

I was even more disturbed because I felt that the profits as a percentage, the rate of return to the amount of money that had been plowed into that enterprise would be even lower.

Your chart here seems to indicate that it is not quite as bad as I had thought.

Mr. LANGUM. That is right. And not as bad as is frequently thought to be the case in many business circles. I do believe, as I said in my testimony, there is a profit squeeze. Businessmen are in a real hard race between cost and sales and in turn, between income and capital invested. But the historical figures, this decline from 1947 to 1961, just simply do not indicate the real profit situation.

Representative CURTIS. The other thing that relates to this is this business of turnover of capital assets and replacement. I had felt that post-World War II inflation, because of the impact of inflation on the corporate tax, had amounted to a capital levy.

I am not sure that it caused as much damage as I thought that it would. But if you follow what I mean, take the telephone company, they have a telephone pole that they put in the ground for a hundred dollars or whatever it is, then they replace it 10 years later and it costs \$200 for the same identical thing. They don't care about the dollar. They want the telephone pole in order to stay in business.

Let us take it another way, they would only be allowed to set aside \$100 on their depreciable asset and then they have to spend \$200. This means they would have to dig up another hundred somewhere else.

I have never seen a study in depth made of the impact of inflation on capital investment as it was affected through our tax structure.

I have felt that it has been a real one. I have seen it come out in this way. Where businessmen have come before the Ways and Means Committee and asked for the LIFO formula instead of FIFO on inventory.

I have never seen any studies made on the inflationary effect on depreciable capital assets comparable to inventory.

Mr. LANGUM. That is a very important point. Some studies have been made on that. I have made those myself in the case of numerous utilities and the American Accounting Association has formally prepared studies on this.

The problem has two aspects. First of all, without any doubt in my judgment after inflation, particularly in the earlier postwar years, that depreciation charges per books understated the cost of plant consumed, and hence overstated the reported profit figures.

That was widely noted at the time in business discussions of profits, and the point was quite right. Parenthetically now we should not use those overstated profits as a measure of where we ought to be.

The other part is this, however. Many corporations have had substantial retained earnings, and beyond that this major rise in depreciation accruals and hence cash flow. So that many corporations have been in this situation; I believe, that the reported earnings and the reported rate of return figures also were really overstated, particularly earlier in the postwar period. But they were not really hurt because the money was coming in, although stated in other forms, to cover the full cost of plant consumed and replaced, except for the point that the reported income was first taxed as income even though the costs were understated.