which you asked me to look at because it was alleged to be a loophole that would result in large revenue losses. We believe this is not the case and that the new rules adopted in 1954 are better than the old law.

Under the old law, companies could take a tax loss on sales of Treasury stock if they had a loss on it, but if there was a gain involved, instead of selling Treasury stock and having a tax to pay on the gain, they could simply issue new stock which did not result in any taxable gain. Thus the old law really provided a loophole because companies could take losses but avoid taxes on gains. The opportunity to handle transactions to the taxpayer's advantage was noted in the report of the joint Treasury and Congressional Staff Committee in 1953 which studied this point of the tax law.

Corporations typically buy and use their own stock only for limited purposes, in connection with mergers, or stock option and bonus plans. These transactions can be and often are handled by newly issued stock and are then clearly capital transactions. The fact that they may buy their own stock and use it instead of new stock does not change the real character of the transactions.

The Securities and Exchange Commission holds that any gain or loss arising from dealings in Treasury stock affects the capital account and should not be reported in income or in earned surplus. Thus the old tax rule was directly contrary to what was required for reports to stockholders and the public.

There are relatively few instances where corporations deal in their own stock for profit and loss. If officers arrange for a corporation to buy up its own stock because of inside information, both the corporation and its officers are liable to the same sort of penalties under the Securities and Exchange Act as the officers would be if they traded in the stock for their own account.

We shall continue to watch the operation of this and all other provisions of the tax law. If any abuses arise we shall promptly report them to the Congress.

Although I have a high regard for the Secretary, as a member of the tax-writing Ways and Means Committee, I feel qualified through actual experience to recognize the inaccuracies of the Secretary's opinions with respect to the existence of a loophole and I was under the impression that his statements regarding the operation of the laws administered by the Securities and Exchange Commission were incorrect. To verify my impression I wrote to the Securities and Exchange Commission on June 7, 1955, asking if there was any law or regulation imposing a penalty on a corporation buying and selling its own stock similar to the penalty imposed upon the officers or directors of corporations who indulge in inside dealings. On this point the Securities and Exchange Commission replied as follows:

There is no law or regulation which imposes upon a corporation that buys and sells its own stock the penalty that is imposed upon officers and directors who trade in such stock, such as provided by section 16 (b) of the Securities Exchange Act of 1934. In this connection rule X-16A-4 (b) exempts from the provisions of section 16 (b) securities reacquired by an issuer for its account during the time they are held by the issuer. Clearly, the issuer could not recover trading profits from itself.

The Securities and Exchange Commission also supplied me with the information that of hundreds of thousands of corporations required to register, only 376 companies subject to the Public Utilities Holding Company Act of 1935 and 354 companies subject to the Investment Company Act of 1940 are subject to restrictions imposed by the Securities and Exchange Commission regarding the acquisition and sale of the companies' own stock. The Securities and Exchange Commission has similar authority with respect to securities issued by closed-end investment companies. It appears that the SEC's statement is directly contrary to that of the Secretary of the Treasury. The rest of the Secretary's statements are similarly subject to criticism because they are not directed to the subject at hand. For example, it is true that the Securities and Exchange Commission holds that gain or loss arising from dealings in Treasury stock affects the capital account of a corporation and should not be treated as income or earned surplus. However, this ruling is premised upon the requirements not of taxation but business reporting. The logic of bookkeeping may require such profits to be excluded from the operating income of a corporation, but the logic of taxation was, until section 1032, and should now be, equally adamant in requiring such profits to be included in income for the purpose of determining the corporation's income tax. These profits should also be included in earnings and profits of the corporation for purposes of determining the amount of dividends to be taxed to the corporation's shareholders. Surely, the Secretary of the Treasury could not believe that earned surplus for purposes of bookkeeping is equivalent to earnings and profits, or that the considerations governing taxation are always identical to those adopted by accountants in their theoretical analyses. Yet, to read his letter, one would think he does.

The Secretary of the Treasury assures me in his letter that there are relatively few instances where corporations deal in their own stock for a profit. However, he does not attempt to prove his point with statistics, and his statement would seem to be contradicted by the fact that 11 cases, involving $830,000, are currently pending before the courts. Untold others involving presection 1032 law are yet to be processed before assessments can be made. If only those companies listed on the New York Stock Exchange are taken into account, the amount of Treasury stock held is tremendous and the volume of trading in such shares is more than substantial.

It is my belief that the enactment of section 1032 has served to increase the volume of trade in Treasury stock, and such trade will continue to increase in volume now that such transactions are no longer subject to the capital gains tax. Section 1032 is more than a loophole. It is an open sesame to speculation by a corporation in its own stock—an invitation to reap untaxed profits.

The law existing prior to the enactment of section 1032 had its imperfections and uncertainties. This, I do not deny. But section 1032 is worse as a cure than the disease. Under the old law, corporations were not freed from the reporting requirement with respect to dealings in Treasury stock generally imposed by the tax laws. This provided a source of information as to the number of corporations dealing in their own stock and as to the number and value of the shares involved. This requirement, together with the fact that corporations were required to pay taxes on any gain derived from dealing in their own shares, acted as a brake on the number of companies indulging in such activity.

Putting the best face possible upon section 1032, it is a poor substitute for the Treasury regulations which its authors intended it to replace. The provision is not as broad as the regulations. It mentions neither the tax consequences to a corporation on acquisition of its own capital stock nor the consequences to the corporation when such stock is exchange for services rather than money or property. If the objectives of the section had any justification at all that justification lies only in th[illegible] that a corporation should be en[illegible] reward the services of its e[illegible] through incentive plans invol[illegible] corporation's stock.

The tax laws have long been d[illegible] to encourage such incentive programs. However, section 1032 fails to include services as one of the considerations for which a corporation can gain its benefits. Yet a loophole is wide open in it for transactions involving money or property.

I believe that it is possible to deal with the problems proposed by the old Treasury regulations without granting the carte blanche of untaxed profits awarded by section 1032. For that reason, I renew my request to the Secretary of the Treasury for a review of section 1032, for a review of the workings of section 1032 in conjunction with subchapter C of chapter 1 of the Internal Revenue Code of 1954, and urge him to make recommendations for bringing that section into line with the sound administrative and fiscal principles which should govern our tax laws.

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## SUPPLEMENTAL APPROPRIATIONS FOR THE FISCAL YEAR ENDING JUNE 30, 1956

Mr. CANNON submitted the following conference report and statement:

CONFERENCE REPORT (H. REPT. No. 1586)

The committee of conference on the disagreeing votes of the two Houses on the amendments of the Senate to the bill (H. R. 7278) "making supplemental appropriations for the fiscal year ending June 30, 1956, and for other purposes," having met, after full and free conference, have agreed to recommend and do recommend to their respective Houses as follows:

That the Senate recede from its amendments numbered 13, 46, 57, 65, 66, 67, 68, 69, 70, 71, 72, 73, 74, 87, 96, 99, 101, 110, 111, 112, 118, 119, 121, and 136.

That the House recede from its disagreement to the amendments of the Senate numbered 1, 4, 5, 6, 7, 8, 9, 10, 11, 15, 17, 18, 26, 32, 36, 42, 44, 47, 51, 55, 60, 77, 90, 94, 97, 102, 106, 108, 113, 114, 120, 124, 125, 126, 129, 132, 133, 134, 135, 137, 139, 140, and 141 and agree to the same.

Amendment numbered 12: That the House recede from its disagreement to the amendof which are annual savings—Senate Committee on Appropriations, hearings on independent offices appropriations, 1956, pages 157–158.

The General Services Administration stated clearly that surveys by such private firms in records management of Government agencies should supplement and not supersede the central program direction and continuing staff work by the General Services Administration—Senate Committee on Appropriations, hearings on the supplemental appropriation bill, 1955, page 936. By judicious and firm central direction by the General Services Administration, the savings in records management can be very large.

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## SPECIAL ORDER

The SPEAKER. Under previous order of the House the gentleman from Illinois [Mr. O'HARA] is recognized for 30 minutes.

[illegible] O'HARA of Illinois. Mr. Speaker, [illegible] unanimous consent to revise and [illegible] my remarks, and I further ask [illegible] consent that the gentleman [illegible] [Mr. FEIGHAN] be permitted [illegible] his remarks following mine.

The SPEAKER. Is there objection to the request of the gentleman from Illinois?

There was no objection.

[Mr. O'HARA of Illinois addressed the House. His remarks and those of Mr. FEIGHAN will appear in the RECORD hereafter.]

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## SECTION 1032 OF THE INTERNAL REVENUE CODE OF 1954

(Mr. MILLS asked and was given permission to address the House for 10 minutes.)

Mr. MILLS. Mr. Speaker, early this spring it came to my attention that the tax services and commercial publications were advertising as a loophole a section of the Internal Revenue Code of 1954 about which I had long had misgivings. That section is section 1032 which provides as follows:

> (a) Nonrecognition of Gain or Loss: No gain or loss shall be recognized to a corporation on the receipt of money or other property in exchange for stock (including treasury stock) of such corporation.
>
> (b) Basis: For basis of property acquired by a corporation in certain exchanges for its stock, see section 362.

The terms of this provision operate to permit corporations who trade in their own stock for a profit to escape taxation on the gains derived from such activity. The only offsetting liability imposed for this generosity is the denial of any losses incurred from such activity.

The issuance of stock by a corporation has never been treated for tax purposes as an event giving rise to the recognition of taxable gain or deductible loss for the sound reason that the proceeds of such transactions produce capital and do not give rise to income. However, until the enactment of section 1032 of the Internal Revenue Code of 1954 Treasury stock had always been dealt with by Treasury regulations interpreting the general provisions of the law defining gross income. These regulations which, with minor changes, date from May 2, 1934—Treasury Decision 4430, XII-1 C. B. 36—provide as follows:

> Section 39.22 (a)-15: Acquisition or disposition by a corporation of its own capital stock. (a) Whether the acquisition or disposition by a corporation of shares of its own capital stock gives rise to taxable gain or deductible loss depends upon the real nature of the transaction, which is to be ascertained from all its facts and circumstances. The receipt by a corporation of the subscription price of shares of its capital stock upon their original issuance gives rise to neither taxable gain nor deductible loss, whether the subscription or issue price be in excess of, or less than, the par or stated value of such stock.
>
> (b) However, if a corporation deals in its own shares as it might in the shares of another corporation, the resulting gain or loss is to be computed in the same manner as though the corporation were dealing in the shares of another. So also if the corporation receives its own stock as consideration upon the sale of property by it, or in satisfaction of indebtedness to it, the gain or loss resulting is to be computed in the same manner as though the payment had been made in any other property. Any gain derived from such transactions is subject to tax, and any loss sustained is allowable as a deduction where permitted by the provisions of the Internal Revenue Code.

The Tax Court has applied these regulations uniformly, holding that a corporation was not dealing in its shares as it might the shares of another corporation where motivated by a nonprofit business purpose requiring the use of its stock. The Circuit Courts of Appeal, with equal uniformity, have refused to follow the motive test laid down by the Tax Court, holding, instead, that any disposition of Treasury stock gives rise to taxable gain or deductible loss except in the case of a capital readjustment actually involving retirement and reissuance of shares.

The rule of the tax court applied the regulation literally to determine whether or not the corporation was trading in its own shares as it might in the shares of another for profit. As so applied the regulation turned on substance rather than form, and application was premised upon a search inquiring into the facts and circumstances surrounding the transaction in Treasury stock for purpose of determining whether or not the transaction was motivated by no more than a desire for profit. The rule of the circuit courts, on the other hand, turned only upon whether or not the corporation went through the mechanics of actually retiring its Treasury stock and issuing new stock. Finally, in *Burrus Mills, Incorporated* (22 T. C. 881 (1954)), the tax court, after remarking upon the futility of its position, in the face of repeated reversals in circuit courts of appeal reversed its position and adopted that of the courts of appeal. The resulting uniformity was shortlived for on the following day the Court of Claims decided the case of *Anderson, Clayton & Company* v. *U. S.* (122 F. Supp. 837 (1954)), holding that a sale of Treasury stock to executives at a profit for the purpose of keeping control in the active management group did not result in taxable gain. The Supreme Court of the United States granted certiorari on February 7, 1955. I am told that this and 11 other cases, involving a total of $830,000, are awaiting the decision of the Supreme Court.

The differences between authorized but unissued stock and Treasury stock, while usually unappreciated by those outside the legal profession, are fundamental to an understanding of why Treasury stock is so much in demand for corporate business purposes.

A corporation desiring to issue new stock must comply with many laws and regulations which exist for the protection of stockholders which are not applicable in the case of treasury stock. For example, the disposition of treasury stock lies completely within the discretion of the board of directors who may dispose of it without considering the wishes of stockholders or considering stockholders' preemptive rights. In addition, the directors may sell treasury stock for less than its par or stated value. Treasury stock is usually nonassessable and free of many of the State and Federal security regulations applicable to unissued stock and last, but not least, the Federal stamp tax imposed on the transfer of such stock is less than that imposed upon the issuance of stock. To these traditional incentives for a corporation acquiring and dealing in its own stock, section 1032 has made another and far more profitable addition. The corporation can now by law deal in its own shares and enjoy its profits free of taxation.

These, and other considerations, are not taken into account by those who argue that there is no practical difference between a purchase and resale of a corporation's stock and the purchase and retirement of stock followed by the issuance of new shares. The logic of bookkeeping may, indeed, take no cognizance of the differences, but this cannot obscure the practical differences inherent in the very nature of the two types of stock.

The differences in tax treatment accorded transactions involving newly issued stock and Treasury stock by the statutes and courts led corporations holding both authorized but unissued stock and Treasury stock to use the Treasury stock only if the price they had paid for it was less than its cost, thus producing a tax loss. However, if the price paid for the Treasury stock was less than its current market price, the authorized but unissued stock would be used to accomplish their purpose, thus avoiding the capital gain tax. In this manner, corporate taxpayers were enabled to eat their cake and have it, too. This coupled with the uncertainty produced by the conflict between the Tax Court and the courts of appeal described above, gave rise to section 1032.

When I drew the tax avoidance possibilities of section 1032 to the attention of the Secretary of the Treasury, he replied, under date of June 6, 1955, denying the existence of the loophole in the following language:

> The Treasury staff has revelwed again section 1032 of the Internal Revenue Code