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The Big Corporations Rule

by ROBERT H. JACKSON

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The Big Corporations Rule

In The New Republic of August 28, we published the more important sections of a recent statement by Robert H. Jackson, Special Counsel to the Internal Revenue Bureau, made for the Senate Finance Committee, discussing income and taxation in the United States at the present time. The document published below is Mr. Jackson's companion statement, also slightly condensed, on the role of the corporation in American life today.—THE EDITORS.

THE President, in his tax message of June 29, 1935, says:

> I, therefore, recommend the substitution of a corporation-income tax graduated according to the size of corporation income in place of the present uniform corporation-income tax of 13¾ percent. The rate for smaller corporations might well be reduced to 10¾ percent, and the rates graduated upward to a rate of 16¾ percent on net income in the case of the largest corporations, with such classifications of business enterprises as the public interest may suggest. . . .

Upon the basis of our estimate of corporation incomes for the calendar year 1935, 182,000 corporations, or 95 percent of all of those expected to report net incomes for this year, would pay a smaller tax under such a schedule than under the flat rate now in effect.

It is apparent, therefore, that the proposal of the President in addition to producing additional revenue involves a redistribution of the corporation-tax burden by which 95 percent of all corporations obtain some tax relief, and about 5 percent, consisting of the largest corporations, would sustain an additional burden. Such a shifting of the burden would produce desirable results from many standpoints.

A weakness of our income-tax structure revealed by the depression is the violent fluctuation of government revenues resulting therefrom. It is apparent that if we can combine a tax based on ability to pay with increased reliance for revenues upon that class of corporations whose income is most stable, and decrease our reliance for revenues upon those corporations whose income shows the greatest fluctuation, we move in the direction of stabilizing the revenues and evening up fluctuations.

The Treasury statistics of income for 1932 show that the statutory net deficit of corporations of less than $50,000 of assets constituted 33 percent of their net worth, and that the percentage deficit was progressively smaller for each succeeding group of corporations, as shown below:

Asset Classes (in thousands of dollars)	*Percentage of Statutory Net Deficit*
Under 50	33.0%
50 — 100	14.0
100 — 250	10.0
250 — 500	7.6
500 — 1,000	6.9
1,000 — 5,000	5.7
5,000 — 10,000	5.1
10,000 — 50,000	3.8
50,000 and over	1.1

The National Industrial Conference Board also made a study of 1931 corporation-income tax returns and arrived at substantially similar conclusions.

The National Bureau of Economic Research on April 18, 1934, called attention to the fact that when corporations are grouped according to the value of their assets, no group earned an aggregate net profit in 1931 except the group whose assets exceeded $50,000,000. These concerns (not including subsidiaries) numbered only 632 out of the 381,000 corporations included in the study. But, with their subsidiaries, they owned more than 50 percent of the total assets reported by the 381,000 corporations—$155,000,000,000 out of $296,000,000,000. Further, the Bureau called attention to the fact that there was an impressive relationship between size of corporations and relative smallness of losses, the group of smallest corporations experiencing the greatest percentage deficit. The Bureau's study of these matters is summarized in the following table, which excludes corporations not reporting balance sheets:

Size of Corporations (Total net assets in thousands of dollars)	*Number of reporting corporations*	*Aggregate net profits after tax (in millions of dollars)*	*Aggregate net profits after tax, relative to total stock equity*
Under 50	182,447	415	21.7%
50 — 100	61,144	218	9.1
100 — 250	63,428	353	6.5
250 — 500	31,052	268	4.6
500 — 1,000	19,335	271	3.9
1,000 — 5,000	18,345	591	3.0
5,000 — 10,000	2,588	166	1.8
10,000 — 50,000	2,117	104	0.5
50,000 — and over	632	1,507	2.2

The Treasury, in the light of information now available, is of the opinion that the graduated income tax proposed by the President, which will base revenue yield more upon larger and less upon smaller corporations, would produce a more reliable, predictable and steady flow of revenue to the government than the present flat rate of tax for all. It also believes that such larger corporations are, by reason of their more stable revenues, better able to anticipate and bear the burdens than smaller corporations, whose incomes tend to fluctuate more erratically.

CONCENTRATION OF CORPORATE WEALTH

However, even though it is desirable to tax big corporations at a higher rate than little corporations, from a revenue point of view, the proposal would need examination as to its secondary consequences and as to the underlying economic conditions on which the proposal would operate.

Concentration of corporate assets in this country today can be determined with a fair degree of accuracy from Treasury statistics. In 1932, the number submitting balance sheets was 392,021, of which the reported total assets were $280,085,000,000. The degree of concentration of assets revealed is startling. Over 53 percent of the value of all

assets owned by corporations in this country was owned by 618 corporations, constituting only 0.2 percent of the number of corporations. At the lower extreme the percentage of assets owned is equally significant. Of all American corporations, 67.6 percent held only 2.9 percent of the aggregate corporate assets. We find that 5 percent of the corporations owned 85 percent of all the wealth owned by corporations in 1932. The 5 percent owning the 85 percent of the corporate wealth and the 5 percent whose taxes would be increased are not necessarily identical, but most of the corporations in one class will also be found in the other. A table shows the distribution of assets among all corporations filing balance sheets with returns in 1932:

Assets class (in thousands of dollars)	*Number of returns*		*Total assets (in millions of dollars)*	
	Number in class	*Percent cumulated*	*Amount in class*	*Percent cumulated*
Under 50	206,477	100.0%	3,870	100.0%
50 — 100	58,320	47.3	4,153	98.6
100 — 250	59,500	32.4	9,414	97.1
250 — 500	28,422	17.3	9,988	93.8
500 — 1,000	17,590	10.0	12,289	90.2
1,000 — 5,000	16,705	5.5	34,432	85.8
5,000 — 10,000	2,442	1.3	16,857	73.5
10,000 — 50,000	1,947	.7	39,839	67.5
50,000 and over	618	.2	149,241	53.3

The Big Grow Bigger

We turn now to a study of the degree of concentration of net income reported by corporations for the year 1932. For this purpose, corporations that failed to have net profits are dropped out of the calculations and we have left, as the basis for the study, 73,291 corporations that reported a net profit and filed balance sheets with their returns.

Of all net income enjoyed by corporations during 1932, 50.4 percent went to 201 corporations, which represented only 0.3 percent of the number of corporations having some net income. On the other hand, 45 percent of such corporations are shown to have had less than 2 percent of the total income.

If we eliminate financial institutions, railroads and public utilities and other classes of business, and consider only manufacturing enterprises, we find a similar degree of concentration. Of the total wealth owned by corporations engaged in manufacturing, 64.4 percent was concentrated in the hands of 0.8 percent of the number of corporations classified in that field. Manufacturing corporations with assets of ten millions and over constituted only 1.2 percent of the total number of manufacturing corporations reporting net income, but this small group accounted for 63.3 percent of the aggregate compiled net profits of all manufacturing enterprises.

We find no evidence that a limit to the continued increase in corporate size has yet been reached, or that any real obstacle, economic or legal, to the continued concentration of corporate wealth has yet been created. By comparison between the figures for 1932 and those for 1926, we find that there was an increase in the concentration of corporate income. In 1926, 1.7 percent of the total number of corporations reporting net income accounted for 69.8 percent of the total of all corporations reporting net income. In 1932 it took only 1.1 percent of the total number of corporations reporting net income to account for 72.6 percent of the aggregate net income reported that year. The two years are not fully comparable and the figures therefore may reflect an increasing degree of concentration or they may simply be another evidence of the greater fluctuation in income on the part of the smaller-income group of corporations.

No condition is so favorable to corporate growth as profits. Profits both provide and attract capital. We may take the distribution of profits as a fair indication of prospects for growth. On that basis concentration and more rapid growth of the big companies in comparison with other companies would appear to be a probable continuing process of our economic life.

There is substantial evidence that the depression, because of the greater stability of the larger units, has hastened the concentration of the wealth owned by corporations—at least in some industries, and especially in finance. For example, on December 31, 1929, one of the largest industrial cities in the United States had 72 banks, 8 of which were controlled by the dominant banking interests of that community, and 64 of which were controlled by other interests. By December 31, 1933, the 8 banks owned by the dominant group had all survived, whereas the 64 competitors had been reduced, through closings and mergers, to 33—and of those, 20 corresponded or cleared through the dominant banks. During that period the percentage of capital and surplus reported by the dominant group of banks had increased 31 percent, while the percentage reported by their competitors within the city had decreased 38 percent. Deposits of the dominant banks increased 63 percent, and those of competing banks decreased 45 percent.

In the trade area outside of the same city, on December 31, 1929, 19 banks in 17 towns dominated by the same banking interests had 30 banks as competitors. By December 31, 1933, the dominant banks were all in business and the number of competing banks had decreased to 13. The proportion of bank capital and deposits under the dominant group had increased accordingly.

The social implications of these facts will be read differently according to the temperament, viewpoint and perhaps the interests of different observers. While it is probably debatable whether size has not often exceeded the requirements of efficient operation, and whether in fact it has not sometimes been accomplished at the expense of efficiency, there can be little doubt that the greater stability, on the whole, of large corporations is attributable to their many advantages over their smaller competitors; and these advantages are reasons why size provides a useful measure of ability to contribute to the cost of government. Some of the more obvious advantages are listed below:

1. As buyers of commodities and services, the large volume of their purchases gives the larger corporations a bargaining power that often results in price concessions that smaller concerns do not share.
2. Through widely distributed branch plants and warehouses, they are able to effect important savings in transportation costs, and to sell in a nationwide market.
3. Their large resources enable them to buy up important patents, often to pool these patents with

those obtained by other large enterprises; and to carry on research programs, the fruits of which, while of public as well as private benefit, accentuate their competitive advantages over their smaller rivals.

4. In many cases large concerns have become of such dominating size that they are able to control the market and protect their profit margins.

5. Large corporations possess distinct advantages over their smaller competitors in the facility and cost of financing, for they are able to tap the large reservoirs of capital that are made available through the organized financial markets.

Effect of a Graduated Tax

The effect upon common-share earnings of the graduated tax is not subject to any fixed rule but would depend upon the capital structure of the particular corporation. All earnings available for preferred as well as for common stock are subject to tax, and the tax would usually be paid by the common stock alone, since the preferred stocks are normally entitled to a fixed return and the cost to common stockholders would therefore be greater in cases where preferred stock is outstanding. Also, in years of low earnings, the amount of the tax per share would be lower, and when no taxable earnings were reported no tax at all would be paid, of course.

We have taken, to illustrate the effect of this tax, the relatively high income year of 1930 and the common-stock earnings of five outstanding corporations in that year:

Corporation	1930 reported earnings per share common	1930 earnings adjusted for 1934 tax rate	1930 earnings adjusted for graduated tax	Decline due to graduated tax Amount	Decline due to graduated tax Percent
A	$9.12	$8.93	$8.52	$0.41	4.6%
B	1.65	1.63	1.60	.03	1.8
C	8.08	7.91	7.54	.37	4.7
D	3.12	3.09	3.03	.06	1.9
E	4.46	4.41	4.30	.11	2.5

Treasury statistics show sources of income, such as dividends, and show the importance, relative to total income, of the various sources. The largest total amount of dividends reported as being received by any income class, according to the preliminary report for 1933, is that received by those under $5,000 of net income, but the relative importance of dividends to total income is least in this class, and the relative importance of dividend income is upon an ascending scale as we climb the income brackets. Thus to those with incomes of less than $5,000, dividends on the average contribute but 5.07 percent of their total, while 50 percent of the total net incomes over $1,000,000, is derived from dividends. The following table shows the relative importance of dividends and wages and salaries in various income groups (amounts are given in thousands of dollars):

Net income classes	Total net income	Dividends on stock of domestic corporations	Percent of income	Wages and salaries	Percent of income
Under 5	8,125,000	412,000	5.07%	5,407,000	66.55%
5 — 10	1,854,420	220,044	11.87	937,923	50.58
100 — 150	158,571	64,551	40.70	25,269	15.94
500 — 1,000	72,586	43,345	59.72	2,327	3.21
Over 1,000	99,015	50,284	50.78	2,761	2.79

ROBERT H. JACKSON.

Washington Notes

Congress Makes a Fire-Alarm Exit—Anti-War Leaders Analyzed—Roosevelt's Soft Voice and Big Battleship

UP TO the time of the revolt staged by the cotton and wheat Senators, Congress moved toward adjournment with significant speed. Measures that had been debated for endless weeks flashed through the legislative machinery in seconds. Senator Glass arose to announce a conference agreement on the administration banking bill, a measure of immense potentialities, and before he could articulate his first word, Vice-President Garner declared that the report stood approved. Glass gulped, closed his mouth and sat down.

There was a reason for the frightened haste of Congress. The Democratic leaders, Robinson, Harrison, Byrns, Doughton and O'Connor, have many business friends. They had heard no cheers arise from the country in general after Mr. Roosevelt's fight for the death-sentence clause in the utilities bill, or after his announcement of his tax program. But they did hear insistent criticism from business circles, together with a steady demand that, for the sake of business, Congress should adjourn. The recent Rhode Island election seemed to them a corroborative portent. Some Democratic professionals went about Washington saying that every day Congress remained in session would cost them ten thousand votes. Even more important was their feeling that every day would cost teh thousand dollars in future campaign contributions from business. Two weeks ago they reportedly told the President that if Congress did not adjourn immediately he would find that he had a serious congressional rebellion to deal with. Although it meant sacrificing a number of his "must" bills, Mr. Roosevelt yielded—and then the revolt took place anyhow.

There was a period last week when Washington suddenly became a suburb of Paris. To the whole liberal wing in Congress, nothing seemed as important as the violent break-up of the Paris negotiations over Ethiopia. The beat of the war drums sounded increasingly near, coming up to the very steps of the Capitol. This uprush of feeling in Congress, in my opinion, was wholly spontaneous and unmotivated by hope of personal political advantage. It was a remarkable proof of the essential, almost religious, pacifism of the country or at least that part of it away from the Eastern seaboard.

Five men were revealed as the principal leaders in Congress against war—Senators Nye, Clark, Bone, Borah and Johnson. In estimating the country's future course, the depth of their pacifism is a factor of first importance.

The conspicuous preoccupation of Nye, Clark and Bone with peace is of recent origin, and begins with their service as members of the Senate munitions investigating committee. In the case of all three men, their conception of the problem of peace has been visibly colored by their experiences in the munitions investigation. The intrinsic horror of the trade and its scandalous profits led them first into a search for ways to do away with armament makers, rather than the war system itself. Many months were