Review of New Revenue Bill

Specially Prepared for The World by Edward J. Dillon, Certified Public Accountant of Kansas City.

The new war revenue bill as revised by the conference committee and adopted by the house and senate February 13, on the 24th became a law. President Wilson signed this bill immediately on his arrival last Tuesday, when the bill automatically became a law.

This bill is estimated to raise about $6,086,000,000 in taxes or about $1,716,000,000 more than was raised in 1917.

The income and war excess profit taxes are expected to reach $4,713,000,000 or about $1,463,000,000 more than was raised from these same taxes in 1917.

About $1,372,000,000 will be raised from special excise and miscellaneous taxes.

Both the normal and surtax has been materially increased over 1917 and the total normal and surtax up to $150,000 has been increased to about double.

The rates on the excess and war excess profit taxes have also been increased, and it is estimated that the average corporation will pay a little over twice the amount of taxes they paid in 1917 on the same income. However, each individual case differs in the amount of the average increase, invested capital and pre war profits entering into the situation very materially.

For a comparison, a corporation with a $200,000 invested capital and $50,000 net profit paid in 1917 a tax of $10,708. The same corporation with the same profits will pay in 1918, if their pre war profits were less than 10 per cent of their invested capital, $25,008 and if their pre war profit was 20 per cent they will pay $16,064. If it was a partnership of four equal partners with the same invested capital and the same profit, instead of a corporation, the total tax for 1918 that the four partners would have to pay, would be $4,940 or $1,235 each.

The payments are to be made in four installments; one fourth at the time of filing returns (which is March 15, for calendar years) and one-fourth in three six and nine months from the time return is filed.

The law states that where an extension of time in which to file return has been granted at the request of the taxpayer, interest will be charged at one half of 1 per cent per month, from the time it would have been due if no extension had been granted.

The income and excess profit sections of the law is retroactive to January 1, 1918, and the blanks for corporations and for individuals with incomes of over $5,000 will not be distributed until about February 26, and no general extension of time will be given for filing the calendar year returns due March 15. The treasury department, however, on February 13 issued a regulation which will serve for all practical purposes as an extension for 45 days.

This regulation gives a corporation permission to make a rough estimate on the tax due, and detach the letter of remittance which is part of the new combined income and excess profits tax blanks, and send same with check for one-fourth of the total estimated tax. When the completed return is made up, adjustments can be made of any differences between the estimated amount paid on the first installment and the amount that should have been paid according to the completed return.

A statement in writing giving the reasons for asking the extension of time must accompany the remittance.

Individual taxpayers will be given the same privileges whenever the extension is really necessary. There is a provision in this new law that where the commissioner shall examine the return, that any difference in the favor of the taxpayer shall be immediately refunded, and any amount due the department shall be paid on the collector's demand.

If the collector increases the tax, and the under statement was not due to any fault of the taxpayer, there is no penalty, but if it was due to the taxpayer's negligence, but without intent to defraud, there shall be added a tax of 5 per cent of the total amount of the deficiency, plus 1 per cent interest per month on the amount of the installment deficiency from the time each installment was due.

If, however, the under statement was made with fraudulent intent, there shall be added as part of the tax 50 per cent of the amount of the deficiency.

Individuals.

Individuals are not subject to the war excess profit tax, as corporations only are subject to these provisions under this bill. In 1917 individuals and partnerships, as well as corporations, were subject to the excess profit tax.

The exemptions are practically the same as in 1917—$1,000 for a single person, $2,000 for a head of a family or married person, and $200 additional exemption for each minor child or dependent.

The normal tax on the first $4,000 above exemptions is 6 per cent, and all over that amount 12 per cent.

The surtax starts at $5,000, the same as in 1917, but the rates have been considerably increased.

The following few comparisons will show the increase in the total normal and surtax of 1918 over 1917:

(On incomes received from salaries, rents, interest and profits, but not from dividends. When part of the income is derived from dividends, the tax will be less than this table, for dividends are exempt from the normal tax).

Based on $2,000 exemption:

Amount.	1917.	1918.
$ 5,000.00	$ 80.00	$ 180.00
10,000.00	355.44	830.00
20,000.00	1,180.00	2,630.00
30,000.00	2,280.00	4,930.00
40,000.00	3,580.00	7,730.00
50,000.00	5,180.00	11,030.00
100,000.00	16,180.00	35,030.00
200,000.00	49,180.00	101,030.00
500,000.00	192,680.00	323,630.00

While a $20,000 income that did not include any dividends would be taxed $2,630, the same amount of income, when $10,000 of the amount was received in dividends would be taxed only $1,430.

Individuals will be allowed this year to deduct all losses incurred in ventures outside their regular business when these ventures are entered into for profit. They could not deduct these losses under the 1917 law, unless their profits amounted to as much as their losses.

Individuals are permitted to declare a fiscal year the same as corporations, but their books must be closed on the same date and clearly reflect their income.

Partnerships.

Partnerships are not subject to the excess profits tax as they were in 1917. Under the new bill they are to make a return for information only, giving the details of their net profit, the names of the partners and their pro rata share of the profits earned.

The individuals when making their tax returns will include with their other income their pro rata share of the partnership net profits regardless of whether or not they are disturbed.

Corporations.

The normal tax of corporations is 12 per cent, which is double that of the 1917 tax.

A special exemption of $2,000 has been allowed corporations in this bill the same as individuals who are married or heads of family.

Corporations only are subject to the war excess profits tax.

Dividends received from other corporations are exempt from income and war excess profits tax under the new bill.

War Excess Profit Tax.

The first and second brackets are figured in a similar manner to the 1917 excess profit tax, and the third bracket is the difference between the totals of the first two brackets and the tax that would be due if the tax was figured under the war excess profit method.

The excess profit tax deductions are a $3,000 exemption plus a flat 8 per cent of invested capital, regardless of what the pre-war percentages of profit might be.

First Bracket.

A tax of 30 per cent will be levied on the net income in excess of the foregoing deductions, that is not in excess of 20 per cent of the invested capital.

Second Bracket.

A tax of 65 per cent will be levied on the amount of the net income in excess of 20 per cent of the invested capital.

Third Bracket.

The sum (if any) of the difference between the first two brackets, and the total of the tax if figured solely under the war excess profit tax.

War Excess Profit Tax Deductions.

If a corporation was in business during the pre-war years of 1911-12 or 13, then the average net profit for that period, plus $3,000, can be used as war excess profit deduction, plus or minus 10 per cent of the difference of the invested capital at the beginning of the taxable year, and the average invested capital of the pre-war period.

If the corporation was not in business one whole year during the pre-war period, or if the average income was less than 10 per cent, then a special exemption of $3,000 plus 10 per cent of the invested capital can be used as a deduction.

The deductions are subtracted from the total of the net income and the remainder is taxed 80 per cent. The third bracket is the difference between the total of the first and second brackets and the 80 per cent of the income after the deductions have been subtracted.

War Excess Profit Tax Exceptions.

A corporation whose income is due to the personal activities of the principal stockholders, and where the investment is not an income producing factor, comes under the head of a personal service corporation, and is not subject to the war excess profit tax. However, they will make out the corporation return the same as a partnership which is for information purposes only, and the stockholders in making up their individual returns will add their pro rata share of the profits, whether distributed or not. If a part of the business of a corporation in excess of 30 per cent of its total net income will constitute a personal service corporation, then two returns may be made out, one as a partnership and one as a corporation.

A corporation with a net income of $20,000 or less shall in no case be compelled to pay more than 30 per cent of their net income for war taxes.

Oil, Gas and Mining Amendments.

In the case of a bona fide sale of mines, oil, or gas wells, or any interest therein by a corporation, where the principal value of property has been demonstrated by prospecting, exploration, and discovery work done by the taxpayer, the portion of the excess profit tax due to the sale, is not to exceed 20 per cent of the selling price.

If the property as above was owned by an individual, the surtax will not exceed 20 per cent of the selling price of such property or interest.

An individual or corporation that developed or discovered an oil or gas well since March 1, 1913, can take a depletion allowance, based upon the fair market value of the property at the date of discovery or within 30 days thereafter.

In the case of leases, the deduction allowed shall be equitably apportioned between the lessor and lessee, such reasonable allowances to be approved by the commissioner.

Considerable judgment will be necessary in arriving at an equitable depreciation.

Income derived from gold mining is not subject to war excess profit taxes.

Miscellaneous Provisions.

All interest paid or accrued by individuals or corporations may be deducted under the new law. There were conditions under previous laws that prevented portions of the interest from being deducted.

The capital stock tax has been increased to double that of 1917, and the exemptions reduced from $99,000 to $5,000.

Inventories.

Inventories are to be taken according to the best accounting methods in vogue by the particular class of business. I would take this to mean that inventories are to be taken at cost or the fair market value at the close of either the calendar or fiscal year.

If the taxpayer discovers by the time he files his returns March 15 that the prices of the merchandise has materially decreased, he can lower his inventory according to that decrease, and make his return on that basis, by filing a bond for double the amount of the difference in the tax that would be due if the original figures were turned in.

If he does not want to file a bond he can pay his tax on the original basis, and redeterminе his tax on a supplementary return and ask for an abatement, or he can wait until the end of the year and make a redetermined return, based on the decrease in inventories or discount refunded on previous sales, and ask for a refund.

General.

The salaries of the president, supreme court, United States judge and employes (but not state employes) are to be included in gross income.

Soldiers and sailors salaries in excess of $3,500 per annum are subject to the income tax.

The undistributed profit tax provision is eliminated in the new law, but individual stockholders, where the profits are not necessary to the business, and is held for the purpose of preventig the imposition of the surtax are to be taxed on their individual income.

Provision is made for consolidated concerns by affiliated corporations and two or more corporations are deemed to be affiliated if the stock is owned or controlled by the same interest.

Information is to be furnished in connection with all payments of $1,000 or more on salaries, rents, etc.

Miscellaneous Provisions Continued.

Stockholders of record owning 1 per cent or more of the outstanding stock are to be allowed to examine the annual return of the corporation upon making request of the commissioner.

A tax of 10 per cent on the entire net proceeds will be taxed where children under 16 years of age have been employed in any mine or quarry, or in any mill or factory which employes children under 14 years of age.

Any dividends made during the first 60 days of any taxable year are deemed to be out of the earnings of the previous year.

1919 and Subsequent Years.

Individuals will be taxed 4 per cent normal tax on the first $4,000, above exemptions, and 8 per cent above that amount. Corporations will be taxed a flat 10 per cent.

Corporations will be taxed for the war excess profit taxes in the first bracket of 30 per cent of the net income, that is not in excess of 20 per cent of the invested capital and 40 per cent on the amount in excess of 20 per cent.

No comment is made in regard to decreasing the surtax and the rate will evidently be the same as in 1918.