

THE RISE AND FALL OF POST-WORLD WAR II CORPORATE TAX REFORM

STEVEN A. BANK*

I

INTRODUCTION

The United States is unique in subjecting corporate income to two layers of tax.¹ In what is called a “classical system,” corporate income is taxed once at the entity level when earned and a second time at the individual level when distributed to shareholders in the form of a dividend.² By contrast, in most other countries, corporate- and shareholder-level taxes are fully or partially integrated through some form of credit or deduction. America’s double taxation of corporate income is a much-criticized but persistent feature of its current tax system despite numerous reform proposals over the last half-century or so.³ Although some measure of integration was finally enacted in 2003 when Congress adopted legislation taxing dividends at the lower capital-gains rate, this legislation, scheduled to expire in 2010, fell far short of including the exemption from individual taxation that was originally proposed.⁴ Some commentators have viewed this modest progress as perhaps the ultimate sounding of the death knell for integration efforts, noting that President Bush was at the height of his power in early 2003 and he had identified this as one of his top priorities.⁵

The entrenchment of our current classical system of corporate taxation is not a recent phenomenon, nor was it a preordained conclusion from the outset

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* Professor of Law, UCLA School of Law. A much-expanded and modified version of this article is a chapter in STEVEN A. BANK, *FROM SWORD TO SHIELD: THE TRANSFORMATION OF THE CORPORATE INCOME TAX, 1861 TO PRESENT* (forthcoming 2010).

1. Michael J. Graetz & Alvin C. Warren Jr., *Integration of Corporate and Individual Income Taxes: An Introduction*, 84 *TAX NOTES* 1767, 1768 (1999).

2. I.R.C. § 11 (2006) (imposing an income tax on corporations); I.R.C. §§ 301, 316 (2006) (imposing a tax on shareholders on distributions out of corporate earnings and profits).

3. Michael Doran, *Managers, Shareholders, and the Corporate Double Tax*, 95 *VA. L. REV.* 517, 518–19, 521 (2009).

4. Jobs and Growth Tax Relief Reconciliation Act of 2003, Pub. L. No. 108-27, § 302, 117 Stat. 752 (codified at I.R.C. § 1(h)(11) (2006)). Originally scheduled to expire in 2008, the relief was extended to 2010. Tax Increase Prevention and Reconciliation Act of 2005, Pub. L. No. 109-222, § 102, 120 Stat. 345, 346.

5. DANIEL N. SHAVIRO, *DECODING THE U.S. CORPORATE TAX* xii (2009).

of the corporate income tax.⁶ The turning point in the corporate tax may have been the decade following World War II. If there ever was a legislative moment for reenvisioning the corporate tax, it was then. Consensus as to the problems with corporate taxation was significant. Businesses had borne the brunt of the burden during the war.⁷ Over that four-year period, corporate income tax rates had more than doubled from nineteen percent to forty percent and Congress had enacted a new excess profits tax at rates topping out at ninety-five percent.⁸ Combined, the two levies accounted for almost fifty-six percent of net income reported to the government by 1944.⁹ The high rates served to heighten scrutiny of the double taxation of corporate income, which had emerged during the New Deal as a byproduct of President Roosevelt's ill-fated experiment with an undistributed-profits tax.¹⁰ Additionally, the winding down of the war promised to lower revenue needs. As a consequence, the push for major corporate tax reform emerged well before V-E Day. By January of 1946, sixty proposals for the relief of double taxation were in circulation,¹¹ many of which were repackaged or reintroduced during succeeding years. It was not until 1954, though, as part of a comprehensive revamp of the Internal Revenue Code, that Congress enacted limited, and ultimately short-lived, dividend tax relief.¹²

This paper considers three questions: (1) Why was dividend-tax relief so long in coming, given the initial momentum for reform; (2) What led dividend-tax reform to rise to the top of the agenda in 1954; and (3) Why, given the degree of interest in integration proposals, was the relief so modest?

6. Compare Steven A. Bank & Kirk J. Stark, *An Evolutionary Perspective on the History of U.S. Business Taxation*, in BUSINESS TAX STORIES 1, 4–5 (Steven A. Bank & Kirk J. Stark eds., 2005) (arguing that the history of the corporate income tax has been “contingent and highly punctuated”), with Robert Charles Clark, *The Morphogenesis of Subchapter C: An Essay in Statutory Evolution and Reform*, 87 YALE L.J. 90, 92 (1977) (arguing that the corporate tax system was the outcome of several basic decisions at the outset).

7. W. ELLIOT BROWNLEE, FEDERAL TAXATION IN AMERICA: A SHORT HISTORY 115 (2d ed. 2004).

8. For corporate income tax and excess profits tax rates, see JACK TAYLOR, INTERNAL REVENUE SERV., CORPORATE INCOME TAX BRACKETS AND RATES, 1909–2002, DATA RELEASE, available at <http://www.irs.gov/pub/irs-soi/02corate.pdf> (last visited October 21, 2009) and Tax Policy Ctr., Major Enacted Tax Legislation, 1940–1949, <http://www.taxpolicycenter.org/legislation/1940.cfm> (last visited October 21, 2009). The excess profits tax, enacted before the U.S. entered the war, used the years 1936 through 1939 as its base, but allowed corporations to elect an invested capital base of eight percent on the first \$5 million and six percent on the next \$5 million. Alfred G. Buehler, *The Problem of the Excess Profits Tax*, in EXCESS PROFITS TAXATION 3, 7 (Tax Institute, Inc. ed., 1953).

9. Buehler, *supra* note 8, at 7–8.

10. See Steven A. Bank, *Corporate Managers, Agency Costs, and the Rise of Double Taxation*, 44 WM. & MARY L. REV. 167, 172 (2002).

11. *Tax Report: A Special Summary and Forecast of Federal and State Tax Developments*, WALL ST. J., Jan. 30, 1946, at 1.

12. I.R.C. §§ 34, 116(a) (1954).

II

POSTWAR CORPORATE TAX REFORM

A. A Flurry of Tax Reform Proposals

In September of 1944, with American troops still fighting in Europe, the Treasury Department's Director of Tax Research, Roy Blough, predicted that the task of crafting a postwar tax program would be "the most difficult tax problem in American history."¹³ Expenses remained at record levels while the appetite for fiscal sacrifice was waning. The excess profits tax and the wartime hikes in corporate income tax rates were considered serious threats to the economy's postwar recovery. At the same time, the individual tax burden had grown dramatically. The fundamental changes wrought by the Revenue Act of 1942, in particular, had both cut individual exemptions drastically and significantly lowered the thresholds for the application of the rising surtax rates on both corporate and individual income. Each of these trends served to increase the stakes for remedying a wide variety of legislative flaws that had been ignored while the war was in high gear.

Double taxation quickly emerged as one of the primary targets of business leaders. This was in large part an outgrowth of the concern for the postwar economy. Several influential studies documented the potential negative effects a high tax burden on corporate income would have on any postwar recovery.¹⁴ In an address before the National Retail Dry Goods Association, investment banker John Hancock advocated reducing corporate rates to their prewar levels "to encourage expansion by private enterprise."¹⁵

One specific concern was the effect of taxes, and particularly double taxation, on incentives for stock investment.¹⁶ George Barnes, a banker and a governor of the Association of Stock Exchange Firms, declared that "[t]he present method of taxing corporate earnings and again taxing the same earnings when they are distributed to the shareholder as dividends, probably constitutes the main stumbling block to a free flow of post-war capital into new industry and the expansion of old ones."¹⁷ The *Wall Street Journal* concurred with this assessment, opining, "With the return of peace it will be vital to our economy that capital flow into new enterprise to provide employment and to increase the

13. *Ruml Asks Repeal of Corporate Tax*, N.Y. TIMES, Sept. 13, 1944, at 20.

14. J. KEITH BUTTERS & JOHN LINTNER, EFFECT OF FEDERAL TAXES ON GROWING ENTERPRISES, STUDY NO. 1: THE LOCKHEED AIRCRAFT CORPORATION 29-30 (1944); J. KEITH BUTTERS & JOHN LINTNER, EFFECT OF FEDERAL TAXES ON GROWING ENTERPRISES, STUDY NO. 2: POLAROID CORPORATION (1944). See *Current Topics of Interest in Wall Street: Taxes and New Ventures*, WALL ST. J., Apr. 25, 1944, at 27; *High Tax Held Curb on Small Business*, N.Y. TIMES, Apr. 25, 1944, at 31.

15. Edward A. Morrow, *Corporate Tax Cut Urged by Hancock*, N.Y. TIMES, Aug. 9, 1944, at 21.

16. See RICHARD B. GOODE, U.S. TREASURY DEP'T, THE POSTWAR CORPORATION TAX STRUCTURE 4-7 (1946).

17. George E. Barnes, *A Plan to Simplify Corporation Taxes and a Solution of Double Taxation of Corporate Earnings*, EXCHANGE, Sept. 1944, at 1, 15.

national income. It is difficult to see how this can happen so long as the present cramping system of double taxation exists.”¹⁸ Corporate leaders’ support for a campaign against double taxation was therefore due in large part to this perceived need for more equity capital.

True tax reform began in the summer of 1944, when three high-profile tax proposals were released within weeks of each other. Despite proposals in 1943 and 1944 to modify the double tax,¹⁹ the tax reform fervor did not begin in earnest until the summer of 1944, when three high-profile tax reform proposals backed by different business groups were released within weeks of each other. Carl Shoup, a Columbia economist and Treasury consultant, called this beginning to what would become a fairly sophisticated national debate over the direction of tax policy “a significant development in American public finance.”²⁰

The most radical corporate-integration-reform proposal of the three was in a report prepared by Beardsley Ruml, the chairman of the Federal Reserve Bank of New York and treasurer of R.H. Macy & Co., and Hans Christian Sonne, a banker originally from Denmark, for the Business Committee of the National Planning Association.²¹ Following on the heels of a briefer, but similar, proposal offered by Princeton economist Harley Lutz,²² Ruml and Sonne advocated repealing the corporate income tax almost completely and replacing it with a five-percent franchise tax and a form of undistributed-profits tax.²³ Effectively, it was a return to Roosevelt’s 1936 plan to replace the corporate income tax with an undistributed-profits tax. The latter was ostensibly imposed “to prevent the use of the corporate form as a device (a) to avoid payment of individual income taxes and (b) to secure undue tax advantages over partnerships and unincorporated businesses,” which suggests it could have been styled as a penalty tax rather than the automatic tax imposed during the New

18. Editorial, *Why Venture*, WALL ST. J., May 4, 1944, at 4. See George B. Bryant Jr., *The Tax Future: Peace Will Bring Little Relief for Individuals but Some for Business*, WALL ST. J., Dec. 5, 1944, at 1 (“It is pretty well agreed among the experts and tax committee members that present corporation taxes cannot be carried over into the post-war period. They would be too much of a drag on the economy.”).

19. A Brookings Institution report proposing a shareholder-credit method of integration was released in 1943, Lewis H. Kimmel, POSTWAR TAX POLICY AND BUSINESS EXPANSION (Brookings Institution, 1943), and Eustace Seligman proposed a near repeal of the corporate income tax in early 1944, Eustace Seligman, *A Post-War Program for Taxation of Corporations and Stockholders*, 159 COM. & FIN. CHRON. 889 (1944).

20. Carl Shoup, *Three Plans for Post-War Taxation*, 34 AM. ECON. REV. 757, 757 (1944).

21. BEARDSLEY RUML & H. CHR. SONNE, FISCAL AND MONETARY POLICY: A MEMORANDUM PREPARED AT THE REQUEST OF THE BUSINESS COMMITTEE OF THE NATIONAL PLANNING ASSOCIATION (1944); *Budget of \$18 Billion, Abolition of Corporate Income Tax Urged as Post-War U.S. Policy*, WALL ST. J., July 24, 1944, at 5; *The New Argument*, TIME, Aug. 7, 1944, at 76.

22. Harley L. Lutz, *A Postwar Tax Program*, 29 BULL. NAT’L TAX ASS’N 260, 262 (1944) (proposing a repeal of the corporate income tax in favor of a federal sales tax).

23. RUML & SONNE, *supra* note 21, at 9. In a footnote to a table in the appendix, the authors contemplate a sixteen percent rate on the undistributed-profits tax. *Id.* at 39.

Deal.²⁴ In elaborating, Ruml and Sonne emphasized that in addition to distorting investment decisions, the corporate income tax imposed inequitable double taxation on corporate income. This was particularly troublesome for small stockholders because “the earnings are first taxed in the hands of the corporation at full, identical rates for all stockholders, and then that portion of the earnings distributed as dividends to stockholders is taxed again, but only in the latter case at progressive rates.”²⁵

A second reform proposal, dubbed the “Twin Cities Plan” because of its backing by a group of twenty-two high-ranking businessmen from Minneapolis and St. Paul, Minnesota, was almost the polar opposite of the Ruml–Sonne proposal.²⁶ Rather than propose to supplant the corporate income tax, the Twin Cities group supported continuing the high corporate rates at 1942 levels, while cutting the excess profits tax and other wartime taxes and sharply reducing individual surtax and capital-gains rates.²⁷ The thesis of the group’s proposal was “that relatively heavy corporate income tax rates are not as harmful to the private enterprise system as are heavy individual income tax rates, for the reason that the latter shut off at the source all possibility of venturing of capital by individuals.”²⁸ After rejecting a variety of integration options as unwieldy or inequitable, the Twin Cities group proposed to relieve double taxation by excluding forty percent of dividends from the individual income tax at the shareholder level. This exclusion, described as “arbitrary” by contemporary observers,²⁹ was justified by the group as ensuring that “in no case should the part of the burden paid by the stockholder exceed fifty percent of the dividend received,” which the group felt was the magic number required to maintain investment incentives.³⁰

The businessmen who proposed retaining high corporate tax rates were not perceived as charitable. Indeed, Carl Shoup suggested that the Twin Cities proposal “bears heavily the stamp of special interest. It is extraordinarily favorable to the sector of the economy that the members of the Twin Cities group represent.”³¹ Shoup characterized the proposal as more favorable to high-income-bracket executives of moderately sized corporations who had invested most of their personal wealth in the corporation. For such businessmen, the lower individual rates and dividend exclusion may have made up for the high

24. *Id.* at 9. Contemporary commentators seemed to assume that it would be similar to the 1936 undistributed-profits tax and would therefore be automatic rather than applied only in the event the government established fraud or tax avoidance. See Shoup, *supra* note 20, at 764.

25. RUML & SONNE, *supra* note 21, at 11.

26. TWIN CITIES RESEARCH BUREAU, THE TWIN CITIES PLAN: POSTWAR TAXES: A REALISTIC APPROACH TO THE PROBLEM OF FEDERAL TAXATION (1944) [hereinafter TWIN CITIES].

27. *Id.* at 12–13.

28. *Id.*

29. John V. Van Sickle, *Reform of the Federal Taxes on Personal and Corporate Income*, 34 AM. ECON. REV. 847, 847 (1944).

30. TWIN CITIES, *supra* note 26, at 16.

31. Shoup, *supra* note 20, at 758.

corporate rates. By contrast, Shoup speculated that the executive of a larger corporation with a diversified portfolio might have been more concerned about the corporate rate and less about the rate on individual stockholders.³² Perhaps on that basis, Shoup thought it the least likely of the three proposals to be adopted.³³

The third and final comprehensive tax reform proposal to be released in the summer of 1944 was the Committee for Economic Development's *Postwar Federal Tax Plan for High Employment*.³⁴ Much like the Ruml-Sonne proposal, the Committee for Economic Development saw the need to reduce rather than maintain corporate income tax rates. It proposed to return to the early days of the income tax, with corporate and individual normal rates each set at between sixteen and twenty percent and with dividends effectively exempted from the normal rate.³⁵ That is, shareholders would be credited with the tax paid at the corporate level and this credit would be refundable in the event the tax exceeded the amount that would have been otherwise due.³⁶ According to the Committee, this system, which was similar to the shareholder-credit system then in place in Britain,³⁷ "would be equivalent to a withholding tax, on behalf of the stockholders, on corporate net income paid out in dividends."³⁸

To at least partially address the criticism that the retained-earnings problem would remain for stockholders seeking to avoid subjecting corporate income to high surtax rates,³⁹ the Committee recommended eventually eliminating the capital-gains preference.⁴⁰ The Committee theorized that "the inclusion of these gains in the personal income tax base is the only way by which all corporate earnings—i.e., stockholders' income—can be eventually subjected to the personal income tax."⁴¹ Shoup pointed out that this failed to account for the inequity caused by a delay in taxation, but that it did seek to address the possible conversion of ordinary income from dividends to the lower-rate capital gains from sale of stock.⁴²

32. *See id.* at 766–67.

33. *Id.* at 758.

34. RESEARCH COMM., COMM. FOR ECON. DEV., A POSTWAR FEDERAL TAX PLAN FOR HIGH EMPLOYMENT (1944) [hereinafter POSTWAR FEDERAL TAX PLAN]. *See also* John H. Crider, *Business Body Asks Corporate Tax End as Way to Job Peak*, N.Y. TIMES, Sept. 6, 1944, at 1.

35. POSTWAR FEDERAL TAX PLAN, *supra* note 34, at 27, 30, 34.

36. *Id.* at 30.

37. *See* Rebecca Newman Golub, *The Postwar Tax Structure—A Discussion of Four Leading Plans*, 78 J. ACCT. 292, 294 (1944) (describing the Committee's approach); HAROLD M. GROVES, POSTWAR TAXATION AND ECONOMIC PROGRESS 68 (1946) (describing Great Britain's shareholder-credit system).

38. POSTWAR FEDERAL TAX PLAN, *supra* note 34, at 34.

39. *See Would End Corporate Tax: Ruml of Committee Says Peril Is Amassing Unneeded Funds*, N.Y. TIMES, Sept. 6, 1944, at 15 (suggesting that "one of the difficulties of administering the plan would be to prevent corporations from accumulating unneeded surpluses").

40. POSTWAR FEDERAL TAX PLAN, *supra* note 34, at 31.

41. *Id.* at 32.

42. Shoup, *supra* note 20, at 768.

Other groups and individuals recommended variants of these three primary tax reform proposals during the summer and fall of 1944. The American Taxpayers Association and the Post-War Planning Committee of the Commerce and Industry Association of New York each proposed major tax overhauls, both advocating the repeal or partial relief of double taxation.⁴³ The former organization had been trumpeting the double-tax issue since at least the summer of 1943, proclaiming in its newsletter that “[t]he great inequity in the corporate tax system arises from the double taxation of corporate earnings paid out in dividends.”⁴⁴ The American Institute of Accountants followed with its own recommendations, advising that “[t]he present double taxation of corporate income . . . should be eliminated as soon as revenue needs permit.”⁴⁵ Banker George Barnes noted that “[a]mong the most-discussed proposals with business men, at least, are those for elimination of corporation taxes as a means to encourage business expansion and end the double taxation of the shareholder’s dividends.”⁴⁶ Although he found it unrealistic to expect the complete end to the corporate income tax, he proposed using a corporate franchise tax to lessen reliance on the income tax and a shareholder credit to alleviate double taxation.⁴⁷ As journalist Godfrey Nelson observed in a *New York Times* article, “The nation appears to have become tax-conscious When business men, economists and even leaders of labor organizations come out for the elimination of taxes on the income of corporations, we realize that courageous thinking is being devoted to the subject of taxation.”⁴⁸

The number and intensity of proposals quickly received Congressional attention. By December 1944, the Joint Committee on Internal Revenue Taxation planned to meet with experts in Congress and at the Treasury to discuss postwar tax reform.⁴⁹ Yet the resulting recommendations were only interim measures. In May of 1945, the Joint Committee announced a “five point program” involving increased excess profits tax exemptions and provisions such as accelerated refund provisions for loss carrybacks and amortization deductions, “designed to improve the cash position of business.” This was signed into law later that summer.⁵⁰

43. AM. TAXPAYERS ASS’N, WHY THE 25 PERCENT LIMIT ON FEDERAL TAXES . . . TAX INSURANCE TO GIVE TAXPAYERS A CHANCE 8 (1944); POST-WAR PLANNING COMM., COMMERCE & INDUS. ASS’N OF N.Y., WINNING THE WAR AND THE PEACE: A PROGRAM OF LEGISLATIVE ACTION 18–19 (1944).

44. AM. TAXPAYERS ASS’N, TAX INFORMATION SERIES NO. 42, DOUBLE TAXATION—ITS BLIGHTING EFFECTS 1 (1943).

45. *Postwar Taxation: Recommendations by the Committee on Federal Taxation of the American Institute of Accountants*, 78 J. ACCT. 361, 363 (1944).

46. Barnes, *supra* note 17, at 1.

47. *Id.* at 2.

48. Godfrey N. Nelson, *Tax Planning Now Hailed as Helpful*, N.Y. TIMES, July 30, 1944, at S5.

49. Bryant, *supra* note 18.

50. *Tax Relief Bill Is Sent to Truman*, N.Y. TIMES, July 21, 1945, at 1.

Groups continued to put forward tax reform proposals in the fall of 1945, but to no avail. The Committee on Post-War Tax Policy, a group of prominent economists, lawyers, and businessmen, released a report in the fall of 1945 advocating the adoption of a shareholder credit for the amount of tax paid at the corporate level for dividends paid to the shareholder.⁵¹ Both the National Association of Manufacturers and the U.S. Chamber of Commerce proposed sharp cuts in individual and corporate rates.⁵² As a writer for *Fortune Magazine* observed, though, all “[t]he tax planners are silent on timing.”⁵³ Like the reform proposals that came earlier, each new proposal ended up being placed on the shelf.

B. Corporate Tax Reform Deferred

The corporate tax reform movement stalled in part because the focus turned to repealing the excess profits tax. The excess profits tax had long been opposed by business, but this opposition only grew stronger with the end of the war. Treasury Secretary Fred Vinson had described the tax as “erratic and in many instances . . . inequitable” and “the strongest impediment to reconversion” of the economy after the war.⁵⁴ Nevertheless, as President Truman declared in his message to Congress on September 6, 1945, “[A] total war effort cannot be liquidated overnight.”⁵⁵ War expenditures were likely to continue at a brisk pace in the immediate aftermath, with the total 1946 budget expected to be at least seven times its 1940 size.⁵⁶ Thus, a transitional tax bill, introduced in the House in 1945, proposed to defer repeal of the excess profits tax until 1947 and to immediately cut corporate tax rates. The Ways and Means Committee explained that while it “recognize[d] the desirability of having no excess-profits tax in our peacetime tax structure,” it did not believe that “the complete elimination of the excess profits tax for 1946 was as desirable as the reduction of other corporate taxes which affect all corporations with taxable income.”⁵⁷ According to the Committee report, only 20,000 corporations would be subject to the excess profits tax in 1946, whereas 260,000 corporations would be subject to the corporate income tax.⁵⁸

51. COMM. ON POSTWAR TAX POLICY, A TAX PROGRAM FOR A SOLVENT AMERICA 17 (1945); see also *Congress Is Urged to Cut Taxes 50%*, N.Y. TIMES, Sept. 20, 1945, at 33.

52. C.P. Trussell, *George Forecasts 5 Billion Tax Cut*, N.Y. TIMES, Oct. 18, 1945, at 15.

53. *Taxes After the War*, FORTUNE, Dec. 1944, at 121, 243.

54. *Revenue Act of 1945: Hearings on H.R. 4309 Before the S. Comm. on Finance*, 79th Cong. 27–28 (1945) [hereinafter *Hearings*] (statement of Fred M. Vinson, Secretary of Treasury); see also RANDOLPH E. PAUL, *TAXATION FOR PROSPERITY* 185 (1947) (noting that Vinson believed the excess profits tax was “too erratic a tax engine to turn loose for even one full year of the postwar period”).

55. Special Message to the Congress Presenting a 21-Point Program for the Reconversion Period, 1945 PUB. PAPERS 263, 294 (Sept. 6, 1945).

56. PAUL, *supra* note 54, at 184.

57. H.R. REP. NO. 79-1106, at 9–10 (1945).

58. *Bill Cutting Corporate and Individual Taxes \$5.3 Billion Due for House Passage Today*, WALL ST. J., Oct. 11, 1945, at 5.

The Committee's report in favor of broader corporate tax reform did nothing to deter opposition to the deferral of excess profits tax repeal.⁵⁹ The *New York Times* reported that the delayed repeal was "the most controversial issue" in the bill.⁶⁰ Business groups—including the National Association of State Chambers of Commerce, the U.S. Chamber of Commerce, the National Association of Manufacturers, and the National Retail Dry Goods Association—lined up in favor of immediate repeal of the excess profits tax, even if it came at the cost of higher corporate tax rates.⁶¹ In part, these groups might have been concerned that delayed repeal would be no repeal at all. Texas Senator Tom Connally may have contributed to such fear, characterizing the tax as "permanently sound" and moving to reduce excess profit tax rates rather than repeal the tax altogether.⁶² Congress eventually acceded to such pressure and repealed the excess profits tax effective immediately, deferring action on broader corporate tax reform measures such as double taxation.

This focus on the excess profits tax was certainly not itself a rejection of corporate tax reform, although it effectively served that end. Shoup observed that "[t]he excess profits tax is assumed by all of the plans to be unsuited to a peacetime economy."⁶³ The Committee for Economic Development report and the Twin Cities Plan both explicitly recommended repeal of the excess profits tax.⁶⁴ The Twin Cities Plan noted that "[t]he excess profits tax is a creature of the war, and has no place in a peacetime tax program."⁶⁵ The American Taxpayers Association made that tax its top priority, recommending that the group "[u]rge repeal of the Excess Profits Tax immediately when 'firing' ceases in the present war."⁶⁶ In all the proposals, though, excess profits tax repeal was intended to be only the first step toward major business tax reform. Nevertheless, corporate tax reform appeared to fall off the postwar agenda altogether after the repeal of the excess profits tax.

Several factors likely contributed to the continued deferral of corporate tax reform even after the excess profits tax controversy passed. One was the high priority given to balancing the budget. The 1945 Act had created a budgetary mess: the repeal of the excess profits tax was only one of many provisions that resulted in a significant loss of revenue. The hope appeared to be that all of the

59. See, e.g., William S. White, *Business, Labor Offer Tax Views*, N.Y. TIMES, Oct. 15, 1945, at 3 (describing the continuing opposition of the National Association of State Chambers of Commerce and others to the bill).

60. C.P. Trussell, *Profits-Tax Clash Faces Conferees*, N.Y. TIMES, Oct. 26, 1945, at 1.

61. White, *supra* note 59; *Hearings, supra* note 54, at 171 (statement of Ellsworth C. Alvord, Chairman, Committee on Federal Finance, Chamber of Commerce of the United States); *id.* at 202 (statement of H.E. Humphreys Jr., Chairman, Finance Committee, United States Rubber Co., and Chairman, Taxation Committee, National Association of Manufacturers); *id.* at 206 (statement of Jay Iglauer, Chairman, Taxation Committee, National Retail Dry Goods Association).

62. PAUL, *supra* note 54, at 192.

63. Shoup, *supra* note 20, at 762.

64. See POSTWAR FEDERAL TAX PLAN, *supra* note 34, at 34.

65. TWIN CITIES, *supra* note 26, at 13.

66. AM. TAXPAYERS ASS'N, *supra* note 44, at 3.

tax cuts would revive the economy and increase profits and taxable income overall. Randolph Paul called this “a revival of nostalgic enthusiasm for the Andrew Mellon economics of the twenties, with member after member recalling those glorious days of normalcy when taxes were reduced and the budget was balanced.”⁶⁷ It soon became readily apparent, though, that actually balancing the budget was an unrealistic goal.⁶⁸

The budget difficulties were often cited as a justification for deferring corporate tax reform. In 1945, House Ways and Means Chairman Robert Doughton warned that “[t]here is nothing to justify the hope now that there will be further corporation tax cuts” until there was “a balanced budget or a near-balanced budget.”⁶⁹ When asked about double taxation, Doughton responded, “Oh, yes, that’s likely to come up. That’s an old subject and it’s likely to be an old one after some one else becomes chairman of this committee.”⁷⁰

The National Association of Manufacturers actually seemed to agree with Doughton’s assessment. One columnist reported that

[i]t has been the considered conclusion of the N.A.M. that the most pressing need in tax revision is not a general reduction in the corporate tax structure. This may seem a strange conclusion from a group the members of which pay a large proportion of corporate taxes. But the facts justify this position. . . . The immediate demand of the N.A.M. is a balanced budget, with appropriate provision for debt retirement.⁷¹

In fact, when the National Association of Manufacturers outlined a tax reform plan in testimony before the Ways and Means Committee in 1947, it focused specifically on individual- and capital-gains rate cuts and recommended that corporate tax reform, including double-tax relief, “be deferred until federal fiscal needs are stabilized at lower peacetime levels.”⁷²

Excess profits tax repeal also permitted politicians to call for a shift from business-tax relief to individual-tax relief. As Randolph Paul reported, “Ever since the tax reduction given so generously to corporations by the 1945 act, strong pressure had been applied to Congress for a compensating reduction to individual income taxpayers.”⁷³ Thus, when several key members of the Ways and Means Committee were asked in late 1946 whether corporate tax relief was on the agenda, they responded, “Not before 1948.”⁷⁴ Their explanation was that “[c]orporations ‘fared pretty well last year Now it’s time for individual taxpayers to get a break.’”⁷⁵ House Ways and Means Committee Chairman Harold Knutson even suggested that Republicans had reached an

67. PAUL, *supra* note 54, at 194.

68. See Godfrey N. Nelson, *Changes in Taxes Past and to Come*, N.Y. TIMES, Jan. 3, 1950, at 57.

69. John H. Crider, *Doubts Tax Cuts Till Budget Is Met*, N.Y. TIMES, Dec. 20, 1945, at 16.

70. *Id.*

71. Raymond Moley, *The N.A.M. and the Budget*, L.A. TIMES, Dec. 12, 1946, at A4.

72. *NAM Urges \$6 Billion Reduction in Individual Income Taxes; Would Graduate Rates from 12% to 50%*, WALL ST. J., July 12, 1947, at 1.

73. RANDOLPH E. PAUL, *TAXATION IN THE UNITED STATES* 454 (1954).

74. *Tax Report*, WALL ST. J., Nov. 27, 1946, at 1.

75. *Id.*

“understanding” with President Truman in 1945 that support for business tax cuts at that time would be followed by more-general, individual-income-tax relief in the following year or two.⁷⁶

Another contributing factor to the failure to fulfill the promise of corporate tax reform was that business groups could not themselves agree on a course of action. As the *Wall Street Journal* reported,

Business itself is far from agreed as to what it wants and a large number of conflicting plans have been submitted to the Treasury and to Congress Double taxation is the biggest snag in evolving a definite tax policy measure Sixty relief plans to cure this one evil are evidence of the widely divergent views on how to reduce double taxation.⁷⁷

In December 1946, a Treasury study of the postwar corporate tax structure summarized the nature of the problem:

There are major differences of opinion as to postwar taxation of corporate income. Many desire radical changes in the present system. Others wish no basic revision. Not all those who favor ultimate elimination of the corporate tax would recommend this step immediately. Moreover, many who approve the present type of corporate tax favor lower rates and other modifications.⁷⁸

These problems were only compounded by what one observer described as “huge gaps in our knowledge of how the economy operates.”⁷⁹ Richard Goode, the author of the 1946 Treasury study, told a group of executives and tax professionals that “[c]orporate tax reform is complicated by uncertainty as to the real effects of the present system.”⁸⁰ Amid such uncertainty, no action was often preferable to radical change, especially for interest groups attempting to assess whose ox was being gored under each plan.

Perhaps the most compelling explanation for the decline in the fervor of corporate tax reform advocates is that the circumstances that originally gave rise to the reform movement in 1944 had changed. By 1946, the predictions of postwar economic ruin had been disproven. Businesses had already started to transition to the postwar economy, and the repeal of the excess profits tax had increased the percentage of retained earnings available for reinvestment. Of the \$3.5 billion in new capital raised in the market in 1946, \$1.5 billion came from the issuance of new common or preferred stock, which was considered a relatively normal debt-to-equity ratio.⁸¹ By contrast, the net acquisition of corporate stocks by individuals, which had been as high as \$4.7 billion in 1929, had stood at only \$519 million in 1944 when the flurry of proposals for the

76. C.P. Trussell, *Tax Commitment with GOP in 1945 Is Laid to Truman*, N.Y. TIMES, June 10, 1947, at 1.

77. *Tax Report*, WALL ST. J., Jan. 30, 1946, at 1.

78. See GOODE, *supra* note 16, at 1.

79. C. Lowell Harriss, Book Review, 30 REV. ECON. & STAT. 72, 72 (1948) (reviewing RICHARD B. GOODE, *THE POSTWAR CORPORATION TAX STRUCTURE* (1946)).

80. *Tax Reform Seen as Complex Task*, N.Y. TIMES, Dec. 7, 1946, at 29.

81. Editorial, *Capital, and Mr. Harriman*, N.Y. TIMES, Jan. 21, 1948, at 24.

integration of the corporate and individual income taxes had begun.⁸² Thus, with capital needs a bit less pressing, corporate managers could focus their attention on more-personally important, entity-level concerns and leave shareholders to fight the double-taxation fight on their own. Though the report of a special House Ways and Means tax-study committee revived the issue in the fall of 1947,⁸³ no action was taken.

C. A Brief Revival of Reform Efforts

Starting in 1948, the focus switched from reform to fighting against an increased corporate tax burden. In his 1948 budget message to Congress, President Harry Truman preached revenue neutrality in budgeting, reminding Congress that “[t]he expenditures of the Federal Government are still inescapably dominated by the war and its aftermath.”⁸⁴ Truman had vetoed an across-the-board income-tax cut in 1947—only the second presidential veto of a tax bill in American history.⁸⁵ To pay now for a decrease in individual income taxes, he proposed a “corresponding increase in corporation taxes.”⁸⁶ Though Truman had always been focused on the budget, his proposal to reject the status quo in favor of shifting taxes from individuals to businesses was new.⁸⁷ Truman’s proposals were reported to be “harmful and short-sighted,” “obviously designed for purely political appeal.”⁸⁸

Truman’s specific proposal for increased corporate taxes—the revival of a modified form of the excess profits tax—was even more galling for business. The major modifications—lowering the excess profits tax rate slightly from its World War II peak of 85.5% to 75% and increasing the exemption for the protection of small businesses—did little to mollify the almost 22,000 larger corporations that would be have been subject to the new levy.⁸⁹ The *Wall Street Journal* called it “tax foolishness” and Congressional leaders on both sides of

82. John A. James & Richard Sylla, *Personal Saving, by Major Components of Assets and Liabilities—Nonagricultural Individuals and Nonprofit Institutions: 1897–1949*, in HISTORICAL STATISTICS OF THE UNITED STATES: MILLENNIAL EDITION 3-304, 3-305 tbl.Ce42-68 (Susan B. Carter et al. eds., 2006), available at <http://hsus.cambridge.org/HSUSWeb/toc/tree TablePath.do?id=Ce42-68>.

83. H.R. DOC. NO. 80-523, at 14–15 (1947); see also W.C. Bryant, *Advocates of Reforms in Corporate Levies Urge End to Double Taxation of Dividends*, WALL ST. J., Oct. 15, 1947, at 4.

84. *The Text of the Message by President Truman Transmitting His \$39,669,000,000 Budget*, N.Y. TIMES, Jan. 13, 1948, at 16 (hereinafter *Text*).

85. See John D. Morris, *Corporate Tax Rise Studied by Truman as Compromise*, N.Y. TIMES, Jan. 7, 1948, at 1.

86. *Text*, supra note 84, at 16.

87. PAUL, supra note 73, at 472–73. The first was President Roosevelt’s veto in 1943. *Id.* at 473.

88. Godfrey N. Nelson, *President’s Plan Only Shifts Taxes*, N.Y. TIMES, Jan. 11, 1948, at F1.

89. See PAUL, supra note 73, at 480–81.

the aisle denounced it.⁹⁰ Despite the prominent support of people like Bernard Baruch,⁹¹ revival of the excess profits tax never gained much traction.

Although opponents managed to resist Truman's excess profits tax in early 1948, a corporate tax increase—possibly in the form of an excess profits tax—remained a threat. The budget situation deteriorated during 1948, and forecasts of surplus proved inaccurate. Truman was adamantly opposed to any form of deficit financing, and experts predicted a tax increase given the reality that defense spending and foreign aid could still not be easily cut.⁹² This reportedly gave businessmen “the jitters,” with many feeling like they had targets on their chests.⁹³ According to the *Wall Street Journal*, “Odds favor[ed] an increase in corporate taxes next year [in 1949], probably in the form of an excess-profits tax.”⁹⁴

Others were less confident about an excess profits tax but did agree that a corporate tax increase was likely. J.S. Seidman, one of the leading tax authorities of the day, explained that

[t]his . . . is the popular approach and politically appealing. It will also have the justification from the fact that in comparison with war taxes, the subsequent removal of the excess profits tax has cut the corporate tax rate from 95 per cent to 38 per cent whereas the top rate on individuals has been reduced from 94 per cent to only 85 per cent.⁹⁵

As Seidman suggested, congressional sentiment for some kind of increase in the corporate tax was growing, with the only question being the form such an increase would take.⁹⁶ The best compromise business interests and legislators could manage was an ultimately unsuccessful proposal to forego a rate increase in favor of accelerating corporate tax payments by about six months in 1950.⁹⁷

An economic downturn from 1948 through 1949 not only helped convince Truman to take tax increases off the table,⁹⁸ but also revived concerns about

90. *Dingell Offers Excess Profits Tax to Distribute \$40 to Each Taxpayer, but Congress Leaders Are Opposed*, WALL ST. J., Jan. 15, 1948, at 2; Editorial, *Tax Foolishness*, WALL ST. J., Jan. 16, 1948, at 4.

91. *Baruch Asks Congress Not to Lower Taxes for Two Years; Wants Excess Profits Levy*, WALL ST. J., Jan. 20, 1948, at 3.

92. H. Walton Cloke, *Truman Due to Ask Higher Taxes, but May Face Fight in Congress*, N.Y. TIMES, Jan. 3, 1949, at 41.

93. Harold Walsh, *Leading Economist Holds that Tax Cuts Rather than Increases Should Be Considered*, L.A. TIMES, Jan. 12, 1949, at 11; see also *Economic Council Says Most New Taxes Should Come from Business; Avoids Excess Profits Levy Stand*, WALL ST. J., Jan. 8, 1949, at 2.

94. *Tax Report*, WALL ST. J., Nov. 10, 1948, at 1.

95. Harold Walsh, *March of Finance: Tax Authority Sees Moderate Shifting of Burden from Individuals to Corporations*, L.A. TIMES, Sept. 8, 1948, at 21.

96. *Sentiment in Congress for Tax Rise Grows but Lawmakers Don't Agree on the Kind of Increase They Favor*, WALL ST. J., Dec. 13, 1948, at 2.

97. See Albert Clark, *Fiscal Finagling: Democrats' New Idea: Speed Corporate Tax Take to Offset Deficit*, WALL ST. J., May 17, 1949, at 1. But see *GOP Attacks Bill to Speed Corporate Tax Take; Says It Will Cut Business by 15%*, WALL ST. J., May 18, 1949, at 3; Harold Walsh, *Undesirable Features of Proposal to Speed up Corporate Tax Payments Outweigh Good*, L.A. TIMES, June 12, 1949, at 35.

98. PAUL, *supra* note 73, at 514.

equity capital.⁹⁹ Although naysayers contended that savings were adequate,¹⁰⁰ those concerned about equity investment cited the larger equity needs of the postwar economy. The head of the Business Structure Division of the U.S. Department of Commerce reflected that

huge capital requirements for expansion of plant and equipment facilities to take care of postwar markets and technological advances . . . inevitably led to a growing pressure of demand upon the available sources of funds for business investment—focusing attention for the first time in many years on possible deficiencies in the supply of capital, particularly equity capital.¹⁰¹

The president of the New York Stock Exchange likewise warned that “the market for equity securities is so anemic that it can absorb only a limited volume of new shares.”¹⁰²

The double-tax system was one obvious target of blame for this shortfall in stock investing. The Chairman of General Electric Company complained that “the present double taxation of dividends is not only inequitable . . . but is a serious deterrent to investment in equity securities.”¹⁰³ Editors of the *Wall Street Journal* concurred: “[D]ouble taxation of corporate profits paid out in dividends not only reduces the amount of capital available for investment in productive enterprise but goes a long way towards destroying the incentive to venture that has contributed so materially to this country’s expansion.”¹⁰⁴

This backlash reopened the door for corporate tax reform proposals. If double taxation was thought to hinder corporate financing, business and its supporters wanted it removed. Thus, Republican Congressman John Byrnes of Wisconsin introduced a bill proposing that shareholders be granted a tax credit equal to as much as twenty percent of dividends they had received, up to a maximum of \$2000. Noting “‘serious implications’ in the current shift from equity financing to debt financing,” Byrnes urged that “means . . . be found to attract individuals in the lower income brackets into corporate financing.”¹⁰⁵ Similar proposals came from the other side of the aisle, as Democratic Representative Walter Lynch of New York offered a measure that included a ten-percent shareholder credit for dividends.¹⁰⁶ Private groups such as the

99. See, e.g., Stanley L. Miller, *The Equity Capital Problem*, 26 HARV. BUS. REV. 671, 672 (1948).

100. See, e.g., Randolph E. Paul, *Cold War Taxation Policy*, 4 TAX L. REV. 35, 42 (1948); cf. Paul L. Howell, *The Effects of Federal Income Taxation on the Form of External Financing by Business*, 4 J. FIN. 208, 221 (1949) (concluding that although tax rates did affect the incentives to invest, the equity crunch had not yet reached a crisis of national proportions).

101. Irwin Friend, *Business Financing in the Postwar Period*, SURV. CURRENT BUS., Mar. 1948, at 10.

102. *Schram Sees Threat of Nationalization in Federal Tax Policies*, WALL ST. J., Mar. 19, 1948, quoted in PAUL, *supra* note 100, at 41.

103. *GE Chairman Urges Congress to Stimulate Investment in Common Stocks by Easing Business Tax Laws*, WALL ST. J., Dec. 15, 1949, at 2.

104. Editorial, *Should be Tax “Musts,”* WALL ST. J., Dec. 12, 1949, at 4.

105. *Dividend Credits in Taxes Proposed*, N.Y. TIMES, Mar. 8, 1949, at 37.

106. *House Democrat Asks Cuts in Excise, Capital Gains, Dividend Taxes*, WALL ST. J., Oct. 14, 1949, at 3.

Brookings Institution rereleased integration plans from the World War II and postwar era.¹⁰⁷

Although these proposals expressed concern about a lack of money coming into corporations, others were concerned about the lack of money leaving corporations in the form of dividends. One member of Congress called for a study of the practice of retaining corporate earnings as a means to avoid double taxation, suggesting that corporations “should be required to pay out in dividends at least two-thirds of their earnings.”¹⁰⁸ The *Los Angeles Times* observed that “[t]he ghost of the undistributed profits tax walks again in Washington,” and quoted J.S. Seidman as saying that “serious consideration is being given to some form of undistributed profits tax on corporations.”¹⁰⁹

This brief revival of the corporate tax reform movement began to backslide around the time of the outbreak of the Korean War. Even before North Korea crossed the 38th parallel to invade South Korea in June 1950, congressional leaders and administration representatives had hinted that a corporate tax increase could replace wartime excise taxes.¹¹⁰ The House Ways and Means Committee began to consider a pre–Korean War return to the excess profits tax, which would, in the opinion of the sponsor of the bill proposing the measure, “tax the few corporations with postwar profits in many cases even above the peak wartime earnings.”¹¹¹ According to the *New York Times*, “[I]f the budget deficit is not to be widened further, rather than narrowed, the taxes will come out of the hide of the country’s corporations, in one form or another.”¹¹²

With the onset of hostilities in Korea, business was once again diverted from integration efforts to an ultimately unsuccessful fight against an excess profits tax. Business lobbyists turned out in full force at House hearings on such a tax.¹¹³ Ralph Button of the National Retail Dry Goods Association lamented that “[a]n equitable excess-profits tax law cannot be written.”¹¹⁴ A newly formed group comprised of officers from more than 100 leading corporations—the

107. See LEWIS H. KIMMEL, BROOKINGS INST., *POSTWAR TAX POLICY AND BUSINESS EXPANSION* 1 (1943); *Brookings Urges Business Tax Cut*, N.Y. TIMES, May 29, 1950, at 8.

108. *Patman Demands Study of Firms’ Undistributed Profits in Last 3 Years*, WALL ST. J., Mar. 26, 1949, at 1.

109. *Undistributed Profits Tax Under Serious Study*, L.A. TIMES, Nov. 4, 1949, at 25.

110. John D. Morris, *Snyder Asks Limit on Excise Tax Cuts to 6 Major Items*, N.Y. TIMES, Feb. 4, 1950, at 1; *Motto: Hit the Corporations: House Group Seeks More Federal Revenue, Considers Hiking Corporate Tax to 40%, Making Firms Pay Faster*, WALL ST. J., May 22, 1950, at 3; William S. White, *Lucas Hints Rise in Corporate Tax*, N.Y. TIMES, Dec. 31, 1949, at 6.

111. *Excess-Profit Tax Proposed in House*, N.Y. TIMES, Apr. 25, 1950, at 21 (quoting Representative Herman P. Eberharter, D-Pa., who was a member of the Ways and Means Committee).

112. *Corporations Do Not Vote*, N.Y. TIMES, May 31, 1950, at 25.

113. John D. Morris, *Business Men Fight Excess-Profit Tax; Substitutes Urged*, N.Y. TIMES, Nov. 17, 1950, at 1.

114. *Excess Profits Tax on Corporations, 1950: Hearings Before the H. Comm. on Ways and Means*, 81st Cong. 306 (1950) [hereinafter *Excess Profits Hearings*] (statement of Ralph W. Button, National Retail Dry Goods Association).

Business Committee on Emergency Corporate Taxation—was particularly strident in opposing an excess profits tax. The group's leader, Beardsley Ruml, criticized excess profits taxation as “an evil brew of inequity, exception, exemption and privilege.”¹¹⁵ Another representative remarked that he “would greatly favor a straight increase in the present corporate tax at whatever level necessary to raise the revenue” rather than a revival of the profits levy.¹¹⁶

Many of those introducing corporate tax reform proposals between 1944 and 1946 again proposed corporate tax increases in 1950 as an alternative to the excess profits tax. The National Association of Manufacturers proposed what was described as a “special ‘defense tax,’ based on percentages of the regular corporate tax,” as a substitute for an excess profits tax.¹¹⁷ According to *The Nation*, the top rate of thirty percent was designed so that “corporations could be sure of retaining 51.3 per cent of their gross profits.”¹¹⁸ The Chamber of Commerce of the State of New York preferred a graduated retail sales tax with higher rates on luxuries than necessities, but noted that, “should Congress choose not to enact such a defense, graduated retail sales tax, then there should be further and temporary increases in the corporate tax rate up toward a top limit of 50 per cent . . . in preference to any so-called excess profits tax.”¹¹⁹ The Committee on Economic Development also introduced its own plan, which included a temporary “defense profits tax” consisting of a flat fifteen percent tax on corporate profits on top of a somewhat reduced normal corporate tax rate of thirty-eight percent.¹²⁰ No group, however, included double-tax relief in its proposals. As Charlie Merrill of the Merrill Lynch brokerage house lamented, “There is no organized pressure group representing investors Yet there are more than six million investors who could make their voices heard from coast to coast.”¹²¹

115. John D. Morris, *House Votes, 378–20, to Place a 75% Tax on Excess Profits*, N.Y. TIMES, Dec. 6, 1950, at 1.

116. *Excess Profits Hearings*, *supra* note 114, at 131 (statements of Robert C. Tait & Leon Henderson, representing the Business Committee on Emergency Corporate Taxation); *see also Business Group Formed to Urge Alternative to Excess Profits Tax*, WALL ST. J., Nov. 10, 1950, at 8.

117. Editorial, *NAM's Tax Proposals*, WALL ST. J., Oct. 25, 1950, at 8; *Excess Profits Hearings*, *supra* note 114, at 422 (statement of Charles Sligh, Chairman of the Taxation Committee of the National Association of Manufacturers).

118. Keith Hutchison, *Everybody's Business: The N.A.M.'s Tax Plan*, 171 NATION 461, 461 (1950).

119. *Sales Tax Urged for Profits Levy*, N.Y. TIMES, Oct. 30, 1950, at 34. A sales tax remained a favorite for some businesses. *See Business Men Back Federal Sales Tax*, N.Y. TIMES, Apr. 23, 1951, at 33.

120. Felix Belair Jr., *Business Men Ask 'Defense' Imposts*, N.Y. TIMES, Nov. 15, 1950, at 20.

121. *Appeal to Main Street*, TIME, Feb. 20, 1950, at 82, 86.

III

1954 AND BEYOND

A. Why Dividend Tax Relief Now?

1. Continued Concerns over Declining Equity Investment

The Korean War had temporarily derailed integration plans, but concerns about declining equity investment continued to simmer. In 1951, the *New York Times* reported that “[o]nly about 6 per cent of our huge national income is now finding its way into [business enterprise],” compared with up to eighteen percent under normal conditions.¹²² According to estimates prepared by the Securities and Exchange Commission, a mere eight percent of aggregate liquid individual savings went toward the net purchase of equity securities such as common stock.¹²³ Moreover, not only did the percentage of new investments drop, but so did the total number of shareholders—from approximately ten million in 1930 to six million by 1952.¹²⁴ By 1953, the volume of trading on the New York Stock Exchange had reached a low point of fewer than one million shares, and G. Keith Funston, the president of the Exchange, subsequently complained that “[n]ew enterprises seeking to create new wealth and productivity are unable to attract the equity capital we need.”¹²⁵

Instead of purchasing stock, many wealthy individuals sought tax-preferred investment vehicles such as life insurance or municipal bonds. For the former, the investment increment in the policy was exempt from tax. For the latter, the interest paid out by the bonds was tax-exempt. Although both paid lower returns than conventional investments, high individual tax rates made the tax exemption quite valuable. In the case of life insurance, a Harvard Business School study on the effects of taxation on individual investment found that approximately one-half of individuals who reported that tax concerns motivated their decisions to buy insurance and annuities were either high-income- or high-net-wealth individuals.¹²⁶ An even more significant example was the case of individual holdings of state and local securities, which almost doubled from \$7

122. Godfrey N. Nelson, *Tax Course Is Held Road to Socialism*, N.Y. TIMES, Sept. 23, 1951, at 137.

123. J. Kirk Eads, *The Tax Man Rings TWICE*, 41 NATION'S BUS. 38, 81–82 (1953).

124. JONATHAN BARRON BASKIN & PAUL J. MIRANTI JR., A HISTORY OF CORPORATE FINANCE 232 (1997); JOHN MICKLETHWAIT & ADRIAN WOOLDRIDGE, THE COMPANY: A SHORT HISTORY OF A REVOLUTIONARY IDEA 117 (2003).

125. 2 JERRY W. MARKHAM, A FINANCIAL HISTORY OF THE UNITED STATES 293 (2002); G. Keith Funston, Double Taxation of Dividends, Before the House Ways and Means Committee (July 16, 1953), in 19 VITAL SPEECHES OF THE DAY 722, 723 (1953).

126. See J. KEITH BUTTERS ET AL., EFFECTS OF TAXATION: INVESTMENTS BY INDIVIDUALS 317, tbl.XIII (reporting that, of investors who had increased holdings due to income or estate tax considerations, 51% had incomes of \$50,000 or greater and 43% had net wealth of \$500,000 or greater).

billion between 1944 and 1947 to \$12 billion by 1953.¹²⁷ The ownership of such tax-exempt municipal securities was highly concentrated in higher-income individuals.¹²⁸ Northwestern University law professor William Cary, who later headed the Securities and Exchange Commission under President Kennedy, observed that, at least in part, “the credit for dividends can be described as an inducement to counteract the existing tax exemption of insurance and municipal bonds.”¹²⁹

This declining appetite for stock investment was likely worsened by the postwar recession that commenced in the fall of 1953. Although brief and mild in comparison to the other economic downturns during the 1950s, the recession exacted a nontrivial price in terms of business failures, a decline in stock prices, and decreases in residential construction and orders for durable goods.¹³⁰ Gross national product dropped as much as three percent and unemployment rose from 2.5% to 6.1%.¹³¹ Most notably for purposes of the taxation of corporate dividends, the net acquisition of corporate stocks dropped sharply during and immediately following the war, from a high of \$1.6 billion in 1951 to \$1 billion in 1952, \$700 million in 1953, and a post–World War II low of \$300 million by 1954.¹³²

There was a determined push to broaden the base of stock ownership to compensate for the departure of wealthier individuals. As Marshall Ketchum of the University of Chicago had observed, the problem was that “[t]he upper income classes no longer have such large percentages of total disposable incomes with which to purchase stocks,” while “[t]he lower-income classes have increased incomes, increased disposable incomes, and increased savings, but they are unacquainted with common stocks and with the manner of acquiring them.”¹³³ In response, the New York Stock Exchange initiated an advertising campaign, entitled “Own Your Share of American Business,” complete with performances from the popular puppet show *Kukla, Fran, and Ollie*, to promote

127. GEORGE E. LENT, THE OWNERSHIP OF TAX-EXEMPT SECURITIES, 1913–1953, at 14 (Nat’l Bureau of Econ. Research, Occasional Paper No. 47, 1955). Federal tax-exempt securities, by contrast, were increasingly concentrated in the hands of institutional investors. *Id.* at 13, 82.

128. *Id.* at 116.

129. William L. Cary, *Pressure Groups and the Revenue Code: A Requiem in Honor of the Departing Uniformity of the Tax Laws*, 68 HARV. L. REV. 745, 765 (1955).

130. JOHN W. SLOAN, EISENHOWER AND THE MANAGEMENT OF PROSPERITY 134 (1991) (describing the Burns report at the September 24, 1953, cabinet meeting, which included a “drop in the stock market”); HAROLD G. VATTER, THE U.S. ECONOMY IN THE 1950S: AN ECONOMIC HISTORY 93 (1963).

131. RAYMOND J. SAULNIER, CONSTRUCTIVE YEARS: THE U.S. ECONOMY UNDER EISENHOWER 71 (1991); see also A.E. HOLMANS, UNITED STATES FISCAL POLICY: 1945–1959, at 211–12 (1961) (providing tables of economic indicators about the 1953 recession).

132. Richard Sutch, *Derivation of Personal Saving: 1946–2002*, in HISTORICAL STATISTICS OF THE UNITED STATES: MILLENNIAL EDITION at 3-310 tbl.Ce91-121 (Susan B. Carter et al. eds., 2006), available at <http://hsus.cambridge.org/HSUSWeb/toc/treeTablePath.do?id=Ce91-121>.

133. M.D. Ketchum, *The Effects of Federal Income Taxation on the Form of External Financing by Business: Discussion*, 4 J. FIN. 222, 224 (1949).

stock investment among the middle class.¹³⁴ The banks followed suit with the “Quimby Plan,” which facilitated individual stock ownership by allowing customers to purchase shares directly through their local banks.¹³⁵ At the same time, retail brokerage houses such as Merrill Lynch started training their brokers on how to serve smaller investors.¹³⁶ None of this, however, appreciably increased the amount of available capital.

The drop in stock investing forced businesses to seek other forms of financing. G. Keith Funston, President of the New York Stock Exchange, noted that companies were increasingly resorting to debt financing because of the dearth of equity capital:

For the seven years, 1946–1952, the long-term debt financing and bank loans of corporate industry totaled \$40 billion, more than three and a half times the \$11 billion obtained from new stock issues. Government officials, economists and business leaders alike have warned of the dangers inherent in this trend.¹³⁷

This policy soon became difficult, though, because inflation concerns had led the Federal Reserve Board, with the Eisenhower Administration’s blessing and support, to pursue a restrictive credit policy complete with rising interest rates.¹³⁸ When companies found debt too expensive, they tried to reduce dividends and rely more on retained earnings, which reportedly further depressed stock prices. J. Kirk Eads of the U.S. Chamber of Commerce wrote in the Chamber’s in-house publication that

[b]efore World War II—in 1939—corporations as a group paid out about 76 per cent of their after-tax earnings to their stockholders. Since the war, this percentage has fallen as low as 35 per cent. This drop in the percentage, and the corresponding effect on the attractiveness of investment in corporate stocks, is in large part a result of the double taxation problem, since corporations find outside capital harder to obtain and must depend more on retained earnings for their growth.¹³⁹

As profits declined during the recession, though, even the retained-earnings strategy became infeasible.

Like Eads, many observers attributed at least part of the blame for the lack of equity capital to the continued high income-tax rates, particularly on dividend income. As early as a symposium of the Tax Institute held in 1950, William Casey remarked that the effect of double taxation and the growing availability of more favorably taxed investments such as municipal bonds and real estate “have clearly reflected themselves in the fact that corporate stock has consistently sold at a lower ratio to earnings, and is still doing so in the

134. 2 MARKHAM, *supra* note 125, at 292.

135. *Id.*

136. CHARLES R. GEISST, *WALL STREET: A HISTORY* 281 (1997).

137. Funston, *supra* note 125, at 724.

138. A.E. Holmans, *The Eisenhower Administration and the Recession, 1953–5*, in 10 OXFORD ECON. PAPERS 34, 35 (1958); SAULNIER, *supra* note 131, at 66–67. There was an attempt to ease credit policy to address this problem. HOLMANS, *supra* note 131, at 224–25.

139. Eads, *supra* note 123, at 39.

current bull market, than ever before.”¹⁴⁰ The New York Stock Exchange’s Funston told the House Ways and Means Committee in July of 1953 that “[t]axation of capital gains and double taxation of dividends are Federally-erected twin dams holding back the free flow of life-giving venture capital into American industry.”¹⁴¹ Although this attempt to pin an equity crisis on double taxation had its dissenters,¹⁴² others acknowledged that the tax provisions, in combination with an economic downturn, might have had some effect.¹⁴³ In any event, the notion that the taxation of dividends was hurting equity investment had clearly become a mainstream view. Even the *Saturday Evening Post* observed that “double taxation can only retard the flow of risk capital into new ventures.”¹⁴⁴

2. Dividend-Tax Relief as a Response to the Equity Crisis

Dwight D. Eisenhower, the first Republican president in twenty years, initially appeared unlikely to respond to concerns about declining equity investment. In fact, Republican congressmen were upset because his positions on taxation appeared to resemble those of President Truman prior to the Korean War.¹⁴⁵ Like Truman, Eisenhower insisted that a balanced budget take precedence over cutting taxes.¹⁴⁶ With a deficit of \$9.4 billion for fiscal year 1953 expected to grow to as high as \$11 billion in 1954,¹⁴⁷ Eisenhower needed to raise revenues. Though he did not explicitly propose increasing the corporate tax rate and reenacting an excess profits tax, as Truman had, he effectively did the same thing by asking Congress in May of 1953 to extend the excess profits tax six months past its expiration date and to rescind a scheduled reduction in the corporate tax rate from fifty-two to forty-seven percent.¹⁴⁸

Unlike with Truman, Eisenhower’s concerns were at least publicly acknowledged by business, perhaps due to longer-term confidence about his tax

140. William J. Casey, *Double Taxation of Dividends*, in TAXATION AND BUSINESS CONCENTRATION 207, 211 (Tax Inst. ed. 1950).

141. Funston, *supra* note 125, at 723.

142. See Editorial, *Taxes and Investment*, 91 AMERICA 493 (1954).

143. Eugene Neil Feingold, *The Internal Revenue Act of 1954: Policy and Politics* 192 (Sept. 1960) (unpublished Ph.D. dissertation, Princeton University) (on file with Law & Contemporary Problems).

144. Raymond F. Rice, Editorial, *The Double Tax on Dividends Deters Venture Investment—Also It’s Unfair*, SATURDAY EVENING POST, Feb. 13, 1954, at 12.

145. See AARON L. FRIEDBERG, IN THE SHADOW OF THE GARRISON STATE: AMERICA’S ANTI-STATISM AND ITS COLD WAR GRAND STRATEGY 131–32 (2000).

146. GARY W. REICHARD, THE REAFFIRMATION OF REPUBLICANISM: EISENHOWER AND THE EIGHTY-THIRD CONGRESS 97 (1975). Eisenhower emphasized that “a government, like a family, should aim over some reasonable period to bring its expenditures into balance with its income.” SAULNIER, *supra* note 131, at 9.

147. Dan T. Smith, *Two Years of Republican Tax Policy: An Economic Appraisal*, 8 NAT’L TAX J. 2, 2 (1955).

148. *Text of President Eisenhower’s Message to Congress on Taxation*, N.Y. TIMES, May 21, 1953, at 27.

plans.¹⁴⁹ John Biggers, chairman of the Business Advisory Council, explained that “much as we business men want to see an end to the excess profits tax and a reduction in individual income taxes, we don’t feel that such reductions should be made before a balanced budget is achieved or is at least in sight.”¹⁵⁰ Even Gordon Grand, CEO of Olin Industries, compared his quest for the elimination of double taxation of dividends to Don Quixote’s assault on the windmills, noting that all proposals must “recognize the existence of three harsh realities—high federal expenditures, a balanced-budget objective and the fact that, as a general rule, Congressmen prefer to be reelected.”¹⁵¹

Business was rewarded for its patience on tax reform. In his January 1954 State of the Union address, Eisenhower called for a complete overhaul of the entire tax system to “remove the more glaring tax inequities.”¹⁵² In his Budget Message later that month, Eisenhower specifically identified double taxation as one such “glaring inequity,” proposing to remove it “by allowing stockholders a credit against their own income taxes as a partial offset for the corporate tax previously paid.”¹⁵³ Under his proposal for addressing double taxation, which had already been approved by the Ways and Means Committee,¹⁵⁴ the first \$50 of dividends would be excluded from income, rising to the first \$100 of dividends starting in 1955. In addition, a tax credit of five percent would be permitted on dividend income beyond the exclusion, rising to ten percent in 1955 and fifteen percent in 1956.¹⁵⁵ The decision to rely on a shareholder exemption and tax credit, rather than on a corporate credit or deduction, was apparently to avoid discriminating between distributed and undistributed profits, thereby reviving the hated undistributed-profits tax.¹⁵⁶

The dividend-tax proposal was designed in large measure to respond to the equity crunch. A Ways and Means Committee spokesman said that the proposal was “designed to stimulate a flow of equity capital,”¹⁵⁷ and the *New York Times* reported that “[o]ne of the avowed aims of the plan is to encourage the purchase of stocks and thus give business the capital needed for modernization and expansion that will help keep the country at a high level of

149. See FRIEDBERG, *supra* note 145, at 132 (noting that corporate executives were greatly relieved when Eisenhower did allow the excess profits tax to expire).

150. Charles E. Egan, *Eisenhower Backed on His Tax Stand*, N.Y. TIMES, May 9, 1953, at 27.

151. Gordon Grand, *Proposals for Revising the Tax System*, 25 PROC. ACAD. POL. SCI. 27, 27 (1954).

152. Dwight D. Eisenhower, Annual Message to the Congress on the State of the Union (Jan. 7, 1954), in 1954 PUB. PAPERS 6, 15 (1954).

153. *Complete Text of Tax Proposals*, L.A. TIMES, Jan. 22, 1954, at 13.

154. Alan L. Otten, *President Asks Congress to Put Corporate Income Taxes Partially on a Pay-as-You-Go Basis, Starting in 1955*, WALL ST. J., Jan. 22, 1954, at 5.

155. *Id.*

156. Feingold, *supra* note 143, at 203.

157. *Tax Revisions: House Unit Votes to Lift Large Part of Double Levy on Dividends*, WALL ST. J., Jan. 15, 1954, at 2.

economic activity.”¹⁵⁸ The Administration’s supporters used this argument frequently. Treasury Secretary George M. Humphrey testified that double taxation

has restricted the market for shares of a stock in companies which want to expand and has forced them to borrow money instead of selling shares in their future. In the past ten years better than 75 per cent of private industry financing has been done by going in debt instead of selling shares.¹⁵⁹

Similarly, Representative Thomas E. Martin of Iowa declared that “[d]ouble taxation of dividends on corporation stock causes many people to invest their funds in tax-exempt bonds rather than invest them as risk capital.” According to Martin, this

caused corporations to turn to bonded indebtedness rather than common stock to keep their business going, even though heavily bonded indebtedness makes any business organization especially vulnerable to adversity when their continued operation is most important.¹⁶⁰

The *New York Times* predicted that this provision “would do about as much as any proposal of the President’s tax program to give business a much wanted shot in the arm.”¹⁶¹

The dividend-tax-relief proposal “proved to be one of the thorniest and most controversial considered in writing the revenue bill.”¹⁶² Though the bill as a whole was developed with remarkable speed, considering its comprehensive nature, the dividend-tax provisions proved to be the one speed bump. As one attorney involved with the legislation explained: “Such Congressional speed was possible because there was little Congressional controversy over the technical portions of the bill. Only on policy questions, especially the provisions for dividend-tax relief, was there strong difference[] of opinion.”¹⁶³ This opposition came primarily from organized labor, with the Congress of Industrial Organizations launching a grassroots effort against the provision.¹⁶⁴

One of the principal criticisms of dividend-tax relief was that an increased exemption for all individual income tax payers should come before corporate tax reform.¹⁶⁵ Democrats “ridiculed the administration’s program as a ‘trickle down’ policy that attempted to indirectly help the unemployed by granting tax relief to corporations and the rich.”¹⁶⁶ The *New York Times* reported that

[t]he section on dividend income is the big fighting point in the bill as it passed the

158. John D. Morris, *Cut in Taxes on Dividends Approved by House Group*, N.Y. TIMES, Jan. 15, 1954, at 1.

159. Charles E. Egan, *Humphrey Views the Business Dip as Readjustment*, N.Y. TIMES, Feb. 3, 1954, at 1, 13.

160. Benjamin L. Masse, *Tax on Dividends: A Moral Inquiry*, 91 AMERICA 185, 186 (1954).

161. John D. Morris, *What’s Behind the Tax Reforms*, N.Y. TIMES, Jan. 24, 1954, at E5.

162. DANIEL M. HOLLAND, *DIVIDENDS UNDER THE INCOME TAX* 147 (1962).

163. Norris Darrell, *Internal Revenue Code of 1954—A Striking Example of the Legislative Process in Action*, in MAJOR TAX PROBLEMS OF 1955, at 1, 15 (John W. Ervin ed., 1955).

164. See Feingold, *supra* note 143, at 205.

165. Morris, *supra* note 161, at 11.

166. SLOAN, *supra* note 130, at 135.

House. The provision has drawn fire from many Democrats on the ground that it will chiefly aid the rich. Some committee members have said they will seek to strike it from the bill.¹⁶⁷

This controversy appeared to be a consequence of the nearly zero-sum nature of the tax bill, which was reportedly designed to obtain “maximum reform with a minimum loss of revenue.”¹⁶⁸ The fear was that if shareholders won, then nonshareholders were likely, in some fashion, to lose. Pennsylvania’s Democratic representative characterized the dividend-tax-credit provision as “an attempt to make the man who earns his bread by the sweat of his brow pay more and more of the \$50 billion cold war with Russia . . . while . . . letting the investor, the corporation and the large stockholder pay less and less.”¹⁶⁹

For the most part, Democratic opposition was “a synthetic controversy” designed to take advantage of election-year politics and the Republicans’ rejection of individual relief in favor of dividend-tax reform.¹⁷⁰ Republican members of the Ways and Means Committee had predicted that it would become “political dynamite” that could be used by Democrats as proof that Eisenhower and the Republicans were favoring the “rich man” over the “little fellow.”¹⁷¹ Such predictions proved largely true. According to the *New York Times*, “The fight against the dividend provision . . . was waged in the belief that it would provide a top campaign issue for the Democrats” in the fall.¹⁷² Although supporters pointed out that the dividend-tax exclusion and credit were not quite the giveaway that was often portrayed,¹⁷³ many attributed the Democrats’ eventual success in the congressional elections to the efforts they took to substitute a general tax cut available to all individuals for the dividend-tax cut for shareholders.¹⁷⁴

167. *Senate Unit Delays on Dividend Tax Cut*, N.Y. TIMES, May 6, 1954, at 40.

168. Smith, *supra* note 147, at 4.

169. Editorial, *Nonsense About Dividends*, N.Y. TIMES, July 15, 1954, at 26 (quoting Rep. Peter Eberharter).

170. Edward H. Collins, *Economics and Finance: A Synthetic Controversy*, N.Y. TIMES, Mar. 29, 1954, at 29.

171. *Republicans Worried over Reaction to Vote to Cut Double Dividend Tax*, WALL ST. J., Feb. 11, 1954, at 5.

172. John D. Morris, *House Votes Tax-Cut Bill, Republican ‘Cornerstone,’* N.Y. TIMES, July 29, 1954, at 1.

173. See, e.g., Editorial, *Double Tax on Dividends Is Hardship on Many Who Have Moderate Incomes*, SATURDAY EVENING POST, Aug. 28, 1954, at 12 (noting that a survey by the United States Steel Corporation revealed that a large percentage of stockholders were members of lower-income brackets); Godfrey N. Nelson, *Basis Graduated for Dividend Aid*, N.Y. TIMES, Mar. 28, 1954, at F1 (“The percentage reduction of tax under the proposed plan is actually greatest in the lowest bracket and declines as the income level rises.”). *But see* FEINGOLD, *supra* note 143, at 208–17 (criticizing the methods of the U.S. Steel Company survey and instead suggesting that most stock was held by those with the highest incomes); DANIEL M. HOLLAND, *THE INCOME-TAX BURDEN ON STOCKHOLDERS 169–70* (1958) (arguing that “at the lowest income levels only a small fraction” of the extra tax burden “is removed; [while] at the highest income levels, the ‘extra’ burden is significantly ameliorated”).

174. John D. Morris, *Eisenhower Sets 1956 for Tax Cut*, N.Y. TIMES, Jan. 21, 1955, at 10.

The Republicans succeeded in enacting some dividend-tax relief, but theirs was ultimately a “limited” victory.¹⁷⁵ The legislation’s four-percent dividend-tax credit was called a “watered down version” of Eisenhower’s initial proposal for a fifteen-percent shareholder credit within three years.¹⁷⁶ Columbia economics professor Carl Shoup noted that

the amounts of change are so small that in most cases they make no notable difference in the pattern of tax distribution[] from the viewpoint of tax equity. . . . [,] [and] a credit of only 4 per cent and an exclusion of only \$50 are not likely to influence the sum total of investment appreciably.¹⁷⁷

Not only was the relief limited, but it was short-lived. The dividend-tax credit was ultimately repealed in 1964 as part of John F. Kennedy’s plan to reduce corporate and individual tax rates and broaden the tax base.¹⁷⁸ The exemption remained for much longer, but eventually was repealed as well as part of the 1986 tax reform.¹⁷⁹

B. Why Was Integration So Limited?

The modest dividend-tax relief enacted was a somewhat surprising result for Eisenhower, especially given reports that “[t]he dividend provision was regarded by the Administration as one of the bill’s two most important features.”¹⁸⁰ His other top priority—an accelerated depreciation provision—was somewhat less controversial and survived largely as proposed.¹⁸¹

Some observers have concluded that the Administration and its supporters in Congress themselves downgraded integration as a priority. Professor Gary Reichard speculated that “[i]n all likelihood, Senate leaders relaxed party discipline on the dividend provision in order to concentrate their energies on defeating the drive for the \$700 individual exemption, which the administration had viewed all along as the greater threat to its program.”¹⁸² This is what the Democrats intended when they introduced the proposal for an increase in the individual exemption and reframed the debate as one between tax cuts for the

175. Feingold, *supra* note 143, at 179.

176. Morris, *supra* note 174.

177. Carl S. Shoup, *The Dividend Exclusion and Credit in the Revenue Code of 1954*, 8 NAT’L TAX J. 136, 141–42 (1955); see JOHN F. WITTE, *THE POLITICS AND DEVELOPMENT OF THE FEDERAL INCOME TAX 147–48* (1985) (noting that the final version of the bill was very close to Eisenhower’s request, though the tax break on dividend income was weak); Masse, *supra* note 160, at 186 (quoting Rep. Edith Nourse Rogers, who charged that “[y]ou must be a special type of individual . . . before you receive one cent of tax relief,” and thus describing the limited effect of the dividend-tax break).

178. See JULIAN E. ZELIZER, *TAXING AMERICA: WILBUR D. MILLS, CONGRESS, AND THE STATE, 1945–1975*, at 205 (1998).

179. STAFF OF JOINT COMM. ON TAX’N, 99TH CONG., *GENERAL EXPLANATION OF THE TAX REFORM ACT OF 1986*, at 276 (Comm. Print, JCS-10-87, 1987).

180. John D. Morris, *Senate, 63–9, Votes Omnibus Tax Bill*, N.Y. TIMES, July 3, 1954, at 1.

181. John D. Morris, *Senators Slash Dividend Tax Aid; Final Vote Nears*, N.Y. TIMES, July 2, 1954, at 1.

182. REICHARD, *supra* note 146, at 113.

rich or the poor and middle class.¹⁸³ Downsizing the dividend-tax relief also ties into Eisenhower's reluctance to exacerbate the budget situation and risk inflation by targeting lower-income taxpayers for cuts that would increase consumer spending.¹⁸⁴ More broadly, the sheer size and scope of the bill suggests there were numerous other potential tradeoffs that could have interceded. A *New York Times* editorial speculated, "The Administration would probably admit that as between reform of the law affecting the taxation of dividends, on the one hand, and reform of the existing mandatory high rigid price supports for 'basic' farm commodities, the latter was decidedly the more urgent."¹⁸⁵ Nevertheless, all of this prompts this question: Why did corporate managers not put up more of a fight to resist the dilution of dividend-tax relief?

One explanation for the absence of business protest was that the economy had begun to strengthen while the bill was still pending. By the time the bill reached the Senate in late June 1954, the chairman of the Council of Economic Advisors announced in a cabinet meeting that "recovery was underway."¹⁸⁶ Total corporate cash flow, which had remained stagnant in 1953 and 1954, and retained profits, which had dipped in 1954, both rose significantly by 1955.¹⁸⁷ The stock market also recovered, with the Dow Jones Industrial Average rising above its 1929 high in November of 1954 for the first time since the stock market crash, and the number of stockholders jumping from 6 million in 1952 to 8.6 million by 1956.¹⁸⁸

This change in underlying economic circumstances may have reduced corporate managers' concern about equity investment. Indeed, managers generally had cause to prefer to use retained earnings because they avoided the scrutiny applied by creditors and stockholders. When profits were down and credit was too expensive, though, the only alternative was to seek external financing through equity investors. Double taxation interfered not only because it made stock less attractive to investors during an economic cycle when stock appreciation was less likely, but because it put pressure on managers to pay higher dividends to provide an attractive after-tax return to investors, thus potentially further reducing the available retained earnings. Once corporate profits resumed normal levels, though, the accelerated-depreciation provision and other entity-level corporate tax reforms—such as more liberal loss-carryforward provisions, current deductions for research-and-development expenses, and an easier standard for retaining earnings—were more valuable to managers, because those managers could use a greater proportion of the profits

183. See *supra* text accompanying notes 165–74.

184. FRIEDBERG, *supra* note 145, at 133.

185. Editorial, *supra* note 169.

186. ROBERT J. DONOVAN, EISENHOWER: THE INSIDE STORY 221 (1956); SLOAN, *supra* note 130, at 143.

187. See VATTER, *supra* note 130, at 96 tbls.3–7.

188. MARKHAM, *supra* note 125, at 293; see also *supra* note 124 and accompanying text.

for internal financing.¹⁸⁹ Even for firms that preferred external financing, the economic recovery made double taxation less concerning. For example, the *Wall Street Journal* reported that a number of utility corporations told members of Congress that the Senate proposal to limit dividend tax relief to a fifty-dollar exclusion “would help bring out sufficient equity capital for the time being, even without any tax credit.”¹⁹⁰ Thus, though a coalition of business interests appeared to form behind Eisenhower’s dividend tax relief proposal in 1953, it is not surprising that consensus did not remain strong enough to push through more-significant dividend-tax relief when the crisis eased.

This is not to suggest that the push for integration disappeared completely. Most notably, in 1958 Congress enacted an elective pass-through scheme—Subchapter S—although it was limited to small business corporations whose concern about double taxation was never particularly great.¹⁹¹ Several integration proposals garnered significant support during the 1980s and 1990s,¹⁹² but none was adopted. At the end of the century, the corporate income tax looked remarkably similar to the one criticized at the end of World War II. It would not be until 2003 that an integration proposal would again garner sufficient support to pass. Rather than adopting full dividend exclusion, though, as originally proposed by President Bush, Congress adopted a compromise measure that taxed certain dividends at the lower capital-gains rate.¹⁹³ As in 1954, therefore, it fell far short of major reform.

189. See VATTER, *supra* note 130, at 191 (“It is therefore apparent that the relaxation of the Treasury’s depreciation policy in 1954 must have gratified to a considerable degree the preference of business for internal financing of long-term investment”); John D. Morris, *Senate Approves Bill to Cut Taxes; President Gets It*, N.Y. TIMES, July 30, 1954, at 1.

190. *Technical Relief Bill: Double Tax on Dividends to Front as House–Senate Conference Opens*, WALL ST. J., July 14, 1954, at 3.

191. For a history of this period, see generally Mirit Eyal-Cohen, *When American Small Business Hit the Jackpot: Taxes, Politics, and the History of Organizational Choice in the 1950s*, 6 PITT. TAX REV. 1 (2008); ZELIZER, *supra* note 178, at 99–100; Note, *Optional Taxation of Closely-Held Corporations Under the Technical Amendments Act of 1958*, 72 HARV. L. REV. 710, 723 (1959).

192. See A.L.I., FEDERAL INCOME TAX PROJECT: INTEGRATION OF THE INDIVIDUAL AND CORPORATE INCOME TAXES: REPORTER’S STUDY OF CORPORATE TAX INTEGRATION (Alvin C. Warren, Reporter, 1993); U.S. DEP’T OF THE TREASURY, INTEGRATION OF THE INDIVIDUAL AND CORPORATE TAX SYSTEMS: TAXING BUSINESS INCOME ONCE (1992); OFFICE OF THE PRESIDENT OF THE UNITED STATES, THE PRESIDENT’S PROPOSALS TO THE CONGRESS FOR FAIRNESS, GROWTH, AND SIMPLICITY 120–29 (1985); 2 OFFICE OF THE SEC’Y OF THE TREASURY, TAX REFORM FOR FAIRNESS, SIMPLICITY, AND ECONOMIC GROWTH: THE TREASURY DEPARTMENT REPORT TO THE PRESIDENT 134–44 (1984).

193. For further discussion of the 2003 changes, see Steven A. Bank, *Dividends and Tax Policy in the Long Run*, 2007 U. ILL. L. REV. 533, 537–41 (2007).