

COPY

COORDINATOR OF INFORMATION

Washington, D.C.

April 29, 1942

Chairman Marriner S. Eccles
Board of Governors of the
Federal Reserve System
Washington, D. C.

Dear Chairman:

A conversation with the Norwegian head of several shipping companies drew my attention again to a familiar and long established tax loophole which needs to be closed, particularly in view of the high domestic corporate profit taxes which are in prospect. The ships are under Panamanian registry and the companies are Panama corporations. The earnings of these corporations - fabulously high at present - are not subject to United States taxation, and the Republic of Panama leaves them untaxed, I am told. The companies in question are closely held, and no more is distributed to stockholders than they require for current living expenses. The ships operate from United States ports and are subject to Maritime Commission control, while the companies receive various subsidies and benefits from the United States Government. It should be possible to bring their income, largely derived from sources within the United States, under our tax structure.

I don't know whether anything can be done with the suggestion, but it seems to me that these profits ought not to be overlooked if the problem of war profits is to be comprehensively dealt with. With warmest regards, I am

Sincerely yours,

(signed) Emile.

Emile Despres

May 6, 1942.

Mr. Emile Despres,
Office of the
Coordinator of Information,
Washington, D. C.

Dear Emile:


I have just returned from a brief visit to the West and, therefore, I am somewhat delinquent in replying to your thoughtful letter of April 29 in regard to the conspicuous tax loophole available to Panama corporations operating ships under that country's registry. My understanding is that the Maritime Commission has now ordered these ships under American registry.

I am passing your letter on to Randolph Paul who is, I suppose, the best loophole expert in the country.

I hope you are finding your work and prospects agreeable and to your liking, and I want to take this opportunity to reciprocate your kind regards.

Sincerely yours,

M. S. Eccles,
Chairman.

 ET:b

May 6, 1942.


Mr. Randolph E. Paul,
Assistant to the
Secretary of the Treasury,
Treasury Department,
Washington, D. C.

Dear Randolph:

The attached from Emile Despres, who was on our economic staff before he was drafted by Bill Donovan to head up the economic section in the Office of Coordinator of Information, speaks for itself.

This particular loophole had not occurred to me, though it may have to you. Anyway, I thought you ought to see this communication.

Sincerely yours,

Enclosure
 ET:b



TREASURY DEPARTMENT

WASHINGTON

MAY 28 1942

Dear Marriner:

Your letter of May 6, 1942, enclosing a letter dated April 29, received by you from Mr. Emile Despres of the Office of Coordinator of Information, has been carefully studied.

The question raised is whether shipping companies which are subject to the control of the Maritime Commission, and which receive subsidies and benefits from the United States Government, can escape Federal taxation by incorporating under the laws of a foreign country and by operating ships under a foreign flag.

The Internal Revenue Code and the several Revenue Acts since the Revenue Act of 1921 have contained a paragraph exempting from Federal taxation the income of a foreign corporation "which consists exclusively of earnings derived from the operation of a ship or ships documented under the laws of a foreign country which grants an equivalent exemption to citizens of the United States and to corporations organized in the United States." The Report of the Finance Committee of the Senate on the Revenue Bill of 1921 states the purpose of this provision to be to encourage the international adoption of uniform tax laws affecting shipping companies in order to prevent double taxation. This legislative device has been effective in eliminating the complicated problem of allocating income among the several countries between which a corporation or an individual is engaged in shipping. Foreign corporations are not taxed by the United States and domestic corporations are not taxed by foreign countries with which trade is maintained, provided the terms of section 231 (d) of the Internal Revenue Code are met.

Mr. Despres suggests that corporations organized under the laws of Panama, operating ships in the Panamanian registry, receive subsidies and benefits from the United States Government, yet pay no Federal taxes. I am advised

FOR DEFENSE

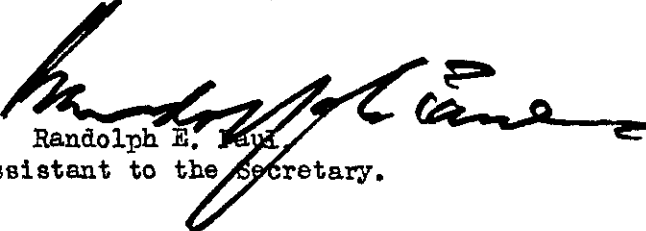


by employees of the Maritime Commission that it is impossible under existing law to transfer to a foreign registry vessels with respect to which the benefit of a subsidy has been received, and that no direct subsidy or benefit can be paid to foreign shipping concerns.

It is possible, of course, for a domestic corporation subsidized by the Federal Government to set up a foreign subsidiary, the income from which would not be subject to Federal taxation until distributed as dividends to the domestic corporation or United States citizen. In some cases this may result in an unwarranted tax benefit, but I doubt the advisability at this time, when shipping facilities are so essential, of turning again to a program which encourages international double taxation of income derived from shipping.

Thanks, nevertheless, for bringing this matter to our attention.

Sincerely yours,



Randolph E. Fava
Assistant to the Secretary.

Honorable Marriner S. Eccles,
Chairman, Board of Governors of
the Federal Reserve System,
Washington, D. C.