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The 1928 Revenue Act

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Driver was jolted off the seat and killed. Held, that his negligence was not equivalent to abandonment of employment. (Appears to be contra decision cited last month.)—*Corrina vs. De Barbieri,* 160 *N. E.* 397 (*N. Y.*).

September 5 and 6

THE 1928 REVENUE ACT

Mr. Dana Latham, of the Los Angeles (Cal.) Bar, has the following interesting comments on the Federal Revenue Act of 1928 in the June issue of the Los Angeles Bar Association Bulletin:

Rates

The new bill reduces the corporate tax rate beginning January 1, 1928, to 12%, but makes no provision for a sliding scale depending on the amount of income. In addition, the credit for determining net income subject to tax was increased from $2,000 to $3,000. This is the first relief afforded corporate taxpayers since 1921. Nevertheless, a small corporation, the stock of which is closely held by its actual managers, could function much more economically from a Federal tax standpoint, as an old-fashioned partnership.

Individuals whose incomes fall within what is generally termed the "intermediate" surtax brackets, that is, from $20,000 to $80,000, received fairly substantial benefits, although the maximum surtax rate of 20% on incomes in excess of $100,000 remains unchanged, as do the normal tax rates on individual incomes.

Professional and salaried individuals fortunate enough to earn up to $30,000 a year from personal services, received some small relief due to the increase in the earned income credit from $20,000 to $30,000. As in the case of corporations, the provisions relative to individuals become effective January 1, 1928.

The automobile excise tax of 3% was repealed, effective May 29, 1928. Theatre patrons received the benefit of an increase in the exemption for admission tax of from 75c to $3.00. Boxing was penalized by the imposition of a tax of 25% where the admission charged is $5.00 or more.

Annual club dues up to $25 are now exempt from tax. Whatever benefit may accrue from this exemption, however, is more than offset by a specific provision to the effect that all payments to a club, in excess of the exemption, even though consisting of payments for stock therein, are subject to tax, either as dues or initiation fees. The new provisions relative to both admissions and club dues are effective thirty days from May 29, 1928.

In the case of tax-free government bonds, where the amount to be withheld is not more than 2% of the interest due, the new act requires 5% to be withheld at the source in the case of non-resident aliens, and 12% in the case of foreign corporations. In such cases the amount to be withheld is the maximum normal tax in the case of individuals, and the flat corporate rate where corporations are concerned.

Federal estate tax rates remain unchanged.

Form

The new act differs radically from all the former acts in form. From 1918 to the present, the same provisions occurred generally in the same numbered sections of each act. The practitioner was thus enabled to locate easily similar provisions in the different statutes. This theory of arrangement has been scrapped in its entirety. For example, "general definitions," which appeared in Section 1 of the prior acts, appear in Section 701 of the new act. The new arrangement renders analysis less difficult to the general public, but will require thorough study by the practitioner.

The text is materially shorter than that of any of the preceding four acts, an achievement attempted with each new statute, but hitherto unattained. The 1926 act contained twelve titles; the new act but five. This is due in a large measure to the fact that the new act, with certain specific exceptions, may be said to have left the 1926 act in full force and effect. Heretofore, each new act was practically complete in itself. It is now necessary to refer to both the 1926 and 1928 acts. For the present this change in procedure should work satisfactorily. At frequent intervals in the future, however, complete restatements for purposes of simplicity will be essential.

Principal Substantive Changes

Fortunately, practically all of the retroactive provisions offered by the treasury to circumvent unfavorable court rulings have been rejected. The opposition to the treasury's persistent efforts to force through such provisions with their consequent disturbing effect on business, was determined.

Unless otherwise noted, all changes hereafter referred to are effective January 1, 1928, and are not retroactive beyond that date.

Deductions

Estate, inheritance and legacy taxes can now only be deducted by the estate of the decedent and in no case by the legatee or devisee.

Deductions for depreciation and depletion are now permitted to beneficiaries, depending on the provisions of the trust instrument or the actual distribution of income. A grave injustice prevailing under prior acts has thus been eliminated. It would have been fortunate had this salutary provision been made retroactive.

Taxpayers who have incurred expenses in connection with controversies relative to their tax matters, both local, State and Federal, may deduct amounts so expended.

Basis for Determining Gain or Loss

In the case of property sold by an executor, the fair market value at date of death will govern.

In the case of a beneficiary receiving personal property by specific bequest, or a devisee receiving real property by a general or specific devise, or by intestacy, the fair market value at date of decedent's death will govern. In all other cases, so far as the heir, legatee or

devisee is concerned, the basis is the fair market value at the time of the distribution of the property in question to the recipient.

Reorganizations

The general provisions relative to non-taxable reorganizations remain unchanged. An important change occurs, however, in connection with the determination of gain or loss from the sale of property acquired as a result of a reorganization. Prior acts required that the basis in such cases should be cost to the transferror, but excepted stock or securities so acquired, thus enabling such stock or securities to be taken in at their fair market value at the date the reorganization was consummated. This exception has been eliminated, but fortunately Congress refused to make this change retroactive in effect. Some question still remains, however, as to whether or not property other than stock or securities so received may be taken in at its fair value at date of acquisition for purposes of determining gain or loss, depreciation or depletion, provided an 80% control of said properties does not remain in the same persons after the reorganization.

Consolidated Returns

For the year 1928, the provisions of the 1926 act govern. For 1929 and subsequent years, however, Class "A" affiliations only are retained, that is, ownership of 95% or more of the stock of other corporations by the parent corporation. Ownership of stock of two or more corporations by the same individuals as a basis for affiliation has been eliminated.

The statute also provides that in general in the case of property acquired during affiliation by one of the affiliated corporations from any other affiliated company, the basis for determining gain or loss on sale after the termination of the affiliation, shall be determined by regulations to be prescribed by the Commissioner. This will unquestionably result in requiring the corporation involved to adopt cost to its transferror, rather than fair market value at date of acquisition.

Installment Sales

The new act permits income to be reported on the installment basis even though 40% of the total sale price is received in the year of sale. The 1926 act limited the amount to 25% of the sale price. In the case of a change from the closed to the installment method of reporting income, relief from double taxation is given to those who changed prior to 1925 if the original return indicating the change was filed prior to February 26, 1926. The relief, however, governs only the year of change, and does not prevent double taxation for years subsequent to the change.

Elimination of Tax on Real Estate Subdivision Trusts

It is well known that the Treasury Department has asserted a tax against real estate subdivision trusts on the theory that they constituted associations taxable as corporations. The new act specifically exempts such subdivision trusts from such taxation for years prior to 1928, provided the trustee so elects, and the trust complies with certain other requirements of the statute.

Burden of Proof

The new act provides that in all cases involving fraud or the assertion of a liability against the transferee of a taxpayer, where the case is pending before the United States Board of Tax Appeals, and the hearing thereon has not been held prior to May 29, 1928, the burden of proving or showing that fraud has been committed or that the individual in question is actually a transferee of the primary taxpayer, shall be upon the Commissioner. These changes indicate a change in administrative policy for which the taxpaying public may well be grateful.

Statute of Limitations

The new act further limits the time within which an additional tax may be asserted to two years from the date the return was filed so far as taxes imposed by the new act are concerned. The provisions of prior acts relative to failure to file any return and fraudulent returns remains unchanged.

Despite protests from many sources, a provision appears in the new act denying refunds where the tax was paid after the expiration of the statute of limitations provided by prior acts, provided the tax was assessed within the statute and prior to June 2, 1924, and a claim in abatement was filed by the taxpayer. This provision renders practically inoperative the decision of the Supreme Court in the case of *Bowers vs. New York and Albany Lighterage Co.* 273 *U. S.* 346.

September 5 and 6

IS IT A WAY OF ESCAPE?

Most of us have probably noted, upon occasion, the "pointing with pride" by state's attorneys to the fact that so many of the criminal causes started by them have been disposed of at little or no expense to the community through pleas of guilty. What is known as the "Cleveland Survey," by Mr. Alfred Bettman of Cincinnati, brings to the attention a view of these pleas of guilty that is not as complimentary to the social success of this method of handling criminal cases as most of us have imagined. It should be remembered, however, that conditions in rural communities, such as are to be found in North Dakota, are not entirely comparable to the conditions in cities; yet, notwithstanding that, there is sufficient in the following quotation from the study of Mr. Bettman to invite a serious thought:

"The popular impression is that when an offender enters a plea of guilty he throws himself upon the 'mercy of the court.' As a practical proposition he does nothing of the kind. He has already thrown himself upon the mercy of, or struck a bargain with, the prosecutor before he takes his plea. The court usually accepts the recommendation of the prosecutor as to the punishment on plea of guilty. The facts show that in the cities a penitentiary sentence follows a conviction by the jury in a much higher percentage of cases than where sentence is imposed upon a plea of guilty, and that a plea of guilty upon arraignment reduces the chances of a penitentiary sentence in the cities above one-half. In the cities . . . the prosecutors have an immense