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Tapering off of Excess Profits

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Taxation after World War I.

The following gives a brief summary of Excess Profits Tax legislation in and after World War I:

Revenue Act of 1916

A 12-1/2 per cent penalty rate was imposed on profits of munition manufacturers.

Revenue Act of March 1917

The first Excess Profits tax was introduced in the form of an 8 per cent rate on excess profits of corporations and partnerships. excess profits were defined as total net profits minus the sum of \$5,000 plus 8 per cent of invested capital. This tax was superseded by the Revenue Act of October 1917.

War Revenue Act of October 1917

This act introduced a full-fledged war Excess Profits Tax. The tax was applicable to corporations, partnerships and individuals. The tax base was the difference between "prewar normal" profits and current profits. Profits subject to excess profits tax were obtained by deducting from current net profits an excess profits credit. To determine the credit, the average net income for 1911 to 1913 was taken as a percentage of the average invested capital for those years, and this percentage was then applied to the invested capital for the year 1917. However, the credit was not to be less than 7 per cent and not more than 9 per cent of the 1917 invested capital. Also, an exemption of \$3,000 for corporations and \$6,000 for individuals and partnerships was allowed.

The rates were as follows: 20 per cent for such excess profits as do not exceed 15 per cent of invested capital; 25 per cent for such excess profits as fall between 15 and 20 per cent of invested capital; 35 per cent for such excess profits as fall between 20 and 25 per cent of invested capital; 45 per cent for such excess profits as fall between 25 and 35 per cent of invested capital; and 60 per cent for such excess profits as fall above 35 per cent of invested capital.

Revenue Act of 1918 (effective February 1919)

The Excess Profits Tax was adjusted under this Act and the War Profits Tax was added.

The Excess Profits Tax was restricted to corporations and the minimum credit was raised from 7 to 8 per cent of invested capital. For the newly imposed War Profits Tax, the credit provision was more liberal. The minimum credit was 10 per cent and a second method of computing the credit was permitted, the alternative credit being equal to the excess of current earnings over the base year earnings average. Thus both the base year earnings and invested capital methods of determining the excess profits credit were allowed for.

The rates applicable for the income year, 1918 were as follows: 30 per cent for such excess profits as do not exceed 20 per cent of invested capital; and 65 per cent for such excess profits as exceed 20 per cent of invested capital. The additional War Profits Tax, however, in effect increased the combined tax rate to 80 per cent of excess profits, as defined on the basis of the credit provisions under the War Profits Tax.

The rates of the Excess Profits Tax applicable for the income years 1919 and thereafter were as follows: 20 per cent for such excess profits as do not exceed 20 per cent of invested capital; and 40 per cent for such excess profits as exceed 20 per cent of invested capital. These Excess Profits Tax rates remained in effect for the income years 1920 and 1921. The 80 per cent rate under the War Profits Tax was discontinued for 1919.

Revenue Act of 1921

The Excess Profits Tax was repealed, effective January 1, 1922.

A brief summary of corporation income tax changes may also be useful. In 1916 the corporation tax rate was 2 per cent, no exemptions being permitted. The rate was increased to 6 per cent in 1917 and 12 per cent in 1918, when an exemption of \$2,000 was allowed. For 1920 and 1921 the rate was 10 per cent and in 1922 it was raised to 12-1/2 per cent.

A table showing receipts from corporation taxes during World War I is attached.

Attachment

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Corporation and Individual Income Taxes, 1913-1922

Calendar Year	Corporation Income Tax	War Profits and Excess-Profits Taxes	Total Corporation Taxes	Grand Total Individual and Corporation Taxes
1913 ^b	\$43,127,740 ^c	.....	\$43,127,740 ^c	\$71,381,275
1914 ^b	39,144,532	.....	39,144,532	80,190,694
1915 ^b	56,993,657	.....	56,993,657	124,937,252
1916	171,805,150	.....	171,805,150	345,191,844
1917	503,698,029	\$1,638,747,740	2,142,445,769	2,937,826,707
1918	653,198,483	2,505,565,939	2,158,764,422	4,286,486,257
1919	743,535,888	1,431,805,690	2,175,341,578	3,444,971,682
1920	636,508,292	988,726,251	1,625,234,543	2,700,288,329
1921	366,443,621	335,131,811	701,575,432	1,420,962,538
1922	775,310,154	8,466,114 ^d	783,776,268	1,644,833,576

^a United States Treasury, Statistics of Income 1922, p. 33. This table shows tax reported by corporations and individuals on income for the years indicated, hence does not correspond exactly with collections reported on the fiscal year basis by the United States Treasury in Table 39, below (Appendix).

^b Report of Commissioner of Internal Revenue for fiscal year ended June 30 immediately following the year shown.

^c Includes excise tax, \$10,071,077, Act of Aug. 5, 1909.

^d On net income earned from July 1 to Dec. 31, 1921, reported on fiscal year returns whose accounting period terminated prior to July 1, 1922.

Source: R. G. Blakey, The Federal Income Tax, p. 195.