in the exploratory drillings of the oil and gas industry does not vary greatly from year to year, suggesting that the degree of risk can be predicted and, in a sense, insured against, with a fair degree of accuracy. It is also contended that there are severe risks connected with investments in other types of industrial activity. It is questioned whether capital invested in the development of electronics, atomic energy, and other new industries is not equally at risk as capital in the extractive industries. It is also pointed out that in the capital markets the major mineral resource companies are not given poorer investment ratings than many other enterprises whose products are widely used.

Moreover, it is argued that the appropriate treatment for any extraordinary risk in prospecting for and developing mineral resources lies in assuring adequate offsets for the losses which may be sustained. In the case of large firms, self-insurance against these risks is provided through the reduction in tax liability which results when losses are offset against the income from established mineral properties or against the income derived in other lines of activity.

Critics also point out that present tax treatment often results in the greatest tax benefit for those who assume the least risk. The risks of exploration and development are assumed to be greatest for small operators. Indeed, it was to offer encouragement to the small operator that special depletion allowances were first introduced. The most recent data available show, however, that 75 percent of the $3.6 billion in depletion allowances claimed by corporations in 1961 was claimed on returns from firms with assets of $100 million or more; 89 percent was claimed by corporations with assets of $10 million or more, and 97 percent was accounted for by corporations with assets of at least $1 million.[13] Companies of this size are in a position to protect themselves from expected losses and, in effect, insure against the extraordinary risks of prospecting and developing particular mineral properties by diversifying their efforts. Moreover, only the large firm is likely to be able to offset any losses fully against other income in the years losses are sustained. Finally, since percentage depletion allowances depend on the income from a property, they offer the small operator little protection against risk in the exploratory stages of an operation. Indeed, the tax benefits of depletion are obtained only after the property begins to produce on an established basis.

Those who favor the continuation of the present system of allowances point out that while the ratio of productive to nonproductive exploratory ventures may not fluctuate greatly in certain mineral

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[13] Internal Revenue Service: Statistics of Income—1960-61, Corporation Income Tax Returns. See appendix table 45.

industries, many productive deposits yield little actual return and therefore the value of new deposits discovered fluctuates markedly. Furthermore, they argue that while percentage depletion may be excessive in a literal accounting sense, the excess represents a necessary incentive to mineral producers for continuing exploration and development activity.

Moreover, it is argued, percentage depletion allowances are an important source of the funds required to finance the development and exploitation of mines and wells. Small, independent producers particularly would be hard hit by elimination of these allowances and would be forced to curtail their exploration and development programs. This would be especially true in the case of the relatively small firms engaged in stripper operations, since the profitability of such operations, it is alleged, depends to a large extent on favorable tax treatment. Curtailing these operations would result in a considerable waste of recoverable mineral resources. On the other hand, large vertically integrated firms would be in a relatively stronger position, since they are able to draw on their resources from processing and marketing operations and have readier access to capital markets.

B. EQUITY AND REVENUE ISSUES

It is maintained that there is no theoretical justification for treating mineral producers in a manner different from other taxpayers. With respect to most expenditures for fixed capital, it is pointed out, the tax law limits total deductions for capital recovery to the amount actually invested by the taxpayer and requires that these deductions be spread over the useful life of the property. In the extractive industries, on the other hand, the taxpayer is allowed to recover tax free virtually the full amount of his investment in a mineral property often in the year the outlays are made and subsequently claim percentage depletion allowances which bear no relationship to the amount of his investment. Accordingly, the law may permit tax-free recovery of his capital costs several times over. In fact, it is contended, from the standpoint of accounting or economics, it is questionable whether these special deductions should properly be called depletion, since they do not relate to any capital sum that is being exhausted.

The effect of present provisions regarding natural resources is said to be apparent from the six specific cases compiled by the Treasury Department in connection with the Senate debate on the Revenue Act of 1964.[14] The economic income of these individual operators was $35.7 billion in 1960. Economic income was defined as receipts less deductions for ordinary costs including operating expenses, depreciation, cost depletion, exploration costs, and abandonment losses. Economic income did not include, however, allowances for percentage depletion in excess of cost depletion, deductions for the current expensing of development costs, the net long-term capital gains exclusion, or provision for the installment treatment of gains from the sale of oil production payments. Because the latter were recognized for Federal tax purposes, total tax paid was only $371,000, or 1 percent of total economic income. The following table summarizes these examples.

[14] The examples were furnished at the request of Senator Paul H. Douglas and appear in the Congressional Record, Dec. 12 and 13, 1963, pp. 23227-23233 and 23316.

TABLE 21.—*Selected examples of high-income taxpayers with income from oil and gas properties and low effective tax rates, 1960*

Taxpayer	Total economic income	Reported economic income	Adjusted gross income	Net taxable income	Federal income tax	Federal income tax as percentage of total reported economic income (col. 2)
A	$4,542,447	$2,110,060	$405,376	$317,284	$166,768	7.9
B	4,020,349	2,271,723	(723,916)	(725,252)	0	0
C	2,201,278	1,707,839	454,404	240,016	142,808	8.4
D	28,716,932	26,440,776	[1](556,626)	[2](846,330)	0	0
E	1,522,478	1,179,248	[1] 330,645	[2](184,992)	0	0
F	1,307,962	1,029,540	135,633	[2] 131,945	61,240	5.9

[1] After carryover of net loss. Parentheses indicate a negative amount.
[2] Before personal exemptions.

Source: Congressional Record, Dec. 12, 1963, p. 23233.

In the most outstanding case, a taxpayer paid no Federal income tax in the year in which he sold a reserved oil and gas production payment upon which he would realize a gain of $26 million. In part, this result was attributable to the application of section 453(b) which permits a taxpayer to receive such a gain in installments. In addition, however, percentage depletion deductions in excess of cost and intangible drilling expenses provided over $2 million of deductions.

In the five remaining examples, of the total economic income of $8.3 million, $3.8 million, or 46 percent, was offset by deductions for percentage depletion and $2.6 million, or 32 percent, was offset by deductions for intangible drilling expenses. In two of the six cases the sum of these deductions exceeded net income derived from oil and gas production and the excess served to reduce the amount of income from other sources subject to tax.

The distinction between these two types of deductions, it is alleged, is important in appraising the present tax provisions for natural resources. Percentage depletion in excess of cost depletion represents, in effect, a deduction which does not represent a specific expenditure involved in the production of income. Expensing deductions are available, however, only where current income is immediately invested in further oil development. Those individuals in this group with the least tax liability were currently investing large amounts of income in oil production. Critics of these allowances contend that while this investment may be socially desirable, it is questionable whether investment in oil has sufficient social priority over other investment to warrant this preferential treatment.

With regard to corporations, it is pointed out that a Treasury survey for the years 1958–60 indicated that of the $3.3 billion in depletion allowances claimed by corporations in 1960, over 91 percent was estimated to be in excess of cost basis depletion.[15]

In support of depletion deductions in excess of cost it is argued that depletion should be based on the value of the mineral deposit discovered rather than on the actual outlay involved in making the discovery. If depletion deductions were limited to the cost of locating producing properties, it is said, no account would be taken of the cost of many unproductive ventures. Assuming that total capital outlays

[15] See the President's 1963 tax message, pp. 290–350.

in mineral development tend to equal the value of deposits discovered, it is contended, discovery value depletion would approximate the results obtained in industries where outlays and investment returns are equal on an individual project basis. Percentage depletion, it is argued, was introduced as an administratively feasible alternative to discovery value depletion and the rates were originally set to approximate deductions under the former method.

The argument that depletion deductions should be based on an approximation to the value of the resources discovered is held to be without substance by observers who point out that capital allowances elsewhere in the law are not based on market valuations but on the actual amount invested by the taxpayer. Generalization of the discovery value approach, it is maintained, would mean the exemption of most, if not all, capital gains from tax, and consistency would require the upward adjustment of deductions for depreciation, inventories, and other cost items whenever the current value of an asset exceeded its original cost. It is maintained that the excess of the value of a developed property over its cost represents income in the form of a capital gain. No occasion, therefore, exists for deducting any amount which exceeds the original investment. Furthermore, even if percentage depletion could be justified on the basis of discovery value, deductions for developmental outlays, such as those for unproductive exploratory ventures, surrendered leases, and intangible drilling costs, should not also be allowed since the final effect is to permit a double deduction for such discovery value.

The revenue effect of percentage depletion and development cost allowances is cited as a major reason for revising the law in this area. The Paley Commission estimated the revenue loss attributable to excess depletion claimed by individuals and corporations in 1948 was about $530 million.[16] Taking into account changes in tax rates, output and prices of mineral products, the extension of percentage depletion to additional minerals, and the increase in depletion rates since 1948, the present loss may total $1.25 to $1.5 billion.

Proponents of percentage depletion point out that in the absence of such allowances, the tax law would involve a much greater impetus than now exists for the taxpayer who discovers and develops mineral properties to sell them rather than to operate them himself. Sale of the property would involve capital gains tax liability on the present value of the proceeds from gradual liquidation of the property over time. This commuted value, which would be taken as the basis of the property by the purchaser, would be written off under the cost-depletion method, the allowances under which would exceed percentage depletion. Accordingly, it is argued that the Government would obtain little, if any, net revenue gain from the elimination of percentage depletion while such elimination would encourage the sale of such properties rather than their operation by those discovering them. This would undoubtedly result in an increasing concentration of mineral properties in the hands of fewer and fewer producing companies, with attendant adverse implications for the competitive structure of the economy.[17]

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[16] "Resources for Freedom," vol. V, a report to the President by the President's Materials Policy Commission, 1952, p. 14.

[17] See hearings, pp. 360–362, 384–387.

The proponents of present provisions further maintain that the extraction and sale of minerals in fact represents the disposition of capital. In this respect, a mineral property differs from a depreciable facility. The latter loses some value in the course of producing income, but nevertheless remains in place as a whole physical asset. A mineral property, on the other hand, actually disappears in the course of its exploitation. Proceeds from the sale or other disposition of the mineral production, therefore, should be treated as capital transactions. Under present law, this would involve a maximum tax of 25 percent. Percentage depletion serves to reduce the effective tax rate below 25 percent only in exceptional cases; as a matter of fact, it is contended, the effective income tax rate on income from mineral properties frequently exceeds that which would be payable with respect to gains realized on other capital transactions.

Finally, proponents of the present system maintain that it has become capitalized in the financial structure of the Nation's extractive industries. It is argued, therefore, that any drastic revision of the present law would occasion significant changes in financial structure and policy, which almost certainly could not be accomplished in an orderly manner. Such changes, moreover, would probably result in the elimination of a substantial number of independent producers and significant capital losses for shareholders in all oil-producing companies. The revenue gains to the Government from elimination of so-called excess depletion allowances, accordingly, would be more than offset by virtue of capital loss offsets and in the long run by a contraction in the tax base.

C. NATIONAL DEFENSE CONSIDERATIONS

Support for continuing the present tax treatment of income from minerals is frequently based on the Nation's defense demands. Many of the mineral resources with respect to which percentage depletion is allowed, it is pointed out, are basic to the Nation's defense. It is essential, therefore, to keep these industries operating vigorously and profitably in order to insure adequate domestic supplies in the event of war. The elimination of percentage depletion, it is argued, would require a substantial increase in the prices of minerals to prevent a substantial contraction of production. Since these prices are largely determined in a world market, however, it is unlikely that the necessary increases would be forthcoming. The result would be dependence on foreign sources, which might leave the Nation in perilous circumstances in a defense emergency.

Moreover, it is argued that since defense demands differ in character from those originating in the private sector of the economy and cannot be evaluated in the market, it cannot be asserted without serious qualification that the present tax provisions lead to overinvestment in the extractive industries. Active hostilities might well establish that present domestic reserves have not been developed extensively enough and place an extraordinary premium on the capacity of the minerals industries.

On the other hand, those opposed to the present tax arrangements contend that to the extent that national defense considerations are dominant, they call for more effective conservation practices in conjunction with exploration and development activity. Percentage depletion, it is pointed out, takes effect only as reserves are used and therefore provides an incentive to draw down rather than conserve reserves. In the absence of this tax preference, it is maintained, the price of mineral products would rise, thereby limiting consumption. Accordingly, it is contended, percentage depletion is not required in the interests of national defense, and in fact is inconsistent with such interests. Moreover, in view of the significant changes that have occurred in methods of warfare and weapons technology, percentage depletion, by diverting resources to the mineral industries, may impede the development of other industries with as much if not more defense importance.

It is pointed out that the national defense argument outlined above assumes that the differential tax treatment of natural resources causes overinvestment in the extractive industries. If, on the other hand, this tax treatment is neutral in the sense that it merely offsets the differential risk in this industry, then its contribution to defense and conservation is neutral. From a broader viewpoint, however, present tax treatment may contribute to a strong economy which in a sense is the best provision for national defense.

D. PRICE EFFECTS

Objection to proposals for repealing or curtailing the tax provisions which deal with natural resources is often based on the effect such a program would allegedly have on prices. It is contended, for example, that reducing or eliminating percentage depletion would tend to raise the price of such products as gasoline by raising the real cost of extraction and discouraging investment in the search for new deposits. The final effect would simply be an increase in the price paid by consumers.

The effect on price has been debated. Some maintain that much of the increased tax resulting from repeal of the present provisions would, at least in the short run, be absorbed by producers who now pay lower-than-average tax liabilities. Furthermore, it is contended, significant cost reductions could be effected through the more efficient use of existing facilities. Present prices are maintained, it is said, in some instances only by the action of State regulatory commissions in restricting production. Finally, eventual price effects would depend on the strength of consumer demand for mineral resources. While consumers might be unable or unwilling to restrict their use of such products in the short run, they might well shift to substitute products in the long run, a tendency which would hold down prices.

III. Proposals for Tax Revision

A wide variety of proposals have been offered for revision of the tax treatment of income derived from mineral properties. In most cases these proposals have sought to mitigate the tax avoidance opportunities in the present law while retaining certain incentive features.

The most extreme proposal calls for the complete elimination of percentage depletion and the limitation of deductions for capital recovery to the adjusted basis of the property.

Another proposal would permit the taxpayer to claim percentage depletion allowances but would limit the total of such allowances to the adjusted basis of the property. Under this proposal, percentage depletion allowances would represent an alternative to expensing the capital costs incurred in exploration and development, since current deductions for such costs would reduce the adjusted basis of the property. A more liberal variation of this proposal would permit both the expensing of capital costs and percentage depletion, limited in the aggregate to the original cost of the property. In effect, this would permit the taxpayer to write off up to twice the amount of his actual investment in the mineral property.

It has also been suggested that a 3-year income tax exemption be substituted for percentage depletion on new mineral deposits. Taxpayers would be permitted to expense exploratory and development costs, as under the present law, and would be exempt from tax on the first 3 years' income from the mineral property. Thereafter, however, no capital recovery allowances of any sort would be permitted.

Perhaps the least drastic revision suggested in this area would make no fundamental change in the present provisions but would reduce percentage depletion rates on most mineral properties. Reduction of the depletion rates for oil and gas and metals produced in the United States to 15 percent has been urged. While this proposal would not eliminate the objection that percentage depletion permits the multiple tax-free recovery of investment, it would significantly reduce the current revenue loss. One variation of this proposal would allow the present depletion rates for small producers and provide a sliding scale of reduced rates for larger producers.

It has also been suggested that the net income limitation be reduced from the present 50 percent to, say, 25 or 30 percent. This revision would bear least heavily on properties with a high ratio of net income to gross income. In the case of many oil royalties, net income commonly is equal to gross income. In such cases the net income limitation would not serve to reduce percentage depletion allowable unless the limitation were less than 27.5 percent of net income.

The contrary proposal has also been offered. It is pointed out that the net income limitation serves to curtail percentage depletion allowances for mineral producers with relatively low ratios of net income to gross income. It is asserted, for example, that a large proportion of the operators in the bituminous coal industry are unable to use the full allowance of 10 percent of gross income because they operate on a very narrow profit margin and are subject to the net income limit. Such firms, it is claimed, need at least as much preferential treatment as is afforded the more profitable operations. Those who defend the net income limitation, however, point out that operators with persistent losses or very small profit margins would derive little benefit from its elimination while the principal benefits would accrue to more successful operations.

Finally, it has been proposed that all elements of preferential tax treatment in the natural resource area be eliminated in favor of relying on nontax incentives for mineral resource development. Direct subsidies, stockpiling of strategic materials, price supports, extension of development loans or bonuses, and similar arrangements have been suggested as more effective devices for directing incentives to those lines of activity where they are most needed. In addition, it is maintained that such programs would reveal the real cost of these incentives to public scrutiny through the regular executive and congressional budget processes, in contrast with tax benefits, which in character and scope receive little public attention.

CHAPTER 7

RETIREMENT PLANS AND DEFERRED COMPENSATION

At the end of 1962 over 23 million employees were covered by some form of private pension, deferred compensation, or profit-sharing plan designed to provide retirement income. Employer contributions to such plans totaled $4.7 billion and were supplemented by $0.8 billion in employee contributions. Benefits totaling more than $2 billion were paid out to slightly over 2 million retired employees. Reserves for future payments had reached $60 billion. The growth of these plans is of relatively recent origin and reflects a number of influences, including employer realization that such plans improve the attitudes and performance of employees, the demands of organized labor, and a general concern for the provision of economic security. The growth of these plans has also been encouraged by tax provisions which allow tax deferral on contributions made on behalf of covered employees. Moreover, the tax benefits of qualified retirement plans formerly reserved for employees have recently been extended to the self-employed.

I. Present Law

A. EMPLOYEE PENSION, PROFIT-SHARING AND STOCK BONUS PLANS

1. Description of plans

Under these plans, an employer makes regular contributions on behalf of covered employees to a trust or to an insurance company which assumes the obligations of meeting benefit payments to employees as they fall due. Frequently these contributions are supplemented by contributions from participating employees. Generally, benefits are not paid unless the employee has reached a designated retirement age, completed a certain number of years of service, or fulfilled similar specific conditions.

Pension plan contributions and benefits, in contrast to those of profit-sharing and stock bonus plans, are generally based on such factors as years of service and compensation received. Moreover, they usually provide specifically determined benefits upon retirement. Under profit-sharing plans the size of benefits depends primarily on the employer's profits, either current or accumulated. Stock bonus plans provide benefits similar to profit-sharing arrangements, except that payments are made in the stock of the employing company and may be made out of capital rather than profits. In some employee retirement programs the features of the three types of plans are mixed.

Retirement plans usually provide definite and predetermined formulas for determining contributions and benefits. Usually, contributions to such plans are funded either in trusts, group annuities, or individual contracts. Trusteed plans involve the creation or designation of a trust organization to receive and manage contributions

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and to make benefit payments. Group annuity plans generally operate without the intercession of a trustee; the employer pays to an insurance company the premiums necessary to cover the full cost of a unit of annuity benefit on behalf of all covered employees taken together. Individual contract plans involve the employer's purchasing from an insurance company on behalf of each employee either an annuity contract or a retirement income contract, which combines the features of life insurance and an annuity.

2. *Tax treatment*

Broadly speaking, the tax treatment of these various types of retirement programs is the same. The nature of the plan, whether pension, profit sharing or stock bonus, and the means of financing benefits generally involve only minor differences in taxation.

(*a*) *The trust.*—The income of a trust forming part of a pension, profit-sharing, or stock bonus plan of an employer for the exclusive benefit of his employees or their beneficiaries is not taxable if the plan meets the following conditions: (1) the plan is permanent; (2) distributions of benefits under the plan are on the basis of some predetermined formula; (3) the principal or income from the fund is not used for any purpose other than distribution to employees until all commitments to employees and their beneficiaries have been met; (4) the plan benefits either (i) 70 percent of all the employees or 80 percent of all eligible employees provided not less than 70 percent of all employees are eligible, or (ii) all employees within a classification which does not discriminate in favor of certain highly paid employees; (5) contributions and benefits under the plan do not discriminate in favor of highly paid employees.[1] A plan which meets these "nondiscrimination" tests is referred to as a "qualified" plan.

(*b*) *Pension reserves of insurance companies.*—Similarly, under the Life Insurance Act of 1959, income attributed to insurance reserves for qualified pension plans is exempt from tax.

(*c*) *The employee.*—Employees participating in a qualified retirement plan do not include in their current taxable income amounts representing their employers' contributions to such plans. Tax liability results only when benefits are distributed.[2] Employees may not deduct their own contributions to the plan.

There are two methods for including employer-financed benefits received in the form of an annuity in a retired employee's taxable income. Under the life-expectancy method, a portion of each annuity receipt is excluded from the recipient's income, the remainder being fully taxable. The excluded portion is determined by applying to the amount of each annuity payment the ratio of the amount paid for the annuity by the employee to the total amount of annuity payments which will be received on the basis of the annuitant's life expectancy. If the employee has made no contributions to the plan, the full amount of each annuity payment he receives is taxable.[3]

A special provision is made in the case of benefits received from a plan to which both employer and employee have contributed where the amount of the annuity to be received in the first 3 years after the pension starts equals or exceeds the employee's contribution. In such cases, the employee excludes from his income the full amount of

[1] Sec. 401.
[2] Sec. 402.
[3] Sec. 72.

each annuity payment received until he has recovered an amount equal to his total contribution; amounts received thereafter are taxable in full.

A lump-sum distribution by a qualified plan made in a single taxable year to the employee or his beneficiary when the employee leaves the firm is taxed to the employee as a long-term capital gain. If the distribution includes securities of the employer corporation, the tax on any appreciation in value of such securities is deferred until the securities are sold.[4]

The tax treatment of the employee under nonqualified plans depends on whether or not his rights to benefits are nonforfeitable. When the rights are nonforfeitable, the employer's contributions must be included in the employee's taxable income. Contributions that are currently taxable to the employee, however, constitute his consideration in the later application of the life-expectancy annuity rule. If the employee does not have vested rights in the benefits of the plan at the time the employer's contributions are made, the contributions are not included in his taxable income currently and the full amount of the benefits are taxable to him when received.[5]

(*d*) *The employer.*—The tax treatment of an employer's contribution to a retirement plan depends first on whether such a plan qualifies under the provisions of section 401 and, second, on the nature of the plan.

The employer may deduct contributions actually paid into plans not qualified under section 401 only if the employee's rights therein are not forfeitable. On the other hand, if employees have no vested rights to benefits under a funded plan, the employer may only deduct his contributions at the time the distributions are made to the employee or his beneficiaries.

If the retirement plan qualifies under section 401, the extent of the employer's deduction for contributions depends on whether it is a pension, profit-sharing, or stock bonus plan.

Deductions for contributions to qualified pension plans, whether trusteed or not, may not exceed 5 percent of covered payrolls, except where a larger amount is necessary to provide the unfunded cost of past and current service credits, distributed as a level amount or as a level percentage of compensation for the future service of each employee. As an alternative, the employer may deduct the normal cost of the plan for the current year (on the assumption that it had been in effect since the beginning of covered service of each employee), plus 10 percent of total past and supplementary service costs as of the date they are included in the plan.[6]

Employer's contributions to qualified profit-sharing and stock bonus plans are deductible up to 15 percent of the compensation of covered employees.[7]

Where qualified pension, profit-sharing, and/or stock bonus plans have been established in combination, the employer's deductible

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[4] Sec. 402.

[5] Sec 72.

[6] Amounts contributed in excess of the deductible portion under these limitations may be deducted in succeeding taxable years to the extent of the difference between the amount contributed and the amount deductible under the limitations in each succeeding year.

[7] Contributions in excess of 15 percent of covered compensation may be carried over and deducted in succeeding taxable years within the preceding limitation. On the other hand, in years in which the contribution is less than 15 percent of covered compensation, a credit carryover arises which is available in succeeding years to absorb contributions exceeding the 15-percent limit.

contributions are limited to 25 percent of the compensation of covered employees.[8]

B. DEFERRED COMPENSATION CONTRACTS

Deferred compensation contracts differ from pension and similar retirement programs in that they do not constitute a formal plan providing retirement benefits for employees generally (or for a particular group of employees, where the nondiscriminatory requirements of section 401 are observed) and, therefore, usually are not funded. Under such contracts, the employee agrees to forgo a specified portion of current compensation which will be paid to him over a specified and limited period of time in the future, often after retirement.

The regulations permit the employer to deduct amounts paid as compensation to employees in the year when paid, regardless of the fact that the employee is no longer active in the employer's behalf, so long as the total compensation for the years of active employment is reasonable. So far as the employer is concerned, therefore, salary payments under deferred compensation contracts may not be deducted until actually distributed to the employee, even though accruing in a year preceding distribution.

For a considerable period of time, the taxability of the employee with respect to deferred compensation under these contracts was not clearly defined in the code or the regulations. In 1960, however, the Internal Revenue Service indicated (Revenue Ruling 60–31) that as a general rule such deferred compensation is taxable in the year it is received provided that the employee did not have a right to receive it previously.

Qualified stock options are a popular method of providing deferred compensation to certain employees. Under such plans, a participating employee is granted an option to acquire shares of stock in the employer corporation at market prices as of the date the option is granted. While the option must be exercised within 5 years, any gain arising as a result of an increase in the value of the stock is not taxed until the employee disposes of the stock, and then, if it has been held at least 3 years, at long-term capital gains tax rates.[9]

C. SELF-EMPLOYED INDIVIDUALS RETIREMENT PLANS

The Self-Employed Individuals Tax Retirement Act of 1962 [10] permits self-employed individuals, including members of a partnership, to establish retirement plans whose benefits and contributions are taxed in roughly the same manner as those pertaining to employee retirement plans. Passage of the act culminated years of controversy which arose from the fact that self-employed persons were formerly not eligible for the tax treatment received by employees covered under a pension or other retirement plan established by their employer. The growing popularity of corporations formed by doctors and other professional men under recently passed State laws allowing them to incorporate is attributed, in part, to an attempt to obtain similar tax treatment for retirement plans as that granted employees under qualified plans.

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[8] Sec. 404. Contributions in excess of this amount may be deducted in succeeding taxable years, provided the total deduction does not exceed 30 percent of the compensation of covered employees.

[9] Secs. 421-425. See Ch. 4, "Capital Gains Taxation."

[10] Public Law 87-792, 87th Cong.

A self-employed individual may deduct 50 percent of the contributions he makes for his own benefit to a qualified retirement plan, but his total contributions for the purposes of the deduction may not exceed the lesser of $2,500 or 10 percent of his earned income.[11] The deductible share of the contributions and the earnings that accrue to the assets in the plan are not taxable until distributed to the self-employed person. Distributions under qualified plans cannot be made before the self-employed person reaches the age of 59½, unless he becomes disabled, but must begin before he reaches the age of 70½. When the benefits are distributed they are taxed as ordinary income. Lump-sum distributions may be eligible for averaging under section 72(n), which permits such benefits to be taxed at five times the increase in liability which results from adding one-fifth of the distribution to the taxpayer's gross income for the year in which the distribution is made.

To qualify, the self-employed retirement plan must provide for the investment of contributions in a specified manner. The funds can only be used to purchase special Federal Government bonds, certain insurance contracts, stock in a regulated investment company, certain face amount certificates of an investment firm or investment trust, or be paid into a trust administered by a bank. The self-employed person must provide comparable retirement benefits on a nondiscriminatory basis to all his full-time employees, if any, who have been employed by him for 3 years or more. Furthermore, the covered employees must be given nonforfeitable rights in connection with the plan.

Penalties are imposed for excess or premature distributions, and for engaging in prohibited transactions involving the use of the funds contributed to the plan.

II. Issues and Proposals

The growth of private pension, stock-bonus and profit-sharing plans and other arrangements for deferring compensation of employees has significant implications for the development of the economy. Accordingly, the effect of tax provisions in encouraging or discouraging the further growth of these devices is an issue in Federal tax policy.

A. ECONOMIC ISSUES

Tax considerations have undoubtedly contributed to the growth of the various types of deferred compensation arrangements now in force.[12] The following table indicates that within the period 1950 to 1962, the number of employees covered by private pension and profit-sharing plans rose from 9.8 to 23.1 million, while total contributions increased from $2.1 to $5.6 billion on an annual basis. The passage of the Self-Employed Individuals Tax Retirement Act is expected to add further to the volume of tax deferred saving. At the time of its passage contributions under the new law were expected to total $650 million in a full year, resulting in a revenue loss of $115 million.

[11] Secs. 401–405.

[12] For discussion of the tax and other motives behind the growth of employee pension plans see Dan M. McGill, "Fundamentals of Private Pensions," Pension research counsel, Wharton School of Finance, 1964, ch. 1.

TABLE 22.—*Private pension and deferred profit-sharing plans:* [1] *Estimated coverage, contributions, beneficiaries, benefit payments, and reserves, 1950–62*

Year	Coverage,[2] end of year (in thousands)			Employer contributions (in millions)			Employee contributions (in millions)			Number of beneficiaries, end of year (in thousands)			Amount of benefit payments (in millions)			Reserves, end of year (in billions)		
	Total	Insured	Noninsured	Total	Insured	Noninsured	Total	Insured	Noninsured	Total	Insured	Noninsured	Total [3]	Insured	Noninsured [3]	Total	Insured	Noninsured
1950	9,800	2,600	7,200	$1,750	$720	$1,030	$330	$200	$130	450	150	300	$370	$80	$290	$11.7	$5.6	$6.1
1951	11,000	2,900	8,100	2,260	820	1,440	380	210	170	540	170	370	450	100	350	14.2	6.6	7.6
1952	11,700	3,200	8,500	2,510	910	1,600	430	240	190	650	200	450	530	120	410	16.9	7.7	9.2
1953	13,200	3,400	9,800	2,930	1,010	1,920	480	260	220	750	230	520	610	140	470	19.9	8.8	11.1
1954	14,200	3,600	10,600	2,930	1,030	1,900	510	270	240	880	270	610	710	160	550	23.1	10.0	13.1
1955	15,400	3,800	11,600	3,190	1,100	2,090	550	280	270	990	300	690	840	180	660	26.7	11.3	15.3
1956	16,800	4,000	12,800	3,490	1,110	2,380	610	290	320	1,110	340	770	990	210	780	30.5	12.5	18.0
1957	18,100	4,400	13,700	3,890	1,220	2,670	680	300	380	1,250	380	870	1,130	240	890	34.9	14.1	20.8
1958	18,800	4,500	14,300	3,950	1,250	2,700	710	310	400	1,410	440	970	1,290	290	1,000	39.5	15.6	23.9
1959	19,900	4,800	15,100	4,410	1,330	3,080	750	330	420	1,590	500	1,090	1,510	340	1,170	44.9	17.6	27.3
1960	21,200	4,900	16,300	4,470	1,190	3,280	770	300	470	1,780	540	1,240	1,710	390	1,320	49.9	18.8	31.1
1961	22,200	5,100	17,100	4,540	1,180	3,360	770	290	480	1,900	560	1,340	1,920	440	1,480	55.3	20.2	35.1
1962	23,100	5,200	17,900	4,740	1,240	3,500	820	310	510	2,090	620	1,470	2,150	500	1,650	60.7	21.6	39.0

[1] Includes pay-as-you-go, multiemployer, and union-administered plans, those of nonprofit organizations, and railroad plans supplementing the Federal railroad retirement program. Insured plans are underwritten by insurance companies; noninsured plans are in general funded through trustees.

[2] Excludes annuitants.

[3] Includes refunds to employees and their survivors and lump sums paid under deferred profit-sharing plans.

Source: Compiled by the Division of the Actuary, Social Security Administration, from data furnished primarily by the Institute of Life Insurance and the Securities and Exchange Commission.

1. "Institutionalizing" personal savings and investment

Interest has focused on the possible effect of the growing number of pension and deferred compensation plans on the volume of personal savings. Such plans may have no significant impact on aggregate savings if the taxpayer is presumed to set a certain dollar savings target, which the tax law merely helps him to achieve. Such a presumption is likely to be accurate, it is contended, in the case of self-employed retirement plans and deferred compensation contracts negotiated directly between the individual employee and his employer. The presumption is less likely to be accurate, however, with respect to group retirement plans since the specific terms of these arrangements do not reflect the savings intentions of individual employees.

The statistical evidence which bears on the impact of employer contributions to retirement plans on the level of personal savings does not yield a definite conclusion. On one hand, employer contributions to private pension funds have increased steadily as a percent of wages and salaries paid by private employers. On the other hand, fluctuations in the ratio of personal savings to personal income do not appear to be correlated to changes in the volume of employer contributions to retirement plans.

It is contended that the growth of deferred compensation arrangements contributes to both economic growth and stability. In the first place, it adds to the supply of investible funds available to industry and thereby facilitates industrial expansion. It is pointed out that this conclusion is consistent with trends evident in the investment of employers' contributions by the recipient trust funds and insurance companies. A recent survey by the Securities and Exchange Commission shows that private funds accounted for slightly over half of the total book value of the assets of all public and private pension funds including the Federal Government's social security programs.[13] Private noninsured pension funds accounted for two-thirds of the assets of these private plans. The latter have grown most rapidly in asset size in recent years and are investing an increasing share of their capital in corporate securities. For example, between 1958 and 1963 the book value of corporate stock in the portfolios of private noninsured pension funds increased by 265 percent and from 27 percent to 39 percent of the total value of the assets of these funds. While corporate bonds fell from 50 percent to 42 percent of the book value of fund assets during this period, they continued to be the most important type of asset held by such funds. On the average, private noninsured pension funds invest primarily in stocks and bonds of companies other than the ones whose employees are covered by the particular plans. Within recent years private noninsured pension funds have purchased a larger volume of corporate securities than life insurance companies, State and local government trust funds, investment companies, and individuals and more corporate bonds than all groups except life insurance companies and State and local government trust funds.

In the second place, it is argued that personal savings through deferred compensation arrangements are likely to be quite sensitive to short-term changes in levels of economic activity and therefore to provide a stabilizing influence. Employer contributions to pension,

[13] SEC, statistical series, release No. 1978, June 4, 1964, "Private Noninsured Pension Funds, 1963."

profit-sharing, and stock-bonus plans depend on the size of payrolls or on current profits. When business activity is increasing, therefore, individual savings through retirement funds will rise, exerting a dampening influence on inflationary pressures. A downturn in business activity, by the same token, will result in a decrease in this type of savings, thereby exerting a countercyclical influence. Because these savings are institutionalized, i.e., are based on formal arrangements, they can more readily be counted on to move in a direction that will serve to counteract the business cycle.

Concern is sometimes expressed over the long-range influence of these formalized savings arrangements. The argument is frequently offered that the most important determinant of investment is the level of and rate of change in consumer demand. While much of the vigorous capital expansion program of the postwar years may have been due to the opportunities for exploiting technological advances, it is argued that sustaining full employment and growth in a future period may require a relatively more important role for consumption. Since personal savings through employer contributions to retirement funds are not geared to investment requirements, it is claimed that the rate of total private savings may advance too rapidly, seriously complicating the problem of sustaining economic growth.

Moreover, it is argued that although this form of institutionalized savings might show an appropriate countercyclical sensitivity if pension arrangements were stabilized, the fact that the number of such plans is on the increase results in a tendency toward a relative increase in savings, regardless of economic conditions.

Continued growth in private retirement plans has important implications for the disposition of personal savings. The investment needs of retirement funds have been regarded by some as offering a major solution to the problem of assuring an adequate supply of external funds for corporate growth. The active participation of these retirement plan trusts in the securities market, it is said, assures corporate enterprise of a ready market for its securities, and more particularly for its equity issues. Moreover, since these trusts have a relatively steady inflow of funds, they can be counted on to be active buyers, particularly at the time of market dips. Finally, trust fund investments in corporate securities, it is claimed, give an increasingly large number of individuals a stake in corporate enterprise at considerably lower risk than would attend direct investments by individuals.

On the other hand, the increased participation of pension funds in the securities market is sometimes regarded as a mixed blessing. It is contended that because of the nature of these funds, their acquisition of securities must be limited largely to the so-called blue chips. Since such securities are in greatest demand, substantial purchases by retirement funds, it is claimed, tend to restrict the supply of equity issues available to other investors and thus make the market more vulnerable to sharp fluctuations.

Moreover, it is contended that retirement fund participation has served to immobilize a large volume of high-grade corporate securities. In contrast with mutual investment funds, many other institutional investors, and individual investors, retirement funds are generally regarded as relatively inactive in portfolio adjustment. Accordingly, securities acquired by these funds tend to be immobilized in their holdings, thereby reducing the fluidity of investable funds in the aggregate.

The overall effect of retirement fund acquisitions and holdings, it is claimed, is to impose an undue upward pressure on high-grade securities relative to less seasoned issues. Such pressures in the securities market, it is said, necessarily have adverse implications for the allocation of investable funds among alternative opportunities.

2. Effect on labor-force mobility

A major criticism directed against deferred compensation arrangements is that they tend to reduce the mobility of covered employees and therefore contribute to a reduction in the effectiveness with which labor services are allocated among competing employers. This result it is claimed, holds both with respect to executive employees and hourly paid workers. Moreover, it is thought to characterize both group retirement plans and individually negotiated deferred compensation contracts.

In the case of the group plans, this result follows from the fact that in most cases the covered employee does not have full vested rights to the retirement benefits accruing on his behalf. To receive these benefits, he must meet the plan's requirements with respect to length of service and retirement age. Resigning a job for another employment, therefore, involves forfeiting all or a part of the retirement benefits previously built up on his behalf. Even if the new employment involves coverage in a retirement plan, the chances are that the new retirement benefits earned will not equal those which would have been claimed had the employee remained in the first job.

By the same token, retirement plans, it is claimed, tend to enhance the bias against employment of older workers. The nondiscrimination qualifications in the tax law generally require retirement plan coverage of workers without reference to the number of years remaining until retirement age. In the case of a new employee with relatively few years remaining before retirement, however, it may well appear to be too costly to hire him in view of the retirement benefits he will subsequently draw. In answer to this assertion, it is argued that the extra pension costs involved in hiring older people are frequently exaggerated.[14]

The forms of individually negotiated deferred compensation arrangements are very often drawn explicitly to hold the employee to the employer. In such cases, changing jobs may well encounter one of two barriers: (1) the cost to the prospective new employer of matching the retirement benefits of the present employer may be prohibitively high, or (2) the cost to the employee in terms of current salary foregone in past years in the present job may outweigh any feasible salary and retirement income provisions that might be made by the prospective employer. This will be particularly true when one of the basic purposes of the deferred compensation contract has been to avoid current tax liability.

Opposing considerations are offered to show benefits in labor force efficiency growing out of the use of private retirement plans. In the first place, it is pointed out that some retirement plans provide vesting of employee's rights to retirement benefits, at least after some minimum period of service. In such cases, once he has acquired vested rights, the restriction on the employee's changing jobs are relatively slight, since such a change will not involve forfeiture of retirement

[14] See, for example, U.S. Department of Labor, "Pension Costs in Relation to the Hiring of Older Workers," BES No. E-150, September 1956.

benefits already built up. It is pointed out, however, that this argument applies only to plans that provide full vesting relatively soon. If full vesting is acquired gradually the employee may be reluctant to change employers until he has attained fully vested rights.

Secondly, many deferred compensation arrangements, it is contended, are specifically designed to foster an interest by the employee in improving the effectiveness of the employing company's operations. This is particularly apparent in the case of profit-sharing and stock-bonus plans, stock-option arrangements, and in a number of specially designed deferred compensation contracts. Even the pension plan for hourly workers, however, is alleged to improve an employee's efficiency, by relieving him, to a considerable extent, of anxiety over financial provision for his retirement years and by imbuing him with a sense of loyalty to the employer company. Moreover, by making it easier financially for the employee to retire at the customarily accepted retirement age, the seniority barrier to upgrading of younger employees is mitigated. This serves as a significant incentive, both at the executive and hourly worker level. In addition, the relatively younger labor force resulting from prompt retirement is said to result in higher levels of labor productivity than would result if workers were not encouraged by retirement plans to retire at relatively early ages.

B. TAX ISSUES IN DEFERRED COMPENSATION PLANS

The present tax provisions applicable to retirement plans involve a number of general issues in tax policy as well as specific problems. The general issues concern the impact of these provisions on the size of the tax base and the distribution of tax burdens.

1. Tax burden distribution

The deferral of tax on an increasingly important component of personal savings, it is contended, has a number of important ramifications for tax burden distribution. In the first place, it involves a net loss of income-tax revenue, since in virtually all cases the employee or self-employed person is taxable at a higher marginal rate during his earning years than during his retirement years. Given the Government's revenue requirements, the tax law necessarily involves a shift in tax burden from the labor income of individuals covered by retirement plans financed in whole or in part by employers to other forms of income, including the labor income of noncovered employees.

Secondly, it involves a basic tax discrimination with respect to various forms of personal savings. Some opponents of the present tax provisions point out that there are no inherent features in saving through formal retirement or deferred compensation plans which warrant deferral of tax as compared with direct individual saving through, say, U.S. Government savings bonds, time deposits, or corporate securities.

Employer contributions to funds to provide retirement benefits for employees, it is contended, are clearly part of the employee's compensation for his labor services. In the absence of such employer contributions, it is maintained, employment contracts would have to provide for higher current wage and salary disbursements so that the employee might make his own provisions for his retirement. Under present law, all of the employee's wage or salary would be includible in his income for tax purposes. By contrast, however, that portion of the employee's compensation which the employer places directly into a retirement fund is not included in the employee's income for tax purposes on a current basis.[15] These amounts are included in the employee's income only when distributed to him as benefits.

Those holding these views feel that wage and salary supplements of this character should be included on a current basis in the covered employee's taxable income and the partial exclusion for the savings of self-employed persons should be revoked. Furthermore, it is argued that current taxability to the employee should be made a necessary condition for the current deductibility by the employer of any contributions he makes to provide deferred compensation benefits. It is recognized that this revision would require prompt vesting of pension rights for covered employees; indeed, such vesting, it is suggested, should be mandatory for qualification of the employer's plan, if for no other reason than to provide opportunity for greater mobility of labor services. These rules, it is contended, should be given the widest possible application to include, in addition to private retirement plans, social security contributions, individually negotiated deferred-compensation arrangements, and stock-option plans, to name only the principal deferred-compensation arrangements.

In the absence of such a reversal of present law, it is argued, there will be continuing pressure for labor and management to employ more and more devices for converting wage and salary payments into tax-deferred forms, involving a continuing shift in relative tax burdens to those so situated as to be unable to take advantage of any special tax provisions. As one author put it:

> Perhaps the time will come when the individual unfortunate enough to receive all of his wages in money will have an impossible tax burden.[16]

On the other hand, it is pointed out that a major stimulus for the growth of deferred compensation arrangements has been the heavy burden of individual income taxes. Straightforward wage and salary payments in amounts equal to employer contributions to retirement plans, it is pointed out, would provide less potential savings by employees for retirement. Accordingly, to match through wage and salary disbursements the accumulation of retirement benefits now possible under the present law would necessarily involve a greater level of total employee compensation than the sum of present wage and salary disbursements plus wage and salary supplements. Since such disbursements are deductible by the employer, the revenue gain from current taxability would be slight; indeed, net revenue losses might result.

Moreover, it is pointed out that requiring current taxability to the employee of employer contributions with respect to deferred compensation would involve a drastic disruption of present arrangements. Many group plans for retirement benefits, it is maintained, cannot afford to vest each covered employee with specific benefit rights, since the overall cost for plans with vesting may considerably exceed that of nonvested plans. Including employer contributions in the income of employees in nonvested or partially vested plans would involve a difficult task of allocation and would require the employee to

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[15] Assuming the employer's plan is a qualified plan or, if not qualified, that the employees' benefit rights are nonforfeitable.

[16] B. U. Ratchford, "Symposium on Practical Limitations of the Net Income Tax," Journal of Finance, May 1952, p. 211.

pay tax on an amount which may never actually be received by him. Accordingly, current taxability to the employee would be feasible only where his rights are vested. Adoption of such a rule might result in a significant contraction of the scope of employee retirement plans.

By the same token if deductions for contributions were denied employers except where equivalent amounts were included in the employee's currently taxable income, a substantial proportion of the total current employer deductions for contributions to retirement plans might be disallowed. In view of the present high rates of tax on corporate income, the nondeductibility of these contributions could result in wholesale abandonment of broad-coverage plans in favor of more narrow coverage under fully vested plans or a marked contraction of benefits under broad-coverage plans.

2. Specific tax issues

As observed above, one of the criticisms frequently directed against the present tax provisions applicable to retirement plans is that they discriminate in favor of savings for retirement by those covered under an employer's or self-employed person's plan and against similar savings by individuals not covered by such arrangements. Prior to 1962 this criticism was most frequently voiced by representatives of the self-employed who then did not have tax deferral privileges with regard to their retirement savings. It was pointed out that a professional person employed by a corporation could enjoy a substantial tax advantage and accordingly more easily provide for his retirement as compared to a self-employed professional person who earned the same income. The Self-Employed Individuals Tax Retirement Act was enacted for the primary purpose of granting the self-employed access to retirement plans on a basis reasonably similar to that accorded many corporate employees.

Some opponents of this approach argue that while it serves to equalize treatment between those covered and those not covered by employer plans, it does so by extending the deficiencies in the present law. A more desirable approach to the elimination of the present tax discrimination, it is contended, would be through basic revision of the present tax provisions. Thus, it is claimed that if employer contributions to all retirement plans, public and private, were currently taxable to the employee (and deductible by the employer only if so taxable), the current discrimination would be eliminated and the occasion for special provisions for the self-employed would disappear. Other critics maintain that present law discriminates in favor of the self-employed, since they can obtain tax benefits with respect to completely nonforfeitable rights, which covered employees do not generally enjoy. In rebuttal it is pointed out that compared to many employee plans, the present tax benefits of qualified self-employed retirement plans are severely restricted and further liberalizations are required as a matter of equity.

Other specific tax issues raised by the present tax provisions with respect to deferred compensation concern the appropriateness of capital gains treatment for lump-sum distributions from retirement plans, the use of individually negotiated deferred compensation arrangements as tax-avoidance devices, the extent to which employers should be permitted to adopt highly differentiated plans for different groups of employees, and the extent to which private plans should be required to parallel and be integrated with public retirement programs.

CHAPTER 8

TAXATION OF INCOME FROM FOREIGN SOURCES

The special provisions which treat income derived from foreign sources by U.S. taxpayers reflect a concern for achieving fair tax results when income is subject to tax in more than one country. In the absence of special reliefs, U.S. citizens and corporations would be fully taxed on foreign income by both the Federal Government and by the government of the foreign country in which the income is earned. The special provisions also reflect the shifting concerns of national economic policy. Throughout the postwar years interest has focused on the use of public policy to encourage private investment in less-developed countries. Within recent years, the balance of payments has become an important concern as well. Considerable discussion has, therefore, centered on the effects of various provisions in the Federal income-tax law on the volume of private investment abroad and the flow of investment funds into and out of the country. A major problem at this time concerns ways to preserve tax incentives for private investment in less-developed regions without encouraging an outflow of funds to developed nations which would seriously weaken the U.S. balance-of-payments position.

I. Present Law

The tax treatment of income derived from foreign sources by U.S. taxpayers is governed by the provisions of the Internal Revenue Code and by tax treaties or conventions between this country and a number of other nations. The provisions of the Revenue Code determine how foreign source income is taxed on the return a U.S. taxpayer files with the Internal Revenue Service. The law determines what income is taxed, when it is taxed, and what credits or deductions are given for foreign taxes paid. Tax treaties, on the other hand, generally govern the manner in which foreign governments tax U.S. residents and, to some extent, the manner in which the United States taxes foreign residents who derive income from this country.

A. PROVISIONS OF U.S. LAW REGARDING THE FOREIGN SOURCE INCOME OF U.S. TAXPAYERS

1. Income earned abroad

U.S. citizens who reside abroad may exclude from gross income on their U.S. tax returns compensation they receive for services performed abroad, unless in the employ of the U.S. Government, under the following conditions: [1]

(1) Bona fide residence abroad for an uninterrupted period which includes the entire tax year, or

(2) Physical presence abroad for at least 510 days (approximately 17 months) during a period of 18 consecutive months.

[1] Secs. 911-912.

The exclusion is limited to $20,000 unless the individual has been a bona fide foreign resident for an uninterrupted period of 3 years or more, in which case the limit is raised to $25,000 ($35,000 prior to January 1, 1965) with respect to income earned after the third year. In addition, amounts received as foreign-area allowances, cost-of-living allowances, and Peace Corps allowances by U.S. Government employees stationed overseas are excluded from gross income.

2. Other foreign income

(*a*) *When Tax is paid.*—Under most circumstances, the income of a foreign corporation which accrues to U.S. shareholders is not taxed by the United States until it is distributed or otherwise remitted to them. Other types of foreign income of U.S. taxpayers are taxed currently, except for the excludable portion of earned income. In some instances the latter course involves the inclusion in the gross income of U.S. shareholders of amounts equivalent to the undistributed income accumulated by foreign corporations controlled by such shareholders. For these purposes, a corporation is considered controlled if more than 50 percent of its voting stock is controlled by U.S. persons or companies, each of whom owns at least 10 percent of such voting stock.

Prior to the Revenue Act of 1962, the income of these controlled foreign corporations was taxed only when distributed. This resulted in a marked difference in the tax treatment accorded foreign branches as opposed to foreign subsidiaries of domestic firms. The income of foreign branches was taxed currently while the tax on the income of foreign subsidiaries was deferred until such income was actually repatriated to the shareholders. This situation, combined with concern over the balance of payments and the effects on tax equity of the use of foreign "tax havens," led to the adoption in 1962 of rules for the attribution of the undistributed income of these foreign corporations.

The income which is attributed to the U.S. shareholders of controlled foreign corporations consists of income from the insurance and reinsurance of U.S. risks and "foreign base company income." [2] The latter includes income derived by such corporations from certain types of passive investments; i.e., dividends, interest, and certain types of rents and royalties. It also includes income derived from selling goods purchased from, or performing services for, related persons, when such goods are sold to, or such services are performed for, persons outside the country in which the foreign corporation is incorporated. The latter provision is intended to forestall tax avoidance which might otherwise occur if, for example, a U.S. company doing business in country A channeled the income earned in A to a subsidiary organized in country B merely to take advantage of low tax rates in country B.

An exception to the attribution rules is made for qualified investment in countries designated by the President as less developed. The President may designate any country except the countries of Western Europe, certain British Commonwealth nations, and Japan as less developed. Furthermore, the attribution rules do not apply to certain income derived from the sale of U.S. exports. Finally, income otherwise attributable to U.S. shareholders is exempt if currency restrictions are such as to prevent actual repatriation.

[2] Secs. 951-964 and 970-974.

Moreover, the entire income of a controlled foreign corporation is considered to have been distributed if a certain minimum percentage of net profits, which varies inversely with the effective foreign tax rate, is distributed. The minimum percentage varies from 90 when the effective foreign tax rate is less than 10 percent, to 0 when the effective foreign tax rate in 1965 and later years exceeds 43 percent. The percentages are designed to eliminate the requirement for attribution when the sum of the U.S. tax paid on distributed earnings and the foreign tax paid on total net profits equals or exceeds 90 percent of the tax (determined without regard to the surtax exemptions) that would have been paid by a domestic U.S. corporation had it earned the income.

Distributions to Americans of income accumulated in foreign trusts are taxed as ordinary income when distributed, but may be spread over a 5-year period to permit averaging.[3] U.S. investors must treat as ordinary income any gains realized from the sale of shares in foreign mutual funds to the extent that the company accumulates earnings after 1962, unless the foreign fund qualifies as a regulated investment trust under U.S. law.[4]

(*b*) *Denial of capital gains tax treatment.*—Prior to the Revenue Act of 1962, the accumulated income of foreign corporations could often be converted from ordinary income to capital gains at the time of repatriation through the sale of the stock of the corporation producing the foreign income. As a result of the 1962 act, however, gains realized by a shareholder owning 10 percent or more of a foreign corporation, regardless of the transactions prior to their repatriation, are viewed as dividends.[5] The act also provides that the full sales price of a patent, copyright, secret formula, or similar item sold by a parent corporation to a controlled subsidiary be taxed as ordinary income.[6]

(*c*) *Foreign tax credits or deductions.*—In determining U.S. tax liability, American taxpayers may either (1) deduct from their gross income the amount of foreign taxes paid, or (2) credit against their U.S. tax liability income taxes paid to a foreign country.[7] The allowable foreign tax credit is limited.

Prior to 1961, the credit for taxes paid to any one country could not exceed a percentage of the precredit U.S. tax equal to the proportion which the income derived from the foreign country bore to the total income of the company. Thus, if a company had a total income of $200,000 of which one-fourth came from country A and one-half from country B, the amount of the tax credit for country A could not exceed one-fourth of the precredit U.S. tax and the tax credit with respect to country B could not exceed one-half of the U.S. tax before credits.

For 1961 and subsequent years, an alternative overall limit on the foreign tax credit is made available. This limit is the percentage of the total U.S. tax equal to the proportion which the income from all foreign countries bears to the total income of the taxpayer. Thus, in the example above, the overall limit on the foreign tax credit would be three-fourths of the total tax before credits.

The law provides a proportional credit to an American corporation for the income taxes paid by a foreign corporation if the American

[3] Secs. 665–669.
[4] Secs. 1246–1247.
[5] Sec. 1248.
[6] Sec. 1249.
[7] Secs. 901–905.

corporation owns 10 percent or more of the foreign company's voting stock.[8] A credit may also be obtained for taxes paid by a foreign subsidiary of such a foreign corporation if the latter holds at least 50 percent of the voting stock of the former.

Foreign taxes denied as credits under the limitations indicated above may be carried back to the 2 preceding taxable years and forward to the 5 succeeding taxable years.

When a domestic corporation receives dividends from a foreign subsidiary (but not a corporation located in a less-developed country) and elects to take the foreign tax credit, it must "gross up" its tax base by including not only the dividends received but also the income tax paid by the foreign corporation on the earnings from which the dividends were paid.[9] For example, a domestic corporation which receives $100 of dividends from a subsidiary in a developed country where the tax rate on net income is 20 percent includes $125 in its gross income and claims a tax credit for foreign taxes paid of $25. Prior to the Revenue Act of 1962 this "gross up" for foreign income tax was not required.

A dividend paid by a foreign corporation in property rather than money is taxable at its fair market value at the time of the transfer.[10] Prior to the 1962 act, the property was taxable at the lesser of (1) the fair market value of the property, or (2) the adjusted basis of the property in the hands of the distributing corporation immediately prior to the time of distribution.

The foreign tax credit is also available to shareholders in certain regulated investment companies, provided more than 50 percent of company assets are invested in foreign securities.[11]

Foreign taxes paid have always been recognized as a legitimate deduction in computing taxable income, but it was not until 1918 that the alternative of a credit was allowed. The credit was at first allowed dollar for dollar, but the 1921 Revenue Act provided that the total credit might not exceed that proportion of the U.S. tax which the income from without the United States bore to total income. In 1932, Congress enacted a per-country limitation in addition to this overall limitation.

The 1918 act also permitted a domestic corporation to claim a proportional credit for taxes paid by a foreign subsidiary if the domestic company held a majority of the stock of the subsidiary. This holding requirement was reduced to 10 percent in 1951. Provision for a credit for the taxes paid by a foreign subsidiary of a foreign subsidiary was added in 1942. As first enacted, 100-percent ownership of the stock of the second subsidiary was required; this was reduced to 50-percent ownership in 1951.

Under the double limitation imposed in 1932, the aggregate of the credits determined by the per-country limitation could not exceed the credit determined under the overall limitation. The overall limitation was eliminated in the Internal Revenue Code of 1954. In 1958, the carryback and carryforward provisions with respect to excess foreign taxes were enacted. In 1960, the overall limitation was restored, but as an alternative to the per-country limitation to be used at the taxpayer's election.

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[8] Sec. 902(a).
[9] Sec. 78.
[10] Sec. 301.
[11] Sec. 853.

3. Western Hemisphere trade corporations [12]

A special rate reduction of 14 percentage points is, in effect, granted to so-called Western Hemisphere trade corporations. Such corporations are defined by the law as U.S. corporations all of whose business, other than incidental purchases, is done in North, South, or Central America, or the West Indies. To qualify they must satisfy the following requirements for a period of 3 years immediately preceding the close of the taxable year:

(1) Ninety-five percent of their gross income must be derived from sources outside the United States; and

(2) Ninety percent of their gross income must be derived from the active conduct of a trade or business.

If a Western Hemisphere trade corporation is a subsidiary of another American corporation, dividends received by the latter are subject to the regular tax provisions regarding dividends received, including the 85-percent intercorporate dividends-received deduction. A Western Hemisphere trade corporation may credit its foreign taxes against its U.S. tax.

This special treatment for Western Hemisphere trade corporations was first granted in 1942 to alleviate an alleged competitive disadvantage suffered by American firms then doing business in the other Americas. It was pointed out that the disadvantage became especially great by reason of the new wartime tax rates imposed by the United States, since other countries often completely exempted the foreign income of their corporations.

In 1961, 682 Western Hemisphere trade corporation tax returns were filed, including returns filed by affiliated groups where at least one member was a Western Hemisphere trade corporation, listing $1.95 billion of net income. While the majority of these firms were engaged in wholesale or retail trade, the largest proportion of their combined net income was earned in manufacturing, specifically in petroleum refining and related industries.

4. Income from U.S. possessions [13]

A U.S. citizen or domestic corporation may exclude from gross income any income, including salary (other than that from the U.S. Government), derived from sources outside the United States, if within a period of 3 years immediately preceding the close of the taxable year:

(1) Eighty percent of gross income for such a period was derived from sources within a possession of the United States; and

(2) Fifty percent of gross income for such a period was derived from the active conduct of a trade or business within a possession.

For the purposes of the foregoing, "possession" does not include the Virgin Islands, and when used with respect to citizens of the United States, does not include Puerto Rico.

A U.S. citizen who is a bona fide resident of Puerto Rico for a full taxable year may exclude income derived from sources within Puerto Rico, other than salary received from the U.S. Government.

[12] Secs. 921–922.
[13] Secs. 931–933.

B. TAX TREATIES

The United States now has income tax conventions with 21 countries which help to eliminate double taxation for individuals and corporations deriving income from foreign sources. The treaties do not alter the U.S. tax liability of U.S. residents. Rather, in return for concessions and adjustments granted by the United States with regard to the U.S. income of corporations and residents of the treaty nations, these countries grant similar concessions to U.S. residents and corporations. The result, in general, establishes aggregate tax liabilities for taxpayers with income from foreign sources equal to those they would incur if their income were entirely from domestic sources.

With regard to U.S. concessions, these tax treaties typically provide that a foreign enterprise shall not be subject to tax in the United States unless it is engaged in business here through a permanent establishment. In the case of income from investments, the treaties usually reduce the tax withheld at source. As respects dividends, the reduction is generally from 30 to 15 percent and, in some cases, to 5 percent. Finally, the tax treaties often provide that aliens may be in the United States for periods up to 6 months in connection with their business activities without becoming liable for U.S. tax on their earnings. These concessions are usually made on a reciprocal basis.

Most of the conventions in effect are with Western European countries, although seven are with non-European countries. Three treaties which were negotiated but withdrawn prior to Senate consideration would have gone beyond the scope of the other conventions by providing a credit to U.S. taxpayers for taxes "spared" by the treaty nation under tax incentive laws designed to promote investment. In addition to the income tax treaties, there are 13 estate and gift tax conventions in effect between the United States and other countries. One other is pending.

II. Issues and Proposals

Changes in international conditions since the end of World War II have altered the emphasis on the issues involved in the Federal tax treatment of income derived abroad. In the early postwar years, U.S. policy was focused primarily on assisting the rebuilding of the war-damaged economies of Europe and Asia and on providing technical assistance in underdeveloped countries around the world.

In the early and mid-1950's, the rapid economic progress of much of Western Europe and the intensification of the cold war began to shift emphasis in American foreign aid from economic reconstruction to military buildup. At the same time, the promotion of economic development in the underdeveloped areas of the world assumed increasing importance in U.S. foreign policy. Under these circumstances, a high rate of private foreign investment from the United States was recognized as a major adjunct to governmental efforts to strengthen the economy of the free world. Considerable interest, therefore, was directed to the use of tax devices to encourage private U.S. investment abroad.

Although the United States began to suffer persistent balance-of-payments deficits in 1950, the need to limit international payments, including private investments abroad, was not apparent in the early years of the decade. At that time, other countries were anxious to rebuild their international reserves and welcomed the opportunity to add to their dollar holdings. Indeed, the free world was concerned until the late 1950's with the possibility of a chronic dollar shortage. As a result, the United States was able to finance its balance-of-payments deficits largely through increases in the dollar holdings of other countries rather than a depletion of its gold reserves.

However, toward the end of the 1950's when many foreign countries' international reserves were again adequate and the leading currencies were restored to convertibility, the United States was increasingly obliged to finance its balance-of-payments deficits through sales of gold rather than increased dollar holdings by foreign governments. A sharply increased rate of gold outflow beginning in 1958 focused public attention on the U.S. balance of payments and made elimination of the payments deficit a matter of high priority. These circumstances significantly altered the perspective on Federal tax policy as related to investments abroad and the income from foreign operations.

The value of private U.S. investments abroad has grown substantially since the end of World War II. The book value of direct, long-term, private investments abroad increased from $8.4 billion at the end of 1945 to $37.1 billion at the end of 1962, or at an average annual rate of 9.1 percent.[14] This vigorous rate of overseas investment by private interests suggests that the U.S. tax provisions applicable to foreign income have not seriously inhibited such investment in an overall sense. The distribution of this investment, however, is concentrated in Canada and Western Europe, where 56 percent of the value of direct, long-term, private investment was located at the end of 1962, and in the oil producing countries of the Near East and South America. In the latter connection, 46 percent of U.S. private, direct, long-term investment in areas outside Canada and Western Europe was devoted to petroleum operations at the end of 1962. Private U.S. investment of a general nature in less developed countries, therefore, has not expanded vigorously in recent years, although governmental aid has increasingly been directed to these areas.

At this time a major policy problem concerns how tax treatment conducive to expanding private investment in less developed countries can be provided while avoiding any incentive to invest larger amounts in advanced industrial countries than would be forthcoming under a neutral tax system. Specific tax issues related to this problem concern tax deferral on the earnings of foreign subsidiaries operating in advanced industrial countries and the need for further tax provisions to stimulate investment in less developed countries. A number of specific proposals have been advanced in connection with these issues and others.

A. TAX DEFERRAL FOR INCOME EARNED ABROAD

Prior to 1962, the U.S. tax treatment of income earned abroad was marked not only by the allowance of a full credit against domestic tax liability for foreign taxes paid, but also by deferral of tax on the income of foreign subsidiaries until such time as it was actually remitted to U.S. shareholders. In the April 1961 Presidential message

[14] Department of Commerce, Survey of Current Business, August 1963, p. 18.

on the tax system, a significant revision in the deferral principle was recommended.[15]

It was proposed that U.S. corporations be required to increase their incomes for domestic tax purposes by the amount of the undistributed earnings of foreign subsidiaries and that individuals be required to make a similar attribution with regard to the undistributed earnings of closely held foreign companies and investment trusts. Subsidiaries and closely held corporations operating in designated less developed countries, other than certain types of so-called tax haven companies, were, however, to be excluded from this rule and free to operate as under former law. The proposal, which was reflected to an extent in the provisions of the Revenue Act of 1962, stimulated extensive debate.

Proponents argued that the then existing deferral privilege created a tax differential in favor of overseas as opposed to domestic investments on the part of the U.S. concerns. Whereas this differential may serve to offset some of the other barriers to investment in less developed countries, it creates an artificial tax incentive to investment in developed nations with lower corporate tax rates than that of the United States. The deferral privilege, it was contended, permits some foreign subsidiaries of U.S. firms to use what is the equivalent of a loan from the Treasury to finance their expansion. Firms operating entirely in the United States do not have this advantage. Furthermore, the proposal was said to eliminate the disparity between the tax treatment of the income of foreign branches as opposed to foreign subsidiaries.

A principal argument for the proposal centered on the balance of payments. It was acknowledged that a choice was faced whether to require that foreign and domestic income be taxed at the same rate or to allow foreign income to be taxed at foreign rates, removing any possibility that tax rate differentials would affect the competitive position of U.S. firms operating abroad in countries with lower effective tax rates. The decision, it was said, was greatly influenced by balance-of-payments considerations. Tax deferral, particularly if employed specifically to avoid U.S. tax, was said to encourage the out-flow of domestic capital and to deter the repatriation of the earnings on foreign investments. While new foreign investments eventually increase the return flow of dividends and interest, it was felt that a relatively long period would elapse before the earnings repatriated exceeded the original capital outlays. During this interim period a severe strain would be placed on the balance of payments. It was estimated that enactment of the proposal would initially improve the U.S. balance-of-payments position by nearly $400 million a year.

The situation was aggravated, it was contended, by the existence of foreign "tax havens"; that is, companies established abroad for the purpose of channeling and accumulating income in countries where tax rates are significantly below domestic levels. Such companies were said to be proliferating at the time the proposal was made. Moreover, it was contended that the income of such concerns was being augmented by artificial arrangements designed to direct a disproportionate share of the profits of trading, licensing, and servicing to such companies from affiliates operating in the United States and

[15] H. Doc. 140, 87th Cong., 1st sess.

other high tax rate countries. This effect was said to intensify equity and balance-of-payments problems.

It was argued that the proposal would not be unfair to investors who had already participated in foreign ventures nor would it have an adverse effect on the competitive position of U.S. firms operating abroad. It was pointed out that the deferral principle had been continued after World War II to encourage private investment overseas in the reconstruction period. It was argued that to retain this treatment would merely protect private gain. It was also argued that any increase in costs resulting from the proposal would be more than offset by the advantages of American technical knowledge and business know-how. Finally, it was contended that by restricting deferral to the less developed countries, a greater incentive would be provided for investment in these countries.

Opponents of the proposal argued that it marked a radical departure from traditional, proven practice. There was said to be no justification for extending U.S. tax jurisdiction to income earned abroad by companies organized under foreign laws merely because they were owned in whole or in part by U.S. shareholders. It was pointed out that the interests of a company and its shareholders are typically far removed. The motives that influence a foreign corporation to reinvest its earnings are likely to be based on economic factors connected with the markets in which it operates rather than the tax concerns of it of its individual shareholders. Moreover, it is contended that it is unfair to tax shareholders on dividends that have not been received, particularly when earnings are in foreign currencies which must be converted to dollars before a real distribution can take place. In this view, enactment of the proposal would require shareholders to advance interest-free loans to the Government.

Furthermore, it was contended that the provisions would seriously weaken the competitive position of subsidiaries of U.S. firms operating abroad relative to the position of their foreign competitors.

On equity grounds it is maintained that the income tax should bear less heavily on income derived abroad than on domestic income. Economic activity abroad, it is alleged, is carried on without many of the benefits accorded to domestic business operation. Similarly, such activity involves less demand on Federal Government resources. Tax contributions, it is argued, should at least roughly reflect this differential.

Doubt was expressed that the balance of payments would be improved significantly by the proposal. On the one hand, it was pointed out that much of the demand for foreign exchange stems from Government programs of foreign aid and military assistance. Any curtailment in the rate of private overseas investment might be offset by the necessity of making larger outlays for foreign aid. On the other hand, it was contended that overseas investments quickly result in a return flow of repatriated earnings. In this regard, a temporary improvement in the balance of payments under the proposal would be brought about only by sacrificing a degree of long-run strength. Oversea investments deterred by the proposal would represent opportunities forever lost rather than merely postponed. Finally, it was pointed out that the philosopy behind the Trade Expansion Act of 1962 ran counter to the spirit of the proposal.

With regard to the so-called tax havens, it was argued that while legislation to cover certain special cases in which the avoidance of U.S. tax was clearly an issue might be desirable and feasible, the Presidential proposal tended to assume that every decision not to distribute foreign earnings was motivated by a desire to avoid taxes. The proposal, it was contended, threatened to affect too many taxpayers not engaged in avoiding United States and foreign taxes to be acceptable. Moreover, to the extent foreign nations were led to retaliate against this attempt by the United States to impose its fiscal sovereignty over income earned within their boundaires, the proposal would result in very little revenue gain to the Treasury.

B. PROPOSALS FOR PREFERENTIAL TAX TREATMENT FOR INVESTMENT IN LESS DEVELOPED COUNTRIES

Concern over the balance of payments has not precluded interest in devising special tax provisions to stimulate investment in less developed countries. On the one hand, existing tax provisions are sometimes cited as a barrier to private foreign investment in such countries. American firms, it is pointed out, must compete with firms taxed at lower rates and U.S. law prevents such countries from using tax rebates as a device to attract U.S. investors. On the other hand, preferential tax treatment is urged as a method for overcoming nontax barriers to investment in less developed areas. These barriers include: (1) the comparatively greater expected profitability of domestic as opposed to foreign investment, after allowing for commercial risk differentials; (2) the great noncommercial risks of investing in less developed regions where social unrest and political instability pose the threat of such occurrences as war, expropriation, the discriminatory application of laws, and resort to exchange controls; and (3) a lack of information on the nature and extent of opportunities for profitable investment in unfamiliar lands. It is argued that U.S. tax provisions should be designed to offset these factors and thus help to direct a larger flow of private investment to less developed countries.

1. Support for preferential treatment of foreign income

The major argument offered in support of virtually all of the proposals for preferential tax treatment of income derived abroad is that the objective of stimulating foreign investment is so important in the present state of international affairs as to outweigh opposing considerations. The success of American policy in fortifying the less developed countries of the free world against the inroads of communism is held to depend, in large part, on strengthening their national economies. This requires a substantial increase in capital formation in those areas, to which the United States must devote some of its resources. These resources will be more effectively utilized, it is maintained, if directed abroad under private auspices—i.e., subject to private managerial decisions—than under those of the Federal Government. According to this view, therefore, tax concessions to stimulate private foreign investment will result in the best possible allocation of investable resources, so long as public policy is committed to foreign economic assistance.

Moreover, it is argued that the market mechanism in many instances does not adequately measure the value of private investment by U.S. firms in underdeveloped countries. Such investment serves American foreign policy objectives as well as the private interests of the companies involved. The fact that net pretax returns on such investment, measured in pecuniary terms, may be lower than on comparable capital outlays at home, accordingly, does not preclude the possibility that the total return, including the economic strengthening of less developed nations against Communist influence, on foreign investment may be substantially greater—at least in the long run.

Proponents also claim that the alleged revenue loss and redistribution of tax burdens are significantly overstated. If tax concessions are successful in providing the desired flow of private investment funds, the Federal Government will be relieved of a substantial portion of its foreign economic assistance obligations, permitting a general reduction in tax revenues which may be provided so as to adjust tax burdens in whatever way is generally regarded as desirable.

Furthermore, it is pointed out that the real cost of expanding foreign investment is not properly measured in tax dollars but in terms of the resources committed for use outside the United States. Measured in these terms, the cost of assisting in foreign economic development will be minimized if the vehicle of private foreign investment is employed since real resources will be more efficiently employed by private business concerns than by Government agencies.

2. Opposition to preferential tax treatment

(*a*) *Equity arguments.*—The principal equity argument offered against special tax treatment for income derived abroad is that the source of any income is not relevant in determining the taxpayer's capacity to meet his obligations to the Federal Government. It is argued that equal amounts of net income should bear equal Federal income tax burdens, regardless of where the income arises. According to this view, special inducements may very well be necessary to overcome the hazards peculiar to foreign investment, but these provisions should not take the form of preferential tax treatment.

Moreover, it is maintained that it would be virtually impossible under most of the tax proposals offered to prevent preferential treatment from being accorded to income from existing investments, or to income from investments in areas in which no significant advantage would accrue to the United States from the standpoint of foreign policy.

In addition, it is contended that preferential tax treatment for the income from foreign investments of U.S. companies in fact represents a hidden subsidy which should be made explicit by the Federal Government directly assuming responsibility for the foreign investment. Although the real cost, measured in terms of the resources committed to the investment, will be the same in either case, the use of tax provisions involves not only a real income transfer from the United States to the foreign country, but also one within the United States from taxpayers in general to the favored investors.

Finally, it is argued that tax concessions for income derived abroad would principally benefit large companies and high-income individuals. Small companies, it is pointed out, very rarely undertake foreign capital commitments since they do not have adequate resources to permit the diversification of activity such commitments involve. Accordingly, it is argued that extending tax benefits to foreign investment would simply enhance the position of large companies in the Nation's business structure at the expense of the smaller companies.

(b) *Economic arguments.*—The principal economic argument offered against the preferential tax treatment of foreign income is that public policy should not seek to alter the allocation of investable resources resulting from the action of basic market factors. Thus, it is maintained that in the absence of a differential tax burden on foreign income the extent to which available resources are committed to foreign ventures will depend on the comparative net returns from foreign and domestic investments. Preferential tax treatment of foreign income, by enhancing the net returns from foreign investment, will undoubtedly serve to shift resources abroad, but at the expense of less efficient resource use overall. Accordingly, it is maintained, revision of the tax treatment of income derived abroad should be limited to providing neutrality as between the income from domestic and foreign investment. The fact that foreign competitors may be subject to lower tax liabilities, it is contended, does not alter the case since optimum allocation of the resources available to U.S. companies depends on equalizing net pretax returns on domestic and foreign investment.

Proponents of this view hold that the only significant way in which the present tax law might be biased against income derived abroad is in providing inadequate allowances for the special risks which may be involved. The principal feature of the law in this connection is the net operating loss deduction and carryover, which at present provides a 9-year period for offsetting business losses against income. This is held to be an adequate offset provision for any but the most extraordinary risks which could be reasonably assumed. Special treatment of gains and losses realized as a result of involuntary conversions are also thought to provide additional risk insurance.

Moreover, it is pointed out that allowing a dollar-for-dollar credit of foreign taxes against the U.S. tax on income derived abroad itself affords more favorable treatment to such income than to earnings on comparable domestic investments. Domestic income is generally liable to State and local government income taxes. Although these may be deducted in computing income subject to Federal income tax, they cannot be credited against Federal liabilities.

Even more important, it is maintained, is the opportunity to defer payment of the Federal income tax on the foreign source income of a foreign subsidiary in a less developed country. This deferral increases aftertax foreign earnings relative to domestic aftertax earnings to the extent that the foreign tax is lower than the U.S. tax. The deferral privilege, accordingly, represents a substantial tax preference for income derived abroad.

C. PROPOSALS FOR REVISING THE TAX TREATMENT OF INCOME EARNED ABROAD

1. Deferral of tax on the income of foreign branches

A major complaint against present law concerns the differential tax treatment of earnings from foreign branches of domestic firms as opposed to foreign subsidiaries. The foreign income of branches, and, for that matter, of domestic subsidiaries, is taxed currently while the tax on the income of foreign subsidiaries may be often deferred until the income is distributed to shareholders.

One proposal for correcting this difficulty is that taxpayers be given the right to elect that income of a foreign branch not be taxed until it is returned to the United States.[16] This in effect would make branches taxable in substantially the same way as foreign subsidiaries. It would permit reinvestment abroad of branch profits without U.S. tax liability.

It is also sometimes proposed that, if requested, a corporation investing in a foreign subsidiary be allowed to have the same treatment as is presently accorded a foreign branch.[17] The advantage of this choice would be to gain certain loss and depletion privileges now available only to foreign branches.

The Internal Revenue Code revision as it passed the House of Representatives in 1954 granted domestic corporations an election to defer taxes on the profits of their foreign branches in a manner similar to that in which taxes are deferred on the profits of foreign subsidiaries. Transactions between the home office and the foreign branch, if such an election were made, would have to be treated as transactions between two separate entities. Numerous objections were raised in the Senate hearings on the proposed change because of its restricted application. The Senate Finance Committee finally rejected the provision. There was a considerable lack of enthusiasm on the part of representatives of business for the proposal made by the Ways and Means Committee.[18]

2. Tax sparing

The efforts of a number of nations, principally those seeking rapid industrial development, to attract capital from the United States and other economically advanced countries sometimes take the form of special, low taxes on the income from specified types of new investment within their jurisdictions. It is pointed out that this favorable tax climate is of no consequence to the U.S. investor, since his combined foreign and U.S. tax on such income is the same as if all of the income originated within the United States. To give effect to the differentially lower foreign tax in such cases, it has been proposed that the U.S. foreign tax credit be based on the generally prevailing tax rate in the foreign jurisdiction, rather than on the income tax actually paid. For example, if the foreign country has a general corporation income tax of 48 percent, the same as the U.S. rate in 1965, but taxes income from certain types of investment at a 32-percent rate, the U.S. firm subject to this preferential rate would nevertheless be able to claim as a credit against its U.S. tax liability a foreign tax computed at the 48-percent rate.

Provisions permitting tax sparing were incorporated in tax treaties negotiated with India, the United Arab Republic, and Israel. These treaties were withdrawn by the President, prior to their consideration by the Senate, on June 18, 1964.

Those opposed to this provision contend that it would require the United States to underwrite the discriminatory investment programs of the foreign taxing jurisdictions, without giving the United States

[16] Message of President Eisenhower on foreign economic policy, Congressional Record, Jan. 10, 1955, p. 161. Commission on Foreign Economic Policy, "Report to the President and the Congress," January 1954, pp. 21–22. Committee for Economic Development, "Federal Tax Issues in 1955," p. 10. Chamber of Commerce of the United States (Foreign Commerce Department), "United States Tax Incentives for Private Foreign Investment," January 1954, pp. 56, 60.

[17] Commission on Foreign Economic Policy, op. cit., pp. 21–22.

[18] See, for example, the Chamber of Commerce of the United States (Foreign Commerce Department), op. cit., January 1954, p. 59.

the right to determine whether this use of Federal revenues is in the best interests of the United States. To the extent that Federal revenues are involved, it is argued, the choice of investment program should be made through the customary negotiations, using the Federal agencies specifically created to convey U.S. financial assistance to less developed countries for their economic development. Moreover, it is pointed out that to allow a taxpayer a credit for a tax liability he has not incurred would violate the most elementary precept of equity in taxation.

3. Western Hemisphere trade corporations

The 14-percentage-point rate reduction which, in effect, is afforded corporations which qualify as Western Hemisphere trade corporations has been the focus of various proposals. On the one hand, it has been proposed that the provision be generalized to apply to business income derived from any foreign source. This proposal was given favorable consideration by the House Ways and Means Committee at the time it deliberated the Internal Revenue Code of 1954,[19] but was omitted by the Senate Finance Committee after numerous objections were raised by business spokesmen regarding the phraseology and limitations of the provision drafted by the House.[20]

On the other hand, elimination of the special rate reduction has been urged on the grounds that the tax treatment of such companies should not be differentiated from that of any other U.S. concern doing business abroad. The argument upon which the 14-point reduction was originally based; i.e., the competitive disadvantage American firms would be at because of the high U.S. corporation income tax rate required in the war effort, it is maintained, is no more applicable to companies operating in the Western Hemisphere than those operating elsewhere in the world. Proponents of the present treatment contend that the tax differential is necessary to compensate for the special risks attendant upon investment in South America, where persistent political instability creates the special hazard of expropriation of foreign investment. Opponents of the present treatment contend that some of this political unrest is engendered by the exploitive investment policies of the U.S. companies, made possible in part by the preferential U.S. tax treatment.

4. The foreign business corporation approach

An entirely new approach to the taxation of foreign income has been proposed as essential to the effective stimulation of foreign investment.[21] Under this new approach a special class of American corporations would be established for tax purposes. These foreign business corporations would be designed to be the vehicle for all foreign operations and would be permitted to engage in export and to operate abroad directly or through foreign subsidiaries. U.S. taxes would be imposed on the income of a foreign business corporation in the same manner as on any other domestic corporation. The payment of the tax due on the income, however, would be deferred until that income was distributed directly or indirectly to its shareholders or used in the United States other than for foreign operations.

[19] H. Rept. 1337, pp. 74-76, A254-A258.
[20] S. Rept. 1622, p. 105.
[21] H.R. 5, 86th Cong., 1st sess.

The particular merit ascribed to this proposal is that it would limit preferential tax treatment to companies committing capital abroad only to the extent that they reinvested the earnings from their foreign investments outside the United States. Full U.S. tax liability would accrue when these were withdrawn from abroad. Accordingly, so long as the income were used abroad, it would be subject only to whatever tax treatment, favorable or otherwise, was afforded in the foreign jurisdiction.

5. A tax credit for investment in less developed countries

One proposal for encouraging investment in less developed countries is a credit against U.S. tax liability for a specified percentage of investment, including both new investment and the reinvestment of foreign earnings, in designated less developed countries.[22] This credit would offset U.S. tax liability in much the same manner as the 7-percent investment credit operates to reduce the liability of domestic investors.

Proponents of this approach argue that it would encourage the investment of larger amounts of U.S. capital, accompanied by the skills and leadership of U.S. investors, in the development of less developed nations. A credit against U.S. tax would offset the fact that many investments in less developed countries require a long period of time before they begin to yield monetary profits in line with their immediate broad social and economic importance. Also, it is argued, it would induce investors to leave large amounts of earnings in these countries, not only increasing the amount of capital investment, but also relieving a drain on the scarce foreign currency reserves of these countries. Suitable statutory safeguards could prevent abuses, require that U.S. capital goods be purchased to implement investment objectives, and restrict the credit to strategic investments such as those made in manufacturing or construction.

Opponents counter that such a credit would induce little investment in less developed countries in addition to that which would otherwise be undertaken. The proposal would therefore be a windfall to investors in established projects. The revenue loss to the Treasury, it is argued, would be more effective if used to provide investment guarantees, finance the dissemination of information on foreign investments, and support programs to strengthen the internal political, administrative, and economic institutions of the countries involved. The need for the latter, it is said, is often a most formidable barrier to investment by U.S. concerns in less developed countries.

An argument raised against the proposal and, indeed, against all proposals for changing the tax provisions regarding income earned abroad at this time, concerns the need for ample time in which to assess the impact of the Revenue Act of 1962. It is pointed out that the revision enacted in 1962 was the first major change in the taxation of income earned abroad since the passage of the Western Hemisphere trade corporation provisions in 1942. Many administrative difficulties have yet to be fully accommodated. For these reasons, some observers feel no further changes should be made until current law has been thoroughly evaluated on the basis of experience.

[22] See, for example, the administration's proposal for a 30-percent credit for money or property contributed or reinvested in the capital of certain enterprises operating in less developed countries, in the Presidential message on foreign assistance, H. Doc. 250, 88th Cong., 2d sess., Mar. 19, 1964.

CHAPTER 9

FEDERAL EXCISE TAXATION

I. Present Law [1]

Federal excises are imposed on a relatively large number of selected products, services, and occupations. Most of the excises on commodities are imposed at the manufacturer level but a few are levied at the retail level.

The table below outlines the major elements of the Federal system of excises:

TABLE 23.—*Major elements of the Federal excise system*

Item	Present law rates
Alcoholic beverages:	
Distilled spirits	$10.50 per proof gallon.
Still wines	17 cents, 67 cents, $2.25 per wine gallon.
Sparkling wines, liqueurs, and cordials	$1.92, $2.40, $3.40 per wine gallon.
Beer	$9 per barrel.
Tobacco:	
Cigarettes	$4 per 1,000.
Cigars	$2.50 to $20 per 1,000.
Tobacco, chewing and smoking; and snuff	10 cents per pound.
Stamp taxes, documentary, etc.:	
Bond issues	11 cents per $100 face value or fraction.
Bond transfers	5 cents per $100 face value or fraction.
Stock issues	10 cents per $100 or major fraction of actual value.
Stock transfers	4 cents per $100 or major fraction of value; not to exceed 8 cents per share.
Deeds, conveyances of realty	55 cents on amount over $100 and not over $500; 55 cents on each additional $500 or fraction.
Foreign insurance policies:	
Life, sickness, accident, annuity contracts, and contracts of reinsurance.	1 cent per dollar or fraction of premium.
Other	4 cents per dollar or fraction of premium.
Playing cards	13 cents per pack.
Manufacturers' excise taxes (based generally on manufacturers' sales price):	
Air conditioners	10 percent.
Automobiles, etc.:	
Passenger cars and auto trailers (other than house trailers).	Do.
Trucks, truck trailers, and truck tractors	Do.
Parts and accessories	8 percent.
Tires	5 cents per pound; 10 cents per pound if the type used on highway vehicles.
Tubes	10 cents per pound.
Tread rubber	5 cents per pound.
Business machines (except retail cash registers)	10 percent.
Cameras, lenses, and film	Do.
Cigarette, cigar, and pipe mechanical lighters	10 percent or 10 cents per unit, whichever is less.
Electric, gas, and oil appliances, household type	5 percent.
Electric-light bulbs and tubes	10 percent.
Firearms, shells, and cartridges	11 percent.
Fountain pens, mechanical pencils, ballpoint pens.	10 percent.
Gasoline	4 cents per gallon.
Lubricating oil	6 cents per gallon.
Matches	2 cents per 1,000 or 10 percent, whichever is less.
Musical instruments, phonographs and records, radio and television sets, and components.	10 percent.
Pistols and revolvers	Do.
Refrigerators, refrigerating apparatus, and quick-freeze units, household type.	5 percent
Sporting goods and equipment	10 percent.

[1] Subtitles D and E, secs. 4001-5862.

TABLE 23.—*Major elements of the Federal excise system*—Continued

Item	Present law rates
Retailers' excise taxes (based on retailers' sales price):	
Furs and fur articles	10 percent.
Jewelry, etc	Do.
Luggage, handbags, etc	Do.
Toilet preparations	Do.
Miscellaneous excise taxes:	
Admissions, amount in excess of $1	1 cent for each 10 cents or major fraction.
Bowling alleys, billiard and pool tables	$20 per alley or table per year.
Cabarets, roof gardens, etc	10 percent of amount paid.
Club dues and initiation fees	20 percent of amount paid.
Coin-operated amusement or gaming devices:	
Amusement or music machines	$10 per machine per year.
Gaming devices	$250 per machine per year.
Diesel fuel for highway vehicles and special motor fuels.	4 cents per gallon.
Leases of safe-deposit boxes	10 percent of amount paid.
Telephone, telegraph, radio, and cable facilities, etc.	8 and 10 percent of amount paid.
Transportation of persons by air	5 percent of amount paid.
Truck use tax (vehicles in excess of 26,000 pounds taxable gross weight).	$3 per 1,000 pounds per year.
Wagering:	
Wagers (except parimutuel)	10 percent of amount of wager.
Occupation of accepting taxable wagers	$50 per year.

The excises contain a variety of exemptions. All the taxes on commodities contain an exemption for exports. Purchases by State and local governments for their own use generally are exempt. The major exception to this rule concerns tobacco products, and, to some extent alcoholic beverages. Nonprofit schools may make purchases free of the manufacturers' and retailers' excises and the taxes on diesel fuel, communications, and transportation. Supplies for military vessels and aircraft, and vessels or aircraft engaged in foreign trade, or the fisheries, are exempt from the manufacturers' taxes and the tax on diesel fuel. Individual taxes contain further exemptions, often dependent on the intended or actual use of the product or service. Thus, the tax on jewelry contains an exemption for any article "used for religious purposes," the tax on toilet preparations contains an exemption for sales "for use in the operation" of a beauty or barber shop, and the taxes on motor fuels contain an exemption (or refund of tax) for fuel sold for use (or used) on a farm for farming purposes.

Tobacco and liquor excises, the two most important elements of the present excise system, were permanently established in the revenue system during the Civil War. These taxes grew in importance and in several of the years preceding the introduction of income taxes produced more revenue than customs duties and thus were the principal source of internal revenue in those years.

Extensive use was made of a wide range of excises during World War I. Most of these were repealed during the following decade, leaving tobacco, liquor, and stamp taxes as the major excises.[2] Most of the present manufacturer's excises were revived during the early 1930's as a depression tax measure adopted in lieu of a general manufacturers' sales tax. This development, in conjunction with falling income tax revenues, resulted in a signficant increase in the revenue importance of excise taxation. Excise revenues increased substantially through 1939 but declined in relative importance toward the end of the decade as individual and corporate income tax yields increased

[2] During the period of prohibition, of course, total liquor taxes were unimportant revenuewise.

Under the impetus of World War II revenue requirements, the rates of most existing excises were substantially increased and the present retailers' excises were introduced, along with taxes on transportation of persons and property. While total excise collections increased very substantially during the war, they continued to decline in relative importance.

Extensive legislation to revise and reduce excises was underway in 1950 when hostilities broke out in Korea. Accordingly, the World War II excises were continued and, in some cases, increased.

The first important postwar excise tax rate reductions were enacted in 1954. Rates were reduced on retail and manufacturers' excises, the general admissions tax, and the communications and transportation taxes. With a few exceptions ad valorem rates in excess of 10 percent were reduced to 10 percent. Rate cuts ranged from 5 to 15 percentage points. Taxes on the transportation of property and oil by pipeline were repealed in 1958. The cabaret tax was reduced from 20 to 10 percent in 1960. The 10-percent tax on transportation of persons was repealed in 1962 except for transportation by air. In the latter case, the rate was reduced to 5 percent.

Many of the excise tax rate increases enacted in response to the Korean emergency originally were effective for only 3 years. Nevertheless, a number of these increases have remained in force through legislation which has extended certain rates on a year-to-year basis for 10 years. This legislation has also delayed implementation of prospective changes in the taxes on general telephone service and the transportation of persons. If another postponement is not enacted before June 30, 1965, the following excise tax revisions will automatically go into effect on July 1 of that year:

TABLE 24.—*Excise tax reductions scheduled for July 1, 1965*

Excise tax	Scheduled rate reduction
Alcohol:	
Distilled spirits	$10.50 to $9 per gallon.
Beer	$9 to $8 per barrel.
Sparkling wines	$3.40 to $3 per gallon.
Artificially carbonated wines	$2.40 to $2 per gallon.
Still wines:	
Not more than 14 percent alcohol	17 to 15 cents per gallon.
More than 14 percent, not over 21 percent alcohol.	67 to 60 cents per gallon.
More than 21 percent, not over 24 percent alcohol.	$2.25 to $2 per gallon.
Wine liqueurs and cordials produced domestically.	$1.92 to $1.60 per gallon.
Tobacco: Cigarettes (small)	$4 to $3.50 per thousand.
Manufacturers' excise taxes:	
Passenger automobiles	10 to 7 percent of manufacturers' price.
Parts and accessories for automobiles	8 to 5 percent of manufacturers' price.
Miscellaneous excise taxes:	
General telephone service	10 percent, repeal.
Transportation of persons by air	5 percent, repeal.

It was estimated that Federal revenues would have been reduced by $1.9 billion, on a full-year basis, if the scheduled reductions had been permitted to go into effect on July 1, 1964.

A significant increase in excise revenues was provided in 1956 to help finance an expanded program of Federal aid to highways. At that time, tax rates were increased on gasoline, diesel, and special motor fuels, trucks, and tires of the type used on highway vehicles.

New taxes were imposed on tread rubber and on the use of heavy trucks on the highways. The revenues from these taxes were transferred into a newly created highway trust fund. Money drawn from this fund is used to finance the Federal share of aid to State highway construction. The Federal share is 90 percent in the case of the interstate highway program. The interstate program is scheduled for completion in 1972, at which time the new highway user taxes are to be repealed and the rate increases enacted in 1956 on existing taxes removed. Because Federal aid for highway construction is limited to moneys derived from the specific user taxes, increases in the original tax rates were required in 1959 and again in 1961 to permit completion of the interstate system in 1972 as originally planned.

Total excise tax receipts were $13.2 billion in the fiscal year 1963 (net of refunds and before transfers to the highway trust fund). The excise receipts comprised 13 percent of Federal cash budget tax receipts for the year. The relative importance of the more important excise taxes in the fiscal year 1963 and, as estimated, in the fiscal year 1965 is shown on the following table:

TABLE 25.—*Excise tax revenues, fiscal 1963 (actual) and fiscal 1965 (estimated)*

[Dollar amounts in millions]

Excises	Fiscal 1963 (actual)		Fiscal 1965 (estimated) [1]	
	Amount	Percent of total	Amount	Percent of total
Liquor	$3,442	26.1	$3,747	25.8
Tobacco	2,079	15.7	2,212	15.3
Gasoline, diesel fuel, and lubricating oil	2,684	20.3	2,880	19.9
Automobiles, trucks, etc	2,586	19.6	2,942	20.3
Retailer's excises	444	3.4	524	3.6
Admissions, cabaret, and dues	154	1.2	188	1.3
Communications	881	6.7	1,000	6.9
All other, net of refunds	925	7.0	998	6.9
Total	13,195	100.0	14,491	100.0

[1] Includes proposed legislation for airways and waterways user charges.

II. Issues and Proposals

The proper role of excises in the Federal revenue system has been the the subject of continuing controversy, particularly since the end of World War II. Specifically, this controversy has focused on the rationale for selective excises, the differential impact of excises on the various taxed industries, on their effectiveness in offsetting cyclical changes in income, and on their impact on consumption and the overall distribution of tax burdens. Interest has also been directed to the more general question of whether excise or general commodity taxation should have more or less weight in the Federal revenue structure. A variety of proposals, ranging from complete elimination of excise taxation to establishing a uniform manufacturers' or retailers' sales tax have emerged from the discussion of the various issues.

A. SPECIFIC ISSUES

1. *The rationale of excise taxation*

Basic to the rationale for excise taxation is the assumption that the burden of a tax based on the value of a commodity is passed from the producer to the consumer.[3] Tax payments by consumers are therefore considered to be directly related to the level of consumption of the taxed articles. In general, justification for this method of distributing the tax burden is based on the view that consumption expenditures provide a suitable measure of taxpaying ability and an acceptable means for distributing the burden of taxation among taxpayers in different situations. Excises in this view are considered supplements to the income tax which permit a reduction in the high marginal income tax rates which would otherwise be required. In addition to this general view of excises, certain special situations are identified by some observers as ones in which the use of excise taxes is particularly appropriate.

An excise tax, it is argued, may serve as an instrument of public policy to discourage or penalize the consumption of certain commodities. Excessive use of certain products is felt to entail costs to society which exceed their cost to individual consumers. Leading examples of these so-called sumptuary excises are the taxes on alcoholic beverages and tobacco products.

Other excises are viewed as direct charges, analogous to prices, levied in return for the provision of a specific service. The taxes on motor fuels, trucks, and tires imposed to finance the expenditures of the highway trust fund are often considered use taxes in the sense that tax payments are made in proportion to use of the highways. The proposed taxes on users of airways and waterways are justified by their proponents on the grounds that users of these facilities should bear a larger share of the cost of maintaining and improving these facilities than they do at present.[4]

Finally, excises are, it is argued, generally easier to collect than income taxes and more efficient to administer.

The applicability of the foregoing rationale has been questioned. It is pointed out that it is not clear in all instances that the burden of excise taxes is fully passed on to consumers. Conditions of supply and demand are likely to result, it is contended, in the sharing of selective excise tax burdens between consumers and producers to an extent that varies from case to case. With regard to sumptuary excises, it is argued that the taxes do little to discourage consumption of the commodities. Indeed, the taxes are important revenue producers precisely because they do not discourage consumption to a significant extent. If social needs dictate a restriction in the use of certain products, more effective means can be found for implementing this objective than the use of excise taxes. With regard to use taxes, it is pointed out that the benefits of an adequate program to provide public facilities such as highways are widely diffused throughout the economy. Since all consumer units benefit from such programs, it is contended, they should be financed from general revenues.

A primary criticism of excise taxes, particularly those upon manufacturers' sales, is that they tend to have a regressive and often arbitrary burden distribution. It is pointed out that high income families are generally able to save a larger proportion of their current incomes and thus tend to pay a smaller proportion of their income for the purchase of taxed items. Among individuals in like circumstances,

[3] Much of this discussion is based on John F. Due, "Criteria for Evaluating Possible Reductions in Federal Excise Taxes," Excise Tax Compendium, pp. 1–12.
[4] See the President's message on transportation, Apr. 4, 1962, H. Doc. 384, 87th Cong., 2d sess.

it is argued that the tax burdens should be distributed on a more rational basis than that provided by individual preferences for taxed and nontaxed items.

Finally, it is pointed out that the bulk of Federal excise tax revenues is derived from taxes on alcoholic beverages, tobacco products, motor fuels, automobiles, and automobile parts. Taxes on the great majority of items subject to Federal excise levies actually produce insignificant amounts of revenue. Under the circumstances, it is argued, administrative costs are high in relation to yield for many of the existing excises.

2. Impact of excises on business costs and prices

One of the principal arguments advanced against excise taxation, particularly in the form of selective manufacturers' sales taxes, is that this type of tax has an adverse impact on production and employment in the taxed industries. It is pointed out that an excise imposed on the production of a taxed commodity enters the cost functions of the manufacturer in the same way as the costs of raw materials, labor services, and other factors of production, the outlays for which vary with output. Such increases in cost result in higher prices and tend to reduce the sales and profits of the taxed producers. Accordingly, investment will tend to decrease in the taxed industry (or at least increase at a slower rate than in nontaxed industries), and to be diverted to nontaxed lines.

It is contended that these results may be justified under wartime or defense emergency circumstances, when as a matter of public policy it is desired to divert resources from uses not essential to the defense effort. This type of tax is regarded as particularly appropriate where the resources used in producing the taxed items are readily transferable to defense production.

Moreover, it is contended that excise taxation has a highly differential impact even within a given industry. Some argue that a manufacturers' excise, for example, will be less burdensome on the highly integrated company in the taxed industry than on the nonintegrated firm, since in the former case the tax will enter the company's cost structure at a later stage between production and sale to the ultimate consumer. In the latter case, however, the tax may very well be pyramided by both wholesaler and retailer, since the wholesale distributor will base his markup on his cost of the commodity including the excise and the retailer's markup will be based on his cost including the marked-up excise.

Others argue, however, that a manufacturer's excise bears more heavily on the integrated than on the nonintegrated company. The integrated company, it is claimed, incurs essentially the same costs of distribution as wholesale distributors for nonintegrated firms. The manufacturer's excise is levied with respect to the manufacturer's sales price. Since for the integrated firms this sales price must reflect distribution as well as manufacturing costs, the tax will tend to be higher per unit of the taxed commodity for an integrated firm than for a nonintegrated firm, whose selling price does not include wholesale and retail distribution costs.

Retailers' excises are regarded as having essentially the same impact on competing retail firms. Since these excises are imposed, generally, on an ad valorem basis, they tend to magnify the absolute differentials

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in the prices paid by consumers between firms with differing pretax prices on the taxed items. For example, if, because of cost advantages, one store can afford to sell a given item for a specified amount less than its competitor, the imposition of an ad valorem retail excise will serve to spread the difference in the price charged the consumer. Alternatively, some portion of the tax will have to be absorbed by the second firm, resulting in a relative cut in its profits.

On the other hand, it is contended that the differential impact of excise taxation reflects basic differences in efficiency among the taxed firms. While it is agreed that a given excise may not be neutral in its impact, it is contended that its nonneutrality works in the right direction by providing an additional impetus for the relatively inefficient company to find savings in other costs.

Moreover, it is argued, the differential impact as between taxed and nontaxed industries does not constitute an argument against excises but rather against a selective excise system. Replacing the present system of excise taxation with a general system, imposed at uniform rates throughout, it is contended, would eliminate objections that the tax interferes with the free market allocation of resources.

3. Impact on consumption

Since excises tend to be reflected in the prices of the taxed commodities, they serve to restrict consumption of the taxed articles. There is general agreement that this result is desirable where it is intended to divert resources to defense uses or where consumption of the taxed item has socially undesirable effects, as in the case of narcotics. The same type of argument is frequently applied in the case of excises on luxuries, to which, it is argued, commodity taxation should be largely restricted.

It is contended, for example, that the taxation of luxury commodities involves a relatively low cost in terms of lower living standards. Restricting the consumption of such goods, it is said, results in more resources being devoted to the production of those goods and services which are basic to the material well-being of the entire country. The relative increase in the output of the latter results in a relative lowering of their prices and therefore provides a stimulus for increased consumption.

On the other hand, it is argued that this basis for excise taxation involves several difficulties. In the first place, it is pointed out that the concept of a "luxury" does not lend itself to objective definition, but depends on arbitrary determinations. Once the excise is imposed, it becomes difficult to remove it, even though what was regarded as a luxury at the time of imposition comes generally to be thought of as a necessity.

Moreover, it is contended that a free market economy depends for its effective operation on free consumer choices with which excises interfere. In a free market, each consumer unit is regarded as having responsibility for allocating its limited consumption budget in such a way as to maximize total satisfaction. It is in this sense only, it is argued, that material well-being is measurable. Accordingly, the imposition of an excise, by discouraging the consumption of the taxed commodity, necessarily results in a reduction in the total satisfaction derived from aggregate consumer purchases.

4. Sensitivity of excise revenues to changes in income

A major criticism directed against extensive reliance on excise taxation in the Federal revenue system is the relative insensitivity of the yield of present excises to changes in national income. This insensitivity, it is maintained, follows from the fact that revenue considerations have dictated the selection of items for tax purposes the consumption of which is relatively stable.

According to some estimates, the change in the yield of excise taxes is less than proportional to changes in income. It is argued, therefore, that excises fail to meet what is now regarded as one important criterion applied to elements of the Federal revenue system; namely, that a tax should make a substantial contribution toward automatic stabilization of the economy.

According to this view, it should be recognized that adopting any proposal which places relatively greater stress on excises in the revenue system necessarily involves a responsibility to undertake greater discretionary action to offset changes in the level of economic activity. To enhance the built-in flexibility of the Federal revenue system as a whole, it is argued, excises should be replaced wherever possible by taxes that are more sensitive to income changes, so that on balance increasing weight will be placed on taxes whose revenues fluctuate more than proportionately with changes in national income.

On the other hand, it is argued that countercyclical tax policy does not require that all elements of the revenue system be highly elastic with respect to income changes. Considerations of the sumptuary and benefit bases for many of our excises, it is contended, outweigh those with respect to built-in flexibility and dictate continued use of those taxes.

Moreover, it is pointed out that the relative insensitivity of the present Federal excise system should not be construed as characterizing all excises. On a selective basis, an alternative excise system might well be devised which would evince considerably greater responsiveness of yield to income changes.

B. RELATIVE EMPHASIS ON EXCISE TAXATION

It is frequently argued that excises should play a larger role in the Federal revenue system.[5] In support of this position, it is pointed out that the system places less emphasis on excises than is to be found in many other major countries. The result has been an undue concentration on income taxation, which at both the corporate and individual levels has had, or may be expected to have in normal times, a highly repressive effect on the economy's growth potentials. Heavier reliance on excises, it is argued, would permit a reduction in corporate and individual income taxes. In turn, this would reduce a deterrent to undertaking new ventures and would induce the greater rate of the personal savings required to finance business growth.

In answer to this argument, it is contended that the principal incentive for growth-generating activity is an expanding total demand, of which consumption outlays are the largest component. Since excises are with few exceptions regressive in character, that is, they

[5] For a discussion of the issues raised by such proposals, see "The Role of Direct and Indirect Taxes in the Federal Revenue System," conference report of the National Bureau of Economic Research and the Brookings Institution, Princeton University Press, 1964.

absorb a larger proportion of income the lower the income of the individual, they have a particularly severe effect on the outlays of persons who must spend a high proportion of their income for consumption. Such persons form the bulk of the Nation's consumers. Accordingly, it is argued, there is no assurance that greater relative emphasis on excises in the Federal revenue system would not serve to retard rather than to enhance economic growth.

Support for proposals favoring greater emphasis on broad-based excise taxes has been engendered by concern over the balance-of-payments position of the United States. Some observers have taken the position that, under the GATT rules, some of our foreign competitors are able to subsidize their exports and impose the equivalent of a tariff on imported articles. The rebate on exported items enables foreign exporters, it is argued, to sell goods in foreign markets below domestic prices while the equalization tax on imports serves to raise the price of U.S. goods sold in foreign markets. Some of those who feel that the present situation discriminates against our exports urge that we meet the situation by adopting a tax structure similar to those of our international competitors.

Central to the issue is a decision on the manner in which the burden of a corporate income tax on the one hand and a sales tax on the other hand are distributed and, therefore, the effects of the separate taxes on prices and resource allocation. The manner in which income and sales taxes are distributed is the subject of considerable debate among economists.[6] Recent studies have failed to resolve the question of whether the corporate income tax is largely absorbed by shareholders or whether it is quickly passed on to consumers in the form of higher product prices. Similarly, there is disagreement on the extent to which a sales tax is reflected in higher product prices or in lower payments to the factors of production. Whereas the GATT position has been criticized for assuming 100 percent shifting in the case of a sales tax and zero shifting in the case of an income tax, no consensus can be said to exist on the proper assumption which should be made. In the absence of such a consensus, there are wide differences of opinion regarding the extent to which a shift to indirect taxes would affect the price of U.S. exports.

Apart from questions as to the degree to which existing taxes are reflected in the prices of products traded, there is debate on the effect that tax measures would have on the balance of payments. It is argued that even if the United States were to shift much of the burden of its corporate and individual income tax to a general sales tax and then follow the practices permitted by GATT, our balance-of-payments problem might persist. It is pointed out that the country has consistently maintained a favorable trade balance; that is, exports of goods and services regularly exceed imports. Balance-of-payments deficits are traceable to capital flows and to Government operations. It is contended, therefore, that efforts to redress balance-of-payments deficits should concentrate on these transactions and not on the flow of trade. Proponents of the sales tax proposals argue, on the other hand, that a further widening in the favorable trade balance would grant the United States greater freedom to invest abroad and pursue foreign policy objectives.

[6] See ch. 3, "Corporate Income Taxation."

Those who are skeptical of the balance-of-payments benefits of a shift to indirect taxes point out that France, which is the foremost example of a country which employs the value-added tax, has lived under its present tax structure for many years yet only recently has become a strong surplus country with respect to its balance of payments. Its present situation, it is contended, is due to other circumstances, such as the devaluation of the franc and tight control over the economy by the Central Government.

Some analysts argue that use of indirect taxes to promote exports through the expedient of rebating the tax on exports and imposing compensating taxes on imports is simply a method of de facto devaluation of the national currency. If so, they argue, straightforward devaluation might be more effective. Proponents of the sales tax proposals point out, however, that the United States, as one of the free world's foremost trading and financial countries, cannot realistically consider devaluing its currency. Supplies of gold are inadequate to finance international reserves and dollars have, therefore, come into wide use as a reserve currency. If uncertainty over the future value of the dollar were to be created by devaluation or the threat thereof, the existing international monetary mechanism would be gravely weakened.

Finally, those opposed to a greater Federal emphasis on commodity taxation point out that a national tax structure, reflecting as it does differing national opinions as to the proper scope of governmental activities, should be considered simply as one aspect of comparative advantage similar to climate, resource endowments, labor skills, and other factors which govern the flow of trade between nations. They argue that there is no reason to single out this one feature of national differences for neutralization. Critics of this view, on the other hand, maintain that tax differences, like tariff barriers, are artificial and should be eliminated so that real factors can control the flow of trade and promote the optimum allocation of world resources.

A further argument offered for greater emphasis on excises is that it would insure greater contributions to the costs of Government on the part of a larger number of individuals who make no significant contributions through other types of taxes. It is pointed out that in 1961 about 12.9 million of the 61.5 million Federal individual income tax returns filed showed no income tax liability. It is contended that for purposes of responsible government every citizen should make some contribution to the costs of Government and since those with low incomes substantially escape income taxation, the role of excises should be broadened.

On the other hand, it is argued, a basic principle of taxation in the United States is that tax burdens should be based on ability to pay. The fact that a substantial number of individuals do not incur Federal income tax liabilities, it is said, reflects an explicit determination that their incomes are insufficient to warrant tax liability. If it is decided that such low-income individuals should contribute to defraying the expenses of Government, adjustment should be made in the income tax to bring these individuals onto the tax rolls in a manner that insures that their relative tax contributions will best conform to the ability-to-pay criterion.

Moreover, it is pointed out that excise and sales taxes play a major role in State and local government revenue systems. Greater use of excises by the Federal Government, it is argued, would not only encroach on the tax sources used by States and localities but would also enhance the regressive features in the combined Federal-State-local revenue structure.

C. PROPOSALS

A wide variety of proposals have been offered for revision of the Federal system of excise taxation, ranging from major substantive proposals to suggestions for technical amendments. Although extensive technical revisions were enacted in 1958, many more such changes have been proposed. Of continued interest is the proposal for replacing the present excises with a general manufacturers' or retail sales tax. A somewhat less extreme proposal calls for the equalization of rates among manufacturers' excises and among retail sales and other excise taxes. At the opposite extreme are proposals for complete elimination of all Federal excises and the more moderate proposal for progressive rate reduction leading to eventual elimination of these taxes.

1. General sales taxes

Proposals for a general manufacturers' sales tax have been offered repeatedly since the 1930's. A number of major arguments are offered in support of this type of levy.

In the first place, it is contended that the present system of excises is highly selective and as such penalizes the taxed industries. Even among the taxed industries, the lack of tax uniformity often results in competitive advantages as between industries producing highly competitive products. Moreover, the wide variety of excises, including those imposed as manufacturers' sales taxes, retailers' sales taxes, transactions taxes, and miscellaneous other forms, has an undesirably varied impact on the taxed businesses. A single uniform levy, it is urged, would remove the inequities and anomalies inherent in the present highly disparate system.

Second, it is claimed that on the basis of administrative considerations, excises should be levied only upon the sale of the taxed articles by the manufacturer. This would provide savings in administrative costs since there are far fewer manufacturers than retailers and wholesalers, and manufacturing establishments may generally be counted on to have more highly developed accounting systems than many of the numerous small retail firms.

It is also pointed out that the present system of excises frequently involves rates so high as to reach the point of diminishing returns. The example most often cited is the tax on alcoholic beverages, which at present levels is regarded by many as responsible for a considerable volume of bootleg sales. Selective rate reductions, however, are not the answer, it is argued, since they necessarily give rise to claims for similar preference in other excises, resulting eventually in a total revenue loss so large as to pose a serious budgetary problem. Accordingly, it is argued that the only practicable way in which prohibitively high rates of excise tax can be reduced is by providing for a general excise system producing the same total revenue as the present selective excises.

Finally, it is argued that only by adopting a general excise system can the unduly heavy burden of progressive income taxation be relieved. Rates in the income tax are regarded as so high as to deter sustained economic growth. Furthermore, it is evident that if such rates are required while the country is in a relatively peaceful era, income taxation cannot be counted on to provide the fiscal resources which would be required if a substantially larger defense program were undertaken. Fiscal preparedness, it is claimed, requires the adoption of a general excise system.

In opposition to this proposal, it is argued that a general excise, whether at the manufacturers' or retailers' level, would violate the basic concept of equity in the Federal revenue system. It is this ability-to-pay concept which is the basis for progression in our income tax. A general sales tax, however, would involve substantial regressivity. This would be true, it is claimed, since the tax could not feasibly be applied to most services, which represent an increasing proportion of total consumption as income rises. In addition, the tax would be imposed only on spending and since low-income individuals generally have no net savings out of current income, the tax would bear far more heavily on them than on upper income groups. Even if, as is frequently proposed in connection with a manufacturers' sales tax, specific exemptions were provided for food, medicine, and shelter, the tax, it is alleged, would nevertheless remain regressive overall.

In addition to its regressivity, a general sales tax, it is argued, would penalize consumption and favor savings. This would be especially true if the tax were designed to produce a significant increase in revenue compared with the present excise system. This result may be tolerable in times of war or heavy defense emergency programs. At other times, it is argued, it would represent a significant deterrent to the sustained growth of aggregate demand. Despite the general bias in favor of thrift, it is contended, too high a savings rate places a heavy burden on private investment and Government spending in the fight to sustain full employment. The historical record, it is alleged, shows no deficiency in personal savings, while, on the contrary, inadequate consumption expenditures have been largely responsible for sluggish growth of total demand.

Objections to a general Federal sales tax are also voiced by those concerned with the financial problems of State and local governments. It is contended that general sales taxation represents one of the major fiscal devices, actual and potential, available to these governments as a means of financing their growing spending programs. The adoption of a Federal levy of this character, it is claimed, would further circumscribe the fiscal autonomy of State and local governments and result in an increasing level of Federal responsibility for programs traditionally undertaken at the State or local level.

2. Rate uniformity

Under a somewhat less extreme proposal than that for a general sales tax, it is suggested that Federal excise revision be directed primarily toward providing a uniform system of rates for all commodities and transactions now taxed. Specifically, it is proposed that all Federal excises be placed on an ad valorem basis and at a single rate or system of rates which will provide about the same total revenue as the present excise system.

In support of this proposal, it is argued that lack of uniformity in rates involves excessively high rates on some items and rates that are too low on others, in view of the competitive relationship among the producers and sellers of the taxed articles. The ad valorem basis for many of the present excises, it is contended, often results in significant disparities in the impact of the tax on prices and profits. Tobacco products and alcoholic beverages are frequently cited in illustration of this point.

On the other hand, it is pointed out that uniformity in rates was substantially achieved by the Excise Tax Reduction Act of 1954. Where nonuniformity persists, it is maintained, the sumptuary, user charge, or regulatory bases of such excises preclude uniformity in rates. In some cases, it is argued, rates are set relatively high in order to discourage the use of the taxed item. In others, for example, the highway program excises, the rates tend to move, at least over time, in response to changes in benefits provided by Federal spending programs. In still other cases, the rates reflect efforts to exact maximum revenue from the taxation of articles the consumption of which is deemed to be of marginal social importance. Uniformity in rates, therefore, would often interfere with the purposes intended to be served by the excises.

3. Elimination of Federal excises

Numerous proposals have been made for the reduction of Federal excises, leading to the eventual elimination from the Federal revenue system of all excises except perhaps those on liquor, tobacco, and gasoline. The arguments offered by the proponents of this approach have been stated above. In summary, it is contended that considerations of equity, economic stabilization, and sustained economic growth require the eventual elimination of most if not all the Federal excise taxes.

Many of the arguments opposed to this position are also indicated above. In addition, it is pointed out that excises, though not a major element of the Federal revenue system, nevertheless represent between one-sixth and one-seventh of total Federal tax collections. Their elimination, therefore, would require an increase in income tax burdens or a postponement of income tax reductions otherwise possible.

CHAPTER 10

FEDERAL ESTATE AND GIFT TAXATION

I. Present Law

A. ESTATE TAX

The Federal estate tax is an excise tax imposed on the transfer of property by a decedent. It differs, therefore, from an inheritance tax in which tax is imposed, generally, on the heir who receives the property.

The base of the estate tax is the gross estate transferred, adjusted for certain deductions and exemptions.[1] The tax is imposed at the following graduated rates: [2]

TABLE 26.—*Estate tax rates*

Taxable net estate:	*Estate tax rate (percent)*
0 to $5,000	3
$5,000 to $10,000	7
$10,000 to $20,000	11
$20,000 to $30,000	14
$30,000 to $40,000	18
$40,000 to $50,000	22
$50,000 to $60,000	25
$60,000 to $100,000	28
$100,000 to $250,000	30
$250,000 to $500,000	32
$500,000 to $750,000	35
$750,000 to $1,000,000	37
$1,000,000 to $1,250,000	39
$1,250,000 to $1,500,000	42
$1,500,000 to $2,000,000	45
$2,000,000 to $2,500,000	49
$2,500,000 to $3,000,000	53
$3,000,000 to $3,500,000	56
$3,500,000 to $4,000,000	59
$4,000,000 to $5,000,000	63
$5,000,000 to $6,000,000	67
$6,000,000 to $7,000,000	70
$7,000,000 to $8,000,000	73
$8,000,000 to $10,000,000	76
$10,000,000 and over	77

An estate tax return is required for the estate of every individual the value of whose gross estate at the date of death exceeds the specific exemption of $60,000.[3] In general, the return and any tax liability are due within 15 months of the date of death, although an extension of time may be granted.[4] If the estate consists largely of an interest in a closely held business, however, the tax on such interest may be paid in installments over a 10-year period.[5] An interest in a

[1] Secs. 2001, 2051.
[2] Sec. 2001.
[3] Secs. 6018, 2052.
[4] Sec. 6075.
[5] Sec. 6166.

closely held business is defined as (1) a sole proprietorship, (2) an interest in a partnership with not more than 10 partners, if at least 20 percent of the total capital interest of the partnership is included in the decedent's gross estate, or (3) stock in a corporation with not more than 10 shareholders if at least 20 percent of the value of the voting stock is in the decedent's gross estate. To qualify for the installment payment election the interest in a closely held business must represent at least 35 percent of the gross estate or 50 percent of the taxable estate.

The graduated estate tax rates are applied to the taxable estate, defined as the gross estate less the specific exemption and certain deductions.[6] The gross estate includes the total amount of property which, under estate tax law, is deemed to have been transferred at death.[7] The value of all property in the gross estate may be determined for tax purposes as of the date of death or as of the date 1 year after death, at the election of the executor.[8]

Specific rules in the law govern the extent to which certain property interests of the decedent, such as those in trusts, joint tenancies, community property, and property transferred during the decedent's lifetime, are to be included in his gross estate.[9] Specific rules also apply with respect to insurance proceeds, which are included unless they are received by beneficiaries other than the executor and the dedecent retained no incidents of ownership in the policies during his lifetime.[10]

Apart from the $60,000 specific exemption, deductions from the gross estate are allowed for funeral expenses, administrative expenses, claims against the estate, and unpaid mortgages upon, or other debt with respect to, property included in the gross estate.[11] In addition, a deduction is allowed for charitable bequests.[12] No limitation is imposed on the amount of this deduction, except that it may not exceed the value of the contributed property which must be included in the gross estate.

Finally, a marital deduction is allowed for property passing to the decedent's husband or wife.[13] This deduction is limited to 50 percent of the "adjusted gross estate," defined as the gross estate minus the sum of the deductions listed above (and after deductions for any community property included in the gross estate). The deduction for charitable transfers and the specific exemption, however, are not required to be taken into account in computing the adjusted gross estate.

Certain credits may be allowed against the estate tax liability. The principal of these is the credit for State inheritance, legacy, or estate taxes.[14] The maximum credit allowable for State death taxes is expressed as a percentage of the decedent's taxable estate in excess of $40,000; the law provides a graduated rate table for the purpose of computing the credit. The credit percentages range from 0.8 percent of the taxable estate in excess of $40,000 but not in excess of $90,000 to 16 percent of the taxable estate in excess of $10,040,000.

[6] Secs. 2051-2056.
[7] Sec. 2031.
[8] Sec. 2032.
[9] Secs. 2031-2044.
[10] Sec. 2042.
[11] Sec. 2053.
[12] Sec. 2055.
[13] Sec. 2056.
[14] Sec. 2011.

These percentages reflect a provision of pre-1954 law which limited the credit to 80 percent of the gross basic tax.[15] The allowance of this credit encourages the States to levy estate taxes by removing much of the incentive to reduce or eliminate these taxes in an interstate competition for wealthy residents.

Credit against the estate tax is also allowed for gift taxes paid by the decedent on transfers made by him during his lifetime but included in his gross estate.[16] Such transfers, even though previously taxed as gifts, are included in the gross estate when it is found that they were made in contemplation of death. The amount of this credit is limited to the amount of the gift tax allocable to the property included in the gross estate and may not exceed the amount of the estate tax allocable to such property.

In order to prevent the imposition of successive estate taxes on the same property within a brief period, a credit is allowed for all or part of the estate tax paid with respect to property transferred to the present decedent from another decedent within 10 years before the present decedent's death.[17] The credit is a "vanishing" one, since it is reduced by 20 percent for each full 2 years separating the deaths.

Finally, a credit is allowable for foreign death taxes with respect to property subject both to the U.S. and foreign estate taxes.[18] Only taxes attributable to property taxed in both the United States and the foreign country may be allowed as a credit, which is limited to that portion of the U.S. tax attributable to such property.

B. GIFT TAX

Like the estate tax, the Federal gift tax is an excise upon transfers of property by gift. The tax is a liability of the person making the gift and is based upon the value of the transferred property.

The tax is imposed at graduated rates on taxable gifts, defined as total gifts less allowable exclusions and deductions. Rates of tax, which are three-fourths of those under the estate tax, are as follows: [19]

[15] Under the prior law, the estate tax consisted of a "basic" tax and an "additional" tax. The latter was added by the Revenue Act of 1932.
[16] Sec. 2012.
[17] Sec. 2013.
[18] Sec. 2014.
[19] Sec. 2502.

TABLE 27.—*Gift tax rates*

	Gift tax rate (percent)
Taxable net gift:	
0 to $5,000	2.25
$5,000 to $10,000	5.25
$10,000 to $20,000	8.25
$20,000 to $30,000	10.50
$30,000 to $40,000	13.50
$40,000 to $50,000	16.50
$50,000 to $60,000	18.75
$60,000 to $100,000	21.00
$100,000 to $250,000	22.50
$250,000 to $500,000	24.00
$500,000 to $750,000	26.25
$750,000 to $1,000,000	27.75
$1,000,000 to $1,250,000	29.25
$1,250,000 to $1,500,000	31.50
$1,500,000 to $2,000,000	33.75
$2,000,000 to $2,500,000	36.75
$2,500,000 to $3,000,000	39.75
$3,000,000 to $3,500,000	42.00
$3,500,000 to $4,000,000	44.25
$4,000,000 to $5,000,000	47.25
$5,000,000 to $6,000,000	50.25
$6,000,000 to $7,000,000	52.50
$7,000,000 to $8,000,000	54.75
$8,000,000 to $10,000,000	57.00
$10,000,000 and over	57.75

The tax is cumulative, that is, it applies each year to the aggregate sum of all taxable gifts made since enactment of the 1932 law. The tax to be paid in any one year is equal to the difference between (1) the tax on the aggregate sum of all taxable gifts made since 1932 and (2) the amount of tax on the aggregate gifts made up to the beginning of the current taxable year. In determining (1) and (2), gift tax rates in effect in the current taxable year are applied.[20]

In computing the amount of "taxable gifts" in any one year, the first $3,000 of gifts to each recipient may be excluded.[21] Where a husband and wife agree to treat gifts by either as having been made one-half by each, each may claim a $3,000 annual exclusion, resulting therefore, in a maximum combined annual exclusion of $6,000 per recipient.

In addition to the annual exclusion, there is, in addition, a specific exemption of $30,000 of total lifetime gifts to all donees.[22] This exemption may be claimed in full in a single year or, at the taxpayer's option, over a number of years until the full $30,000 exemption is exhausted. When a married couple treats gifts as made one-half by each, the specific exemption is increased to $60,000.

Certain deductions are also allowed in computing the amount of taxable gifts. Gifts made to charitable, civic, religious, public, and similar organizations may be deducted in full.[23] In addition, one-half of the value of gifts made between a husband and wife after April 2, 1948, may be deducted from the net aggregate gifts subject to tax.[24] This marital deduction corresponds roughly to that allowed for estate tax purposes.

[20] Sec. 2502.
[21] Sec. 2503.
[22] Sec. 2521.
[23] Sec. 2522.
[24] Sec. 2523.

C. LEGISLATIVE HISTORY

The Federal estate tax was first imposed in 1916 at rates ranging from 1 percent on taxable estates under $5,000 to 10 percent on the amount of a taxable estate in excess of $50 million. Rates were increased by successive legislation, reaching a top rate of 25 percent under the Revenue Act of 1917. In 1926 the top rate was reduced to 20 percent while the former $50,000 exemption was increased to $100,000.

The gift tax was first levied for the 2 years 1924 and 1925, on a noncumulative basis, at rates ranging from 1 percent on net gifts not in excess of $50,000 to 25 percent on the amount of gifts over $50 million. The annual per donee exclusion was $500 and a $50,000 specific exemption was provided.

In 1932, substantial revisions were made in the estate tax and the present gift tax was introduced. Under the 1932 act, the estate tax exemption was reduced from $100,000 to $50,000, and the maximum rate was increased from 20 to 45 percent. Subsequent legislation during the 1930's further reduced the exemption and increased rates. Rates were again revised in 1941, providing the schedule now in effect. In 1942, in connection with the disallowance of a limited deduction for insurance proceeds, the exemption was increased to its present level of $60,000.

Rates under the gift tax of 1932 were set at 75 percent of those in the estate tax. This relationship was maintained through the subsequent estate-tax rate revisions. The specific exemption under the 1932 gift tax was $50,000, reduced to $40,000 in 1935, and to the present $30,000 in 1942. The annual exclusion, originally $5,000 under the 1932 act, was reduced to $4,000 in 1938 and to $3,000 in 1942.

The 1942 legislation also made a significant change in the treatment for estate and gift tax purposes of transfers between a husband and wife. Prior to that time, only one-half of the community property so transferred was taxable in community-property States under the estate tax, and gifts to third parties in these States were attributed one-half to each spouse. In non-community-property States, on the other hand, the entire amount of property was taxable to the spouse accumulating it.

In an effort to equalize treatment between residents of community and non-community-property States, the Revenue Act of 1942 provided that transfers of community property were taxable to the transferor to the extent either that the property was economically attributable to him or that he had control over its disposition.

The Revenue Act of 1948 repealed these provisions of the 1942 legislation and provided the marital deduction for estate and gift tax purposes. Thus, the applicable rules in community property States reverted to the pre-1942 period, while in non-community-property States, the taxable estate is reduced by the amount transferred to the surviving spouse, but by not more than one-half the estate. A similar deduction is allowed in case of gifts, and gifts to a third person are treated as made one-half by each spouse.

D. CHARACTERISTICS OF THE ESTATE AND GIFT TAX BASES

1. *Estate tax*

The estates of only a relatively small proportion of the adults who die each year are subject to Federal estate tax liability. In 1961, for example, 45,439 estate tax returns were filed, compared with an estimated 1.5 million adult deaths which occurred that year. The returns filed in 1961 generally pertained to deaths which occurred in 1960 and earlier years, but the number is a fair estimate of the number of taxable estate tax returns which will be filed with respect to deaths that occurred in 1961.

The total value of the gross estates for which tax returns were filed in 1961 by residents and citizens was $14.7 billion. Corporate stock, which aggregated $6.8 billion, was the largest single property component in these gross estates while real estate, valued at $2.9 billion, was the second largest. Exemptions and deductions comprised roughly 60 percent of the gross estate values. The taxable portions of gross estates totaled $6 billion. The specific exemption and the marital deduction were the most important deduction categories. Nontaxable returns comprised 30 percent of all the estate tax returns filed and accounted for $1.9 billion of gross estates.

The net estate tax liability on returns filed in 1961 by residents and citizens was $1.6 billion, or 11 percent of the value of gross estates and 27 percent of net estates. Taxable returns listing gross estates of $150,000 or less accounted for 51 percent of all returns filed in 1961, but only 4 percent of the overall tax liability. Returns with gross estates of $1 million or more, on the other hand, accounted for 50 percent of the total tax liability and only 3 percent of the returns filed. Tax liabilities as a percent of gross estates ranged from an average of less than 2 percent on returns with gross estates of $60,000 to $70,000 to an average of 21 percent on returns listing gross estates of $20 million or more.

2. *Gift tax*

The total value of the gifts reported in the year on the 78,232 gift tax returns filed in 1961 was $2.3 billion, of which $1.2 billion was reported on the 17,936 returns with gift tax liabilities in 1961. Taxable gifts for the year totaled $657 million or 54 percent of the gifts listed on taxable returns before exclusions and deductions. The gift tax paid, $158 million, was equal to 24 percent of taxable gifts in the year.

II. ISSUES AND PROPOSALS

A. THE ROLE OF ESTATE AND GIFT TAXATION IN THE FEDERAL REVENUE SYSTEM

In recent years net receipts from the Federal estate and gift taxes have represented a small percentage of total Federal revenues. Estate and gift taxes were most important, relatively, as a source of Federal receipts in the decade of the 1930's. While revenues from these taxes have increased steadily since that time, the revenues under the individual and corporate income taxes and excise taxes have increased at a much more rapid rate. Estate and gift taxes therefore have declined in relative importance. For the most part, however, this development took place during World War II and the

Korean emergency. A gradual increase in the relative importance of estate and gift taxes is discernible at the present time. The following table shows receipts, after refunds, from the Federal estate and gift taxes as a percent of administrative budget receipts in the fiscal years 1939 through 1965:

TABLE 28.—*Combined estate and gift tax revenues, fiscal years 1939–65*

Fiscal year	Estate and gift taxes (millions) [1]	Percent of administrative budget receipts	Fiscal year	Estate and gift taxes (millions) [1]	Percent of administrative budget receipts
1939	$357	7.1	1953	$881	1.4
1940	357	6.9	1954	934	1.5
1941	403	5.7	1955	924	1.5
1942	421	3.4	1956	1,161	1.7
1943	442	2.0	1957	1,365	1.9
1944	507	1.2	1958	1,393	1.9
1945	638	1.4	1959	1,333	2.0
1946	669	1.7	1960	1,606	2.1
1947	770	1.9	1961	1,896	2.4
1948	890	2.2	1962	2,016	2.5
1949	780	2.1	1963	2,167	2.5
1950	698	1.9	1964 [2]	2,392	2.7
1951	708	1.5	1965 [3]	2,740	2.9
1952	818	1.3			

[1] Net of refunds.
[2] Preliminary.
[3] January 1964 budget estimate.

Source: U.S. Treasury Department.

The relatively small yield of these taxes in relation to other taxes in the Federal revenue system has been remarked both by proponents of more extensive reliance on estate and gift taxes and by those favoring their elimination, at least at the Federal level. The former criticize the present taxes as evidently inadequate to achieve the objectives for which they were introduced into the Revenue Code. They contend that the legislative history of the Federal estate and gift taxes clearly establishes that these taxes were regarded, at least originally, as important revenue devices. That this purpose is not being served by the present taxes, they maintain, is evidenced by the fact that even with the substantial increase in property values in recent years, annual combined estate and gift tax liabilities remain less than $3 billion and a very small fraction of total Federal taxes. The relatively insignificant role of these taxes in the Federal revenue system, it is claimed, is attributable, at least in part, to the disinclination of the Congress to correct those provisions of the present law which permit large amounts of property transferred by gift or at death to escape taxation.

In addition, proponents of this view maintain that the present estate and gift taxes largely fail to accomplish the important social objective generally ascribed to them. Estate and gift taxes, it is argued, are intended to prevent the continuing accumulation through successive generations of giant family fortunes and to promote a more even distribution of wealth. This objective is characterized as being of basic importance in a democratic society. An ever increasing concentration of wealth is regarded as a serious threat to the basic tenets of a society which seeks to offer equal economic opportunity. While some proponents of this view favor use of these taxes to confiscate wealth transfers in excess of some stipulated amount, most would be content with an estate and gift tax system which served more effectively to damp down wealth accumulations. In either case, it is maintained that an estate tax which yielded only $1.6 billion in revenue on gross estates totaling $14.6 billion in 1961 can hardly be said to be a significant deterrent to the building up and maintaining of family fortunes. Even in the case of gross estates of $10 million or more reported on returns filed in 1961, it is pointed out, the estate tax claimed only 22 percent of the reported total gross estates.

Moreover, it is argued that no other form of taxation is less likely to distort economic relationships than estate and gift taxes. It is contended, for example, that these taxes have little if any tendency to influence individuals to substitute leisure for productive effort. Nor do these taxes interfere with choices between types of consumer goods or methods of production, as selective excises may do. Furthermore, these taxes do not reduce consumption or savings out of current income.

Finally, it is argued that, for equity reasons, estate and gift taxes are necessary supplements to income taxes, insuring that income which, for one reason or another, cannot be brought into the income tax base does not entirely escape taxation. Gift taxes are designed to limit avoidance with respect to income as well as estate taxes.

Opponents of the Federal estate and gift taxes contend that their small revenue yield is a reflection of the basic deficiency of these taxes as revenue sources. It is contended that these taxes cannot be designed to be important continuing sources of revenue, since the more effectively they apply to property transfers the greater is the likelihood that future property transfers will be of a diminished magnitude. This is particularly true, it is claimed, under the present steeply graduated individual income tax rates which tend to prevent heirs and donees from recouping the reduction in an estate effected by estate and gift taxation. In the same context, it is claimed that the very heavy level of income taxation since the early 1940's, coupled with the high rates of estate and gift taxes, are responsible, to some extent, for the failure of estate and gift taxes to retain an important revenue role.

Opponents of estate and gift taxation, in urging their elimination from the Federal revenue system, point to a number of adverse consequences of these taxes on property management and disposition. The necessity for making provision for the payment of these taxes, it is said, sets up pressure for maintaining a higher degree of liquidity in personal investment portfolios than would be dictated by nontax considerations.

This problem of providing for estate tax and gift tax payment is said to be particularly acute in the case of family businesses, in which a considerable proportion of the gross estate may constitute business property. In such cases, it is alleged, estate tax considerations may often lead to the liquidation of assets to the immediate detriment of the business and to its continuing successful operation in the hands of the donees and heirs. The breakup of family enterprises effected by the tax, it is argued, can hardly be viewed as serving any imperative social objective. Through time, moreover, it may be expected to have adverse consequences for both income tax and estate tax and gift tax revenues.

These considerations were responsible, to a large extent, for the provision in the Technical Amendments Act of 1958 of the 10-year installment payment privilege where the estate consists largely of an interest in a closely held business. This provision is expected by many to ease payment problems considerably. Others point out, however, that these provisions may cause grave difficulties if the family business suffers severe reverses while fixed annual estate tax payments remain to be met.

By the same token, the estate tax is said to be an important factor contributing to the absorption of relatively small business units, by purchase or merger, into large firms. The type of case cited in this connection is that of a relatively small company whose stock is closely held in a family so that virtually no market exists to establish the value of the holdings. Under these circumstances, uncertainty about the Internal Revenue Service's valuation of the business assets and difficulties in liquidating assets to meet the estate tax liability, it is argued, may incline the individual to accept an offer for the purchase of his business or its merger with another company through an exchange of stock, particularly when the acquiring company's stock enjoys a good market.

On the other hand, it is contended that this effect is in fact rarely observed. In the first place, it is argued, even those estates which consist primarily of business assets are seldom so illiquid that large-scale sale of assets is necessary to meet tax liability. Secondly, it is pointed out that in the infrequent cases in which liquidity is a problem, the extension of time for paying the estate tax and, since 1958, the availability of the installment payment privilege permitted under the law greatly reduce the likelihood that the estate will have to make forced sales of the business assets at a serious financial loss. In addition, the law permits the tax free redemption of stock in closely held companies for the payment of estate tax liabilities, thereby mitigating pressure for liquidation of a business.[25] Moreover, the individual in these circumstances can and frequently does provide for the tax-free transfer of at least a substantial part of his interests in the closely held business to members of his family during his lifetime, taking advantage of the annual exclusions and specific exemption in the gift tax law.

While proposals for the elimination of estate and gift taxes generally emanate from those opposed to taxes on wealth transfers, one proposal for eliminating estate and gift taxes calls for effectively increasing the tax on wealth transfers by requiring that they be taxed as income to the recipient in the year transferred.[26]

B. THE MARITAL DEDUCTION

Since it was introduced into the law by the Revenue Act of 1948, the marital deduction in the estate and gift taxes has been the subject of considerable controversy. Those who favor the deduction contend that it is the only feasible way of equalizing the treatment of transfers in noncommunity property States as compared with community property jurisdictions. The method provided in the 1942 law, it is argued, was not practical because it required determination of the

[25] Sec. 303.
[26] Henry C. Simons, "Personal Income Taxation," pp. 125–147.

spouse to which the transferred property was economically attributable.

Moreover, the marital deduction is defended in principle apart from its use as a means of equalizing tax treatment between community and noncommunity property States. The estate tax and gift tax laws, it is argued, should recognize the common interest of a married couple in the family's fortune, and should defer the imposition of the tax until both man and wife have died and the estate is transferred to a succeeding generation.

Some students of death and gift taxation have urged that the marital deduction be modified to permit the tax-free transfer of any and all property between spouses at the time of death. This proposal is based on the assertion that such transfers would not lessen the tax on an estate when it passes between generations. Moreover, it recognizes that the death of the family breadwinner is often not a propitious time for imposing a tax on the family wealth. It is pointed out, however, that while this provision would permit tax postponement on more than 50 percent of the gross estate of a decedent with a surviving spouse, this effect would be offset by the fact that, because of progressive tax rates, the final overall estate tax liability might be greater if more or less than 50 percent were so transferred.

It has also been proposed that a deduction be permitted based on the portion of the estate which passes to the decedent's children. The latter proposal would further "personalize" the tax by taking into account the number of heirs and their relation to the deceased as well as the size of the total estate. It would do so, however, without transforming the estate tax into an inheritance tax; that is, into a tax on the shares of the estate received by the individual heirs. The proposal would simply add another deduction to the present law.

Critics argue that the marital deduction, whatever its merit in principle, in fact is primarily an avoidance device the value of which increases with the size of the estate. It is contended that even if the principle of deferring the tax on transfers between husband and wife until the property is transferred to their heirs is accepted, the present marital deduction goes beyond this and permits not merely deferral but in many cases a lower tax than if the property were transferred directly to the heirs. This results from the fact that the portion of the estate left to the surviving spouse and covered by the marital deduction is not taxed at the time of the first decedent's death, but is separately taxed and at a lower tax rate (because of graduation in the rate structure) when transferred to the subsequent heirs. For example, if an individual left half of a $4 million net estate to his wife and the other half to their children, the tax at his death would be $753,200 and at her death, a like amount, or a combined tax of $1,506,400. If, on the other hand, the full $4 million had been transferred by the individual directly to the children the tax would have been $1,838,200.

To avoid this reduction but still permit deferral of tax, some propose that the amount previously allowed as a marital deduction be brought back into the tax base at the time of the surviving spouse's death. In the example given above, the taxable estate at the time of the wife's death would be regarded as $4 million, resulting in a tax of $1,838,200, against which a credit would be allowed for the $753,200 paid at the time of the husband's death.

Proponents of this method of treating transfers between spouses recognize that it would offer a strong inducement for leaving substantial amounts to the surviving spouse rather than directly to the heirs of the succeeding generation by virtue of the interest which might be accumulated on the deferred tax. They contend that this consideration is minor compared with the improvement in the use of the marital deduction as a means of confining the estate tax to a levy on transfers to the succeeding generation. Moreover, it is argued that this treatment of transfers between spouses, if applied to estates in community property jurisdictions, would provide the desired equalization.

Others urge the outright elimination of the marital deduction and the restoration of the 1942 act treatment of transfers between spouses in community property States. They contend that the cumulative treatment of transfers between spouses, described above, would be inequitable in a substantial number of cases in which the wealth of husbands and wives was separately accumulated or inherited. The estate tax, they argue, should be levied on the property which, economically speaking, belonged to the decedent, without resort to the legal fictions of community property.

C. INTEGRATION OF ESTATE AND GIFT TAXES

One of the major criticisms of the present estate tax and gift tax system is that it discriminates against transfers made at death by reason of the lower gift tax rates and the annual exclusion allowed under the gift tax in addition to the specific exemption. It is argued that the estate of an individual who found it impossible to transfer substantial amounts of property during his lifetime should not be more heavily burdened at his death than that of an individual whose property holdings offered no substantial barriers to transfers by gift.

To overcome this discrimination, the Secretary of the Treasury, in connection with the Revenue Act of 1950, proposed an integrated transfer tax. [27] The basic features of this proposal called for the cumulation of gifts during life, as under the present law, with transfers at death regarded as the final "gift" and therefore cumulated with the gifts previously made by the taxpayer. In lieu of separate exemptions for estate and gift taxes, the proposal would have provided a single $45,000 exemption, of which $15,000 would be available for transfers during life. Any unused portion of the $15,000, however, would be available at death, as well as the portion specifically reserved for final transfers.

In his testimony, the Secretary maintained that the present dual transfer tax defeats the purpose of the estate tax by permitting annual or periodic transfers by gift of relatively small amounts of property, subject therefore to lower marginal rates of tax under the gift tax. He also pointed out that by virtue of the 1948 act provision, the effective annual gift tax exclusion and specific exemption and the estate tax exemption were increased to $6,000, $60,000, and $120,000, respectively. The result of these revisions, he maintained, was a substantial increase in the amount of property that might be transferred tax free.

[27] Cf. statement of Secretary Snyder before the Committee on Ways and Means in its hearings on the revenue revision of 1950, 81st Cong., 2d sess., vol. 1, pp. 22–26, and accompanying exhibit 5, pp. 75–89.

It has also been pointed out that estate tax burdens are computed on the basis of a capital sum which includes the money which will be used to pay the tax. The gift tax, however, is based only on the amount actually transferred. Even if estate and gift tax rates were equal, the gift tax liability would be lower than the estate tax liability on any given taxable wealth transfer.

It has also been argued that integration of the estate and gift taxes would eliminate the problem of treating gifts made in contemplation of death. Prior to the Revenue Act of 1950, the problem of determining whether a gift was made in contemplation of death to avoid the higher estate tax rates was an exceedingly difficult one which often gave rise to litigation. Under the 1950 act, gifts made more than 3 years before death are not subject to the estate tax. While this simplifies the administration of the estate tax, it is argued that it does so at the expense of providing an attractive avoidance device.

In opposition to the proposal for an integrated transfer tax, it is contended that this proposal would defeat the major purpose of providing differentially lower rates in the gift tax; that is, to encourage transfers of property during life in relatively small amounts and to a relatively large number of donees. If the taxes were integrated, it is said, individuals would have little tax inducement to divest themselves of their estates before death. This might well result in greater wealth accumulations than occur under the present circumstances.

With respect to the problem of gifts in contemplation of death, opponents of an integrated transfer tax maintain that the motives of the taxpayer who transfers property during his lifetime are irrelevant. The differential between estate tax and gift tax rates, it is contended, serves to encourage such transfers, in itself a desirable objective.

D. LIFE ESTATES

Some critics of present law regard as one of its major deficiencies the failure to treat the termination of an interest in a life estate as a taxable transfer.[28] In his 1950 proposals, the Secretary of the Treasury illustrated the use of life estates as a means of avoiding estate and gift tax for at least one generation of transferees. He pointed out that if property is left outright to a child, it may become taxable in his estate upon his death. This may be avoided under the present law by placing the property in trust for the child's life, with the body of the trust to go to, say, a grandchild upon the child's death. While the creation of the life estate is treated as a taxable transfer, the termination of the child's interest is not. Accordingly, it is contended, transfers covering at least one generation may be made free of tax. The Secretary referred to data provided by a special statistical analysis of estate tax returns filed in 1945 to show that about 45 percent of the property transferred by individuals with net estates exceeding $500,000 had been put in such trusts.[29] This analysis also showed that the beneficiaries of these transfers through trusts were generally the same—mainly lineal descendants and other close relatives—as the beneficiaries of outright transfers. To block this type of estate tax avoidance, it is proposed that the termination of life interests in estates be treated as taxable transfers. Proponents contend that

[28] See, for example, Dan Throop Smith, op. cit., pp. 288-290.
[29] Secretary Snyder, hearings on the revenue revision of 1950, p. 23.

while there are limitations which may apply to the control over the corpus of the estate by the individual with a life interest therein, such an interest itself is a property, the rights in which may be sold or exchanged. The transfer at the time of death of an interest in a life estate, therefore, differs in no material way from the transfer of any other property which is now subject to the estate tax.

This recommendation for treating the termination of a life interest in an estate as a taxable transfer is opposed as lacking proper legal basis. The individual enjoying such an interest, it is maintained, does not own the property to which the interest attaches. Including such property in his estate upon the termination of his interest, therefore, would involve taxing him with respect to the transfer of property over which he had no control and none of the incidents of ownership required by the general statutory provisions.

Moreover, it is contended that this treatment would, in many cases, serve to diminish the principal of the estate before it was in fact finally transferred. The estate therefore would be diminished not only by the tax but also by the interest on its advance collection.

Finally, it has been pointed out that such treatment would require complex implementing regulations and would seriously interfere with property dispositions. It has been pointed out, for example, that such treatment might induce fathers to leave property to their grandsons and not their sons.

E. LIFE INSURANCE

Criticism has been directed against the provision of the 1954 Revenue Code which eliminates the premium-payment test for determining whether life insurance proceeds are to be included in the decedent's gross estate. Those opposed to this provision point out that the 1942 Revenue Act had specifically provided for the inclusion of life insurance proceeds when it was discovered that wealthy individuals were increasingly converting property into insurance policies which were previously omitted from the definition of a taxable estate. The 1942 act, it is contended, recognized that life insurance, by its very nature, is a testamentary disposition of the decedent's property, and therefore properly includible in his gross estate.

On the other hand, the report of the Ways and Means Committee on the 1954 provision pointed out that no other property except life insurance proceeds—

> is subject to estate tax where the decedent initially purchased it and then long before his death gave away all rights to the property.[30]

According to this view, the test as to who had purchased the insurance policy is not appropriate in determining whether the decedent owned it at the time of his death.

F. DEDUCTIONS FOR CHARITABLE CONTRIBUTIONS

The objective of providing a deduction for contributions from an estate to charitable, religious, and similar organizations is widely agreed to be a worthy one. It has been suggested, however, that some limitation be imposed on the deductibility of these contributions in order to check their use as a means of avoiding estate or gift tax

[30] H. Rept. 1337, 83d Cong., 2d sess., p. 91.

liability while leaving the donated property substantially under the control of members of the decedent's family. In this connection, reference is made to arrangements whereby a charitable trust is set up to which the preferred and nonvoting common stock holdings of a family business are donated as deductible charitable contributions. Small but controlling amounts of voting common stock are transferred to the surviving members of the family, enabling them to retain control of the business property through a largely or completely tax-free transfer. Moreover, that portion of the business income claimed by the trust is exempt from the income tax. It is argued that the use of charitable trusts for such purposes is not embraced by the objective of encouraging donations to tax-exempt organizations.

On the other hand, it is contended that little, if any, use has been made of charitable trusts for avoidance of estate and gift tax liability. Where these arrangements have been made, it is pointed out, trustees have generally been chosen who represent the public interest in the type of activities for which the trust was created. To limit the deductibility of charitable contributions, it is argued, would tend to impair one of the Nation's most important financial sources for the research upon which continuing technological progress depends as well as the support for a wide range of cultural and charitable activities.

G. INHERITANCE TAXES

It has been suggested that consideration be given to converting the Federal estate tax to an inheritance tax.[31] Support for this proposal is based on the contention that the burden of a tax on the transfer of wealth following death is borne by the decedent's heirs. It is unfair, it is argued, not to take into consideration the number of shares into which the estate will be divided. An inheritance tax relates the tax burden to the bequests received by the individual heirs. This approach would, it is contended, encourage a wider distribution of large fortunes since the size of the overall tax burden would be inversely related to the number of distributive shares. Furthermore, while an inheritance tax poses some difficult administrative problems, the advantage of simplicity under the estate tax has been dissipated as a consequence of present high tax rates and special provisions.

Those who favor the estate tax approach argue that it effectively conforms to the social objective of death taxation by taxing aggregate accumulations of wealth in a graduated fashion. An inheritance tax would impose varying burdens on equivalent fortunes merely because of variations in the number of designated heirs. Furthermore, in some cases the distributions would be to members of the same family and would not represent a real dilution of the wealth transferred. An inheritance tax would be difficult to administer, particularly when there were trust instruments involved. Finally, it is pointed out that the graduated estate tax is desirable as long as unrealized capital gains transferred at death are not subject to income tax.

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[31] See, for example Dan Throop Smith, op. cit., pp. 294-296.

CHAPTER 11

EMPLOYMENT TAXES

I. Present Law

Federal employment taxes were first imposed in the mid-1930's to finance the various social insurance programs introduced at that time. These programs are (1) old-age, survivors, and disability insurance (OASDI), which provides retirement and, since 1957, disability benefits for covered workers and their dependents and death benefits for their widows and dependent children; (2) unemployment insurance, a Federal-State program subject to certain broad Federal standards; and (3) similar but separate programs for railroad employees.

Revenues from these taxes have grown quite rapidly since their introduction in 1937. In the fiscal year 1963, employment tax receipts amounted to almost $20 billion as compared to receipts of $1.2 billion in fiscal 1938.

A. OLD-AGE, SURVIVORS, AND DISABILITY INSURANCE TAXES

The old-age, survivors, and disability insurance program is financed by social security taxes paid by employees [1] and, beginning in 1951, self-employed persons [2] and by taxes paid by employers [3] with respect to the wages paid to each employee. The employee and employer tax rates are identical. The tax on the self-employed is levied at a rate equal to 1.5 times the corresponding rate for employees, except that the rates for the self-employed are rounded to the nearest one-tenth of 1 percent.

The current rate of tax on employee and employer is 3⅝ percent, and on a self-employed individual 5.4 percent, applicable to the first $4,800 of covered annual earnings. Under the original legislation in 1935, the tax was 1 percent each for employer and employee with respect to covered payrolls up to $3,000 per employee per year. Although the legislation provided a schedule of rate increases for subsequent years, these increases were deferred through 1949 by amendments to the act. Since 1949, however, both the rate of tax and the amount of covered earnings to which it applies have been increased. A new schedule of rate increases was enacted in 1961, providing for rate step-ups in 1962, 1963, 1966, and 1968, when a rate of 4⅝ percent would be attained for employers and employees, and a rate of 6.9 percent for self-employed persons. The tax base to which these rates would be applied is $4,800. The following table shows the tax rates and the applicable amount of earnings in the years since 1937 and projected to 1968 under the 1961 legislation. At the time of this writing further amendments affecting the tax rate and tax base were under consideration by the Congress.

[1] Sec. 3101.
[2] Sec. 1401.
[3] Sec. 3111.

TABLE 29.—*OASDI tax rates and maximum amount of taxable compensation, 1937–68* [1]

Year	Rate for employee and employer, each	Rate for self-employed	Maximum annual earnings subject to tax
	(Percent)	*(Percent)*	
1937–49	1	----------	$3,000
1950	1½	----------	3,000
1951–53	1½	2¼	3,600
1954	2	3	3,600
1955–56	2	3	4,200
1957–58	[2] 2¼	[3] 3⅜	4,200
1959	2½	3¾	4,800
1960–61	3	4½	4,800
1962	3⅛	4.7	4,800
1963–65	3⅝	5.4	4,800
1966–67	4⅛	6.2	4,800
1968 and following	4⅝	6.9	4,800

[1] Effect of Social Security Act Amendments proposed in 1964 not included.
[2] Includes ¼ percentage point to finance disability insurance in 1957 and subsequent years.
[3] Includes ⅜ percentage point to finance disability insurance in 1957 and subsequent years.

Since 1957, the tax rates for employers and employees have included one-fourth of 1 percent on the first $4,800 of earnings to provide benefits to insured workers no longer able to work because of extended disability. The tax rate for this purpose is three-eighths of 1 percent on self-employed persons.

The original legislation exempted from coverage under the old-age and survivors insurance program, and therefore from tax, various categories of employment such as agricultural labor, domestic service in private homes, casual labor, services performed for religious, charitable, scientific, literary, and educational organizations, services performed for the United States, a State, or its political subdivisions, and services performed by officers and crews of certain vessels. Successively since 1950 these exemptions have been eliminated as coverage under the program has been extended to substantially all people in paid employment. The major types of employment and earnings not now covered are those of self-employed doctors of medicine, Federal civilian employees, self-employed persons whose income from self-employment is under $400 a year, and domestic and farm workers when they earn less than a specified amount with a single employer.

Benefits are payable to people who have worked a sufficient number of quarters to be insured under the program and to their dependents and their survivors. Monthly old-age insurance benefits are payable, beginning at age 62, to a retired insured worker. Benefits are also payable to the wife of a retired worker if she is either 62 or has a child in her care who is entitled to child's benefits. Child's benefits are payable to a retired worker's unmarried children under the age of 18 or, regardless of age, to any of his children who were permanently and totally disabled before age 18. Benefits are also payable to a dependent husband who has reached the age of 62.

Survivor benefits are payable to the widow of an insured worker if she has reached the age of 62 or has a child entitled to benefits in her care; to unmarried children of such a worker under 18 or, if over 18, who were disabled before age 18; to his dependent parent aged 62 or more; and to a dependent widower aged 62 or more.

Full monthly benefits are payable in the case of widows, widowers, and dependent parents aged 62 or over but benefits to retired workers, wives, or dependent husbands who choose to receive them before age 65 are actuarially reduced on a permanent basis.

Disability insurance benefits are payable to a worker under age 65 who is unable to engage in any substantial gainful work because of a disability that can be expected to last for a long and indefinite period or result in death. Benefits for the dependents of a disabled worker are payable under the same conditions as for dependents of retired workers.

A lump-sum benefit equal to three times the workers monthly benefit amount but not to exceed $255 is also payable on the death of an insured worker.

The old-age insurance benefit amount is based on monthly average earnings. The benefit for each amount of average monthly earnings is set forth in the law. The average monthly earnings are arrived at by adding up a worker's total covered earnings over the number of years specified in the law (generally the years between 1951 and the age of 65, or 62 for women) and dividing by the number of months in those years. The 5 years in which earnings were lowest and periods of disability are, however, excluded from the calculations.

Primary benefit amounts (beginning at age 65 for an insured individual) range from $40 a month to $127. Benefits for dependents and survivors are based on a percentage of the benefit payable to the insured worker (50 percent in the case of a wife). A wife who is also insured on her own earnings may, in effect, draw the larger of her own benefit or the benefit due her as the wife of an insured worker.

Generally benefits are paid only to people under age 72 who do not have substantial earnings from work—those who have retired. If a person's annual earnings from either covered or noncovered work are not more than $1,200, all of his benefits for the year will be paid. If his earnings are more than $1,200 in a year, $1 in benefits is withheld for each $2 of earnings between $1,200 and $1,700, and for each $1 of earnings above $1,700. Benefits are payable, however, regardless of annual earnings, for any month in which the beneficiary neither renders substantial services in self-employment nor works for wages of more than $100. Benefits are paid to people age 72 and over regardless of earnings.

The old-age, survivors, and disability insurance program is financed on a self-supporting basis. The determination of tax rates has been guided by consideration of the revenue needed to meet projected retirement, disability, and survivors' benefits. The Congress has reviewed the schedule of tax rates whenever legislative changes affected prior estimates of program costs.

Two separate trust funds, the Federal old-age and survivors insurance trust fund and the Federal disability insurance trust fund, are maintained by the Treasury to meet the obligations of the program. Amounts equivalent to collections from the OASDI taxes are appropriated to these funds, and are invested in interest-bearing securities of the Federal Government.

On July 29, 1964, the House of Representatives passed H.R. 11865, a bill which would amend the Social Security Act with regard to the old age, survivors, and disability insurance program. The bill provides for a 5-percent increase in benefit payments for the 20 million persons presently receiving benefits and for increases of at least 5 percent in the payments to future beneficiaries. This would raise the minimum monthly primary benefit, prior to any required acturial reduction, for a worker now retired to $42 a month, and the maximum benefit to $133.40 a month. Increases in benefits would be accompanied by an increase in the maximum amount of annual covered earnings subject to tax and the enactment of a new schedule of tax rate increases. The earnings base would be increased from $4,800 to $5,400 beginning with 1965 and the rate of tax on covered wages for employers and employees would be increased from the present 3.625 percent to 3.8 percent in 1965, 4 percent in 1966, 4.5 percent in 1968, and finally to 4.8 percent in 1971. The tax rate for the self-employed would be increased to 5.7, 6, 6.8, and 7.2 percent in the respective years. The increase in the earnings base would have the effect of increasing benefit payments for many future retirees, establishing an eventual maximum primary benefit of $143.40 a month for a worker retiring at age 65 or later.

Other features of the bill include the provision of limited benefits for certain aged individuals who have some social security coverage, but not enough to meet the eligibility requirements of present law; the payment of child's insurance benefits at the ages of 18 to 21 if the child is a full-time student; and provision of benefits on an actuarially reduced basis to widows aged 60 and 61. The bill would extend social security coverage to self-employed physicians and interns and make such coverage available to policemen and firemen in the employ of State and local governments under certain conditions. The bill would also include cash tips received by employees in the social security wage base.

On August 20, 1964, the Committee on Finance of the Senate favorably reported on H.R. 11865, with certain amendments to the bill as passed by the House. While the committee accepted the major provisions of the House-approved measure, it deleted the provisions extending coverage to self-employed physicians, interns, policemen, and firemen, and the provision which would include cash tips in the social security wage base. The committee added to the bill sections preserving the existing relationship between social security and railroad retirement benefits and tax rates and protecting certain payments made to veterans. At the time of this writing further action on H.R. 11865 is pending.

B. UNEMPLOYMENT INSURANCE TAXES

1. *The basic program*

The unemployment insurance program is a Federal-State program, involving both Federal and State laws and taxes. Both the Federal Government and the States impose payroll taxes on employers. The program's framework was established by the provisions of titles III and IX of the original Social Security Act, which imposed a Federal excise tax on certain employers, and provided that if a State unemployment insurance law and administration met certain requirements, the Federal Government would pay 100 percent of the law's administrative costs, and would permit employers to credit State taxes against the major portion of Federal taxes. All States have enacted unemployment insurance laws meeting the Federal requirements. Within the Federal requirements provided by this framework, States have individually determined coverage, tax rates, benefits, eligibility, disqualification provisions, and administrative procedures.

The Federal tax, set forth in chapter 23 of the Internal Revenue Code, is a uniform national payroll tax of 3.1 percent, applicable to the first $3,000 of annual wages paid each employee, and imposed on employers having four or more employees on at least 1 day in each of 20 weeks in the calendar year. In 1962, this rate was temporarily raised to 3.5 percent and in 1963 to 3.35 percent. As a result of the credit for State taxes, however, most employers actually pay only a small part of this tax to the Federal Government.

An estimated monthly average of 47.7 million wage earners were covered by unemployment insurance during 1962. Approximately 14.6 million wage earners were not covered by a program, including 1.8 million employees of small firms, 1.6 million employees of non-profit institutions, 6.4 million State and local government employees, 2.6 million domestic workers, 1.9 million farm and agricultural processing workers, and 0.3 million workers in miscellaneous employment.

Since 1955, unemployment insurance coverage has been provided by Federal law for civilian employees of the Federal Government, with benefits payable under the terms and conditions of the law in the State in which the employee is stationed. The States act as agents of the Federal Government for this program and are paid by the Federal Government for the benefit and administrative costs of the program. Ex-servicemen are covered under a similar program administered by the States as agents and financed by the Federal Government.

Prior to January 1, 1961, the Federal unemployment tax rate was 3 percent. Employers subject to the 3-percent tax were allowed a credit not in excess of 90 percent of Federal tax liability for unemployment compensation taxes paid to States with approved laws, as certified by the Secretary of Labor to the Secretary of the Treasury. In effect, therefore, the Federal tax payable was 0.3 percent of taxable payrolls; the remaining 2.7 percent was the credit for State taxes. Effective January 1, 1961, the Federal unemployment tax rate became 3.1 percent. The additional 0.1 percent, earmarked for the Federal share of the tax, was required to meet rising State and Federal administrative costs and to provide additional moneys for the "loan fund" which finances advances to States whose unemployment reserves have been depleted. State tax credits are computed, as before, on the basis of a Federal tax rate of 3 percent.

Employers may pay less than 2.7 percent of federally covered payrolls to the States and still receive the full credit against Federal tax if their State determines an employer's contribution rate according to his unemployment risk as determined by a period of at least 3 years of experience. Federal legislation enacted in 1954 authorized the States to apply their experience-rating provisions to newly covered employers after 1 year of experience instead of 3 years. The Secretary of Labor certifies annually the States where reduced rates of contribution are allowable. Experience-rating systems are said to allocate the costs of the benefits among employers in accordance with the frequency with which they lay off workers. They also encourage employers to adopt personnel practices which minimize the chance of frequent employee layoffs. Such provisions are now in force in all the States and the District of Columbia. State tax rates therefore usually average below 2.7 percent of covered payrolls.

No Federal tax is imposed on employees. In three States, however, employer taxes are supplemented by employee taxes. In the early days of the program seven other States imposed employee taxes but these have been discontinued.

Taxes collected by the States are deposited in the unemployment trust fund in the U.S. Treasury to the account of the individual States. The States draw against these accounts such amounts as they require for benefit payments.

The portion of the tax collected by the Federal Government is credited to the employment security administration account in the unemployment trust fund. Administrative costs of the entire employment security program, both State and Federal, are paid from this account in accordance with congressional appropriations. Receipts in excess of administrative expenses are transferred each fiscal year first to the Federal unemployment account, a "loan fund" for making advances to States with depleted reserves. A maximum balance of $550 million or 0.4 percent of taxable payrolls, whichever is greater, is prescribed for the loan fund. When this fund has the maximum statutory balance, excess receipts are credited to the employment security administration account, until the net year-end balance in that account reaches a maximum of $250 million. Any remaining excess is distributed to the trust fund accounts of the individual States in proportion to their respective taxable payrolls. Distributions to the States were made in 1956, 1957, and 1958; additional distributions are not likely in the foreseeable future.

2. Temporary supplementary benefit acts of 1958 and 1961

The Temporary Unemployment Compensation Act of 1958 (TUC) provided, subject to agreements with individual States, Federal payments to States to finance temporary unemployment compensation to individuals who had exhausted their benefit rights under existing State programs between June 30, 1957, and April 1, 1959. This emergency program was subsequently extended to June 30, 1959.

This program was to be financed by a deferred Federal unemployment tax on employers in States which participated in the program unless the amounts made available to such States were otherwise restored.

Of the 17 States which participated in this program, 2 have made full restoration of the funds made available to them. Restorations must still be made with respect to the remaining 15 States. The restorations may be made from a number of State sources of funds, including the transfer of funds from the State's account in the Federal unemployment trust fund, although restoration of certain administrative costs cannot be made from the latter account. Unless the full balance or a specified installment thereof is restored by November 10 of each taxable year, however, the Federal unemployment tax is increased for employers in the State who are subject to the Federal Unemployment Tax Act. The increase is effected by reducing the 2.7 percent allowable credit which may be taken with respect to amounts paid the States. The additional Federal taxes amounted to 0.15 percent of wages subject to the Federal tax and paid during 1963. Employers in nine States were required to pay tax at the additional rate for 1963. As a rule, payments were actually made in the early months of 1964. In 1964 and later years the additional tax rate will be 0.3 percentage points unless the States concerned meet their repayment obligations in other ways.

Three of the States which participated in the TUC program, Alaska, Michigan, and Pennsylvania, also received advances from the Federal unemployment account (loan fund) to finance compensation payments to the unemployed. Repayments of such advances may be made by these States from reserve or other funds, or, if not so repaid, by employers in the State through the payment of higher Federal taxes. Additional Federal taxes for this purpose amount to 0.15 percent on federally subject wages paid in each of the taxable years 1963–67. For 1968 and subsequent years, the additional tax will increase by 0.15 percentage points per year (0.30, 0.45, 0.60, etc.) until the advance is repaid in full. As in the case of TUC advances, the increased tax will take the form of a reduction in the allowable credit for State unemployment taxes.

The Temporary Extended Unemployment Compensation Act of 1961 (TEC) provided for up to 13 weeks of additional benefits to unemployed workers who had exhausted their benefits under regular State programs. Former servicemen and Federal employees were also eligible, as they were under the 1958 TUC Act. Payments were only authorized, however, to persons who had exhausted their benefit rights after June 30, 1960, and before April 1, 1962, with respect to periods of unemployment which ended before July 1, 1962. This program, in which all States participated, was financed through a temporary increase of 0.4 percentage points in the Federal unemployment tax for the year 1962 and an increase of 0.25 percentage points in the rate for 1963. These additional Federal taxes, which were added to the regular overall rate of 3.1 percent, financed the benefits paid under this program.

Effective Federal unemployment tax rates vary from State to State because of differentials imposed to restore advances made in the 1958–59 period. In 1963, for example, the general rate of 0.65 percent (3.35 less 2.7) was further increased in nine States to 0.8 percent as a result of taxes levied to restore advances made under the TUC program. In Alaska and Michigan, the overall rate was increased still further to 0.95 percent as a result of the tax levied to restore funds borrowed from the Federal unemployment account. In 1964, while the basic tax rate is 3.1 percent, the portion which cannot be offset by a credit for State taxes may remain as high as 0.55 percent of taxable payrolls in those States which have not repaid the full amount of their TUC advances and as high as 0.7 percent in Alaska, Michigan, or Pennsylvania if these States do not by other means also repay the specified amount of funds advanced to them from the Federal unemployment account.

C. PROGRAMS FOR EMPLOYEES IN THE RAILROAD INDUSTRY

1. *Railroad retirement taxes*

The retirement and survivor benefit program for railroad employees is operated apart from the OASDI. It is supported by a payroll tax on employees and an excise tax on employers in the railroad industry,[4] except for contributions by the Federal Government with respect to military service performed by railroad employees and credited under

[4] Ch. 22.

the Railroad Retirement Act. The current tax rate is 7¼ percent on employers and employees. The combined rate of 14½ percent is payable with respect to the first $450 of monthly wages. The maximum limitation on taxable wages was $400 per month prior to November 1, 1963. The following table shows the tax rates and applicable earnings since 1937 and projected to 1968:

TABLE 30.—*Railroad retirement tax rates and maximum amount of taxable compensation, 1937–68*

Year	Rate for employee and employer, each [1]	Maximum monthly earnings subject to tax
	Percent	
1937–39	2¾	$300
1940–42	3	300
1943–45	3¼	300
1946	3½	300
1947–48	5¾	300
1949–51	6	300
1952 through May 31, 1959	6¼	[2] 300 [3] 350
June 1, 1959, through 1961	6¾	400
1962–64	7¼	[4] 400 [5] 450
1965	8⅛	450
1966–67	8⅝	450
1968 and following	9⅛	450

[1] Rate increases after 1964 will be effective only if social security rate increases scheduled after 1964 become effective. Table does not reflect amendments to the Social Security Act discussed in 1964.
[2] Prior to July 1, 1954.
[3] After June 30, 1954.
[4] Prior to Nov. 1, 1963.
[5] After Oct. 31, 1963.

The employee tax, deducted by the employer from wages, and the employer tax are collected by the Internal Revenue Service as Federal revenue. However, a railroad retirement account is established in the Treasury, to which annual appropriations are made. Funds in the account not needed immediately for benefit payments are invested in Federal obligations or Federal guaranteed obligations with yields at least equal to the average market yield borne by all marketable interest-bearing obligations of the United States then forming a part of the public debt that are not due or callable until after the expiration of 3 years, but the yields shall in no event be less than 3 percent.

2. *Railroad unemployment insurance taxes*

Unemployment insurance for railroad workers is a Federal insurance program outside the Federal-State unemployment insurance system, under which cash benefits are payable to railroad workers in the event of their unemployment because of lack of work or because of sickness or maternity. The program is supported by a levy (contribution) imposed on employers with respect to wages paid to their employees (not in excess of $400 per month per employee). The contribution rate during any calendar year is now determined on the basis of a sliding scale ranging from 1½ to 4 percent, depending upon the combined balance to the credit of the railroad unemployment insurance account and the railroad unemployment administration fund at the close of business on September 30 of the preceding year. The schedule effective since January 1, 1964, is as follows:

	Contribution rate (percent)
If the combined balance to the credit of the account and fund is—	
$450,000,000 or more	1½
$400,000,000 to $450,000,000	2
$350,000,000 to $400,000,000	2½
$300,000,000 to $350,000,000	3
Less than $300,000,000	4

Prior to 1948 the rate was fixed at 3 percent. Since 1948 the contribution rate has been as follows:

	Percent
1948–55	½
1956	1½
1957	2
1958	2½
Jan. 1–May 31, 1959	3
June 1, 1959–Dec. 31, 1961	3¾
1962–63	[1] 4
1964	4

[1] Consisting of the maximum rate of 3¾ percent under the schedule then in effect plus ¼ percent added by the Temporary Extended Railroad Unemployment Insurance Benefits Act of 1961.

The contributions for the railroad unemployment insurance program are collected by the Railroad Retirement Board and deposited with the U.S. Treasury to the railroad unemployment insurance account (except for 0.25 percent of taxable compensation which is credited to the railroad insurance administration fund to cover expenses of administration).

A temporary program of extended unemployment benefits was in effect for unemployed railroad workers who had exhausted their unemployment benefits after June 30, 1957, and before April 1, 1959. The contribution rate was not increased specifically for the financing of this program. However, as a result of the temporary program of extended benefits, the combined balance to the credit of the railroad unemployment insurance account and the railroad unemployment administration fund dropped below $300 million, thus bringing the employer's contribution for 1960 up to the then maximum rate of 3¾ percent. In addition, it became necessary for the Railroad Retirement Board to request the Secretary of the Treasury for a temporary transfer of funds from the railroad retirement account to the railroad unemployment insurance account, as provided by law.

The Temporary Extended Railroad Unemployment Insurance Benefits Act of 1961 provided temporary extended benefits to unemployed railroad workers who exhausted their benefit rights after June 30, 1960, and before April 1, 1962. This program was financed by advances from the Treasury to the railroad unemployment insurance account. In order to provide additional revenue to repay the advances from the Treasury, the employer contribution rate was raised by one-fourth of 1 percent on taxable wages paid in 1962 and 1963. The advances have been repaid in full.

II. Issues

Many of the basic issues concerning Federal employment taxes stem from fundamental disagreements about the role of the Federal Government in providing retirement, survivors, and disability benefits and unemployment insurance for employees. Such issues are more appropriately discussed in a broader context than tax policy alone. With respect to these taxes as a component of the Federal revenue system, however, a longstanding and basic issue concerns the use of payroll taxes as opposed to general revenues to finance social security programs.

Opponents of employment taxes have based their arguments on (1) the alleged lack of any close relationship between tax liabilities and benefits; (2) the distribution by income levels of the burden of these taxes; and (3) the limitations imposed by these taxes on effective use of tax policy for economic stabilization purposes.

A. RELATIONSHIP OF BENEFITS TO TAX LIABILITIES

Social security programs, it is argued, do not need to have the actuarial characteristics of private insurance systems, and, on the whole, do not possess such characteristics. Thus it is pointed out that the fiscal soundness of these Federal programs does not require the accumulation of reserve funds sufficient at any given time to meet all obligations regarding benefits, both present and future, to all the participants in the programs. The credit of the Federal Government insures that these programs will have sufficient funds to meet liabilities as they fall due. Moreover, it is contended that in a broad sense the social security program provides benefits to society at large which are at least as important as the insurance protection it provides individuals.

Unemployment compensation benefits, for example, represent a major line of defense against the cumulation of recessionary pressures and thus limit losses of output and income which would otherwise be borne by the entire economy, not merely by the unemployed. Similarly, retirement and survivors benefits under the OASDI and railroad retirement plans, by bolstering the economic position of recipients, serve to enhance aggregate demand and thereby provide a stimulus for expanding economic activity. Viewing these programs in this light, it is argued, leads to the conclusion that they should be financed in the same manner as any other Government program which provides benefits to a large segment of the population. It is contended, therefore, that these funds should be financed from general revenues and not special, earmarked taxes.

A contrary view holds that, despite superficial differences in the actuarial characteristics of social security compared with private insurance, the public programs are nevertheless basically insurance systems. Apart from the provision of minimum benefit levels, for example, OASDI benefits are computed on the basis of past earnings, up to the maximum wage base, and thus are related to the amounts contributed by employer and employee. This relationship will become even closer in future years as more and more beneficiaries are covered throughout their entire employment careers. The justification for public rather than private insurance against the risks covered by social security, it is maintained, is the substantial economy provided by large-scale operation and the elimination of any barrier to labor mobility which might be erected if such a program were locally administered. This justification, it is argued, does not suggest that the immediate beneficiaries of the program should be subsidized by the rest of the economy. The fact that the economy as a whole derives some secondary benefits from social security is not relevant to the question of the proper means for financing benefit payments. Presumably the entire economy benefits from the fact that a substantial number of individuals and families carry fire and other hazards insurance on their property, yet these social benefits are not cited as an argument for charging the cost of such insurance to anyone other than the individual policyholders.

In this context, it is argued that the major improvement required in the social security system is to strengthen its actuarial basis. Under the present arrangements, it is maintained, payments received by a beneficiary are not sufficiently dependent on the contributions of the insured to protect the soundness of the fund over long periods of time. The more rigorous application of actuarial principles would make possible a more equitable system of contributions and benefits without jeopardizing the future adequacy of social security funds.

B. DISTRIBUTION OF EMPLOYMENT TAX BURDENS

In support of the view that the social security program should be financed from general revenues, it is argued that employment taxes have a regressive impact in terms of their distribution by income levels. This characteristic stems from the fact that these taxes apply to only a limited amount of an employee's wages, and an amount which begins with the first dollar of earnings in covered employment. Thus these taxes tend to offset the burden distribution effects of the individual income tax provided by exemptions and progressive tax rates. The employer's share, it is argued, is passed forward to consumers in higher prices or backward in lower wages to the employees whose wages and salaries are taxed. Thus in essential respects the incidence of the tax, it is contended, is the same as that of a general sales tax and serves to reduce the degree of overall progression in the tax system.

Moreover, it is argued that because payroll taxes increase the cost of hiring new employees in covered employments, they promote the substitution of capital for labor, i.e., automation, on the one hand, and tend to draw labor into noncovered employment on the other hand. Accordingly, these taxes tend to result in a shift in the distribution of national income away from labor services in taxed employments. This allocation is less efficient in the sense that it differs from the allocation which would be made in the absence of the tax. Covered employments, it is pointed out, embrace most skilled workers while noncovered employments include occupations where productivity is low. Furthermore, payroll taxes reduce the differential between the cost of hiring a new employee and placing an existing employee on overtime work. Payroll taxes, therefore, are said to be inconsistent with the achievement of the objectives of the Employment Act of 1946.

In answer to these arguments it is pointed out that the OASDI taxes are not taxes in the usual sense but rather contributions which form the basis for future tangible benefits. It is important in this sense that benefits and contributions be related. It is also pointed out that as a practical matter little improvement in the overall progression of the tax system could be expected from elimination of payroll taxes and a compensatory increase in other taxes to finance social security benefits. If not all, at least a substantial part of the over $14 billion of revenues now produced by Federal payroll taxes would have to come from the individual income tax. In view of the present structure of the tax, this would mean increasing income tax burdens primarily at the lower end of the tax scale. Accordingly, little net increase in the degree of progression would result.

Whereas the chief issue concerning the burden of employment taxes involves the distribution by income levels, a related problem concerns the distribution of tax liabilities among taxpayers with equivalent incomes. In this connection it has been pointed out that under the unemployment insurance program effective tax rates vary between States and between employers in the same State. Present tax rates are relatively low, but there is speculation that if increased in the future they may exert some influence on the allocation of resources.

On the one hand, not all employers are subject to unemployment taxes and not all are subject to both Federal and State taxes. For example, some State laws include more employers than the Federal law, which covers those employers with four persons or more in their employ during at least 1 day in each of 20 calendar weeks during a given year. On the other hand, Federal and State tax rates and State taxable income maximums vary from State to State. The effective Federal tax rate; that is, the 3.1 percent rate reduced by allowable credits for State taxes, varies as a result of advances made under the TUC program and advances from the Federal unemployment account. To restore these advances the credit allowed under the Federal law for State unemployment taxes is reduced below 2.7 percent of taxable wages for employers in certain States. Consequently, effective Federal tax rates on the first $3,000 of taxable wages varied from 0.65 to 0.95 percent in 1963. Wider variations in effective rates occur under State programs because of variations in the taxable wage base and the application of experience ratings. The extent of State-by-State variations in unemployment tax liabilities in 1963 is indicated in the following table:

TABLE 31.—*Federal and State unemployment insurance employer contribution rates, by States, 1963*

State	State unemployment insurance: Tax base, $3,000 except as shown	State unemployment insurance: Average tax rate as percent of total wages in covered employment [2]	Federal unemployment tax,[1] tax rates payable by employers on 1963 wages
Alabama		1.4	0.65
Alaska	$7,200	2.4	.95
Arizona		.9	.65
Arkansas		1.0	.65
California	3,800	2.0	.80
Colorado		.8	.65
Connecticut		1.2	.65
Delaware	3,600	1.3	.80
District of Columbia		.6	.65
Florida		.9	.65
Georgia		.9	.65
Hawaii	3,600	.9	.65
Idaho	3,600	1.5	.65
Illinois		1.1	.65
Indiana		.7	.80
Iowa		.5	.65
Kansas		.7	.65
Kentucky		1.3	.65
Louisiana		1.2	.65
Maine		1.6	.65
Maryland		1.9	.65
Massachusetts	3,600	1.6	.80
Michigan	[3] 3,600	1.7	.95
Minnesota		.8	.80
Mississippi		1.7	.65
Missouri		.9	.65
Montana		1.2	.65
Nebraska		.8	.65
Nevada	3,600	1.8	.65
New Hampshire		1.1	.65
New Jersey		1.4	.80
New Mexico		.9	.65
New York		1.8	.65
North Carolina		1.1	.65
North Dakota		1.6	.65
Ohio		1.1	.65
Oklahoma		1.2	.65
Oregon	3,800	1.9	.65
Pennsylvania		1.8	.65
Puerto Rico		2.3	.65
Rhode Island	3,600	1.9	.65
South Carolina		.9	.65
South Dakota		.8	.65
Tennessee	3,300	1.3	.65
Texas		.5	.65
Utah	[4] 4,200	1.2	.65
Vermont	[4] 3,600	1.2	.65
Virginia		.7	.65
Washington		1.5	.65
West Virginia	3,600	1.8	.80
Wisconsin		.9	.65
Wyoming		1.7	.65

[1] Portion of 3.35 percent tax on covered wages up to $3,000 a year which could not be offset by credit for State taxes paid.
[2] Estimated. Total wages include wages in excess of State tax base, but only in covered employment. Covered wages are not necessarily the same under State law as under Federal law.
[3] As of April 1963.
[4] As of January 1964.

Source: Department of Labor, Bureau of Employment Security.

It is pointed out that these variations are based upon the incidence of unemployment in a particular State. Employers, in effect, therefore, must assume part of the financial responsibility for unemployment and are provided an incentive to initiate procedures which will minimize employee layoffs. It is also pointed out, however, that higher unemployment tax rates in a State with chronic unemployment increase prospective costs for firms which might consider opening new facilities in the stricken areas. The extent of the differential cost is said to be relatively minor, however, and, in the case of the tax paid the Federal Government, transitional. Uniformity with respect to the tax paid the Federal Government will presumably be restored once TUC and loan fund advances have been fully restored.

C. EMPLOYMENT TAXES AND COUNTERCYCLICAL TAX POLICY

The present policy with respect to employment taxes, it is maintained, tends to limit the usefulness of the tax system for economic stabilization purposes. It is conceded that, all other things being equal, these taxes might contribute to the overall "built-in flexibility" of the Federal revenue system. With constant coverage, tax rates, and base for application of the taxes, revenues from employment taxes would increase with rising levels of economic activity and employment and fall under recession conditions. These revenue changes very likely would be less than proportionate to changes in total wages and salaries, however, since the tax rates do not apply to the full amount of wages or salaries of covered employees.

On the other hand, it is pointed out that a number of factors have significantly restricted the countercyclical flexibility of employment tax revenues. In the first place, increases in taxes to finance the retirement and survivors benefit programs are, in general, scheduled in advance of the time they take effect. Whether these increases in rates will coincide with high employment conditions and contribute to restraining inflationary pressures cannot, of course, be accurately predicted at the time the schedule is enacted.

For example, a one-half percentage point increase in the OASDI contribution rate became effective on January 1, 1954, in the midst of a recessionary period. This increase offset the reduction in individual income tax rates which took effect on the same date for a substantial number of individuals. For example, a married individual with two dependents whose income consisted entirely of wages and salaries had a net increase in taxes in 1954 if his total wages were less than $3,568. Similarly, the increase in tax rates associated with the adoption of the disability insurance program on January 1, 1957, coincided with a leveling off in economic activity and continued in force in 1958, a year in which economic activity declined sharply in the early months. Finally, the one-half percentage point increase that occurred in January 1961 came in the trough of a mild recession.

Secondly, it is contended that employment tax rates have been more directly influenced by the prospective condition of the funds to which these taxes are allocated than by prospective economic and employment conditions. Over the years, the scope of the social security program has been extended and benefits have been increased. Increasing demands for expenditures have resulted periodically in threats of a deficit in the funds which have led to increases in tax rates or in the amount of wages and salaries to which the rates apply. The expansion of benefits and the consequent increase in revenue requirements, however, have not been based directly on the general condition of the economy. Although an expansion of benefits even if associated with an increase in tax rates during a recession may have an expansionary effect overall, the extent of the stimulus to aggregate demand is less than it would be in the absence of the increase in employment taxes.

Similar pressures for increasing tax rates are experienced in State unemployment insurance programs. The inroads in State reserves resulting from extended and relatively high unemployment serve to increase the average tax rate paid by employers. For the United States as a whole, the average employer contribution rate under State unemployment insurance programs rose from 0.81 percent of total wages paid in covered employment in 1955 to 1.4 percent in 1963.

In answer to these arguments, it is pointed out that the present social security system makes a significant contribution to economic stability. While it might be desirable in some instances to time changes in payroll tax rates on the basis of stabilization criteria, these are not the only relevant criteria to be considered. The long-run condition and effectiveness of the social security programs, it is said, are more important standards against which to evaluate proposals for the revision of payroll taxes. Changes in benefits and coverage, it is contended, need not and should not be determined to any significant extent by economic stabilization requirements. Such changes generally involve tax adjustments as well. To the extent that such tax changes may involve destabilizing effects, these may be offset by changes in other elements of the revenue system.

CHAPTER 12

FEDERAL-STATE-LOCAL GOVERNMENT FISCAL RELATIONS[1]

I. Tax Overlapping

A. EXTENT OF TAX OVERLAPPING

The types of taxes levied by the Federal Government are also imposed by State and local jurisdictions. Taxes used concurrently by the Federal Government and other levels of government include individual and corporate income taxes, death and gift taxes, and excise taxes on motor vehicles, motor fuel, alcoholic beverages, tobacco products, amusements, and public utilities. Customs duties, however, are levied only by the Federal Government, and property, general sales, and motor vehicle license taxes are levied only by State and local jurisdictions, although Federal excise taxes are imposed on items included in the base for the general sales taxes levied by other jurisdictions.

The degree of tax overlapping is affected by a number of factors. The three levels of government tend to rely on different types of taxes for the bulk of their revenue. Thus the Federal Government, which accounts for two-thirds of all tax revenues, relies primarily on individual and corporate income taxes. The States derive more than half of their tax revenues from general sales and gross receipts taxes while local jurisdictions receive almost 90 percent of their tax revenue from property taxes.

With regard to particular types of taxes there is a considerable degree of jurisdictional specialization. The Federal Government collects the major share of all individual and corporate income tax revenues, death and gift taxes, and alcoholic beverage and tobacco taxes. The States receive the major share of general sales taxes, motor fuel taxes, and motor vehicle and operators license fees. Local jurisdictions account for more than 95 percent of property tax collections. Federal, State, and local tax collections in 1962 are shown in the following table:

[1] Much of this discussion is based on "Tax Overlapping in the United States, 1964," prepared by the staff of the Advisory Commission on Intergovernmental Relations, and on "Overlapping Taxes in the United States," prepared for the Commission on Intergovernmental Relations by the Analysis Staff, Tax Division, Treasury Department, Jan. 1, 1954.

TABLE 32.—*Federal, State, and local tax collections, by source,[1] 1962*

Tax	Amount (millions)				Distribution among governments (percent)			
	All governments	Federal	State	Local	All governments	Federal	State	Local
Individual income	$48,607	$45,571	$2,728	$308	100.0	93.8	5.6	0.6
Corporation income	21,831	20,523	1,308	(2)	100.0	94.0	6.0	(2)
Inheritance, estate, and gift	2,532	2,016	516	(3)	100.0	79.6	20.4	(3)
Sales and gross receipts, total	26,815	13,428	11,915	1,472	100.0	50.1	44.4	5.5
Customs duties	1,142	1,142	--------	--------	100.0	100.0	--------	--------
General sales and gross receipts	5,962	--------	[4] 4,988	974	100.0	--------	[4] 83.7	16.3
Selective sales and gross receipts, total	19,711	12,286	6,927	498	100.0	62.3	35.1	2.5
Motor fuel	6,153	2,451	3,665	37	100.0	39.8	59.6	.6
Alcoholic beverages	4,013	3,248	740	25	100.0	80.9	18.4	.6
Tobacco	3,160	2,022	1,075	63	100.0	64.0	34.0	2.0
Amusements [5]	453	147	306	(5)	100.0	32.5	67.5	(5)
Public utilities [6]	1,824	1,094	420	310	100.0	60.0	23.0	17.0
Other [7]	4,109	3,324	721	64	100.0	80.9	17.5	1.6
Property	19,056	--------	640	18,416	100.0	--------	3.4	96.6
Motor vehicle and operators' licenses	1,790	--------	1,667	123	100.0	--------	93.1	6.9
All other [8]	3,153	724	1,786	643	100.0	23.0	56.6	20.4
Total	123,786	82,262	20,561	20,963	100.0	66.5	16.6	16.9

[1] Exclusive of all employment taxes except $466,000,000 included in the "All other" category for the Federal Government which is used to cover costs of administering insurance programs. Total Federal employment tax collections in fiscal 1962 were approximately $13,000,000,000; State collections approximately $2,500,000,000. These collection figures include penalties and interest, but exclude refunds which are substantial in the case of Federal income taxes and State gasoline taxes.

[2] Minor amount included in "Individual income taxes."

[3] Minor amount included in "All other."

[4] Excludes collections from the Washington and West Virginia business and occupation taxes ($69,000,000 and $54,000,000, respectively, included in "All other"), which are classified as "general sales taxes" by the Bureau of the Census.

[5] The Federal total includes taxes on admissions to theaters, concerts, athletic contests, cabarets, etc., club dues and initiation fees, and wagering taxes. The State total includes excises applicable to admissions on amusement operators in general and to specified types of amusement businesses, but does not include amounts collected from admissions by the 20 States which tax admissions under the general sales tax. The major portion of State collections ($286,000,000) is derived from taxes on parimutuels (which are specifically exempt from the Federal wagering tax). Local collections from amusement taxes are not separately classified and therefore are included in "All other taxes."

[6] Federal collections are from the excises on transportation, telephone, telegraph, and other communication services. The State and local total includes taxes imposed specifically on public passenger and freight transportation companies, telephone, telegraph, light and power companies, and other public utility companies, which are measured by gross receipts, gross earnings, or units of service sold. It does not include amounts collected under State and local general sales taxes which apply to public utility services

[7] Important among the sources of revenue included here are: for the Federal Government, the manufacturers' excise on automobiles and parts, and the retailers' excises on luggage, jewelry, furs, and toilet preparations, for State governments, insurance taxes.

[8] The significant taxes included in "All other" are Federal and State document and stock transfer taxes, the portion of Federal unemployment tax collections used to cover the cost of administering the insurance program, State severance taxes, and local license revenues.

Sources: Compiled by the Advisory Commission on Intergovernmental Relations from U.S. Bureau of the Census, "Governmental Finances in 1962," October 1963.

In a sense, grouping taxes into broad categories tends to exaggerate the actual degree of overlapping since taxes which differ extensively with regard to their detailed provisions are grouped together in the same broad class. The property tax category, for example, includes taxes on special types of property as well as taxes on real estate. Finally, the degree of overlapping varies greatly from one State or locality to another. Thus, while some jurisdictions employ a number of taxes, others rely almost exclusively on one source. Variations in the composition of tax collections among the States are presented in appendix table 82.

Measured in terms of tax dollars collected, therefore, the degree of tax overlapping is not as extensive as a checklist of types of taxes employed by more than one level of government would suggest. One study concludes that the existing amount of tax overlapping could be eliminated, without changing the rates or other provisions of existing taxes, by foregoing about 20 percent of present collections.[2]

B. HISTORICAL DEVELOPMENT

The use of the same tax base by more than one level of government is largely a development of the post-1930 period. Prior to that time, although the basic elements of the problem were in existence, revenue requirements at each level of government were for the most part relatively modest compared with traditional revenue sources. From the beginning of the century until World War I an informal but effective separation of revenue sources existed. State and local governments depended primarily on property taxation while the Federal Government's principal revenue sources were customs and excises, principally on alcoholic beverages and tobacco. Under the impetus of World War I revenue needs the individual and corporate income taxes developed as important revenue sources at the Federal level.

During the 1920's, the major development in intergovernmental fiscal relations was the introduction of a credit in the Federal estate tax for State death taxes. The credit served not only to reduce the overall burden of Federal and State death taxes but also to encourage uniformity in the level of such State taxes. The credit was intended to deter interstate competition for wealthy residents.

In the depression of the 1930's demands imposed on State and local governments for relief and welfare services increased significantly while existing, traditional revenue sources declined in productivity. The inadequacy of property taxes, which resulted from a substantial decline in property values and the statutory debt and tax rate limitations in many jurisdictions, led State and local governments to search for additional revenue sources. The following table indicates the diversification of State revenue sources during this period.

TABLE 33.—*Dates of adoption of major State taxes: Frequency distribution by decades*[1]

Type of tax	Decade								
	Pre-1901	1901–10	1911–20	1921–30	1931–40	1941–50	1951–60	1961–63	Total
Death	23	15	7	2	2				49
Gift					9	3			12
Automobile registration		33	15		1				49
Individual income		1	9	6	16	1		3	36
Corporation income [2]		1	8	8	15	2	2	1	37
Gasoline			5	43	1	1			50
Cigarettes				8	19	15	5		47
Distilled spirits					29	2	1		32
General sales					24	5	6	2	37
Total	23	50	44	67	116	29	14	6	

[1] Includes only States which employed the particular tax as of Jan. 1, 1964.
[2] Does not include South Dakota's tax which applies only to financial institutions.

Source: Advisory Commission on Intergovernmental Relations.

Concurrently, Federal participation in social welfare programs increased, both through direct assumption of responsibility and through financial assistance to States and their subdivisions. Thus, from 1932 through the remainder of the decade, both Federal receipts

[2] Advisory Commission on Intergovernmental Relations, "Overlapping Taxes in the United States," ch. 2.

and expenditures increased in relation to total Government revenue and outlays.

The outbreak of World War II arrested the growing pressures in intergovernmental finances. Rapidly rising incomes increased State and local government tax yields while expenditures by these governments were necessarily restricted to nonpostponable essentials. Federal revenue requirements increased very rapidly, resulting in a substantial expansion of excise taxes and increases in individual and corporate income tax levies.

From the end of the war to the present time, State and local government revenues have increased, reflecting the general expansion of the economy. Rapidly rising property values and the expansion of the property tax base have been particularly significant at the local level. At the State level, many of the levies adopted during the depression years of the 1930's have proved to be productive revenue sources; this is particularly true of general sales and corporate and individual income taxes.

At the same time, revenue requirements at the State and local level have grown very rapidly. Especially pressing have been the demands for additional schools, highways, and health facilities. The rapid population increase underlying these growing demands has also required more elaborate systems of police and fire protection, sewage disposal and water supply, and, in a large number of communities, urban redevelopment. Concurrently, Federal revenue requirements, particularly for defense, remain high.

State and local governments are presently confronted with serious fiscal problems. State governments continue the search for new revenue sources while increasing tax rates under existing levies. Many States have given the property tax over to their subdivisions, and have granted them wider latitude in nonproperty taxing powers. Local governments continue to rely primarily on property taxation, although diversification through income taxes, general sales taxes, and selective excises is apparent. Although State-local overlapping in the property tax area has been almost completely eliminated, it is increasing with respect to such nonproperty taxes as income, retail sales, motor fuel, and cigarette taxes.

II. Issues and Proposals

A. ALLOCATION OF GOVERNMENT FUNCTIONS

Underlying the overlapping of Federal, State, and local government revenue systems is the very substantial growth in Government functions since the early 1900's. Apart from Federal outlays directly and indirectly related to national defense, this growth in the scope of Government activities has been largely the result of the increased demand for public services accompanying industrialization and urbanization.

In the process of meeting these demands, the Federal Government has frequently taken the lead, sometimes because the State and local governments were financially incapable of doing so, sometimes because the problems giving rise to the demands have been so broad as to cross local and State jurisdictional boundaries. At the same time, shifts in responsibilities have occurred between the State and local levels, reflecting in many cases the increasing concentration of the population in urban centers. Often, the States have been required to assume functions formerly discharged by localities so that local governments could concentrate their more limited resources on the basic requirements of growing cities and towns.

Much of this shift in responsibility between levels of government has represented acceptance of practical expedients rather than deliberate and explicit determination of the proper allocation of functional responsibility and authority.

Accordingly, an issue frequently raised concerns the respective roles of the Federal, State, and local governments in meeting the aggregate demand for government services.[3]

On the one hand, there is a widespread view in favor of confining a maximum amount of public services to States and localities. It is argued that State and local governments are better suited than the Federal Government for determining the needs of the communities within their jurisdictions. In view of the high degree of variability in these needs from one community to another, it is maintained, the uniformity of standards imposed by the Federal Government may often lead to inefficient use of the total resources committed to public service. Moreover, it is contended, the subsidy element in many Federal programs focusing on State or local, as opposed to nationwide, problems, tends to dull the sense of financial responsibility of the State or locality and makes it increasingly difficult for it to meet new service requirements.

Finally, it is argued, a wide range of civic benefits, basic to preserving and strengthening our most highly prized political and social virtues, require maximum responsibility at the local and State level.[4] According to this view, every effort should be made to increase the scope of State and local government functions while reserving for the Federal Government only those functions which by their very nature exceed the jurisdictional authority of States and localities. Such explicit decentralization, it is argued, is basic to any broad solution to the problem of overlapping revenue systems.

A contrary view holds that the enlargement of Federal functions is a necessary concomitant of our industrially advanced economy. It is pointed out that apart from defense and defense-related functions, most of the increase in Federal expenditures reflects attempts to deal with problems emerging from our rapid industrial growth which are so broadly based as to exceed the competence of State and local governments. Many of the Federal programs developed or expanded during the 1930's are cited as efforts to deal with situations not limited by geographical or political boundary lines.

Moreover, it is argued that many of the continually emerging demands so vitally affect the national well-being as to transcend the traditional views of State and local government responsibilities. Particularly in the case of highways and similar public facilities, health, and education, it is contended, the Nation cannot afford to permit public programs to lag behind in any community, whether because of a lack of awareness of needs, indifference, or limited

[3] For a comprehensive discussion of the allocation of government functions among levels of government see "Federal Expenditure Policy for Economic Growth and Stability," papers submitted by panelists appearing before the Subcommittee on Fiscal Policy, Joint Economic Committee, Joint Committee Print, 85th Cong., 1st sess., sec. III, "Level of Government at Which Public Functions are Performed," pp. 163–219.

[4] Cf. the Commission on Intergovernmental Relations, "Report to the President," June 1955, pp. 3, 34.

financial resources. While the local and State governments should be encouraged to act on their own initiative in such cases, Federal participation should also be enlarged in order to insure adequate programs.

According to this view, explicit decentralization of Government functions is not a prime objective. Rather it should be deferred until basic programs are well established and the willingness and capability of State and local governments to bear increased responsibility for them is clearly determined. Coordination of revenue systems among the three levels of government, accordingly, should proceed without necessarily referring to the respective functional responsibilities of each.

A final argument is that a substantial shift in aggregate public services from the Federal to State and local governments would have significantly adverse consequences for economic stability. Such a move, it is pointed out, would necessarily involve a decline in the relative importance of Federal revenues and a commensurate increase in State and local taxes. The latter, however, are generally characterized as regressive or at best proportional in their incidence, while the Federal revenue system is predominately progressive. Accordingly, it is argued, the proposed decentralization would involve greater overall regressivity in the distribution of tax burdens. This in turn, would mean that the overall fiscal system would become less responsive to changes in levels of economic activity, since it is the progressive Federal revenue system which provides the major automatic compensatory adjustments. Economic stabilization, therefore, would require a greater degree of discretionary action by the Federal Government.

B. TAX COORDINATION

Continuing growth in the American economy implies a continued rise in the level of many types of public services. Regardless of the respective responsibilities of the Federal, State, and local governments in providing these services, it is generally agreed that coordination of revenue systems is required if the discharge of these responsibilities is to be effectively financed. A wide range of coordination methods has been and continues to be explored, both in theory and in practice.

1. Separation of revenue sources

A proposal frequently made to increase the fiscal capacity of State and local governments calls for the repeal of certain Federal taxes, leaving them for the exclusive use of States and their subdivisions.

This proposal is particularly appealing to those who hold that an explicit reallocation of government functions among various governmental levels is essential. Separation of revenue sources, it is argued, conforms with a well-established principle that each level of government should support its functions from its own, independent income. Sharing the revenue source with another level of government necessarily limits the extent to which either can expand its use of the source and accordingly limits the extent to which either can expand its functions in response to new and growing demands.

On the other hand, it is pointed out that in practice revenue separation would offer a far from ideal solution to the problem of expanding fiscal capacity. In the first place, there is no general agreement even among those proposing separation as to the specific taxes which should be allocated to each government level. The taxes that would appear to be best suited for some States and localities would be viewed by others as inadequate or inappropriate to their particular situation. Differences with respect to basic economic resources, the general course of economic development, constitutional and traditional limitations on the use of specific levies—all contribute to widely divergent preferences in tax sources.

Moreover, it is pointed out that complete separation of revenue sources would not affect one of the basic problems in intergovernmental fiscal relations—the uneven geographical distribution of taxpaying potential. A substantial reallocation of government functions and tax sources would result in some States and localities having a revenue potential far in excess of their current demands while others would be able to provide for only a very low level of public services.

Finally, it is pointed out that some of the revenue sources which are frequently suggested for the exclusive use of States and localities can be economically employed by them only if also used by the Federal Government. These are the taxes which involve a relatively high ratio of administrative costs to revenue yield. Federal use of such taxes permits other governments to minimize administrative costs by relying heavily on Federal collection and enforcement efforts to identify the taxpayers and the tax base.

2. Tax sharing

A frequent proposal for intergovernmental tax coordination is that the Federal Government collect certain taxes and share a portion of the revenue with the States and their subdivisions. This suggestion recognizes the limits on State and local use of many revenue sources resulting from high administrative overhead. The taxes suggested for sharing are those the administrative costs of which increase less than proportionately with revenues as the area of jurisdiction expands.

It has been suggested, for example, that the State and local governments withdraw from such taxes as the cigarette excises which are now in effect in 48 States. Considerable saving in administrative costs, it is claimed, could be obtained by adopting tax sharing, with the tax collected at the Federal level. Moreover, tax sharing would eliminate the problem of tax collection where the cigarettes are shipped across State lines.[5]

This proposal raises major difficulties with respect to the distribution of tax revenues. Some method would have to be developed for assuring all of the States now levying such taxes that they would receive their proper share of aggregate collections. Because of the wide range of rates imposed by the several States, those with the higher rates would have to be willing to accept shares of the total revenue which, compared to the relative productivity of the State levies, would appear to be disporportionately low. Moreover, in those States in which localities also employ the revenue device to be "shared," the problem of allocation would be further complicated.

[5] Under legislation enacted in 1949 and strengthened in 1955, the Federal Government is assisting the States in the collection of these taxes. This legislation requires persons who ship cigarettes in interstate commerce to report the shipment to the tax authorities of the buyer's State. State officials report that firms previously engaged in interstate shipments to avoid State cigarette taxes have discontinued their operations.

3. Deductibility

One of the major devices now used for intergovernmental tax coordination is deductibility. The Federal income tax allows deductions for income, general sales and use taxes, personal property taxes, and gasoline taxes paid to other jurisdictions and many State income taxes allow deductions for the Federal income tax. In addition, deductions are allowed by State Governments in the case of certain excises.

Deductibility, it is argued, serves to minimize duplication of tax rates, contributes to uniformity of tax burdens among taxpayers living in different jurisdictions, and reduces intrajurisdictional competition. For example, the deductibility of State and local taxes for Federal income tax purposes reduces tax liability and diverts part of the impact of the State and local taxes to the Federal Government. Accordingly, States are able to impose or increase income taxes, say, without imposing an equivalent net burden on their taxpayers. On the other hand, it is pointed out that allowing deductions in one jurisdiction for the taxes paid to another does not completely eliminate multiple-level taxation. In the case of income taxation, for example, some additional liability remains so long as rates are less than 100 percent. (See appendix table 86.)

4. Tax credits

The use of tax credits is often suggested as an alternative to tax deductibility as a practical coordinating device. Some use of credits is now made at all levels of government. For example, a limited credit for State death taxes paid is allowed against Federal estate tax liability, and a 90-percent credit is generally allowed against the Federal payroll levy for contributions paid into State unemployment compensation plans. States frequently allow credits against their income taxes for income taxes paid to other States, and one State has used the tax-credit method as a State-local coordinating device in the cigarette tax field.

Use of tax credits is urged as a better means of eliminating multiple taxation than can be achieved through tax deductions. On the other hand, it is pointed out that unlimited tax credits would result in the highest rate among competing jurisdictions becoming the standard rate for all. Since in the case of taxes which produce the largest revenues, the Federal levy generally involves higher rates than those of State or local governments, complete crediting of the latter against corresponding Federal liabilities would tend to induce a rise in the State or local rates up to those in the Federal tax. The result would be a substantial curtailment or even the virtual elimination of these taxes as Federal revenue devices. Accordingly, it would not be possible to allow full credit against Federal income tax liabilities, for example, for income taxes paid to State or local governments.

The Joint Federal-State Action Committee composed of Governors and Federal representatives, which was created in 1957 by the Governors' Conference and the President, considered methods of increasing the Federal estate tax credit for death taxes paid to States. The Advisory Commission on Intergovernmental Relations subsequently developed specific recommendations for revising the credit to increase the State's share of death tax revenues. Bills giving effect to the

Commission's recommendation were introduced in the 87th and 88th Congresses.[6]

5. Uniformity of tax bases and the use of tax supplements

Particularly in the case of income taxation there has been a trend toward the adoption by the States of the same tax base and method of tax payment as employed in the Federal tax. As of January 1, 1964, 14 of the 33 States with broad based income taxes and the District of Columbia had adopted Federal definitions, in many essential respects, for the purposes of determining the base of their individual income taxes. Some States employ the same personal exemptions and standard deduction as the Federal Government. Even States that do not use the Federal concept of adjusted gross income often follow Federal law with respect to specific provisions such as capital gains, depreciation, and depletion. Twenty-seven States and the District of Columbia employ withholding to collect income taxes from resident wage earners.

Such uniformity has facilitated Federal-State cooperation in enforcement. Twenty-one States and the District of Columbia have agreements with the Internal Revenue Service which provide for the cooperative use of the income tax returns supplied each jurisdiction and similar agreements with other States are in the process of negotiation.

The tax supplement approach employed for a time in Alaska and West Virginia provides, in a sense, the closest degree of integration between Federal and State taxes. Individual income taxes in these States were assessed as a percentage of the Federal tax. New Mexico and Utah in the past permitted their residents the option of computing their State tax as a percentage of Federal tax.

Tax supplements have also made some headway in State-local fiscal relations. In Mississippi, for example, the State has authorized cities to levy sales taxes of either one-half of 1 percent or 1 percent, and the local taxes are collected along with the State tax on a single return. California in 1955, in effect, made its municipal and county sales taxes supplements to the State tax by enacting a uniform sales tax law which authorizes enactment of 1 percent local sales taxes but requires the local governments to contract with the State tax administration for collection of the tax.

These developments have led to the suggestion that a solution to many of the problems of overlapping taxes lies in the extensive use of tax supplements and joint administration. In the case of Federal-State tax relations, for example, it is suggested that the Federal income-tax return be elaborated to provide for supplemental State taxes, designated by the various States as given percentages of the Federal tax liability. Collection and enforcement activities would be concentrated at the Federal level and a pro rata sharing of these expenses would be reflected in the distributions to the State governments. The same approach might also be employed with respect to all other major revenue sources.

A principal advantage claimed for this approach is that it would integrate Federal-State-local revenue systems and in doing so would enhance overall progressivity. State and local tax systems, accord-

[6] Advisory Commission on Intergovernmental Relations, "Coordination of State and Federal Inheritance, Estate, and Gift Taxes," January 1961.

ingly, would contribute more extensively than at present to economic stabilization.

Those who are critical of the use of tax supplements point out that they tend to make changes in the revenues of the jurisdiction with the supplementary tax dependent upon actions taken by the principal jurisdiction; actions which may be taken for reasons entirely unrelated to the situation faced by the former. For example, it is pointed out that Alaska was forced to abandon the supplementary form of its individual income tax when the reduction in Federal tax rates enacted in 1964 threatened to reduce State income tax revenues substantially.[7] Enactment of other revisions in the Federal tax code have altered the tax bases of States which follow Federal definitions.

Those objecting to this approach further contend that it would tend to undermine the sense of immediate financial responsibility in the States and localities and would remove much of the impetus for developing new and diversified revenue sources best suited to meet the particular needs of the respective jurisdictions. Moreover, it is argued that as a practical matter, the use of tax supplements would be limited in numerous cases by the fact that the taxpayer's income or property situs is not confined to a single political jurisdiction. Allocation problems, accordingly, would be extremely difficult to resolve.

One problem regarding tax base uniformity concerns the manner in which companies that do business in more than one State are taxed by the States. Many State laws require that income be attributed for tax purposes to the State if a business sells its products to customers in that State. To comply with various State laws, the 120,000 businesses with interstate sales must first determine whether they are liable to tax in a particular State and, if so, how they must compute taxable income under the laws of that State and how they must allocate the proper proportion of such taxable income to that State under the rules laid down in its laws. The great diversity of State laws governing these questions and the relatively small size of many of the businesses affected by them have created a difficult compliance situation. One study concludes that because of legal inconsistencies and widespread noncompliance resulting from business' response to the complexity of the law, there are wide differences in State tax burdens between firms of comparable size.[8] The average firm with extensive interstate sales pays less in tax than a similarly placed firm whose sales are almost entirely within one jurisdiction. But some firms engaged in interstate business pay tax on more income than they earn and pay tax in years in which, overall, they suffer losses. Moreover, compliance costs for firms which strive to fulfill the letter of the law in all States in which they operate may be quite high. While much of the present unevenness in the distribution of State business tax liabilities could be eliminated if strict compliance were enforced, costs for many businesses would be higher, exceeding the tax remitted in a significant number of cases. In summary, it has been said:

> Overall, in cost terms, it would seem that the major significance of the prevailing system is not that it produces expensive compliance, but that the cost of full compliance is a major cause of noncompliance.

[7] The State adopted statutory tax rates equal to the rates which, in effect, existed in 1963 under the prior supplementary tax approach.

[8] "State Taxation of Interstate Commerce," Report of the Special Subcommittee on State Taxation of Interstate Commerce of the Committee on the Judiciary, House of Representatives, H. Rept. 1480, 88th Cong., 2d sess., vol. 1, pp. 593–599.

This, then, is an assessment of the State income tax system and its effect on interstate commerce in the United States today. It is the picture of a system which works badly for both business and the States. It is the picture of a system in which the States are reaching farther and farther to impose smaller and smaller liabilities on more and more companies. It is the picture of a system which calls upon tax administrators to enforce the unenforcible, and the taxpayer to comply with the uncompliable.[9]

C. GRANTS-IN-AID

Particularly since the 1930's, grants-in-aid from the Federal Government to the States and their subdivisions have played an increasingly important role in intergovernmental fiscal relations. Between 1946 and 1962 Federal aid to States and localities, including amounts received for contractual services and shared revenues, rose from $855 million to nearly $7.9 billion, or at an average annual rate of nearly 15 percent. During this period Federal aid rose from 7 percent to 14 percent of State and local government general revenues.[10]

The Federal-aid system has grown out of a consciousness that certain functions normally viewed as primarily State or local responsibilities but having a national interest (for example, highways and assistance to the needy aged), were not being performed, or were being performed inadequately, at the State and local level. Generally to promote nationwide uniformity in minimum standards of service, Federal aid has been granted, conditional upon matching or related State and local expenditures.

Another important factor leading to Federal aid has been a demand from lower levels for Federal assistance in programs which the States and the local units felt they should develop, but were financially unable to do so.

Federal-aid money is allocated according to formulas usually laid down in the controlling statutes. The formulas, which vary as between programs, are based on such measures as population, area, road milage, per capita income, incidence of disease, etc. A few grants are allocated as a percentage of State expenditures within specified statutory limitations.

The Federal-aid system has raised a number of issues in intergovernmental fiscal relations. It is sometimes criticized as an unwarranted extension of Federal fiscal powers for the purpose of redistributing income and wealth along geographic lines. This result follows, it is claimed, from the fact that the cost of Federal aid is financed by taxes raised primarily in the relatively well-to-do States while the benefits, by the very nature of the functions to which Federal aid is allocated, rebound primarily to the less fortunately situated States.

On the other hand, it is pointed out that whatever the focus of the immediate benefits from Federal aid, the entire Nation benefits from the provision of the services such aid finances. In a highly developed industrial economy such as ours, it is contended, there is a very high degree of economic interdependence. Accordingly, the entire Nation suffers, at least over the long run, from the inadequate performance of essential public functions in any one community. Federal aid, by effecting minimum standards of performance throughout the country, mitigates the drag on the national economy from those States whose

[9] Ibid. p. 598.
[10] Advisory Commission on Intergovernmental Relations, "The Role of Equalization in Federal Grants," January 1964, p. 14.

progress has been relatively slow. Moreover, it is claimed, in many cases it assists such States in moving forward in economic development, with positive benefits for the whole economy.

Federal aid is sometimes characterized as a means of transferring to the Federal level functions which are primarily State and local in nature. The aid system, it is contended, tends to sap the initiative of the beneficiary States and subdivisions and to induce a financial dependence on the Federal Government out of proportion to their fiscal capacities.

Supporters of more extensive use of Federal aid contend, however, that one of its primary virtues is stimulating States to develop programs to meet growing public needs. The matching funds arrangement generally employed, it is argued, provides a strong incentive for the States to explore their revenue potentials more fully and therefore represents a stimulus to, rather than a drag on, fiscal initiative. Finally, it is argued that Federal aid is directed primarily to programs in which the national interest is so large that the States and their subdivisions should not be required to bear the full fiscal burden. Highway construction is cited as an important case in point and health and education programs are coming to be increasingly regarded as involving joint Federal, State, and local responsibility, particularly under the pressure of defense demands.

D. FEDERAL-STATE TAX IMMUNITY

Historically, immunity problems have created sore points in Federal-State fiscal relations. The difficulties stem in part from the fact that the immunities are not spelled out in the Constitution, but arise from a long line of judicial decisions beginning early in the life of the Nation when Federal-State relations were far different than they are today.[11] For 80 years the court continued to broaden the range of immunities. In more recent years, the scope of immunities has been narrowed.

The principal tax immunity problems are (1) the exemption of properties of the Federal Government and its agencies from State and local property taxes, and (2) the mutual income-tax exemption of interest on Federal and State Government obligations.

At the present time, no consistent pattern is followed in determining the revenue contribution to the States and localities with respect to Federal properties. With respect to most Federal property, no payments are made. Some small amount of Federal property is subject to taxation in the same way as private property. In other cases, payments in lieu of property taxes are made. For a third group of properties, the Federal Government shares the revenue derived therefrom.

The lack of an established system in this context is frequently criticized by the affected States and localities. Since providing for the general taxability of Federal properties would probably open the whole question of Federal-State tax immunities, it is sometimes proposed that a general system of in-lieu payments be established. On the other hand, it is recognized that any formal system of such payments would, in effect, represent taxation of Federal property by the States

[11] Principally *McCulloch* v. *Maryland*, 4 Wheat. 316 (1819).

or their subdivisions. Accordingly, it is suggested that this step should be regarded as an integral part of a general change in intergovernmental tax status.

The Federal income tax law specifically excludes from gross income amounts received as interest on the obligations of State and local governments.[12] Apart from the constitutional issues involved, this provision has been justified as a means of keeping State and local government interest costs at manageable levels. On the other hand, the provision is criticized as an unwarranted Federal tax subsidy of State and local government debt, the benefits of which accrue primarily to high-income taxpayers. Tax exemption is also criticized as constituting a strong inducement for diversion of investable funds away from the corporate security market.

An issue of current importance concerns the issuance of industrial development bonds.[13] Such bonds are issued by localities to finance projects whose purpose is to encourage business firms to locate facilities within their jurisdictions. It is argued that such bond issues are sometimes used to provide special benefits to the business firms concerned. For example, in some instances municipalities have issued bonds to finance the construction of a plant which were sold to the very firm which subsequently leased the plant. The arrangement served to grant the firm tax-exempt interest income. It is also contended that the bonds disrupt conventional financing and normal competitive relationships. In defense of such issues, it is argued that public support for local development projects is a longstanding tradition and that the amount of abuse is not great. Furthermore, it is pointed out that industrial development bonds are legally no different than other tax-exempt issues.

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[12] Sec. 103(a).

[13] For a discussion of this issue see the Advisory Commission on Intergovernmental Relations, "Industrial Development Bond Financing," June 1963.

APPENDIX

STATISTICAL MATERIAL

NOTE.—Detail in the tables of this statistical appendix may not add to the totals because of rounding.

Listed sources should be consulted for precise definition of terms and the nature of any limitations, such as sampling variability.

Figures for recent years may be subject to later revision.

TABLES

GENERAL

TABLE 1.—*Selected economic indicators, calendar years 1929–1963*

[Dollar amounts in billions]

	1929	1939	1944	1949	1950	1951	1952	1953	1954	1955	1956	1957	1958	1959	1960	1961 [1]	1962 [1]	1963 [1]
Gross national product [2]	$104.4	$91.1	$211.4	$258.1	$284.6	$329.0	$347.0	$365.4	$363.1	$397.5	$419.2	$442.8	$444.5	$482.7	$502.6	$518.2	$554.9	$585.1
Personal consumption expenditures	$79.0	$67.6	$109.8	$181.2	$195.0	$209.8	$219.8	$232.6	$238.0	$256.9	$269.9	$285.2	$293.2	$313.5	$328.2	$336.8	$355.4	$373.1
Gross private domestic investment	$16.2	$9.3	$7.1	$33.0	$50.0	$56.3	$49.9	$50.3	$48.9	$63.8	$67.4	$66.1	$56.6	$72.7	$71.6	$69.0	$78.8	$82.3
Net exports of goods and services	$0.8	$0.9	−$2.1	$3.8	$0.6	$2.4	$1.3	−$0.4	$1.0	$1.1	$2.9	$4.9	$1.2	−$0.8	$3.9	$4.4	$3.8	$4.5
Government purchases of goods and services	$8.5	$13.3	$96.5	$40.2	$39.0	$60.5	$76.0	$82.8	$75.3	$75.6	$79.0	$86.5	$93.5	$97.2	$99.6	$107.9	$117.0	$125.1
National income	$87.8	$72.8	$182.6	$217.7	$241.9	$279.3	$292.2	$305.6	$301.8	$330.2	$350.8	$366.9	$367.4	$400.5	$414.5	$426.1	$453.7	$478.4
Personal income	$85.8	$72.9	$165.7	$208.3	$228.5	$256.7	$273.1	$288.3	$289.8	$310.2	$332.9	$351.4	$360.3	$383.9	$401.3	$417.4	$442.1	$463.0
Personal taxes	$2.6	$2.4	$18.9	$18.7	$20.8	$29.2	$34.4	$35.8	$32.9	$35.7	$40.0	$42.6	$42.3	$46.8	$51.4	$52.9	$57.7	$60.4
Disposable personal income	$83.1	$70.4	$146.8	$189.7	$207.7	$227.5	$238.7	$252.5	$256.9	$274.4	$292.9	$308.8	$317.9	$337.1	$349.9	$364.4	$384.4	$402.4
Personal saving	$4.2	$2.9	$36.9	$8.5	$12.6	$17.7	$18.9	$19.8	$18.9	$17.5	$23.0	$23.6	$24.7	$23.6	$21.7	$27.6	$29.1	$29.3
Business expenditures on new plant and equipment [3]	(4)	$5.5	(4)	$19.3	$20.6	$25.6	$26.5	$28.3	$26.8	$28.7	$35.1	$37.0	$30.5	$32.5	$35.7	$34.4	$37.3	$39.1
Total new construction	$10.8	$8.2	$5.3	$24.2	$29.9	$32.7	$34.7	$37.0	$39.2	$44.2	$45.8	$47.8	$49.0	[5] $55.3	$53.9	$55.5	$59.0	$62.8
Population (millions)	121.9	131.0	138.4	149.2	151.7	154.3	156.9	159.6	162.4	165.3	168.2	171.3	174.2	177.1	180.7	183.7	186.6	189.3
Civilian labor force (millions)	49.2	55.2	54.6	[6] 62.1	63.1	62.9	63.0	63.8	64.5	65.8	67.5	67.9	68.6	69.4	[7] 70.6	71.6	72.0	73.0
Unemployment rate (percent of labor force)	3.2	17.2	1.2	5.9	5.3	3.3	3.1	2.9	5.6	4.4	4.2	4.3	6.8	5.5	5.6	6.7	5.6	5.7
Balance of payments (surplus or deficit)	−$0.1	+$1.9	−$1.9	+$0.2	−$3.6	−$0.3	−$1.0	−$2.2	−$1.6	−$1.1	−$0.9	+$0.5	−$3.5	−$3.7	−$3.9	−$2.4	−$2.2	−$2.7
Industrial production index (1957–59=100)	38.4	38.3	81.7	64.7	74.9	81.3	84.3	91.3	85.8	96.6	99.9	100.7	93.7	105.6	108.7	109.8	118.3	124.3
Consumer price index (1957–59=100)	59.7	48.4	61.3	83.0	83.8	90.5	92.5	93.2	93.6	93.3	94.7	98.0	100.7	101.5	103.1	104.2	105.4	106.7
Wholesale price index (1957–59=100)	52.1	42.2	56.9	83.5	86.8	96.7	94.0	92.7	92.9	93.2	96.2	99.0	100.4	100.6	100.7	100.3	100.6	100.3

[1] Preliminary.
[2] Components may not add to total GNP because of rounding.
[3] Excludes agriculture.
[4] Not available.
[5] New series beginning in 1959 (not entirely comparable with previous data).
[6] New series beginning in 1947 (not entirely comparable with previous data).
[7] Includes Alaska and Hawaii, beginning in 1960.

Source: Departments of Labor and Commerce, Board of Governors of the Federal Reserve System, Securities and Exchange Commission, and the 1964 Economic Report of the President.

TABLE 2.—*Federal receipts, expenditures, surplus or deficit, and public debt, fiscal years 1929–65*

[In billions of dollars]

Fiscal year	Administrative budget			Consolidated cash budget			National income accounts budget			Public debt
	Receipts	Expenditures	Surplus (+) or deficit (−)	Receipts	Expenditures	Surplus (+) or deficit (−)	Receipts	Expenditures	Surplus (+) or deficit (−)	
1929	3.9	3.1	+0.7	3.8	2.9	+0.8	--------	--------	--------	16.9
1930	4.1	3.3	+.7	4.0	3.1	+.9	--------	--------	--------	16.2
1931	3.1	3.6	−.5	3.2	4.1	−1.0	--------	--------	--------	16.8
1932	1.9	4.7	−2.7	2.0	4.8	−2.7	--------	--------	--------	19.5
1933	2.0	4.6	−2.6	2.1	4.7	−2.6	--------	--------	--------	22.5
1934	3.0	6.6	−3.6	3.1	6.4	−3.3	--------	--------	--------	27.1
1935	3.7	6.5	−2.8	3.8	6.3	−2.4	--------	--------	--------	28.7
1936	4.0	8.4	−4.4	4.2	7.6	−3.5	--------	--------	--------	33.8
1937	5.0	7.7	−2.8	5.6	8.4	−2.8	--------	--------	--------	36.4
1938	5.6	6.8	−1.2	7.0	7.2	−.1	--------	--------	--------	37.2
1939	5.0	8.8	−3.9	6.6	9.4	−2.9	--------	--------	--------	40.4
1940	5.1	9.1	−3.9	6.9	9.6	−2.7	--------	--------	--------	43.0
1941	7.1	13.3	−6.2	9.2	14.0	−4.8	--------	--------	--------	49.0
1942	12.5	34.0	−21.5	15.1	34.5	−19.4	--------	--------	--------	72.4
1943	21.9	79.4	−57.4	25.1	78.9	−53.8	--------	--------	--------	136.7
1944	43.6	95.0	−51.4	47.8	94.0	−46.1	--------	--------	--------	201.0
1945	44.4	98.3	−53.9	50.2	95.2	−45.0	--------	--------	--------	258.7
1946	39.7	60.3	−20.7	43.5	61.7	−18.2	37.3	56.6	−19.3	269.4
1947	39.7	38.9	+.7	43.5	36.9	+6.6	42.9	31.7	+11.2	258.3
1948	41.4	33.0	+8.4	45.4	36.5	+8.9	43.7	32.3	+11.4	252.3
1949	37.7	39.5	−1.8	41.6	40.6	+1.0	40.1	40.0	+.2	252.8
1950	36.4	39.5	−3.1	40.9	43.1	−2.2	42.0	42.2	−.2	257.4
1951	47.5	44.0	+3.5	53.4	45.8	+7.6	61.7	45.3	+16.3	255.2
1952	61.3	65.3	−4.0	68.0	68.0	(1)	65.5	66.6	−1.1	259.1
1953	64.7	74.1	−9.4	71.5	76.8	−5.3	69.9	76.2	−6.3	266.1
1954	64.4	67.5	−3.1	71.6	71.9	−.2	65.9	74.5	−8.6	271.3
1955	60.2	64.4	−4.2	67.8	70.5	−2.7	67.0	68.1	−1.1	274.4
1956	67.9	66.2	+1.6	77.1	72.5	+4.5	76.3	69.5	+6.8	272.8
1957	70.6	69.0	+1.6	82.1	80.0	+2.1	80.9	76.5	+4.4	270.5
1958	68.6	71.4	−2.8	81.9	83.5	−1.6	77.8	82.8	−4.9	276.3
1959	67.9	80.3	−12.4	81.7	94.8	−13.1	85.9	90.3	−4.4	284.7
1960	77.8	76.5	+1.2	95.1	94.3	+.8	94.5	92.1	+2.4	286.3
1961	77.7	81.5	−3.9	97.2	99.5	−2.3	95.2	97.8	−2.7	289.0
1962	81.4	87.8	−6.4	101.9	107.7	−5.8	103.6	106.4	−2.7	298.2
1963	86.4	92.6	−6.3	109.7	113.8	−4.0	109.3	112.6	−3.3	305.9
1964 [2]	88.4	98.4	−10.0	114.4	122.7	−8.3	113.6	119.1	−5.5	311.8
1965 [2]	93.0	97.9	−4.9	119.7	122.7	−2.9	118.8	121.5	−2.8	317.0

[1] +$49,000,000.
[2] Preliminary.

Source: Bureau of the Budget.

TABLE 3.—*Federal administrative budget receipts by source, fiscal years 1939–65*

Fiscal year	Total budget receipts [1]	Individual income tax	Corporation income and excess profits taxes	Excise taxes	Customs	Net employment taxes [2]	Estate and gift taxes	Miscellaneous receipts [3]
	Amounts (in millions of dollars)							
1939	4,996	1,022	1,138	1,861	302	128	357	188
1940	5,144	959	1,123	1,973	331	164	357	237
1941	7,103	1,400	2,029	2,555	365	116	403	235
1942	12,555	3,205	4,727	3,393	369	155	421	286
1943	21,987	6,490	9,570	4,093	308	160	442	924
1944	43,635	19,701	14,737	4,761	417	200	507	3,313
1945	44,475	18,415	15,146	6,267	341	188	638	3,480
1946	39,771	16,157	11,833	6,999	424	214	669	3,476
1947	39,786	17,835	8,569	7,207	477	315	770	4,614
1948 [4]	41,375	19,305	9,678	7,356	403	49	890	3,694
1949	37,663	15,548	11,195	7,502	367	235	780	2,036
1950	36,422	15,745	10,448	7,549	407	226	698	1,349
1951	47,480	21,643	14,106	8,648	609	234	708	1,532
1952	61,287	27,913	21,225	8,851	533	256	818	1,691
1953	64,671	30,108	21,238	9,868	596	274	881	1,705
1954	64,420	29,542	21,101	9,945	542	283	934	2,074
1955	60,209	28,747	17,861	9,131	585	579	924	2,381
1956	67,850	32,188	20,880	9,929	682	322	1,161	2,689
1957	70,562	35,620	21,167	9,055	735	328	1,365	2,293
1958	68,550	34,724	20,074	8,612	782	333	1,393	2,633
1959	67,915	36,719	17,309	8,504	925	321	1,333	2,804
1960	77,763	40,715	21,494	9,137	1,105	339	1,606	3,367
1961	77,659	41,338	20,954	9,063	982	(6)	1,896	3,426
1962	81,409	45,571	20,523	9,585	1,142	(6)	2,016	2,571
1963	86,376	47,588	21,579	9,915	1,205	(6)	2,167	3,922
1964 [5]	88,400	47,500	23,700	10,221	1,275	(6)	2,335	3,369
1965 [5]	93,000	48,500	25,800	10,987	1,460	(6)	2,740	3,513
	Percentage distribution							
1939	100.0	20.5	22.8	37.2	6.0	2.6	7.1	3.8
1940	100.0	18.7	21.8	38.4	6.4	3.2	6.9	4.6
1941	100.0	19.7	28.6	36.0	5.1	1.6	5.7	3.3
1942	100.0	25.5	37.7	27.0	2.9	1.2	3.4	2.3
1943	100.0	29.6	43.5	18.6	1.4	.7	2.0	4.2
1944	100.0	45.1	33.8	10.9	.9	.5	1.2	7.6
1945	100.0	41.4	34.1	14.1	.8	.4	1.4	7.8
1946	100.0	40.6	29.8	17.6	1.1	.5	1.7	8.7
1947	100.0	44.8	21.6	18.1	1.2	.8	1.9	11.6
1948 [4]	100.0	46.7	23.4	17.8	1.0	.1	2.2	8.9
1949	100.0	41.3	29.7	19.9	1.0	.6	2.1	5.4
1950	100.0	43.2	28.7	20.7	1.1	.7	1.9	3.7
1951	100.0	45.6	29.7	18.2	1.3	.5	1.5	3.2
1952	100.0	45.5	34.6	14.4	.9	.4	1.3	2.8
1953	100.0	46.6	32.8	15.3	.9	.4	1.4	2.6
1954	100.0	45.9	32.8	15.4	.8	.4	1.4	3.2
1955	100.0	47.7	29.7	15.2	1.0	1.0	1.5	4.0
1956	100.0	47.4	30.8	14.6	1.0	.5	1.7	4.0
1957	100.0	50.5	30.0	12.8	1.0	.5	1.9	3.2
1958	100.0	50.7	29.3	12.6	1.1	.5	2.0	3.8
1959	100.0	54.1	25.5	12.5	1.4	.5	2.0	4.1
1960	100.0	52.4	27.6	11.8	1.4	.4	2.1	4.3
1961	100.0	53.2	27.0	11.7	1.3	----------	2.4	4.4
1962	100.0	56.0	25.2	11.8	1.4	----------	2.5	3.2
1963	100.0	55.1	25.0	11.5	1.4	----------	2.5	4.5
1964 [5]	100.0	53.7	26.8	11.6	1.4	----------	2.6	3.8
1965 [5]	100.0	52.2	27.7	11.8	1.6	----------	2.9	3.8

1 Receipts are net of refunds and transfers.
2 Net after deducting appropriations to Federal old-age and survivors insurance trust fund and railroad retirement account. Includes Railroad Unemployment Insurance Act receipts from 1950 through 1952.
3 Includes receipts not otherwise classified such as proceeds from sale of surplus property and from Government-owned securities, deposits resulting from renegotiation of war contracts, repayment on credit to United Kingdom, recoveries, refunds, gifts, license fees, fines, etc.
4 Beginning with 1948, net budget receipts and budget expenditures have been adjusted to exclude certain interfund transactions. The adjustment was made in the totals and the "all other" categories. The change does not affect the budget surplus or deficit.
5 Estimate, January 1964.
6 Less than $50.

Source: Bureau of the Budget.

TABLE 4.—*Federal cash budget receipts by source, fiscal years 1948–65*

[In millions of dollars]

	Actual																Estimate	
	1948	1949	1950	1951	1952	1953	1954	1955	1956	1957	1958	1959	1960	1961	1962	1963	1964	1965
RECEIPTS FROM THE PUBLIC																		
Individual income taxes	19,305	15,548	15,745	21,643	27,913	30,108	29,542	28,747	32,188	35,620	34,724	36,719	40,715	41,338	45,571	47,588	47,500	48,500
Corporation income taxes	9,678	11,195	10,448	14,106	21,225	21,238	21,101	17,861	20,880	21,167	20,074	17,309	21,494	20,954	20,523	21,579	23,700	25,800
Excise taxes	7,356	7,502	7,549	8,648	8,851	9,868	9,945	9,131	9,929	10,534	10,638	10,578	11,676	11,860	12,534	13,194	13,699	14,491
Employment taxes	2,388	2,476	2,881	3,928	4,563	4,980	5,382	6,166	7,228	7,520	8,565	8,767	11,067	12,405	12,561	14,862	16,777	16,996
Estate and gift taxes	890	780	698	708	818	881	934	924	1,161	1,365	1,393	1,333	1,606	1,896	2,016	2,167	2,335	2,740
Customs	403	367	407	609	533	596	542	585	682	735	782	925	1,105	982	1,142	1,205	1,275	1,460
Deposits by States, unemployment insurance	1,007	985	1,098	1,363	1,439	1,371	1,246	1,146	1,330	1,542	1,501	1,701	2,167	2,398	2,729	3,009	2,900	2,825
Veterans life insurance premiums	434	431	440	520	473	428	426	441	441	452	485	478	482	504	501	494	501	499
Other budget and trust receipts	3,895	2,293	1,673	1,865	2,197	2,027	2,508	2,834	3,249	3,171	3,730	3,851	4,766	4,905	4,288	5,641	5,678	6,432
Total, receipts from the public	45.357	41,576	40,940	53,390	68,013	71,495	71,626	67,836	77,087	82,105	81,892	81,660	95,078	97,242	101,865	109,739	114,366	119,742

Source: Bureau of the Budget.

TABLE 5.—*Relationship of Federal, State, and local government receipts to net national product, 1929–63*

[Dollar amounts in billions]

Calendar year	Net national product [1]	Amount			Percent of net national product		
		Total	Federal	State and local [2]	Total	Federal	State and local [2]
1929	$95.8	$11.3	$3.8	$7.5	11.8	4.0	7.8
1930	82.6	10.8	3.0	7.7	13.1	3.6	9.4
1931	68.1	9.5	2.0	7.1	14.0	2.9	10.4
1932	50.9	8.9	1.7	7.3	17.5	3.3	14.3
1933	48.8	9.3	2.7	6.7	19.1	5.5	13.7
1934	57.9	10.5	3.5	6.9	18.1	6.1	11.9
1935	65.3	11.4	4.0	7.4	17.5	6.1	11.3
1936	75.2	12.9	5.0	7.9	17.2	6.6	10.5
1937	83.0	15.4	7.0	8.3	18.6	8.5	10.0
1938	77.4	15.0	6.5	8.5	19.4	8.4	11.0
1939	83.3	15.4	6.7	8.7	18.5	8.0	10.4
1940	92.5	17.7	8.6	9.1	19.1	9.3	9.8
1941	116.8	25.0	15.4	9.6	21.4	13.2	8.2
1942	149.0	32.6	22.9	9.7	21.9	15.4	6.5
1943	181.6	49.2	39.3	9.9	27.1	21.6	5.5
1944	199.4	51.2	41.0	10.2	25.7	20.6	5.1
1945	201.0	53.2	42.5	10.7	26.5	21.1	5.3
1946	200.0	51.1	39.2	11.9	25.6	19.6	6.0
1947	221.3	57.1	43.3	13.8	25.8	19.6	6.2
1948	244.0	59.2	43.4	15.8	24.3	17.8	6.5
1949	240.8	56.4	39.1	17.4	23.4	16.2	7.2
1950	265.5	69.3	50.2	19.1	26.1	18.9	7.2
1951	307.0	85.5	64.5	21.0	27.9	21.0	6.8
1952	323.0	90.6	67.7	22.9	28.0	21.0	7.1
1953	338.9	94.9	70.3	24.6	28.0	20.7	7.3
1954	334.3	90.0	63.8	26.2	26.9	19.1	7.8
1955	365.5	101.4	72.8	28.7	27.7	19.9	7.9
1956	384.8	109.5	77.5	31.9	28.5	20.1	8.3
1957	405.3	116.3	81.7	34.5	28.7	20.2	8.5
1958	405.9	115.1	78.5	36.6	28.4	19.3	9.0
1959	441.7	130.2	90.3	39.9	29.5	20.4	9.0
1960	459.6	140.6	96.6	44.1	30.6	21.0	9.6
1961 [3]	473.9	145.5	98.2	47.3	30.7	20.7	10.0
1962 [3]	505.4	156.8	105.4	51.3	31.0	20.9	10.2
1963 [3]	533.4	168.8	113.3	55.5	31.6	21.2	10.4

[1] Net national product is equal to gross national product less capital consumption allowances.
[2] State and local receipts have been adjusted to exclude Federal grants-in-aid.
[3] Preliminary.

NOTE.—The receipts in this table are on the national income and product account basis of the Department of Commerce and therefore differ from both "administrative" and "cash" receipts as defined in the budget message. In this table, receipts of trust funds and taxes other than corporation taxes are on a cash basis and receipts from corporation taxes are on an accrual basis.

Source: Department of Commerce.

TABLE 6.—*Relationship of Federal, State, and local government expenditures to gross national product, 1929–63*

[Dollar amounts in billions]

Calendar year	Gross national product	Amount			Percent of gross national product		
		Total	Federal	State and local [1]	Total	Federal	State and local [1]
1929	$104.4	$10.2	$2.6	$7.6	9.8	2.5	7.3
1930	91.1	11.0	2.8	8.3	12.1	3.1	9.1
1931	76.3	12.3	4.2	8.1	16.1	5.5	10.6
1932	58.5	10.6	3.2	7.4	18.1	5.5	12.6
1933	56.0	10.7	4.0	6.7	19.1	7.1	12.0
1934	65.0	12.8	6.4	6.4	19.7	9.8	9.8
1935	72.5	13.3	6.5	6.8	18.3	9.0	9.4
1936	82.7	15.9	8.5	7.4	19.2	10.3	8.9
1937	90.8	14.8	7.2	7.6	16.3	7.9	8.4
1938	85.2	16.6	8.5	8.1	19.5	10.0	9.5
1939	91.1	17.5	9.0	8.6	19.2	9.9	9.4
1940	100.6	18.5	10.1	8.4	18.4	10.0	8.3
1941	125.8	28.8	20.5	8.2	22.9	16.3	6.5
1942	159.1	64.0	56.1	7.9	40.2	35.3	5.0
1943	192.5	93.4	86.0	7.4	48.5	44.7	3.8
1944	211.4	103.1	95.6	7.5	48.8	45.2	3.5
1945	213.6	92.9	84.8	8.1	43.5	39.7	3.8
1946	210.7	47.0	37.0	10.0	22.3	17.6	4.7
1947	234.3	43.8	31.1	12.7	18.7	13.3	5.4
1948	259.4	51.0	35.4	15.6	19.7	13.6	6.0
1949	258.1	59.5	41.6	17.9	23.1	16.1	6.9
1950	284.6	61.1	41.0	20.1	21.5	14.4	7.1
1951	329.0	79.4	58.0	21.3	24.1	17.6	6.5
1952	347.0	94.4	71.6	22.8	27.2	20.6	6.6
1953	365.4	102.0	77.7	24.3	27.9	21.3	6.7
1954	363.1	96.7	69.6	27.2	26.6	19.2	7.5
1955	397.5	98.6	68.9	29.7	24.8	17.3	7.5
1956	419.2	104.3	71.8	32.4	24.9	17.1	7.7
1957	442.8	115.3	79.7	35.5	26.0	18.0	8.0
1958	444.5	126.6	87.9	38.7	28.5	19.8	8.7
1959	482.7	131.6	91.4	40.3	27.3	18.9	8.3
1960	502.6	136.7	93.1	43.7	27.2	18.5	8.7
1961 [2]	518.2	150.2	102.8	47.4	29.0	19.8	9.1
1962 [2]	554.9	160.7	109.8	51.0	29.0	19.8	9.2
1963 [2]	585.1	170.5	116.1	54.4	29.1	19.8	9.3

[1] State and local expenditures have been adjusted to exclude Federal grants-in-aid, which are included in Federal expenditures.
[2] Preliminary.

NOTE.—The expenditures in this table are on the national income and product account basis of the Department of Commerce and therefore differ from budget receipts and expenditures as defined in the budget message. These accounts, like the cash budget, include the transactions of the trust accounts. Unlike both the conventional budget and the cash statement, they exclude certain capital and lending transactions. In general, they do not use the cash basis for transactions with business. Instead, corporate profits taxes are included in receipts on an accrual instead of a cash basis; expenditures are timed with the delivery instead of the payment for goods and services; and CCC guaranteed price-support crop loans financed by banks are counted as expenditures when the loans are made, not when CCC redeems them.

Source: Department of Commerce.

TABLE 7.—*Tax collections: State, local, and all governments, selected fiscal years, 1902–62* [1]

Fiscal year	All governments—Federal, State, and local		State and local governments combined [2]			State governments [2]			Local governments		
	Total	Per capita [3]	Total	Percent of all governments	Per capita [3]	Total	Percent of all governments	Per capita [3]	Total	Percent of all governments	Per capita [3]
	Millions		*Millions*			*Millions*			*Millions*		
1902	$1,373	$17.34	$860	62.6	$10.86	$156	11.4	$1.97	$704	51.3	$8.89
1913	2,271	23.36	1,609	70.8	16.55	301	13.3	3.10	1,308	57.6	13.45
1922	7,387	67.12	4,016	54.4	36.49	947	12.8	8.60	3,069	41.5	27.89
1929	9,976	81.98	6,436	64.5	52.85	1,951	19.6	16.02	4,485	45.0	38.86
1932	7,977	63.90	6,164	77.3	49.38	1,890	23.7	15.14	4,274	53.6	34.24
1936	10,583	82.64	6,701	63.3	52.33	2,618	24.7	20.44	4,083	38.6	31.89
1940	12,688	96.03	718,0	61.6	59.11	3,313	26.1	25.07	4,497	35.4	34.04
1942	20,793	154.18	8,528	41.0	63.24	3,903	18.8	28.94	4,625	22.2	34.03
1944	49,095	354.76	8,774	17.9	63.40	4,071	8.3	28.91	4,703	9.6	34.94
1945	50,075	357.86	9,193	18.4	65.70	4,307	8.6	30.78	4,886	9.8	34.92
1946	46,380	328.05	10,094	21.8	71.39	4,937	10.6	34.92	5,157	11.1	36.47
1947	46,642	323.62	11,554	24.8	80.17	5,721	12.3	39.69	5,833	12.5	40.47
1948	51,218	349.31	13,342	26.0	90.99	6,743	13.2	45.99	6,599	12.9	45.00
1949	50,358	337.55	14,790	29.4	99.14	7,376	14.6	49.44	7,414	14.7	49.70
1950	51,100	336.90	15,914	31.1	104.92	7,930	15.5	52.28	7,984	15.6	52.64
1951	63,585	411.94	17,554	27.6	113.73	8,933	14.0	57.87	8,621	13.6	55.85
1952	79,066	503.49	19,323	24.4	123.06	9,856	12.5	62.77	9,466	12.0	60.29
1953	83,704	524.32	20,908	25.0	130.98	10,552	12.6	66.10	10,356	12.4	64.88
1954	84,476	520.12	22,067	26.1	135.87	11,089	13.1	68.27	10,978	13.0	67.60
1955	81,072	491.05	23,483	29.0	142.24	11,597	14.3	70.24	11,886	14.7	71.99
1956	91,593	547.61	26,368	28.8	157.65	13,375	14.6	79.97	12,992	14.2	77.68
1957	98,632	578.91	28,817	29.2	169.14	14,531	14.7	85.32	14,286	14.5	83.90
1958	98,387	567.62	30,380	30.9	175.27	14,919	15.2	86.09	15,461	15.7	89.25
1959	99,636	564.46	32,379	32.5	183.43	15,848	15.9	89.85	16,531	16.6	93.74
1960	113,120	628.50	36,117	31.9	200.67	18,036	15.9	100.21	18,081	16.0	100.46
1961	116,331	635.54	38,861	33.4	212.31	19,057	16.4	104.09	19,606	16.9	108.22
1962 [4]	123,785	666.15	41,523	33.5	223.46	20,561	16.6	110.65	20,963	16.9	112.81

[1] Exclusive of social insurance contributions.
[2] Includes the District of Columbia.
[3] Based on estimate of population of continental United States as of July 1. For 1940–55 includes Armed Forces overseas.
[4] Preliminary.

Source: Bureau of the Census, "Governmental Finances and Governmental Finances in the United States, 1902 to 1959," and "Summary of Governmental Finances in 1961," and Treasury Department, Annual Report of the Secretary of the Treasury.

TABLE 8.—*Expenditures for new plant and equipment (excluding agriculture), in current prices and constant 1954 dollars, in relation to gross national product, 1946–63*

Year	Expenditures for new plant and equipment (billions of dollars)		Gross national product (billions of dollars)		Expenditures for new plant and equipment as a percent of gross national product	
	Current prices	Constant (1954) dollars	Current prices	Constant (1954) dollars	Current prices	Constant (1954) dollars
1946	$14.8	$22.7	$210.7	$282.5	7.0	8.0
1947	20.6	27.1	234.3	282.3	8.8	9.6
1948	22.1	26.5	259.4	293.1	8.5	9.0
1949	19.3	22.6	258.1	292.7	7.5	7.7
1950	20.6	23.5	284.6	318.1	7.2	7.4
1951	25.6	26.8	329.0	341.8	7.7	7.8
1952	26.5	27.3	347.0	353.5	7.6	7.7
1953	28.3	28.6	365.4	369.0	7.7	7.8
1954	26.8	26.8	363.1	363.1	7.4	7.4
1955	28.7	27.8	397.5	392.7	7.2	7.1
1956	35.1	32.0	419.2	400.9	8.4	8.0
1957	37.0	31.9	442.8	408.6	8.4	7.8
1958	30.5	25.6	444.5	401.3	6.9	6.4
1959	32.5	26.9	482.7	428.6	6.7	6.3
1960	35.7	29.4	502.6	439.9	7.1	6.7
1961 [1]	34.4	28.2	518.2	447.7	6.6	6.3
1962 [1]	37.3	30.4	554.9	474.8	6.7	6.4
1963 [1]	39.2	31.7	585.1	492.9	6.7	6.4

[1] Preliminary.

Source: Joint Economic Committee; 86th Cong., 1st sess., Staff Report on Employment, Growth, and Price Levels; U.S. Income and Output, Supplement to the Survey of Current Business; and Business News Reports, U.S. Department of Commerce.

TABLE 9.—*Business cycle reference dates and duration of expansions and contractions in the United States: 1904–61*

Business cycle reference dates		Duration in months			
Trough	Peak	Contraction (trough from previous peak)	Expansion (trough to peak)	Cycle: Trough from previous trough	Cycle: Peak from previous peak
August 1904	May 1907	23	33	44	56
June 1908	January 1910	13	19	46	32
January 1912	January 1913	24	12	43	36
December 1914	August 1918	23	*44*	35	*67*
March 1919	January 1920	*7*	10	*51*	17
July 1921	May 1923	18	22	28	40
July 1924	October 1926	14	27	36	41
November 1927	August 1929	13	21	40	34
March 1933	May 1937	43	50	64	93
June 1938	February 1945	13	*80*	63	*93*
October 1945	November 1948	*8*	37	*88*	45
October 1949	July 1953	11	*45*	48	*56*
August 1954	July 1957	*13*	35	*58*	48
April 1958	May 1960	9	25	44	34
February 1961		9		34	
Average, all cycles:					
10 cycles, 1919–61		15	35	50	[1] 54
4 cycles, 1945–61		10	36	46	[2] 46
Average, peacetime cycles:					
8 cycles, 1919–61		16	28	45	[3] 48
3 cycles, 1945–61		10	32	42	[4] 42

[1] 9 cycles, 1920–60.
[2] 4 cycles, 1945–60.
[3] 7 cycles, 1920–60.
[4] 3 cycles, 1945–60.

NOTE.—Italic figures are the wartime expansions (World Wars I and II, and Korean war), the postwar contractions, and the full cycles that include the wartime expansions.

Source: National Bureau of Economic Research.

TABLES

INDIVIDUAL INCOME TAXES

TABLE 10.—*Individual income tax returns, 1913–61*

PART I.—NUMBER OF RETURNS, ADJUSTED GROSS INCOME, TAXABLE INCOME, AND TAX, 1944-61

Income year	Number of returns			Returns with adjusted gross income					Returns with no adjusted gross income	
	Total	Taxable	Nontaxable	Number		Adjusted gross income	Taxable income	Income tax (after credits)	Number	Adjusted gross deficit
				Total	Taxable					
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
						Thousands	*Thousands*	*Thousands*		*Thousands*
1961	61,499,420	48,582,765	12,916,655	61,067,589	48,582,765	$330,935,737	$181,779,732	$42,225,498	431,831	$1,074,453
1960	61,027,931	48.060,985	12,966,946	60,592,712	48,060,985	316,557,566	171,627,771	39,464,156	435,219	1,091,184
1959	60,271,297	47,496,913	12,774,394	59,838,162	47,496,913	306,616,924	166,540,616	38,645,299	433,135	1,521,945
1958	59,085,182	45,652.134	13,433,048	58,700,924	45,652,134	282,166.418	149,337,414	34,335,652	384,258	1,012,326
1957	59,825,121	46,865,315	12,959,806	59,407,673	46,865,315	281,308,431	149,363,077	34,393,639	417,448	987,865
1956	59,197.004	46.258.646	12,938,358	58,798,843	46,258,646	268,583,814	141,532,061	32,732,132	398,161	859,546
1955	58,250,188	44,689,065	13,561,123	57,818,164	44,689,065	249,429,182	128,020,111	29,613,722	432,024	898,865
1954	56,747,008	42,633,060	14,113.948	56,306,704	42.633,060	230,235.855	115,331,301	26,665,753	440,304	1,014,480
1953	57,838,184	45,223.151	12,615,033	57,415,885	44,159,622	229,863,409	------------	29,430,659	422,299	1,165,153
1952	56,528,817	43,876,273	12,652,544	56,107,089	42,833,675	216,087,449	------------	27,802,831	421,728	797,541
1951	55,447,009	42,648,610	12,798.399	55.042,597	41,594,222	203.097,033	------------	24,227,780	404,412	760.548
1950	53,060,098	38,186,682	14,873,416	52,655,564	38,186,682	179,874,478	------------	18,374,922	404,534	726,202
1949	51,814,124	35,628,295	16,185,829	51,301,910	35,628,295	161,373,205	------------	14,538,141	512,214	799,280
1948	52,072,006	36,411,248	15,660,758	51,745,697	36,411,248	164,173,861	------------	15,441,529	326,309	657,847
1947	55,099,008	41,578,524	13,520,484	54,799,936	41,578,524	150,295,275	------------	18,076,281	299,072	559,193
1946	52,816,547	37,915,696	14,900,851	52,600,470	37,915,696	134,330,006	------------	16,075,913	216,077	247,206
1945	49,932,783	42,650,502	7,282,281	49,750,991	42,650,502	120,301,131	------------	17,050,378	181,792	292,472
1944	47,111,495	42,354,468	4,757,027	46,919,590	42,354,463	116,714,736	------------	16,216,401	191,905	249,771

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Income year	Returns with net income[1]					
	Number of returns			Total income	Net income[2]	Income tax[3]
	Total	Taxable	Nontaxable			
	(1)	(2)	(3)	(4)	(5)	(6)
				Thousands	*Thousands*	*Thousands*
1943	43,506,553	40,222,699	3,283,854	$106,614,214	$99,209,862	$14,449,441
1942	36,456,110	27,637,051	8,819,059	85,876,118	78,589,729	8,823,041
1941	25,170,089	17,502,587	8,267,502	63,841,047	58,527,217	3,815,415
1940	14,598,074	7,437,261	7,160,813	40,277,645	36,309,719	1,440,967
1939	7,570,320	3,896,418	3,673,902	25,816,147	22,938,918	890,934
1938	6,150,776	2,995,664	3,155,112	21,549,277	18,660,929	726,120
1937	6,301,833	3,326,912	2,974,921	23,891,481	20,941,302	1,093,163
1936	5,413,499	2,861,108	2,552,391	21,888,373	19,240,110	1,214,017
1935	4,575,012	2,110,890	2,464,122	17,316,505	14,909,812	657,439
1934	4,094,420	1,795,920	2,298,500	15,092,960	12,796,802	511,400
1933	3,723,558	1,747,740	1,975,818	13,393,825	11,008,638	374,120
1932	3,877,430	1,936,095	1,941,335	14,392,080	11,655,909	329,962
1931	3,225,924	1,525,546	1,700,378	17,268,451	13,604,996	246,127
1930	3,707,509	2,037,645	1,669,864	22,319,446	18,118,635	476,715
1929	4,044,327	2,458,049	1,586.278	29,844,758	24,800,736	1,001,938
1928	4,070,851	2,523,063	1,547,788	28,987,634	25,226,327	1,164,254
1927	4,101,547	2,440,941	1,660,606	26,208,561	22,545,091	830,639
1926	4,138,092	2,470,990	1,667,102	25,447,436	21,958,506	732,471
1925	4,171,051	2,501,166	1,669,885	25,272,035	21,894,576	734,555
1924	7,369,788	4,489,698	2,880,090	29,578,997	25,656,153	704,265
1923	7,698,321	4,270,121	3,428,200	29,247,593	24,777,466	661,666
1922	6,787,481	3,681,249	3,106,232	24,871,908	21,336,213	861,057
1921	6,662,176	3,589,985	3,072,191	23,328,782	19,577,213	719,387
1920	7,259,944	5,518,310	1,741,634	26,690,270	23,735,629	1,075,054
1919	5,332,760	4,231,181	1,101,579	22,437,686	19,859,491	1,269,630
1918	4,425,114	3,392,863	1,032,251	17,745,761	15,924,639	1,127,722
1917	3,472,890	2,707,234	765,656	[5] 14,538,146	13,407,303	691,493
1916	437,036	362,970	74,066	8,349,902	6,298,578	173,387
1915	336,652	([4])	([4])	([4])	4,600,000	67,944
1914	357,515	([4])	([4])	([4])	4,000,000	41,046
1913[6]	357,598	([4])	([4])	([4])	3,900,000	28,254

Income year	Returns with no net income			
	Number of returns	Total income	Net deficit	Tax
	(7)	(8)	(9)	(10)
		Thousands	*Thousands*	*Thousands*
1943	215,485	$170,866	$225,683	$643
1942	163,136	181,486	198,598	----------
1941	99,828	264,032	292,023	2,326
1940	112,697	239,583	311,385	473
1939	82,461	228,690	284,327	300
1938	100,233	318,769	354,156	615
1937	83,904	250,394	308,518	----------
1936	73,272	248,530	286,632	----------
1935	94.609	288,653	381,353	----------
1934	104,170	344,055	412,859	----------
1933	168,449	725,817	1,141,331	----------
1932	206,293	831,592	1,480,922	----------
1931	184,583	1,299,750	1,936,878	----------
1930	144,867	1,204,383	1,539,452	----------
1929	92,545	902,251	1,025,130	----------
1928	72,829	420,649	499,213	----------
1927	([4])	([4])	([4])	----------
1926	([4])	([4])	([4])	----------
1925	([4])	([4])	([4])	----------
1924	([4])	([4])	([4])	----------
1923	([4])	([4])	([4])	----------
1922	([4])	([4])	([4])	----------
1921	([4])	([4])	([4])	----------
1920	([4])	([4])	([4])	----------
1919	([4])	([4])	([4])	----------
1918	([4])	([4])	([4])	----------
1917	([4])	([4])	([4])	----------
1916	([4])	([4])	([4])	----------
1915	([4])	([4])	([4])	----------
1914	([4])	([4])	([4])	----------
1913[6]	([4])	([4])	([4])	----------

[1] Includes fiduciary returns with net income filed on form 1040, 1913–36.
[2] For 1941–43, total income on form 1040A was also used as net income.
[3] Tax for 1924–31, after earned income credit and capital loss credit; 1932–33, after capital loss credit only; 1943, after foreign tax credit and tax paid at source. Tax for 1940–41 includes defense tax and for 1943, victory tax.
[4] Not available.
[5] Somewhat understated because net income was used also as total income on returns with income of $1,000 to $2,000.
[6] Data pertain to last 10 months of year.

Source: Internal Revenue Service: Statistics of Income—1961, Individual Income Tax Returns.

TABLE 11.—*Personal income, adjusted gross income, individual income tax base, and income tax, 1945–61*

[Dollar amounts in billions]

Calendar year	Personal income [1]	Adjusted gross income [2]	Individual income tax base [3]		Income tax after credits
			Amount	As percent of personal income	
1945	$171.2	$117.6	$52.3	30.5	$17.1
1946	179.3	118.1	65.2	36.4	16.1
1947	191.6	135.3	75.4	39.4	18.1
1948	210.4	142.1	74.7	35.5	15.4
1949	208.3	138.6	71.6	34.4	14.5
1950	228.5	158.5	84.3	36.9	18.4
1951	256.7	183.2	97.1	37.8	24.2
1952	273.1	196.6	107.4	39.3	27.8
1953	288.3	210.5	115.5	40.1	29.4
1954	289.8	209.7	115.2	39.8	26.7
1955	310.2	229.6	127.9	41.2	29.6
1956	332.9	249.6	141.4	42.5	32.7
1957	351.4	262.2	149.2	42.5	34.4
1958	360.3	262.2	149.2	41.4	34.3
1959	383.9	287.8	166.4	43.3	38.6
1960	401.3	297.2	171.5	42.7	39.5
1961	417.6	311.3	181.6	43.5	42.2

[1] Department of Commerce concept.
[2] Individual returns with income tax liability.
[3] Income subject to surtax or alternative tax on capital gains. Excludes fiduciaries.

Source: Internal Revenue Service: Statistics of Income; Department of Commerce; Treasury Department, Office of Tax Analysis.

TABLE 12.—*Individual income tax returns: Number of returns, adjusted gross income, taxable income, and income tax, by adjusted gross income classes, 1961*

[Dollar amounts in thousands]

Adjusted gross income classes	Number of returns (1)	Adjusted gross income (2)	Taxable income (3)	Income tax after credits (4)
Taxable returns:				
$600 under $1,000	1,385,033	$1,156,177	$203.641	$40,683
$1,000 and under $3,000	9,005,107	18,392,079	7,769.784	1,538,895
$3,000 and under $5,000	11,716,380	47,176,117	22,297,013	4,478,541
$5,000 and under $10,000	20.477,578	143.170,239	77,929,046	15,936,076
$10,000 and under $15,000	4,118,486	48.473,930	32,440,908	6,950,821
$15,000 and under $20,000	888,100	15,126,018	11,030,651	2,576,761
$20,000 and under $50,000	852,327	24,485,963	19,197,768	5,611,955
$50,000 and under $100,000	110,192	7,249,539	5,927,647	2,483,556
$100,000 and over	29,562	6,053,297	4,838,239	2.608,210
Total taxable returns	48,582,765	311,283,359	181,634,697	42,225,498
Nontaxable returns:				
Under $1,000	6,034,762	[1] 1,461,033	255	-------------
$1,000 and under $3,000	5,003,656	9,165,135	70,769	-------------
$3,000 and over	1,878,237	7,951,757	74,011	-------------
Total nontaxable returns	12,916,655	[1] 18,577,925	145,035	-------------
Total all returns	61,499,420	[1] 329,861,284	181,779,732	42,225,498
	Percentage distribution			
Taxable returns:				
$600 and under $1,000	2.3	0.4	0.1	0.1
$1,000 and under $3,000	14.6	5.6	4.3	3.6
$3,000 and under $5,000	19.1	14.3	12.3	10.6
$5,000 and under $10,000	33.3	43.4	42.9	37.7
$10,000 and under $15,000	6.7	14.7	17.8	16.5
$15,000 and under $20,000	1.4	4.6	6.1	6.1
$20,000 and under $50,000	1.4	7.4	10.6	13.3
$50,000 and under $100,000	.2	2.2	3.3	5.9
$100,000 and over	[2]	1.8	2.7	6.2
Total taxable returns	79.0	94.4	99.9	100.0
Nontaxable returns:				
Under $1,000	9.8	.4	[2]	-------------
$1,000 and under $3,000	8.1	2.8	[2]	-------------
$3,000 and over	3.1	2.4	[2]	-------------
Total nontaxable returns	21.0	5.6	.1	-------------
Total all returns	100.0	100.0	100.0	100.0

[1] Adjusted gross income less deficit.
[2] Less than 0.05 percent.

Source: Internal Revenue Service: Statistics of Income—1961, Individual Income Tax Returns.

TABLE 13.—*Individual income tax returns: Sources of income by adjusted gross income classes, 1961*

Adjusted gross income classes	Salaries and wages (net)	Dividends (after exclusions)	Interest received	Net profit (or loss) from—		Net gain (or loss) from sales of capital assets	Pensions and annuities	Net income (or loss) from—		Other sources [1]	Adjusted gross income
				Business or profession	Partnership			Rents and royalties	Estates and trusts		
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
	Thousands of dollars										
Taxable returns:											
$600 under $1,000	1,052,734	12,457	13,003	43,801	5,947	4,504	1,447	7,740	3,029	11,515	1,156,177
$1,000 and under $3,000	15,865,996	202,958	337,175	1,133,302	156,483	138,860	141,762	196,913	26,549	192,081	18,392,079
$3,000 and under $5,000	41,499,836	414,700	615,928	2,804,633	507,981	307,008	356,122	311,175	38,388	320,346	47,176,117
$5,000 and under $10,000	129,694,712	1,235,541	1,468,702	6,246,184	1,681,227	893,574	444,879	660,590	118,248	726,582	143,170,239
$10,000 and under $15,000	40,448,291	1,026,176	775,525	3,317,800	1,250,086	706,069	140,845	390,155	84,665	334,318	48,473,930
$15,000 and under $20,000	9,836,806	790,044	403,202	2,106,460	928,028	514,124	59,326	243,276	60,803	183,949	15,126,018
$20,000 and under $50,000	11,009,126	2,428,554	820,380	4,636,811	2,833,087	1,511,117	99,463	584,185	139,144	424,096	24,485,963
$50,000 and under $100,000	2,452,091	1,311,215	252,488	917,015	1,022,735	896,315	30,210	177,033	55,774	134,663	7,249,539
$100,000 and over	1,022,477	1,892,012	164,706	80,533	504,061	2,178,690	17,125	87,563	61,214	44,916	6,053,297
Total taxable returns	252,882,069	9,313,657	4,851,109	21,286,539	8,889,635	7,150,261	1,291,179	2,658,630	587,814	2,372,466	311,283,359
Nontaxable returns:											
Under $1,000	2,132,779	89,562	172,517	[2] 741,583	[2] 196,552	123,476	32,583	92,353	3,186	[2] 247,288	1,461,033
$1,000 and under $3,000	5,933,324	214,455	472,012	1,272,181	119,461	165,789	388,249	389,670	18,299	191,695	9,165,135
$3,000 and over	5,954,107	272,069	187,529	812,569	136,301	181,268	148,182	123,293	19,730	116,709	7,951,757
Total nontaxable returns	14,020,210	576,086	832,058	1,343,167	59,210	470,533	569,014	605,316	41,215	61,116	18,577,925
Total all returns	266,902,279	9,889,743	5,683,167	22,629,706	8,948,845	7,620,794	1,860,193	3,263,946	629,029	2,433,582	329,861,284

	Percentage distribution										
Taxable returns:											
$600 and under $1,000	0.4	0.1	0.2	0.2	0.1	0.1	0.1	0.2	0.5	0.5	0.4
$1,000 and under $3,000	5.9	2.1	5.9	5.0	1.8	1.8	7.6	6.0	4.2	7.9	5.6
$3,000 and under $5,000	15.5	4.2	10.8	12.4	5.7	4.0	19.1	9.5	6.1	13.2	14.3
$5,000 and under $10,000	48.6	12.5	25.8	27.6	18.8	11.7	23.9	20.2	18.8	29.9	43.4
$10,000 and under $15,000	15.2	10.4	13.6	14.7	14.0	9.3	7.6	12.0	13.5	13.7	14.7
$15,000 and under $20,000	3.7	8.0	7.1	9.3	10.4	6.7	3.2	7.5	9.7	7.6	4.6
$20,000 and under $50,000	4.1	24.6	14.4	20.5	31.7	19.8	5.3	17.9	22.1	17.4	7.4
$50,000 and under $100,000	.9	13.3	4.4	4.1	11.4	11.8	1.6	5.4	8.9	5.6	2.2
$100,000 and over	.4	19.1	2.9	.4	5.6	28.6	.9	2.7	9.7	1.8	1.8
Total taxable returns	94.7	94.2	85.4	94.1	99.3	93.8	69.4	81.5	93.4	97.5	94.4
Nontaxable returns:											
Under $1,000	.8	.9	3.0	[2] 3.3	[2] 2.2	1.6	1.8	2.8	.5	[2] 10.2	.4
$1,000 and under $3,000	2.2	2.2	8.3	5.6	1.3	2.2	20.9	11.9	2.9	7.9	2.8
$3,000 and over	2.2	2.8	3.3	3.6	1.5	2.4	8.0	3.8	3.1	4.8	2.4
Total nontaxable returns	5.3	5.8	14.6	5.9	.7	6.2	30.6	18.5	6.6	2.5	5.6
Total all returns	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

[1] Includes sales of property other than capital assets, net operating loss deduction, "other" income on Schedule B and sources not supported by Schedule B.
[2] Net loss exceeded net profit or net income.

Source: Internal Revenue Service: Statistics of Income—1961, Individual Income Tax Returns.

TABLE 14.—*Individual income tax returns: Sources of income as percent of adjusted gross income, by adjusted gross income classes, 1961*]

[In percent]

Adjusted gross income classes	Adjusted gross income	Salaries and wages (net)	Dividends (after exclusions)	Interest received	Net profit (or loss) from—		Net gain (or loss) from sales of capital assets	Pensions and annuities	Net income (or loss) from—		Other sources [1]
					Business or profession	Partnership			Rents and royalties	Estates and trusts	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
Taxable returns:											
$600 under $1,000	100.0	91.1	1.1	1.1	3.8	0.5	0.4	0.1	0.7	0.3	1.0
$1,000 and under $3,000	100.0	86.3	1.1	1.8	6.2	.9	.8	.8	1.1	.1	1.0
$3,000 and under $5,000	100.0	88.0	.9	1.3	5.9	1.1	.7	.8	.7	.1	.7
$5,000 and under $10,000	100.0	90.6	.9	1.0	4.4	1.2	.6	.3	.5	.1	.5
$10,000 and under $15,000	100.0	83.4	2.1	1.6	6.8	2.6	1.5	.3	.8	.2	.7
$15,000 and under $20,000	100.0	65.0	5.2	2.7	13.9	6.1	3.4	.4	1.6	.4	1.2
$20,000 and under $50,000	100.0	45.0	9.9	3.4	18.9	11.6	6.2	.4	2.4	.6	1.7
$50,000 and under $100,000	100.0	33.8	18.1	3.5	12.6	14.1	12.4	.4	2.4	.8	1.9
$100,000 and over	100.0	16.9	31.3	2.7	1.3	8.3	36.0	.3	1.4	1.0	.7
Total taxable returns	100.0	81.2	3.0	1.6	6.8	2.9	2.3	.4	.9	.2	.8
Nontaxable returns:											
Under $1,000	100.0	146.0	6.1	11.8	[2] 50.8	[2] 13.5	8.5	2.2	6.3	.2	[2] 16.9
$1,000 and under $3,000	100.0	64.7	2.3	5.2	13.9	1.3	1.8	4.2	4.3	.2	2.1
$3,000 and over	100.0	74.9	3.4	2.4	10.2	1.7	2.3	1.9	1.6	.2	1.5
Total nontaxable returns	100.0	75.5	3.1	4.5	7.2	.3	2.5	3.1	3.3	.2	.3
Total all returns	100.0	80.9	3.0	1.7	6.9	2.7	2.3	.6	1.0	.2	.7

[1] Includes sales of property other than capital assets, net operating loss deduction, "other" income on schedule B and sources not supported by schedule B.
[2] Net loss exceeded net profit or net income.

Source: Internal Revenue Service: Statistics of Income—1961, Individual Income Tax Returns.

TABLE 15.—*Individual income tax returns: Percent of returns reporting each source of income, by adjusted gross income classes, 1961*

Adjusted gross income classes	Total number of returns	Percent of returns with—								
		Salaries and wages (net)	Dividends (after exclusions)	Interest received	Net profit (or loss) from—		Net gain (or loss) from sales of capital assets	Pensions and annuities	Net income (or loss) from—	
					Business or profession	Partnership			Rents and royalties	Estates and trusts
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Taxable returns:										
$600 and under $1,000	1,385,033	92.6	2.2	2.2	3.8	0.8	2.0	0.2	1.6	0.4
$1,000 and under $3,000	9,005,107	89.5	3.8	8.6	10.3	1.3	4.3	1.5	5.1	.4
$3,000 and under $5,000	11,716,380	91.3	4.9	11.4	12.8	1.9	6.1	1.9	7.6	.4
$5,000 and under $10,000	20,477,578	94.3	7.3	17.3	11.0	2.7	8.6	1.3	10.5	.6
$10,000 and under $15,000	4,118,486	90.6	20.6	36.1	14.3	6.3	21.7	1.9	15.8	1.5
$15,000 and under $20,000	888,100	78.7	44.3	57.9	24.7	14.5	44.1	3.3	23.4	4.0
$20,000 and under $50,000	852,327	67.2	65.2	72.2	32.6	26.6	63.3	4.8	31.7	6.8
$50,000 and under $100,000	110,192	64.5	86.7	82.9	30.2	38.9	83.0	7.4	41.0	12.3
$100,000 and over	29,562	64.4	94.4	87.0	25.1	42.0	92.3	10.3	47.0	19.0
Total taxable returns	48,582,765	91.5	9.0	17.4	12.1	3.2	10.0	1.6	9.7	.8
Nontaxable returns:										
Under $1,000	6,034,762	76.2	2.9	7.5	19.3	2.0	5.4	.9	7.7	.4
$1,000 and under $3,000	5,003,656	68.8	7.4	18.2	25.0	2.3	9.0	7.0	14.3	.6
$3,000 and over	1,878,237	81.5	6.5	12.5	21.5	3.7	9.4	4.1	11.2	.9
Total nontaxable returns	12,916,655	74.1	5.2	12.3	21.8	2.4	7.4	3.7	10.7	.5
Total all returns	61,499,420	87.8	8.2	16.3	14.2	3.1	9.4	2.1	9.9	.7

Source: Internal Revenue Service: Statistics of Income—1961, Individual Income Tax Returns.

TABLE 16.—*Individual income tax returns: Number of returns, number of exemptions, returns with standard deduction, and returns with itemized deductions, by adjusted gross income classes, 1961*

Adjusted gross income classes	Total returns				Returns with standard deduction				Returns with itemized deductions			
	Number of returns	Number of exemptions			Number of returns	Percent of total returns [1]	Number of exemptions	Percent of total exemptions [1]	Number of returns	Percent of total returns [1]	Number of exemptions	Percent of total exemptions [1]
		Total	For age and blindness	For other than age and blindness								
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
Taxable returns:												
$600 and under $1,900	1, 385, 033	1, 385, 033	----------	1, 385, 033	1, 322, 744	95. 5	1, 322, 744	95. 5	62, 289	4. 5	62, 289	4. 5
$1,000 and under $3,000	9, 005, 107	13, 596, 070	567, 747	13, 028, 323	7, 090, 017	78. 7	10, 520, 682	77. 4	1, 915, 090	21. 3	3, 075, 388	22. 6
$3,000 and under $5,000	11, 716, 380	29, 820, 624	1, 080, 737	28, 739, 887	7, 084, 930	60. 5	17, 379, 146	58. 3	4, 631, 450	39. 5	12, 441, 478	41. 7
$5,000 and under $10,000	20, 477, 578	71, 047, 940	1, 215, 020	69, 832, 920	8, 319, 657	40. 6	26, 195, 261	36. 9	12, 157, 921	59. 4	44, 852, 679	63. 1
$10,000 and under $15,000	4, 118, 486	14, 734, 217	290, 009	14, 444, 208	1, 238, 127	30. 1	3, 868, 368	26. 3	2, 880, 359	69. 9	10, 865, 849	73. 7
$15,000 and under $20,000	888, 100	3, 241, 087	113, 561	3, 127, 526	173, 824	19. 6	536, 389	16. 5	714, 276	80. 4	2, 704, 698	83. 5
$20,000 and under $50,000	852, 327	3, 236, 990	169, 659	3, 067, 331	91, 929	10. 8	300, 391	9. 3	760, 398	89. 2	2, 936, 599	90. 7
$50,000 and under $100,000	110, 192	413, 384	33, 589	379, 795	3, 219	2. 9	10, 233	2. 5	106, 973	97. 1	403, 151	97. 5
$100,000 and over	29, 562	105, 159	13, 400	91, 759	381	1. 3	1, 120	1. 1	29, 181	98. 7	104, 039	98. 9
Total taxable returns	48, 582, 765	137, 580, 504	3, 483, 722	134, 096, 782	25, 324, 828	52. 1	60, 134, 334	43. 7	23, 257, 937	47. 9	77, 446, 170	56. 3
Nontaxable returns:												
Under $1,000 [2]	6, 034, 762	10, 357, 701	1, 024, 348	9, 333, 353	5, 408, 798	89. 6	8, 836, 770	85. 3	194, 133	3. 2	315, 531	3. 0
$1,000 and under $3,000	5, 003, 656	18, 160, 015	2, 075, 904	16, 084, 111	3, 984, 821	79. 6	15, 470, 513	85. 2	1, 018, 835	20. 4	2, 689, 502	14. 8
$3,000 and over	1, 878, 237	11, 422, 115	332, 137	11, 089, 978	1, 087, 310	57. 9	7, 520, 125	65. 8	790, 927	42. 1	3, 901, 990	34. 2
Total nontaxable returns [2]	12, 916, 655	39, 939, 831	3, 432, 389	36, 507, 442	10, 480, 929	81. 1	31, 827, 408	80. 0	2, 003, 895	15. 5	6, 907, 023	17. 3
Total, all returns [2]	61, 499, 420	177, 520, 335	6, 916, 111	170, 604, 224	35, 805, 757	58. 2	91, 961, 742	51. 8	25, 261, 832	41. 1	84, 353, 193	47. 5

[1] In adjusted gross income class.
[2] Includes returns with no adjusted gross income which are not classified as either standard or itemized deduction returns and, therefore, details do not necessarily add to totals.

Source: Internal Revenue Service: Statistics of Income—1961, Individual Income Tax Returns.

TABLE 17.—*Individual income tax returns: Returns with itemized deductions as a percent of all returns and the amount of itemized deductions as a percent of adjusted gross income on all returns and on returns with itemized deductions, 1944–61*

Year	Individual returns with itemized deductions		Adjusted gross income on all returns	Returns with itemized deductions			
				Adjusted gross income	Itemized deductions	Itemized deductions as percent of adjusted gross income on—	
	Number	Percent of total number				All returns [1]	Returns with itemized deductions [2]
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
	Millions		*Millions*	*Millions*	*Millions*		
1944	8.4	17.8	$116,465	$32,694	$4,838	4.2	14.8
1945	8.5	17.1	120,301	34,954	5,539	4.6	15.8
1946	8.7	16.5	134,330	39,569	6,290	4.7	15.9
1947	10.4	18.9	149,736	45,862	7,813	5.2	17.0
1948	8.8	16.9	163,516	44,890	7,889	4.8	17.6
1949	9.7	18.7	160,573	46,825	8,780	5.5	18.8
1950	10.3	19.4	179,148	55,116	9,933	5.5	18.0
1951	11.6	20.9	202,336	65,261	11,856	5.9	18.2
1952	12.8	22.7	215,290	73,643	13,557	6.3	18.4
1953	14.4	24.9	228,708	82,871	15,589	6.8	18.8
1954	15.7	27.7	229,221	92,334	17,403	7.6	18.8
1955	16.9	29.0	248,530	108,528	19,997	8.0	18.4
1956	18.5	31.2	267,724	123,719	22,613	8.4	18.3
1957	20.2	33.7	280,321	138,626	25,692	9.2	18.5
1958	20.8	35.2	281,154	145,359	27,498	9.8	18.9
1959	22.5	37.3	305,095	167,413	32,017	10.5	19.1
1960	24.1	39.5	315,466	181,131	35,313	11.2	19.5
1961	25.3	41.1	329,861	196,877	38,391	11.6	19.5

[1] Cols. 5 and 3.
[2] Cols. 5 and 4.

Source: Treasury Department, Office of Tax Analysis.

TABLE 18.—*Individual income tax returns: Itemized deductions by adjusted gross income classes, 1960*

Adjusted gross income classes	Adjusted gross income	Contributions		Interest paid		Taxes		Medical and dental expenses		Other deductions	Total deductions
		Number of returns	Amount	Number of returns	Amount	Number of returns	Amount	Number of returns	Amount		
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
Taxable returns:	*Thousands*		*Thousands*		*Thousands*		*Thousands*		*Thousands*	*Thousands*	*Thousands*
$600 under $1,000	$49,573	49,627	$3,245	11,516	$674	50,159	$2,901	24,647	$2,441	$1,546	$10,807
$1,000 and under $3,000	4,231,422	1,743,677	222,542	883,448	115,852	1,802,993	256,302	1,256,491	283,922	141,793	1,020,411
$3,000 and under $5,000	19,265,075	4,483,099	800,676	3,339,490	819,380	4,635,559	1,112,760	3,161,115	916,100	535,721	4,184,637
$5,000 and under $10,000	81,558,299	11,373,357	2,719,829	10,159,592	4,380,155	11,589,219	4,699,180	6,934,231	2,208,827	1,880,591	15,888,582
$10,000 and under $15,000	29,112,735	2,432,924	935,476	2,165,706	1,363,786	2,452,500	1,644,398	1,161,908	526,059	594,496	5,064,215
$15,000 and under $20,000	10,560,158	610,062	342,695	495,039	388,705	615,917	594,646	248,458	170,738	209,628	1,706,412
$20,000 and under $50,000	19,648,332	670,619	669,917	489,335	558,440	674,631	1,083,054	218,439	246,191	388,938	2,946,540
$50,000 and under $100,000	6,442,264	96,631	272,761	66,159	166,294	97,123	349,563	29,010	56,337	155,333	1,000,288
$100,000 and over	4,833,665	23,856	425,465	16,775	137,783	23,970	261,916	8,809	21,331	146,471	992,966
Total taxable returns	175,701,523	21,483,852	6,392,606	17,627,060	7,931,069	21,942,071	10,004,720	13,043,108	4,431,946	4,054,517	32,814,858
Nontaxable returns:											
Under $1,000	127,230	128,622	11,698	57,734	12,765	142,948	24,548	96,732	32,238	8,872	90,121
$1,000 and under $3,000	2,013,244	841,951	125,646	432,656	133,293	890,172	219,572	698,924	335,351	86,233	900,095
$3,000 and over	3,289,133	651,874	220,376	548,431	339,081	691,254	276,858	513,985	419,650	252,090	1,508,055
Total nontaxable returns	5,429,607	1,622,447	357,720	1,038,821	485,139	1,724,374	520,978	1,309,641	787,239	347,195	2,498,271
Total all returns	181,131,130	23,106,299	6,750,326	18,665,881	8,416,208	23,666,445	10,525,698	14,352,749	5,219,185	4,401,712	35,313,129

	Percentage distribution										
Taxable returns:											
$600 and under $1,000	(1)	0.2	(1)	0.1	(1)	0.2	(1)	0.2	(1)	(1)	(1)
$1,000 and under $3,000	2.3	7.5	3.3	4.7	1.4	7.6	2.4	8.8	5.4	3.2	2.9
$3,000 and under $5,000	10.6	19.4	11.9	17.9	9.7	19.6	10.6	22.0	17.6	12.2	11.9
$5,000 and under $10,000	45.0	49.2	40.3	54.4	52.0	49.0	44.6	48.3	42.3	42.7	45.0
$10,000 and under $15,000	16.1	10.5	13.9	11.6	16.2	10.4	15.6	8.1	10.1	13.5	14.3
$15,000 and under $20,000	5.8	2.6	5.1	2.7	4.6	2.6	5.6	1.7	3.3	4.8	4.8
$20,000 and under $50,000	10.8	2.9	9.9	2.6	6.6	2.9	10.3	1.5	4.7	8.8	8.3
$50,000 and under $100,000	3.6	.4	4.0	.4	2.0	.4	3.3	.2	1.1	3.5	2.8
$100,000 and over	2.7	.1	6.3	.1	1.6	.1	2.5	.1	.4	3.3	2.8
Total taxable returns	97.0	93.0	94.7	94.4	94.2	92.7	95.1	90.9	84.9	92.1	92.9
Nontaxable returns:											
Under $1,000	.1	.6	.2	.3	.2	.6	.2	.7	.6	.2	.3
$1,000 and under $3,000	1.1	3.6	1.9	2.3	1.6	3.8	2.1	4.9	6.4	2.0	2.5
$3,000 and over	1.8	2.8	3.3	2.9	4.0	2.9	2.6	3.6	8.0	5.7	4.3
Total nontaxable returns	3.0	7.0	5.3	5.6	5.8	7.3	4.9	9.1	15.1	7.9	7.1
Total all returns	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

[1] Less than 0.05 percent.

Source: Internal Revenue Service: Statistics of Income—1960, Individual Income Tax Returns.

TABLE 19.—*Individual income tax returns: Income tax generated at each tax rate for all returns and returns under each of the three tax rate schedules, 1961*

Tax rate	Returns with tax rate as marginal rate					Returns with any tax at tax rate		
	Number of returns	Tax base taxed at marginal rate	Tax generated at marginal rate	Tax base taxed at all rates	Tax generated at all rates	Number of returns	Tax base at tax rate	Tax generated at tax rate
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
		Thousands	*Thousands*	*Thousands*	*Thousands*		*Thousands*	*Thousands*
ALL RETURNS								
Total	61, 499, 420	$75, 421, 635	$17, 427, 066	$181,795,111	$42, 714, 640	[1] 61, 499, 420	$181,795,111	$42, 739, 724
0 percent (returns with no tax base)	12, 685, 042					12, 685, 042		
20 percent	28, 446, 871	45, 671, 637	9, 134, 327	45, 763, 324	9, 171, 662	48, 813, 503	111, 232, 759	22, 246, 552
21 percent	524, 793	492, 128	103, 347	1, 542, 091	312, 888	850, 849	1, 144, 240	240, 290
22 percent	13, 792, 788	18, 238, 382	4, 012, 444	63, 903, 174	13, 158, 280	19, 515, 783	36, 507, 592	8, 031, 671
24 percent	209, 237	161, 652	38, 796	1, 000, 331	211, 138	326, 056	395, 290	94, 870
26 percent	3, 670, 107	4, 366, 332	1, 135, 246	27, 388, 704	5, 999, 488	5, 839, 814	11, 470, 190	2, 982, 249
30 percent	1, 011, 057	1, 317, 041	395, 113	10, 980, 453	2, 613, 612	2, 169, 707	5, 249, 091	1, 574, 728
32 percent	11, 114	9, 855	3, 154	122, 096	30, 596	36, 192	60, 011	19, 204
34 percent	391, 826	585, 818	199, 178	5, 977, 377	1, 549, 897	1, 122, 458	3, 126, 958	1, 063, 166
36 percent	6, 206	5, 867	2, 112	81, 859	21, 861	25, 078	43, 611	15, 700
38 percent	216, 345	346, 815	131, 790	4, 253, 988	1, 201, 342	730, 632	2, 138, 845	812, 761
39 percent	3, 955	3, 971	1, 549	60, 975	17, 316	18, 872	33, 805	13, 184
42 percent	2, 878	2, 555	1, 073	49, 746	14, 767	14, 917	26, 633	11, 186
43 percent	142, 690	231, 851	99, 696	3, 358, 805	1, 017, 878	526, 326	1, 553, 545	668, 024
47 percent	97, 632	162, 584	76, 415	2, 703, 304	879, 425	383, 636	1, 144, 442	537, 888
49 percent	1, 358	1, 390	681	32, 847	11, 249	7, 779	14, 232	6, 974
50 percent (returns with capital gains tax only)	808	301, 564	150, 782	301, 564	150, 782	808	301, 564	150, 782
50 percent (returns with capital gains tax and normal tax and surtax)	[2] 107, 951	2, 484, 803	1, 242, 402	[3] 7, 887, 107	[3] 3, 762, 862	107, 951	2, 484, 803	1, 242, 402
50 percent	74, 576	129, 881	64, 941	2, 406, 061	831, 818	278, 225	831, 045	415, 523
52 percent	1, 648	3, 077	1, 600	48, 390	17, 963	6, 421	22, 169	11, 528
53 percent	48, 664	80, 202	42, 507	1, 735, 259	634, 388	203, 649	613, 146	324, 968
54 percent	1, 427	2, 815	1, 520	47, 065	18, 307	4, 773	16, 199	8, 747
56 percent	33, 767	55, 089	30, 850	1, 356, 946	520, 579	154, 985	470, 469	263, 463
58 percent	1, 206	3, 518	2, 040	46, 484	19, 203	3, 346	16, 358	9, 488
59 percent	42, 235	132, 724	78, 307	1, 955, 493	704, 894	121, 218	666, 648	393, 323
62 percent	33, 140	151, 605	93, 995	1, 882, 279	829, 269	81, 123	622, 485	385, 941
65 percent	17, 210	76, 901	49, 986	1, 158, 446	545, 959	46, 490	365, 093	237, 310
66 percent	367	1, 115	736	19, 080	8, 849	1, 493	7, 871	5, 195
68 percent	414	1, 683	1, 144	26, 930	13, 175	1, 126	8, 803	5, 986
69 percent	9, 458	42, 761	29, 505	752, 616	374, 189	29, 280	235, 799	162, 702
71 percent	243	1, 271	902	19, 203	9, 945	712	5, 961	4, 232
72 percent	5, 683	25, 557	18, 401	505, 256	262, 822	19, 822	162, 573	117, 053
74 percent	137	653	483	10, 848	5, 917	469	3, 973	2, 940

75 percent	5,222	37,889	28,417	567,869	309,004	14,139	180,129	135,097
76 percent	70	326	248	6,509	3,681	332	2,946	2,239
78 percent	3,006	22,634	17,655	383,189	219,560	8,917	114,654	89,430
80 percent	51	256	205	5,371	3,147	262	2,366	1,893
81 percent	1,711	12,984	10,517	239,387	143,206	5,911	77,614	62,867
83 percent	127	2,688	2,231	17,404	10,900	211	6,888	5,717
84 percent	1,131	8,327	6,995	174,008	107,909	4,200	55,227	46,391
87 percent (returns eligible for 87-percent limitation)	67	112,160	97,579	114,838	98,946	67	112,160	97,579
87 percent	724	6,055	5,268	123,745	79,994	3,153	44,245	38,493
89 percent	1,483	43,442	38,664	313,029	213,183	2,386	108,892	96,914
90 percent	500	15,182	13,664	140,511	102,621	946	47,192	42,473
91 percent	446	66,595	60,601	218,257	173,031	446	66,595	60,601
JOINT RETURNS AND RETURNS OF SURVIVING SPOUSE								
Total	36,999,423	59,159,424	13,609,412	139,828,692	32,914,070	[1] 36,999,423	139,828,692	32,927,441
0 percent (returns with no tax base)	6,221,441					6,221,441		
20 percent	18,363,506	36,949,357	7,389,871	37,027,386	7,422,215	30,777,435	86,605,073	17,321,015
21 percent								
22 percent	9,002,319	14,023,681	3,085,210	50,093,145	10,312,990	12,413,929	27,670,121	6,087,427
24 percent								
26 percent	2,029,388	3,076,058	799,775	19,396,793	4,251,012	3,411,610	8,604,946	2,237,286
30 percent	574,847	978,502	293,551	7,962,708	1,899,938	1,382,222	4,208,002	1,262,401
32 percent								
34 percent	267,437	482,913	164,190	4,860,934	1,261,944	807,375	2,642,665	898,506
36 percent								
38 percent	158,210	293,770	111,633	3,592,003	1,013,936	539,938	1,820,682	691,859
39 percent								
42 percent								
43 percent	104,517	196,154	84,346	2,821,984	853,756	381,728	1,304,998	561,149
47 percent	72,286	138,892	65,279	2,293,980	746,652	277,211	958,592	450,538
49 percent								
50 percent (returns with capital gains tax only)	542	229,314	114,657	229,314	114,657	542	229,314	114,657
50 percent (returns with capital gains tax and normal tax and surtax)	[2] 82,199	2,045,790	1,022,895	[3] 6,545,918	[3] 3,072,346	82,199	2,045,790	1,022,895
50 percent	57,992	114,273	57,137	2,101,578	726,038	204,925	702,005	351,003
52 percent								
53 percent	35,446	67,759	35,912	1,465,979	536,405	146,933	513,707	272,265
54 percent								
56 percent	25,015	46,867	26,246	1,155,125	443,200	111,487	392,755	219,943
58 percent								
59 percent	31,974	114,941	67,815	1,689,938	687,532	86,472	550,925	325,046
62 percent	24,001	126,900	78,678	1,580,443	696,730	54,498	492,864	305,576
65 percent	11,745	61,589	40,033	942,880	444,386	30,497	286,613	186,298
66 percent								
68 percent								
69 percent	6,401	34,483	23,793	610,933	303,774	18,752	182,695	126,060
71 percent								
72 percent	3,654	19,930	14,350	398,813	207,366	12,351	124,294	89,492

See footnotes at end of table, p. 231.

TABLE 19. *Individual income tax returns: Income tax generated at each tax rate for all returns and returns under each of the three tax rate schedules, 1961*—Continued

Tax rate	Returns with tax rate as marginal rate: Number of returns (1)	Tax base taxed at marginal rate (2)	Tax generated at marginal rate (3)	Tax base taxed at all rates (4)	Tax generated at all rates (5)	Returns with any tax at tax rate: Number of returns (6)	Tax base at tax rate (7)	Tax generated at tax rate (8)
		Thousands	*Thousands*	*Thousands*	*Thousands*		*Thousands*	*Thousands*
JOINT RETURNS AND RETURNS OF SURVIVING SPOUSE—continued								
74 percent								
75 percent	3,390	$30,065	$22,549	$454,615	$247,093	8,597	$136,205	$102,154
76 percent								
78 percent	2,016	18,192	14,190	309,043	176,972	5,307	84,012	65,529
80 percent								
81 percent	1,028	9,723	7,876	179,695	107,502	3,291	54,983	44,536
83 percent								
84 percent	642	5,807	4,878	127,209	78,685	2,263	38,227	32,111
87 percent (returns eligible for 87-percent limitation)	5	14,299	12,440	14,315	12,452	5	14,299	12,440
87 percent	403	3,807	3,312	84,964	54,859	1,621	28,167	24,505
89 percent	812	30,102	26,791	222,564	151,134	1,218	70,702	62,925
90 percent	208	8,862	7,976	82,616	60,159	406	28,662	25,796
91 percent	198	37,394	34,029	129,735	102,683	198	37,394	34,029
SEPARATE RETURNS OF HUSBANDS AND WIVES AND OF SINGLE PERSONS NOT HEAD OF HOUSEHOLD OR SURVIVING SPOUSE								
Total	22,921,646	14,897,673	3,492,175	37,548,601	8,762,577	[1] 22,921,646	37,548,601	8,773,478
0 percent (returns with no tax base)	6,262,801					6,262,801		
20 percent	9,556,699	8,195,723	1,639,145	8,208,067	1,643,566	16,658,553	22,399,431	4,479,886
21 percent								
22 percent	4,790,469	4,214,701	927,234	13,810,029	2,845,290	7,101,854	8,837,471	1,944,244
24 percent								
26 percent	1,582,086	1,239,919	322,379	7,588,910	1,658,750	2,311,385	2,698,517	701,614
30 percent	414,216	319,606	95,882	2,821,989	667,541	729,299	949,772	284,932
32 percent								
34 percent	124,389	102,905	34,988	1,116,443	287,953	315,083	484,293	164,660
36 percent								
38 percent	58,135	53,045	20,157	661,985	187,406	190,694	318,163	120,902
39 percent								
42 percent								
43 percent	35,641	33,213	14,282	485,348	147,673	132,559	227,049	97,631
47 percent	23,618	21,944	10,314	370,878	120,059	96,918	168,544	79,216
49 percent								

50 percent (returns with capital gains tax only)	231	63,156	31,578	63,156	31,578	231	63,156	31,578
50 percent (returns with capital gains tax and normal tax and surtax)	[3] 22,778	386,969	193,485	[3] 1,167,508	[3] 606,439	22,778	386,969	193,485
50 percent	16,584	15,608	7,804	304,483	105,780	73,300	129,040	64,520
52 percent	-	-	-	-	-	-	-	-
53 percent	13,218	12,443	6,595	269,280	97,983	56,716	99,439	52,703
54 percent	-	-	-	-	-	-	-	-
56 percent	8,752	8,222	4,604	201,821	77,379	43,498	77,714	43,520
58 percent	-	-	-	-	-	-	-	-
59 percent	10,261	17,783	10,492	265,555	107,362	34,746	115,723	68,277
62 percent	8,492	22,945	14,226	270,658	118,761	24,485	118,903	73,720
65 percent	5,465	15,312	9,953	215,566	101,573	15,993	78,480	51,012
66 percent	-	-	-	-	-	-	-	-
68 percent	-	-	-	-	-	-	-	-
69 percent	3,057	8,278	5,712	141,683	70,415	10,528	53,104	36,642
71 percent	-	-	-	-	-	-	-	-
72 percent	2,029	5,627	4,051	106,443	55,456	7,471	38,279	27,561
74 percent	-	-	-	-	-	-	-	-
75 percent	1,832	7,824	5,868	113,254	61,911	5,442	43,924	32,943
76 percent	-	-	-	-	-	-	-	-
78 percent	990	4,442	3,465	74,146	42,588	3,610	30,642	23,901
80 percent	-	-	-	-	-	-	-	-
81 percent	683	3,261	2,641	59,692	35,704	2,620	22,631	18,331
83 percent	-	-	-	-	-	-	-	-
84 percent	489	2,520	2,117	46,799	29,224	1,937	17,000	14,280
87 percent (returns eligible for 87-percent limitation)	61	96,208	83,701	98,870	85,027	61	96,208	83,701
87 percent	280	1,334	1,161	31,111	19,857	1,448	13,014	11,322
89 percent	671	13,340	11,873	90,465	62,049	1,168	38,190	33,989
90 percent	265	5,550	4,995	51,295	37,625	497	17,150	15,435
90 percent	232	25,795	23,473	80,675	64,067	232	25,795	23,473
HEAD OF HOUSEHOLD RETURNS								
Total	1,578,351	1,364,538	325,479	4,417,818	1,037,993	[1] 1,578,351	4,417,818	1,038,805
0 percent (returns with no tax base)	200,800	-	-	-	-	200,800	-	-
20 percent	526,666	526,557	105,311	527,871	105,881	1,377,515	2,228,255	445,651
21 percent	524,793	492,128	103,347	1,542,091	312,888	850,849	1,144,240	240,290
22 percent	-	-	-	-	-	-	-	-
24 percent	209,237	161,652	38,796	1,000,331	211,138	326,056	395,290	94,870
26 percent	58,633	50,355	13,092	403,001	89,726	116,819	166,727	43,349
30 percent	21,994	18,933	5,680	195,756	46,133	58,186	91,317	27,395
32 percent	11,114	9,855	3,154	122,096	30,596	36,192	60,011	19,204
34 percent	-	-	-	-	-	-	-	-
36 percent	6,206	5,867	2,112	81,859	21,861	25,078	43,611	15,700
38 percent	-	-	-	-	-	-	-	-
39 percent	3,955	3,971	1,549	60,975	17,316	18,872	33,805	13,184
42 percent	2,878	2,555	1,073	49,746	14,767	14,917	26,633	11,186
43 percent	2,532	2,484	1,068	51,473	16,449	12,039	21,498	9,244
47 percent	1,728	1,748	822	38,446	12,714	9,507	17,306	8,134
49 percent	1,358	1,390	681	32,847	11,249	7,779	14,232	6,974

See footnotes at end of table, p. 231.

TABLE 19.—*Individual income tax returns: Income tax generated at each tax rate for all returns and returns under each of the three tax rate schedules, 1961*—Continued

Tax rate	Returns with tax rate as marginal rate					Returns with any tax at tax rate		
	Number of returns (1)	Tax base taxed at marginal rate (2)	Tax generated at marginal rate (3)	Tax base taxed at all rates (4)	Tax generated at all rates (5)	Number of returns (6)	Tax base at tax rate (7)	Tax generated at tax rate (8)
HEAD OF HOUSEHOLD RETURNS—continued		*Thousands*	*Thousands*	*Thousands*	*Thousands*		*Thousands*	*Thousands*
50 percent (returns with capital gains tax only)	35	$9,094	$4,547	$9,094	$4,547	35	$9,094	$4,547
50 percent (returns with capital gains tax and normal tax and surtax)	[2] 2,974	52,044	26,022	[3] 173,681	[3] 84,077	2,974	52,044	26,022
50 percent	---	---	---	---	---	---	---	---
52 percent	1,648	3,077	1,600	48,390	17,963	6,421	22,169	11,528
53 percent	---	---	---	---	---	---	---	---
54 percent	1,427	2,815	1,520	47,065	18,307	4,773	16,199	8,747
56 percent	---	---	---	---	---	---	---	---
58 percent	1,206	3,518	2,040	46,484	19,203	3,346	16,358	9,488
59 percent	---	---	---	---	---	---	---	---
62 percent	647	1,760	1,091	31,178	13,778	2,140	10,718	6,645
65 percent	---	---	---	---	---	---	---	---
66 percent	367	1,115	736	19,080	8,849	1,4933	7,871	5,195
68 percent	414	1,683	1,144	26,930	13,175	1,126	8,803	5,966
69 percent	---	---	---	---	---	---	---	---
71 percent	243	1,271	902	19,203	9,945	712	5,961	4,232
72 percent	---	---	---	---	---	---	---	---
74 percent	137	653	483	10,848	5,917	469	3,973	2,940
75 percent	---	---	---	---	---	---	---	---
76 percent	70	326	248	6,509	3,681	332	2,946	2,239
78 percent	---	---	---	---	---	---	---	---
80 percent	51	256	205	5,371	3,147	262	2,366	1,893
81 percent	---	---	---	---	---	---	---	---
83 percent	127	2,688	2,231	17,404	10,900	211	6,888	5,717
84 percent	---	---	---	---	---	---	---	---
87 percent (returns eligible for 87 percent limitation)	1	1,653	1,438	1,653	1,467	1	1,653	1,438
87 percent	41	914	795	7,670	5,278	84	3,064	2,666
89 percent	---	---	---	---	---	---	---	---
90 percent	27	770	693	6,600	4,837	43	1,380	1,242
91 percent	16	3,406	3,099	7,847	6,281	16	3,406	3,099

[1] This total is not the sum of the following tax rate classes as many returns have a tax base taxed at more than 1 rate.
[2] These returns are not included in the total as they already appear in the class which is their marginal normal tax and surtax rate.
[3] This amount is not included in the total for the reason stated in footnote 2.

NOTE.—Blank entries in this table denote "not applicable."

34-435—64——16

EXPLANATORY NOTE.—Tax base for returns with normal tax and surtax only is taxable income. For returns with alternative tax computation, the tax base is either (1) taxable income, where that amount is greater than ½ the excess long-term capital gain or (2) ½ the excess long-term capital gain, where that amount is equal to or greater than taxable income.

Tax rate is the rate at which all or a portion of an individual's tax base is taxed. Some of the tax rates are described below:

(*a*) 0 percent (returns with no tax base): This is the rate applicable to returns that show deductions plus exemptions equal to or exceeding adjusted gross income and returns with no adjusted gross income.

(*b*) 50 percent (returns with capital gains tax only): This is the rate applicable to returns with alternative tax computation which show the amount of ½ the excess long-term capital gain equal to or greater than the taxable income. The ½ excess, therefore, is the tax base instead of taxable income.

(*c*) 50 percent (returns with capital gains tax and normal tax and surtax): This is the rate applicable to returns with alternative tax computation where a portion of the tax base is taxed at the capital gains rate (50 percent), and a portion at normal tax and surtax rates.

(*d*) 87 percent (returns eligible for 87 percent limitation): This limitation of tax is 87 percent of the tax base subject to the regular normal and surtax rates.

Marginal rate is the maximum rate applied to any part of the tax base. Returns with a tax base subject to both the capital gains rate and the normal tax and surtax rates were classified in their marginal surtax rate classes.

Tax base taxed at marginal rate (col. 2) is that portion of the tax base that is taxed only at the marginal tax rate. For example, a joint return with $11,000 of tax base (for normal tax and surtax rates) would have $3,000 taxed at a marginal rate of 26 percent. The remaining tax base was taxed at lower rates.

Tax generated at marginal rate (col. 3) is that portion of the tax liability of each return that is taxed at the maximum rate.

Tax base taxed at all rates (col. 4) is the entire tax base of each return classified by the marginal tax rate of the return.

Tax generated at all rates (col. 5) is the total reported tax before credits of each return classified by the marginal tax rate of the return.

Number of returns with any tax at tax rate (col. 6) is a distribution of returns by applicable tax rates. It includes each return which had some portion of the tax base taxed at the tax rate shown in the stub. For example, a joint return with $11,000 tax base (for normal tax and surtax rates) would have some tax base taxed at the 20, 22, and 26 percent rates.

Tax base at tax rate (col. 7) is the tax base spread among the applicable tax rates. For example, a joint return with $11,000 tax base (for normal tax and surtax rates) would have $4,000 taxed at 20 percent, $4,000 taxed at 22 percent, and $3,000 taxed at 26 percent.

Tax generated at tax rate (col. 8) is the total tax generated at each tax rate and is obtained by applying the tax rate in the stub to the tax base amount in col. 7. This amount is the recalculated income tax before credits. Minor differences occurred between this total and the total for income tax before credits reported by the taxpayers for 1961 (col. 5) because of the method used in statistically processing unaudited returns.

Source: Internal Revenue Service: Statistics of Income—1961, Individual Income Tax Returns.

TABLE 20.—*Individual income tax returns: Effective tax rates on taxable returns based on adjusted gross income and amended gross income,[1] 1961*

[Dollar amounts in millions]

Adjusted gross income classes	Number of returns (thousands)	Adjusted gross income	Excluded net long-term capital gains	Amended gross income	Tax after credits	Tax as percent of adjusted gross income	Tax as percent of amended gross income
Up to $5,000	22,106.5	$66,724	$562	$67,286	$6,058	9.1	9.0
$5,000 to $10,000	20,477.6	143,170	1,086	144,256	15,936	11.1	11.0
$10,000 to $20,000	5,006.6	63,600	1,366	64,966	9,528	15.0	14.7
$20,000 to $50,000	852.3	24,486	1,587	26,073	5,612	22.9	21.5
$50,000 to $100,000	110.2	7,250	909	8,159	2,484	34.3	30.4
$100,000 to $150,000	16.7	2,008	444	2,452	809	40.3	33.0
$150,000 to $200,000	5.4	931	265	1,196	397	42.6	33.2
$200,000 to $500,000	6.1	1,737	681	2,418	764	44.0	31.6
$500,000 to $1,000,000	1.0	650	357	1,007	297	45.7	29.5
$1,000,000 and over	.4	727	434	1,161	342	47.0	29.5
Total	48,582.8	311,283	7,690	318,973	42,225	13.6	13.2

[1] Amended gross income is adjusted gross income plus excluded net long-term capital gains.

Source: Treasury Department, Office of Tax Analysis.

TABLE 21.—*Individual income tax returns: Number of returns by effective tax rates based on adjusted gross income by income classes; all returns with adjusted gross income of $500,000 or more, 1959*

Adjusted gross income	Total	Effective tax rate (percent)									
		0	0.1 to 9.9	10 to 19.9	20 to 29.9	30 to 39.9	40 to 49.9	50 to 59.9	60 to 69.9	70 to 79.9	80 to 84.9
$500,000 to $749,999	529	3	4	6	34	90	241	73	47	27	4
$750,000 to $999,999	193	2	3	3	9	23	90	36	16	9	2
$1,000,000 to $1,999,999	197	8	1	1	8	22	93	34	17	12	1
$2,000,000 to $4,999,999	64	2	------	------	4	6	31	9	6	5	1
$5,000,000 and over	19	5	------	------	------	1	6	3	3	1	------
All returns $500,000 and over.	1,002	20	8	10	55	142	461	155	89	54	8
		Percentage distribution									
$500,000 to $749,999	100	0.6	0.8	1.1	6.4	17.0	45.6	13.8	8.8	5.1	0.8
$750,000 to $999,999	100	1.0	1.6	1.6	4.7	11.9	46.6	18.7	8.3	4.6	1.0
$1,000,000 to $1,999,999	100	4.0	.5	.5	4.1	11.2	47.2	17.3	8.6	6.1	.5
$2,000,000 to $4,999,999	100	3.1	------	------	6.3	9.4	48.4	14.1	9.4	7.8	1.5
$5,000,000 and over	100	26.3	------	------	------	5.3	31.6	15.8	15.8	5.2	------
All returns $500,000 and over	100	2.0	.8	1.0	5.4	14.2	46.0	15.5	8.9	5.4	.8

NOTE.—For a discussion of this table, see the Revenue Act of 1963, hearings before the Committee on Finance, U.S. Senate on H.R. 8363, 88th Cong., 1st sess., pt. 1, pp. 278–284.

Source: Treasury Department, Office of Tax Analysis.

TABLE 22.—*Federal individual income-tax exemptions and first and top bracket rates, 1913–65*

Income year	Personal exemptions					Tax rates			
	Single	Married				First bracket		Top bracket	
		Dependents				Rate	Amount of income	Rate	Income over
		No	1	2	3				
						Percent		*Percent*	
1913–15	$3,000	$4,000	$4,000	$4,000	$4,000	1	$20,000	7	$500,000
1916	3,000	4,000	4,000	4,000	4,000	2	20,000	15	2,000,000
1917	1,000	2,000	2,200	2,400	2,600	2	2,000	67	2,000,000
1918	1,000	2,000	2,200	2,400	2,600	6	4,000	77	1,000,000
1919–20	1,000	2,000	2,200	2,400	2,600	4	4,000	73	1,000,000
1921	1,000	[1] 2,500	2,900	3,300	3,700	4	4,000	73	1,000,000
1922	1,000	[1] 2,500	2,900	3,300	3,700	4	4,000	56	200,000
1923	1,000	[1] 2,500	2,900	3,300	3,700	3	4,000	56	200,000
1924	1,000	2,500	2,900	3,300	3,700	[2] 1½	4,000	46	500,000
1925–28	1,500	3,500	3,900	4,300	4,700	[2] 1⅛	4,000	25	100,000
1929	1,500	3,500	3,900	4,300	4,700	[2] ⅜	4,000	24	100,000
1930–31	1,500	3,500	3,900	4,300	4,700	[2] 1⅛	4,000	25	100,000
1932–33	1,000	2,500	2,900	3,300	3,700	4	4,000	63	1,000,000
1934–35	1,000	2,500	2,900	3,300	3,700	[3] 4	4,000	63	1,000,000
1936–39	1,000	2,500	2,900	3,300	3,700	[3] 4	4,000	79	5,000,000
1940	800	2,000	2,400	2,800	3,200	[3] 4.4	4,000	81.1	5,000,000
1941	750	1,500	1,900	2,300	2,700	[3] 10	2,000	81	5,000,000
1942–43 [4]	500	1,200	1,550	1,900	2,250	[3] 19	2,000	88	200,000
1944–45	500	1,000	1,500	2,000	2,500	23	2,000	[5] 94	200,000
1946–47	500	1,000	1,500	2,000	2,500	19	2,000	[5] 86.45	200,000
1948–49 [6]	600	1,200	1,800	2,400	3,000	16.6	2,000	[5] 82.13	200,000
1950 [6]	600	1,200	1,800	2,400	3,000	17.4	2,000	[5] 91	200,000
1951 [6]	600	1,200	1,800	2,400	3,000	20.4	2,000	[5] 91	200,000
1952–53 [6]	600	1,200	1,800	2,400	3,000	22.2	2,000	[5] 92	200,000
1954–63 [6]	600	1,200	1,800	2,400	3,000	20	2,000	[5] 91	200,000
1964 [6]	600	1,200	1,800	2,400	3,000	16	500	77	200,000
1965 [6]	600	1,200	1,800	2,400	3,000	14	500	70	100,000

[1] If net income exceeds $5,000, married person's exemption is $2,000.
[2] After earned income credit equal to 25 percent of tax on earned income.
[3] Before earned income credit allowed as a deduction equal to 10 percent of earned net income.
[4] Exclusive of Victory tax.
[5] Subject to maximum effective rate limitation: 90 percent for 1944–45, 85.5 percent for 1946–47, 77 percent for 1948–49, 87 percent for 1950, 87.2 percent for 1951, 88 percent for 1952–53 and 87 percent for 1954–63.
[6] Additional exemptions of $600 are allowed to taxpayers and their spouses on account of blindness and/or age over 65.

Source: Treasury Department, Office of Tax Analysis.

TABLE 23.—*Individual income tax rate schedules under the Revenue Acts of 1944, 1945, 1948, 1950, 1951, and 1964*

[Percent]

Surtax net income	1944 act (highest war-time rates)	1945 act [1]	1948 act [1]	1950 act calendar year 1950	1951 act: Calendar year 1951	1951 act: Calendar years 1952–53	1951 act: Calendar years 1954–63	1964 act: Calendar year 1964	1964 act: Calendar year 1965
0 to $500	23	19.00	16.60	17.40	20.4	22.2	20	16.0	14
$500 to $1,000								16.5	15
$1,000 to $1,500								17.5	16
$1,500 to $2,000								18.0	17
$2,000 to $4,000	25	20.90	19.36	20.02	22.4	24.6	22	20.0	19
$4,000 to $6,000	29	24.70	22.88	23.66	27.0	29.0	26	23.5	22
$6,000 to $8,000	33	28.50	26.40	27.30	30.0	34.0	30	27.0	25
$8,000 to $10,000	37	32.30	29.92	30.94	35.0	38.0	34	30.5	28
$10,000 to $12,000	41	36.10	33.44	34.58	39.0	42.0	38	34.0	32
$12,000 to $14,000	46	40.85	37.84	39.13	43.0	48.0	43	37.5	36
$14,000 to $16,000	50	44.65	41.36	42.77	48.0	53.0	47	41.0	39
$16,000 to $18,000	53	47.50	44.00	45.50	51.0	56.0	50	44.5	42
$18,000 to $20,000	56	50.35	46.64	48.23	54.0	59.0	53	47.5	45
$20,000 to $22,000	59	53.20	49.28	50.96	57.0	62.0	56	50.5	48
$22,000 to $26,000	62	56.05	51.92	53.69	60.0	66.0	59	53.5	50
$26,000 to $32,000	65	58.90	54.56	56.42	63.0	67.0	62	56.0	53
$32,000 to $38,000	68	61.75	57.20	59.15	66.0	68.0	65	58.5	55
$38,000 to $44,000	72	65.55	60.72	62.79	69.0	72.0	69	61.0	58
$44,000 to $50,000	75	68.40	63.36	65.52	73.0	75.0	72	63.5	60
$50,000 to $60,000	78	71.25	66.00	68.25	75.0	77.0	75	66.0	62
$60,000 to $70,000	81	74.10	68.64	70.98	78.0	80.0	78	68.5	64
$70,000 to $80,000	84	76.95	71.28	73.71	82.0	83.0	81	71.0	66
$80,000 to $90,000	87	79.80	73.92	76.44	84.0	85.0	84	73.5	68
$90,000 to $100,000	90	82.65	76.56	79.17	87.0	88.0	87	75.0	69
$100,000 to $136,719.10	92	84.55	78.32	80.99	89.0	90.0	89	76.5	70
$136,719.10 to $150,000			80.3225	82.503					
$150,000 to $200,000	93	85.50	81.2250	83.43	90.0	91.0	90	76.5	
$200,000 and over [2]	94	86.45	82.1275	84.357	91.0	92.0	91	77.0	

[1] After reductions from tentative tax.

[2] Subject to the following maximum rate limitations; Revenue Act of 1944, 90 percent; Revenue Act of 1945, 85.5 percent; Revenue Act of 1948, 77 percent; Revenue Act of 1950, 80 percent; Revenue Act of 1951, rates for 1951, 87.2 percent; rates for 1952–53, 88 percent; rates for 1954–63, 87 percent; Revenue Act of 1964, no limitation.

Source: Treasury Department, Office of Tax Analysis.

TABLE 24.—*Effective rates of individual income tax at selected net income levels, 1913–65*

SINGLE PERSON—NO DEPENDENTS

[Percent]

Income year	Level of net income [1]					
	$3,000	$5,000	$10,000	$50,000	$100,000	$500,000
1913–15		0.4	0.7	1.5	2.5	5.0
1916		.8	1.4	2.7	3.9	8.6
1917	1.3	2.4	4.0	10.4	16.2	38.5
1918	4.0	4.8	9.5	22.3	35.2	64.6
1919–20	2.7	3.2	6.7	18.5	31.3	60.7
1921	2.7	3.2	6.7	18.5	31.3	60.7
1922	2.7	3.2	6.0	17.4	30.2	52.1
1923	2.0	2.4	4.5	13.1	22.7	39.1
1924	1.0	1.2	2.3	12.3	22.7	39.9
1925–27	.6	.8	1.5	9.9	16.1	23.2
1928	.6	.8	1.5	9.3	15.8	23.2
1929	.2	.3	.9	8.5	14.9	22.2
1930–31	.6	.8	1.5	9.3	15.8	23.2
1932–33	2.7	3.2	6.0	17.4	30.2	52.7
1934–35	2.3	2.8	5.6	18.7	31.4	53.0
1936–39	2.3	2.8	5.6	18.7	33.4	61.0
1940	2.8	3.4	6.9	29.4	44.3	66.2
1941	7.4	9.7	14.9	41.8	53.2	69.1
1942 [2]	15.7	18.4	23.9	51.6	64.6	82.9
1943 [2]	19.1	22.1	27.8	56.1	69.7	88.4
1944–45	19.5	22.1	27.6	55.9	69.9	88.9
1946–47	16.2	18.4	23.5	50.3	63.5	81.6
1948–49	13.6	16.2	21.2	46.4	58.8	77.0
1950	14.3	16.9	22.0	48.0	60.8	79.2
1951	16.6	19.3	24.9	53.5	67.3	86.0
1952–53	18.1	21.0	27.2	56.9	69.7	87.2
1954–63	16.3	18.9	24.4	52.8	66.8	85.9
1964	14.0	16.7	21.8	47.1	58.9	73.3
1965	12.9	15.6	20.2	44.5	55.1	67.0

MARRIED PERSONS—2 DEPENDENTS

Income year	$3,000	$5,000	$10,000	$50,000	$100,000	$500,000
1913–15		0.2	0.6	1.5	2.5	5.0
1916		.4	1.2	2.6	3.9	8.6
1917	0.4	1.3	3.4	10.3	16.2	38.5
1918	1.2	3.1	7.8	22.0	35.0	64.6
1919–20	.8	2.1	5.6	18.3	31.2	60.6
1921		1.4	5.3	18.3	31.1	60.6
1922		1.4	4.6	17.2	30.1	52.1
1923		1.0	3.4	12.9	22.6	39.1
1924		.5	1.4	12.1	22.5	39.9
1925–27		.2	.8	9.7	16.0	23.1
1928		.2	.8	9.1	15.7	23.1
1929		.1	.4	8.3	14.9	22.2
1930–31		.2	.8	9.1	15.7	23.1
1932–33		1.4	4.2	17.1	30.0	52.7
1934–35		1.0	3.4	17.2	30.2	52.7
1936–39		1.0	3.4	17.2	32.0	60.7
1940		1.5	4.4	27.5	42.9	65.9
1941	1.9	5.4	11.2	39.9	52.2	68.9
1942 [2]	6.4	11.8	19.1	49.7	63.5	82.7
1943 [2]	8.9	14.6	22.1	52.8	67.8	88.0
1944–45	9.2	15.1	22.5	53.7	68.6	88.6
1946–47	6.3	11.8	18.6	48.2	62.3	81.3
1948–49	3.3	8.6	13.6	33.2	45.6	71.7
1950	3.5	9.0	14.2	34.3	47.2	73.9
1951	4.1	10.6	16.2	38.5	52.6	80.7
1952–53	4.4	11.5	17.7	42.2	56.0	82.2
1954–63	4.0	10.4	15.9	37.8	51.9	80.5
1964	3.2	8.6	14.0	33.7	46.4	69.4
1965	2.8	7.7	13.0	31.7	43.7	63.9

[1] Income after deductions but before personal exemptions.
[2] Unadjusted for transition to current taxpayment.

Source: Treasury Department, Office of Tax Analysis.

TABLES

BUSINESS TAXES

TABLE 25.—*Sole proprietorships, partnerships, and corporations: Number of businesses, business receipts, depreciation, and net profit, by industrial division, 1961*

Industrial division	Number of businesses				Business receipts			
	Total	Sole proprietorships	Partnerships	Corporations	Total	Sole proprietorships	Partnerships	Corporations
					Thousands	*Thousands*	*Thousands*	*Thousands*
All industrial divisions	11,371,007	9,241,755	938,966	1,190,286	$1,068,337,342	$170,981,413	$73,412,664	$823,943,265
Agriculture, forestry, and fisheries	3,642,703	3,487,190	136,532	18,981	37,602,024	27,914,902	4,609,720	5,077,402
Mining	65,219	35,549	15,939	13,731	13,809,598	1,209,179	984,842	11,615,577
Construction	824,537	678,456	62,290	83,791	58,662,946	14,487,676	7,432,568	36,742,702
Manufacturing	412,345	194,325	44,462	173,558	383,356,963	6,599,828	6,845,687	369,911,448
Transportation, communication, electric, gas, and sanitary services	353,820	286,672	18,100	49,048	71,589,070	4,100,142	1,166,703	66,322,225
Wholesale and retail trade	2,585,318	1,942,804	277,567	364,947	389,447,749	85,639,324	37,389,282	266,419,143
Wholesale trade	493,492	328,130	41,950	123,412	160,404,613	16,973,390	12,842,911	130,588,312
Retail trade	2,022,957	1,563,939	228,775	230,243	218,635,186	65,157,786	23,420,711	130,056,689
Wholesale and retail trade not allocable	68,869	50,735	6,842	11,292	10,407,950	3,508,148	1,125,660	5,774,142
Finance, insurance, and real estate	1,009,537	461,649	207,678	340,210	53,392,643	5,275,142	4,901,991	43,215,510
Services	2,384,922	2,075,689	171,278	137,955	58,903,426	24,355,060	9,985,284	24,563,082
Nature of business not allocable	92,606	79,421	5,120	8,065	1,572,923	1,400,160	96,587	76,176
	Percentage distribution							
All industrial divisions	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Agriculture, forestry, and fisheries	32.0	37.7	14.5	1.6	3.5	16.3	6.3	0.6
Mining	.6	.4	1.7	1.2	1.3	.7	1.3	1.4
Construction	7.3	7.3	6.6	7.0	5.5	8.5	10.1	4.5
Manufacturing	3.6	2.1	4.7	14.6	35.9	3.9	9.3	44.9
Transportation, communication, electric, gas, and sanitary services	3.1	3.1	1.9	4.1	6.7	2.4	1.6	8.0
Wholesale and retail trade	22.7	21.0	29.6	30.7	36.5	50.1	50.9	32.3
Wholesale trade	4.3	3.6	4.5	10.4	15.0	9.9	17.5	15.8
Retail trade	17.8	16.9	24.4	19.4	20.5	38.1	31.9	15.8
Wholesale and retail trade not allocable	.6	.5	.7	.9	1.0	2.1	1.5	.7
Finance, insurance, and real estate	8.9	5.0	22.1	28.6	5.0	3.1	6.7	5.2
Services	21.0	22.5	18.2	11.6	5.5	14.2	13.6	3.0
Nature of business not allocable	.8	.9	.5	.7	.1	.8	.1	(1)

	Depreciation				Net profit (less loss) [1]			
	Total	Sole proprietorships	Partnerships	Corporations	Total	Sole proprietorships	Partnerships	Corporations
	Thousands	*Thousands*	*Thousands*	*Thousands*	*Thousands*	*Thousands*	*Thousands*	*Thousands*
All industrial divisions	$32,778,167	$6,912,088	$2,178,293	$23,687,786	$77,279,512	$22,696,990	$8,688,622	$45,893,900
Agriculture, forestry, and fisheries	3,681,423	3,126,214	345,647	209,562	4,341,890	3,621,946	609,793	110,151
Mining	967,854	107,972	99,763	760,119	841,632	[2] 12,580	[2] 8,225	862,437
Construction	1,230,488	403,401	165,377	661,710	3,197,234	1,997,795	690,280	509,159
Manufacturing	10,868,981	214,480	151,271	10,503,230	23,721,373	660,681	567,114	22,493,578
Transportation, communication, electric, gas, and sanitary services	6,159,620	395,346	74,601	5,689,673	8,202,953	570,078	146,189	7,486,686
Wholesale and retail trade	3,809,036	1,225,264	394,477	2,189,295	12,367,600	5,579,784	2,224,007	4,563,809
Wholesale trade	1,035,402	229,720	93,514	712,168	4,298,664	1,409,257	602,757	2,286,650
Retail trade	2,636,603	939,192	286,873	1,410,538	7,680,090	3,974,775	1,553,413	2,151,902
Wholesale and retail trade not allocable	137,031	56,352	14,090	66,589	388,846	195,752	67,837	125,257
Finance, insurance, and real estate	2,944,821	224,224	580,081	2,140,516	11,647,840	1,548,197	1,117,534	8,982,109
Services	3,061,801	1,166,927	364,684	1,530,190	12,781,979	8,580,176	3,311,877	889,926
Nature of business not allocable	54,143	48,260	2,392	3,491	177,011	150,913	30,053	[2] 3,955
	Percentage distribution							
All industrial divisions	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Agriculture, forestry, and fisheries	11.2	45.2	15.9	0.9	5.6	16.0	7.0	.2
Mining	3.0	1.6	4.6	3.2	1.1	(3)	(3)	1.9
Construction	3.8	5.8	7.6	2.8	4.1	8.8	7.9	1.2
Manufacturing	33.2	3.1	6.9	44.3	30.7	2.9	6.5	49.0
Transportation, communication, electric, gas, and sanitary services	18.8	5.7	3.4	24.0	10.6	2.5	1.7	16.3
Wholesale and retail trade	11.6	17.7	18.1	9.2	16.0	24.6	25.6	9.9
Wholesale trade	3.2	3.3	4.3	3.0	5.6	6.2	6.9	5.0
Retail trade	8.0	13.6	13.2	6.0	9.9	17.5	17.9	4.6
Wholesale and retail trade not allocable	.4	.8	.6	.2	.5	.9	.8	.3
Finance, insurance, and real estate	9.0	3.2	26.6	9.0	15.1	6.8	12.9	19.6
Services	9.3	16.9	16.7	6.5	16.5	37.8	38.1	1.9
Nature of business not allocable	.2	.7	.1	0	.2	.7	.3	(3)

[1] For corporations, net income (less deficit).
[2] Net loss exceeds net profit.
[3] Percentage not computed because data are negative
[4] Less than 0.05 percent.

Source: Internal Revenue Service: Statistics of Income—1961–62, U.S. Business Tax Returns.

TABLE 26.—*Sole proprietorships, partnerships, and corporations: Distributive shares by industry of number of businesses, business receipts, depreciation, and net profit (less loss), 1961*

[Percent]

Industrial division	Number of businesses				Business receipts			
	Total	Sole proprietorships	Partnerships	Corporations	Total	Sole proprietorships	Partnerships	Corporations
All industrial divisions	100	81.3	8.3	10.4	100	16.0	6.9	77.1
Agriculture, forestry, and fisheries	100	95.7	3.7	0.6	100	74.2	12.3	13.5
Mining	100	54.5	24.4	21.1	100	8.8	7.1	84.1
Construction	100	82.3	7.6	10.1	100	24.7	12.7	62.6
Manufacturing	100	47.1	10.8	42.1	100	1.7	1.8	96.5
Transportation, communication, electric, gas, and sanitary services	100	81.0	5.1	13.9	100	5.8	1.6	92.6
Wholesale and retail trade	100	75.1	10.7	14.2	100	22.0	9.6	68.4
Wholesale trade	100	66.5	8.5	25.0	100	10.6	8.0	81.4
Retail trade	100	77.3	11.3	11.4	100	29.8	10.7	59.5
Wholesale and retail trade not allocable	100	73.7	9.9	16.4	100	33.7	10.8	55.5
Finance, insurance, and real estate	100	45.7	20.6	33.7	100	9.9	9.2	80.9
Services	100	87.0	7.2	5.8	100	41.3	17.0	41.7
Nature of business not allocable	100	85.8	5.5	8.7	100	89.0	6.2	4.8

TABLE 26.—*Sole proprietorships, partnerships, and corporations: Distributive shares by industry of number of businesses, business receipts depreciation, and net profit (less loss), 1961*—Continued

[Percent]

Industrial division	Depreciation				Net profit (less loss) [1]			
	Total	Sole proprietorships	Partnerships	Corporations	Total	Sole proprietorships	Partnerships	Corporations
All industrial divisions	100	21.1	6.6	72.3	100	29.4	11.2	59.4
Agriculture, forestry, and fisheries	100	84.9	9.4	5.7	100	83.4	14.0	2.6
Mining	100	11.2	10.3	78.5	100	(2)	(2)	102.5
Construction	100	32.8	13.4	53.8	100	62.5	21.6	15.9
Manufacturing	100	2.0	1.4	96.6	100	2.8	2.4	94.8
Transportation, communication, electric, gas, and sanitary services	100	6.4	1.2	92.4	100	6.9	1.8	91.3
Wholesale and retail trade	100	32.2	10.3	57.5	100	45.1	18.0	36.9
Wholesale trade	100	22.2	9.0	68.8	100	32.8	14.0	53.2
Retail trade	100	35.6	10.9	53.5	100	51.8	20.2	28.0
Wholesale and retail trade not allocable	100	41.1	10.3	48.6	100	50.4	17.4	32.2
Finance, insurance, and real estate	100	7.6	19.7	72.7	100	13.3	9.6	77.1
Services	100	38.1	11.9	50.0	100	67.1	25.9	7.0
Nature of business not allocable	100	89.1	4.5	6.4	100	85.3	17.0	(2)

[1] For corporations, net income (less deficit).
[2] Percentage not computed because data are negative.

Source: Internal Revenue Service: Statistics of Income—1961-62, U.S. Business Tax Returns.

TABLE 27.—*Sole proprietorships and partnerships: Number of businesses, business receipts, and net profit, by size of net profit, 1961*

Size of net profit	Number of businesses		Business receipts		Net profit (less loss)	
	Sole proprietorships	Partnerships	Sole proprietorships	Partnerships	Sole proprietorships	Partnerships
			Thousands	*Thousands*	*Thousands*	*Thousands*
Businesses with net profit, total	7,294,133	727,725	$151,761,498	$65,217,119	$25,756,867	$9,745,507
Under $2,000	3,902,104	192,136	25,768,565	3,323,386	3,198,391	166,197
$2,000 under $5,000	1,995,366	152,480	39,982,443	5,336,956	6,480,746	511,423
$5,000 under $10,000	880,306	150,398	37,456,610	8,859,067	6,059,686	1,095,361
$10,000 under $20,000	357,508	123,624	26,402,541	12,972,308	4,896,865	1,730,629
$20,000 under $50,000	145,449	76,877	17,679,412	15,873,996	4,161,735	2,310,468
$50,000 under $100,000	12,091	22,189	3,273,393	8,048,154	764,661	1,513,155
$100,000 under $500,000	1,309	9,377	1,198,534	7,161,686	194,783	1,574,471
$500,000 or more	(1)	644	(1)	3,641,566	(1)	843,803
Businesses without net profit, total	[2] 1,947,622	[3] 211,241	19,219,915	8,195,545	[4] 3,059,877	[4] 1,056,885
Total businesses	[2] 9,241,755	[3] 938,966	170,981,413	73,412,664	22,696,990	8,688,622
	Percentage distribution					
Businesses with net profit, total	78.9	77.5	88.8	88.8	(6)	(6)
Under $2,000	42.2	20.5	15.1	4.5	14.1	1.9
$2,000 under $5,000	21.6	16.2	23.4	7.3	28.6	5.9
$5,000 under $10,000	9.5	16.0	21.9	12.1	26.7	12.6
$10,000 under $20,000	3.9	13.2	15.4	17.7	21.6	19.9
$20,000 under $50,000	1.6	8.2	10.3	21.6	18.3	26.6
$50,000 under $100,000	.1	2.4	1.9	11.0	3.4	17.4
$100,000 under $500,000	(5)	1.0	.7	9.8	.9	18.1
$500,000 or more	(1)	.1	(1)	5.0	(1)	9.7
Businesses without net profit, total	21.1	22.5	11.2	11.2	(6)	(6)
Total businesses	100.0	100.0	100.0	100.0	100.0	100.0

[1] Included in size "$100,000 under $500,000."
[2] Includes 17,835 businesses with neither profit nor loss.
[3] Includes 4,352 partnerships with neither profit nor loss.
[4] Net loss exceeds net profit.
[5] Less than 0.05 percent.
[6] Percentage not shown because for businesses with net profit percent would equal more than 100; and for businesses without net profit percent would be negative.

Source: Internal Revenue Service: Statistics of Income—1961-62, U.S. Business Tax Returns.

TABLES

FIDUCIARY INCOME TAXES

TABLE 28.—*Taxable fiduciary income tax returns: Number of returns, total income, charitable deductions, distributions to beneficiaries, exemptions, taxable income and income tax after credits, 1941–60*

Item	1960	1958	1956	1954	1952	1950	1948	1946	1944	1942	1941
Number of returns	[1] 226,382	188,805	172,185	127,779	132,927	115,252	101,283	121,725	92,369	81,483	84,884
Trusts	[1] 158,882	127,436	121,254	89,470	87,301	72,157	59,945	75,294	55,832	(2)	(2)
Estates	67,500	61,369	50,931	38,309	45,626	43,095	41,338	46,431	36,537	(2)	(2)
	Thousands	*Thousands*	*Thousands*	*Thousands*	*Thousands*	*Thousands*	*Thousands*	*Thousands*	*Thousands*	*Thousands*	*Thousands*
Total income	$2,810,714	$2,445,266	$2,543,617	$1,868,922	$1,307,721	$1,233,957	$986,806	$1,065,765	$655,623	$573,753	$700,790
Charitable deductions	22,031	13,466	11,038	7,117	567,276	522,580	377,021	394,551	243,625	208,605	282,136
Distributions to beneficiaries	706,411	650,668	752,547	579,353							
Exemptions	65,626	57,061	51,644	37,825	36,122	33,075	30,799	30,745	(2)	(2)	(2)
Net income taxable to fiduciary [3]					626,760	615,614	530,360	594,924	357,017	299,633	340,808
Taxable income [3]	1,045,676	888,993	901,626	696,999							
Income tax after credits	361,665	308,599	326,945	263,893	234,933	208,756	176,309	205,457	131,078	103,670	90,210

[1] Number of estates and trusts for earlier years represents number of returns; in some instances multiple trusts were reported on 1 return.
[2] Not available.
[3] Net income taxable to fiduciary is before exemption and taxable income is after exemption.

Source: Internal Revenue Service: Statistics of Income, Fiduciary, Gift, and Estate Tax Returns.

TABLE 29.—*Fiduciary income tax returns: Number of estates, sources of income, distributions to beneficiaries, exemptions, taxable income of fiduciary, and income tax after credits, by total income classes, 1960*

Total income classes	Number of estates	Total income	Sources of income: Dividends	Sources of income: Net gain from sales of capital assets	Sources of income: Gross rents and royalties	Sources of income: Interest	Sources of income: All other	Distributions to beneficiaries	Exemptions	Taxable income of fiduciary	Income tax after credits
		Thousands	*Thousands*	*Thousands*	*Thousands*	*Thousands*	*Thousands*	*Thousands*	*Thousands*	*Thousands*	*Thousands*
Taxable estates, total	67,500	$716,321	$227,752	$138,618	$119,881	$89,678	$140,392	$98,889	$40,328	$294,328	$91,160
Under $600											
$600 and under $3,000	28,009	46,770	18,331	1,967	7,022	13,213	6,237	619	16,732	20,203	3,676
$3,000 and under $5,000	11,425	44,340	16,595	3,525	8,643	9,129	6,448	1,996	6,816	23,862	4,443
$5,000 and under $10,000	12,743	89,414	31,975	10,986	15,700	15,276	15,477	6,639	7,613	49,405	10,025
$10,000 and under $20,000	8,117	113,941	38,564	12,983	23,798	16,012	22,584	12,718	4,857	58,591	14,404
$20,000 and under $100,000	6,525	254,319	77,310	46,628	43,064	25,917	61,400	41,513	3,902	97,006	34,892
$100,000 and under $1,000,000	665	137,075	37,169	50,459	14,739	8,487	26,221	27,579	398	40,901	21,260
$1,000,000 or more	16	30,462	7,808	12,070	6,915	1,644	2,025	7,825	10	4,360	2,460
Nontaxable estates, total	86,736	464,903	108,981	54,713	124,313	67,834	109,062	215,226	52,044	494	----------
Under $600	17,210	[1] 3,360	2,439	[1] 1,058	1,820	2,543	[1] 9,104	1,744	10,326		----------
$600 and under $3,000	39,243	57,660	15,027	3,223	17,555	14,258	7,597	20,879	23,547		----------
$3,000 and under $5,000	10,796	41,871	12,745	9,037	11,639	7,322	21,058	21,816	6,478		----------
$5,000 and under $10,000	9,849	68,545	17,495		20,617	10,503		37,460	5,911		----------
$10,000 and under $20,000	5,326	73,508	17,799	5,857	23,292	8,298	18,262	35,102	3,196	494	----------
$20,000 and under $100,000	4,013	144,361	27,220	19,241	33,341	17,987	46,572	64,496	2,407		----------
$100,000 and under $1,000,000	287	63,134	11,516	13,678	12,700	4,462	20,778	27,490	172		----------
$1,000,000 or more	12	19,184	4,740	4,735	3,349	2,461	3,899	6,239	7		----------
Total, all estates	154,236	1,181,224	336,733	193,331	244,194	157,512	249,454	314,115	92,372	294,822	91,160

[1] Net deficit.

Source: Internal Revenue Service: Statistics of Income—1960, Fiduciary, Gift, and Estate Tax Returns.

TABLE 30.—*Fiduciary income tax returns: Number of trusts, sources of income, distributions to beneficiaries, exemptions, taxable income of fiduciary, and income tax after credits, by total income classes, 1960*

Total income classes	Number of trusts	Sources of income: Total income	Sources of income: Dividends	Sources of income: Net gain from sales of capital assets	Sources of income: Gross rents and royalties	Sources of income: Interest	Sources of income: All other	Distributions to beneficiaries	Exemptions	Taxable income of fiduciary	Income tax after credits
		Thousands	*Thousands*	*Thousands*	*Thousands*	*Thousands*	*Thousands*	*Thousands*	*Thousands*	*Thousands*	*Thousands*
Taxable trusts, total	158,882	$2,094,393	$744,985	$850,185	$211,715	$114,974	$172,534	$607,522	$25,298	$751,348	$270,505
Under $600	25,285	8,603	4,633	400	362	2,518	690	126	2,585	4,062	709
$600 and under $3,000	46,309	73,061	32,304	11,760	8,754	12,089	8,154	10,542	5,810	40,532	7,281
$3,000 and under $5,000	19,710	77,878	32,319	16,717	9,716	10,215	8,911	21,095	3,279	35,283	6,632
$5,000 and under $10,000	26,122	187,172	75,424	49,690	21,467	19,622	20,969	57,703	4,996	75,058	15,369
$10,000 and under $20,000	20,639	292,324	113,430	89,876	36,317	23,903	28,798	93,475	4,123	110,352	26,733
$20,000 and under $100,000	18,186	707,680	271,356	269,249	76,253	33,297	57,525	228,015	3,924	240,222	86,194
$100,000 and under $1,000,000	2,530	558,161	164,236	297,466	47,215	12,245	36,999	146,460	557	187,333	98,032
$1,000,000 or more	101	189,514	51,283	115,027	11,631	1,085	10,488	50,106	24	58,506	29,555
Non-taxable trusts, total	266,542	1,991,405	1,101,388	193,705	341,275	214,782	140,255	1,476,545	71,528	337	----------
Under $600	39,707	4,637	6,509	[1] 3,177	771	4,498	[1] 3,964	8,860	9,097	(2)	----------
$600 and under $3,000	109,498	169,945	95,400	6,261	14,016	40,890	13,378	134,133	29,834	9	----------
$3,000 and under $5,000	37,013	143,294	83,382	5,923	17,391	25,979	10,619	114,874	10,222	313	----------
$5,000 and under $10,000	39,978	279,299	170,778	9,705	36,856	42,125	19,835	225,096	11,284		----------
$10,000 and under $20,000	22,754	315,308	185,947	20,653	59,162	31,724	17,822	239,240	6,282		----------
$20,000 and under $100,000	15,871	594,489	317,009	62,247	127,961	42,595	44,677	424,740	4,357		----------
$100,000 and under $1,000,000	1,664	359,333	185,788	61,575	61,612	20,360	29,998	245,879	436	15	----------
$1,000,000 or more	57	125,100	56,575	30,518	23,506	6,611	7,890	83,723	16	----------	----------
Total, all trusts	425,424	4,085,798	1,846,373	1,043,890	552,990	329,756	312,789	2,084,067	96,826	751,685	270,505

[1] Net deficit.
[2] Sample variability too large to show separately.

Source: Internal Revenue Service: Statistics of Income—1960, Fiduciary, Gift, and Estate Tax Returns.

TABLES

CORPORATIONS

34-435—64——17

TABLE 31.—*Corporate profits before and after taxes as a percent of national income, 1929–63*

	Corporate profits before taxes	Corporate tax liability [1]	Corporate profits after taxes: Total	Corporate profits after taxes: Dividend payments	Corporate profits after taxes: Undistributed profits	National income	Percent of national income: Corporate profits before taxes	Percent of national income: Tax liability	Percent of national income: Corporate profits after taxes
	Billions	*Billions*	*Billions*	*Billions*	*Billions*	*Billions*			
1929	$9.6	$1.4	$8.3	$5.8	$2.4	$87.1	11.0	1.6	9.5
1930	3.3	.8	2.5	5.5	−3.0	75.7	4.4	1.1	.3
1931	−.8	.5	−1.3	4.1	−5.4	59.7	−1.3	.8	−2.2
1932	−3.0	.4	−3.4	2.6	−6.0	42.5	−7.1	.9	−8.0
1933	.2	.5	−.4	2.1	−2.4	40.2	.5	1.2	−1.0
1934	1.7	.7	1.0	2.6	−1.6	49.0	3.5	1.4	2.0
1935	3.1	1.0	2.2	2.9	−.7	57.1	5.4	1.8	3.9
1936	5.7	1.4	4.3	4.5	−.2	64.9	8.8	2.2	6.6
1937	6.2	1.5	4.7	4.7	(2)	73.6	8.4	2.0	6.4
1938	3.3	1.0	2.3	3.2	−.9	67.6	4.9	1.5	3.4
1939	6.4	1.4	5.0	3.8	1.2	72.8	8.8	1.9	6.9
1940	9.3	2.8	6.5	4.0	2.4	81.6	11.4	3.4	8.0
1941	17.0	7.6	9.4	4.5	4.9	104.7	16.2	7.3	9.0
1942	20.9	11.4	9.5	4.3	5.2	137.7	15.2	8.3	6.9
1943	24.6	14.1	10.5	4.5	6.0	170.3	14.4	8.3	6.2
1944	23.3	12.9	10.4	4.7	5.7	182.6	12.8	7.1	5.7
1945	19.0	10.7	8.3	4.7	3.6	181.2	10.5	5.9	4.6
1946	22.6	9.1	13.4	5.8	7.7	180.9	12.5	5.0	7.4
1947	29.5	11.3	18.2	6.5	11.7	198.2	14.9	5.7	9.2
1948	33.0	12.5	20.5	7.2	13.3	223.5	14.8	5.6	9.2
1949	26.4	10.4	16.0	7.5	8.5	217.7	12.1	4.8	7.3
1950	40.6	17.9	22.8	9.2	13.6	241.9	16.8	7.4	9.4
1951	42.2	22.4	19.7	9.0	10.7	279.3	15.1	8.0	7.1
1952	36.7	19.5	17.2	9.0	8.3	292.2	12.6	6.7	5.9
1953	38.3	20.2	18.1	9.2	8.9	305.6	12.5	6.6	5.9
1954	34.1	17.2	16.8	9.8	7.0	301.8	11.3	5.7	5.6
1955	44.9	21.8	23.0	11.2	11.8	330.2	13.6	6.6	7.0
1956	44.7	21.2	23.5	12.1	11.3	350.8	12.7	6.0	6.7
1957	43.2	20.9	22.3	12.6	9.7	366.9	11.8	5.7	6.1
1958	37.4	18.6	18.8	12.4	6.4	367.4	10.2	5.1	5.1
1959	47.7	23.2	24.5	13.7	10.8	400.5	11.9	5.8	6.1
1960	44.3	22.3	22.0	14.5	7.5	414.5	10.7	5.4	5.3
1961 [3]	43.8	22.0	21.8	15.3	6.5	426.1	10.3	5.2	5.1
1962 [3, 4]	46.8	22.2	24.6	16.6	8.1	453.7	10.3	4.9	5.4
1963 [3, 4]	51.5	24.4	27.1	17.8	9.3	478.1	10.8	5.1	5.7

[1] Federal and State corporate income and excess profits taxes.
[2] Less than $50,000,000.
[3] Preliminary.
[4] The figures for 1962 and 1963 reflect the new depreciation guidelines issued by the Treasury Department July 11, 1962, and the investment tax credit provided in the Revenue Act of 1962.

Source: Department of Commerce.

TABLE 32.—*Corporate profits after tax and corporate capital consumption allowances, 1929–63*

	Corporate profits after taxes	Corporate capital consumption allowances [1]	Total (1 + 2)	Gross national product	Percent of gross national product		
					Corporate profits after taxes	Corporate capital consumption allowances	Total (5 + 6)
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
	Billions	*Billions*	*Billions*	*Billions*			
1929	$8.3	$4.4	$12.7	$104.4	7.8	4.2	12.1
1930	2.5	4.4	6.9	91.1	2.7	4.8	7.6
1931	−1.3	4.3	3.0	76.3	−1.7	5.6	3.9
1932	−3.4	4.0	.6	58.5	−5.8	6.8	1.0
1933	−.4	3.8	3.4	56.0	−.7	6.8	6.1
1934	1.0	3.6	4.6	65.0	1.5	5.5	7.1
1935	2.2	3.7	5.9	72.5	3.0	5.1	8.1
1936	4.3	3.7	8.0	82.7	5.2	4.5	9.7
1937	4.7	3.8	8.5	90.8	5.2	4.2	9.4
1938	2.3	3.8	6.1	85.2	2.7	4.5	7.2
1939	5.0	3.9	8.9	91.1	5.5	4.3	9.8
1940	6.5	4.0	10.5	100.6	6.5	4.0	10.4
1941	9.4	4.5	13.9	125.8	7.5	3.6	11.0
1942	9.5	5.1	14.6	159.1	6.0	3.2	9.2
1943	10.5	5.5	16.0	192.5	5.5	2.9	8.3
1944	10.4	6.3	16.7	211.4	4.9	3.0	7.9
1945	8.3	6.7	15.0	213.6	3.9	3.1	7.0
1946	13.4	5.2	18.6	210.7	6.4	2.5	8.8
1947	18.2	6.3	24.5	234.3	7.8	2.7	10.5
1948	20.5	7.7	28.2	259.4	7.9	3.0	10.9
1949	16.0	8.5	24.5	258.1	6.2	3.3	9.5
1950	22.8	9.4	32.2	284.6	8.0	3.3	11.3
1951	19.7	11.0	30.7	329.0	6.0	3.3	9.3
1952	17.2	12.3	29.6	347.0	5.0	3.5	8.5
1953	18.1	14.1	32.2	365.4	5.0	3.9	8.8
1954	16.8	15.8	32.7	363.1	4.6	4.4	9.0
1955	23.0	18.4	41.4	397.5	5.8	4.6	10.4
1956	23.5	20.0	43.5	419.2	5.6	4.8	10.4
1957	22.3	21.8	44.1	442.8	5.0	4.9	9.9
1958	18.8	22.7	41.4	444.5	4.2	5.1	9.3
1959	24.5	24.3	48.7	482.7	5.1	5.0	10.1
1960	22.0	25.6	47.6	502.6	4.4	5.1	9.5
1961 [3]	21.8	26.8	48.6	518.2	4.2	5.2	9.4
1962 [3]	[2] 24.6	30.8	55.4	554.9	4.4	5.6	10.0
1963 [3]	[2] 27.1	32.4	59.5	585.1	4.6	5.5	10.2

[1] Includes depreciation, capital outlays charged to current accounts and accidental damages.
[2] The figures for 1962 and 1963 reflect the new depreciation guidelines issued by the Treasury Department, July 11, 1962, and the investment tax credit provided in the Revenue Act of 1962.
[3] Preliminary.

Source: Department of Commerce.

TABLE 33.—*Corporate profits after tax and corporate profits after tax, depreciation, amortization, and inventory valuation adjustment as percentages of corporate gross product, 1947–62*

Year (1)	Corporate profits after tax as a percent of corporate gross product (2)	Corporate profits after tax plus depreciation, amortization, and inventory valuation adjustment as a percent of corporate gross product (3)
1947	14.3	13.8
1948	14.0	17.0
1949	11.0	17.7
1950	13.9	15.8
1951	10.3	14.7
1952	8.5	14.6
1953	8.4	13.8
1954	7.8	14.6
1955	9.6	16.0
1956	9.1	15.4
1957	8.2	15.3
1958	7.0	15.3
1959	8.3	16.2
1960	7.2	15.5
1961	6.8	15.3
1962	7.2	16.4

Source: Department of Commerce, Office of Business Economics.

TABLE 34.—*Corporation income tax returns: Net income and income tax by size of net income, 1961*

Size of net income	Total [1]		Returns with income tax							
			Total			With alternative tax				
									Income tax	
	Number of returns	Net income or deficit [2]	Number of returns	Net income or deficit [2]	Income tax	Number of returns	Net income [2]	Net long-term capital gain taxed at 25 percent	Alternative method	If alternative method had not been used
Active corporation returns, total	1,190,286	*Millions* $45,894	553,873	*Millions* $48,939	*Millions* $22,188	77,647	*Millions* $33,386	*Millions* $2,588	*Millions* $15,641	*Millions* $16,341
Returns with net income, total	715,589	52,401	553,628	48,974	22,187	77,647	33,386	2,588	15,641	16,341
Under $5,000	336,062	494	236.550	349	86	10,857	25	9	6	17
$5,000 under $10,000	107,425	728	82,833	559	158	8,880	61	16	16	25
$10,000 under $15,000	63,126	752	51,503	612	174	7,143	85	19	23	30
$15,000 under $20,000	42,996	727	36,618	617	177	6,389	108	22	30	36
$20,000 under $25,000	38,593	850	34,359	756	219	5,987	132	22	37	43
$25,000 under $50,000	65,357	2,163	56,031	1,845	608	13,963	473	84	148	169
$50,000 under $100,000	29,629	2,045	25,722	1,780	720	9,203	646	116	247	276
$100,000 under $250,000	18,232	2,799	16,650	2,565	1,126	7,442	1,169	187	492	540
$250,000 under $500,000	6,516	2,267	6,171	2,149	983	3,201	1,127	168	495	539
$500,000 under $1,000,000	3,415	2,377	3,227	2,243	1,041	1,189	1,327	174	606	650
$1,000,000 under $5,000,000	3,100	6,420	2,902	6,012	2,797	1,905	4,070	491	1,878	2,006
$5,000,000 under $10,000,000	557	3,891	518	3,618	1,681	381	2,673	270	1,233	1,306
$10,000,000 under $25,000,000	339	5,335	313	4,896	2,321	223	3,498	310	1,652	1,733
$25,000,000 under $50,000,000	138	5,091	132	4,899	2,385	105	3,889	320	1,884	1,969
$50,000,000 under $100,000,000	69	4,741	65	4,468	2,178	52	3,597	139	1,782	1,819
$100,000,000 or more	35	11,721	34	11,606	5,534	27	10,506	241	5,112	5,183
Returns with no net income, total	474,697	[3] 6,507	245	[3] 35	1	----------	----------	----------	----------	----------

[1] Includes small business corporations filing Form 1120-S for which an election had been made to be taxed through shareholders.

[2] Excludes tax-exempt interest.

[3] Deficit.

Source: Internal Revenue Service: Statistics of Income—1961-62, Corporation Income Tax Returns.

TABLE 35.—*Corporation income tax returns: Total assets, net income, and income tax, by size of total assets, 1961*

Size of total assets	All returns		Returns with net income			
	Number of returns	Total assets	Number of returns	Total assets	Net income [1]	Income tax
		Thousands		*Thousands*	*Thousands*	*Thousands*
Total	1,190,286	$1,289,516,071	715,589	$1,086,797,445	$52,401,331	$22,188,057
Under $50,000	506,738	9,606,722	233,179	5,163,741	1,105,453	284,981
$50,000 under $100,000	206,039	14,756,377	131,645	9,514,786	941,740	205,647
$100,000 under $250,000	239,057	38,022,849	171,639	27,472,199	2,229,741	587,768
$250,000 under $500,000	111,593	38,925,387	83,021	29,005,247	2,035,017	624,386
$500,000 under $1,000,000	58,065	40,246,513	43,710	30,290,477	2,170,025	797,201
$1,000,000 under $5,000,000	49,262	103,911,467	37,550	79,646,406	4,900,429	2,075,262
$5,000,000 under $10,000,000	8,564	59,864,509	6,584	45,945,122	2,201,212	969,873
$10,000,000 under $50,000,000	8,336	171,786,141	6,120	125,368,147	5,889,661	2,592,973
$50,000,000 under $100,000,000	1,204	84,155,342	901	63,170,187	3,298,736	1,451,503
$100,000,000 or more	1,428	728,240,764	1,240	671,221,133	27,629,317	12,598,463
	Percentage distribution					
Total	100.0	100.0	100.0	100.0	100.0	100.0
Under $50,000	42.6	.7	32.6	.5	2.1	1.3
$50,000 under $100,000	17.3	1.1	18.4	.9	1.8	.9
$100,000 under $250,000	20.1	2.9	24.0	2.5	4.3	2.6
$250,000 under $500,000	9.4	3.0	11.6	2.7	3.9	2.8
$500,000 under $1,000,000	4.9	3.1	6.1	2.8	4.1	3.6
$1,000,000 under $5,000,000	4.1	8.1	5.2	7.3	9.4	9.4
$5,000,000 under $10,000,000	.8	4.6	.9	4.2	4.2	4.4
$10,000,000 under $50,000,000	.7	13.3	.9	11.5	11.2	11.7
$50,000,000 under $100,000,000	.1	6.5	.1	5.8	6.3	6.5
$100,000,000 or more	.1	57.5	.2	61.8	52.7	56.8

[1] Excludes tax-exempt interest.

Source: Internal Revenue Service: Statistics of Income—1961–62, Corporation Income Tax Returns.

TABLE 36.—*Corporation income tax returns: Distribution of taxable income and income tax by size of income taxed at normal and surtax rates, 1961*

Size of income taxed at normal tax and surtax rates	Number of taxable returns	Taxable income			Income tax [1,2]	
		Total	Taxed at normal tax and surtax rates	Net long-term capital gain taxed at 25 percent	Amount	Percent distribution
		Millions	*Millions*	*Millions*	*Millions*	
Total	[1] 553,873	[1,2] $47,937.7	[1] $43,636.0	[1] $2,611.9	$22,188.1	100.0
0	4,632	508.3	------------	508.3	165.5	0.6
$1 under $5,000	248,877	437.6	349.5	88.1	114.9	.5
$5,000 under $10,000	80,539	603.2	540.9	62.3	178.2	.8
$10,000 under $15,000	49,992	643.3	593.2	50.1	189.1	.9
$15,000 under $20,000	34,779	625.4	586.9	38.5	185.9	.8
$20,000 under $25,000	33,657	777.6	741.6	36.0	230.6	1.0
$25,000 under $50,000	51,541	1,831.6	1,691.3	140.3	631.0	2.8
$50,000 under $100,000	23,050	1,683.8	1,590.9	92.9	723.4	3.3
$100,000 under $250,000	14,816	2,475.5	2,271.7	203.8	1,150.8	5.2
$250,000 under $500,000	5,441	2,027.0	1,889.8	137.2	987.0	4.4
$500,000 under $1,000,000	2,858	2,124.0	1,990.5	133.5	1,052.4	4.7
$1,000,000 under $5,000,000	2,510	5,543.4	5,237.8	305.6	2,786.0	12.6
$5,000,000 under $10,000,000	449	3,213.2	3,086.6	126.6	1,633.9	7.4
$10,000,000 under $25,000,000	276	4,564.6	4,329.9	234.7	2,311.4	10.4
$25,000,000 under $50,000,000	120	4,492.3	4,357.6	134.7	2,299.9	10.4
$50,000,000 under $100,000,000	63	4,428.4	4,306.9	121.5	2,269.0	10.2
$100,000,000 or more	28	10,265.2	10,069.4	195.8	5,299.8	23.9

[1] Included in the total but not in the detail are data from 245 returns without net income which were taxable due to special provisions of the law affecting insurance businesses.
[2] Included in the total but not in the detail are amounts reported by 391 mutual insurance companies subject to tax on gross income under sec. 821(a)(2) of the Internal Revenue Code. Taxable income for these companies was $1,690,000,000 and income tax was $16,900,000.

Source: Internal Revenue Service: Statistics of Income—1961–62, Corporation Income Tax Returns.

TABLE 37.—*Depreciation deductions, by guideline and nonguideline use, and investment tax credit, all corporations, 1962*

[In millions of dollars]

	Corporate Depreciation						1962 investment tax credit
	1960	1961	1962				
			Total	Using Guidelines	Not using Guidelines	Additional depreciation from guideline use	
All corporations	22,160	23,577	27,708	14,771	12,937	2,431	1,041
Manufacturing and mining	10,559	11,202	13,623	9,323	4,300	1,723	516
Food and beverage	965	1,016	1,234	745	489	119	58
Textile	319	353	425	245	180	38	20
Paper	466	511	673	586	87	121	25
Chemical	1,154	1,266	1,562	1,380	182	263	68
Petroleum refining and extraction	1,739	1,803	2,055	1,223	832	166	45
Rubber	214	237	300	178	122	30	16
Stone, clay and glass	460	482	599	386	213	92	29
Metal refining and extraction	1,188	1,228	1,590	1,288	302	287	61
Iron and steel manufacturing	661	n.a.	899	813	86	182	27
Machinery except electrical	860	926	1,130	532	598	75	30
Electrical machinery	478	528	628	489	139	71	24
Motor vehicles and parts	713	721	870	841	29	149	32
Transportation equipment excluding motor vehicles	255	254	245	90	155	14	10
Other manufacturing and mining	1,748	1,877	2,312	1,340	972	298	98
Transportation	1,942	2,066	2,557	1,481	1,076	365	102
Public utilities	2,220	2,395	2,621	1,279	1,342	104	103
Communication	1,084	1,199	1,334	210	1,124	11	75
Commercial and other	6,355	6,715	7,573	2,478	5,095	228	245

NOTE.—For further information relating to this table, see Department of Commerce, Survey of Current Business, July 1963, pp. 3–9.

Source: Data for 1960 and 1961 from the Internal Revenue Service; 1962 estimates based on survey by the Office of Business Economics, Department of Commerce.

TABLE 38.—*Corporate tax liabilities, tax reductions resulting from investment tax credit and new depreciation guidelines, and cash flow, 1962*

	Tax liability	Tax reduction			Cash[1] flow	Reduction in tax liability as a percentage of cash flow
		Total	From investment tax credit	From depreciation guidelines		
	Millions of dollars					
All corporations	22,169	2,271	1,041	1,230	36,352	6
Manufacturing and mining	11,993	1,387	516	871	19,195	7
Communications and public utilities	3,249	235	178	57	4,966	5
Transportation	402	274	102	172	2,341	12
Trade and services	2,802	247	158	89	5,631	4
All other	3,723	128	87	41	4,219	3

[1] Undistributed profits plus depreciation allowances.

NOTE.—For futher information relating to this table, see Department of Commerce, Survey of Current Business, July 1963, pp. 3–9.

Source: U.S. Department of Commerce, Office of Business Economics.

TABLE 39.—*Corporate depreciation and amortization deductions, 1941–61—Statistics of Income data* [1]

Year	Corporate profits before deductions for depreciation and amortization [2]	Depreciation	Amortization	Total depreciation and amortization: Amount	Total depreciation and amortization: Percent of corporate profits
	Millions	*Millions*	*Millions*	*Millions*	
1941	$20,554	$3,765	$114	$3,879	18.9
1942	27,714	3,914	411	4,325	15.6
1943	32,733	3,916	691	4,607	14.1
1944	31,478	3,950	981	4,931	15.7
1945	27,273	3,977	1,951	5,928	21.7
1946	29,665	4,202	64	4,266	14.4
1947	36,894	5,220	59	5,279	14.3
1948	40,926	6,299	39	6,338	15.5
1949	35,608	7,191	31	7,222	20.3
1950	50,733	7,858	43	7,901	15.6
1951	52,920	8,829	292	9,121	17.2
1952	49,171	9,604	831	10,436	21.2
1953	51,827	10,511	1,515	12,026	23.2
1954	50,412	(3)	(3)	13,691	27.2
1955	63,958	13,419	2,590	16,009	25.0
1956	64,991	14,953	2,626	17,579	27.0
1957	64,506	16,968	2,464	19,432	30.1
1958	59,900	18,677	1,999	20,676	34.5
1959	69,714	20,494	1,566	22,060	31.6
1960	67,876	22,160	1,217	23,377	34.4
1961	71,694	23,688	972	24,660	34.4

[1] Statistics of Income and national income data differ in certain respects.
[2] Also before Federal income and excess profits taxes.
[3] Not available separately.

Source: Internal Revenue Service: Statistics of Income, Corporation Income Tax Returns.

TABLE 40.—*Corporation income tax returns: Depreciation and amortization deductions by size of total assets, 1961*

Size of total assets	Amount: Depreciation	Amount: Amortization	Amount: Total	Percentage distribution: Depreciation	Percentage distribution: Amortization	Percentage distribution: Total
	Millions	*Millions*	*Millions*			
Total	$23,687.8	$971.8	$24,659.6	100.0	100.0	100.0
Under $50,000	714.5	21.0	735.5	3.0	2.2	3.0
$50,000 under $100,000	634.4	6.7	641.1	2.7	.7	2.6
$100,000 under $250,000	1,484.1	26.9	1,511.0	6.3	2.8	6.1
$250,000 under $500,000	1,322.9	23.1	1,346.0	5.6	2.4	5.5
$500,000 under $1,000,000	1,251.9	20.3	1,272.2	5.3	2.1	5.2
$1,000,000 under $5,000,000	2,399.9	62.6	2,462.5	10.1	6.4	10.0
$5,000,000 under $10,000,000	920.0	20.7	940.7	3.9	2.1	3.8
$10,000,000 under $50,000,000	2,282.4	53.2	2,335.6	9.6	5.5	9.5
$50,000,000 under $100,000,000	1,247.2	25.6	1,272.8	5.3	2.6	5.2
$100,000,000 or more	11,430.6	711.6	12,142.2	48.3	73.2	49.2

Source: Internal Revenue Service: Statistics of Income—1961–62, Corporation Income Tax Returns.

TABLE 41.—*Corporation income tax returns: Depreciation and amortization deductions as a percent of net income, by size of total assets, 1961*

Size of total assets	Net income [1]	Depreciation deduction	Amortization deduction	Total amortization and depreciation deductions	Total amortization and depreciation as a percent of net income
	Millions	*Millions*	*Millions*	*Millions*	
Total	$47, 034. 1	$23, 687. 8	$971. 8	$24, 659. 6	------------
Returns with net income, total	53, 479. 0	19, 769. 3	721. 5	20, 490. 8	38. 3
Under $50,000	1, 109. 8	381. 7	14. 1	395. 8	35. 7
$50,000 under $100,000	942. 3	404. 0	3. 8	407. 8	43. 3
$100,000 under $250,000	2, 231. 2	1, 071. 8	18. 8	1, 090. 6	48. 9
$250,000 under $500,000	2, 037. 4	967. 7	16. 6	984. 3	48. 3
$500,000 under $1,000,000	2, 174. 8	930. 5	12. 3	942. 8	43. 4
$1,000,000 under $5,000,000	4, 953. 1	1, 780. 6	34. 9	1, 815. 5	36. 7
$5,000,000 under $10,000,000	2, 263. 5	719. 1	12. 6	731. 7	32. 3
$10,000,000 under $50,000,000	6, 109. 4	1, 856. 6	37. 8	1, 894. 4	31. 0
$50,000,000 under $100,000,000	3, 385. 2	1, 016. 9	21. 3	1, 038. 2	30. 7
$100,000,000 or more	28, 272. 4	10, 640. 4	549. 3	11, 189. 7	39. 6
Returns without net income	[2] 6, 444. 8	3, 918. 5	250. 3	4, 168. 9	------------

[1] Includes tax-exempt interest.
[2] Net loss.

Source: Internal Revenue Service: Statistics of Income—1961–62, Corporation Income Tax Returns.

TABLE 42.—*Corporation income tax returns: Methods used by corporations to compute tax depreciation, by size of total assets and by industrial division, 1960* [1]

Size of total assets, by industrial division	Total number of active corporation returns	Returns with depreciation										
		Number of returns	Amount of depreciation	Returns with methods of depreciation shown [2]								
				Total		Straight line		Declining balance		Sum of years-digits		Depreciation claimed under other methods and with methods not shown
				Number of returns	Amount of depreciation	Number of returns	Amount of depreciation	Number of returns	Amount of depreciation	Number of returns	Amount of depreciation	
			Millions		*Millions*		*Millions*		*Millions*		*Millions*	*Millions*
All industrial divisions	1,140,574	932,977	$22,159.7	816,417	$19,293.1	769,515	$11,222.7	194,913	$4,672.8	47,810	$2,858.9	$473.4
Under $500,000	1,018,930	818,892	3,910.4	720,984	3,738.0	679,216	2,687.0	157,339	837.4	33,268	154.7	17.6
$500,000 under $1,000,000	54,991	51,128	1,200.3	43,774	1,005.4	41,163	633.6	16,876	292.1	5,362	65.5	5.6
$1,000,000 under $10,000,000	56,263	52,980	3,243.0	43,512	2,747.7	41,193	1,600.7	17,512	784.9	7,249	292.9	56.7
$10,000 under $50,000,000	7,912	7,604	2,142.5	6,149	1,703.2	5,994	968.5	2,305	435.9	1,289	253.5	43.2
$50,000,000 under $250,000,000	1,911	1,823	3,094.0	1,531	2,655.6	1,498	1,391.1	642	654.1	459	527.3	82.6
$250,000,000 or more	567	550	8,569.4	467	7,443.1	451	3,941.8	239	1,668.4	183	1,565.0	267.7
Agriculture, forestry, and fisheries	17,139	15,517	178.2	12,270	128.5	11,619	92.1	3,321	29.9	644	4.9	.3
Under $500,000	15,750	14,187	100.4	11,223	75.3	10,604	55.7	2,917	16.2	530	2.3	(3)
$500,000 under $1,000,000	838	788	18.7	644	16.9	624	11.4	229	4.8	63	.6	(3)
$1,000,000 under $10,000,000	528	519	35.3	383	28.8	371	19.3	167	7.4	47	1.7	.3
$10,000,000 under $50,000,000	21	21	7.7	20	7.5	20	5.7	8	1.5	4	.3	(3)
$50,000,000 under $250,000,000	1	1	2.1	---	---	---	---	---	---	---	---	---
$250,000,000 or more	1	1	14.0	---	---	---	---	---	---	---	---	---
Mining	13,017	10,274	719.6	7,718	508.8	7,311	308.6	2,279	98.1	549	20.1	81.0
Under $500,000	10,784	8,131	106.3	6,152	86.3	5,827	60.1	1,659	20.0	382	2.6	2.9
$500,000 under $1,000,000	953	924	51.5	695	36.1	670	22.8	284	10.2	52	1.1	1.8
$1,000,000 under $10,000,000	1,084	1,024	181.3	727	126.5	679	75.5	285	32.5	92	5.2	13.1
$10,000,000 under $50,000,000	144	144	116.1	107	79.6	102	49.9	34	10.9	14	6.1	12.6
$50,000,000 under $250,000,000	40	39	131.2	29	90.1	27	55.4	14	8.6	8	4.5	21.6
$250,000,000 or more	12	12	133.0	8	90.3	6	45.0	3	15.9	1	.5	29.0
Construction	72,332	60,106	627.0	53,228	510.0	50,809	287.0	14,193	184.0	3,216	32.5	3.3
Under $500,000	67,191	55,273	287.6	49,282	255.0	47,027	172.3	12,130	68.0	2,628	12.1	.2
$500,000 under $1,000,000	2,873	2,660	83.3	2,149	60.6	2,054	31.4	1,065	25.7	259	3.0	(3

$1,000,000 under $10,000,000	2,156	2,063	180.8	1,717	147.7	1,650	62.6	952	69.4	311	12.4	2.9
$10,000,000 under $50,000,000	103	101	53.9	72	33.3	70	16.6	40	13.5	15	3.2	(2)
$50,000,000 under $250,000,000	9	9	21.5	8	13.3	8	4.0	6	7.4	3	1.9	(2)
$250,000,000 or more	----	----	----	----	----	----	----	----	----	----	----	----
Manufacturing	165,862	151,153	9,838.6	136,504	8,540.8	131,842	4,325.8	40,771	1,913.1	14,300	1,993.6	281.1
Under $500,000	137,871	123,433	835.7	112,590	754.1	108,708	535.9	29,619	157.9	8,124	42.0	2.8
$500,000 under $1,000,000	12,107	11,991	340.5	10,356	293.9	10,020	188.5	4,427	72.3	2,079	27.0	1.9
$1,000,000 under $10,000,000	13,674	13,520	1,256.8	11,657	1,104.3	11,263	649.5	5,716	278.2	3,256	154.7	15.4
$10,000,000 under $50,000,000	1,605	1,604	1,099.0	1,359	913.1	1,320	500.4	700	217.0	547	181.8	13.2
$50,000,000 under $250,000,000	480	480	1,731.6	427	1,507.5	420	741.0	236	330.8	227	400.4	35.1
$250,000,000 or more	125	125	4,575.0	115	3,967.8	111	1,710.5	73	856.9	67	1,187.8	212.6
Transportation, communication, electric, gas, and sanitary services	43,852	38,958	5,246.4	33,545	4,611.8	31,634	2,923.6	7,834	1,233.1	1,860	400.9	51.2
Under $500,000	38,979	34,192	315.9	29,631	325.5	27,919	229.2	6,234	81.5	1,302	10.8	2.1
$500,000 under $1,000,000	2,038	1,974	104.1	1,695	88.2	1,602	55.4	593	26.3	161	5.2	.8
$1,000,000 under $10,000,000	2,226	2,189	395.0	1,703	307.1	1,622	179.0	710	92.4	285	30.7	4.6
$10,000,000 under $50,000,000	329	323	310.5	268	247.1	253	149.0	132	77.9	46	18.4	3.8
$50,000,000 under $250,000,000	171	171	773.6	151	657.7	143	357.6	95	225.3	30	55.2	19.6
$250,000,000 or more	109	109	3,347.2	97	2,984.2	95	1,953.5	70	729.7	36	280.7	20.3
Wholesale and retail trade	355,623	312,431	2,125.2	269,575	1,928.5	257,673	1,303.9	57,717	398.4	12,941	199.8	11.5
Under $500,000	330,624	288,048	932.4	248,872	913.7	237,620	692.4	49,706	182.7	9,828	25.6	2.0
$500,000 under $1,000,000	15,041	14,679	211.0	12,636	182.0	12,236	122.1	4,606	45.0	1,521	12.7	.3
$1,000,000 under $10,000,000	9,348	9,105	393.2	7,580	330.2	7,336	215.9	3,177	76.0	1,436	34.0	2.3
$10,000,000 under $50,000,000	517	507	197.8	407	149.8	402	89.7	191	36.2	117	22.1	1.7
$50,000,000 under $250,000,000	74	74	188.8	64	163.1	64	85.2	31	29.9	30	47.0	1.0
$250,000,000 or more	19	18	202.0	16	189.8	15	98.6	6	28.6	9	58.4	4.2
Finance, insurance, and real estate	334,388	238,363	1,986.8	209,811	1,861.4	191,041	1,245.5	46,872	474.5	9,251	119.8	14.5
Under $500,000	284,841	194,608	662.2	173,785	741.7	157,839	556.5	35,159	154.3	6,146	26.9	1.4
$500,000 under $1,000,000	17,906	15,041	207.9	13,029	184.7	11,657	114.5	4,452	62.0	825	7.4	.1
$1,000,000 under $10,000,000	25,175	22,633	475.8	18,120	436.2	16,774	253.6	5,780	148.7	1,531	26.4	5.2
$10,000,000 under $50,000,000	5,050	4,767	213.0	3,813	177.6	3,729	113.6	1,146	47.3	525	14.5	.9
$50,000,000 under $250,000,000	1,116	1,030	146.7	834	127.3	819	80.4	249	28.6	155	12.8	5.2
$250,000,000 or more	300	284	281.2	230	194.0	223	126.9	86	33.5	69	31.9	1.6
Services	121,024	102,846	1,433.2	91,274	1,200.0	85,287	734.0	21,548	340.9	4,995	87.3	30.6
Under $500,000	115,718	97,746	666.5	86,999	583.7	81,413	382.8	19,549	156.3	4,276	32.3	6.1
$500,000 under $1,000,000	3,132	3,039	182.8	2,548	142.6	2,278	87.3	1,209	45.5	402	8.6	.6
$1,000,000 under $10,000,000	2,011	1,905	324.6	1,605	266.9	1,480	145.3	724	80.2	289	27.9	13.1
$10,000,000 under $50,000,000	142	136	143.9	103	93.2	98	43.6	54	31.6	21	7.1	10.9
$50,000,000 under $250,000,000	20	19	98.4	18	96.6	17	67.5	11	23.6	6	5.5	----
$250,000,000 or more	1	1	16.9	1	16.9	1	7.4	1	3.8	1	5.8	----

See footnotes at end of table, p. 258.

TABLE 42.—*Corporation income tax returns: Methods used by corporations to compute tax depreciation, by size of total assets and by industrial division, 1960* [1]—Continued

Size of total assets, by industrial division	Total number of active corporation returns	Returns with depreciation										
		Number of returns	Amount of depreciation	Returns with methods of depreciation shown [2]								
				Total		Straight line		Declining balance		Sum of years-digits		Depreciation claimed under other methods and with methods not shown
				Number of returns	Amount of depreciation	Number of returns	Amount of depreciation	Number of returns	Amount of depreciation	Number of returns	Amount of depreciation	
			Millions		*Millions*		*Millions*		*Millions*		*Millions*	*Millions*
Nature of business not allocable	17,337	3,329	$4.7	2,492	$3.3	2,299	$2.3	378	$.8	54	(2)	----------
Under $500,000	17,172	3,274	3.4	2,450	2.7	2,259	2.1	366	.5	52	(2)	----------
$500,000 under $1,000,000	103	32	.5	22	.5	22	.2	11	.3	----------	----------	----------
$1,000,000 under $10,000,000	61	22	(2)	20	(2)	18	(2)	1	----------	2	----------	----------
$10,000,000 under $50,000,000	1	1	.6	----------	----------	----------	----------	----------	----------	----------	----------	----------
$50,000,000 under $250,000,000	----------	----------	----------	----------	----------	----------	----------	----------	----------	----------	----------	----------
$250,000,000 or more	----------	----------	----------	----------	----------	----------	----------	----------	----------	----------	----------	----------

[1] Corporation income tax returns with accounting periods ended July 1960 through June 1961.
[2] Corporations may use more than 1 method; therefore, number of returns for each method exceeds total with methods shown.

Source: Internal Revenue Service: Statistics Division.

TABLE 43.—*Corporation income tax returns: Depletion deductions, by size of total assets, 1950–61* [1]

[Dollar amounts in millions]

Size of total assets	1950	1951	1952	1953	1954	1955	1956	1957	1958	1959	1960	1961
Total	$1,691.8	$2,065.8	$2,112.9	$2,284.3	$2,242.4	$2,779.1	$3,056.7	$3,329.7	$3,137.0	$3,239.4	$3,522.6	$3,586.6
Under $50,000	4.0	3.5	3.1	4.7	4.2	5.7	8.6	12.5	9.2	25.4	17.5	22.1
$50,000, under $100,000	4.4	3.7	5.2	3.7	4.3	5.2	6.9	6.4	5.9	4.5	5.2	7.7
$100,000, under $250,000	12.6	12.1	13.5	13.5	15.7	27.2	21.1	22.7	22.3	16.4	18.3	22.0
$250,000, under $500,000	17.1	21.4	21.2	21.4	22.6	26.0	27.5	33.8	32.1	28.6	60.6	32.2
$500,000, under $1,000,000	31.5	41.4	35.1	38.6	32.2	45.1	43.1	47.0	42.8	28.8	36.0	36.2
$1,000,000, under $5,000,000	120.8	160.8	150.3	154.0	147.0	191.5	181.6	174.1	167.0	165.6	190.2	179.2
$5,000,000, under $10,000,000	68.5	83.8	85.7	83.3	73.7	80.0	96.7	124.6	91.4	96.4	139.9	98.4
$10,000,000, under $50,000,000	278.9	318.9	297.7	306.1	290.3	351.2	339.9	358.3	333.6	341.0	306.6	297.1
$50,000,000, under $100,000,000	115.2	120.8	131.2	119.8	134.0	178.1	249.0	241.6	200.2	206.3	222.2	213.9
$100,000,000 or more	1,038.8	1,299.3	1,370.0	1,539.3	1,517.9	1,869.0	2,082.5	2,308.6	2,232.5	2,326.5	2,526.0	2,677.7
	Percentage distribution											
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Under $50,000	.2	.2	.1	.2	.2	.2	.3	.4	.3	.8	.5	.6
$50,000, under $100,000	.3	.2	.2	.2	.2	.2	.2	.2	.2	.1	.1	.2
$100,000, under $250,000	.7	.6	.6	.6	.7	1.0	.7	.7	.7	.5	.5	.6
$250,000, under $500,000	1.0	1.0	1.0	.9	1.0	.9	.9	1.0	1.0	.9	1.7	.9
$500,000, under $1,000,000	1.9	2.0	1.7	1.7	1.4	1.6	1.4	1.4	1.4	.9	1.0	1.0
$1,000,000, under $5,000,000	7.1	7.8	7.1	6.7	6.6	6.9	5.9	5.2	5.3	5.1	5.4	5.0
$5,000,000, under $10,000,000	4.1	4.1	4.1	3.6	3.3	2.9	3.2	3.7	2.9	3.0	4.0	2.7
$10,000,000, under $50,000,000	16.5	15.4	14.1	13.4	12.9	12.6	11.1	10.8	10.6	10.5	8.7	8.3
$50,000,000, under $100,000,000	6.8	5.8	6.2	5.2	6.0	6.4	8.1	7.3	6.4	6.4	6.3	6.0
$100,000,000, or more	61.4	62.9	64.8	67.4	67.7	67.3	68.1	69.3	71.2	71.8	71.7	74.7

[1] Based on all returns with balance sheets for 1950–58; for 1959–61 based on all active corporation returns.

Source: Internal Revenue Service: Statistics of Income, Corporation Income Tax Returns.

TABLE 44.—*Corporation income tax returns: Depletion deductions and net income, selected major industrial groups, 1961* [1]

Major industrial group	Net income [2]	Depletion deduction	Depletion deduction as percent of net income
	Millions	*Millions*	
All industrial groups	$52,401.3	$3,118.1	6.0
Agriculture, forestry, and fisheries	249.0	11.1	4.5
Mining, total	1,351.1	766.8	56.8
Crude petroleum and natural gas	768.9	497.4	64.7
Other mining	582.2	269.4	46.3
Construction	978.4	7.4	.8
Manufacturing, total	24,549.1	2,121.2	8.6
Chemicals and allied products	3,398.9	87.8	2.6
Petroleum refining and related industries	1,794.0	1,605.4	89.5
Stone, clay and glass products	952.3	68.3	7.2
Primary metal industries	1,761.6	134.7	7.6
Transportation, communication, electric, gas, and sanitary services	8,022.2	96.9	1.2
Wholesale and retail trade	5,861.9	23.4	.4
Finance, insurance, and real estate, total	9,911.1	89.6	.9
Lessors of real properties except buildings	113.4	30.3	26.7
Services, total	1,471.2	1.6	.1
Nature of business not allocable	6.9		

[1] Corporation income tax returns with net income.
[2] Excludes tax-exempt interest.

Source: Internal Revenue Service: Statistics of Income—1961-62, Corporation Income Tax Returns.

TABLE 45.—*Corporation income tax returns: Depletion deduction and net income, by size of total assets, 1961* [1]

Size of total assets	Net income [2]	Depletion deductions	Depletion deduction as percent of net income
	Millions	*Millions*	
Total	$52,401.3	$3,118.1	6.0
Under $50,000	1,105.5	12.3	1.1
$50,000 under $100,000	941.7	5.8	.6
$100,000 under $250,000	2,229.7	12.3	.6
$250,000 under $500,000	2,035.0	22.5	1.1
$500,000 under $1,000,000	2,170.0	23.2	1.1
$1,000,000 under $5,000,000	4,900.4	105.2	2.1
$5,000,000 under $10,000,000	2,201.2	67.6	3.1
$10,000,000 under $50,000,000	5,889.7	209.4	3.6
$50,000,000 under $100,000,000	3,298.7	143.2	4.3
$100,000,000 or more	27,629.3	2,516.7	9.1

[1] Corporation income tax returns with net income.
[2] Excludes tax-exempt interest.

Source: Internal Revenue Service; Statistics of Income—1961-62, Corporation Income Tax Returns.

TABLE 46.—*Dividend distributions as a percent of corporate profits after tax and of corporate profits after tax, depreciation, amortization and inventory valuation adjustment, 1946–62*

[Millions of dollars]

Year	Net dividends paid (1)	Corporate profits after tax (2)	Corporate depreciation and amortization (3)	Inventory valuation adjustment (4)	Net dividends as a percent of profits after tax (5)	Net dividends as a percent of cols. 2, 3, and 4 (6)
1946	5,784	13,440	4,267	−5,263	43.0	46.5
1947	6,521	18,242	5,280	−5,899	35.7	37.0
1948	7,243	20,517	6,340	−2,152	35.3	29.3
1949	7,473	15,995	7,223	1,856	46.7	29.8
1950	9,208	22,763	7,904	−4,965	40.5	35.8
1951	9,029	19,706	9,129	−1,199	45.8	32.7
1952	8,954	17,232	10,423	981	52.0	31.3
1953	9,225	18,089	12,029	−997	51.0	31.7
1954	9,839	16,841	13,694	−318	58.4	32.6
1955	11,215	23,035	15,928	−1,736	48.7	30.1
1956	12,132	23,456	17,488	−2,693	51.7	31.7
1957	12,588	22,286	19,333	−1,539	56.5	31.4
1958	12,358	18,764	20,550	−255	65.9	31.6
1959	13,682	24,469	21,913	−465	55.9	29.8
1960	14,523	22,009	23,204	192	66.0	32.0
1961	15,266	21,770	24,372	−16	70.1	33.1
1962	16,563	24,645	28,270	183	67.2	31.2

Source: Department of Commerce, Office of Business Economics.

TABLE 47.—*Sources and uses of corporate funds, 1946–63*

[In billions of dollars]

Source or use of funds	1946	1947	1948	1949	1950	1951	1952	1953	1954	1955	1956	1957	1958	1959	1960	1961	1962	1963
Uses:																		
Plant and equipment outlays	12.5	17.0	18.8	16.3	16.9	21.6	22.4	23.9	22.4	24.2	29.9	32.7	26.4	27.7	30.8	29.6	32.0	34.0
Inventories (change in book value)	11.2	7.1	4.2	−3.6	9.8	9.8	1.3	1.8	−1.6	6.7	7.6	2.1	−2.4	6.6	2.5	1.8	3.8	4.3
Change in customer net receivables [2]	1.1	3.1	2.8	.9	5.0	2.0	3.1	.7	2.4	6.4	3.3	2.1	2.9	5.6	4.2	3.5	5.8	6.4
Cash and U.S. Government securities	−4.7	1.0	1.0	3.2	4.5	2.8	.1	1.8	(3)	5.0	−4.3	−.3	2.7	2.9	−1.7	2.5	1.2	.9
Other assets	−.6	(3)	.2	(3)	.3	.6	.4	(3)	.8	2.8	3.0	1.3	1.9	4.1	3.5	4.9	5.3	6.8
Total uses	19.5	28.2	27.0	16.8	36.5	36.8	27.3	28.2	24.0	45.1	39.5	37.8	31.5	46.8	39.3	42.3	48.1	52.4
Sources:																		
Internal:																		
Retained profits and depletion allowances	7.2	11.4	12.6	7.8	13.0	10.0	7.4	7.9	6.3	10.9	10.5	8.9	5.7	9.5	6.2	5.6	7.0	7.8
Depreciation and amortization allowances	4.2	5.2	6.2	7.1	7.8	9.0	10.4	11.8	13.5	15.7	17.3	19.1	20.3	21.6	22.9	24.0	27.8	29.5
Total internal sources	11.4	16.6	18.8	14.9	20.8	19.0	17.8	19.7	19.8	26.6	27.8	28.0	26.0	31.1	29.1	29.6	34.9	37.4
External:																		
Change in Federal income tax liability	−1.6	2.1	.9	−2.2	7.3	4.3	−3.1	.6	−3.1	3.8	−1.7	−2.2	−2.5	2.1	−1.6	.6	.9	1.2
Other liabilities	2.1	1.5	.4	.5	1.0	1.9	2.4	2.2	.4	2.1	3.0	2.1	1.7	3.7	3.2	1.8	3.2	2.5
Change in bank loans and mortgage loans	3.9	3.3	1.8	−2.3	2.6	5.4	3.1	.4	−.6	5.4	5.4	1.7	1.0	7.2	3.0	2.6	7.3	9.3
Net new issues	2.4	4.4	5.9	4.9	3.7	6.3	7.9	7.1	5.9	6.9	7.9	10.5	9.4	7.8	8.0	9.6	7.1	5.9
Stocks	1.3	1.4	1.2	1.6	1.7	2.7	3.0	2.3	2.1	2.7	3.2	3.5	3.6	3.7	3.0	4.5	2.1	.6
Bonds	1.1	3.0	4.7	3.3	2.0	3.6	4.9	4.8	3.8	4.2	4.7	7.0	5.9	4.1	5.0	5.1	5.0	5.3
Total external sources	6.8	11.3	9.0	.9	14.6	17.9	10.3	10.3	2.6	18.2	14.6	12.1	9.7	20.8	12.6	14.5	18.5	19.0
Total sources	18.2	27.9	27.8	15.8	35.4	36.9	28.1	30.0	22.4	44.8	42.4	40.1	35.7	51.9	41.7	44.1	53.4	56.3
Discrepancy (uses less sources)	1.3	.3	−.8	1.0	1.1	−.1	−.8	−1.8	1.6	.3	−2.9	−2.2	−4.2	−5.0	−2.4	−1.8	−5.2	−4.0

[1] Excludes banks and insurance companies.
[2] Receivables are net of payables, which are therefore not shown separately.
[3] Less than $50,000,000.

Source: Department of Commerce, Office of Business Economics.

TABLE 48.—*Corporate securities offered for sale in the United States, 1946–63*

[Estimated gross proceeds in millions of dollars]

Year	Total corporate offerings	Type of security		
		Common stock	Preferred stock	Bonds and notes
1946	6,900	891	1,127	4,882
1947	6,577	779	762	5,036
1948	7,078	614	492	5,973
1949	6,052	736	425	4,890
1950	6,362	811	631	4,920
1951	7,741	1,212	838	5,691
1952	9,534	1,369	564	7,601
1953	8,898	1,326	489	7,083
1954	9,516	1,213	816	7,488
1955	10,240	2,185	635	7,420
1956	10,939	2,301	636	8,002
1957	12,884	2,516	411	9,957
1958	11,558	1,334	571	9,653
1959	9,748	2,027	531	7,190
1960	10,154	1,664	409	8,081
1961	13,147	3,273	449	9,425
1962	10,770	1,318	436	9,016
1963	12,237	1,022	342	10,872
	Percentage distribution			
1946	100	12.9	16.3	70.8
1947	100	11.8	11.6	76.6
1948	100	8.7	7.0	84.4
1949	100	12.2	7.0	80.8
1950	100	12.7	9.9	77.3
1951	100	15.7	10.8	73.5
1952	100	14.4	5.9	79.7
1953	100	14.9	5.5	79.6
1954	100	12.7	8.6	78.7
1955	100	21.3	6.2	72.5
1956	100	21.0	5.8	73.2
1957	100	19.5	3.2	77.3
1958	100	11.5	4.9	83.5
1959	100	20.8	5.4	73.8
1960	100	16.4	4.0	79.6
1961	100	24.9	3.4	71.7
1962	100	12.2	4.0	83.7
1963	100	8.4	2.8	88.8

Source: Securities and Exchange Commission.

TABLE 49.—*Corporation income tax returns: Rates of return on net worth before and after taxes, corporations with net income, 1936–61* [1]

Year	Net income [2]		Net worth	Net income as percent of net worth	
	Before tax	After tax		Before tax	After tax
	Millions	*Millions*	*Millions*		
1936	$9,102	$7,957	$105,553	8.6	7.5
1937	9,392	8,146	112,902	8.3	7.2
1938	6,369	5,525	99,553	6.4	5.5
1939	8,709	7,492	110,347	7.9	6.8
1940	11,068	8,543	116,231	9.5	7.4
1941	17,797	10,733	127,674	13.4	8.4
1942	23,785	11,647	131,183	18.1	8.9
1943	28,399	12,647	139,294	20.4	9.1
1944	26,880	12,111	144,950	18.5	8.4
1945	21,945	11,243	144,559	15.2	7.8
1946	26,681	17,971	148,635	18.0	12.1
1947	32,790	22,003	169,588	19.3	13.0
1948	35,791	24,020	188,524	19.0	12.7
1949	30,158	20,469	195,195	15.4	10.5
1950	43,704	26,536	215,714	20.3	12.3
1951	44,903	23,001	229,377	19.6	10.0
1952	40,085	21,083	239,969	16.7	8.8
1953	41,441	21,747	251,640	16.5	8.6
1954	39,137	22,455	252,926	15.5	8.9
1955	49,821	28,284	285,223	17.6	9.9
1956	49,818	28,597	304,383	16.4	9.4
1957	48,338	27,872	309,802	15.6	9.0
1958	43,061	24,402	329,653	13.1	7.4
1959	51,651	29,127	354,717	14.6	8.2
1960	50,382	28,516	367,185	13.7	7.8
1961	52,401	30,213	389,225	13.5	7.8

[1] Based on all returns with balance sheets for 1936–58; for 1959–61 based on all active corporation returns.
[2] Excludes tax-exempt interest.

Source: Internal Revenue Service: Statistics of Income, Corporation Income Tax Returns.

TABLE 50.—*Corporation income tax rates, 1909–65*

Calendar year	Reduced rates on small corporations	General rate (percent)
1909–13	$5,000 exemption	1
1913–15	None after Mar. 1, 1913	1
1916		2
1917		6
1918	$2,000 exemption	12
1919–21	do	10
1922–24	do	12½
1925	do	13
1926–27	do	13½
1928	$3,000 exemption	12
1929	do	11
1930–31	do	12
1932–35	None	13¾
1936–37	Graduated normal tax ranging from—	
	First $2,000	8
	Over $40,000	15
	Graduated surtax on undistributed profits ranging from	7–27
1938–39	First $25,000	12½–16
	Over $25,000	[1] 19
1940	First $25,000	14.85–18.7
	$25,000 to $31,964.30	38.3
	$31,964.30 to $38,565.89	36.9
	Over $38,565.89	24
1941	First $25,000	21–25
	$25,000 to $38,461.54	44
	Over $38,461.54	31
1942–45	First $25,000	25–29
	$25,000 to $50,000	53
	Over $50,000	40
1946–49	First $25,000	21–25
	$25,000 to $50,000	53
	Over $50,000	38
1950	Normal tax 23; Surtax (over $25,000 surtax exemption) 19	42
1951	Normal tax 28¾; Surtax (over $25,000 surtax exemption) 22	50¾
1952–63	Normal tax 30; Surtax (over $25,000 surtax exemption) 22	52
1964	Normal tax 22; Surtax (over $25,000 surtax exemption) 28	50
1965	Normal tax 22; Surtax (over $25,000 surtax exemption) 26	48

[1] Less adjustments: 14.025 percent of dividends received and 2½ percent of dividends paid.

Source: Treasury Department, Office of Tax Analysis.

TABLE 51.—*Effective rates of corporation income tax at selected taxable income levels, 1946–65* [1]

[Percent]

Taxable income	1946–49	1950	1951	1952–63	1964	1965
$5,000	21.00	23.00	28.75	30.00	22.00	22.00
$10,000	22.00	23.00	28.75	30.00	22.00	22.00
$25,000	23.00	23.00	28.75	30.00	22.00	22.00
$50,000	38.00	32.50	39.75	41.00	36.00	35.00
$75,000	38.00	35.67	43.42	44.67	40.67	39.33
$100,000	38.00	37.25	45.25	46.50	43.00	41.50
$250,000	38.00	40.10	48.55	49.80	47.20	45.40
$500,000	38.00	41.05	49.65	50.90	48.60	46.70
$1,000,000	38.00	41.53	50.20	51.45	49.30	47.35
$10,000,000	38.00	41.95	50.70	51.95	49.93	47.94
$100,000,000	38.00	42.00	50.74	51.99	49.99	47.99

[1] Excluding excess-profits tax.

Source: Treasury Department, Office of Tax Analysis.

TABLE 52.—*Schedule of taxpayments for calendar-year corporations under 1950 law (1949–54), under Revenue Act of 1954 (1955–63), and under Revenue Act of 1964 (1964–1970)*

[Percent of tax liability due in each installment]

Income year	Income year				Following year				Total
	April	June	September	December	March	June	September	December	
1949	------	------	------	------	25	25	25	25	100
1950	------	------	------	------	30	30	20	20	100
1951	------	------	------	------	35	35	15	15	100
1952	------	------	------	------	40	40	10	10	100
1953	------	------	------	------	45	45	5	5	100
1954	------	------	------	------	50	50	------	------	100
1955 [1]	------	------	5	5	45	45	------	------	100
1956 [1]	------	------	10	10	40	40	------	------	100
1957 [1]	------	------	15	15	35	35	------	------	100
1958 [1]	------	------	20	20	30	30	------	------	100
1959 [1]	------	------	25	25	25	25	------	------	100
1960 [1]	------	------	25	25	25	25	------	------	100
1961 [1]	------	------	25	25	25	25	------	------	100
1962 [1]	------	------	25	25	25	25	------	------	100
1963 [1]	------	------	25	25	25	25	------	------	100
1964 [1]	1	1	25	25	24	24	------	------	100
1965 [1]	4	4	25	25	21	21	------	------	100
1966 [1]	9	9	25	25	16	16	------	------	100
1967 [1]	14	14	25	25	11	11	------	------	100
1968 [1]	19	19	25	25	6	6	------	------	100
1969 [1]	22	22	25	25	3	3	------	------	100
1970 [1] [2]	25	25	25	25	------	------	------	------	100

[1] Applicable only to tax liability in excess of $100,000. The 1st $100,000 of a corporation's tax liability is paid in equal installments in March and June of the following year.
[2] And subsequent years.

Source: Treasury Department, Office of Tax Analysis.

TABLES

CAPITAL GAINS

TABLE 53.—*Capital gains of individuals and fiduciaries and stock prices, 1917–61*

Calendar year	Capital gains at 100 percent [1]	Stock price index [2] (1929=100)	Calendar year	Capital gains at 100 percent [1]	Stock price index [2] (1929=100)
	Millions			*Millions*	
1917	$248	29.7	1940	−$80	42.3
1918	−68	33.3	1941	−482	35.9
1919	263	37.5	1942	−301	38.7
1920	−17	29.5	1943	1,057	46.4
1921	−639	30.9	1944	1,602	53.1
1922	232	37.4	1945	4,267	70.8
1923	192	36.8	1946	6,644	62.4
1924	1,037	43.9	1947	4,383	60.4
1925	2,573	53.1	1948	4,382	59.8
1926	2,166	55.5	1949	3,100	66.6
1927	2,619	70.3	1950	6,058	81.4
1928	4,595	93.7	1951	6,238	91.9
1929	3,645	81.5	1952	5,172	98.2
1930	−121	58.2	1953	4,105	96.1
1931	−929	30.5	1954	7,228	132.7
1932	−1,652	25.4	1955	10,079	161.8
1933	−654	38.4	1956	9,654	167.8
1934	−459	36.5	1957	7,492	150.1
1935	38	51.9	1958	9,323	201.1
1936	661	65.6	1959	13,355	215.8
1937	76	43.1	1960	11,290	216.6
1938	31	48.3	1961	15,914	261.7
1939	31	48.4			

[1] The excess of net gains over net losses on all returns reporting gain or loss on sales of capital and other assets. For the years 1917–42 the data are from L. H. Seltzer, "The Nature and Tax Treatment of Capital Gains and Losses," The National Bureau of Economic Research, 1951, table 1, p. 367. Figures for 1943–52 are those reported by Seltzer in National Bureau of Economic Research, "The Uses of Economic Research" (Annual Report), 1963, table IV.11, p. 89. For 1953–60 the Seltzer figures given in the National Bureau of EconomicResearch annual report are increased by Office of Tax Analysis estimates of the excess of fiduciary gains over losses. The estimates of fiduciary excess gains in the years 1953, 1955, 1957, 1959, 1961, when fiduciary returns were not tabulated, were derived using gains reported on individual returns to interpolate between even-year fiduciary gains as reported in "Statistics of Income." The 1961 individual excess gain is from the "Statistics of Income."

[2] R. Goldsmith and R. Lipsey, "Studies in the National Balance Sheet of the United States," Princeton University Press, 1963, vol. I, table 39, pp. 170–171.

Source: Treasury Department, Office of Tax Analysis.

TABLE 54.—*Taxable individual income tax returns with net gain from sale of capital assets: Total returns and returns with alternative tax computation, 1942–61*

Year	Number of returns			Net capital gain in adjusted gross income		
	Total	With alternative tax computation		Total [1]	Subject to alternative tax computation [2]	
		Number	Percent of total		Amount	Percent of total
				Millions	*Millions*	
1961	3,914,000	108,759	2.8	$7,690	$2,786	36.2
1960	3,063,671	91,818	3.0	5,362	1,870	34.9
1959	3,206,962	110,296	3.4	6,185	2,076	33.6
1958	2,791,712	88,941	3.2	4,406	1,385	31.4
1957	2,281,393	76,413	3.3	3,721	1,207	32.4
1956	2,466,281	86,499	3.5	4,556	1,534	33.7
1955	2,284,784	91,014	4.0	4,712	1,668	35.4
1954	1,943,303	73,618	3.8	3,359	1,121	33.4
1953	1,611,659	68,665	4.3	2,267	722	31.8
1952	1,648,372	80,700	4.9	2,559	848	33.1
1951	1,732,266	70,655	4.1	2,939	994	33.8
1950	1,556,019	49,316	3.2	3,000	949	31.6
1949	1,134,541	25,139	2.2	1,714	406	23.7
1948	1,364,697	30,896	2.3	2,263	550	24.3
1947	1,624,931	69,444	4.3	2,291	678	29.6
1946	1,975,105	84,021	4.3	3,158	923	29.2
1945	1,583,347	88,485	5.6	2,246	779	34.7
1944	983,492	51,993	5.3	1,109	368	33.2
1943	638,004	31,850	5.0	771	288	37.4
1942	277,539	12,507	4.5	304	128	42.1

[1] Includes both short- and long-term capital gains, with net long-term capital gain in excess of any net short-term capital loss reduced by 50 percent.
[2] For taxpayers who elect this computation, this amount comprises 50 percent of the net long-term capital gain in excess of any net short-term capital loss, which is taxed at a rate of 50 percent, thereby resulting in a maximum effective rate of 25 percent. The 25 percent maximum rate holds for all of the years included in the table except 1951 to 1953 when it was 26 percent.

Source: Internal Revenue Service: Statistics of Income—Individual Income Tax Returns.

TABLE 55.—*Individual income tax returns with net gains and losses from sales of capital assets by size of adjusted gross income, 1961*

Adjusted gross income classes	Returns with sales of capital assets		Returns with net gain: Returns		Net gain: Net gain in adjusted gross income		Net short-term capital gain in excess of net long-term capital loss		Net long-term capital gain in excess of net short-term capital loss		Capital loss carryover	
	Number	Percent of total	Number	Percent of total	Amount	Percent of total	Amount	Percent of total	Amount	Percent of total	Amount	Percent of total
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
					Millions		*Millions*		*Millions*		*Millions*	
Taxable returns, total	4,841,720	83.5	3,914,000	83.3	$7,689	92.8	$551	94.7	$14,278	92.6	$108	93.3
Under $3,000	413,269	7.1	358,855	7.6	176	2.1	13	2.2	327	2.1	4	3.1
$3,000 under $5,000	720,055	12.4	587,355	12.5	385	4.6	27	4.7	717	4.7		
$5,000 under $10,000	1,764,965	30.5	1,413,655	30.1	1,086	13.1	104	17.9	1,964	12.7	10	8.7
$10,000 under $15,000	893,543	15.4	713,805	15.2	804	9.7	93	16.1	1,422	9.2	12	10.2
$15,000 under $20,000	391,305	6.8	311,967	6.6	561	6.8	65	11.1	994	6.4	9	7.4
$20,000 under $50,000	539,778	9.3	429,382	9.1	1,587	19.1	152	26.2	2,868	18.6	36	31.4
$50,000 under $100,000	91,508	1.6	74,886	1.6	909	11.1	50	8.6	1,717	11.1	20	16.9
$100,000 under $500,000	25,977	.4	22,854	.5	1,390	16.8	35	5.9	2,710	17.6	15	12.9
$500,000 and over	1,320	(1)	1,241	(1)	791	9.5	12	2.0	1,559	10.1	3	2.6
Nontaxable returns, total	954,234	16.5	784,499	16.7	601	7.2	31	5.3	1,141	7.4	8	6.7
Total, all returns	5,795,954	100.0	4,698,499	100.0	8,291	100.0	581	100.0	15,419	100.0	116	100.0

Adjusted gross income classes	Returns with net loss							
	Returns		Net loss				Capital loss carryover	
			Before statutory limitation		After statutory limitation, deducted from adjusted gross income			
	Number	Percent of total	Amount	Percent of total	Amount	Percent of total	Amount	Percent of total
	(13)	(14)	(15)	(16)	(17)	(18)	(19)	(20)
			Millions		*Millions*		*Millions*	
Taxable returns, total	927,720	84.5	$1,793	77.8	$540	80.5	$778	82.7
Under $3,000	54,414	5.0	86	3.7	33	4.9	34	3.6
$3,000 under $5,000	132,700	12.0	261	11.3	78	11.7	92	9.8
$5,000 under $10,000	351,310	32.0	554	24.0	192	28.7	199	21.1
$10,000 under $15,000	279,738	16.4	297	12.9	98	14.7	131	13.9
$15,000 under $20,000	79,338	7.2	163	7.1	47	7.1	69	7.4
$20,000 under $50,000	110,396	10.1	318	13.8	75	11.2	171	18.2
$50,000 under $100,000	16,622	1.5	85	3.7	13	1.9	57	6.1
$100,000 under $500,000	3,123	.3	27	1.2	3	.4	22	2.3
$500,000 and over	79	(1)	2	.1	(2)	(2)	3	.3
Nontaxable returns, total	169,735	15.4	512	22.2	130	19.5	163	17.3
Total all returns	1,097,455	100.0	2,305	100.0	670	100.0	941	100.0

[1] Less than 0.05 percent.
[2] Less than $500,000.

Source: Internal Revenue Service: Statistics of Income—1961, Individual Income Tax Returns.

TABLE 56.—*Individual income tax returns with sales of long-term capital assets by asset type, 1959*

Asset type	Net long-term capital gain	
	Amount	Percent of total
	Millions	
Total net long-term capital gain	$12,331,867	100.0
Corporation stocks, including rights	5,116,261	41.5
Bonds and notes	189,480	1.5
Distributions from regulated investment companies	360,371	2.9
Share of gain or loss from partnerships and fiduciaries	1,010,202	8.2
Livestock	701,116	5.7
Natural resources [1]	262,593	2.1
Business buildings, machinery	537,631	4.4
Real estate	2,217,438	18.0
Other capital assets	1,936,775	15.7

[1] Includes timber and timber royalties, oil and mineral rights and leases, oil well ventures and production payments in oil and minerals.

Source: Internal Revenue Service: Statistics of Income—1959, Supplemental Report, Sales of Capital Assets.

TABLE 57.—*Individual income tax returns with sales of long-term capital assets, percentage distribution by asset type and by size of adjusted gross income, 1959*

Adjusted gross income classes	All asset types	Security-type gains						Real estate	Business buildings and machinery	Livestock	Natural resource	Other
		Total	Securities			Capital gain dividend	Share of partnership or fiduciary gain or loss					
			Total	Corporate stock	Bonds and notes							
		(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
All size classes	100.0	54.1	43.0	41.5	1.5	2.9	8.2	18.0	4.4	5.7	2.1	15.7
Under $10,000	100.0	30.6	19.4	18.1	1.4	3.8	7.4	29.4	5.9	16.3	3.9	13.9
$10,000 under $50,000	100.0	55.9	43.1	41.7	1.4	4.0	8.8	18.2	5.9	2.2	1.2	16.6
$50,000 under $100,000	100.0	67.3	55.2	53.4	1.8	2.2	9.9	11.3	2.2	1.0	.9	17.3
$100,000 under $500,000	100.0	70.5	61.6	59.8	1.8	.7	8.3	10.2	1.5	.5	1.7	15.5
$500,000 or more	100.0	78.5	72.4	70.5	2.0	.5	5.6	1.5	1.0	.2	2.6	16.2
Gain as a percent of gross sales	[1]	[1]	1.7	48.3	9.1	[1]	[1]	27.6	6.7	2.7	1.1	[1]

[1] Sales data not available or incomplete for this asset type.

Source: Internal Revenue Service: Statistics of Income—1959, Supplemental Report, Sales of Capital Assets.

TABLE 58.—*Estimated revenue yield from capital gains and income taxation, 1948–61*

[Dollar amounts in billions]

Calendar year of liability	Individuals and fiduciaries: Total income taxes [1]	Individuals and fiduciaries: Estimated tax on capital gains and losses: Amount	Individuals and fiduciaries: Estimated tax on capital gains and losses: Percent of total tax [2]	Corporations: Total income and excess profits taxes [1]	Corporations: Estimated tax on capital gains and losses: Amount	Corporations: Estimated tax on capital gains and losses: Percent of total tax [2]	Individuals, fiduciaries, and corporations: Total income and excess profits taxes	Individuals, fiduciaries, and corporations: Estimated tax on capital gains and losses: Amount	Individuals, fiduciaries, and corporations: Estimated tax on capital gains and losses: Percent of total tax [2]
1948	$15.6	$0.6	3.8	$11.9	$0.2	1.7	$27.5	$0.8	2.9
1949	14.7	.4	2.7	9.8	.2	2.0	24.5	.6	2.4
1950	18.5	.9	4.9	17.3	.3	1.7	35.9	1.2	3.3
1951	24.4	.9	3.7	22.1	.3	1.4	46.5	1.2	2.6
1952	28.0	.8	2.9	19.1	.3	1.6	47.2	1.1	2.3
1953	29.7	.7	2.4	19.9	.3	1.5	49.6	1.0	2.0
1954	26.9	1.1	4.1	16.9	.5	3.0	43.8	1.6	3.7
1955	29.9	1.6	5.4	21.7	.5	2.3	51.6	2.1	4.1
1956	33.1	1.5	4.5	21.4	.5	2.3	54.5	2.0	3.7
1957	34.8	1.2	3.4	20.6	.4	1.9	55.4	1.6	2.9
1958	34.7	1.4	4.0	18.8	.6	3.1	53.5	2.0	3.7
1959	40.0	2.3	5.8	22.5	.4	1.9	62.5	2.7	4.3
1960	39.8	1.9	5.0	21.9	.5	2.2	61.7	2.4	3.9
1961	42.6	2.9	6.8	22.2	.8	3.6	64.8	3.7	5.7

[1] As reported in Statistics of Income.
[2] Derived from rounded data.

NOTE.—The estimated tax on capital gains and losses for each of the specified years is the difference between (1) the total individual and corporation income taxes reported in Statistics of Income, and (2) the total of such taxes which would have been realized if capital gains and losses had been entirely excluded from the tax computation.

Estimates of capital gains tax revenue are subject to a rather significant margin of error for individuals. These estimates are approximations of the effect upon tax liabilities of a recomputation of tax excluding the amount reported as capital gains and losses. These gains and losses are treated as final sources of income or deduction and therefore the revenue effect is based on marginal rates. In addition, the estimates are based upon summary data. The possible error is reduced somewhat where cross classifications by size of adjusted gross income and size of capital gain income or loss are available.

Source: Treasury Department, Office of Tax Analysis.

TABLES

EXCISE TAXES

TABLE 59.—*Collections from Federal excise taxes on liquor, tobacco, gasoline, retail sales, and general admissions, 1939–63*

[Dollar amounts in millions]

Fiscal year	Total excise tax collections	Alcohol	Tobacco	Gasoline [1]	Retail taxes	General admissions	Other
1939	$1,750	$588	$580	$207	----------	$18	$357
1940	1,867	624	608	226	----------	20	389
1941	2,381	820	698	343	----------	69	451
1942	3,124	1,048	781	370	$80	108	737
1943	3,794	1,423	924	289	165	138	855
1944	4,461	1,618	988	271	225	179	1,180
1945	5,945	2,310	932	406	424	301	1,572
1946	6,684	2,526	1,166	406	492	343	1,751
1947	7,283	2,475	1,238	434	514	393	2,229
1948	7,410	2,255	1,300	479	470	385	2,521
1949	7,579	2,211	1,322	504	449	386	2,707
1950	7,599	2,219	1,328	527	409	371	2,745
1951	8,703	2,547	1,380	569	457	346	3,404
1952	8,971	2,549	1,565	713	475	331	3,338
1953	9,946	2,781	1,655	891	496	313	3,810
1954	9,532	2,798	1,581	837	438	272	3,606
1955 [2]	9,211	2,743	1,571	955	292	106	3,544
1956	10,004	2,921	1,613	1,030	322	104	4,014
1957	10,638	2,973	1,674	1,458	336	76	4,121
1958	10,814	2,946	1,734	1,637	342	55	4,100
1959	10,760	3,002	1,807	1,700	356	50	3,845
1960	11,865	3,194	1,932	2,016	379	34	4,310
1961	12,064	3,213	1,991	2,370	398	37	4,055
1962	12,752	3,341	2,026	2,413	421	39	4,512
1963	13,410	3,442	2,079	2,497	444	43	4,905
	Percentage distribution						
1939	100.0	33.6	33.1	11.8	----------	1.0	20.4
1940	100.0	33.4	32.6	12.1	----------	1.1	20.8
1941	100.0	34.4	29.3	14.4	----------	2.9	18.9
1942	100.0	33.5	25.0	11.8	2.6	3.5	23.6
1943	100.0	37.5	24.4	7.6	4.3	3.6	22.5
1944	100.0	36.3	22.1	6.1	5.0	4.0	26.5
1945	100.0	38.9	15.7	6.8	7.1	5.1	26.4
1946	100.0	37.8	17.4	6.1	7.4	5.1	26.2
1947	100.0	34.0	17.0	6.0	7.1	5.4	30.6
1948	100.0	30.4	17.5	6.5	6.3	5.2	34.0
1949	100.0	29.2	17.4	6.6	5.9	5.1	35.7
1950	100.0	29.2	17.5	6.9	5.4	4.9	36.1
1951	100.0	29.3	15.9	6.5	5.3	4.0	39.1
1952	100.0	28.4	17.4	8.0	5.3	3.7	37.1
1953	100.0	28.0	16.6	9.0	5.0	3.1	38.3
1954	100.0	29.4	16.6	8.8	4.6	2.9	37.8
1955 [2]	100.0	29.8	17.1	10.4	3.2	1.2	38.5
1956	100.0	29.2	16.1	10.3	3.2	1.0	40.1
1957	100.0	27.9	15.7	13.7	3.2	.7	38.7
1958	100.0	27.2	16.0	15.1	3.2	.5	37.9
1959	100.0	27.9	16.8	15.8	3.3	.5	35.7
1960	100.0	26.9	16.3	17.0	3.2	.3	36.3
1961	100.0	26.6	16.5	19.7	3.3	.3	33.6
1962	100.0	26.2	15.9	19.9	3.3	.3	35.4
1963	100.0	25.7	15.5	18.6	3.3	.3	36.6

[1] Beginning with fiscal year 1957, collections reflect the provisions of the Highway Revenue Act of 1956, approved June 29, 1956.
[2] Beginning with fiscal year 1955, collections shown include undistributed depositary receipts and unapplied collections.

Source: Treasury Bulletin.

TABLE 60.—*Excise tax collections by major sources, fiscal year 1963*

Source	Collections	
	Amount (millions)	Percent of total
Alcohol taxes	$3,441.7	25.7
Tobacco taxes	2,079.2	15.5
Documentary and certain other stamp taxes	149.1	1.1
Manufacturers' excise taxes:		
Gasoline	2,497.3	18.6
Tires, tubes, and tread rubber	398.9	3.0
Passenger automobiles, trucks and buses, chassis, bodies, etc	1,862.7	13.9
Parts and accessories for automobiles, trucks, etc. (including lubricating oil, etc.)	298.9	2.2
Radio and television sets, phonographs, components, etc	184.2	1.4
Electric, gas, and oil appliances (including refrigerators, freezers, air conditioners, etc.)	129.7	1.0
Phonograph records, musical instruments, sporting goods, firearms, shells and cartridges, and camera equipment	115.1	.9
Business and store machines	74.8	.5
Electric light bulbs and tubes, matches, mechanical pencils, pens, and lighters	48.8	.4
Retailers' excise taxes	443.6	3.3
Amusements (admissions, club dues, coin-operated devices, bowling and billiards, wagering)	184.5	1.4
Communications	880.6	6.6
Transportation of persons	234.0	1.7
Sugar	99.9	.7
Diesel and special motor fuels	113.0	.8
Undistributed depositary receipts	62.5	.5
All other	111.4	.8
Total excise taxes	13,409.7	100.0

Source: Treasury Bulletin.

TABLES

ESTATE AND GIFT TAXES

TABLE 61.—*Estate tax returns: Number of returns, gross estate, net estate, and tax, 1916–61* [1]

Year filed	Number of returns	Gross estate	Taxable estate	Tax
		Millions	*Millions*	*Millions*
Sept. 9, 1916 to Jan. 15, 1922	45,216	$8,893	$5,510	$357
Jan. 15 to Dec. 31, 1922	13,876	3,014	1,705	121
1923	15,119	2,804	1,532	89
1924	14,513	2,567	1,396	72
1925	16,019	3,002	1,659	87
1926	14,567	3,408	1,973	102
1927	10,700	3,173	1,762	42
1928	10,236	3,554	1,993	42
1929	10,343	3,893	2,314	44
1930	10,382	4,166	2,427	42
1931	9,889	4,076	2,356	45
1932	8,507	2,830	1,423	24
1933	10,275	2,061	1,001	61
1934	11,853	2,267	1,171	96
1935	12,724	2,460	1,340	155
1936	13,321	2,312	1,260	196
1937	17,032	2,794	1,647	308
1938	17,642	3,070	1,745	317
1939	16,926	2,768	1,558	279
1940	16,876	2,648	1,493	252
1941	17,122	2,793	1,576	293
1942	17,396	2,737	1,536	310
1943	16,033	2,638	1,405	363
1944	14,857	2,916	1,516	406
1945	16,550	3,450	1,911	533
1946	(2)	(2)	(2)	(2)
1947	22,007	4,251	2,341	626
1948	24,381	4,791	2,597	717
1949	25,904	4,958	2,126	571
1950	27,144	4,942	1,935	487
1951	29,002	5,526	2,205	580
1952	(2)	(2)	(2)	(2)
1953	(2)	(2)	(2)	(2)
1954	37,672	7,435	2,985	782
1955	37,565	7,490	3,007	781
1956	(2)	(2)	(2)	(2)
1957	47,381	10,323	4,363	1,181
1958	(2)	(2)	(2)	(2)
1959	56,977	11,680	4,672	1,189
1960	(2)	(2)	(2)	(2)
1961	65,789	14,666	6,038	1,623

[1] Includes nonresident aliens having property in the United States.
[2] Not available.

Source: Internal Revenue Service: Statistics of Income—1960, Fiduciary, Gift, and Estate Tax Returns; Statistics of Income—1949, pt. I, Estate Tax Returns.

TABLE 62.—*Estate tax returns: Number of taxable estate tax returns filed as percent of total number of adult deaths, 1939–61*

Year	Adult deaths in the United States [1]	Taxable estate tax returns filed		Year	Adult deaths in the United States [1]	Taxable estate tax returns filed	
		Number	Percent of adult deaths [2]			Number	Percent of adult deaths [2]
1939	1,204,080	12,720	1.06	1951	1,328,809	18,941	1.43
1940	1,235,484	12,907	1.04	1952	1,339.182	[3]	[3]
1941	1,215,627	13,336	1.10	1953	1,363,386	[3]	[3]
1942	1,209,661	13,493	1.12	1954	1,331,498	24,997	1.88
1943	1,275,400	12,726	1.00	1955	1,378,588	25,143	1.82
1944	1,237,508	12,154	.98	1956	1,413,005	[3]	[3]
1945	1,238,360	13,869	1.12	1957	1,475,320	32,131	2.18
1946	1,230,754	[3]	[3]	1958	1,488,954	[3]	[3]
1947	1,277,852	18,232	1.43	1959	1,498,549	38,515	2.57
1948	1,284,535	19,742	1.54	1960	1,553,985	[3]	[3]
1949	1,284,196	17,469	1.36	1961	1,548,061	45,439	2.94
1950	1,303,171	17,411	1.34				

[1] Age 20 and over: Data from U.S. Public Health Service.
[2] Actual ratio of estate tax returns to adult deaths may differ somewhat from these percentages because the filling of estate tax returns may lag as much as 15 months behind date of death.
[3] Not available.

Source: Internal Revenue Service: Statistics of Income for Estate Tax Returns.

TABLE 63.—*Estate Tax Returns: Federal estate tax liability before State death tax credit, and State death tax credit, 1929–61*

Year	Federal estate tax liability before State death tax credit [1]	State death tax credit		Year	Federal estate tax liability before State death tax credit [1]	State death tax credit	
		Amount (millions)	Percent of Federal tax before credit			Amount (millions)	Percent of Federal tax before credit
1929	$165.4	$122.1	73.8	1946	[2]	[2]	[2]
1930	152.4	113.4	74.4	1947	$693.6	$69.9	10.1
1931	182.2	137.7	75.6	1948	799.3	82.7	10.3
1932	84.0	61.6	73.4	1949	634.9	65.8	10.4
1933	76.7	20.1	26.2	1950	533.9	48.9	9.2
1934	129.2	33.9	26.3	1951	644.4	64.5	10.0
1935	197.7	43.9	22.2	1952	[2]	[2]	[2]
1936	239.6	44.2	18.5	1953	[2]	[2]	[2]
1937	364.2	58.3	16.0	1954	868.6	85.8	9.9
1938	374.6	59.8	16.0	1955	872.5	86.2	9.9
1939	330.2	53.1	16.1	1956	[2]	[2]	[2]
1940	295.7	45.3	15.3	1957	1,353.2	146.8	10.8
1941	336.5	53.6	15.9	1958	[2]	[2]	[2]
1942	330.7	45.6	13.8	1959	1,346.3	131.5	9.8
1943	398.2	36.0	9.0	1960	[2]	[2]	[2]
1944	452.2	46.3	10.2	1961	1,847.0	195.6	10.6
1945	596.1	64.5	10.8				

[1] And before other tax credits including Federal gift taxes, foreign death duties, and prior transfers. Does not include tax on estates of nonresident aliens.
[2] Not available.

Source: Internal Revenue Service: Statistics of Income for Estate Tax Returns.

TABLE 64.—*Estate tax returns: Number of returns, gross estate by types of property, selected deductions, net estate, and tax, 1945–61*

[Dollar amounts in thousands]

Items	Returns filed during—										
	1945	1947	1948	1949	1950	1951	1954	1955	1957	1959	1961
RETURNS OF CITIZENS AND RESIDENTS											
Number of returns, total	15,898	20,899	23,356	24,552	25,858	27,958	36,699	36,595	46,473	55,685	64,538
Taxable	13,869	18,232	19,742	17,469	17,411	18,941	24,997	25,143	32,131	38,515	45,439
Nontaxable	2,029	2,667	3,614	7,083	8,447	9,017	11,702	11,452	14,342	17,170	19,099
Gross estate, total	$3,436,901	$4,224,210	$4,774,783	$4,933,215	$4,918,994	$5,504,961	$7,411,754	$7,467,443	$10,293,669	$11,648,017	$14,622,073
Real estate	521,570	763,631	894,504	950,521	1,009,133	(1)	1,551,720	1,559,672	(1)	2,509,159	2,857,330
Federal bonds	289,245	378,936	434,678	425,879	425,650	(1)	490,793	457,054	(1)	553,896	702,209
State and municipal bonds	195,391	164,925	154,323	193,654	138,941	(1)	239,321	201,013	(1)	351,616	477,043
Other bonds	137,059	111,184	104,472	94,891	89,263	(1)	91,597	81,885	(1)	109,614	125,248
Corporate stocks	1,358,301	1,621,747	1,772,128	1,802,641	1,773,054	(1)	2,982,597	3,073,922	(1)	4,984,850	6,766,373
Cash	330,195	439,812	551,140	549,139	524,601	(1)	745,028	747,880	(1)	1,152,029	1,396,260
Mortgages and notes	123,337	137,307	152,882	171,480	191,583	(1)	253,293	274,575	(1)	414,904	522,272
Taxable insurance	237,212	289,003	325,424	348,297	356,691	(1)	476,151	468,498	(1)	651,876	755,157
Other property	244,591	317,665	385,231	396,713	409,134	(1)	581,604	602,944	(1)	920,073	1,020,181
Deductions, total	1,570,660	1,941,919	2,246,035	2,950,399	3,154,994	(1)	4,647,459	4,677,803	(1)	7,291,220	8,929,625
Marital deductions	------	------	41,979	583,614	799,597	923,210	1,343,926	1,371,730	(1)	2,176,137	2,795,891
Charitable bequests	191,701	185,627	223,125	296,150	205,863	274,398	354,542	397,835	(1)	668,900	950,813
Specific exemption	949,350	1,252,010	1,399,860	1,472,150	1,550,830	1,677,190	2,201,560	2,195,460	2,788,290	3,341,100	3,872,400
Other deductions	429,609	504,282	581,071	598,485	598,705	(1)	747,431	712,778	(1)	1,105,083	1,310,521
Disallowed deductions	3,796	2,972	3,492	8,036	7,243	(1)	2,987	2,753	(1)	6,193	2,141
Allowable deductions	1,566,864	1,938,947	2,242,543	2,942,363	3,147,751	3,479,886	4,644,472	4,675,050	3,408,010	7,285,027	8,927,484
Net estate	1,900,159	2,319,310	2,584,595	2,106,827	1,916,645	2,188,878	2,969,174	2,990,810	4,342,072	4,650,979	6,014,498
Net estate tax	531,052	621,966	714,707	567,421	483,520	577,401	778,504	778,342	1,176,710	1,185,620	1,618,548
RETURNS OF NONRESIDENT ALIENS											
Number of returns, total	652	1,108	1,025	1,352	1,286	1,044	973	970	908	1,292	1,251
Taxable	(1)	(1)	(1)	1,240	1,115	819	687	696	696	958	989
Nontaxable	(1)	(1)	(1)	112	171	225	286	274	212	334	262
Gross estate in the United States	13,524	27,198	16,266	24,511	24,157	20,666	23,383	22,803	28,884	31,656	43,733
Net estate	10,997	21,872	12,602	19,356	18,192	16,052	16,206	15,948	20,987	21,422	23,336
Net estate tax	1,876	4,389	1,825	3,407	3,229	3,081	3,096	2,913	4,589	3,667	4,142

[1] Data not available.

NOTE.—In the Statistics of Income volumes containing statistics based on estate tax returns filed in 1959 and 1961, the specific exemption has not been included in total deductions but appears after allowable deductions. In each of the last 2 columns in the present table the total of deductions exceeds the total deductions in the Statistics of Income volume by the amount of specific exemptions, and the amount of allowable deductions exceeds the corresponding figure in the Statistics of Income volume by the same amount.

Source: Internal Revenue Service: Statistics of Income for Estate Tax Returns.

TABLE 65.—*Estate tax returns: Taxable returns—Number of returns, gross estate, deductions, specific exemption, taxable estate, and tax, by gross estate classes, returns filed in 1961* [1]

[Dollar amounts in thousands]

Items	Total	Gross estate classes: Under $60,000	$60,000, under $70,000	$70,000, under $80,000	$80,000, under $90,000	$90,000, under $100,000	$100,000, under $120,000	$120,000, under $150,000	$150,000, under $200,000
Number of returns	45,439	----------	2,051	3,874	3,144	2,792	4,398	6,523	7,183
Total gross estate	$12,733,459	----------	$137,351	$290,441	$289,759	$265,106	$481,419	$879,856	$1,238,744
Real estate	2,236,726	----------	43,070	94,088	94,263	81,113	144,844	246,862	321,516
Federal bonds	612,155	----------	9,527	18,858	17,138	15,589	26,672	47,299	62,888
State and municipal bonds	468,410	----------	393	659	545	603	1,415	3,432	6,399
Other bonds	113,713	----------	911	1,968	1,877	1,541	4,116	6,172	10,449
Corporate stock	6,294,499	----------	37,402	80,039	82,395	83,730	157,859	298,070	447,079
Cash	1,150,770	----------	28,391	55,140	51,571	42,919	74,419	122,863	152,815
Mortgages and notes	440,788	----------	6,285	14,293	14,690	13,236	21,893	39,891	58,811
Taxable insurance	551,126	----------	4,690	9,984	10,598	10,165	19,734	56,378	91,997
Annuities	35,857	----------	483	864	735	783	1,331	3,485	4,425
Other property	829,415	----------	6,199	14,548	15,947	15,428	29,136	55,404	82,365
Total deductions	3,993,100	----------	7,630	22,522	25,906	27,723	58,785	228,556	377,916
Funeral and administrative expense	535,192	----------	6,168	15,893	15,634	14,129	25,613	40,623	55,649
Debts and mortgages	519,986	----------	1,243	4,971	6,886	7,507	14,724	25,806	48,061
Net losses during administration	787	----------	9	18	27	38	29	31	89
Marital deduction	2,187,970	----------	68	927	2,239	4,439	15,150	156,534	262,849
Total charitable bequests	747,554	----------	141	705	1,118	1,603	3,269	5,562	11,259
Other deductions	1,611	----------	1	8	2	7	(2)	----------	9
Disallowed deductions	459	----------	----------	6	9	15	64	61	61
Allowable deductions	3,992,641	----------	7,360	22,516	25,897	27,708	58,721	228,495	377,855
Net estate before specific exemption	8,740,818	----------	129,721	267,925	263,862	237,398	422,698	651,361	860,889
Specific exemption	2,726,320	----------	123,060	232,420	204,840	167,520	263,880	391,380	430,980
Taxable estate	6,014,498	----------	6,661	35,505	59,022	69,878	158,818	259,981	429,909
Gross estate tax before credit	1,847,044	----------	225	1,963	4,612	6,718	19,313	40,329	79,399
Total tax credits	228,496	----------	4	18	73	111	411	1,450	3,864
State, inheritance, etc. taxes	195,581	----------	1	6	8	11	123	731	1,939
Federal gift taxes	4,167	----------	1	3	14	24	27	83	192
Prior transfers	24,068	----------	2	8	46	64	230	561	1,635
Foreign death duties	4,680	----------	(2)	1	5	12	31	75	98
Net tax liability	1,618,548	----------	221	1,945	4,539	6,607	18,902	38,879	75,535

[Dollar amounts in thousands]

Items	Gross estate classes								
	$200,000, under $300,000	$300,000, under $500,000	$500,000, under $1,000,000	$1,000,000, under $2,000,000	$2,000,000, under $3,000,000	$3,000,000, under $5,000,000	$5,000,000, under $10,000,000	$10,000,000, under $20,000,000	$20,000,000 or more
Number of returns	6,575	4,469	2,684	966	242	165	65	26	12
Total gross estate	$1,596,002	$1,696,526	$1,822,426	$1,311,299	$589,056	$618,242	$442,915	$351,245	$723,072
Real estate	362,646	316,937	259,676	123,337	48,678	45,026	11,749	17,007	25,914
Federal bonds	79,794	79,383	85,205	61,270	22,992	26,805	16,136	13,566	29,033
State and municipal bonds	14,933	29,158	68,041	72,715	51,410	56,132	50,533	33,779	78,263
Other bonds	16,479	17,745	19,926	11,825	4,776	5,695	1,912	6,444	1,877
Corporate stock	654,344	820,251	1,003,460	820,275	379,459	406,623	309,622	237,634	476,857
Cash	165,867	154,563	127,083	70,005	29,472	27,211	17,675	10,168	20,608
Mortgages and notes	69,432	68,723	61,340	26,733	12,028	11,629	6,710	12,365	2,729
Taxable insurance	114,331	93,264	74,457	37,781	10,326	9,820	5,154	1,674	774
Annuities	6,273	6,634	5,226	3,611	761	572	259	385	30
Other property	111,903	109,868	118,012	83,747	29,154	28,729	23,165	18,823	86,987
Total deductions	508,545	526,245	576,858	425,931	198,124	219,269	176,958	166,537	445,595
Funerals and administrative expenses	71,475	73,832	74,544	48,783	21,214	22,775	17,075	11,061	20,724
Debts and mortgages	76,134	81,656	92,548	66,767	27,697	20,723	16,775	11,863	16,625
Net losses during administration	183	159	71	5	68	51	9	------	------
Marital deduction	336,120	330,196	338,178	225,993	88,845	112,100	74,331	87,446	152,555
Total charitable bequests	24,568	40,324	71,363	83,200	60,196	63,620	68,768	56,167	255,691
Other deductions	65	78	154	1,183	104	------	------	------	------
Disallowed deductions	145	91	5	------	------	------	2	------	------
Allowable deductions	508,400	526,154	576,853	425,931	198,124	219,269	176,956	166,537	445,595
Net estate before specific exemptions	1,087,602	1,170,372	1,245,573	885,368	390,932	398,973	265,959	184,708	277,477
Specific exemptions	394,500	268,140	161,040	57,960	14,520	9,900	3,900	1,560	720
Taxable estate	693,102	902,232	1,084,533	827,408	376,412	389,073	262,059	183,148	276,757
Gross estate before credit	152,470	231,857	313,640	270,706	139,252	158,360	128,349	105,983	193,868
Total tax credits	9,938	18,922	32,494	35,136	20,753	23,770	21,143	21,066	39,343
State inheritance, etc., taxes	5,951	13,528	25,743	29,965	18,573	22,744	19,747	18,440	38,071
Federal gift taxes	399	470	811	449	377	28	------	1,251	38
Prior transfers	3,216	4,434	5,338	3,936	1,673	432	979	1,245	269
Foreign death duties	372	490	602	786	130	566	417	130	965
Net tax liability	142,532	212,935	281,146	235,570	118,499	134,590	107,206	84,917	154,525

[1] Citizens and resident aliens.
[2] Less than $500.

Source: Internal Revenue Service: Statistics of Income—1960, Fiduciary, Gift, and Estate Tax Returns.

TABLE 66.—*Estate tax returns: Nontaxable returns—Number of returns, gross estate, deductions, specific exemptions, by gross estate classes, returns filed in 1961* [1]

[Dollar amounts in thousands]

Items	Total	Gross estate classes							
		Under $60,000	$60,000, under $70,000	$70,000, under $80,000	$80,000, under $90,000	$90,000, under $100,000	$100,000, under $120,000	$120,000, under $150,000	$150,000, under $200,000
Number of returns	19,009	9	4,793	3,178	2,722	2,251	3,542	1,655	483
Total gross estate	$1,888,614	$500	$309,577	$237,862	$231,146	$213,554	$387,837	$214,273	$82,083
Real estate	620,604	110	114,126	88,385	81,752	72,793	123,483	73,071	29,746
Federal bonds	90,054	1	18,187	12,340	11,078	9,795	19,056	6,854	2,295
State and municipal bonds	8,633	----------	491	234	246	266	946	429	450
Other bonds	11,535	14	1,637	1,104	983	913	2,055	1,224	733
Corporate stock	471,874	193	63,362	46,801	46,779	45,190	91,297	49,714	20,472
Cash	245,490	70	55,253	34,293	31,458	28,071	47,959	21,314	7,282
Mortgages and notes	81,484	39	13,262	10,529	10,426	10,042	17,421	8,913	3,692
Taxable insurance	204,031	54	22,802	25,301	29,215	27,519	51,963	31,372	8,499
Annuities	9,247	1	1,091	1,337	1,543	1,389	2,643	992	144
Other property	145,662	18	19,366	17,538	17,666	17,576	31,014	20,390	8,770
Total deductions	1,064,125	94	101,901	117,245	122,329	114,960	215,231	131,450	62,614
Funeral and administrative expense	82,146	34	16,757	10,607	9,319	8,104	13,801	8.967	4,186
Debts and mortgages	170,052	18	15,346	15,160	14,729	13,267	25,002	28,025	21.456
Net losses during administration	299	----------	26	29	37	6	121	36	23
Marital deductions	607,921	29	62,110	84,371	90,163	87,413	163,794	78,262	16,519
Total charitable bequests	203,259	13	7,650	7,004	8,055	6,131	12,452	16,077	20,430
Other deductions	448	----------	12	74	26	39	61	83	----------
Disallowed deductions	1,682	----------	163	145	83	33	151	373	142
Allowable deductions	1,062,443	94	101,738	117,100	122,246	114,927	215,080	131,077	62,472
Net estate before specific exemption	826,171	406	207,839	120,762	108,900	98,627	172,757	83,196	19,611
Specific exemption	1,146,080	540	287,720	190,680	163,320	135,060	212,520	99,300	28,980

[Dollar amounts in thousands]

Item	Gross estate classes							
	$200,000, under $300,000	$300,000, under $500,000	$500,000, under $1,000,000	$1,000,000, under $2,000,000	$2,000,000, under $3,000,000	$3,000,000, under $5,000,000	$5,000,000, under $10,000,000	$10,000,000, or more
Number of returns	256	120	63	21	4	1		1
Total gross estate	$60,768	$45,741	$41,553	$27,320	$10,530	$3,360		$22,510
Real estate	15,639	9,062	9,303	880	2,249	5		
Federal bonds	2,974	2,360	1,089	2,030	1,995			
State and municipal bonds	575	539	2,062	1,499	881	15		
Other bonds	585	1,197	472	568	50			
Corporate stock	22,369	21,091	19,363	16,636	3,138	3,210		22,259
Cash	7,161	4,588	3,753	2,205	1,948	80		55
Mortgages and notes	2,886	2,193	1,268	638	137	1		37
Taxable insurance	3,785	1,776	1,228	399	6	27		85
Annuities	55	18	34					
Other property	4,739	2,917	2,981	2,465	126	22		74
Total deductions	52,541	42,894	39,851	26,806	10,455	3,301		22,453
Funeral and administrative expense	3,125	2,309	1,877	1,405	196	112		1,347
Debts and mortgages	14,628	8,632	8,584	3,640	404	139		1,022
Net losses during administration	1	20	(2)					
Marital deductions	7,161	2,770	2,093	1,611		1,555		10,070
Total charitable bequests	27,626	29,163	27,144	20,150	9,855	1,495		10,014
Other deductions			153					
Disallowed deductions	306	272	14					
Allowable deductions	52,235	42,622	39,837	26,806	10,455	3,301		22,453
Net estate before specific exemptions	8,533	3,119	1,716	514	75	59		57
Specific exemption	15,360	7,200	3,780	1,260	240	60		60

1 Citizens and resident aliens.
2 Less than $500.

Source: Internal Revenue Service: Statistics of Income—1960, Fiduciary, Gift, and Estate Tax Returns.

TABLE 67.—*Federal gift tax: Effective rate for single and married persons at selected net gift levels*

Net gift before exemption and exclusion	Married person: Gift to spouse	Married person: Gift to 2 children	Single person: Gift to 2 persons	Net gift before exemption and exclusion	Married person: Gift to spouse	Married person: Gift to 2 children	Single person: Gift to 2 persons
	Percent	*Percent*	*Percent*		*Percent*	*Percent*	*Percent*
$30,000				$500,000	8.4	16.5	20.1
$40,000			0.2	$1,000,000	10.1	20.1	23.4
$50,000			1.4	$1,500,000	11.1	22.1	25.7
$75,000	0.1	0.1	4.6	$2,000,000	11.8	23.4	27.6
$100,000	1.0	1.4	8.0	$2,500,000	12.3	24.5	29.4
$150,000	2.6	4.6	12.5	$4,000,000	13.8	27.6	34.1
$200,000	4.3	8.0	15.0	$5,000,000	14.7	29.4	36.7
$250,000	5.5	10.6	16.5	$10,000,000	18.4	36.7	45.5
$400,000	7.7	15.0	19.2				

Source: Treasury Department, Office of Tax Analysis.

TABLE 68.—*Gift tax returns: Number of returns, total gifts before exclusions, net gifts, and gift tax, 1933–60*

Year [1]	Number of returns: Total	Number of returns: Taxable	Total gifts before exclusions [2]	Net taxable gifts	Gift tax
			Thousands	*Thousands*	*Thousands*
1933	3,683	878	$241,008	$101,793	$8,943
1934	9,270	2,528	888,753	537,083	68,383
1935	22,563	8,718	2,130,514	1,196,001	162,798
1936	13,420	3,770	482,783	134,979	15,664
1937	13,695	4,128	568,109	180,939	22,758
1938	11,042	3,515	399,773	138,801	17,839
1939	12,226	3,929	371,604	131,577	18,701
1940	15,623	4,930	570,042	225,972	34,445
1941	25,788	8,940	1,081,482	484,319	69,819
1942	16,906	4,380	480,223	120,653	24,665
1943	16,987	4,656	412,655	122,936	29,637
1944	18,397	4,979	499,012	148,420	37,781
1945	20,095	5,540	535,559	169,625	36,633
1946	24,826	6,808	755,604	265,246	62,336
1947	24,857	6,882	777,613	256,534	64,402
1948	26,200	6,559	740,923	209,148	45,338
1949	31,547	6,114	708,381	178,035	36,087
1950	39,056	8,366	1,064,200	337,719	77,605
1951	41,703	8,360	999,518	304,131	67,426
1952	(3)	(3)	(3)	(3)	(3)
1953	44,695	8,464	1,012,054	258,478	55,528
1954	(3)	(3)	(3)	(3)	(3)
1955	(3)	(3)	(3)	(3)	(3)
1956	76,720	14,736	[4] 1,342,435	517,583	113,005
1957	(3)	(3)	(3)	(3)	(3)
1958	77,920	15,793	[4] 1,843,968	478,289	104,838
1959	(3)	(3)	(3)	(3)	(3)
1960	78,232	17,926	[4] 2,184,157	657,024	157,687

[1] Beginning with 1956 the data in the table are based on the returns of donors filing in the following year, regardless of the year of donation. For the earlier years coverage was based on returns for gifts made in the year shown in the table.
[2] Includes gifts made on nontaxable returns.
[3] Not available.
[4] Excludes nontaxable returns without consent. Such returns are those reporting gifts with respect to which one or the other spouse withheld consent for treating the gift as coming in equal parts from both.

Source: Internal Revenue Service: Statistics of Income for Gift Tax Returns.

TABLE 69.—*Gift tax returns: Total gifts, exclusions, deductions, taxable gifts and tax, by size of total taxable gifts, all returns, 1960* [1]

[Dollar amounts in thousands]

Size of taxable gifts	Number of returns	Total gifts	Total gifts before exclusions	Exclusions	Total gifts after exclusions	Deductions				Taxable gifts			Gift tax		
						Total	Charitable gifts after exclusions	Marital deduction	Specific exemption	Current year	Prior years	Aggregate	Current year	Prior years	Aggregate
Total taxable returns	17,936	$1,219,482	$1,187,246	$178,170	$1,009,076	$352,052	$175,105	$28,254	$148,693	$657,024	$1,947,396	$2,604,420	$157,687	$614,909	$772,596
Under $3,000	5,193	127,086	117,747	46,990	70,757	64,803	28,755	4,645	31,403	5,954	367,379	373,333	484	98,233	98,717
$3,000 under $5,000	1,764	54,088	49,928	15,583	34,345	27,533	11,414	1,955	14,164	6,812	127,009	133,821	568	36,354	36,922
$5,000 under $10,000	2,860	88,444	82,200	25,542	56,658	36,185	9,109	3,395	23,681	20,473	143,428	163,901	1,744	31,092	32,836
$10,000 under $20,000	2,783	114,839	109,985	25,703	84,282	44,722	12,258	4,894	27,570	39,560	131,725	171,285	3,915	26,114	30,029
$20,000 under $30,000	1,564	79,873	78,914	15,227	63,687	25,375	6,207	3,140	16,028	38,312	92,541	130,853	4,432	19,972	24,404
$30,000 under $40,000	799	50,280	50,147	9,211	40,936	13,355	3,991	1,152	8,212	27,581	65,941	93,522	3,630	15,970	19,600
$40,000 under $50,000	610	44,196	43,997	5,886	38,111	10,772	2,806	1,137	6,829	27,339	61,072	88,411	3,951	16,047	19,998
$50,000 under $100,000	1,241	132,543	130,499	14,950	115,549	29,278	13,739	3,046	12,493	86,271	156,737	243,008	15,027	40,518	55,545
$100,000 under $200,000	604	108,627	107,051	8,536	98,515	14,968	8,195	1,454	5,319	83,547	136,996	220,543	17,719	37,910	55,629
$200,000 under $400,000	293	101,016	103,011	5,615	97,396	17,288	14,288	1,364	1,636	80,108	382,392	462,500	19,943	180,355	200,298
$400,000 under $600,000	101	65,420	61,575	1,742	59,833	11,046	10,307	90	649	48,787	100,373	149,160	13,585	37,327	50,912
$600,000 under $800,000	33	27,983	27,445	788	26,657	3,168	2,731	115	322	23,489	18,930	42,419	6,244	6,355	12,599
$800,000 under $1,000,000	22	20,650	20,650	409	20,241	233	180	------	53	20,008	12,821	32,829	5,706	3,551	9,257
$1,000,000 under $2,000,000	51	87,580	87,240	1,463	85,777	19,627	17,486	1,867	274	66,150	61,307	127,457	20,952	23,111	44,063
$2,000,000 under $3,000,000	11	29,093	29,093	233	28,860	2,191	2,131	--------	60	26,669	21,411	48,080	9,932	8,762	18,694
$3,000,000 under $4,000,000	2	29,782	29,782	6	29,776	22,338	22,338	--------	--------	7,438	7,101	14,539	3,613	2,521	6,134
$4,000,000 under $5,000,000	3	13,371	13,371	226	13,145	197	197	--------	--------	12,948	7,436	20,384	6,040	2,297	8,337
$5,000,000 under $7,000,000	1	6,196	6,196	33	6,163	102	102	--------	--------	6,061	3,481	9,542	3,156	1,149	4,305
$7,000,000 under $10,000,000	--------	--------	--------	--------	--------	--------	--------	--------	--------	--------	--------	--------	--------	--------	--------
$10,000,000 or more	1	38,415	38,415	27	38,388	8,871	8,871	--------	--------	29,517	49,316	78,833	17,046	27,271	44,317
Total nontaxable returns	60,296	1,096,581	996,911	391,696	605,215	605,215	125,013	65,927	414,275	--------	895,200	895,200	--------	226,142	226,142
Total all returns	78,232	2,316,063	2,184,157	569,866	1,614,291	957,267	300,118	94,181	562,968	657,024	2,842,596	3,499,620	157,687	841,051	998,738

[1] Returns filed in 1961.

Source: Internal Revenue Service: Statistics of Income—1960, Fiduciary, Gift, and Estate Tax Returns.

TABLE 70.—*Gift tax returns: Total gifts, exclusions, deductions, taxable gifts, and gift tax, by size of total taxable gifts, returns of recurrent donors, 1960* [1]

[Dollar amounts in thousands]

Size of taxable gifts	Number of returns	Total gifts	Total gifts before exclusions	Exclusions	Total gifts after exclusions	Deductions: Total	Deductions: Charitable gifts after exclusions	Deductions: Marital deduction	Deductions: Specific exemption	Taxable gifts: Current year	Taxable gifts: Prior years	Taxable gifts: Aggregate	Gift tax: Current year	Gift tax: Prior years	Gift tax: Aggregate
Total taxable returns	13,624	$945,850	$907,890	$146,240	$761,650	$224,936	$169,012	$17,859	$38,065	$536,714	$1,942,942	$2,479,656	$140,631	$613,757	$754,388
Under $3,000	4,112	92,276	83,729	39,591	44,138	39,437	28,318	2,502	8,617	4,701	367,234	371,935	456	98,207	98,663
$3,000 under $5,000	1,344	36,284	33,546	12,799	20,747	15,577	11,258	1,027	3,292	5,170	126,996	132,166	530	36,328	36,858
$5,000 under $10,000	2,214	59,008	53,920	20,977	32,943	16,942	8,034	1,972	6,936	16,001	143,355	159,356	1,600	31,089	32,689
$10,000 under $20,000	2,008	74,271	69,817	20,157	49,660	21,015	11,814	2,729	6,472	28,645	131,449	160,094	3,342	26,069	29,411
$20,000 under $30,000	1,121	52,122	50,678	11,838	38,840	11,369	5,914	1,746	3,709	27,471	89,592	117,063	3,681	19,116	22,797
$30,000 under $40,000	573	33,994	33,220	7,306	25,914	6,105	3,336	774	1,995	19,809	65,941	85,750	2,988	15,970	18,958
$40,000 under $50,000	416	28,099	27,174	4,109	23,065	4,371	2,382	620	1,369	18,694	60,999	79,693	3,104	16,039	19,143
$50,000 under $100,000	923	98,677	94,435	12,381	82,054	17,605	12,150	2,111	3,344	64,449	156,500	220,949	12,166	40,474	52,640
$100,000 under $200,000	465	86,041	82,514	7,306	75,208	10,298	7,876	1,057	1,365	64,910	136,308	201,218	14,474	37,766	52,240
$200,000 under $400,000	254	89,222	90,937	5,098	85,839	15,869	14,024	1,364	481	69,970	382,392	452,362	17,924	180,355	198,279
$400,000 under $600,000	86	59,482	53,956	1,661	52,295	10,617	10,271	90	256	41,678	100,373	142,051	12,038	37,327	49,365
$600,000 under $800,000	26	22,795	22,027	728	21,299	2,800	2,688	---------	112	18,499	18,930	37,429	5,087	6,355	11,442
$800,000 under $1,000,000	21	19,752	19,752	397	19,355	203	180	---------	23	19,152	12,821	31,973	5,502	3,551	9,053
$1,000,000 under $2,000,000	45	79,331	80,098	1,412	78,686	19,120	17,159	1,867	94	59,566	61,307	120,873	19,315	23,111	42,426
$2,000,000 under $3,000,000	9	26,732	24,323	188	24,135	2,100	2,100	---------	---------	22,035	21,411	43,446	8,569	8,762	17,331
$3,000,000 under $4,000,000	2	29,782	29,782	6	29,776	22,338	22,338	---------	---------	7,438	7,101	14,539	3,613	2,521	6,134
$4,000,000 under $5,000,000	3	13,371	13,371	226	13,145	197	197	---------	---------	12,948	7,436	20,384	6,040	2,297	8,337
$5,000,000 under $7,000,000	1	6,196	6,196	33	6,163	102	102	---------	---------	6,061	3,481	9,542	3,156	1,149	4,305
$7,000,000 under $10,000,000	---------	---------	---------	---------	---------	---------	---------	---------	---------	---------	---------	---------	---------	---------	---------
$10,000,000 or more	1	38,415	38,415	27	38,388	8,871	8,871	---------	---------	29,517	49,316	78,833	17,046	27,271	44,317
Total nontaxable returns	21,329	384,517	339,122	168,526	170,596	170,596	87,523	17,354	65,719	---------	894,110	894,110	---------	225,993	225,993
Total all returns	34,953	1,330,367	1,247,012	314,766	932,246	395,532	256,535	35,213	103,784	536,714	2,837,052	3,373,766	140,631	839,750	980,381

[1] Returns filed in 1961.

NOTE.—Recurrent donors are those who reported taxable gifts or used part of their exemptions in the current year and had reported taxable gifts or used part of their exemption in earlier years.

Source: Internal Revenue Service: Statistics of Income—1960, Fiduciary, Gift, and Estate Tax Returns.

TABLE 71.—*Gift tax returns: Types of gifts by size of taxable gifts, all returns, 1960* [1]

[Dollar amounts in thousands]

Size of taxable gifts	Total gifts of donors	Type of property							
		Real estate	Federal bonds	State and municipal bonds	Other bonds	Corporate stock	Cash	Insurance	Other
Total taxable returns	$1,219,482	$140,531	$8,730	$15,177	$5,662	$793,692	$129,679	$23,040	$102,971
Under $3,000	127,086	16,717	834	787	472	76,901	15,735	3,932	11,708
$3.000 under $5,000	54,088	10,639	593	160	279	28,586	7,786	1,236	4,809
$5,000 under $10,000	88,444	19,135	601	409	453	41,139	13,636	3,249	9,822
$10,000 under $20,000	114,839	22,324	1,116	1,030	904	55,507	18,220	3,415	12,323
$20,000 under $30,000	79,873	16,219	934	785	592	41,619	10,101	1,860	7,763
$30,000 under $40,000	50,280	9,149	637	842	375	27,126	7,114	1,360	4,650
$40,000 under $50,000	44,196	7,546				23,590	6,234	1,181	4,672
$50,000 under $100,000	132,543	19,782	1,229	1,536	404	77,180	17,735	3,312	11,365
$100,000 under $200,000	108,627	10,064	1,169	3,328	1,054	70,205	11,881	1,861	9,065
$200,000 under $400,000	101,016	4,141	529	1,248	703	76,081	9,579	1,383	7,352
$400,000 under $600,000	65,420	1,806	666	2,323	319	49,734	7,021	95	3,456
$600,000 under $800,000	27,983	---	---	914	74	23,358	1,900	110	1,627
$800,000 under $1,000,000	20,650	924	---	398	---	15,835	1,372	---	2,121
$1,000,000 under $2,000,000	87,580	2,075	422	1,273	---	72,973	645	28	10,164
$2,000,000 under $3,000,000	29,093	---	---	---	---	28,589	54	3	447
$3,000,000 under $4,000,000	29,782	---	---	---	---	29,735	47	---	---
$4,000,000 under $5,000,000	13,371	---	---	144	33	11,086	468	15	1,625
$5,000,000 under $7,000,000	6,196	10	---	---	---	6,061	123	---	2
$7,000,000 under $10,000,000	---	---	---	---	---	---	---	---	---
$10,000,000 or more	38,415	---	---	---	---	38,387	28	---	---
Total nontaxable returns	1,096,581	226,828	12,911	6,487	7,588	505,947	176,830	34,399	125,591
Total all returns	2,316,063	367,359	211,641	21,664	13,250	1,299,639	306,509	57,439	228,562

[1] Returns filed in 1961.

Source: Internal Revenue Service: Statistics of Income—1960, Fiduciary, Gift, and Estate Tax Returns.

TABLE 72.—*Gift tax returns: Types of gifts by size of taxable gifts, returns of recurrent donors, 1960* [1]

[Dollar amounts in thousands]

Size of taxable gifts	Total gifts of donors	Type of property							
		Real estate	Federal bonds	State and municipal bonds	Other bonds	Corporate stock	Cash	Insurance	Other
Total taxable returns	$945,850	$69,725	$5,574	$12,465	$4,125	$658,387	$103,922	$17,513	$74,139
Under $3,000	92,276	7,076	445	524	403	59,113	13,409	2,680	8,626
$3,000 under $5,000	36,284	3,436	863	513	318	22,768	5,912	1,010	2,570
$5,000 under $10,000	59,008	8,943				28,635	10,654	2,520	7,150
$10,000 under $20,000	74,271	10,079	657	504	606	38,699	13,482	2,769	7,475
$20,000 under $30,000	52,122	8,202	599	915	651	27,989	7,682	1,395	5,729
$30,000 under $40,000	33,994	4,509				20,214	5,219	945	2,720
$40,000 under $50,000	28,099	3,593				15,183	4,933	972	2,765
$50,000 under $100,000	98,677	12,149	515	1,150	323	60,781	13,051	2,157	8,551
$100,000 under $200,000	86,041	5,624	920	2,869	695	58,237	9,767	1,787	6,142
$200,000 under $400,000	89,222	3,169	492	1,105	703	68,151	9,557	1,090	4,955
$400,000 under $600,000	59,482	704	661	2,156	319	46,109	5,983	95	3,455
$600,000 under $800,000	22,795	-	-	914	74	18,222	1,885	73	1,627
$800,000 under $1,000,000	19,752	326	-	398	-	15,835	1,072	-	2,121
$1,000,000 under $2,000,000	79,331	1,905	422	1,273	-	66,951	597	2	8,181
$2,000,000 under $3,000,000	26,732	-	-	-	-	26,231	53	3	445
$3,000,000 under $4,000,000	29,782	-	-	-	-	29,735	47	-	-
$4,000,000 under $5,000,000	13,371	-	-	144	33	11,086	468	15	1,625
$5,000,000 under $7,000,000	6,196	10	-	-	-	6,061	123	-	2
$7,000,000 under $10,000,000	-	-	-	-	-	-	-	-	-
$10,000,000 or more	38,415	-	-	-	-	38,387	28	-	-
Total nontaxable returns	384,517	38,197	2,771	1,651	2,106	213,724	71,848	11,652	42,568
Total all returns	1,330,367	107,922	8,345	14,116	6,231	872,111	175,770	29,165	116,707

[1] Returns filed in 1961.

Source: Internal Revenue Service; Statistics of Income—1960, Fiduciary, Gift, and Estate Tax Returns.

TABLE 73.—*Estate and gift tax rates, 1916 to present*

Date of death	Tax rates		Bracket subject to—	
	Estates	Gifts	Minimum rate	Maximum rate
	Percent	*Percent*		
Sept. 9, 1916, to Mar. 2, 1917	1.0-10		0-$50,000	$5,000,000 and over
Mar. 3, to Oct. 3, 1917	1.5-15		0- 50,000	Do.
Oct. 4, 1917, to Feb. 24, 1919	2.0-25		0- 50,000	$10,000,000 and over.
Feb. 24, 1919, to Feb. 26, 1926	1.0-25	[1] 1.0-25	0- 50,000	Do.
Feb. 26, 1926, to June 6, 1932	1.0-20		0- 50,000	Do.
June 6, 1932, to May 10, 1934	1.0-45	.75-33.5	0- 10,000	Do.
May 11, 1934, to July 30, 1935	1.0-60	.75-45	0- 10,000	Do.
July 30, 1935, to June 25, 1940	2.0-70	1.55-52.5	0- 10,000	$50,000,000 and over.
June 25, 1940, to Sept. 20, 1941	[2] 2.2-77	[2] 1.65-57.75	0- 10,000	Do.
Sept. 20, 1941, to date	3.0-77	2.25-57.75	0- 5,000	$10,000,000 and over.

[1] In effect June 2, 1924, to Dec. 31, 1925.
[2] Includes defense tax equal to 10 percent of tax liability.

Source: Treasury Department, Office of Tax Analysis.

TABLE 74.—*Estate and gift taxes: Specific exemptions and exclusions, revenue acts 1916–42*

Revenue act	Estate tax		Gift tax	
	Specific exemption [1]	Insurance exclusion	Specific exemption [2]	Annual exclusion per donee
1916	$50,000		(3)	(3)
1918	50,000	$40,000	(3)	(3)
1924	50,000	40,000	$50,000	$500
1926	100,000	40,000	(4)	(4)
1932	50,000	40,000	50,000	5,000
1935	40,000	40,000	40,000	5,000
1938	40,000	40,000	40,000	4,000
1942	60,000		30,000	3,000

[1] Specific exemption granted to estates of nonresident citizens dying after May 11, 1934, on the same basis as resident decedents. No exemptions granted to estates of resident aliens until Oct. 21, 1942, when a $2,000 exemption was made available.
[2] Under the 1924 act, exemption allowed each calendar year. Under the 1932 and later acts, specific exemption allowed only once.
[3] No gift tax.
[4] Gift tax repealed.

Source: Treasury Department, Office of Tax Analysis.

TABLES

EMPLOYMENT TAXES

TABLE 75.—*Federal employment tax receipts, 1937–65* [1]

[Millions of dollars]

Fiscal year	Total	Old-age, survivors, and disability insurance [2] [3]	Railroad retirement [4]	Unemployment insurance [5]
1937	253	194		58
1938	755	514	150	90
1939	740	530	109	101
1940	833	604	121	108
1941	925	691	137	98
1942	1,186	896	170	120
1943	1,498	1,130	209	158
1944	1,739	1,292	267	180
1945	1,780	1,310	285	185
1946	1,701	1,238	283	180
1947	2,024	1,459	380	185
1948	2,381	1,616	557	208
1949	2,477	1,690	564	223
1950	2,883	2,106	550	226
1951	3,931	3,120	578	234
1952	4,562	3,569	735	259
1953	4,983	4,086	620	277
1954	5,425	4,537	603	285
1955	6,220	5,340	600	280
1956	7,296	6,337	634	325
1957	7,581	6,634	616	330
1958	8,644	7,733	575	336
1959	8,854	8,004	525	324
1960	11,159	10,211	607	341
1961	12,502	11,586	571	345
1962	12,708	11,686	564	458
1963	15,004	13,484	572	948
1964 (estimate)	16,932	15,415	617	900
1965 (estimate)	17,182	15,789	682	711

[1] Before refunds.

[2] The distribution of receipts between individual income taxes and old-age and disability insurance taxes is made in accordance with provisions of sec. 201 of the Social Security Act, as amended (42 U.S.C. 401), for transfer to the Federal old-age and survivors insurance trust fund, and also for transfer to the Federal disability insurance trust fund.

[3] Taxes on employers and employees under the Federal Insurance Contributions Act, as amended (26 U.S.C. 3101–3125), and tax on self-employed individuals under the Self-Employment Contributions Act, as amended (26 U.S.C. 1401–1403). The Social Security Act Amendments of 1956, approved Aug. 1, 1956, increased the rates of tax applicable to wages paid and taxable years beginning after Dec. 31, 1956, to provide for disability insurance.

[4] Taxes on carriers and their employees under the Railroad Retirement Tax Act, as amended (26 U.S.C. 3201–3233).

[5] Tax on employers of 4 or more under the Federal Unemployment Tax Act, as amended (26 U.S.C. 3301–3308); with respect to services performed before Jan. 1, 1956, the tax was imposed on employers of 8 or more.

Source: Treasury Department, Treasury Bulletin.

TABLE 76.—*Federal old-age and survivors insurance trust fund* [1], *1937–65*

[In millions of dollars]

Fiscal year or month	Receipts					Expenditures other than investments							Net increase, or decrease (−), in assets	Assets, end of period		
										Administrative expenses						
	Total [2]	Appropriations [3]	Deposits by States [4]	Net earnings on investments	Payments from railroad retirement account [5]	Total	Benefit payments	Payments to railroad retirement account [5]	Construction [6]	Reimbursement to general fund [7]	Bureau of OASI [8]	Reimbursement (−) from Federal disability insurance trust fund [9]		Total	Investments	Unexpended balance [10]
1937-52	24,000.1	21,819.9	26.6	2,138.2	----------	7,400.1	6,856.0	----------	--------	291.1	252.9	----------	16,600.0	16,600.0	16,273.1	327.1
1953	[11] 4,483.3	[11] 4,053.3	43.3	386.6	----------	[11] 2,717.0	2,627.5	----------	--------	24.4	65.1	----------	1,766.3	18,366.4	17,817.6	548.8
1954	5,039.8	4,496.8	92.4	438.9	11.6	3,364.3	3,275.6	----------	(*)	26.0	62.7	----------	1,675.5	[12] 20,042.6	19,339.9	702.8
1955	5,534.8	4,988.6	98.6	438.0	9.6	4,436.5	4,333.1	----------	0.1	27.1	76.0	----------	1,098.4	21,141.0	20,580.5	560.5
1956	6,937.4	6,270.8	171.6	487.5	7.4	5,485.3	5,360.8	----------	.1	30.7	93.7	----------	1,452.1	22,593.1	22,043.0	550.1
1957	7,100.6	6,243.0	296.8	555.3	5.2	6,664.8	6,514.6	----------	.3	30.9	119.0	----------	435.8	23,028.9	22,263.3	765.6
1958	7,824.4	6,794.9	472.1	555.4	1.6	8,040.7	7,874.9	----------	1.6	34.5	138.9	−9.1	−216.3	22,812.6	21,764.2	1,048.4
1959	8,108.7	7,084.0	481.1	543.0	----------	9,379.8	9,049.1	124.4	11.6	39.0	173.2	−17.5	−1,271.2	21,541.4	20,474.4	1,067.0
1960	10,360.0	9,192.4	650.3	516.4	----------	11,072.7	10,269.7	600.4	12.5	39.4	179.3	−28.8	−712.7	20,828.7	19,748.8	1,079.9
1961	11,823.9	10,537.2	755.4	530.2	----------	11,752.3	11,184.5	331.7	1.8	43.8	223.6	−33.2	71.6	20,900.3	19,523.5	1,376.8
1962	12,011.0	10,600.0	869.6	539.0	----------	13,270.2	12,657.8	360.8	3.1	45.3	263.5	−60.3	−1,259.2	19,641.1	18,434.7	1,206.5
1963	13,855.7	12,351.2	989.6	512.4	----------	14,529.7	13,844.6	422.5	1.7	48.5	275.4	−62.9	−674.1	18,967.1	17,613.2	1,353.9
1964 (estimate)	15,845.6	14,214.0	1,100.0	529.0	----------	15,358.6	14,629.0	423.0	2.8	52.9	314.8	−63.8	486.9	19,454.0	18,100.4	1,353.6
1965 (estimate)	[13] 16,271.2	14,531.0	1,128.0	553.0	----------	16,090.7	15,376.0	418.5	1.7	53.9	318.9	−78.3	180.5	19,634.5	18,281.3	1,353.2
1937 to date [12]	127,606.2	113,863.7	5,744.6	7,936.3	35.4	109,162.0	104,693.3	1,839.9	35.0	719.3	2,150.2	−275.7	18,444.2	18,444.2	16,958.1	1,486.0

[1] Includes transactions under the predecessor old-age reserve account.

[2] Total includes: $15,400,000 transferred from general fund for administrative and other costs of benefits payable to survivors of certain World War II veterans (60 Stat. 979 and 64 Stat. 512); beginning November 1951, small amounts in the nature of recoveries from expenditures incidental to the operations; and beginning 1958, interest payments from Federal disability insurance trust fund, and sale of waste paper.

[3] Includes unappropriated receipts beginning January 1962.

[4] To cover employees of States and their political subdivisions, under the Social Security Act Amendments of 1950 (42 U.S.C. 418).

[5] See table 78.

[6] Construction and equipment of office buildings for the Bureau (Public Law 170, approved July 31, 1953 (67 Stat. 254)).

[7] Under the Social Security Act, as amended (42 U.S.C. 401(g)(1)), for administration of titles II and VIII of that act and related parts of the Internal Revenue Code (26 U.S.C. 480–482, 1400–1432). (See also footnote 11.)

[8] Salaries and expenses of the Bureau of Old-Age and Survivors Insurance are paid directly from the trust fund beginning 1947, under provision of annual appropriation acts until passage of the Social Security Act Amendments of 1956 (42 U.S.C. 401(g)(1)); previously these expenses were included in reimbursements to the general fund.

[9] See table 77. This reimbursement is treated as a reduction in administrative expenses paid from the Federal old-age and survivors insurance trust fund. Figures exclude interest. (See footnote 2.)

[10] Includes unappropriated receipts beginning January 1962.

[11] Amounts for refunds of taxes (formerly included under expenditures) have been deducted from receipts.

[12] Includes adjustments to monthly statement basis to March 1964.

[13] Includes $56,000,000 proposed legislation, military service credits.

*Less than $50,000.

Source: Treasury Department, Treasury Bulletin, May 1964.

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TABLE 77.—*Federal disability insurance trust fund, 1957–65*

[In millions of dollars]

Fiscal year or month	Receipts: Total	Receipts: Appropriations [1]	Receipts: Deposits by States [2]	Receipts: Payments from railroad retirement account [3]	Receipts: Interest on investments	Expenditures other than investments: Total	Expenditures: Benefit payments	Expenditures: Payments to railroad retirement account [3]	Expenditures: Administrative: Reimbursement to— FOASI trust fund [4]	Expenditures: Administrative: Reimbursement to— General fund [5]	Net increase, or decrease (−), in assets	Assets, end of period: Total	Assets: Investments	Assets: Unexpended balance [6]
1957	338.6	333.3	3.9	----------	1.4	1.3	----------	----------	----------	1.3	337.3	337.3	325.4	11.9
1958	942.5	862.9	63.5	----------	16.1	180.8	168.4	----------	9.4	3.0	761.7	1,099.0	1,054.5	44.5
1959	[7] 928.7	[7] 836.9	58.1	----------	33.7	[7] 361.1	339.2	----------	18.0	3.9	567.6	1,666.6	1,606.9	59.7
1960	1,061.5	928.9	58.1	26.8	47.6	561.0	528.3	----------	29.5	3.1	500.6	2,167.2	2,100.9	66.4
1961	1,083.5	953.3	68.7	----------	61.5	746.3	704.0	5.1	34.1	3.1	337.2	2,504.4	2,385.6	118.8
1962	1,091.8	944.5	77.3	----------	70.0	1,088.5	1,011.4	11.0	62.5	3.7	3.3	2,507.7	2,406.1	101.5
1963	1,145.3	993.8	81.9	----------	69.6	1,259.2	1,170.7	19.6	65.3	3.6	−114.0	2,393.7	2,277.2	116.5
1964 (estimate)	1,198.4	1,050.0	81.0	----------	67.4	1,345.2	1,255.0	20.0	66.4	3.8	−146.8	2,246.9	2,130.7	116.2
1965 (estimate)	[8] 1,227.6	1,076.0	83.0	----------	64.6	1,427.8	1,324.0	18.5	81.4	3.9	−200.2	2,046.7	1,930.6	116.1
1957 to March 1964	7,381.4	6,547.9	470.2	26.8	336.5	5,193.1	4,847.7	35.8	285.1	24.5	2,188.2	2,188.2	2,056.3	131.9

[1] Includes unappropriated receipts beginning January 1962.

[2] To cover employees of States and their political subdivisions under the Social Security Act (42 U.S.C. 418).

[3] See table 78.

[4] Federal old-age and survivors insurance trust fund. For appropriate share of administrative expenses paid from the trust fund during the preceding fiscal year, as determined by the Secretary of Health, Education, and Welfare (42 U.S.C. 401(g)(1)). Payments include interest.

[5] For amounts paid from the general fund (42 U.S.C. 401(g)(1)).

[6] Includes unappropriated receipts beginning January 1962.

[7] See table 76, footnote 11.

[8] Includes $4,000,000 proposed legislation, military service credits.

Source: Treasury Department, Treasury Bulletin, May 1964.

Table 78.—*Railroad retirement account, 1936–65*

[In millions of dollars]

Fiscal year or month	Receipts: Total	Receipts: Appropriations [1]	Receipts: Interest on investments	Receipts: From FOASI and Federal disability insurance trust fund [2]	Receipts: From unemployment trust fund [3]	Expenditures other than investments: Total	Expenditures: Benefit payments	Expenditures: To FOASI and Federal disability insurance trust fund [2]	Expenditures: To unemployment trust fund [3]	Expenditures: Administrative expenses [4]	Net increase, or decrease (−), in assets	Assets, end of period: Total	Assets: Investments	Assets: Unexpended balance [5]
1936–55	7,879.0	7,202.5	676.5	----------	----------	4,346.5	4,291.6	21.1	----------	33.7	3,532.5	3,532.5	3,485.9	46.6
1956 [6]	739.3	634.3	105.5	----------	----------	610.6	596.4	7.4	----------	6.8	128.6	3,661.2	3,606.5	54.7
1957	722.6	615.9	106.7	----------	----------	682.0	669.7	5.2	----------	7.1	40.5	3,701.7	3,642.1	59.7
1958	695.2	574.9	120.3	----------	----------	729.7	719.5	1.6	----------	8.6	−34.6	3,667.1	3,609.0	58.2
1959	758.3	525.2	108.6	124.4	----------	777.6	768.2	----------	----------	9.4	−19.3	3,647.8	3,573.6	74.2
1960	1,403.4	606.9	110.0	600.4	86.1	1,136.0	916.4	26.8	183.7	9.0	267.4	3,915.3	3,837.8	77.5
1961	[7] 1,050.7	[7] 570.7	110.9	336.9	32.2	[7] 1,124.1	981.8	----------	132.3	9.9	−73.4	3,841.9	3,759.5	82.4
1962	1,080.7	564.3	107.4	371.8	37.2	1,134.6	1,023.9	----------	101.5	9.2	−53.9	3,787.9	3,697.0	91.0
1963	1,127.8	571.5	105.2	442.1	8.9	1,111.5	1,064.0	----------	37.7	9.8	16.3	3,805.3	3,697.5	107.9
1964 (estimate)	1,201.6	617.0	131.9	443.0	9.7	1,129.0	1,100.0	----------	18.0	11.0	72.6	3,878.0	3,782.0	96.0
1965 (estimate)	[8] 1,279.1	682.0	133.7	437.0	12.6	1,143.5	1,125.0	----------	8.0	10.5	135.6	4,013.6	3,918.0	95.6
1936 to date [9]	15,974.5	12,309.9	1,597.6	1,875.7	191.3	12,503.2	11,847.1	62.2	482.1	111.8	3,471.3	3,471.3	3,378.0	93.2

[1] Includes the Government's contribution for creditable military service (45 U.S.C. 228c -1 (n)) until payment was completed in 1954. Beginning 1952, appropriations of receipts are equal to the amount of taxes deposited in the Treasury (less refunds) under the Railroad Retirement Tax Act, and transfers are made currently subject to later adjustments. Includes unappropriated transfers of tax receipts.

[2] Payments are made between the railroad retirement account and the Federal old-age and survivors and the Federal disability insurance trust funds so as to place those funds in the position in which they would have been if railroad employment after 1936 had been included in social security coverage (45 U.S.C. 228e (k)). See tables 76 and 77.

[3] See table 79. Receipts include repayment and interest.

[4] Paid from the trust fund beginning 1950 (63 Stat. 297).

[5] Includes unappropriated receipts.

[6] Includes adjustment for change in reporting to a collection basis.

[7] Beginning fiscal 1961, amounts for interest on refunds of taxes, formerly included under budget expenditures, are treated as transfers of budget receipts to trust receipts and are included in trust expenditures.

[8] Includes $13,800,000 for military service credits.

[9] Includes adjustments to monthly statement basis to Mar. 10, 1964.

Source: Treasury Department, Treasury Bulletin, May, 1964

TABLE 79.—*Unemployment trust fund, 1936–65*

[In millions of dollars]

Fiscal year or month	Receipts											
	Total	Employment security program					Railroad unemployment insurance					Interest and profits on investments
		State accounts,[1] deposits by States	Employment Security Administration account[2]		Federal unemployment account[4]	Federal extended compensation account[5]	Railroad unemployment insurance account[6]				Administration fund[10] deposits by Railroad Retirement Board	
			Appropriations	Advances from general fund[3]			Deposits by Railroad Retirement Board[7]	Advances from—		Transfers from administration fund[9]		
								Railroad retirement account[8]	General fund			
1936–52	[11] 19,209.9	16,447.3					917.0			85.3		1,653.1
1953	1,593.8	1,371.1					15.0			4.9		202.8
1954	1,492.5	1,246.0					17.8			4.2		224.4
1955	1,425.4	1,146.2			64.3		14.2			1.6		199.1
1956	1,728.1	1,330.1			167.8		27.6			3.6		198.9
1957	1,912.0	1,541.7			71.2		71.1			3.2		224.8
1958	1,855.5	1,500.7			33.5		90.4					230.9
1959	1,997.4	1,700.6			(*)		102.0				7.9	186.9
1960	2,703.3	2,167.0			2.6		153.0	183.7			8.9	188.1
1961	[12] 3,803.3	2,398.1	[12] 344.4	51.5	(*)	498.1	152.7	132.3	13.0		8.6	204.5
1962	3,985.4	2,728.6	452.6	34.9		332.9	147.1	101.5	7.0		8.1	172.6
1963	4,260.7	3,008.9	945.4	−81.9		2.4	149.8	37.7	−.6		7.9	191.1
1964 (estimated)	4,190.7	2,900.0	896.5				147.0	18.0			13.0	216.3
1965 (estimated)	3,932.8	2,825.0	707.0				153.8	8.0			10.2	228.8
1936 to date[13]	48,967.2	38,489.8	2,577.8		339.3	833.5	1,965.7	482.1	19.4	102.9	51.8	3,997.9

See footnotes at end of table, p. 300.

TABLE 79.—*Unemployment trust fund, 1936–65*—Continued

[In millions of dollars]

Fiscal year or month	Expenditures other than investments								
	Total	Employment security program							
		State accounts,[1] withdrawals by States	Employment Security Administration account [2]				Federal extended compensation account [5]		
			Grants to States	Payments to general fund		Salaries and expenses	Temporary extended compensation payments	Repayment of advances from general fund	Reimbursement to State accounts [1]
				Reimbursement for administrative expenses	Interest on advances [14]				
1936–52	[11] 10, 535. 9	9, 920. 9	----	----	----	----	----	----	----
1953	1, 009. 8	912. 6	----	----	----	----	----	----	----
1954	1, 744. 9	1, 604. 8	----	----	----	----	----	----	----
1955	1, 965. 4	1, 759. 5	----	----	----	----	----	----	----
1956	1, 392. 6	1, 287. 0	----	----	----	----	----	----	----
1957	1, 643. 9	1, 510. 7	----	----	----	----	----	----	----
1958	3, 148. 0	2, 926. 4	----	----	----	----	----	----	----
1959	3, 053. 9	2, 796. 9	----	----	----	----	----	----	----
1960	2, 736. 4	2, 366. 3	----	----	----	----	----	----	----
1961	[12] 4, 733. 7	3, 552. 0	375. 0	5. 1	3. 0	7. 7	481. 2	----	6. 1
1962	3, 906. 4	2, 818. 8	467. 6	5. 1	3. 5	10. 0	303. 9	----	37. 8
1963	3, 815. 5	2, 810. 2	336. 4	5. 6	3. 4	11. 6	−15. 0	466. 3	2. 4
1964 (estimated)	[15] 3, 555. 4	2, 550. 0	410. 0	5. 6	3. 2	12. 4	----	302. 5	----
1965 (estimated)	[16] 3, 442. 6	2, 450. 0	438. 7	5. 8	3. 6	13. 3	----	----	----
1936 to date [13]	42, 597. 2	36, 356. 6	1, 488. 4	66. 0	12. 9	38. 9	769. 1	766. 7	46. 3

Fiscal year or month	Expenditures other than investments—Continued					Net increase, or decrease (−), in assets	Assets, end of period		
	Railroad unemployment insurance								
	Railroad unemployment insurance account[6]				Administration fund,[10] administrative expenses		Total	Investments	Unexpended balance
	Benefit payments	Temporary extended benefit payments	Repayment of advances to—						
			Railroad retirement account[17]	General fund					
1936–52	507.8					8,673.9	8,673.9	8,647.1	26.9
1953	97.3					584.0	[13] 9,246.7	9,237.0	9.7
1954	140.0					−252.4	8,994.3	8,989.0	5.4
1955	205.9					−540.0	8,454.3	8,443.8	10.5
1956	105.7					335.5	8,789.8	8,701.5	88.3
1957	133.1					268.2	9,057.9	8,975.7	82.3
1958	221.6					−1,292.5	7,765.4	7,720.6	44.8
1959	247.7				9.3	[18] −1,056.5	[19] 6,716.2	6,709.4	6.7
1960	275.0		86.1		9.1	−33.1	6,683.0	6,668.5	14.5
1961	251.7	10.0	32.2		9.7	−930.4	5,752.6	5,716.5	[20] 36.0
1962	201.6	9.3	37.2	2.5	9.1	79.0	5,831.6	5,788.7	42.9
1963	166.7	.1	8.9	9.9	8.8	445.2	6,276.8	6,245.1	31.6
1964 (estimate)	152.2		9.7	7.1	9.3	635.3	6,912.1	6,874.6	37.5
1965 (estimate)	150.0		12.6		8.6	490.2	7,402.3	7,348.9	53.5
1936 to date [13]	2,662.0	19.4	191.3	19.4	53.1	6,370.0	6,377.2	6,344.7	32.5

TABLE 79.—*Unemployment trust fund, 1936–65*—Continued

[1] State unemployment funds; used for benefit payments mainly. Beginning August 1961, withdrawals by States have been reduced by reimbursements to State accounts from Federal extended compensation account.

[2] Established by the Employment Security Act of 1960, approved Sept. 13, 1960 (42 U.S.C. 1101(a)), into which are deposited tax receipts transferred in accordance with the act and from which are paid the administrative expenses of the employment security program and reimbursement for tax refunds. Previously the corresponding amounts were included, respectively, in budget receipts and budget expenditures, and only the excess of receipts over expenditures, if any, was transferred to the trust account by appropriation. Receipts consist of appropriated and unappropriated transfers of tax collections. The Federal unemployment tax allows to the taxpayer credit for contributions to State unemployment funds up to 90 percent of the tax.

[3] Net repayments.

[4] Excess of collections from Federal unemployment tax over expenditures for benefits and administrative expenses each year is deposited in this account to maintain a reserve of $200,000,000 available for loans to States when needed to replenish the balances in their accounts in the trust fund. Beginning 1961, these transfers are from the administration fund in the trust account; previously they were from the general fund. Any remaining excess is credited to the State accounts (42 U.S.C. 1101–1103).

[5] Established by the act approved Mar. 24, 1961 (42 U.S.C. 1105(a)), which provides for a temporary program of extended unemployment compensation payments.

[6] For payment of benefits and refunds (45 U.S.C. 360). Figures exclude interim advance of $15,000,000 from the Treasury and subsequent repayment, both in 1940.

[7] Contributions under the Railroad Unemployment Insurance Act of 1938, as amended (45 U.S.C. 360(a)), in excess of the amount specified for administrative expenses. (See footnote 8.)

[8] Temporary advances are made when the balance in the railroad unemployment insurance account is insufficient to meet payments of benefits and refunds due or to become due. Whenever the balance is sufficient to pay such benefits and refunds, repayments are made, plus interest at 3 percent per annum, pursuant to an act approved May 19, 1959 (45 U.S.C. 360(d)).

[9] Excess, if any, over specified balance at end of year is transferred to the account (45 U.S.C. 361(d)).

[10] Consists of a specified proportion of contributions deposited in the fund to be available for administrative expenses. The Railroad Unemployment Insurance Administration fund was established in the unemployment trust fund pursuant to the amending act of Sept. 6, 1958; before that the administration fund was a separate trust fund (45 U.S.C. 361).

[11] Total includes $107.2 million transferred from State accounts to the railroad unemployment insurance account in connection with its establishment (45 U.S.C. 363).

[12] Beginning fiscal 1961 refunds of taxes (principal only) are reported as deduction from receipts. Interest paid on refunds of taxes is included under expenditures. See footnote 16.

[13] Includes adjustments to monthly statement basis to March 1964.

[14] Includes small amounts for interest on refunds of taxes.

[15] Total includes repayment to Treasury of $93,400,000, temporary unemployment compensation (1958 act).

[16] Total includes repayment to Treasury of $190,000,000, temporary unemployment compensation (1958 act), and $170,000,000 for proposed legislation.

[17] Includes interest.

[18] Excludes adjustment pursuant to the act of Sept. 6, 1958 (45 U.S.C. 361(a)); see footnote 19.

[19] Includes an adjustment of $7,200,000 pursuant to the act of Sept. 6, 1958 (45 U.S.C. 361(a)); see footnote 10.

[20] Includes unappropriated receipts beginning September 1960.

*Less than $50,000.

Source: Treasury Department, Treasury Bulletin, May 1964.

TABLES

STATE AND LOCAL TAXES

TABLE 80.—*State tax collections by major sources, selected years, 1902–63*

[In millions of dollars]

Year	Total excluding unemployment compensation	General sales or gross receipts	Income			Motor fuels sales	Motor vehicle and operator licenses	Tobacco products sales	Alcoholic beverage sales and licenses	Death and gift	Property	Severance	Other
			Total	Individual	Corporation								
1902	$156	----------	----------	----------	----------	----------	(2)	----------	$10	(1)	$82	----------	$64
1913	301	----------	(1)	(1)	(1)	----------	$5	----------	21	(1)	140	----------	135
1919	594	----------	$50	(1)	(1)	$1	65	----------	14	$46	237	----------	181
1922	947	----------	98	(1)	(1)	13	152	(1)	----------	66	348	----------	270
1925	1,305	----------	103	(1)	(1)	148	261	(1)	----------	86	359	(1)	348
1927	1,608	----------	162	(1)	(1)	259	301	(1)	----------	106	370	(1)	410
1930	2,108	$1	233	(1)	(1)	495	356	$12	----------	183	345	(1)	483
1932	1,890	7	153	$74	$79	527	335	19	1	148	328	$19	353
1934	1,979	173	129	80	49	565	305	25	81	93	273	21	314
1936	2,618	364	266	153	113	687	360	44	166	117	228	34	352
1938	3,132	447	383	218	165	777	359	55	227	142	244	58	440
1940	3,313	499	361	206	155	839	387	97	255	113	260	53	449
1941	3,606	575	422	225	197	913	434	106	272	118	268	53	445
1942	3,903	632	518	249	269	940	431	130	313	110	264	62	503
1944	4,071	720	762	316	446	684	394	159	322	114	243	71	602
1946	4,937	899	831	389	442	886	439	198	469	141	249	90	735
1948	6,743	1,478	1,084	499	585	1,259	593	337	499	179	276	131	907
1949	7,380	1,609	1,234	593	641	1,361	665	388	502	176	280	201	964
1950	7,930	1,670	1,310	724	586	1,544	755	414	497	168	307	211	1,054
1951	8,933	2,001	1,492	805	687	1,710	840	430	546	196	346	222	1,150
1952	9,857	2,229	1,751	913	838	1,870	924	449	519	211	370	272	1,262
1953	10,552	2,433	1,779	969	810	2,019	1,012	469	544	222	365	286	1,424
1954	11,089	2,540	1,776	1,004	772	2,218	1,098	464	542	247	391	312	1,502
1955	11,597	2,637	1,831	1,094	737	2,353	1,184	459	550	249	412	306	1,617
1956	13,375	3,036	2,264	1,374	890	2,687	1,295	515	625	310	467	361	1,815
1957	14,531	3,373	2,547	1,563	984	2,828	1,368	556	650	338	479	388	2,004
1958	14,919	3,507	2,562	1,544	1,018	2,919	1,413	616	647	351	533	370	2,001
1959	15,848	3,697	2,764	1,764	1,001	3,058	1,492	675	684	347	566	394	2,171
1960	18,036	4,302	3,389	2,209	1,180	3,335	1,573	923	734	420	607	420	2,333
1961	19,057	4,510	3,621	2,355	1,266	3,431	1,641	1,001	774	501	631	451	2,496
1962	20,561	5,111	4,036	2,728	1,308	3,665	1,666	1,075	831	516	640	451	2,570
1963 [3]	22,099	5,533	4,461	2,954	1,507	3,845	1,779	1,124	884	595	688	465	2,725

DISTRIBUTION OF STATE TAX COLLECTIONS BY MAJOR SOURCES, SELECTED YEARS 1902-63

[In percent]

1902	100.0	----------	----------	----------	----------	----------	(4)	----------	6.4	(1)	52.6	----------	41.0
1913	100.0	----------	(1)	(1)	(1)	----------	1.7	----------	7.0	(1)	46.5	----------	44.8
1919	100.0	----------	8.4	(1)	(1)	0.2	10.9	----------	2.4	7.7	39.9	----------	30.5
1922	100.0	----------	10.3	(1)	(1)	1.4	16.1	(1)	----------	7.0	36.7	----------	28.5
1925	100.0	----------	7.9	(1)	(1)	11.3	20.0	(1)	----------	6.6	27.5	(1)	26.7
1927	100.0	----------	10.1	(1)	(1)	16.1	18.7	(1)	----------	6.6	23.0	(1)	25.5
1930	100.0	(4)	11.0	(1)	(1)	23.5	16.9	0.6	----------	8.7	16.4	(1)	22.9
1932	100.0	0.4	8.1	3.9	4.2	27.9	17.7	1.0	.1	7.8	17.3	1.0	18.7
1934	100.0	8.7	6.5	4.0	2.5	28.5	15.4	1.3	4.1	4.7	13.8	1.1	15.9
1936	100.0	13.9	10.2	5.9	4.3	26.2	13.8	1.7	6.3	4.5	8.7	1.3	13.4
1938	100.0	14.3	12.2	6.9	5.3	24.8	11.5	1.8	7.2	4.5	7.8	1.9	14.0
1940	100.0	15.1	10.9	6.2	4.7	25.3	11.7	2.9	7.7	3.4	7.8	1.6	13.6
1941	100.0	16.0	11.7	6.2	5.5	25.3	12.0	2.9	7.6	3.3	7.4	1.5	12.3
1942	100.9	16.2	13.3	6.4	6.9	24.1	11.0	3.3	8.0	2.8	6.8	1.6	12.9
1944	100.0	17.7	18.7	7.8	10.9	16.8	9.7	3.9	7.9	2.8	6.0	1.7	14.8
1946	100.0	18.2	16.8	7.9	8.9	18.0	8.9	4.0	9.5	2.9	5.0	1.8	14.9
1948	100.0	21.9	16.1	7.4	8.7	18.7	8.8	5.0	7.4	2.7	4.1	1.9	13.4
1949	100.0	21.8	16.7	8.0	8.7	18.4	9.0	5.3	6.8	2.4	3.8	2.7	13.1
1950	100.0	21.0	16.5	9.1	7.4	19.5	9.5	5.2	6.3	2.1	3.9	2.7	13.3
1951	100.0	22.4	16.7	9.0	7.7	19.1	9.4	4.8	6.1	2.2	3.9	2.5	12.9
1952	100.0	22.6	17.8	9.3	8.5	19.0	9.4	4.5	5.3	2.1	3.7	2.8	12.8
1953	100.0	23.1	16.9	9.2	7.7	19.1	9.6	4.4	5.2	2.1	3.5	2.7	13.5
1954	100.0	22.9	16.0	9.1	7.0	20.0	9.9	4.2	4.9	2.2	3.5	2.8	13.5
1955	100.0	22.7	15.8	9.4	6.4	20.3	10.2	4.0	4.7	2.1	3.6	2.6	13.9
1956	100.0	22.7	16.9	10.3	6.7	20.1	9.7	3.9	4.7	2.3	3.5	2.7	13.6
1957	100.0	23.2	17.5	10.8	6.8	19.5	9.4	3.8	4.5	2.3	3.3	2.7	13.8
1958	100.0	23.5	17.2	10.3	6.8	19.6	9.5	4.1	4.3	2.4	3.6	2.5	13.4
1959	100.0	23.3	17.4	11.1	6.3	19.3	9.4	4.3	4.3	2.2	3.6	2.5	13.7
1960	100.0	23.9	18.8	12.2	6.5	18.5	8.7	5.1	4.1	2.3	3.4	2.3	12.9
1961	100.0	23.7	19.0	12.4	6.6	18.0	8.6	5.3	4.1	2.6	3.3	2.4	13.1
1962	100.0	24.9	19.6	13.3	6.4	17.8	8.1	5.2	4.0	2.5	3.1	2.2	12.5
1963 [3]	100.0	25.0	20.2	13.4	6.8	17.4	8.1	5.1	4.0	2.7	3.1	2.1	12.3

1 Distribution not available.
2 Less than $500,000.
3 Preliminary.
4 Less than 0.5 percent.

Sources: 1902, 1913: Bureau of the Census, based on "Wealth, Public Debt, and Taxation"; 1915-41, 1943, 1945, 1947: Bureau of the Census, "Historical Review of State and Local Government Finances," June 1948; 1942, 1944, 1946, 1948, 1950: Bureau of the Census, "Revised Summary of State Government Finances," 1942-50; 1949, 1951: Bureau of the Census, "Compendium of State Government Finances in 1949, 1951"; 1952-63: Bureau of the Census, "State Tax Collections". Compiled by Treasury Department. Office of Tax Analysis.

TABLE 81.—*Local tax collections by major sources,*[1] *selected years, 1902–62*

I. AMOUNTS IN MILLIONS OF DOLLARS

Year	Total	Property taxes	Nonproperty taxes			
			Total	Sales and gross receipts	Income taxes	All other taxes
1902	704	624	80	-----	-----	80
1913	1,308	1,192	116	3	-----	113
1922	3,069	2,973	96	20	-----	76
1927	4,479	4,360	119	25	-----	94
1932	4,274	4,159	115	26	-----	89
1934	3,933	3,803	130	30	-----	100
1936	4,083	3,865	218	90	-----	128
1938	4,473	4,196	277	120	-----	157
1940	4,497	4,170	327	130	19	178
1942	4,625	4,273	352	133	30	189
1944	4,703	4,361	342	136	31	175
1946	5,157	4,737	420	183	38	199
1948	6,599	5,850	749	400	51	298
1950	7,984	7,042	942	484	71	387
1952	9,466	8,282	1,185	627	93	465
1953	10,356	9,010	1,345	718	103	523
1954	10,978	9,577	1,401	703	129	569
1955	11,886	10,323	1,563	779	150	634
1956	12,992	11,282	1,710	889	164	657
1957	14,286	12,385	1,901	1,031	191	679
1958	15,461	13,514	1,946	1,079	215	652
1959	16,531	14,417	2,114	1,150	230	734
1960	18,081	15,798	2,283	1,339	254	692
1961	19,804	17,370	2,434	1,432	258	744
1962 (preliminary)	20,963	18,416	2,546	1,472	308	766

II. PERCENTAGE DISTRIBUTION

Year	Total	Property taxes	Nonproperty taxes: Total	Sales and gross receipts	Income taxes	All other taxes
1902	100	89	11	-----	-----	11
1913	100	91	9	[2]	-----	9
1922	100	97	3	1	-----	2
1927	100	97	3	1	-----	2
1932	100	97	3	1	-----	2
1934	100	97	3	1	-----	3
1936	100	95	5	2	-----	3
1938	100	94	6	3	-----	4
1940	100	93	7	3	[2]	4
1942	100	92	8	3	1	4
1944	100	93	7	3	1	4
1946	100	92	8	4	1	4
1948	100	89	11	6	1	5
1950	100	88	12	6	1	5
1952	100	87	13	7	1	5
1953	100	87	13	7	1	5
1954	100	87	13	6	1	5
1955	100	87	13	7	1	5
1956	100	87	13	7	1	5
1957	100	87	13	7	1	5
1958	100	87	13	7	1	4
1959	100	87	13	7	1	4
1960	100	87	13	7	1	4
1961	100	88	12	7	1	4
1962 (preliminary)	100	88	12	7	1	4

[1] Includes Washington, D.C.
[2] Less than 0.5 percent.

Source: Compiled by Treasury Department, Office of Tax Analysis, from Bureau of the Census "Governmental Finances."

TABLE 82.—*Amounts and percentages of tax revenue obtained from various types of taxes in the several States, fiscal year 1963*

I. AMOUNTS IN MILLIONS

State	Total	General sales	Income			Automotive			Tobacco	Liquor [3]	Death and gift	Property [4]
			Individual [1]	Corporation [1]	Total, income	Motor vehicle licenses [2]	Motor fuels	Total, automotive				
Alabama	$319.5	$100.3	$29.5	$9.9	$39.4	$6.2	$78.2	$84.4	$19.1	$21.9	$0.9	$16.1
Alaska	39.1	--------	13.0	2.2	15.2	3.1	6.1	9.2	2.1	3.1	.1	(5)
Arizona	208.0	82.2	14.0	7.0	21.0	11.9	29.6	41.4	4.1	5.5	1.3	37.6
Arkansas	189.7	66.7	14.0	10.6	24.7	17.5	44.5	62.0	10.7	7.0	.4	.4
California	2,559.3	813.3	321.9	311.3	633.2	153.7	386.7	540.4	70.6	73.0	92.2	147.9
Colorado	231.9	57.9	46.5	21.0	67.5	19.8	41.9	61.8	--------	8.0	8.1	6.9
Connecticut	336.5	101.9	--------	47.1	47.1	24.7	52.2	76.9	19.4	18.9	26.0	(5)
Delaware	97.7	--------	36.6	8.9	45.5	5.4	11.9	17.3	3.8	2.2	5.5	.2
Florida	592.2	191.3	--------	--------	--------	66.9	139.4	206.3	10.7	53.6	5.8	22.3
Georgia	442.6	172.0	49.4	36.0	85.3	20.8	94.3	115.1	22.3	23.2	2.2	1.5
Hawaii	133.1	67.6	31.6	6.1	37.7	(5)	9.7	9.7	2.4	3.6	1.7	--------
Idaho	76.1	--------	21.6	5.4	27.0	11.7	15.5	27.3	4.0	2.9	.6	4.0
Illinois	1,079.9	545.1	--------	--------	--------	115.9	155.8	271.7	56.0	43.5	32.0	1.6
Indiana	441.5	215.0	--------	--------	--------	42.2	108.2	150.3	19.1	19.4	8.9	9.9
Iowa	290.3	88.1	45.5	4.7	50.2	48.1	61.6	109.6	12.1	3.4	8.3	4.1
Kansas	239.0	84.3	28.3	10.9	39.2	26.7	44.3	71.1	9.8	5.8	4.1	9.3
Kentucky	336.7	102.4	47.2	21.7	68.9	14.3	69.4	83.7	9.2	15.8	7.2	18.9
Louisiana	509.3	96.9	18.5	17.5	36.0	15.0	69.2	84.2	29.0	23.1	5.7	16.6
Maine	97.8	30.1	--------	--------	--------	10.4	24.5	34.9	8.0	3.9	4.8	2.3
Maryland	435.2	96.9	112.9	22.5	135.5	31.0	62.3	93.3	22.3	10.3	6.7	16.4
Massachusetts	580.4	--------	186.3	35.9	222.2	28.5	83.4	111.9	43.1	29.0	27.7	.3
Michigan	1,142.7	499.9	--------	--------	--------	80.6	158.3	239.0	68.5	53.8	16.9	60.0
Minnesota	442.5	--------	144.6	37.7	182.3	46.3	62.0	108.3	27.6	20.3	15.2	26.0
Mississippi	221.7	82.8	8.0	13.0	21.0	9.5	51.2	60.7	14.9	5.7	.7	4.3
Missouri	413.5	135.4	65.8	10.4	76.2	45.6	81.1	126.7	22.4	9.6	6.7	5.7
Montana	73.9	--------	13.9	4.7	18.7	4.8	19.7	24.5	6.4	5.1	2.1	6.2
Nebraska	98.6	--------	--------	--------	--------	6.6	40.9	47.5	6.9	3.7	.9	30.5
Nevada	65.7	19.5	--------	--------	--------	7.0	10.4	17.4	4.5	2.7	--------	2.4
New Hampshire	47.5	--------	1.7	--------	1.7	7.7	15.1	22.8	4.8	1.4	2.0	2.0
New Jersey	470.3	--------	7.4	30.8	38.3	80.8	126.9	207.7	60.5	25.3	40.1	2.7
New Mexico	149.0	42.8	14.2	--------	14.2	12.5	26.7	39.2	7.2	2.5	.7	12.0
New York	2,506.3	--------	1,018.7	423.2	1,441.9	149.9	244.8	394.7	123.6	85.3	91.3	4.8
North Carolina	588.6	145.9	103.9	62.7	166.6	36.1	114.0	150.2	--------	22.2	14.6	13.1
North Dakota	68.6	17.6	6.1	1.8	8.0	10.4	13.5	24.0	4.2	3.5	.4	2.7
Ohio	927.2	277.5	--------	--------	--------	107.8	225.4	333.2	64.0	46.6	11.2	42.6
Oklahoma	321.9	62.8	16.8	22.9	39.7	43.4	65.3	108.7	20.7	13.3	7.1	--------
Oregon	225.5	--------	99.9	21.9	121.8	34.5	41.4	75.9	--------	2.2	6.1	(5)
Pennsylvania	1,268.3	397.8	--------	142.8	142.8	106.4	244.9	351.3	86.7	56.3	51.7	1.8

See footnotes at end of table, p. 307.

TABLE 82.—*Amount and percentages of tax revenue obtained from various types of taxes in the several States, fiscal year 1963*—Continued

I. AMOUNTS IN MILLIONS—Continued

State	Total	General sales	Income			Automotive			Tobacco	Liquor [3]	Death and gift	Property [4]
			Individual [1]	Corporation [1]	Total, income	Motor vehicle licenses [2]	Motor fuels	Total, automotive				
Rhode Island	105.7	28.9		10.6	10.6	10.2	18.2	28.4	7.2	3.6	5.1	
South Carolina	264.1	80.5	32.6	18.8	51.4	10.7	56.4	67.2	12.0	20.0	2.4	1.2
South Dakota	64.9	18.2				10.7	16.9	27.6	3.6	3.5	1.2	(5)
Tennessee	352.1	121.3	6.8	22.9	29.7	28.8	86.4	115.1	21.2	10.3	10.4	(5)
Texas	1,041.2	178.9				103.1	203.2	306.3	96.7	41.0	13.2	42.2
Utah	122.1	41.2	18.7	6.4	25.1	7.4	23.1	30.5	2.6	1.0	1.5	10.0
Vermont	51.3		13.5	2.6	16.0	8.3	9.4	17.6	3.7	4.8	1.2	.3
Virginia	410.8		128.9	31.9	160.8	28.4	98.3	126.7	15.1	23.0	5.7	14.7
Washington	549.7	301.7				28.7	78.4	107.1	21.7	20.5	14.2	39.6
West Virginia	225.5	100.0	17.2		17.2	22.6	37.8	60.3	11.3	3.6	3.5	.3
Wisconsin	599.4	55.4	218.8	62.7	281.5	48.5	78.5	127.0	26.2	15.4	18.0	38.5
Wyoming	45.0	12.4				8.3	8.8	17.1	1.7	.6	.5	7.9

II. PERCENTAGE DISTRIBUTION

State	General sales	Income			Automotive			Tobacco	Liquor [3]	Death and gift	Property [4]
		Individual [1]	Corporation [1]	Total, income	Motor vehicle licenses [2]	Motor fuels	Total, automotive				
Alabama	31.4	9.2	3.1	12.3	1.9	24.5	26.4	6.0	6.9	0.3	5.0
Alaska		33.2	5.6	38.9	7.9	15.6	23.5	5.4	7.9	.3	(6)
Arizona	39.5	6.7	3.4	10.1	5.7	14.2	19.9	2.0	2.6	.6	18.1
Arkansas	35.2	7.4	5.6	13.0	9.2	23.5	32.7	5.6	3.7	.2	.2
California	31.8	12.6	12.2	24.7	6.0	15.1	21.1	2.8	2.9	3.6	5.8
Colorado	25.0	20.1	9.1	29.1	8.5	18.1	26.6		3.4	3.5	3.0
Connecticut	30.3		14.0	14.0	7.3	15.5	22.9	5.8	5.6	7.7	(6)
Delaware		37.5	9.1	46.6	5.5	12.2	17.7	3.9	2.3	5.6	.2
Florida	32.3				11.3	23.5	34.8	1.8	9.1	1.0	3.7
Georgia	38.9	11.2	8.1	19.3	4.7	21.3	26.0	5.0	5.2	.5	.3
Hawaii	50.8	23.7	4.6	28.3	(6)	7.3	7.3	1.8	2.7	1.3	
Idaho		28.4	7.1	35.5	15.4	20.4	35.9	5.3	3.8	.8	5.3
Illinois	50.5				10.7	14.4	25.2	5.2	4.0	3.0	.1
Indiana	48.7				9.6	24.5	34.0	4.3	4.4	2.0	2.2

Iowa	30.3	15.7	1.6	17.3	16.6	21.2	37.8	4.2	1.2	2.9	1.4
Kansas	35.3	11.8	4.6	16.4	11.2	18.5	29.7	4.1	2.4	1.7	3.9
Kentucky	30.4	14.0	6.4	20.5	4.2	20.6	24.9	2.7	4.7	2.1	5.6
Louisiana	19.0	3.6	3.4	7.1	2.9	13.6	16.5	5.7	4.5	1.1	3.3
Maine	30.8	-----	-----	-----	10.6	25.1	35.7	8.2	4.0	4.9	2.4
Maryland	22.3	25.9	5.2	31.1	7.1	14.3	21.4	5.1	2.4	1.5	3.8
Massachusetts	-----	32.1	6.2	38.3	4.9	14.4	19.3	7.4	5.0	4.8	.1
Michigan	43.7	-----	-----	-----	7.1	13.9	20.9	6.0	4.7	1.5	5.3
Minnesota	-----	32.7	8.5	41.2	10.5	14.0	24.5	6.2	4.6	3.4	5.9
Mississippi	37.3	3.6	5.9	9.5	4.3	23.1	27.4	6.7	2.6	.3	1.9
Missouri	32.7	15.9	2.5	18.4	11.0	19.6	30.6	5.4	2.3	1.6	1.4
Montana	-----	18.8	6.4	25.3	6.5	26.7	33.2	8.7	6.9	2.8	8.4
Nebraska	-----	-----	-----	-----	6.7	41.5	48.2	7.0	3.8	.9	30.9
Nevada	29.7	-----	-----	-----	10.7	15.8	26.5	6.8	4.1	-----	3.7
New Hampshire	-----	3.6	-----	3.6	16.2	31.8	48.0	10.1	2.9	4.2	4.2
New Jersey	-----	1.6	6.5	8.1	17.2	27.0	44.2	12.9	5.4	8.5	.6
New Mexico	28.7	9.5	-----	9.5	8.4	17.9	26.3	4.8	1.7	.5	8.1
New York	-----	40.6	16.9	57.5	6.0	9.8	15.7	4.9	3.4	3.6	.2
North Carolina	24.8	17.7	10.7	28.3	6.1	19.4	25.5	-----	3.8	2.5	2.2
North Dakota	25.7	8.9	2.6	11.7	15.2	19.7	35.0	6.1	5.1	.6	3.9
Ohio	29.9	-----	-----	-----	11.6	24.3	35.9	6.9	5.0	1.2	4.6
Oklahoma	19.5	5.2	7.1	12.3	13.5	20.3	33.8	6.4	4.1	2.2	-----
Oregon	-----	44.3	9.7	54.0	15.3	18.4	33.7	-----	1.0	2.7	[6]
Pennsylvania	31.4	-----	11.3	11.3	8.4	19.3	27.7	6.8	4.4	4.1	.1
Rhode Island	27.3	-----	10.0	10.0	9.6	17.2	26.9	6.8	3.4	4.8	-----
South Carolina	30.5	12.3	7.1	19.5	4.1	21.4	25.4	4.5	7.6	.9	.5
South Dakota	28.0	-----	-----	-----	16.5	26.0	42.5	5.5	5.4	1.8	[6]
Tennessee	34.5	1.9	6.5	8.4	8.2	24.5	32.7	6.0	2.9	3.0	[6]
Texas	17.2	-----	-----	-----	9.9	19.5	29.4	9.3	3.9	1.3	4.1
Utah	33.7	15.3	5.2	20.6	6.1	18.9	25.0	2.1	.8	1.2	8.2
Vermont	-----	26.3	5.1	31.2	16.2	18.3	34.3	7.2	9.4	2.3	.6
Virginia	-----	31.4	7.8	39.1	6.9	23.9	30.8	3.7	5.6	1.4	3.6
Washington	54.9	-----	-----	-----	5.2	14.3	19.5	3.9	3.7	2.6	7.2
West Virginia	44.3	7.6	-----	7.6	10.0	16.8	26.7	5.0	1.6	1.6	.1
Wisconsin	9.2	36.5	10.5	47.0	8.1	13.1	21.2	4.4	2.6	3.0	6.4
Wyoming	27.6	-----	-----	-----	18.4	19.6	38.0	3.8	1.3	1.1	17.6

[1] New Mexico reports combined individual and corporation income taxes. Both are included under "Individual." The corporation tax in South Dakota is not included since it applies only to financial institutions.
[2] Includes motor vehicle operators' licenses.
[3] Includes both excises and licenses.
[4] Alaska and Tennessee report only back taxes and do not currently use this tax.
[5] Less than $50,000.
[6] Less than 0.05 percent.

NOTE.—Figures are rounded and do not necessarily add to totals.

Source: Compiled by Treasury Department, Office of Tax Analysis, from Bureau of the Census "State Tax Collections in 1963."

TABLE 83.—*State and local tax collections, by State, 1962*

State	Tax collections							
	Amount (millions)			Percentage collected by State government	Per capita		As a percent of personal income	
	State and local	State	Local		Amount	Rank	Amount	Rank
Alabama	$436.7	$304.4	$132.2	69.7	$131.66	51	8.3	42
Alaska	51.9	36.5	15.4	70.3	214.48	26	7.9	46
Arizona	331.4	186.9	144.5	56.4	223.05	22	10.5	10
Arkansas	257.5	177.3	80.2	68.9	139.77	49	9.4	27
California	5,171.4	2,369.4	2,802.0	45.8	303.68	2	10.5	11
Colorado	483.0	234.4	248.6	48.5	255.15	6	10.7	7
Connecticut	674.9	314.7	360.2	46.6	257.10	5	8.4	41
Delaware	112.8	87.9	24.9	77.9	241.56	13	7.8	48
District of Columbia	183.0	----------	183.0	----------	231.89	17	7.3	51
Florida	1,075.2	563.6	511.6	52.4	197.86	34	9.6	24
Georgia	622.4	402.9	219.5	64.7	152.43	44	8.6	37
Hawaii	173.8	132.3	41.5	76.1	250.75	8	10.9	5
Idaho	134.0	71.9	62.1	53.7	191.37	36	9.9	20
Illinois	2,441.1	980.4	1,460.7	40.2	241.74	12	8.5	39
Indiana	947.2	420.1	527.0	44.4	203.13	31	8.6	38
Iowa	639.2	276.5	362.6	43.3	230.41	20	10.5	12
Kansas	516.6	228.3	288.3	44.2	233.21	16	10.6	8
Kentucky	463.3	309.3	154.0	66.8	150.21	45	8.8	34
Louisiana	654.2	485.3	169.0	74.2	194.07	35	11.5	1
Maine	207.3	93.4	114.0	45.1	212.05	28	10.8	6
Maryland	713.9	404.0	310.0	56.6	220.83	23	8.3	43
Massachusetts	1,404.0	549.7	854.2	39.2	270.62	4	9.8	21
Michigan	1,899.2	1,007.5	891.7	53.0	236.54	14	9.8	22
Minnesota	867.0	403.4	463.6	46.5	250.51	9	11.2	3
Mississippi	316.7	204.6	112.1	64.6	140.07	48	11.0	4
Missouri	808.6	392.6	416.1	48.6	187.36	37	7.8	49
Montana	161.6	71.8	89.8	44.4	231.86	18	10.3	15
Nebraska	266.4	94.8	171.7	35.6	184.24	40	7.9	47
Nevada	95.5	56.6	38.9	59.3	272.99	3	8.7	36
New Hampshire	123.5	46.3	77.2	37.5	198.56	32	8.9	32
New Jersey	1,491.6	431.2	1,060.3	28.9	234.64	15	8.3	44
New Mexico	186.5	137.2	49.3	73.6	187.05	38	10.0	18
New York	5,407.7	2,328.6	3,079.1	43.1	309.05	1	10.6	9
North Carolina	739.6	539.1	200.5	72.9	157.23	43	9.0	31
North Dakota	137.2	63.7	73.4	46.4	216.68	25	9.4	28
Ohio	1,992.7	891.7	1,101.0	44.7	198.52	33	8.2	45
Oklahoma	456.2	307.9	148.3	67.5	186.35	39	9.8	23
Oregon	415.6	212.7	202.9	51.2	229.98	21	9.6	25
Pennsylvania	2,360.0	1,258.3	1,101.7	53.3	207.35	29	8.8	35
Rhode Island	191.2	96.8	94.4	50.6	217.81	24	9.3	29
South Carolina	333.6	245.5	88.1	73.6	136.26	50	8.9	33
South Dakota	148.9	56.8	92.1	38.1	206.50	30	10.0	19
Tennessee	526.9	329.1	197.9	62.5	144.29	47	8.5	40
Texas	1,856.6	991.5	865.1	53.4	183.42	41	9.1	30
Utah	205.0	115.9	89.1	56.5	214.00	27	10.2	16
Vermont	89.7	49.7	40.0	55.4	231.79	19	11.5	2
Virginia	623.2	359.6	263.6	57.7	146.70	46	7.4	50
Washington	760.1	522.6	237.6	68.8	252.54	7	10.2	17
West Virginia	306.5	212.7	93.8	69.4	170.68	42	9.5	26
Wisconsin	979.4	459.7	519.8	46.9	243.70	11	10.5	13
Wyoming	81.8	44.0	37.8	53.8	246.45	10	10.4	14
Total	41,523.3	20,561.1	20,962.5	49.5	223.46	x x	9.4	x x

Source: U.S. Bureau of the Census, Governmental Finances in 1962, October 1963. Compiled by the Advisory Commission on Intergovernmental Relations.

TABLE 84.—*State individual income taxes: Personal exemptions and credits for dependents, April 1 1964*

State	Personal exemption		Credit for dependents	Additional exemption on account of—	
	Single	Married or head of family		Age	Blindness
Alabama	$1,500	$3,000	$300	----	----
Alaska	600	1,200	600	$600	$600
Arizona	1,000	2,000	600	1,000	500
Arkansas [1]	17.50 (1,750)	35 (3,250)	6 (300)	----	----
California	1,500	3,000	600	----	600
Colorado	750	1,500	750	750	750
Delaware	600	1,200	600	600	600
Georgia	1,500	3,000	600	600	600
Hawaii	600	1,200	600	600	[2] 5,000
Idaho	600	1,200	600	600	600
Indiana	1,000	(3)	500	500	500
Iowa [1]	15 (1,500)	30 (2,333)	7.50 (333)	15	15
Kansas	600	1,200	600	600	600
Kentucky [1]	20 (1,000)	40 (2,000)	20 (1,000)	20 (1,000)	20 (1,000)
Louisiana [4]	2,500 (50)	5,000 (100)	[5] 400 (8)	----	1,000
Maryland	800	1,600	[6] 800	800	800
Massachusetts [7]	2,000	2,500–4,000	400	----	2,000
Minnesota [1]	10 (833)	30 (1,700)	15 (514)	(8) (8)	(8) (8)
Mississippi	5,000	7,000	----	----	----
Missouri	1,200	2,400	400	----	----
Montana	600	1,200	600	600	600
New Hampshire [9]	600	600	----	----	----
New Jersey [10]	600	1,200	600	600	600
New Mexico	600	1,200	600	600	600
New York [11]	600	1,200	600	600	600
North Carolina	1,000	[12] 2,000	300	----	1,000
North Dakota	600	1,500	600	600	600
Oklahoma	1,000	2,000	500	----	----
Oregon	600	1,200	[13] 600	(13)	[13] 600
South Carolina	800	1,600	800	800	800
Tennessee [11]	----	----	----	----	----
Utah	600	1,200	600	----	600
Vermont	500	1,000	500	500	500
Virginia	1,000	2,000	200	600	600
West Virginia	600	1,200	600	600	600
Wisconsin [1]	10 (435)	20 (870)	10 (404)	15	----
District of Columbia	1,000	2,000	500	500	500

[1] Personal exemptions and credits for dependents are allowed in the form of tax credits which are deductible from an amount of tax. With respect to personal exemptions, the sum in parentheses is the exemption equivalent of the tax credit assuming that the exemption is deducted from the lowest brackets. With respect to the credits for dependents, the sum in parentheses is the amount by which the 1st dependent raises the level at which a married couple becomes taxable.

[2] The $5,000 deduction is allowed in lieu of the personal exemption.

[3] Lesser of $1,000 or adjusted gross income of each spouse.

[4] The exemptions and credits for dependents are deductible from the lowest income bracket and are equivalent to the tax credits shown in parentheses.

[5] The $1,000 additional exemption for blindness is also allowed for dependents.

[6] An additional credit of $800 is allowed for each dependent 65 years of age or over.

[7] The exemptions shown are those allowed against business income, including salaries and wages. A specific exemption of $2,000 is allowed for each taxpayer. In addition, a dependency exemption of $500 is allowed for a dependent spouse who has income from all sources of less than $2,000. In the case of a joint return, the exemption is the smaller of (1) $4,000 or (2) $2,000 plus the income of the spouse having the smaller income. For nonbusiness income (annuities, interest, and dividends), the exemption is the smaller of (1) $1,000 or (2) the unused portion of the exemption applicable to business income. Married persons must file a joint return in order to obtain any nonbusiness income exemption. If a single person, or either party to a joint return, is 65 years of age, the exemption is increased from $1,000 to $1,500. No exemption is allowed against nonbusiness income if income from all sources exceeds $5,000 for a single person or $7,500 for married persons.

[8] An additional tax credit of $10 for single persons and $15 each for taxpayer and spouse is allowed for persons 65 years of age or over and for blind persons.

[9] The tax applies only to interest and dividends.

[10] The tax is imposed on the net income and net capital gain derived from New York sources by New Jersey resident individuals and from New Jersey sources by New York resident individuals.

[11] A statutory credit of $10 for a single person and $25 for a married person living with spouse or a head of household is provided.

[12] An additional exemption of $1,000 is allowed a married woman with separate income.

[13] A credit of $1 is allowed for each $100 actually contributed by the taxpayer as partial support of a person who would qualify as a dependent except for the "chief support" provision. The credit shall not exceed $6. Taxpayers and their spouses aged 65 or over receive a $12 credit against the amount of tax otherwise owed. Blind taxpayers and their spouses receive a credit of $18.

Source: Compiled by Treasury Department, Office of Tax Analysis.

TABLE 85.—*State individual income taxes: Tax rates, April 1, 1964*

State	Net income after personal exemption	Rate	Special rates or features
Alabama	First $1,000	1.5	A standard deduction and an optional tax table are provided.
	$1,001 to $3,000	3	
	$3,001 to $5,000	4.5	
	Over $5,000	5	
Alaska	First $2,000	3.20	Do.
	$2,001 to $4,000	3.52	
	$4,001 to $6,000	4.16	
	$6,001 to $8,000	4.80	
	$8,001 to $10,000	5.44	
	$10,001 to $12,000	6.08	
	$12,001 to $14,000	6.88	
	$14,001 to $16,000	7.52	
	$16,001 to $18,000	8	
	$18,001 to $20,000	8.48	
	$20,001 to $22,000	8.96	
	$22,001 to $26,000	9.44	
	$26,001 to $32,000	9.92	
	$32,001 to $38,000	10.40	
	$38,001 to $44,000	11.04	
	$44,001 to $50,000	11.52	
	$50,001 to $60,000	12	
	$60,001 to $70,000	12.48	
	$70,001 to $80,000	12.96	
	$80,001 to $90,000	13.44	
	$90,001 to $100,000	13.92	
	$100,001 to $150,000	14.24	
	$150,001 to $200,000	14.40	
	Over $200,000	14.56	
Arizona	First $1,000	1	A standard deduction and an optional tax table are provided. Resident taxpayers have the option of using as a tax base Federal net income less Federal income tax and certain Federal credits.
	$1,001 to $2,000	1.5	
	$2,001 to $3,000	2	
	$3,001 to $4,000	2.5	
	$4,001 to $5,000	3	
	$5,001 to $6,000	3.5	
	$6,001 to $7,000	4	
	Over $7,000	4.5	
Arkansas	First $3,000	1	A standard deduction is allowed.
	$3,001 to $6,000	2	
	$6,001 to $11,000	3	
	$11,001 to $25,000	4	
	Over $25,000	5	
California	First $2,500	1	A standard deduction and an optional tax table are provided.
	$2,501 to $5,000	2	
	$5,001 to $7,500	3	
	$7,501 to $10,000	4	
	$10,001 to $12,500	5	
	$12,501 to $15,000	6	
	Over $15,000	7	
Colorado	First $1,000	3	A standard deduction and an optional tax table are provided. Surtax on intangible income in excess of $5,000, 2 percent.
	$1,001 to $2,000	3.5	
	$2,001 to $3,000	4	
	$3,001 to $4,000	4.5	
	$4,001 to $5,000	5	
	$5,001 to $6,000	5.5	A credit of ½ of 1 percent of net taxable income against income tax otherwise due is allowed for income under $9,000.
	$6,001 to $7,000	6	
	$7,001 to $8,000	6.5	
	$8,001 to $9,000	7	
	$9,001 to $10,000	7.5	
	Over $10,000	8	
Delaware	First $1,000	1.5	A standard deduction and optional tax table are provided.
	$1,001 to $2,000	2	
	$2,001 to $3,000	3	
	$3,001 to $4,000	4	
	$4,001 to $5,000	5	
	$5,001 to $6,000	6	
	$6,001 to $8,000	7	
	$8,001 to $30,000	8	
	$30,001 to $50,000	9	
	$50,001 to $100,000	10	
	Over $100,000	11	
Georgia	First $1,000	1	A standard deduction is allowed.
	$1,001 to $3,000	2	
	$3,001 to $5,000	3	
	$5,001 to $7,000	4	
	$7,001 to $10,000	5	
	Over $10,000	6	

TABLE 85.—*State indivudual income taxes: Tax rates, April 1, 1964*—Continued

State	Net income after personal exemption	Rate	Special rates or features
Hawaii	First $500	3	A standard deduction and an optional tax table are provided. Alternative tax on capital gains: Deduct 50 percent of capital gains and pay an additional tax of 3 percent of the entire amount of such gains.
	$501 to $1,000	3.5	
	$1,001 to $2,000	4	
	$2,001 to $5,000	5	
	$5,001 to $10,000	6	
	$10,001 to $20,000	7	
	$20,001 to $30,000	8	
	Over $30,000	9	
Idaho	First $1,000	3.4	A standard deduction is allowed. A $10 filing fee is imposed.
	$1,001 to $2,000	5.5	
	$2,001 to $3,000	7.2	
	$3,001 to $4,000	8.25	
	$4,001 to $5,000	9.35	
	Over $5,000	10.5	
Indiana		2	The tax is applied to adjusted gross income less personal exemptions.
Iowa	First $1,000	.75	A standard deduction and an optional tax table are provided.
	$1,001 to $2,000	1.5	
	$2,001 to $3,000	2.25	
	$3,001 to $4,000	3	
	Over $4,000	3.75	
Kansas	First $2,000	1.5	Do.
	$2,001 to $3,000	2.5	
	$3,001 to $5,000	3	
	$5,001 to $7,000	4	
	Over $7,000	5.5	
Kentucky	First $3,000	2	A standard deduction and an optional tax table are provided.
	$3,001 to $4,000	3	
	$4,001 to $5,000	4	
	$5,001 to $8,000	5	
	Over $8,000	6	
Louisiana	First $10,000	2	A standard deduction is allowed.
	$10,001 to $50,000	4	
	Over $50,000	6	
Maryland	Ordinary income	3	A standard deduction and an optional tax table are provided. For taxable year 1965, the rate on ordinary income and on the 1st $500 of investment income will be 4 percent. All or any part of a surplus over $8,000,000 may be applied to a reduction of the 1965 tax.
	Investment income:		
	First $500	3	
	Balance	5	
Massachusetts	Earned income and business income.	3.075	An optional tax table is provided for earned income and business income. Rates include additional taxes: 3 percent permanent surtax on all types of income; and, through June 30, 1965, 20 percent surtax on all types of income, 1 percent on earned and business income, and 3 percent on capital gains on intangibles.
	Interest and dividends, capital gains on intangibles.	7.38	
	Annuities	1.845	
Minnesota	First $500	1	A standard deduction and an optional tax table are provided. For taxable years beginning before Jan. 1, 1965, the tax is increased by 15 percent. An additional tax of 1 percent of the 1st $1,000 or fraction thereof of gross income is levied on persons whose net tax plus surtaxes does not exceed $10. However, the additional tax shall not increase the total tax payable by such persons to more than $10.
	$501 to $1,000	1.5	
	$1,001 to $2,000	2.5	
	$2,001 to $3,000	3.5	
	$3,001 to $4,000	4.5	
	$4,001 to $5,000	5.5	
	$5,001 to $7,000	6.5	
	$7,001 to $9,000	7.5	
	$9,001 to $12,500	8.5	
	$12,501 to $20,000	9.5	
	Over $20,000	10.5	
Mississippi	First $5,000	2	A standard deduction is allowed. The maximum rate for later years will be: 1965, 3.5 percent on income in excess of $10,000; 1966 and after, 3 percent on income in excess of $5,000.
	$5,001 to 10,000	3	
	Over $10,000	4	
Missouri	First $1,000	1	A standard deduction and an optional tax table are provided.
	$1,001 to $2,000	1.5	The rates apply to total income not merely to the portion of income falling within a given bracket, but as a result of the following tax credits, the schedule in effect is a bracket rate schedule:
	$2,001 to $3,000	2	$1,001 to $2,000 — $5
	$3,001 to $5,000	2.5	$2,001 to $3,000 — 15
	$5,001 to $7,000	3	$3,001 to $5,000 — 30
	$7,001 to $9,000	3.5	$5,001 to $7,000 — 55
	Over $9,000	4	$7,001 to $9,000 — 90
			Over $9,000 — 135

TABLE 85.—*State individual income taxes: Tax rates, April 1, 1964*—Continued

State	Net income after personal exemption	Rate	Special rates or features
Montana	First $1,000	1	A standard deduction is allowed.
	$1,001 to $2,000	2	
	$2,001 to $3,000	3	
	$3,001 to $5,000	4	
	$5,001 to $7,000	5	
	Over $7,000	7	
New Hampshire	Interest and dividends (excluding interest on savings deposits).	4.25	
New Jersey	First $1,000	2	A standard deduction is allowed. The tax is imposed on the net income and net capital gain derived from New York sources by New Jersey resident individuals and from New Jersey sources by New York resident individuals. The rates are the same as those in effect in New York. Capital gains are taxed at ½ the net income rates.
	$1,001 to $3,000	3	
	$3,001 to $5,000	4	
	$5,001 to $7,000	5	
	$7,001 to $9,000	6	
	$9,001 to $11,000	7	
	$11,001 to $13,000	8	
	$13,001 to $15,000	9	
	Over $15,000	10	
New Mexico	First $10,000	1.5	The Federal standard deduction is applicable.
	$10,001 to $20,000	3.0	
	$20,001 to $100,000	4.5	Married taxpayers eligible to file joint returns and individual taxpayers who have 1 or more dependents will not be taxed on net income of $1,500 or less.
	Over $100,000	6.0	
New York	First $1,000	2	A standard deduction and an optional tax table are provided.
	$1,001 to $3,000	3	
	$3,001 to $5,000	4	
	$5,001 to $7,000	5	The tax is reduced by $10 for single persons and $25 for married taxpayers living with spouse and heads of households.
	$7,001 to $9,000	6	
	$9,001 to $11,000	7	
	$11,001 to $13,000	8	
	$13,001 to $15,000	9	
	Over $15,000	10	Income from unincorporated business is taxed at 4 percent. The following credit is allowed: *If tax is* — *Credit is* $100 or less — Full amount of tax $100 to $200 — Difference between $200 and amount of tax. $200 or more — No credit.
North Carolina	First $2,000	3	A standard deduction is allowed.
	$2,001 to $4,000	4	
	$4,001 to $6,000	5	
	$6,001 to $10,000	6	
	Over $10,000	7	
North Dakota	First $3,000	1	Do.
	$3,001 to $4,000	2	
	$4,001 to $5,000	3	
	$5,001 to $6,000	5	
	$6,001 to $8,000	7.5	
	$8,001 to $15,000	10	
	Over $15,000	11	
Oklahoma	First $1,500	1	A standard deduction and an optional tax table are provided.
	$1,501 to $3,000	2	
	$3,001 to $4,500	3	
	$4,501 to $6,000	4	
	$6,001 to $7,500	5	
	Over $7,500	6	
Oregon	First $500	3	A standard deduction and an optional tax table are provided.
	$501 to $1,000	4	
	$1,001 to $1,500	5	
	$1,501 to $2,000	6	
	$2,001 to $4,000	7	
	$4,001 to $8,000	9	
	Over $8,000	9.5	
South Carolina	First $2,000	2	Do.
	$2,001 to $4,000	3	
	$4,001 to $6,000	4	
	$6,001 to $8,000	5	
	$8,001 to $10,000	6	
	Over $10,000	7	
Tennessee	Interest and dividends	6	Dividends from corporations having at least 75 percent of their property subject to the Tennessee ad valorem tax are taxed at 4 percent.

TABLE 85.—*State individual income taxes: Tax rates, April 1, 1964*—Continued

State	Net income after personal exemption	Rate	Special rates or features
Utah	First $1,000	1	A standard deduction is allowed.
	$1,001 to $2,000	2	
	$2,001 to $3,000	3	
	$3,001 to $4,000	4	
	Over $4,000	5	
Vermont	First $1,000	2	A standard deduction and an optional tax table are provided. The rates are subject to reduction if there is sufficient surplus in the general fund.
	$1,001 to $3,000	4	
	$3,001 to $5,000	6	
	Over $5,000	7.5	
Virginia	First $3,000	2	A standard deduction is allowed.
	$3,001 to $5,000	3	
	Over $5,000	5	
West Virginia	First $2,000	1.2	A standard deduction and an optional tax table are provided. For married persons filing joint returns, the size of the brackets is doubled.
	$2,000 to $4,000	1.2	
	$4,001 to $6,000	1.6	
	$6,001 to $8,000	1.8	
	$8,001 to $10,000	2	
	$10,001 to $12,000	2.3	
	$12,001 to $14,000	2.6	
	$14,001 to $16,000	2.8	
	$16,001 to $18,000	3	
	$18,001 to $20,000	3.1	
	$20,001 to $22,000	3.4	
	$22,001 to $26,000	3.5	
	$26,001 to $32,000	3.7	
	$32,001 to $38,000	3.9	
	$38,001 to $44,000	4.1	
	$44,001 to $50,000	4.3	
	$50,001 to $60,000	4.5	
	$60,001 to $70,000	4.7	
	$70,001 to $80,000	4.9	
	$80,001 to $90,000	5	
	$90,001 to $100,000	5.2	
	$100,001 to $150,000	5.3	
	$150,001 to $200,000	5.4	
	Over $200,000	5.5	
Wisconsin	First $1,000	2.3	A standard deduction and an optional tax table are provided.
	$1,001 to $2,000	2.55	
	$2,001 to $3,000	2.8	
	$3,001 to $4,000	3.8	
	$4,001 to $5,000	4.3	
	$5,001 to $6,000	4.8	
	$6,001 to $7,000	5.3	
	$7,001 to $8,000	6.3	
	$8,001 to $9,000	6.8	
	$9,001 to $10,000	7.3	
	$10,001 to $11,000	7.8	
	$11,001 to $12,000	8.3	
	$12,001 to $13,000	8.8	
	$13,001 to $14,000	9.3	
	$14,001 to $15,000	9.8	
	Over $15,000	10	
District of Columbia	First $5,000	2.5	A standard deduction and an optional tax table are provided. Income from unincorporated business is taxed at at 5 percent.
	$5,001 to $10,000	3	
	$10,001 to $15,000	3.5	
	$15,001 to $20,000	4	
	$20,001 to $25,000	4.5	
	Over $25,000	5	

Source: Compiled by Treasury Department, Office of Tax Analysis.

TABLE 86.—*Effect of deductibility*[1] *on combined Federal and State individual income tax marginal rates,*[2] *at selected net income levels under 1965 Federal rates*

Federal taxable income before additional dollar of income	Federal marginal rate for a single individual	State marginal rate[3]	State does not allow deduction of Federal tax: Percentage of additional dollar of income paid to—			State allows deduction of Federal tax: Percentage of additional dollar of income paid to—		
			Federal Government	State government	Federal and State	Federal Government	State government	Federal and State
	Percent	*Percent*	*Percent*	*Percent*	*Percent*	*Percent*	*Percent*	*Percent*
$25,000	50	10	45.0	10	55.0	47.37	5.26	52.63
$30,000	53	10	47.7	10	57.7	50.37	4.96	55.33
$50,000	62	10	55.8	10	65.8	59.49	4.05	63.54
$100,000	70	10	63.0	10	73.0	67.74	3.23	70.97
$200,000	70	10	63.0	10	73.0	67.74	3.23	70.97

[1] The Federal Government allows taxpayers to deduct State income taxes in computing net taxable income for Federal purposes. More than half of the income tax States allow deduction of Federal tax in computing the State tax.

[2] The marginal rate is the rate applicable to the additional taxable income resulting from an additional dollar of income.

[3] The top rate is as high as 10 percent in only 8 States. In 3 of these the rate is 10 percent; in 2 States the top rate is 10.5 percent; and in 2 it is 11 percent. In Alaska a rate of 14.56 percent is applicable to income above $200,000.

Source: Treasury Department, Office of Tax Analysis.

TABLE 87.—*State corporation net income taxes: Tax rates, April 1, 1964*

State	Rate		Related provisions
		Percent	
Alabama		5	
Alaska		5.4	A surtax of 3.96 percent is levied on taxable income in excess of $25,000.
Arizona	1st $1,000	1	
	$1,001 to 2,000	2	
	$2,001 to 3,000	2.5	
	$3,001 to $4,000	3	
	$4,001 to $5,000	3.5	
	$5,001 to $6,000	4.5	
	Over $6,000	5	
Arkansas	1st $3,000	1	
	$3,001 to 6,000	2	
	$6,001 to 11,000	3	
	$11,001 to 25,000	4	
	Over $25,000	5	
California		5.5	Minimum tax, $100.
Colorado		5	
Connecticut		5	If tax yield is greater, 2.5 mills per dollar of asset value. Minimum tax, $25.
Delaware		5	
Georgia		5	
Hawaii	1st $25,000	5	Capital gains entitled to alternative tax treatment are taxed at 2¾ percent.
	Over $25,000	5.5	
Idaho		10.5	A $10 filing fee is imposed.
Indiana		2	The tax is applied to income from sources within Indiana.
Iowa		3	
Kansas		3.5	
Kentucky	1st $25,000	5	
	Over $25,000	7	
Louisiana		4	A specific exemption of $3,000, prorated according to the proportion of total net income taxable in Louisiana, is allowed against net income.
Maryland		5	
Massachusetts		6.765	The tax, including the 3-percent additional tax and the 23-percent surtax, will equal the greater of the following: (*a*) $7.65 per $1,000 on the value of Massachusetts tangible property not taxed locally, or net worth allocable to Massachusetts, plus 6.765 percent of net income; or (*b*) 0.0615 percent of gross receipts assignable to Massachusetts, plus 3.69 percent of net income (not applicable to a corporation deriving 80 percent or more of its total gross receipts from dealing in intangibles); or (*c*) $100.

TABLE 87.—*State corporation net income taxes: Tax rates, April 1, 1964*—Continued

State	Rate		Related provisions
		Percent	
Minnesota		10.23	Includes the primary tax of 7.5 percent, and an additional 1.8 percent for taxable years beginning before Jan. 1, 1965. The basic rate and the surtax are increased 10 percent from Jan. 1, 1961, to Dec. 31, 1965. A credit of $500, deductible from net income, is allowed each corporation. Minimum tax, $10.
Mississippi	1st $5,000	2	
	$5,001 to $10,000	3	
	Over $10,000	4	
Missouri		2	
Montana		4.5	Minimum tax, $10.
New Jersey		1.75	All corporations pay additional tax on net worth.
New Mexico		2	
New York	5.5 percent plus a tax on allocated subsidiary capital of ½ mill per $1.		Corporations are subject to the 5½-percent tax on net income or a tax on 3 alternative bases, whichever is greatest. The alternative taxes are: (1) 1 mill on each dollar of business and investment capital; or (2) 5½ percent of 30 percent of net income plus compensation paid to officers and holders of more than 5 percent of capital stock, less $15,000 and any net loss; or (3) $25, plus the tax on allocated subsidiary capital.
North Carolina		6	
North Dakota	1st $3,000	3	
	$3,001 to $8,000	4	
	$8,001 to $15,000	5	
	Over $15,000	6	
Oklahoma		4	
Oregon		6	Minimum tax, $10.
Pennsylvania		6	
Rhode Island		6	Alternative tax: 40 cents per $100 on corporate excess, if tax yield is greater. Minimum tax, $10.
South Carolina		5	
Tennessee		4	
Utah		4	Corporations are subject to the 4-percent tax or a tax of ⅒ of 1 percent of the value of tangible property within the State, whichever is greater. Minimum tax, $10.
Vermont		5	Minimum tax, $25.
Virginia		5	
Wisconsin	1st $1,000	2	
	$1,001 to $2,000	2.5	
	$2,001 to $3,000	3	
	$3,001 to $4,000	4	
	$4,001 to $5,000	5	
	$5,001 to $6,000	6	
	Over $6,000	7	
District of Columbia		5	

Source: Compiled by Treasury Department, Office of Tax Analysis.

TABLE 88.—*State sales taxes: Types and rates, April 1, 1964*

State	Type of tax [1]	Rates on retail sales				Rates on other services and nonretail businesses
		Tangible personal property (percent)	Selected services			
			Amusements (percent)	Restaurants (percent)	Public utilities (percent)	
Alabama	Retail sales	4	4	4		Motor vehicles, trailers, mining and manufacturing machinery, 1½ percent. A 4 percent occupancy tax is imposed on transient lodging for less than 30 days.
Arizona [2]	do	3	3	1½	1½	Meatpacking, ⅜ percent; wholesale sales of feed to poultry and livestock producers, ½ percent; advertising, printing, publishing, contracting, extracting and processing minerals, and timber, 1½ percent; hotel, apartment, and office rentals, storage, 3 percent.
Arkansas [3]	do	3	3	3	3	Printing and photography; transient lodging, coin-operated devices, alcoholic beverages, 3 percent.
California	do	3		3		Food and medicines are exempt. Manufacturing, processing, printing, 3 percent.
Colorado [4]	do	2		2	2	Transient lodging, 2 percent.
Connecticut [5]	do	3½		3½		Food and medicines are exempt. Transient lodging, 30 days or less, 3½ percent.
Florida [6]	do	3	3	3		Food and medicines are exempt. Rental of living quarters for 12 months or less; vending and amusement machines, 3 percent; motor vehicles, 2 percent.
Georgia [7]	do	3	3	3	3	Transient lodging for less than 90 consecutive days, amusement devices, 3 percent.
Hawaii	Multiple-stage sales	3½	3½	3½		Manufacturers, producers, wholesalers, and selected service businesses, ½ percent; sugar processors and pineapple canners, 1 percent (½ percent after June 30, 1964); insurance solicitors, 1½ percent; contractors, sales representatives, professions, radio broadcasting stations, transient lodging, service businesses and other businesses not otherwise specified, 3½ percent.
Illinois [8]	Retail sales	3½		3½		Sales of services, 3½ percent.
Indiana	do	2		2		Lodging for less than 30 days, 2 percent. Manufacturers, wholesalers (except grocery wholesalers) display advertising, laundry and dry cleaning, ½ percent; all other income, 2 percent.
Iowa [3 9]	do	2	2	2	2	Commercial amusement devices, 2 percent.
Kansas [3]	do	2½	2½	2½	2½	Hotel rooms for periods of less than 28 days; coin-operated devices, 2½ percent.
Kentucky [3]	do	3	3	3	3	Transient lodging for less than 90 days, photography and photo finishing, sewer services, 3 percent.

Louisiana	do	2	2	2	----	Hotels, laundry, dry cleaning, automobile and cold storage, printing, repair services to tangible personal property, 2 percent.
Maine [10]	do	4	----	4	4	Food and medicines are exempt. Lodging in excess of 28 days, 4 percent.
Maryland [5, 11]	do	3	----	3	3	Food and medicines are exempt. Farm vehicles and equipment, 2 percent; production, fabrication, or printing on special order; transient lodging, 3 percent.
Michigan [12]	do	4	----	4	4	50 percent of the amount charged for prescription medicine is exempt. Transient lodging for 1 month or less, 4 percent.
Mississippi [2, 13]	Multiple-stage sales	3	(14)	3	3	Wholesaling, ⅛ percent, (beer and motor fuel 3 percent); sales of tractors to farmers, 1 percent; contracts exceeding $10,000, 2 percent; automobiles, aircraft, trucks, 2 percent; manufacturing or processing machinery, 1 percent; extracting or mining, miscellaneous businesses including warehouses, hotels and tourist courts, laundry, cleaning, meat curing, parking lots, photography, storage, termite or pest control services, specified repair services, 3 percent; cotton ginning, 30 cents per bale.
Missouri [3]	Retail sales	3	3	3	3	Transient lodging, motor vehicles, trailer camps, 3 percent.
Nevada	do	2	----	2	----	
New Mexico [7]	do	3	3	3	3	Liquor wholesalers, ½ percent; extracting minerals (except potash, coal, oil, and gas) and timber, ¾ percent; potash extracting, 3 percent; coal sold directly from mine, ½ percent; smelting, refining or processing of minerals, including oil and gas, ¾ percent; preparing timber or lumber, ⅜ percent; contracting, 1½ percent; transient lodging, professions and service businesses, excluding wages and salaries, 3 percent; farm implements, 1½ percent.
North Carolina [14]	do	3	3	3	----	Prescription medicines are exempt. Motor vehicles, airplanes 1½ percent ($120 maximum); fuel to farmers and manufacturers, machinery and equipment to farmers, dairymen, and certain industries, 1 percent ($80 maximum); laundry, dry cleaning, transient lodging for less than 90 days, 3 percent.
North Dakota [3]	do	2¼	2¼	2¼	2¼	Sales of drugs are exempt. Hotels and motels for less than 30 days, cleaning and repair services, coin-operated music machines, 2¼ percent.
Ohio	do	3	----	3	----	Food and medicines are exempt. Transient lodging for less than 30 days, printing and reproducing, 3 percent.
Oklahoma [15]	do	2	2	2	2	Advertising (exclusive of newspapers, periodicals, and billboards), printing, automobile storage, transient lodging; 2 percent.
Pennsylvania [16]	do	5	----	5	5	Food and medicines are exempt. Transient lodging for less than 30 days; repairing, altering, cleaning of tangible personal property; washing, waxing, lubricating, and inspecting motor vehicles; printing; rental income of coin-operated amusement devices, 5 percent.
Rhode Island [17]	do	3	----	3	3	Food and medicines are exempt.
South Carolina [12]	do	3	----	3	3	Transient lodging for less than 90 days, laundry and dry cleaning, 3 percent.
South Dakota [3]	do	2	2	2	2	Amusement devices, room rentals, 2 percent.

See footnotes at end of table, p. 318.

TABLE 88.—*State sales taxes: Types and rates, April 1, 1964*—Continued

State	Type of tax [1]	Rates on retail sales				Rates on other services and nonretail businesses
		Tangible personal property (percent)	Selected services			
			Amusements (percent)	Restaurants (percent)	Public utilities (percent)	
Tennessee [3]	Retail sales	3		3	3	Transient lodging for less than 90 days, parking lots and storage of motor vehicles, repair service, installations, laundry and dry cleaning, 3 percent; industrial machinery and fuels to manufacturers, 1 percent.
Texas [18]	do	2		2	2	Food and medicines are exempt.
Utah [19]	do	3	3	3	3	Repairing, renovating, installing, rental of living quarters for less than 30 days, laundry, dry cleaning, 3 percent.
Washington	do	4	4	4		Transient lodging, certain specified services, 4 percent.
West Virginia [20]	do	3	3	3		All services except personal, professional, and public utilities, 3 percent.
Wisconsin [21]	do	3	3	3	3	Food and medicines are exempt. Laundry, dry cleaning, repair services, photography, transient lodging for less than 1 month, 3 percent.
Wyoming [7]	do	2	2	2	2	
District of Columbia [22]	do	3		3	3	Prescription medicines are exempt. Transient lodging, 4 percent; food for off-premises consumption, 1 percent.

[1] All but a few States levy sales taxes of the single-stage retail type. Hawaii and Mississippi levy multiple-stage sales taxes. The Arizona and New Mexico taxes, although applicable to some nonretail businesses, are essentially retail sales taxes. Washington and West Virginia levy gross receipts taxes on all businesses, distinct from their sales taxes. Alaska also levies a gross receipts tax on businesses. The rates applicable to retailers, with exceptions, under these gross receipts taxes are as follows: Alaska, ½ per cent on gross receipts of $20,000; $100,000 and ¼ percent on gross receipts in excess of $100,000; Washington, 44/100 percent; and West Virginia, ½ percent. Michigan imposes a form of value-added tax in addition to a retail sales tax. The tax is applicable to the professions and the self-employed, as well as to businesses, and the rate is 7¾ mills, except public utilities which are taxed at 2 mills. In Indiana, an additional tax of ½ percent is imposed on retailers under the gross income tax.

[2] Applies to all public utilities. In Mississippi the rate on sales of industrial gas and electricity is 1 percent and on bus and taxicab fares, 2 percent.

[3] Applies to all public utilities except transportation. In Missouri, to all except transportation of freight.

[4] Applies to gas, electricity, and intrastate telephone and telegraph service.

[5] Meals selling for less than $1 are exempt.

[6] Electricity, gas, water, and communications are specifically exempt.

[7] Applies to all public utilities except water. In Arizona and New Mexico only water for irrigation purposes is exempt. In Wyoming, city taxicab and bus fares less than 24 cents are also exempt.

[8] The 3½-percent rate is effective for the period July 1, 1961, to June 30, 1965.

[9] Sales of new motor vehicles are specifically exempt from the sales tax but are subject to the use tax.

[10] Applies to electricity, gas, and water.

[11] Applies to electricity and gas. Sales of motor vehicles are exempt from the sales tax but are subject to a titling tax of 2 percent (3 percent after June 1, 1964).

[12] Applies to sales of electricity, gas, and intrastate telephone and telegraph service. In South Carolina, to electricity and communitcaions.

[13] Applies to billiard parlors and bowling alleys only. Admissions to theaters and other amusement places are subject to a special amusements tax.

[14] The tax on amusements is a license tax, based on gross receipts of amusement operators, which is levied at the rate applicable to retail sales under the sales tax.

[15] Sales of motor vehicles are specifically exempt but are subject to a 2-percent excise tax. The tax applies to all public utilities except water, transportation of freight, lo transportation, and fares which do not exceed 15 cents.

[16] Meals not over 50 cents are exempt. Applies to gas, electricity, and intrastate telephone and telegraph service.

[17] The tax is scheduled to be increased to 3½ percent on June 1, 1964.

[18] Water, intrastate telephone and telegraph service, and industrial gas and elctreitity are specifically exempt.

[19] Specifically excluded are water, intrastate freight, and street railway fares.

[20] The 3-percent rate includes a 1-percent additional tax applicable to sales in excess of $1 effective through June 30, 1965.

[21] The tax applies to only intrastate telephone and telegraph services.

[22] Transportation and communication services are exempt. Motor vehicles are subject to a 2-percent titling tax.

Source: Compiled by Treasury Department, Office of Tax Analysis.

TABLE 89.—*State tax rates on distilled spirits,*[1] *April 1, 1964*

$1 to $1.50	$1.50 to $2	$2 to $2.50	$2.50 to $4	$4	16 percent of wholesale price
Arizona	California	Connecticut	Arkansas [2]	Alaska	Hawaii.
Delaware	Colorado	Indiana [3]	Florida [4]		
Kentucky [5]	Illinois	Massachusetts [6]	Georgia [7]		
Missouri	Kansas [8]	Oklahoma	Minnesota [9]		
Nevada	Louisiana	Rhode Island [10]	North Dakota [11]		
South Dakota [12]	Maryland	Wisconsin	South Carolina		
	Nebraska		Tennessee [13]		
	New Jersey				
	New Mexico [14]				
	New York				
	Texas				
	District of Columbia				
Total 6	12	6	7	1	1

[1] This tabulation includes only the taxes imposed by the District of Columbia and the 32 States which use the license system for the distribution of distilled spirits. Of the remaining 18 States, 16 have State-operated stores (Alabama, Idaho, Iowa, Maine, Michigan, Montana, New Hampshire, Ohio, Oregon, Pennsylvania, Utah, Vermont, Virginia, Washington, West Virginia, and Wyoming). North Carolina has county-operated stores supervised by the State, and Mississippi prohibits the sales of distilled spirits. The rates used in this table are those applicable to distilled spirits of standard alcoholic content.

[2] An additional 5 cents per gallon is imposed on persons blending, rectifying, mixing, and transporting distilled spirits. A wholesaler's tax of 20 cents per case is also levied. In addition, a 3-percent tax is imposed on all retail sales of liquors.

[3] Includes an enforcement tax of 8 cents per gallon.

[4] Includes a tax of $1.53 and 2 additional taxes of 72 cents and 25 cents. Beverages containing more than 48 percent alcohol (except wines) are taxed at $5 per gallon, including a tax of $3.06 and additional taxes of $1.44 and 50 cents. Beverages manufactured in Florida are taxed as follows: 14 percent to 48 percent alcohol, 28 cents per gallon; more than 48 percent, 55 cents per gallon.

[5] In addition, a tax of 10 cents per gallon is levied on manufacturers, transporters, rectifiers, and blenders. Wholesalers are taxed at 5 cents per case.

[6] Includes a temporary additional tax of 25 cents per gallon scheduled to expire on June 30, 1965.

[7] The tax on distilled spirits manufactured in the State is $1.875 per gallon.

[8] In addition, an enforcement tax of 2½ percent of gross receipts from retail sales is levied.

[9] Includes a 15 percent surtax effective through June 30, 1965.

[10] Distilled spirits imported into the State are taxed on the basis of reciprocity. The current rate, as fixed by the liquor control commission, is $1.50 per gallon.

[11] Includes a temporary additional tax of 80 cents per gallon scheduled to expire on July 1, 1967, and a wholesale liquor transactions tax of $1.10.

[12] In addition, a 10 percent tax is imposed on gross receipts from all intoxicating liquor except high point beer.

[13] In addition, a tax of 15 cents per case is imposed upon sales at wholesale.

[14] If over 100 proof, $2.40 per gallon.

Source: Compiled from Commerce Clearing House, "State Tax Reporter," by Treasury Department, Office of Tax Analysis.

TABLE 90.—*State cigarette tax rates (per standard package of 20 cigarettes), April 1, 1964*

2 cents	2½ cents	3 cents	4 cents	5 cents
Arizona	Kentucky	California	Illinois	Delaware
District of Columbia	(Total 1)	Colorado [1]	Indiana	Iowa
(Total 2)		Virginia [2]	Missouri	New York
		(Total 3)	Wyoming	Ohio
			(Total 4)	South Carolina
				(Total 5)

6 cents	7 cents	8 cents
Alabama	Idaho	Alaska
Arkansas	Michigan	Florida
Connecticut	Nevada	Georgia
Kansas	North Dakota	Louisiana
Maine	Oklahoma	Minnesota
Maryland	Tennessee	Mississippi
Massachusetts	Washington	Montana [3]
Nebraska	(Total 7)	New Jersey
Rhode Island [4]		New Mexico
South Dakota		Pennsylvania [3]
West Virginia		Texas
(Total 11)		Utah
		Vermont
		Wisconsin
		(Total 14)

20 percent of wholesale price	15 percent of retail price
Hawaii (Total 1)	New Hampshire (Total 1)

[1] A tax of 3 cents per package is scheduled to become effective July 1, 1964.
[2] The tax is scheduled to expire June 30, 1966.
[3] Includes the following additional temporary taxes to be levied until veterans' bonus bonds are retired: Montana, 3 cents; Pennsylvania, 1 cent.
[4] The tax is scheduled to be increased to 8 cents beginning June 1, 1964.

Source: Compiled from the Commerce Clearing House, State Tax Reporter by Treasury Department, Office of Tax Analysis.

TABLE 91.—*State gasoline tax rates* [1] *(per gallon), April 1, 1964*

5 cents	5½ cents	6 cents	6½ cents	7 cents	7½ cents	8 cents
Hawaii [1] [2] Illinois Kansas [1] Missouri Texas [1] Wyoming [1] (Total 6)	Massachusetts (Total 1)	Arizona Colorado Connecticut Delaware Idaho Indiana Iowa [1] Maryland [3] Michigan Minnesota Montana [1] Nevada New Jersey New Mexico New York [1] North Dakota Oregon South Dakota [1] Utah Wisconsin District of Columbia (Total 21)	Arkansas Georgia Oklahoma (6.58 cents) Vermont [1] (Total 4)	Alabama California Florida Kentucky Louisiana Maine Mississippi [1] Nebraska New Hampshire [4] North Carolina Ohio Pennsylvania Rhode Island South Carolina [4] Tennessee [1] Virginia West Virginia (Total 17)	Washington (Total 1)	Alaska (Total 1)

[1] In most States, diesel fuel is taxed at the same rate as gasoline. The States which tax diesel fuel at a different rate are: Hawaii, 1 cent plus county taxes; Iowa, 7 cents; Kansas, 7 cents; Mississippi, 8 cents; Montana, 9 cents; New York, 9 cents; South Dakota, 7 cents; Tennessee, 8 cents; Texas, 6.5 cents; Wyoming 7 cents. In all but a few States, liquefied petroleum is taxed at the same rate as gasoline. Vermont does not tax diesel fuel and liquefied petroleum.

[2] In Hawaii County, the State tax rate is 8 cents.

[3] Beginning June 1, 1964, the tax will be 7 cents per gallon.

[4] The rates shown include temporary rates scheduled to expire as follows: New Hampshire, 1 cent, June 30, 1966; South Carolina, 1 cent, June 30, 1972.

Source: Compiled from Commerce Clearing House, State Tax Reporter, by Treasury Department, Office of Tax Analysis.