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No _____



74TH CONGRESS }
2d Session }

SENATE

{ REPORT
No. 944
Part 7 }

U.S. Congress, Senate, Special Committee
" on Investigation of the Munitions Industry "

MUNITIONS INDUSTRY

REPORT ON GOVERNMENT MANUFACTURE OF MUNITIONS

BY THE

SPECIAL COMMITTEE ON INVESTIGATION OF THE MUNITIONS INDUSTRY UNITED STATES SENATE

PERSUANT TO

S. Res. 206 (73d Congress)

A RESOLUTION TO MAKE CERTAIN INVESTIGATIONS
CONCERNING THE MANUFACTURE AND SALE
OF ARMS AND OTHER WAR MUNITIONS



JUNE 15 (calendar day, JUNE 19), 1936.—Ordered to be printed

UNITED STATES
GOVERNMENT PRINTING OFFICE
WASHINGTON : 1936

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MUNITIONS INDUSTRY

JUNE 15 (calendar day, JUNE 19), 1936.—Ordered to be printed

Mr. NYE, from the Special Committee on Investigation of the Munitions Industry, submitted the following

REPORT ON GOVERNMENT MANUFACTURE OF MUNITIONS

[Pursuant to S. Res. 206, 73d Cong.]

INTRODUCTORY STATEMENT

The Special Committee on Investigation of the Munitions Industry was authorized by Senate Resolution 206 of the Seventy-third Congress, which began—

Whereas the influence of the commercial motive is an inevitable factor in consideration involving the maintenance of the national defense; and

Whereas the influence of the commercial motive is one of the inevitable factors often believed to stimulate and sustain wars * * *

and which directed the committee—

(d) To inquire into the desirability of creating a Government monopoly in respect to the manufacture of armaments and munitions and other implements of war, and to submit recommendations thereon.

Under the authority the committee considered not only the cost of purchase and construction of certain munitions facilities, but also many other factors bearing on the problem, such as the general social desirability of munitions sales abroad, the activities of the munitions companies abroad, their relations with governmental departments, the price and profit experience of the Nation with these companies during the World War, the need for adequate national defense in peacetime as well as in wartime and the influence of the commercial motive “in considerations involving the maintenance of national defense.”

The committee, in considering the desirability of a Government monopoly in respect to the manufacture of munitions, wishes to incorporate, herewith, by this reference, its findings on the character and functioning of the munitions industry, concurred in unanimously by

all members of the committee and submitted as part of its report on activities and sales of the munitions companies on April 20, 1936 (S. Rept. No. 944, Part 3, 74th Cong., 2d sess.).

The committee, in considering the naval shipbuilding aspects of this subject, also wishes to incorporate in this report, by this reference, its findings in that regard, concurred in unanimously by all members of the committee, and submitted as part of its preliminary report in naval shipbuilding on June 24, 1935 (S. Rept. No. 944, 74th Cong. 1st sess.).

The committee, in considering the price and profit experience of this Nation with private munitions companies during the World War, also wishes to incorporate in this report, by this reference, its findings in that regard, concurred in unanimously by all members of the committee, and submitted as part of its preliminary report on wartime taxation and price control on July 29, 1935 (S. Rept. No. 944, Part 2, 74th Cong., 1st sess.).

The findings referred to above have led all members of the committee to conclude that there should at the very least be strict regulation of the industry.

CONSIDERATIONS OF POLICY

In discussing the desirability of Government monopoly, a duty laid upon the committee by the Senate, more than the question of cost must be taken into consideration, although that is a very important item. It is necessary also to consider the effect of such a monopoly and of the absence of such a monopoly on prices and profits in wartime as well as in peacetime. It is necessary to consider the possibility of effective regulation, and its cost. It is necessary to consider the effect of such a monopoly upon the readiness of the Nation to produce munitions in the event of war.

I. THE RELATION BETWEEN PEACETIME AND WARTIME PROFITS

The committee did not have sufficient staff to check the peacetime profits of the munitions companies, on individual contracts, because this procedure would have involved years of work by a very large body of accountants. Several of the companies testified to large profits on peacetime munitions work for the Government, using their own figures, unchecked by the committee. Examples are: Bethlehem Ship Building Co., cruiser *Portland*, \$2,058,796, 21.8 percent profit; cruiser *Northampton*, \$2,200,000, 25.4 percent profit. Newport News Shipbuilding & Dry Dock Co., cruiser *Augusta*, \$2,800,945, and *Houston* \$2,800,945, 35 percent profit; aircraft carrier *Ranger*, \$3,050,000, 23.1 percent profit. New York Shipbuilding Co., cruiser *Chester*, \$2,946,706, 36.9 percent profit; cruiser *Indianapolis*, \$3,007,049, 33.4 percent profit. Carnegie Steel Co., armor plate, *NOD-272*, profit 57.9 percent; *NOD-331*, profit 43.4 percent; *NOD-432*, profit 42.7 percent. Bethlehem Steel Co., certain gun-forging contracts showed 28.27, 18.47, and 18.09 percent. Sperry Gyroscope Co. (Army auditor's figures, exhibit 4917), 108 flight indicators for Army Air Corps, 54.6 percent profit; 114 turn indicators, 40.4 percent profit. Douglas Aircraft Co. (exhibit 4889), showed estimated costs and profits, before commissions, of 30 percent on fighters and attack planes for China.

The significance of these high prices and profits in war preparation during peacetime is the probability that such prices and profits will be used as the base of wartime profits and prices, and that the courts will insist upon their use to justify high wartime profits.

This was indicated clearly in the report of the special master and referee, District Court of United States, Eastern District of Pennsylvania (*U. S. Complainant v. Bethlehem Steel Corporation, etc.*) in 1933. The master used the following chain of reasoning (exhibit 4872):

The Government aimed to win the war. Bethlehem was deemed essential to doing so. A failure to induce Bethlehem to undertake the ship-building program covered by these contracts, followed by the taking possession by the Fleet Corporation of the Bethlehem plants, could not have accomplished the desired result. It was Bethlehem's organization that was necessary to insure success to the ship-building program of the Fleet Corporation and, as the Government did not have power to compel performance by an unwilling organization, if Bethlehem demanded its price on the basis of substantial commercial profits rather than contribute such services on a patriotic basis, the Government was obliged to take the contracts on such basis or not at all.

The evidence shows, and the master finds, that the Fleet Corporation made the contracts with open eyes, although resenting the commercial attitude of Bethlehem and condemning Bethlehem for demanding its "pound of flesh", and did so because of a realization of the necessity of attaining an objective with the ship-building program which, without Bethlehem, might not be possible.

The master then quotes the position of the Government from 823 of the bill of complaint in equity:

Complainant avers that said representations were knowingly false in that the Bethlehem Shipbuilding Corporation, Ltd., as hereinbefore set forth, was in a position to know what would be the approximate cost of constructing said vessels, and the said amounts stated in said contracts were known by the said representatives of said corporation to be greatly in excess of any costs which could reasonably be anticipated, based upon the wage scale then in effect, and the existing costs of material. Complainant avers that said estimates and representations were made for the purpose of enabling the Bethlehem Shipbuilding Corporation, Ltd., to derive excessive, unreasonable, and unconscionable profits from said contracts.

The master also quotes the major brief for the Government (pp. 321-322):

Having perpetrated a gross fraud upon the Government in connection with such contracts, it would be unconscionable to hold that notwithstanding such fraud, Bethlehem should receive as compensation the same amount which would afford just compensation to an honest shipbuilder for doing the same work done by it. Any such decision would mean that Bethlehem had everything to gain and nothing to lose, finally, in attempting to defraud the Government and would encourage dishonest contractors to take advantage of the Government under like circumstances.

No one can say that this country is done with war or how soon a national emergency will again exist calling for the maximum production of every shipyard throughout the United States. At such time plant requisition will again prove impracticable. There will again be no time for haggling, and the Government will again be obliged to depend upon the integrity and patriotism of the manufacturers with whom it is forced to deal. At such time there will undoubtedly again be those who will look upon the national emergency as an opportunity to make enormous profits for their respective companies and themselves at the expense of the Government, and whose patriotism and sense of propriety will not, in themselves, be sufficient to restrain them from taking full advantage of such opportunity—in its influence upon such dealings—the decision in these proceedings will be of far more importance than the millions now involved.

In reply to this concern on the part of the Government, the master gave judicial notice to the findings and testimony of the Senate Munitions Committee, especially the increase of prices which followed the big naval-construction program and the admission of the shipbuilders that they were putting up prices because of the great amount of work available at the time. He cited the profits of 36.7 percent on the *Chester*, built by New York Shipbuilding Co., and of 25.4 percent on the *Northampton* built by the Bethlehem Shipbuilding Co. He found the average wartime profits to Bethlehem upon the contracts with the Emergency Fleet Corporation to be 22.245 percent of actual cost, and less than the peacetime profits and found no fraud on Bethlehem's part, as charged by the United States.

The case will presumably be appealed by the Government. Meanwhile, however, the committee is impressed with the fact that the master used figures of high profits during peacetime which were put on record for the first time by this committee, as a means of justifying wartime profits of over 22 percent. This sets a precedent and makes all the high profits earned in peacetime a base which can and doubtless will be used by the companies in wartime.

The committee is also impressed with the master's simple statement that the Government had no means to force Bethlehem to produce ships, and that if Bethlehem chose, as it did, to demand "its price on the basis of substantial commercial profits rather than contribute such services on a patriotic basis, the Government was obliged to

take the contracts on such basis or not at all." The committee, in its report on wartime taxation and price control (S. Rept. 944, pt. 2, 74th Cong., 1st sess.) found numerous other such cases, and found that "the apparent alternative of commandeering industry is in fact not an available alternative."

The committee is also impressed with the Government's fear, expressed above, that a decision allowing high wartime profits, obtained under duress, will influence the attitude of the manufacturers with whom the Government is forced to deal, and that "at such time there will undoubtedly again be those who will look upon the national emergency as an opportunity to make enormous profits for their respective companies and themselves at the expense of the Government, and whose patriotism and sense of propriety will not, in themselves, be sufficient to restrain them from taking full advantage of such opportunity."

The committee feels that the way is now wide open for the munitions companies to claim the right to make profits in wartime as high as they did in peacetime, and that therefore strict profit control in peacetime is essential if the Government is not to pay through its nose in wartime. Failure to hold down munitions profits during peacetime will be paid for many million times over in wartime.

The committee notes also from the master's report the situation confronting the Government in wartime: It needs the manufacturing plants of the Nation for its program of munitions production and has no means of imposing that production upon them. They will, in fact, take it at their own price or leave it. The Government cannot afford to have them leave it, so they get it at their own price. Patriotism and sacrifice is something to talk about to the public, as the president of Bethlehem Steel did fully, early in 1917. To the War Department in private they talk prices and profits, and say, in effect, "take it or leave it", knowing that they have the Government at their mercy. When, as in the case cited above, the Government claims that it was forced to make contracts under duress, the master of a United States district court points out that the Government knew at the time that the prices in the contracts were too high, and, having its eyes open at the time, later has no redress.

This legalized use of a national emergency to obtain high profits must be considered in any discussion of the desirability of a governmental monopoly of the manufacture of munitions.

II. DIFFICULTIES OF REGULATION IN PEACETIME AND WARTIME

In considering the question of the desirability of producing all the naval ships (except auxiliaries) in Government navy yards, the committee recurs to the testimony developed in several months of hearings on the naval shipbuilding companies, and especially the committee's findings in its report on naval shipbuilding (S. Rept. 944, 74th Cong.):

A. AGREEMENTS ON NAVAL BIDDING

Specifically, the committee finds, under the head of Agreements on Naval Bidding:

The Navy has become a big business. It is one of the largest governmental contractors in the world.

During the years 1933 and 1934 it gave out to private companies contracts totaling over \$180,000,000.

The committee heard 9 companies, 67 witnesses, largely on the subject of these contracts. It spent 38 days, and took 4,036 pages of testimony.

The committee finds that the evidence indicates clearly that:

(1) In most cases the Navy wishes work to begin as soon as possible. The result of this is that there is often not time to prepare designs, let alone examine figures or to analyze the bids put before it by private companies.

(2) The rush has made it impossible for the Navy to use its own navy yards as current up-to-date yardsticks of private bids. The navy yards do not even know such essentials of the bids of private yards as the speed guaranties or oil guaranties until after the private bids are opened.

(3) The Navy has never examined the underlying costs or profits of the private builders. It makes no pretense of doing this. It has no staff for it. The figures studied by the Munitions Committee were all news to it.

The Navy makes no attempt to examine the costs of the private companies to determine whether the profit limitation of 11.1 percent in the Vinson-Trammell Act is enforced or evaded. That is left to the Treasury to do after 3 years, after a job is done.

(4) This rush, this lack of staff, this lack of acquaintanceship with the strange ups and downs of bidding by the private companies on the part of the Navy, leaves the Navy at the mercy of the shipbuilders. A series of bids are put before the Navy, and the Navy has to take the low one, and the taxpayers have to hope and pray that the low one is somewhere within a few million dollars of being reasonable and proper.

(5) The evidence presented to the committee showed that in 1933 on contracts worth \$130,000,000 to the private shipbuilders, there was no hard-hitting competition among equally desirous bidders able to take on the work: On the aircraft carriers, worth \$38,000,000; on

the two light cruisers, worth \$24,000,000; on the heavy cruiser, worth \$12,000,000. There was no competition of that character on the heavy destroyer leaders, worth \$30,000,000, nor on the light destroyers, worth \$18,000,000. On the submarines there may have been honest competition, but one competitor possessed all the patents and would not tell the other company how much those patents would cost them. That is the way \$130,000,000 worth of work was given out in 1933.

(6) From 1927 on when the cruiser program started, the record is the same. If there was no collusion, there was a sympathetic understanding among the big companies of each other's desires.

If there were no conversations about bidding among them, there was telepathy.

In 1927 the shipbuilders made profits of 35 and 25.4 and 36.9 percent on the cruisers. That was too good to spoil by hard competition. In 1929 the Navy asked for bids on two cruisers. Not one of the "Big Three" yards obliged. They bid on 1 each, and got 1 each. Their profits on these were around 22 percent.

The record is the same in 1931.

(7) In 1933 two shipbuilders knew and wrote down lists of the low bidders weeks in advance of the time the bids were opened. Mr. Bardo was one of them. Mr. Wilder was another. Mr. Bardo admitted discussing his desires for certain ships only with his two main competitors.

(8) The fact that many bids are submitted by shipbuilders does not mean that there is real competition. It does not mean lower prices. In fact, quite the contrary is true. When there is lots of work to go around the charges go up. The shipbuilders know that the Navy feels it has to have the ships, and they raise the prices. They admitted this frankly.

B. EXCESSIVE PROFITS

The committee finds, under the head of Excessive Profits, that the profit figures on the only naval vessels on which such figures are available were 35 percent (Newport News, 2 cruisers); 36.9 and 33.4 percent (New York Ship, 2 cruisers); 25.4 and 21.8 percent (Bethlehem Shipbuilding, 2 cruisers); 23.1 percent (Aircraft Carrier *Ranger*, Newport News).

C. PRICES INCREASED WITH BIG NAVY

The committee finds, under the head Prices Increased with Big Navy, that the need of the Navy for many ships in 1933 was the main cause for the increase in prices charged by the private shipbuilders, and that they frankly admitted this, and that the Navy recognized the fact.

Q. They (the shipbuilders) were frank enough to say they were putting up prices because of the great amount of work at the time?—A. (Admiral Robinson) There is no question about that.

D. NAVY YARDS AS YARDSTICKS

The committee finds, under the head of Navy Yards as Yardsticks, that preliminary studies show the cost of building cruisers in navy yards to have been \$2,116,304 lower than in private yards in 1927 and \$1,843,693 lower in 1929. It also finds that in 1933 the low

navy-yard estimate was \$1,122,000 below the lowest private-yard fixed-price bid and \$5,351,000 below the highest fixed-price bid. It also finds that the navy-yard estimates on the cost of building light destroyers averaged \$1,240,459 lower than the average bids of the private yards and \$943,460 below the lowest private-yard bid on a fixed-price basis.

The committee finds, further, that Navy officials have been transmitting to congressional committees figures on comparative costs of private and navy yards showing the profits on a privately built ship, the cruiser *Chester*, as \$983,000, whereas the New York Shipbuilding Corporation informed the Munitions Committee that its profit on this cruiser was \$2,946,706.

The committee finds, further, that the opposition of the private shipbuilders to navy-yard construction has been intense, reaching the point where the vice president of Newport News thought it better "to kill the Navy bill entirely" than to spend part of it in navy yards.

The committee notes the language used concerning a naval appropriation in 1931 by the Washington representative of Bath Iron Works:

I understand the morning after the (appropriation) bill went through every East-coast yard had its representatives in Washington with their tongues hanging out and all teeth showing ready to fight for their share of the plunder, and the only thing that stopped the West-coast yards from being here was the fact that they couldn't come bodily by telegraph.

E. THE NAVY'S DEPENDENCE ON PRIVATE YARDS

The committee finds, under the head of the Navy's Dependence on Private Yards, that at present light cruisers, aircraft carriers, light destroyers, destroyer leaders, and submarines are being built largely or entirely from the plans drawn by private companies, and that there are very definite disadvantages to a system in which the Navy has to depend on private companies for such an important part of the national defense.

The committee notes the awareness of several of the shipbuilding companies of the fact that the Navy is completely dependent on them for this work.

The committee notes the statement by Commander E. L. Cochrane: The Navy's developments of 15 years were—handed to the Electric Boat Co. on a silver platter, so to speak, on the conviction that it was desirable to keep at least one commercial company in the submarine game. * * *

and also notes the statements of Sun Shipbuilding officials who wanted to build submarines that they could not find out what the Electric Boat patents would cost them prior to entering a bid. The committee finds this apparent monopoly an unwholesome and unsatisfactory situation, especially in view of Electric Boat Co.'s foreign connections.

The committee finds further that a very considerable delay followed the allocation of \$238,000,000 of Public Works Administration money to the Navy in 1933, and that a large amount of this was due to delay in the planning work by these shipbuilding companies which had contracted to do this part of the work for the others and for the navy yards. The committee notes that this delay took place in spite of pledges by all shipbuilders to begin work as soon as possible for the benefit of the unemployed.

The committee finds, further, that while the Navy is dependent on the private shipbuilders for ways and plans, the private shipbuilders are dependent on the Navy for special favors, and have received a considerable number of them. Most notable among these are the adjusted price contracts of 1933 and 1934, the failure to use the navy yards as yardsticks, the failure to make itself independent of the private yards in planning work, and the Navy's opposition to profit limitation in 1934.

The committee finds indications of the use by the Navy of the shipbuilders as a lobby for its interests.

F. INFLUENCE AND LOBBYING OF SHIPBUILDERS

The committee finds, under the head of Influence and Lobbying of Shipbuilders, that the Navy contractors, subcontractors, and suppliers constitute a very large and influential financial group.

The committee finds that three big shipbuilding companies had \$53,744,000 of work at stake in the Geneva Disarmament Conference which the Navy had given to them a few months before the opening of the conference in 1927. It notes the admitted interest of the companies in the unfavorable outcome of that conference. It notes Mr. Shearer's testimony that he was urged to go to the conference by Admiral Pratt, and was supplied with secret Navy information. It notes the secrecy of his employment by the shipbuilders, and the explanation for that secrecy. It notes his activities in the promotion of a war scare with England in 1928 and 1929, while being paid by the shipbuilders. It notes certain discrepancies between testimony given by the shipbuilders at the Shortridge hearings and the hearings of the Munitions Committee. It notes Mr. Shearer's claim that "as a result of my activities, eight 10,000-ton cruisers are under construction." Further, that owing to the failure of the tripower naval conference at Geneva, there is now before the Seventieth Congress a 71-ship building program costing \$740,000,000. It notes Mr. Shearer's further testimony of his activities at the request of various Naval officials. It notes his description of his Geneva campaign as "fast and vicious." It notes his report at the "delight" of the shipbuilders at the result. It notes the payment by the shipbuilders of the costs of a pamphlet he wrote attacking certain private citizens, including Newton D. Baker and Franklin D. Roosevelt. It notes the payments he received from Mr. Hearst of \$5,000 in 1929. It notes the spreading through a friendly newspaper syndicate of an alarmist story concerning alleged Japanese intentions by the president of the Bath Iron Works, with the intent and result of activity by a Senator and Representatives from Maine in connection with an appropriation bill in 1932.

The committee finds, on the basis of this and other testimony, that there is a clear and definite danger in allowing self-interested groups, such as the shipbuilders and their allied interests, to be in the close position of influence, as they are at present, to such an important instrument of national policy as the Navy is, and the danger in allowing them to remain in a position where it is to their financial interest to confuse public opinion between the needs of the country for a purely defensive Navy and their own continued needs for profits.

The committee finds, further, that there has been a large amount of bipartisan political activity on the part of the shipbuilders locally, in Congress, and also at the national headquarters of the two parties. It makes no claim to have gone into this field thoroughly. The committee notes the claims of the Washington representative of United Drydocks in 1934 that he could get a bill through Congress for \$50,000. and that "there is no virtue in being quixotic at this state." It notes the placing of Congressmen on certain committees at the request of the shipbuilders. It notes their claim to have helped the Navy on certain bills and to have elected Members to the House Rules Committee. It notes the reference to United Drydock Co. securing through Dave Hogan, secretary to Mr. McCooey, prominent Brooklyn Democrat, the award of \$6,800,000 in destroyers in 1933.

The committee finds that the matter of national defense should be above and separated from lobbying and the use of political influence by self-interested groups and that it has not been above or separated from either of them.

The committee finds, further, under this head, that the main lobby for the Merchant Marine Act of 1928 was conducted by the shipbuilders under the leadership of Mr. Laurence R. Wilder, then president of American Brown Boveri (New York Shipbuilding Co.), and that a sum of over \$140,000 was spent in putting that bill over.

The committee finds further that New York Shipbuilding Co. was acquired as a speculative investment by the Bragg-Smith-Cord interests just prior to the 1933 naval awards; that the present owners are not experienced shipbuilders and have since tried to divest themselves of the ownership, and that it is not a satisfactory situation to have such an important part of our potentially necessary national defense in the hands of people who are willing to sell it to the first bidder. Speculators and speculation should have no place in our national defense.

The success of the shipbuilders in securing an allocation of \$238,000,000 for shipbuilding from Public Works Administration funds has been their most recent demonstration of power. In this their purpose was aided by labor groups who later, when the expected employment failed to materialize, spoke of the matter as a "double cross" to the Navy officials who had solicited their support for the measure.

G. ATTEMPTS TO LIMIT PROFITS

The committee finds, under the head of Attempts to Limit Profits, that the failure of the Navy Department to turn the navy yards into effective yardsticks by which the charges of private shipyards could be measured and kept down, has resulted in leaving the profits of the shipbuilders practically uncontrolled.

The committee finds that the Vinson-Trammell bill of 1934 limiting profits to 11.1 percent of cost cannot be enforced without a huge police force of accountants and that disputes concerning its interpretation, similar to those which delayed the payment of wartime taxes by the companies for 12 years may confidently be expected.

The committee finds that the Navy's grant of adjusted price contracts in 1933 with limitations on the amount of risk the Government assumed for the benefit of the shipbuilders and in 1934 without any

limitation on the Government burden for increased costs has resulted, in effect, in cost-plus contracts. It finds these cost-plus contracts more profitable than the wartime contracts when only a 10-percent profit over cost was allowed.

The committee finds that in the case of the 1934 adjusted-price contracts on light cruisers, destroyer leaders, light destroyers, and submarines, the Government has assumed all the risk of increasing prices, and has lowered the risk for which the companies received 11.1-percent profit by an enormous amount.

The committee finds that the Navy, which has no responsibility for enforcing the act, and which has no reliable figures about private costs, is in a position to allow—and according to one company has actually allowed—increased overhead charges, which can invalidate the whole attempt by Congress to limit profits. The committee notes that it was by the allowance of such theoretical overheads during the war years above actual overheads that New York Shipbuilding Corporation was paid \$2,152,976 more by the Government than it actually paid out itself.

The committee finds that the shipbuilding industry and its sub-contractors and suppliers have united in efforts to find ways to avoid the incidence of this law, and that Mr. Gillmor, president of Sperry Gyroscope, Navy suppliers, told them, "If the shipbuilders, boiler manufacturers, and electrical manufacturers act in accordance with uniform rules, it will be so strong I think the Income Tax Bureau will have a hard time resisting it." The committee notes the unreliability of the shipbuilders' figures as indicated by the wide differences between their wartime reports and the audits of those reports by the Treasury (sec. VIII). It notes also in this matter of reliability the recent discrepancy of almost \$2,000,000 out of a profit of \$2,900,000 in the reports furnished by the New York Shipbuilding Co., passed on by the National Council of Shipbuilders and circulated recently among congressional committees by Navy officials. It also notes in this matter the evidence tending to show that the Bath Iron Works transferred an item of \$60,000 incurred on a lighthouse tender to the costs of the destroyer *Dewey*.

The committee finds that there is no enforcement of the profit limitation law in effect until 4 years after the beginning of a cruiser. It finds, from wartime experience (sec. VIII) enough evidence of the difficulty of auditing thousands of old vouchers and of properly allocating overhead which the companies may have improperly saddled onto Navy vessels, to declare that there is no effective profit-limitation law today.

It finds the price of real enforcement of the attempts of Congress to limit profits to be a costly policing force of accountants and auditors who would be in the yard for at least 3 years, and a series of costly lawsuits after those audits have been completed. It finds that the only way to prove that a company had not improperly allocated overheads from commercial jobs onto Navy jobs would be to audit all the commercial jobs being done by a private yard as well as the Navy work; in short, to audit all the work done by the yard and to establish uniform accounting.

The committee questions whether this additional cost for auditing and policing, plus the cost of lawsuits after such audits, on top of the 1 to 2 million dollars extra cost of private construction, and the \$300,000 spent by the Navy for inspection of the privately built

cruisers, justify the continuance of private yards as naval contractors. They have the appearance of being expensive luxuries.

The committee reserves decision on this phase of the matter until the completion of its investigation of the costs of governmental construction.

H. WARTIME ATTITUDE OF SHIPBUILDERS

The committee finds, under the head of Wartime Attitude of Shipbuilders, that the record of the present shipbuilding companies during the war, wherever examined, was close to being disgraceful.

They made very considerable profits. On Treasury audits they showed up to 90 percent. They secured cost-plus contracts and added questionable charges to the costs. They took their profits on these ships after the wartime taxes had been repealed. They secured changes in contract dates to avoid war taxes. They bought from the Government, very cheaply, yards which had been built expensively at Government costs. In one case this was prearranged before the yard was built. One yard did not build necessary additions until it was threatened with being commandeered. Knowingly exorbitant claims were filed against the Government for cancellation. Huge bonuses were paid to officers. Profits were concealed as rentals.

After the war was over keels for \$181,247,000 worth of destroyers were laid, which was probably the largest post-war favor done by any Government to any munitions group.

The committee finds no assurance in the wartime history of these companies to lead it to believe that they would suddenly change their spots in the case of another war.

After the committee's hearings on shipbuilding had closed, Gen. Hugh Johnson, at one time connected with the War Industries Board, later with B. M. Baruch, and later Director of the National Recovery Administration, explained that the N. R. A. had grown out of the plans developed by the War Department for the conduct of a future war. It was, he stated, developed directly from the war plans and was not shown to the industrialists for their approval until practically completed. In view of this statement, the committee finds significance in the testimony of a Department of Labor official concerning the unwillingness of the New York Shipbuilding Co. to observe the N. R. A. rules, with the result of a serious labor dispute in 1934. The company did not raise the question of constitutionality, and all that was involved was the question of observance or evasion of the law.

The committee finds in this evidence, taken together with the actual wartime experience of the Government with these companies, little hope for obedience by them of more stringent wartime provisions in the case of another emergency.

The committee especially holds that the attempts to enforce profit limitation are being thwarted, and in view of that fact and the fact that peacetime precedents are now being established in the course of attempts to avoid the enforcement of profit limitation, and in view of the probability that the peacetime procedure will govern tax cases during any war, the committee refers to section VII, Attempts to Limit Profits of the Report on Naval Shipbuilding, and wishes to incorporate a portion of that section in this report.

ATTEMPTS TO LIMIT PROFITS

The failure of the Navy Department to turn the navy yards into effective yardsticks by which the charges of private shipyards could be measured and kept down has resulted in leaving the profits of the shipbuilders practically uncontrolled.

In 1933 and 1934 the companies secured contracts from the Navy Department whereby the companies are indemnified by the Department for rises in the cost of labor or materials. In other words, they made the Government bear a large share of whatever risk there was in the business.

The companies knew that the Navy Department needed the ships and frankly stated that they were bidding so high on a fixed-price basis as to make it impossible for the Navy to accept those prices. (Testimony of Ferguson, p. 5468, Feb. 20; Wakeman, p. 5930, Feb. 28.) To the extent that the Navy needed those yards, this was a very effective method of forcing the Government to bear a large share of the risk, something it had never done before, except during the war.

The allowances for increased prices were quite unequal in various categories of ships. In 1933 there was a limitation of 15 percent on the amount the Government would pay for increased prices on labor and material on light destroyers. On the two aircraft carriers, however, which were contracted for at \$19,000,000 each, the limitation was \$4,000,000, or 21 percent.

In 1934 the Navy went further and took off all limitations. The light cruisers, destroyer leaders, and light destroyers, as well as the submarines, were all contracted on an adjusted-price basis without any limitation on the amount of risk the Government would have to carry for the benefit of the shipbuilders.

In 1934, before the Navy took off all these limitations, and by so doing practically underwrote the companies and did the gambling for them, the Congress had passed the Vinson-Trammell bill, which was intended to limit the profits of the shipbuilders to 11.1 percent of actual cost (10 percent of the total charge to the Government).

Various of the companies stated on the stand that they had in no way opposed this bill.

Very shortly after the bill was passed the shipbuilders and the large suppliers and Navy subcontractors, and later the comptrollers of these various groups, got together in long sessions to determine how the interpretations of the bill could be arranged to suit their interest. The main question was how to increase costs.

It will be remembered (sec. IV) that the Navy has no information at all about costs in private yards. Neither the Comptroller General nor the Treasury have examined the costs, ratios of overhead, etc., since the war.

The law provides that all profits over 11.1 percent shall go into the Treasury. A ship takes from 2 to 3 years to build. Another half year passes before adjustments resulting from the final trials are made. Another half year elapses before the company puts the final figures of cost and profit on its books. Three or four years have gone by at the time the profits are reported to the Treasury on any particular ship.

The Treasury is not expected to be willing to put auditors to work to go through 4 years of vouchers, or to analyze the accuracy of a company's statement that 60 or 90 percent of all the overhead in its yard should be allocated to a naval ship.

There is absolutely no effective control of costs possible without a huge policing system of auditors and inspectors constantly on the premises.

Some indication of the awareness of the shipbuilding companies of this fact is given in the abstracts of testimony quoted below taken from the minutes of their meetings.

Mr. Powell, president of United Drydocks, pointed out that "the thing will go along all right until somebody turns back some money." Mr. Smith, president of the trade association, thought it important to get unanimity on the large subject of overhead. Mr. Gillmor, president of the Sperry Gyroscope Co., Navy suppliers, said: "If the shipbuilders, boiler manufacturers, and electrical manufacturers act in accordance with uniform rules, it will be so strong that I think the Income Tax Bureau would have a hard time resisting it."

The Navy Department disclaims all intent to enforce this bill, since the duty to collect the taxes is laid upon the Treasury Department. Nevertheless, according to the minutes, Mr. Blewett, of Newport News, informed the associated groups that the Navy had allowed his company an increase in overhead of 10 percent on changes. How the Navy could allow this while in complete ignorance of all the figures concerning the company is hard to understand.

Later Mr. Ferguson, of Newport News, testified that an addition to plant of \$900,000 was being put into the overhead of the two aircraft carriers. This is already an increase of over 2 percent in the total of \$38,000,000, or 3 percent on the expected actual cost to the company.

If this practice of allowing larger overheads for Navy work continues, it should be noted that an additional 10-percent overhead for Newport on the two aircraft carriers would equal \$2,000,000, a sum equal to more than 5-percent profit.

In this connection it is interesting to note (sec. VIII) that an arbitrary allowance made by the Emergency Fleet Corporation in 1918 of an overhead of 50 percent was \$2,152,976 more than that actually paid out by the New York Shipbuilding Corporation (Jan. 21).

Presumably the Treasury would have to allow any increase claimed overhead approved by the Navy.

The Navy has no responsibility in the matter of this profit-limitation law, but its decisions can completely invalidate the act.

The intent of the shipbuilders to get an agreement on a theoretical overhead instead of an actual one can be seen in the statement by Mr. Shick, of Bethlehem:

We should decide what we are going to do. For our own protection it would be a good thing if we did have an understanding so that on the completion of these contracts the overhead rate will not be out of line. If Bethlehem had 60 percent, Newport News 50 percent, and somebody else 40 percent, they will ask what is wrong. Therefore, it is important for the shipbuilders to have a very clear definition as to what is direct labor if that is the base of distributing overhead. I believe we can agree on a definition of direct labor (p. 5094).

The shipbuilders asked the Treasury Department to allow them to charge State income taxes and selling expenses into costs. E. I. du Pont de Nemours asked the Treasury Department to allow these items and also Federal income taxes and unemployment-insurance costs.

The shipbuilders arranged to have the subcontractors charge them no more for work than cost plus 10 percent. Instead of turning the difference over to the Treasury, it is in effect turned over to the shipbuilder, thus giving him a larger margin of profit on which to operate.

The reliability of the shipbuilders' figures was already referred to in section IV, where almost \$2,000,000 in profits was not mentioned by the shipyard in a comparison of the cost to the Government of the *Chester*. On certain claims after the war, the president of Newport News filed a bill against the Government for \$14,973,165 at the same time he was writing the president of the company that the minimum claim was \$6,635,000.

There is some evidence that Bath Iron Works transferred an item of \$60,000 incurred on a lighthouse tender and a tug to the destroyer *Dewey*. The ability of companies to do this has a bearing on all attempts to limit profits.

Abstracts of this evidence are given below.

The discussion by the shipbuilders of the provisions of the Vinson-Trammell bill in limiting profits to 11.1 percent of cost was referred to during the testimony of Mr. Parker, of New York Ship (Feb. 6, (p. 5090 seq.):

Mr. RAUSHENBUSH. Now, Mr. Parker, coming to the various meetings held by the shipbuilders after the Vinson Act had been passed, I show you a memorandum, treating of a meeting held on May 8, 1934, and ask you to follow that, at which were present the representatives not only of the "big three" but from the "little three" and suppliers, such as United Dry Docks, Sperry Gyroscope, Babcock & Wilcox, Worthington Pump & Machinery, Westinghouse Electric, General Electric, Electric Boat Co., and so forth [handing paper to witness]?

That is the summary of a discussion, is it not, that the representative officials of the shipbuilding companies and the main suppliers had concerning the effect of the Vinson bill on their business? Do you recognize that?

Mr. PARKER. I did not attend that meeting.

Mr. RAUSHENBUSH. No; but you attended a subsequent meeting, for which this was the basis. You have had this in your possession, have you not?

Mr. PARKER. Yes.

Mr. RAUSHENBUSH. And you have studied it? The answer is "Yes"?

Mr. PARKER. Yes.

Mr. RAUSHENBUSH. I turn to page 4, where there is discussion of how much overhead should be allowed, and discussion as to what the Treasury Department will do, and what the Navy Department will do. It refers to Mr. Smith. He is president of the council, is he not?

Mr. PARKER. Yes.

Mr. RAUSHENBUSH (reading). At the top of the page, Mr. Smith says:

Yes. That is where it is going to be unless there is a change in the law. The Navy Department does not want to deal with it.

Mr. GILLMOR. They do not want to get into it.

Mr. SMITH. The man who drafted this bill drafted it with the purpose of allowing some leeway.

Mr. KING—

of Babcock & Wilcox—

Are you going to be allowed your actual expense? Will they allow the actual overhead or a predetermined one?

Mr. SMITH. I think you can collect your actual overhead as long as it goes against all work.

Mr. GILLMOR—

of Sperry Gyroscope—

They point to this provision in the act that the contractor must make his statement under oath.

Mr. NIVEN—

of General Electric—

They go on to say that the books shall be open for inspection at all times.

Mr. GILLMOR. I believe their present idea is to make check inspections only.

Mr. POWELL—
of United Dry Docks—

This thing will go along all right until somebody turns back some money.

Mr. GILLMOR. I think the only thing to do is act in unison.

Mr. SMITH. Supposing you do have 10-percent profit and a few dollars left over. The industry may find itself in a situation where there are items of cost which could have properly gone in but were not included. It seems to me very desirable that so far as the outstanding items of overhead are concerned there should be unanimity of opinion.

Does not that give pretty much the tone of the general discussion? The shipbuilders here wanted to get together and decide very definitely what proportion, predetermined proportion, they would agree upon as an overhead charge.

Mr. PARKER. No, sir; I do not think that is the case at all. I think that what the shipbuilders and the main material suppliers were trying to find out is what the Vinson Act meant so far as their particular business is concerned.

Mr. RAUSHENBUSH. Let us follow on with the rest of it through and see where we come out.

Turn, please, to page 7, Mr. Parker. They are starting to discuss overhead, as I understand it [reading]:

Mr. SMITH. When you say "actual", I suppose you mean your actual average—

Of General Electric—

Mr. WHITSTONE. No; I mean actual expenditures.

Mr. SMITH. As supplied to that particular contract?

Mr. WHITSTONE. In the case of shipbuilding, it will probably apply to a whole ship.

Mr. SMITH. If you had one plant using actual and another normal—

Mr. POWELL. Suppose three or four yards take contracts on a competitive basis. Then one fellow turns in actual and has a very low overhead and he turns back a lot of money—it simply throws out your whole idea of competitive bidding. It seems to me you have almost got to come to a basis of agreeing with the Treasury Department on some fixed overhead. If we could spread our overhead over 10 years, I would say it would be high enough. I think it would be high enough so that you would not have to worry about your 10-percent profit. The average overhead would be plenty high enough to satisfy anybody.

They are beginning the discussion, or resuming it, are they not, of trying to agree on a fixed percentage of overhead that all companies could charge, and that the Treasury would have to approve?

Mr. PARKER. These expressions, Mr. Raushenbush, are expressions of individuals thinking of their own particular business, how this act affects their own particular situation, but the purpose of it all was to find out how it affected everybody, and particularly how it affected the prime contractor, the shipbuilder.

Mr. RAUSHENBUSH. Turn to page 8 in reply to that [reading]:

Mr. SMITH—

President of this conference and of the council—

What is your reaction to this: You have the shipyards and the allied groups, but your uniformity should be attained first amongst the shipbuilders themselves and then there can be some approach to uniformity between the shipbuilders and the allied groups.

Mr. GILLMOR. If the shipbuilders, boiler manufacturers, and electrical manufacturers—

That is taking in a rather large group, is it not?—

act in accordance with uniform rules, it will be so strong that I think the Income Tax Bureau would have a hard time resisting it.

Is not that the reasonable idea of this whole matter, that not only the shipbuilders but the operators who have a definite interest in the work and in the Vinson bill should get together and put up uniform rules; and is it not Mr. Gillmor's idea that if they do that they will be so strong that the Income Tax Bureau will have a hard time resisting it? Is that not what they are trying to do there?

Mr. PARKER. They were trying to find some way by which those elements of actual cost would be unquestioned by the Treasury Department.

Mr. RAUSHENBUSH. Now, on the next page, Mr. Parker, Mr. Bardo comments after this statement [reading]:

If the shipbuilders, boiler manufacturers, and electrical manufacturers act in accordance with uniform rules, it will be so strong that I think the Income Tax Bureau would have a hard time resisting it.

Mr. Bardo comments:

They could not break it down. You have two established recognized systems of accounting in the two principal groups with which we do all our business. We should get our accounting offices together. I do not think we can decide anything.

Mr. Bardo, a little later, says:

I think we should get the shipbuilders together first on a uniform plan.

Mr. SMITH. Homer—
of Bethlehem—

what do you think about it?

Mr. HOMER. The method of determining the 10-percent profit is to be established by the Treasury Department, and the obvious thing is that the industry will have to establish something for its protection.

Mr. JACKSON—

Worthington Pump & Machinery Corporation—

They can establish it, but the Treasury Department will have to approve it. And the whole discussion turns, as I look at it, on whether it is possible for the shipbuilding companies to get any agreement, and they decide that the controllers of the companies better meet together, and then you and others meet directly a little later, at the same place—11 Broadway. You were present for New York Ship, together with Mr. Langell; Mr. Ferguson was present for Newport News, and Mr. Shiek and Mr. Harper and Mr. Rittor for Bethlehem Shipbuilding Corporation, Ltd.

Mr. PARKER. That is correct.

Mr. RAUSHENBUSH. I do not know whether I have an extra copy of this. I want to offer that for the record—the meeting of the shipbuilders—as Exhibit no. 1531.

(The document referred to was marked "Exhibit No. 1531" and is included in the appendix.)

Mr. RAUSHENBUSH. Turn now to this meeting at which you were present, and at which the subject was gone into further, and Mr. Blewett, of Newport, makes a comment here on which we would like to have your comment. I will have to show you this until we find our extra copy [handing paper to witness].

On page 3 of this mimeographed memorandum, Mr. Blewett says:

We have recently gone through the cost of changes. We asked a higher overhead on the changes than on normal overhead. We asked for 20 points higher and they granted us 10.

He means the Navy granted them 10, does he not?

Mr. PARKER. I assume so, speaking of Navy changes.

Mr. RAUSHENBUSH. Speaking of Navy changes [reading]:

In other words, they admitted naval work called for higher overhead than commercial work. If we could obtain 20 percent higher it would cover everything such as equipment, development charges, and all items. So far as going into a uniform cost-accounting system, that is a job of 5 or 10 years rather than a months or so.

You remember this meeting fairly well, do you not?

Mr. PARKER. I do.

Mr. RAUSHENBUSH. Mr. Blewett, speaking for Newport News, was trying constantly to make the point, was he not, that the shipbuilders should definitely agree upon an overhead that was normally uniform but was very considerably higher for Navy work than for merchant marine work? Is that not correct, so far as your memory goes?

Mr. PARKER. Mr. Blewett was trying to make the Navy work bear an actual proportion of overhead which Navy work should bear. It is a fact that with all of the limitation of Navy work, inspection and various changes and consequential damage from changes, the actual overhead applicable to Navy work is truly higher than to other work, and when you spread that to all work on the same basis, Navy, of course, gets the benefit and the other work gets some penalty.

Mr. RAUSHENBUSH. He was trying very definitely to get it on a fixed basis higher than other work, 20 percent?

Mr. PARKER. Yes, sir.

Mr. RAUSHENBUSH. He reports Newport News asked for 20 and had gotten 10 and was apparently suggesting that the other companies agree on their overhead, too. That, of course, involved an agreement on what labor was, so that overhead could be determined.

Here is a copy, if you want to follow it [handing paper to witness].

Mr. Smith at page 6 shows some considerable anxiety that everything is going to be put into cost by everybody, so that some of the shipbuilders do not charge the Government too little. Mr. Smith says:

I would not do that. This group ought to go away satisfied as to what items get into cost. Each and every one of us should be assured that we are going to put into cost everything that properly belongs there.

In other words, they do not leave out anything, and not, as Mr. Gillmor said in the other meeting, so that some money does not get returned to the Government and then the Government forces them to get into action.

Can you explain the comment on page 7 of Mr. Shick, of Bethlehem, where Mr. Blewett said:

Didn't we have such a thing as adjusted prices during the war? We took such things as cost of machinery and put it into an adjusted price.

To which Mr. Shick replied:

That was a cost-plus contract. You only got 10 percent of it. I can give you an example of what happened on a gun contract. The Navy wanted a 16-inch gun. We had to buy the equipment to machine it. Daniels—

that was the Secretary of the Navy, was he not?

Mr. PARKER. I suppose that is who he is speaking of.

Mr. RAUSHENBUSH (continuing reading):

said, "All right, this is not the last order we are going to give you for 16-inch guns. We will let you add \$35,000 per gun so you can amortize this equipment. We will let you amortize part of the cost through this job so you will get paid for your new equipment, but you have to take a little chance."

They did that for the reason they did not want to say to us, "We will pay you for this." If they did, then they would own it, but they wanted it to stay in our possession. We were only amortizing \$35,000 on that job.

Do you have any comment on that? Does it mean anything to you?

Mr. PARKER. No.

Mr. RAUSHENBUSH. It seems to be an illustration of where the Government was paying very definitely for the equipment, but just because they did not want to own it they let the gun people, in this case Bethlehem, charge up an extra \$35,000 per gun and amortize it immediately.

The discussion goes on at some length, and the net result of all this was that there was an interchange of information among the companies, was there not, as to definitions of their costs as regards direct labor and overhead?

Mr. PARKER. That is correct.

Mr. RAUSHENBUSH. On page 12 Mr. Shick, of Bethlehem, makes one point:

We should decide what we are going to do. For our own protection it would be a good thing if we did have an understanding so that on the completion of these contracts the overhead rate will not be out of line. If Bethlehem had 60 percent, Newport News 50 percent, and somebody else 40 percent, they will ask what is wrong? Therefore, it is important for shipbuilders to have a very clear definition as to what is direct labor if that is the base of distributing overhead. I believe we can agree on a definition of direct labor.

After that these interchanges of information took place, did they not?

Mr. PARKER. They did.

Mr. RAUSHENBUSH. So that the point of all of this was, Mr. Parker, quite frankly, to have the shipbuilders agree on something that was not an actual cost that came out of it—and if that was so they would not need any agreement—but they agreed on a perfectly arbitrary amount of overhead, which they would unite on in trying to have the Treasury Department accept as a basis for fixing profits under the Vinson Act, thereby agreeing or following out the suggestion made by Mr. Gillmor in the earlier meeting that if they all got together they would be stronger than the Income Tax Bureau.

Mr. PARKER. Not at all. That is not my understanding.

Mr. RAUSHENBUSH. If that is not true, what is your understanding?

Mr. PARKER. I never heard the theory advanced that there should be a definite rate of overhead applied to every yard alike.

Mr. RAUSHENBUSH. They were certainly discussing the possibilities of it all through here, were they not?

Mr. PARKER. No; the only discussion that this refers to is that the books of each of the companies will reflect the actual and proper charges to cost that the contract provided, so that in any one of them, if they should inadvertently submit some cost, or by his method, or changing his method so that it would result in a question for the whole group. But only, of course, included those items which are proper elements of cost.

Mr. RAUSHENBUSH. What is all this discussion about as to fixed percentage of overhead, Mr. Blewett's idea that they asked for 20 percent for naval work; that is an arbitrary thing, rather than an actual one?

Mr. PARKER. That is on changes, alone, Mr. Raushenbush.

Mr. RAUSHENBUSH. That is on changes?

Mr. PARKER. The practice has always been on changes to fix a definite rate of overhead.

Mr. RAUSHENBUSH. These are changes, but, still, changes often amount to a very considerable amount in the cost of a ship, do they not?

Mr. PARKER. Yes, sir.

Mr. RAUSHENBUSH. In some cases a million dollars more than what the bids were.

Mr. PARKER. What Blewett was talking about was just a rate of overhead which was a proper rate of overhead. We already have a fixed rate of overhead applicable to changes, fixed by the board of changes.

Mr. RAUSHENBUSH. On page 4, if you will follow that—

Mr. PARKER. Back again?

Mr. RAUSHENBUSH. It gets into the normal overhead, and Mr. Bates, of United Dry Docks, says:

You mean a standard or normal overhead?

Mr. BLEWETT. Yes.

Mr. SMITH. Let me ask you this, Blewett: You say you asked for so many points higher; would you do that on the basis of each plant saying here is my average overhead, we want 20 points higher for naval work taking into account no two plants might have the same?

Mr. BLEWETT. Yes.

Mr. SHICK. Only if you get it high enough.

Mr. SMITH. That is the point where I see difficulty with the Government.

They are talking about overhead for naval jobs rather than for changes at that point, are they not?

Mr. PARKER. No; I believe they are still referring to changes.

Mr. RAUSHENBUSH. There is no mention of changes right at that point.

Then later on in the quotation I read from the Bethlehem man he was particularly talking about the general overhead rather than the changes, was he not?

Mr. PARKER. I do not know what he was talking about particularly.

Mr. RAUSHENBUSH. On page 12. Look at it again. All the way through—I do not want to bore the committee with reading the whole story, but I want to put it into the record.

By the way, what percentage of overhead did the Navy board on changes allow you on changes in ships before this bill went through?

Mr. PARKER. It varies. Periodically the Navy makes an investigation of the actual overhead of the plant and sets a rate of overhead to be used on changes. The rate varies with the average variance of overhead rates in the yard generally, some place between 70 and 90 percent.

Mr. RAUSHENBUSH. Do you not make quite a lot of money on changes?

Mr. PARKER. No, sir; we do not make money on changes. No one ever made any money on changes. The consequential damages and delay due to the interruption of work, which are never paid for, make changes the most unprofitable part of Government work.

Mr. RAUSHENBUSH. The changes are all paid for, are they not?

Mr. PARKER. The changes and the actual material, but no one can collect consequential damages.

Mr. RAUSHENBUSH. You are taking in a lot of territory when you say no one makes any profit on them. You mean your own company?

Mr. PARKER. I mean my own company, and am sure the business of the other companies are so closely related that their situation is identical.

Mr. RAUSHENBUSH. I will offer this as exhibit no. 1532.

(The document referred to was marked "Exhibit No. 1532" and is included in the appendix.)

Mr. RAUSHENBUSH. The upshot of all this was several things, was it not, Mr. Parker? The companies got together and agreed on what they wanted to ask of the Treasury Department, and, in addition to any informal conversations they had with the Treasury Department, they did ask for several specific changes. They asked the Treasury Department the allowance for the income taxes, did they not?

Mr. PARKER. I believe a brief was filed by the National Council requesting that.

Mr. RAUSHENBUSH. That is the protest of the National Council of American Shipbuilders on rulings of the Commissioner of Internal Revenue excluding State income tax as items of cost? There was a definite protest on that, and they wanted selling expenses as a proper item, did they not?

Mr. PARKER. Correct.

Mr. RAUSHENBUSH. They also made a point about compensation insurance. That was all touched on in the conversations with the Treasury Department and any other arrangements that had been made. Then we find here a letter from the du Pont Co. as to the Vinson Act, together with comments from the National Council of American Shipbuilders, in which the du Ponts say that in addition to all the items that the shipbuilders wanted charged into the costs under the Vinson Act, they also want to have Federal income taxes. Do you remember that?

Mr. PARKER. I remember reading the letter.

Mr. RAUSHENBUSH. They wanted to charge the State income tax in, the Federal income tax; they wanted to charge unemployment insurance costs in. So that they went you one better, a little bit, did they not? You people were not asking for the inclusion of Federal income taxes any longer as an item of cost, were you?

Mr. PARKER. No.

Mr. RAUSHENBUSH. This was the du Pont idea, and they included it in a letter to the Bureau of Internal Revenue, explaining why they wanted to have that allowed under the Vinson Act. I offer that series of correspondence for the record as exhibit no. 1533.

(The documents referred to were collectively marked "Exhibit No. 1533" and are included in the appendix.)

Mr. RAUSHENBUSH. Then, Mr. Parker, you worked out yourself, did you not, a way of handling the subcontractors under the Vinson Act, a way of seeing that they never made more than 10-percent profit?

Mr. PARKER. No; I would not say that I worked it out myself.

Mr. RAUSHENBUSH. Who else gets credit for it?

Mr. PARKER. I think it is a composite idea which several people contributed to.

Mr. RAUSHENBUSH. Could you describe that very briefly, what you had in mind when you tried to do that?

Mr. PARKER. The Vinson Act, in attempting to limit the profit to 10 percent—and I am fully in accord with the limitation of profit—does not guarantee 10 percent nor does it prevent you from sustaining a loss of 10 percent, 20 or 50 percent. The Vinson Act, as we understand its intent, is a profit-limitation matter, but it intends to limit the profit of the contractor and requires that contractor to require of all his subcontractors an agreement to the same profit limitation that the contractor subscribes to. The problem was to find a way by which the intent of the act or the profit limitation could be passed on to the subcontractors who were limited in profit in the same manner that the contractor was.

It naturally occurred to several of us that if the subcontractor did not earn in excess of 10 percent, the act was not at all detrimental to him; that under the various codes most industries were permitted to sell at cost, and prohibited from selling at less than cost, and it seemed that since the Vinson Act is, in itself, a cost-plus contract, regardless of the so-called "topside price", which is subject to much adjustment, it is, nevertheless, in the final analysis, a cost-plus contract, and that the contractor having a cost-plus contract on his hands, would necessarily have to make his subcontracts on a cost-plus basis.

Mr. RAUSHENBUSH. Just explain that one point once more, why you say the Vinson bill is a cost-plus contract. How do you figure that, Mr. Parker?

Mr. PARKER. The Vinson Act is a cost-plus contract, unquestionably, because what you finally receive is cost, as determined by the Treasury Department.

Mr. RAUSHENBUSH. Now you are talking, are you, about the bids put in under an adjusted-price basis?

Mr. PARKER. I am talking about any contract under the Vinson Act. The amount that any contractor or subcontractor can receive under the Vinson Act

is his cost—that is, the maximum he can receive—is his cost plus 10 percent of his contract price.

Senator BONE. There is no guarantee of that in the bill, is there?

Mr. PARKER. That is the maximum he can receive.

Senator BONE. I understand; but there is no guarantee of that in the bill, is there?

Mr. PARKER. The bill provides that that is exactly what he can get as a maximum.

Senator BONE. The bill provides that he may not get more than 10 percent?

Mr. PARKER. That is right.

Senator BONE. That is the provision of the bill?

Mr. PARKER. That is right.

Senator BONE. That does not guarantee him it.

Mr. PARKER. Not at all. He has no guarantee of 10 percent.

Senator BONE. It is not really a cost-plus contract.

The Navy Department does not undertake to enforce the profit-limitation section of the Naval Act (Feb. 21, p. 5593 et seq.).

Senator CLARK. What I am referring to is the suggestion by Senator Vandenberg, where the Chairman of the Naval Affairs Committee of the Senate wrote the Navy and called attention to this rising scale, shown by the chart, and said that the bids submitted were absolutely exorbitant and a fraud upon the Government, and within a day or two the Secretary of the Navy wrote back to him and told him he was entirely in error and the bids were entirely fair. Unless he was able to determine these various items entering into the increase of cost, I do not see how he could possibly have been in a position to make that answer.

Senator VANDENBERG. Captain, how can you administer the 10-percent profit limitation which is now in the law, unless you have accurate information respecting the cost items, for proving anything before the 10-percent profit is attached?

Captain DuBOSE. The Navy Department will make no attempt whatsoever to ascertain or determine anything in connection with this 10-percent profit. It is incorporated in the contracts, but it is a matter between the shipbuilder, the contractor, and the Bureau of Internal Revenue of the Treasury Department.

Senator VANDENBERG. Then the 10-percent protection in fact is no real protection, so far as the Navy Department is concerned?

Captain DuBOSE. I would not say that; no—because very definitely under the law they limit the profit to 10 percent.

Senator VANDENBERG. But if the shipbuilder put \$1,000,000 into cost, which does not belong there, then what?

Captain DuBOSE. The Internal Revenue people have a perfect right to examine the books of the shipbuilder.

Senator VANDENBERG. Do you mean by that you rely upon the Internal Revenue Department for the integrity of the 10-percent clause in the naval bill?

Captain DuBOSE. There is no possible way for the Navy Department to do anything else.

Senator VANDENBERG. And you do not attempt to do anything else?

Captain DuBOSE. And we do not attempt to do anything else except to provide in the contract the provision of law which is to be taken care of as an administrative procedure by the Internal Revenue Department.

Senator CLARK. Captain, do we understand that the Navy Department feels there is no reason whatever for enforcing the law as to 10-percent profit, except as included in the contract?

Captain DuBOSE. The thing, I state, was agreed upon in a conference between the Navy Department and the Treasury Department. We did not adopt that policy without discussion. There were conferences held between representatives of the Navy Department and the Treasury as to how this thing could be done.

Senator CLARK. But in expending the funds allotted to the Navy Department, either by act of Congress, Public Works authority, or anybody else, the Navy Department has no actual responsibility for determining the cost basis upon which this 10-percent profit is to be figured? Is that what I understand?

Captain DuBOSE. It has been agreed upon mutually by the Navy Department and the Treasury that that particular duty would be taken care of by the Treasury for the Government and not the Navy.

There was further indication that the Navy takes no responsibility for the enforcement of profit limitation (Feb. 21, p. 5595, et seq.).

Senator VANDENBERG. What happens, Captain—let us make this specific and suppose this is a 10-million-dollar cruiser which is being built under contract at a private yard, and this provision of law limits the profit to 10 percent or \$1,000,000. Now, when this private shipyard sends you its costs, do you accept the costs as submitted by the shipyard as valid? In other words, does the shipyard determine what the costs are?

Captain DuBOSE. The shipyard determines what the costs are, yes, sir; and that information is transmitted to the Secretary of the Treasury, and if he thinks it advisable or necessary to investigate in detail, he has that right.

Senator VANDENBERG. Do you know whether he ever does investigate?

Captain DuBOSE. We have had no contracts with this excess-profits clause in it—there are a few—

Senator VANDENBERG. So far as the Navy Department is concerned, it takes no responsibility for the integrity of the calculation which finally leads to the 10-percent profit?

Captain DuBOSE. The Navy Department has nothing whatever to do with the detailed method that a shipbuilder follows in determining his costs. He determines his costs. He submits the statement under oath, and it is then examined by the Treasury Department.

Senator VANDENBERG. And that is satisfactory to the Navy Department, and that ends it, when he files his costs under oath?

Captain DuBOSE. It ends it as far as the Navy Department is concerned, but it does not end it as far as the Government is concerned because the Secretary of the Treasury has got to do something.

Senator BONE. Do you know any statutory provision which authorizes them to go into the operating overhead on the naval contracts?

Captain DuBOSE. The Vinson Act provides that for all contracts placed after the date of that act.

Senator BONE. There is nothing there to limit and circumscribe the character of the operating overheads.

Captain DuBOSE. In that connection I would like to read a provision of our contracts, bearing on that point. This is the law and is also copied in our contracts [reading]:

That the manufacturing spaces and books of its own plant affiliates and subdivisions shall at all times be subject to inspection and audit by any person designated by the Secretary of the Navy and the Secretary of the Treasury and/or by a duly authorized committee of Congress.

Senator CLARK. When it comes to manufacturing spaces, Captain DuBOSE, do you depend on the Internal Revenue Bureau to compare the manufacturing processes in determining costs? Is not that a highly technical matter which belongs to the Navy Department?

Captain DuBOSE. The Navy Department could not possibly, without a tremendous force of people, investigate and examine in detail the methods followed by a private shipbuilder in charging for details of the work done. He submits a bid, a lump-sum price, and that is accepted by the Navy Department, if he gets the contract. Now, the Navy Department requires, in accordance with the law, that upon completion of that contract the shipbuilder shall make a statement under oath.

We also require, under our contract, that we have the right at any time to make a detailed investigation of his methods, books, and so forth.

Senator CLARK. Yes, sir; but you do not do it, as I understand.

Captain DuBOSE. I do not say we would not do it. There has been no necessity or occasion so far for doing it because the limitation-on-profit provision has been incorporated in the contracts only recently.

Senator CLARK. I understand that you have not yet had an opportunity, but I understood you to testify, Captain, that you in the Navy Department assumed no responsibility whatever, but put the whole responsibility of determining proper cost, on which profit was to be determined, naturally, in the hands of the Internal Revenue Bureau, which necessarily, of course, would have no technical personnel.

Captain DuBOSE. I do not think the law determines proper course. The law refers to profit.

Further discussion on the profit limitation was had on February 20 (p. 5562 seq.) with Mr. Blewett, of Newport News, testifying:

Mr. RAUSHENBUSH. Mr. Blewett, as I understand it, from the record on page 8, you say in the discussion of this matter which deals, I take it, with the matter of the shipbuilders direct:

We have recently gone through the cost of changes. We asked a higher overhead on the changes than our normal overhead. We asked for 20 points higher, and they granted us 10.

Is that correct? Did the Navy grant you 10?

Mr. BLEWETT. Yes; we feel that Navy work demands a higher overhead than merchant work. That is fairly understood. If you are building a barge or a cruiser, on a barge your equipment is nothing, and on a cruiser you have to have equipment and personnel.

Mr. RAUSHENBUSH. You were successful on that?

Mr. BLEWETT. They granted us a 10-point additional overhead for that.

Mr. RAUSHENBUSH. Have they done that with other companies, or is your company the only one?

Mr. BLEWETT. I am not prepared to state.

Mr. RAUSHENBUSH. Did you recommend in the other jobs that the other companies generally try to get the Navy to add that much more?

Mr. BLEWETT. Yes; for this reason: We never could get together on a cost-accounting method. It would be impossible for the yards or the shipbuilding companies in this country to agree on any one cost-accounting system. Physical conditions prevent it. So that, in order to simplify matters, I thought if we asked for an additional overhead it would take care of everything. We, at this time, charge more overhead to our naval work than we do to our merchant work.

Mr. RAUSHENBUSH. Yes; I notice that.

Mr. BLEWETT. We charge as overhead on that about 15 percent more to our Navy work than we do to our merchant work.

Mr. RAUSHENBUSH. It was on top of that?

Mr. FERGUSON. No, sir.

Mr. RAUSHENBUSH. The 10 percent allowed to you explains that higher overhead, does it not?

Mr. BLEWETT. Yes.

Mr. RAUSHENBUSH. When did the Navy allow that extra 10 percent?

Mr. BLEWETT. They permitted some changes on the *Ranger*, hull no. 353.

Mr. RAUSHENBUSH. When?

Mr. BLEWETT. 1934, the summer.

Mr. RAUSHENBUSH. After the *Ranger* had been finished and you were doing the accounting together.

On page 4 of the same document, let me read you this, Mr. Blewett:

Mr. SMITH. Let me ask you this, Blewett, you say you asked for so many points higher. Would you do that on the basis of each plant saying here is my average overhead, we want 20 points higher for naval work, taking into account no two plants might have the same?

Mr. BLEWETT. Yes.

Mr. RAUSHENBUSH. That is your proposal, that all the plants ask for a uniform increase in overhead of 20 percent?

Mr. BLEWETT. Ask for an increase in overhead of 20 percent, which would consequently result in a reduction of the common overhead, as applied to other jobs.

Mr. RAUSHENBUSH. The merchant marine jobs would gain the benefit of having the Navy pay a higher cost?

Mr. BLEWETT. That is right. The Navy would pay a higher cost because they demand of us more overhead.

Mr. RAUSHENBUSH. And the merchant marine ships would get the benefit of that to the extent the Navy carries that?

Mr. BLEWETT. They require less equipment or overhead.

The arrangements of the shipbuilders and their subcontractors were discussed in "Exhibit 1534", entered on February 6 (p. 5100 seq.), while Mr. Parker, of New York Ship, was on the stand.

Mr. RAUSHENBUSH. There is a memorandum here, Mr. Parker, prepared by a committee of which you seem to be chairman, and I want to offer it for the record as "Exhibit No. 1534."

(The memorandum referred to was marked "Exhibit No. 1534" and is included in the appendix.)

Mr. RAUSHENBUSH. In that memorandum the advantages to the contractor and the advantages to the subcontractor are fairly clearly set out. Under the disadvantages to the subcontractor, you say:

(1) Loss of a part of the maximum profit allowed by the Vinson Act, if it should be earned.

(2) Will require adoption by code authorities of resolutions permitting violation of any code provisions now in effect which would prevent members from bidding on this basis.

(3) Will disclose costs to shipbuilders currently, and perhaps create a precedent which may be difficult to overcome in the future. A similar disclosure may be made under the Vinson Act, but probably at a much later date, and with no certainty that excess profits under individual contracts will be made public.

Then the memorandum continues:

E. Possible general advantages.—(1) Mr. Parker fears that the Vinson Act may lead to a new and permanent form of taxation by the Federal Government on all profits over a certain maximum without regard for losses which may be incurred. The general adoption of this proposed plan of letting subcontracts may, in his opinion, either avoid this possibility entirely or at least limit it to Government work, and then only on the main contract without extension to subcontracts.

Do you remember that whole memorandum?

Mr. PARKER. Yes, sir.

Mr. RAUSHENBUSH. The net result of that is, is it not, Mr. Parker, that by making it impossible for subcontractors to turn back any amounts to the Bureau of Internal Revenue for excess profits under the Vinson Act you have increased the margin between your total costs and your bid price?

Mr. PARKER. The explanation of that is rather lengthy. If you will just bear with me, I will give it to you.

Say, assuming you are familiar with the Vinson Act, that under any subcontract in excess of \$10,000 the subcontractor must comply with the provisions of the act and must indicate his compliance with the acceptance of it and must certify under oath his costs.

Just shortly after the passage of the Vinson Act it was quite apparent to us, and it was apparent in the requests for tentative proposals to be used in bids, that the subcontractors were very fearful of the effect on them of the Vinson Act as applied to subcontractors. Many of the subcontractors were supplying several types of equipment. The "X" company, for instance, would supply one piece of apparatus at \$65,000. Normally and ordinarily we would make that a separate contract. Another piece of equipment would be supplied by the same company or the company's competitors on the basis of competitive bids, which would amount to \$110,000, and the result was that "X" company got in the course of the whole contract there 8 or 10 contracts, each in excess of \$10,000, all of which would be subject, or each of which would be subject, to the Vinson Act.

It was apparent to them that with a limited profit of 10 percent that on maybe eight or nine contracts they might lose. The loss was all theirs. And that on the one contract they might win, maybe 25 or 30 percent, and that would have to be repaid, and the net which they would get out of the whole would be a loss. They were a little averse to giving us prices, or averse to quoting. And we recognized the fact that we were going to have great difficulty in performing the contract on this basis, unless we found some solution to it. The solution, then, was just naturally that we would make this on basis of the cost, and instead of making a contract or several contracts, or a dozen contracts, we would make one contract for the ship as a whole. We would give to "X" company all the apparatus on the ship, on a cost-plus 11.11 basis, making one contract out of it. So that if all lost money on one piece of apparatus, due to operating conditions, and made money on another piece of apparatus, he would have the benefit which we do not enjoy, of placing his losses against his profits, and sharing a net profit, if the net profit results.

Mr. RAUSHENBUSH. Just in that connection, let me interrupt with a section of this memorandum. Mr. Parker, where you point out the advantages to the contractor. The first one is:

If the subcontractor should exceed the full 10-percent profit allowed by the Vinson Act, the shipbuilder would benefit by, and the subcontractor would lose, a part of such profit.

Was that not really the reason why you were interested in that thing?

Mr. PARKER. We were interested in that angle, for this reason: We are entering into a contract with a definite price basis, with a limited profit, taking risk on a rising commodity and labor index, where, if we lose, it is just tough luck, and, if we win, our profits are limited. It is like in a poker game, where you can only keep 10 percent of your winning hands, and the losing hands are all your own. In a very short time the poker game will get you. You cannot live under those conditions.

We realize that if a profit is made, if we can, through operations, economies, and efficiency of building the ship, develop a profit in excess of 10 percent, it goes to the Government, but it was quite apparent to us that if we made arrangements with some of the subcontractors, which include the same sort of contingencies, over a 3-year period, where they could protect themselves and would have to put in 25 or 30 percent in excess of their normal price for extraordinary contingencies, it might develop—and we would have to pay that price—where we might create a situation where we might lose \$2,000,000 on the subcontract and subcontractors might return \$2,000,000 to the Treasury on the subcontract.

The shipbuilding companies stated on the stand that they did not oppose the profit limitation in the Vinson-Trammell Act of 1933 (Eugene G. Grace, Feb. 26, p. 5776).

Mr. Parker, treasurer of New York Shipbuilding, was questioned concerning the similarity of the Vinson bill, limiting profits to 11.1 percent, and the wartime cost-plus contracts (Feb. 6, 1935, p. 5087).

Senator CLARK. Did that contract during the war include provision for assessing the services of your Chinese and Japanese representatives and for wines, liquors, and cigars which you actually put into the cost?

Mr. PARKER. It included all costs having to do with operating the business, and wines and liquors in shipbuilding are just as necessary as steel in many cases.

Senator CLARK. Do I understand that the contract provided for under the Vinson bill should include wines, liquors, and cigars?

Mr. PARKER. Absolutely so.

Senator CLARK. That is very illuminating.

Some light on the impossibility of checking a company's costs and profits is given in a report by the head of the Consolidated Returns Audit in regard to wartime work (Jan. 22, p. 4597, seq.)

Mr. RAUSHENBUSH. Apparently in 1926 the revenue agents went into this thing. I have a document here, and there are a great many pages which I want to put in, but there is just one paragraph to which I wish to call your attention. They say [reading]:

After a very careful study of conditions, viz, the system of bookkeeping and record keeping, the practices of the corporation, etc., it is the opinion of your examiners that it is an utterly impossible task to attempt to determine correct costs in connection with each contract. It is our unqualified opinion that even a large corps of men working for an indefinite time could not even approach accuracy. Thousands and probably hundreds of thousands of vouchers, labor tickets, store requisitions, etc., would have to be examined and reanalyzed, and the books all recast. During the war emergency the plant employed in the neighborhood of 22,000 men.

I would like to offer that for the record.

(The document referred to was marked "Exhibit No. 1435" and is included in the appendix.)

The CHAIRMAN. But there was no real effort made at that time to get away from cost plus?

Mr. RAUSHENBUSH. There were many efforts made, but in 1926 they go back over the whole thing and find it cannot be done.

I have here a letter which I would like to offer for the record, being addressed to H. B. Robinson, head, Consolidated Returns Audit Division.

(The letter referred to was marked "Exhibit No. 1435" and is included in the appendix.)

Mr. RAUSHENBUSH. That letter reads, in part, as follows [reading]:

In the course of our examination of the records of the cost inspector of the Navy, we have noted that it has been the continued practice of the

taxpayer to include everything possible in expenses (cost of construction of ships) regardless of whether or not they represented correct costs. We have also noted that approximately \$1,037,000 has been disallowed as expense by the Navy Department on billings to it by the taxpayer; and the items composing this amount capitalized and depreciation allowed thereon. This necessitates the computation of voluminous detailed schedules of depreciation, spread over the years 1918 to 1921, inclusive. Of necessity, in connection with the Navy dealings with the taxpayer, separate schedules of depreciation have to be prepared for every month of every year.

They say here:

We have been informed by the commander in charge of the Navy cost-inspection office that the corporation included in 1 month in the cost of construction of ships a dividend in the amount of \$35,000.

Is that correct, Mr. Parker? Was the attempt made to charge a dividend on preferred stock into the cost of the Navy vessels?

Mr. PARKER. It was charged to expense?

Mr. RAUSHENBUSH. Expense of the ship?

Mr. PARKER. It was charged to the cost, the expense of which was prorated to all work, and a part to naval vessels.

Mr. RAUSHENBUSH. So that you were in a position of asking the Government to pay a certain part of your preferred-stock dividends?

Mr. PARKER. Mr. Raushenbush, you may have read the first cost-plus contract with the Navy Department, in which there was a semblance of a definition of cost, which item provided that cost shall include all taxes. Yesterday it was brought out by your investigator of the Revenue Department that income taxes to the extent of some \$300,000 were included.

Mr. RAUSHENBUSH. \$377,000.

Newport News, which, according to Mr. Blewett's statement in Exhibit 1532, had secured an additional 10-percent allowance on overhead from the Navy for naval work, stated that expenditure for plant to prepare for the aircraft carriers, amounting to \$900,000, would be charged into the overhead of the carriers (p. 5312, Feb. 13).

Mr. FERGUSON. In 1933, we agreed to perform the maximum amount of work that we could in 2 years, regardless of ordinary procedures. We have attempted to carry that out, and in doing that have made an expenditure for plant of around \$900,000, for new equipment, for modern equipment in order to carry it through.

The shipbuilding business, or the advantage to any company in the shipbuilding business, lies tremendously with the character of the equipment, because the work is very large and difficult. Now, Mr. Archer Huntington, as well as his predecessor, has approved of keeping the plant in fine condition instead of wanting dividends this year.

Mr. RAUSHENBUSH. Of course, with a contract for aircraft carriers of—what was it? \$38,000,000?

Mr. FERGUSON. \$38,000,000.

Mr. RAUSHENBUSH. On aircraft carriers, some expenditure would be justified.

Mr. FERGUSON. You understand that that is charged not against the ships.

Mr. RAUSHENBUSH. No.

Mr. FERGUSON. Of course, that is charged against plant.

Mr. RAUSHENBUSH. And gets into the overhead, does it not?

Mr. FERGUSON. If we should not build any more ships requiring that equipment, a lot of it would naturally be written off.

Mr. RAUSHENBUSH. But it gets into the overhead of these two aircraft carriers?

Mr. FERGUSON. Yes; it does.

It is to be noted that an extra allowance of 10 percent as overhead, referred to by Mr. Blewett, might amount to \$2,000,000 on a contract of \$38,000,000 plus for the two aircraft carriers which Newport News was awarded in 1933.

The reliability of the industry's figures in cases involving the Government was indicated by the Newport News claim for damages and costs because of cancellation of contracts after the war (Feb. 13, p. 5310, et seq.).

Mr. RAUSHENBUSH. Coming now to a memorandum from you to Mr. Huntington of May 15, 1924, we definitely get into the question of the cancellation claim you were making against two battle cruisers and the battleship *Iowa*. You add up fixed overhead, Federal taxes, special plant, remainder of fee, interest on unused plant, fixed overhead, and occupancy of plant during scrapping, a sum totaling \$14,973,165.

Then you go ahead and say to Mr. Huntington:

We did not expect to get both fixed overhead and remainder of fee, but I thought there was a good chance of getting a part of the fixed overhead and the whole of the fee. The cancellation board has recommended against giving us any part of fixed fee. We feel, however, that we are entitled to this, so that a minimum I would be willing to take in settlement would be represented approximately by the following—

And you add up various things totaling \$6,636,000.

Now, as we gather this, Mr. Ferguson—

Mr. FERGUSON. I have not got that.

Mr. RAUSHENBUSH (handing paper to witness). As we gather it, what you are doing is putting in a claim against the Government of \$14,973,165 and telling Mr. Huntington that your minimum claim is \$6,635,000.

Mr. FERGUSON. Nothing of the kind.

Mr. RAUSHENBUSH. Will you explain that?

Mr. FERGUSON. I am putting in here the things on which a claim can be based. We made no claim for \$14,000,000. The job was settled in regular order in the Navy Department, and the complete records are there.

Mr. RAUSHENBUSH. You say, "Our claim was"; that is, "Our claim against the Government was as follows":

Mr. FERGUSON. For trading purposes. We did not expect to get it or did not expect to get within a mile of it, but the question was involved as to how our company could be treated justly in these cancellations; and anticipated profits were not waived, but anticipated profits had been disallowed, even where the anticipated profit had been mentioned in figures by the courts, on account of just what I have told you. We still had a claim, and we could have carried it through the courts.

There was also a question of our agreeing during the term of the contract to take the proper proportion of overhead expense. That is a damage claim.

There was, in addition to that, the special plant which had been put up by us and the Navy Department in conjunction, and had to be settled.

While the claim could be stated to be a claim, it is just like any other trading position, where you keep everything you can keep until you reach a point of settlement.

If you went in with a tax, or any other case, and yielded all the talking points you had, it would be contrary to usual practice.

Mr. RAUSHENBUSH. That is all we wanted to get, Mr. Ferguson, that you put in a claim for \$14,973,000 and did not expect to get within a mile of it, and you told Mr. Huntington, in the same breath, you would be satisfied with \$8,300,000 less and put that in as a trading claim.

That interests us, of course, from this angle: That where there is no competition between companies for the Navy work, the question of the guaranties of the Navy Department in paying a higher claim is involved. I mean in bidding for ships you have, or are supposed to have, competition to keep down these trading claims to a minimum. But here you were putting in such a great number of items, and thought the way to conduct the business was to put in for \$8,300,000 more than you expected to get or were willing to take.

Mr. FERGUSON. We knew perfectly well we would not get it.

Mr. RAUSHENBUSH. I will offer that memorandum for the record.

(The memorandum referred to was marked "Exhibit No. 1572" and is included in the appendix.)

Mr. RAUSHENBUSH. There is a good deal more on that, Mr. Chairman.

Senator BONE. Can you tell us, Mr. Ferguson, which of those items were ultimately allowed?

Mr. FERGUSON. The items which were ultimately allowed were the damage item, and a settlement was made under the contracts for what we call "plant rental." That was appraised and adjudicated by the Navy Department, and complete records are there, and also the damage item, which amounted, as I remember it, to around \$4,500,000 for their proportionate share during the life of the contract of overhead expenses.

Senator BONE. What about the item of taxation?

Mr. FERGUSON. That was not allowed in the settlement.

Senator BONE. Just so that we do not get any confusion in our own minds here, I am not referring to income taxes but I am referring to property tax levied on the property by the State of Virginia, or whatever tax subdivision levies taxes on your plant. Was that allowed? That is an overhead operating expense.

Mr. FERGUSON. Yes; the local taxes were allowed, I think.

Senator BONE. That is what I am getting at. In other words, your State or local taxes.

Mr. RAUSHENBUSH. Now, you have stated this, Mr. Ferguson. When you referred to \$6,999,204 as being for damages; that was overhead, was it not?

Mr. FERGUSON. Yes, sir.

Mr. RAUSHENBUSH. It is overhead you are being paid for at the rate of \$100,000 a month for 46 or 47 months?

Mr. FERGUSON. Yes, sir.

Mr. RAUSHENBUSH. What position were you stating for the Government paying the overhead on canceled ships, if it was not simply under the head of anticipated profits or to take the place of anticipated profits? You were not building on those ships during this period. You were not paying your own salary, and you were not paying power under that item.

Mr. FERGUSON. We were. They had agreed to take their proportionate share of the overhead expense during the life of the contracts. The contracts were canceled. It was worked out by the Navy Department that for the time the contracts would have extended, if completed, that they owed us their proportionate share of our overhead expense, and it was settled on that basis, and the complete record is in the Navy Department.

Mr. RAUSHENBUSH. We know they gave you the overhead expense. My question was: How much of that overhead expense was actually spent by your company? How much of that \$100,000 a month?

Mr. FERGUSON. It was the overhead expense actually expended.

Mr. RAUSHENBUSH. The question was interrupted. How much of the overhead expense was expended for the purpose of those Navy vessels? You had your ordinary business and could devote the \$100,000 to that; but the question is: How much of that overhead was really spent on those Navy vessels on which construction had stopped?

Mr. FERGUSON. It was spent on the plant as a whole, and our ordinary business would not at that time anything like carry the overhead. We nearly went broke as it was.

Mr. RAUSHENBUSH. This helped out a great deal.

Mr. FERGUSON. Here was this overhead which had been built up to very much larger proportions during the war, as a result largely of these same contracts, and a lot of plant which we still did not need, and we still had to keep our plant a going concern, unless we shut it up and quit, and the Navy Department—who was it settled there? Secretary Wilbur finally settled after several years of investigation on these figures.

Mr. RAUSHENBUSH. This was not several years. This was dated August 17, 1923.

Mr. FERGUSON. However long it was; 2 years.

Mr. RAUSHENBUSH. I still do not feel that the question has quite been answered. We can understand how this helped the company carry itself on as a going concern, to get this figure, but the question was whether any of that was spent on naval vessels whose construction had stopped and whether it was not just a gift by the Navy Department.

Mr. FERGUSON. No, sir; it was in settlement of a canceled contract. You do not accept a canceled contract for \$70,000,000 and tell a man to go chase himself, do you?

Mr. RAUSHENBUSH. We are interested in the way the settlement was made. Why should you not be paid for the cost which you incurred up to date and not be given anything which looks like loss of anticipated profits, \$4,648,000; under the head of Overhead another two-million-odd dollars; under the head of Plant, which was your own plant, the \$6,999,204, except to justify anticipated profits? We see no other possible explanation for it, because you were not using the plant and you were not using the overhead for the benefit of the naval vessels.

Mr. FERGUSON. I do not agree with you at all. The Navy Department worked this out and the Treasury Department, as I remember it, permitted the \$100,000 to be distributed at the rate of \$100,000 a month for the 46 months. I do not see anything strange or irregular about it.

Mr. RAUSHENBUSH. Certainly the Treasury Department would have to allow the distribution of income when you once got it, but the question was whether this was not anticipated profit.

Mr. FERGUSON. If that was anticipated profit, you do not think for a minute that the Treasury Department would not put it in profits?

Mr. RAUSHENBUSH. They did, did they not? They allowed \$100,000 a month for anticipated profits.

Mr. FERGUSON. At the rate of \$100,000 a month.

Mr. RAUSHENBUSH. That is the way it comes in.

Mr. FERGUSON. If it had all been put in at once, it would have given us a very high and fictitious earning for that year.

Mr. RAUSHENBUSH. You could not put it in in a lump sum, because you were not getting it that way.

Mr. FERGUSON. They make you put it in in a lump sum frequently, when you do not get it, if you have an agreement to get it. As a matter of fact, we did get it in a lump sum and distributed it on our payments at \$100,000 a month.

Mr. RAUSHENBUSH. To what account?

Mr. BRANCH. To overhead.

Mr. RAUSHENBUSH. That was allowed as a deduction from the regular overhead?

Mr. BRANCH. Yes; we reduced our regular overhead by that amount.

Mr. RAUSHENBUSH. My other question still remains: As to how much of the \$100,000 which you distributed to overhead, and which carried your going plant, was really spent on these naval vessels. If the answer to the question is you were not building any naval vessels, the naval vessels had stopped, then it was by way of damage, as you say, or, as we say, "anticipated profits."

Mr. BRANCH. It was spent by us to build under naval contracts.

Mr. RAUSHENBUSH. As an indemnity?

Mr. BRANCH. As an indemnity; as a settlement.

There is evidence that Bath Iron Works transferred an item of \$60,000 to the destroyer *Dewey*, thus showing an improperly high cost (Part 23, p. 6758).

Do you remember any difficulty you had with your auditors, or with anyone else, regarding the putting of a sum of money or having a certain sum of money against the destroyer *Dewey*, which expense apparently was incurred on their negotiation? Do you recall anything of that kind?

Mr. NEWELL. Yes. There was a loss on two of the contracts, that, for book-keeping purposes, was put in on that account. You people were informed, and that whole matter was explained to them when they were in Bath. It was simply a bookkeeping question.

Mr. LAROUCHE. Here is a letter on that, which I offer for the record as exhibit no. 1821. This appears to be a letter from you to your auditing firm.

Mr. THEBEAU. I beg you pardon. I think that is written by the chief clerk.

Mr. LAROUCHE. From your firm, I meant to say.

Mr. THEBEAU. Yes, sir.

Mr. LAROUCHE. Your chief clerk in one place says [reading]:

Your attitude seemed to be that I was a little careless in not calling your attention in my letters of September 9 and 14 to the fact that the transfer above mentioned was included in the *Dewey* cost.

The transfer, as I take it, details a figure of \$60,482.57, which cost was incurred on the lighthouse tender *Hickory* and on a tug. Is that correct?

Mr. NEWELL. That was not put into the cost account of the *Dewey*. It was simply added on the end of the résumé of the *Dewey's* cost account to show the net result of the three jobs. Do I make it clear? It was not there as an item of cost. I think that your committee must have a copy of the résumé of cost of the *Dewey*, that had, as a separate item and last entry on the sheet, a cost item to which you refer, which was added to it, but it was not in any way absorbed or put in the *Dewey's* account. The *Dewey's* account was an item all by itself. I have seen it. I know that, because I talked with your people, when they were in Bath, about that same thing. I said, "That does not have anything to do with the *Dewey*" and it is very clear as to what it was on the sheet which was handed to you.

(The letter referred to was marked "Exhibit No. 1821" and is included in the appendix.)

Mr. LAROUCHE. You mean by that, you are saying that that \$60,000 was not at any time entered in your books as a charge against the *Dewey*?

Mr. NEWELL. No; it never was.

Mr. LAROUCHE. I submit another letter on that subject for a number, "Exhibit No. 1822." This is a letter from your auditors, in response to the one from your chief clerk. I will read one paragraph [reading]:

I am surprised to note the contents of your letter of the 26th. In calling you regarding the \$60,000 transfer item, included in the cost of the *Dewey*, my concern was to make sure that the principals of your company were familiar with the actual outcome on the *Dewey*.

What does he mean by that? Does he not rather strongly state that that was transferred to the cost of the *Dewey*?

Mr. THEBEAU. No.

Mr. NEWELL. No. He says it was not.

Mr. LAROUCHE. It was not?

Mr. NEWELL. It was not in there at all.

Mr. LAROUCHE (continuing reading):

In all of Mr. Thebeau's conversations with me—the letter continues—

he expressed great disappointment that the approximate profit on the *Dewey* was only about \$51,000. We, of course, knew that the costs were burdened with the \$60,000 transfer item, but none of your letters made any comment as to the real profit from the point of view of the management, and we were naturally interested that the management knew the facts.

Mr. NEWELL. We knew it anyway.

Mr. LAROUCHE. Then your answer is that you never did at any time charge that into the cost of the *Dewey*?

Mr. NEWELL. Into the direct cost of the *Dewey*?

Mr. LAROUCHE. Into the costs, direct or otherwise.

Mr. NEWELL. No, sir.

(The letter referred to was marked "Exhibit No. 1822", and is included in the appendix.)

Mr. LAROUCHE. I submit another letter on the same subject for its appropriate number, exhibit no. 1823. I think we can enter that without reading it.

Mr. THEBEAU. Yes, sir.

(The letter referred to was marked "Exhibit No. 1823", and is included in the appendix.)

Mr. LAROUCHE. I submit this letter for a number, exhibit no. 1824, being a letter from S. L. Eaton, chief clerk of the Bath Iron Works Corporation, to Henry Brout & Co., 295 Madison Avenue, New York, N. Y.

(The letter referred to was marked "Exhibit No. 1825", and is included in the appendix.)

Mr. LAROUCHE. You would not say that that \$60,000 item had anything to do with your claim for increased cost?

Mr. NEWELL. No, sir.

Mr. LAROUCHE. It had nothing to do with it?

Mr. NEWELL. Absolutely no.

Mr. LAROUCHE. I submit a letter from you to Mr. Spear, for its appropriate number.

(The letter referred to was marked "Exhibit No. 1825" and is included in the appendix.)

The CHAIRMAN. Mr. LaRouche, what is the general direction of the matters which you are bringing into evidence at this time?

Mr. LAROUCHE. Merely that there seems to be some impression gained from this correspondence that this \$60,000 was somehow transferred as a bad debt from one job to another, with the apparent result that the data show a naval ship, a destroyer, was burdened with a charge that was not properly assigned to it.

The CHAIRMAN. I see.

Mr. LAROUCHE. Mr. Newell says that was not the the fact.

Mr. NEWELL. What you really mean to infer is that we were trying to get that \$60,000 out of the Government, which was not so, and it was not in there, and it had nothing to do with the *Dewey* cost or in any way had anything to do with the building up of the amount of money which we claimed was due us under the conditions imposed upon us by the code. Is that clear?

The CHAIRMAN. Mr. Newell, there would have been large advantage, shortly after that, would there not, in your being able to put a larger cost, a larger production cost, in light of the fact that the Vinson bill, limiting the profit that could be had from the building of ships, came along shortly thereafter?

Mr. NEWELL. No; the Vinson bill did not enter into this at all. The bill passed by Congress extending relief to contractors who were caught under the code—

The CHAIRMAN. That was not my question, as to whether the Vinson bill had entered into the consideration. But the advantage would have been yours, if you could have increased that showing of cost by \$60,000?

Mr. NEWELL. I know, but we honestly could not do a thing like that. That is impossible and unthinkable. No; you could not do a thing like that, Senator. It was absolutely wrong, and it could be very easily checked.

The CHAIRMAN. Is there anything in this correspondence with which you are dealing, Mr. LaRouche, that indicates that that was in the mind of the company at the time?

Mr. LAROCHE. No; I am not prepared to say that the correspondence shows clearly that that was in the minds of the officials of the company.

Mr. NEWELL. I can say—

Mr. LAROCHE. I think the letters should be in the record and should tell their own story.

Mr. NEWELL. It absolutely is not that way.

The CHAIRMAN. Proceed, Mr. LaRouche.

Mr. NEWELL. I do not like even the thought of it. I do not think there is anything there that makes that possible.

The CHAIRMAN. Mr. Newell, I do not see what there would be more repulsive about your doing that—I am not wanting to give it a bill of health, by any means—but I see nothing more repulsive in that than your organization inviting improper propaganda for the purpose of instilling a fear of war to the end that a number of contracts might be let for more ships, and that your company did do prior to the Vinson naval building bill.

Mr. LAROCHE. I think, Mr. Chairman, to shed a little further light on that, that some of this correspondence might well be read, and perhaps Mr. Newell can explain it.

Your firm of auditors, Henry Brout & Co., writes on September 27, 1934 [reading]:

I am surprised to note the contents of your letter of the 26th.

This is to Mr. Eaton:

In calling you regarding the \$60,000 transfer item, included in the cost of the *Dewey*, my concern was to make sure that the principals of your company were familiar with the actual outcome on the *Dewey*.

Then he says further [reading]:

In all of Mr. Thebeau's conversations with me he expressed great disappointment that the approximate profit on the *Dewey* was only about \$51,000.

He says:

We, of course, knew that the costs were burdened with the \$60,000 transfer item * * *

What does he mean by that?

Mr. NEWELL. I do not know.

Mr. LAROCHE. What could he mean but that the costs on the *Dewey* were burdened with \$60,000 which did not belong there?

Mr. NEWELL. I would think the same as you, but I do not understand that. Maybe Mr. Thebeau can answer it.

Mr. THEBEAU. The auditor might have recommended it, but that is no fair test of it at all. With regard to our claim, we have to give a detailed account, a sworn statement, to the commission that we filed the claim with, showing how our costs have been kept, both as to material and as to labor. That is absolutely all in detail when we present our claim, which we are working on now. But that \$60,000, you can see he was referring to me, and I do not recollect now, but I know it is not charged to the *Dewey*, and would not be handled that way. It is impossible to handle it that way.

Mr. LAROCHE. How do you account, then, for this further language:

We, of course, knew that the costs were burdened with the \$60,000 transfer item, but none of your letters made any comment as to the real profit from the point of view of the management, and we were naturally interested that the management knew the facts.

Did you know the facts?

Mr. NEWELL. Of course, we did.

Mr. LAROCHE. You did know the facts?

Mr. NEWELL. Yes. I do not know what the auditor means by that. I would suggest that the committee either get the auditor down here or write and ask for a written interpretation of it.

Mr. LAROCHE. What is your explanation of the language?

Mr. NEWELL. It puzzles me. I have a clear picture in my mind as to the set-up of the final cost résumé of the *Dewey*, and that \$60,000 was a separate item in it, and it showed the net result of those three jobs, as far as net profit on the three was concerned, just the same as you would set it up for your income-tax purposes. It does not have anything to do with the costs of the *Dewey*. It had nothing to do with the cost of operation, whether those three jobs were going along together.

Mr. LAROCHE. He says further—this is the auditor's letter, again [reading]:

Let me also add that I was rather shocked to read the submitted copies of your schedule of cost of construction of July 31 and August 31. I hardly think you meant to use our name in the item describing the transfer of labor and overhead. It was not a very politic thing to do, especially if you consider that the information and the theory for this method of treatment was obtained from Mr. Newell, who undoubtedly approved it, bearing in mind the primary interest of the company.

Why was he so shocked?

Mr. NEWELL. I do not know. I do not know what he refers to.

Mr. LAROCHE. He says [reading]:

I would further suggest the impropriety of making such reference in the corporate books. If by chance our name has been used in the books, as authority for this or any other entry, please make the correction by deletion immediately, and I would appreciate your advising me to this effect at once. Also, please show this letter to Mr. Thebeau, since it affects the fiscal affairs of the company.

This auditor apparently wanted no part of it.

Mr. THEBEAU. I can answer that. He objected to his name being written in the accounts, saying that he authorized this or he authorized that. That is the point. He did not want his name written in authorizing the account.

Mr. LAROCHE. Because he was shocked, according to his language?

Mr. THEBEAU. That is the way I interpret it.

Mr. LAROCHE. In the way the entries had been made.

Mr. THEBEAU. He might have recommended certain changes, and he objected against the chief clerk writing his name opposite them. Auditors do not always agree with accountants:

Mr. NEWELL. Why can you not ask the auditor who wrote the letter about it?

Mr. LAROCHE. We thought perhaps you could throw some light on it.

Mr. NEWELL. I cannot tell you anything more than I have already.

Mr. LAROCHE. There is just a further pertinent paragraph. Your chief clerk, in replying to the auditing firm says [reading]:

I am very sorry if I have done anything out of order.

What does he mean by that?

Mr. NEWELL. I do not know.

Mr. LAROCHE. Apparently Mr. Brout, the auditor, is accusing him of having done something improper.

Mr. THEBEAU. I can answer that. He considers it improper writing his name opposite the entries.

Mr. LAROCHE. He says:

I have tried very hard to cooperate in every way with both you and Mr. Stoler, as I think Mr. Stoler will testify.

Who is Mr. Stoler?

Mr. THEBEAU. He is one of the auditors for Mr. Brout.

Mr. LAROCHE. (continuing reading):

I have tried equally as hard to keep accurate accounts and to place the facts before the officials of the company at all times, and to cooperate with them in every way.

I understand Mr. Stoler is coming here next week and at that time I will go over all the adjusting entries I have made with him:

The shipbuilders hold a different idea of what the Navy knows about costs than the Navy officials. Mr. Bardo, on April 5 (Hearings, Part 23, p. 6925), informed the committee that the Navy knew the cost of building the ships.

The wartime experience of the Government with the shipbuilding companies was not of the character as to lead to a great desire on the part of the committee for repetition of it. If the Government by setting up its own yards to produce the necessary naval vessels (other than auxiliaries) can not only build them more cheaply, but can also thereby avoid the experiences encountered during the last war with the shipbuilding companies, it will be highly desirable.

The shipbuilding companies will be more than occupied with building merchant vessels in the event of another war, especially since the technique of sinking vessels has been perfected with the development of airplane bombing. During peacetime they should confine themselves to the building of merchant vessels and naval auxiliaries.

The committee wishes to repeat a portion of that section of its report on naval shipbuilding dealing with the wartime experience of the Government in a financial way with the shipbuilding companies.

I. WARTIME COSTS, PROFITS, AND TAXES

Undoubtedly one of the greatest favors done for the private shipyards during the war period was expressed in the order to have ships begun after the armistice, the keels of which had not been laid up to that time.

The result of this order gave the companies a great amount of work at profits which were not subject to the wartime taxes.

The work on destroyers alone, whose keels had not been laid at the time of the armistice, was distributed as follows:

Bethlehem	\$90, 540, 975
New York Ship.....	22, 014, 041
Newport News.....	5, 332, 504
Wm. Cramp & Son.....	31, 103, 702

During the war years the large shipbuilding companies made very considerable profits. They secured cost-plus contracts and added questionable charges to the costs. They took profits on these ships after the war taxes had been repealed. They secured changes in contract dates to avoid the war taxes. They bought from the Government very cheaply yards which had been built at Government costs. One yard built additions only under the threat of being commandeered. Exorbitant claims were knowingly filed against the Government for cancelations. Huge bonuses were paid.

Much of this evidence is spread out in exhibits not printed at the time of the preparation of this preliminary report (June 1935). Some indication of it, however, can be gained from the following excerpts from the testimony:

New York Ship had received an assurance from Director Schwab (U. S. Shipping Board) that it would receive such improvements after the war as a gift or compensation (Jan. 21, 1935, p. 4539):

Mr. RAUSHENBUSH. Before you went into the construction of that \$14,000,000 south yard did you and your company make an arrangement with Director General Schwab, of the Emergency Fleet Corporation, determining on what terms that would be given back or be sold to the company?

Mr. PARKER. There was an agreement made by which we would be permitted to repurchase the property on the basis of an appraisal or on the basis of earnings.

Mr. RAUSHENBUSH. So that before you acceded to this threat of the Government commandeering, an arrangement was made with Schwab, who was head of the Emergency Fleet Corporation, determining pretty definitely the terms on which you would get that at the end of the war. Is that not correct?

Mr. PARKER. That is right.

Mr. RAUSHENBUSH. In that connection, Mr. Chairman, I would like to read a letter from Charles J. Fay, of the firm of White & Case—White & Case have been your attorneys on these matters, have they not?

Mr. PARKER. Up to 1933.

Mr. RAUSHENBUSH. The letter is dated May 25, 1923, and is addressed to James W. Talbert, of the Emergency Fleet Corporation. [Reading:]

DEAR MR. TALBERT: This is to confirm the appointment you gave Mr. Neeland and myself for Thursday morning, the 31st instant. Mr. Neeland and I will endeavor to be on hand promptly, and my thought is to be there at 9:45 a. m. (standard time). If you cannot see us at that time, we will wait until you are free.

I enclose a memorandum regarding this plant-acquisition matter by the New York Ship of the improvements made at the cost of the Fleet.

As the situation now stands, the acquisition arrangements (which was formulated in 1918 to avoid a possible war-tax cash liability for the ways and shop improvements which Director General Schwab intended, and proposed, should be acquired by New York Ship without specific payment therefor but in the nature of a gift for added fee or compensation) was, and is, based on the improvements themselves, providing their valuation through earnings.

Does not that indicate fairly clearly that this whole arrangement by which you got the property, and in which the Emergency Fleet Corporation had sunk \$14,000,000, for one-half million dollars, was determined before you went into that supervision of the construction of the yard?

Mr. PARKER. It was recognized at the time the work was undertaken that the land belonged to the New York Shipbuilding Corporation. The facilities placed on that land and attached to that land by the Shipping Board became a part of the realty.

Nevertheless, there was an agreement executed by which the Government would be paid for that on basis of the earnings, which earnings developed from the operation of that unit.

Mr. RAUSHENBUSH. So that there was not only the threat of commandeering, but there was a promise obtained from Mr. Schwab, as quoted, "in the nature of a gift or added fee or compensation" before you went into this?

Mr. PARKER. That was not a motive to agree. That was rather a motive to make us avoid, because, if, by any chance, it was a fee on the construction, or if, by any chance, it was a gift, it would have been subject to tax, and we would be in position of having an obsolete, nonoperating plant, which would be subject to a high rate of income tax. It would be having a bear by the tail.

Mr. RAUSHENBUSH. The arrangement was to get around the tax there, by having that sort of an arrangement, and it should not be exactly a gift, but in the nature of a gift or added fee or compensation.

I would like to offer the letter for the record, as exhibit no. 1417.

(The letter referred to was marked "Exhibit No. 1417" and is included in the appendix.)

Bethlehem Shipbuilding Co. paid \$12,639,000 in taxes out of a profit for the war years of \$68,205,000 (Feb. 27, 1935, p. 5809.)

Mr. RAUSHENBUSH. So that you could allocate as much as you wanted of the total taxes to be borne to any one of your hundred-odd companies, could you not?

Mr. SHICK. We could, if we thought that that would be advisable to do, but we did proportion it more or less, based on the earnings of the particular companies. That was the basis of our proportion.

Mr. RAUSHENBUSH. What sort of proposition is that?

Mr. SHICK. For instance, in the years 1917 to 1921, we proportioned out of the total taxes, \$12,639,000 in taxes to the Bethlehem Shipbuilding group, which included the six subsidiary companies.

Mr. RAUSHENBUSH. That would be in a ratio of 12 to 63 million net income before taxes, would it not?

Mr. SHICK. That is about right.

Mr. RAUSHENBUSH. That is our figure.

Mr. SCHLOTTMAN. \$12,069,000.

Mr. RAUSHENBUSH. On the final settlement it is \$68,205,000, according to our figures.

Mr. SCHLOTTMAN. All right.

Mr. RAUSHENBUSH. That would be about one-sixth of it, somewhere between a fifth and a sixth, would it not?

Mr. SCHLOTTMAN. That is correct.

Bethlehem Ship during the war used a rental system which made its profits appear lower than they actually were. The "rentals" were larger than the plant values of the companies (Feb. 27, p. 5801 seq. and p. 5810).

Mr. RAUSHENBUSH. Mr. Shick, in examining the figures presented by you to the committee on the net income of Bethlehem Ship during the war years, we checked with the Bureau of Internal Revenue and found that there were very large rentals to other companies. Could you explain the point and purpose of those rentals?

Mr. SHICK. At the time the Bethlehem Shipbuilding was organized, in October 1917, there were certain properties that were owned by other subsidiaries of Bethlehem, which were not grouped in the Bethlehem Shipbuilding Corporation at that time, and until that could be done there were rentals. These properties were rented to the Bethlehem Shipbuilding Corporation for certain years, with an idea of just making the distribution of the profits that were earned on ships that were manufactured by those facilities.

Mr. RAUSHENBUSH. Were those so much rentals of property as a profit-sharing arrangement?

Mr. SHICK. There was a profit-sharing arrangement. That was the basis of it.

Mr. RAUSHENBUSH. Do you have the terms of that?

Mr. SHICK. I have a synopsis of the leases here, which explains the rental of the plant to the Bethlehem Shipbuilding Corporation, and the basis of the rental was from November 1, 1917, to December 31, 1918, and in the case of the Hunter's Point Drydock Co., at Hunter's Point, San Francisco, was from November 1, 1917, to December 31, 1918, and for the Potrero and Alameda works of the Union plant, at San Francisco, from November 1, 1917, to December 12, 1924. Here is the information [handing paper to secretary].

Mr. RAUSHENBUSH. The sheet you hand me shows what you describe a profit-sharing arrangement, 35 percent of all profits up to and including \$2,000,000, 15 percent of all profits in excess, and so forth. In the case of the Potrero and Alameda works, 85 percent of all profits. I will offer that for the record.

(The document referred to was marked "Exhibit No. 1641" and is included in the appendix.)

Mr. RAUSHENBUSH. That was a profit-sharing arrangement, somewhat, more than a rental arrangement, was it not?

Mr. SHICK. It was really a profit-sharing arrangement for the purpose of renting those particular facilities.

Mr. RAUSHENBUSH. And the rentals paid to those particular companies were far larger than the plant value of those companies?

Mr. SHICK. No doubt that might be true, because we did not know at the time what the earnings would be from those facilities, and in order to distribute those to profits, that was the basis on which the rentals were made.

Mr. RAUSHENBUSH. Do you have the sum total of those rentals before you?

Mr. SHICK. I do not think I have.

Mr. RAUSHENBUSH. Do you have those, Mr. Mitchell?

Mr. MITCHELL. Yes, sir.

Mr. RAUSHENBUSH. You have been sworn before, Mr. Mitchell?

Mr. MITCHELL. Yes, sir.

Mr. RAUSHENBUSH. Will you give those rentals by years?

Mr. MITCHELL. According to the income-tax returns filed by the Bethlehem Steel Corporation, which is a consolidation with the companies including Bethlehem Ship and so forth, the rentals paid by Bethlehem Ship Co. in 1918 were \$14,049,121.93; and 1919, \$7,535,196.10; in 1920, \$4,934,393.67; 1921, \$8,881,727.63.

Mr. RAUSHENBUSH. Mr. Shick, if those rentals which you describe as a profit-sharing arrangement were added back into this net income of Bethlehem Shipbuilding Corporation, the net income would be somewhat larger?

Mr. SHICK. Yes; it would. In order to explain that situation, I would like to present to the committee a consolidated profit-and-loss statement and a consolidated balance sheet of those companies to which those rentals were paid with the idea of showing a complete picture of the shipbuilding operations [handing paper to secretary].

Mr. RAUSHENBUSH. May we see to what extent that checks with the figures which we have been able to obtain from the Bureau of Internal Revenue? Is this after taxes, Mr. Shick?

Mr. SHICK. That is the net income after taxes.

Mr. RAUSHENBUSH. After paying Federal taxes?

Mr. SHICK. After paying Federal taxes.

Mr. RAUSHENBUSH. Do you have any sheets prepared showing the income before taxes for this consolidated group?

Mr. SHICK. I have it from the summary, showing it.

Mr. RAUSHENBUSH. For this consolidated group?

Mr. SHICK. For this consolidated group, by dividing it between the war years and the years after the war, showing the amount of business that was done, the net income before interest charges, but after depreciation and the net income, profit-and-loss statement, and here is the amount of the income and excess profits which have been deducted [indicating] so that by adding this back to this income here [indicating] that would be the income.

Mr. RAUSHENBUSH. You have not got it by individual years, though, before taxes? That is the usual way that the Bureau of Internal Revenue determines the net taxable income.

Mr. SHICK. We have not got it in exhibit form, but we could readily prepare it.

Mr. RAUSHENBUSH. I wonder if you would check with our figures. I do not think it would be very long. We found that by grouping these various shipbuilding subsidiaries of Bethlehem Steel, we arrive at certain figures which were reported, in fact, by these companies themselves for each individual year, and we would like to get that for 1917, 1918, 1919, 1920, and 1921.

Mr. Mitchell, can you give us the information you secured from the Bureau of Internal Revenue as to the company's original reports on these consolidated groups of shipbuilding companies as far as invested capital and net income or loss go for these years?

Mr. MITCHELL. Yes, sir; do you want the individual companies, starting off with Bethlehem Shipbuilding?

Mr. RAUSHENBUSH. No; let us group them. List the ones which you have so that Mr. Shick can check them.

Later the question was discussed again (p. 5810).

Mr. RAUSHENBUSH. Mr. Shick, coming back a minute, I did not quite understand what was the purpose of this siphoning procedure, this rental procedure, of giving such large rentals to the other companies? Did that have something to do with the taxation question, or what was the point of it?

Mr. SHICK. It had nothing to do with taxes.

Mr. RAUSHENBUSH. What was the point of it?

Mr. SHICK. It was distributing the profits over to the facilities which the Bethlehem Shipbuilding Co. were using and on such facilities they were using there, trying to put it back to profits, because they had the use of the facilities. There was no advantage from the taxation point of view. That is all.

Mr. RAUSHENBUSH. Those rentals were away out of relation to any plant investment in them?

Mr. SHICK. But they were getting the earnings on those facilities from Bethlehem Ship. It was the proportion of the earnings of each plant that was being used.

Mr. RAUSHENBUSH. Mr. Mitchell, do you have the plant investment of some of the companies which got these high rentals?

Mr. MITCHELL. Yes, sir; I do. From the revenue agent's report, and from the balance sheet submitted, I have taken the net plant values, which consist of the plant costs, less reserves for the following subsidiaries:

Union Iron Works Co. had a net plant value in 1918 of \$4,982,591.63. Rental was paid to the company for the use of plant of \$11,305,216.21, which for that year was 227 percent of the plant's value.

Union Iron Works Drydock Co. received \$556,000 rent for their net plant of \$3,913,379.

Fore River Shipbuilding Co., for 1917, received \$2,187,906 rental for a plant value of \$3,235,000 odd. Those figures are for 1918.

For 1919, the only plant receiving rental from Bethlehem Shipbuilding Co. was the Union Iron Works Co. It had a net plant value for that year of \$4,454,302. for which it was paid rental of \$7,535,196, which was 169 percent of the plant value.

For 1920 its plant value was \$4,142,686, and it received rental of \$4,934,393, a return of 119 percent.

1921 net plant value shown by the balance sheet was \$3,609,614, for which it received rental of \$8,881,727, which was 227 percent of the plant value for that year.

These plant-value figures are taken from the balance sheets at the beginning of the respective years.

Mr. RAUSHENBUSH. Mr. Shick, would you mind stating your answer to my other question again? I did not quite understand it. Did you describe these rentals as the proportion of the profit which those companies earned?

Mr. SHICK. Those particular facilities earned.

Mr. RAUSHENBUSH. Those particular facilities earned?

Mr. SHICK. Yes; which belonged to the former companies.

Mr. RAUSHENBUSH. So that rental was not the phrase at all; was it?

Mr. SHICK. We used the term "rental."

Mr. RAUSHENBUSH. How much was paid in dividends to the Bethlehem Steel by these various companies, would you say, Mr. Shick, by Bethlehem Shipbuilding Co. during those years, Fore River and Union Iron Works?

Mr. SHICK. It was our practice to have those companies practically pay out all their earnings which were available over to the Bethlehem Steel Corporation because the Bethlehem Steel Corporation was the one paying dividends to the stockholders. There was no reason leaving the earnings accumulate in those companies, so that they were paid over to the Bethlehem Steel Corporation.

Mr. RAUSHENBUSH. Do you have the dividends before you?

Mr. SHICK. I do not.

Mr. RAUSHENBUSH. Do you have them, Mr. Mitchell?

Mr. MITCHELL. I have them, as obtained from the revenue agent's working papers of the income-tax unit. He analyzed the surplus for the various years, and, according to the books, the dividends paid were as follows:

Bethlehem Shipbuilding Corporation, Ltd., paid in 1919, \$1,782,500; in 1920 it paid \$1,705,000; and in 1921 it paid \$20,282,700—a total for the years 1917 to 1921 of \$23,770,200.

The Fore River Shipbuilding Corporation paid in 1917, \$90,000; in 1920, \$4,010,400—a total of \$4,100,400.

The Union Iron Works Co. in 1917 paid \$400,000; 1918, \$1,130,000; 1919, \$1,400,000; 1920, \$5,697,928.19; 1921, \$24,000,000—a total of \$32,627,928.19.

The total dividends paid by these three companies to Bethlehem Steel Co. amounted for those years to \$60,498,528.19.

After the war, Newport News filed a claim against the Government for \$14,973,165 (Ex. 1572). At the same time the president of the company was informing the owner that the company should be satisfied with \$6,636,000. This was "for trading purposes" (p. 5340, Feb. 13).

Newport News also bought facilities added by the Government during war time at a much lower cost (Feb. 13, 1935, p. 5323).

Mr. RAUSHENBUSH. Now, coming to the war-time facilities which the company got out of this, the Navy at various times advanced considerable sums to the company, did it not, to build additional vessels?

Mr. FERGUSON. Yes.

Mr. RAUSHENBUSH. Have you the figures there of how much that was?

Mr. PARKER. That is the plant rental, is it not? Do you recall the question?

Mr. FERGUSON. What number is it?

Mr. RAUSHENBUSH. War-time facilities that the Government added.

Mr. PARKER. Do you remember the number of the question?

Mr. RAUSHENBUSH. I do not think it was in a question.

Mr. FERGUSON. In this Price, Waterhouse report, we find the following:

Total cost of facilities known as plant rentals A, B, and Shipping Board special fund, \$10,167,272.50—

and—

Net cost of same to the company, including estimated value of the facilities under destroyer contracts transferred to the company in settlement of canceled destroyers, \$2,168,333.92—

which leaves an—

Excess of cost over net book value thereof, \$7,988,938.58.

Does that figure accurately represent the gain in money value to the company of the facilities?

Mr. FERGUSON. No, sir.

Mr. RAUSHENBUSH. Will you explain that, please?

Mr. FERGUSON. I can only explain it in general terms; Mr. Branch would have to give you the details.

Further (p. 5324):

Mr. RAUSHENBUSH. Is there any question on that? We found this in the Price, Waterhouse report and assumed that that was correct, that the company had gained practically \$8,000,000 in its wartime facilities through advances by the Navy Department, which it then retained.

Mr. FERGUSON (examining book handed witness by secretary). I have never seen it before, Mr. Raushenbush, and I am trying, in answer to one of your queries, to answer it, which tells what benefit there accrued to us in response to the taking over by purchase in final settlement of the facilities provided by the Navy Department and the Shipping Board, and if I can get the number of the question, I can find the answer.

Mr. RAUSHENBUSH. I do not remember having asked the question in that form about facilities.

Mr. FERGUSON. As I understand it, you are asking me if we get the benefit of \$7,988,000.

Mr. RAUSHENBUSH. That was not one of my questions. I am asking it now.

Mr. FERGUSON. My answer to that is that we did not, but I have got to see it. Will you repeat the question?

(The pending question, as above recorded, was read by the reporter.)

Mr. RAUSHENBUSH. The question prior to that was a reference to the Price, Waterhouse report, showing that the total cost of facilities was \$10,157,272, and the net cost of same to the company was \$2,168,333, and the excess of cost over net book value to be \$7,988,938. The question was to as the accuracy of the Price, Waterhouse computation in that manner. Is that accurate?

Mr. FERGUSON. So far as I know it is accurate as to the figures in the total settlement, but I would like to say that in putting in plant for the Navy Department—I do not remember the Shipping Board—it was agreed that the Navy Department would advance 50 percent of the cost of the plant, approximately, and we would advance the other 50 percent, and in our contracts it was provided that at the conclusion of the work this plant which had been put in would be appraised by the Navy Department and the price to be paid by us for this additional plant would be fixed by them, and that was done. The reason was that you could not tell. It was generally assumed at the beginning that the plant would cost, as shown by the agreement, approximately at that time twice what it would cost, let us say, in normal times. And after the contracts were terminated and these three large contracts were settled, this proposition of plant appraisal was made, after years—I do not know how many, 2 or 3 or 4 years—negotiation with the Board in the Navy Department that had cognizance of it, and the settlement was made by that Board.

Mr. RAUSHENBUSH. Let me interrupt just a moment, Mr. Ferguson.

Mr. FERGUSON. Yes.

Mr. RAUSHENBUSH. Was not the basis of that arrangement fixed way back in 1919?

Mr. FERGUSON. Yes.

Mr. RAUSHENBUSH. So that the matter was all settled then, rather than later?

Mr. FERGUSON. It was written, Mr. Raushenbush, into the contracts.

Mr. RAUSHENBUSH. Here is a letter of yours to Mr. Huntington of January 7, 1919, which I want to read in this connection on the phase of appraisal of values:

I wired you Saturday the status of the two new battleship contracts, as we had to get our letter in the hands of the Department today. I have since been in telephone communication with Mr. Gauntlett—

Who was Mr. Gauntlett?

Mr. FERGUSON. He was our Washington representative.

Mr. RAUSHENBUSH. Is he the representative of any other companies?

Mr. FERGUSON. Yes, sir; two or three more.

Mr. RAUSHENBUSH. Which ones?

Mr. FERGUSON. He is a representative of the Aluminum Co. and the Matson Navigation Co.

Mr. RAUSHENBUSH (continuing reading):

I have since been in telephone communication with Mr. Gauntlett, who informs me that the Department will probably agree to give us these two battleships at a cash profit of \$1,250,000 each, and will agree to make the necessary plant extensions to take care of them, at a cost of not more than \$2,500,000.

This was after the war, was it not? This was January 27, 1919.

Mr. FERGUSON. It was after the armistice, but the war, I think, officially went on some time longer.

Senator VANDENBERG. It is still going on.

Mr. RAUSHENBUSH. Here it says about the plant extensions:

* * * the plant extensions to be turned over to us at the end of the contracts, and if the appraised value at that time is 1½ million, or less, they will become our property, and if more than 1½ million, we will pay the difference between the 1½ million and the appraised value, the appraisers to be appointed, 1 by the Navy Department, 1 by ourselves, and the third to be selected by those 2. I do not think that the appraised value for the 2½ million plant extensions, such as is contemplated of shipways, piers, etc., will be as much as 1½ million, and I instructed Mr. Gauntlett to tell the Secretary that we will agree to this arrangement.

Then it goes on with an explanation which I would like to have you explain [reading]:

The Department's interest in the matter lies in the fact that they are not willing to show on the face of a contract that they are paying more than 10 percent as profit. At the present time the total cash profit of 2½ million on the two battleships, plus the 1½ million they are willing to allow us as profit on the plant, will amount to \$4,000,000, which is 10 percent of the estimated cost of the two vessels.

Here, apparently, if this letter is correct, Mr. Ferguson, the Department was, after the war, making an arrangement to allow more than a 10-percent profit by giving you an increase in your facilities which would amount to a considerable sum over the 10 percent. Is that letter correct that way?

Mr. FERGUSON. No such arrangement was made.

Senator CLARK. You indicate in that letter that the Navy Department was just trying to beat the devil around the stump to try to allow you more than 10 percent, do you not?

Mr. FERGUSON. We did not take a contract for the two battleships, Senator.

Senator CLARK. But that was your impression at the time you wrote this letter, that that was what the Navy Department was trying to do, to figure out a scheme to give you additional plant facilities, to keep it from appearing on the actual face of the contract that they were giving you more than 10-percent profits. That was your impression at the time of writing the letter?

Mr. FERGUSON. It was; but it was not done.

Senator CLARK. The only reason it did not go through was because you were not satisfied with the arrangement?

Mr. FERGUSON. No; this was preliminary to a two-battleship contract. It was actually changed to a one-battleship contract, and the contract for the battleship indicates exactly the arrangement made.

Senator CLARK. Why was it that the Navy Department did not want it to appear on the face of the record what the transaction actually was? In paragraph 2 of this letter, Mr. Ferguson, you state:

The Department's interest in the matter lies in the fact that they are not willing to show on the face of a contract that they are paying more than 10 percent as profit.

Mr. FERGUSON. Yes, sir.

Senator CLARK. The arrangement suggested was in effect paying more than 10-percent profit, was it not?

Mr. FERGUSON. The arrangement suggested; yes.

Senator CLARK. Yes, sir. Do you know why it was that the Navy Department was not willing to have it shown on the face of the contract exactly what the real transaction was?

Mr. FERGUSON. All I can say, Senator, is that the arrangement—I had forgotten the letter—did not go through, and I have here the contract.

Senator CLARK. I understand it did not go through, Mr. Ferguson, but what I am interested in is, on January 27, 1919, in writing to the owner of your company you explained the fact that the Navy Department was not willing to have it shown on the face of a contract what the real transaction was intended to be. That is correct, is it not?

Mr. FERGUSON. I have no doubt, Senator, that it was discussed, from this letter, with the representatives of the Navy Department, but it was not done.

Senator CLARK. Yes, sir; but it was stated to you, or at least you stated to Mr. Huntington, that the Navy Department's interest in the matter was to cover up what the exact transaction was to be.

Newport News attempted to have its war-time taxes lowered on the ground that its war-time naval contracts were force contracts (Feb. 12, 1935, p. 5299, et seq.)

Mr. RAUSHENBUSH. I am not making any recrimination about it. That is the inference shown by these letters.

There are some more things about this tax business which we are going into, not to do anything more—and I hope you understand this—than to plan for taxes for any possible future war, because the tax matter worked out in the last war is about the only light we have guiding us for any future taxes.

We find something which interests us quite a little bit: That in 1924, apparently one of your employees, Mr. Gatewood—he was the manager at that time and still is?

Mr. FERGUSON. He is manager now; at that time naval architect.

Mr. RAUSHENBUSH. This letter dated December 11, 1924, to Mr. Rearick, of your legal staff, is signed by "W. Gatewood, manager."

Mr. FERGUSON. He may have been.

Mr. RAUSHENBUSH. This is a rather long story, and I think we can shorten it somewhat, but he got the idea, did he not, that all these somewhat profitable contracts you had made with the Government for warships were not contracts at all but they were force orders imposed upon you by the President?

Mr. FERGUSON. They were order contracts, and our war contracts for these vessels were under Presidential order, and so stated in the contracts.

Mr. RAUSHENBUSH. And so stated in the contracts, as you contend?

Mr. FERGUSON. Yes.

Mr. RAUSHENBUSH. And Mr. Gatewood goes on in this letter to Mr. Rearick, which I offer for appropriate number, to state:

No opportunity was afforded the taxpayer to decline to make the contracts or to adjust his price to suit the excessive tax. This provision of the act which seemed to be ex post facto even though the larger part of the income from the contracts subject to the excessive tax would not accrue until after the date of the act.

What he was trying to do through here, was he not, if you will remember the situation, Mr. Ferguson, was trying to avoid the payment of taxes at the 1918 rates, the high rates by stating and making a case that these many contracts you had with the Government were not contracts but were force orders and consequently did not come under the head of the taxes imposed on war contracts, which were high?

Mr. FERGUSON. I am not familiar with the letter.

Mr. RAUSHENBUSH. You are familiar with the whole company's attitude?

Mr. FERGUSON. I am familiar with their attitude; yes.

Mr. RAUSHENBUSH. You know that the company took this up with its attorneys and then the attorneys and Mr. Montgomery made complaint to the Government, protest to the Government?

Mr. FERGUSON. Yes.

Mr. RAUSHENBUSH. Under this, do you mean?

Mr. FERGUSON. Yes.

Mr. RAUSHENBUSH. They did attempt to have all your war contracts, the taxes on all your war contracts, thrown out on the ground that they were not contracts but were force orders?

Mr. FERGUSON. I do not know whether they attempted to have them thrown out.

Mr. RAUSHENBUSH. You have the high taxes thrown out. We have your protest by Bickford and Rearick, your counsel, before the Bureau of Internal Revenue to that effect.

(The letter referred to was marked "Exhibit No. 1559" and is included in the appendix.)

Mr. RAUSHENBUSH. Mr. Chairman, the point of going into this is this: The field seems to offer some opportunities. Quite a constitutional question is made here, not only by the company, but its attorneys, that if you are in a state of war, and a contract is forced on you, it is not a contract, and so if Congress comes along and says an 80-percent tax shall be imposed on all war contracts,

between certain dates, that that does not go for the business of some of the companies because of their contracts being on force orders and therefore the taxes would not apply.

And in planning taxation matters that field should be plowed one way or the other. If I may, with the consent of the committee, I will go ahead on that for just a moment.

We have here a letter from Mr. Bickford. He was of your counsel, was he not?

Mr. FERGUSON. General counsel at that time.

Mr. RAUSHENBUSH. To Mr. Rearick. He was special counsel for you?

Mr. FERGUSON. Yes, sir.

Mr. RAUSHENBUSH. Stating in the second paragraph:

I concur with Mr. Gatewood that it is unjust and unconstitutional, but

I think it would be dangerous to urge the grounds which he assigns as they fly too far and expand the case unnecessarily.

Mr. RAUSHENBUSH. I offer that as exhibit no. 1560.

(The letter referred to was marked "Exhibit No. 1560" and is included in the appendix.)

Mr. RAUSHENBUSH. Following that we have a claim before the Commissioner of Internal Revenue, and if you care to follow this from the book, or we have copies of it here, you may. We have taken extracts out, if you care to look at that, and it makes the whole case there. In the first paragraph it says:

Taxpayer was required to proceed with the orders without any of the power, privileges, or profits of a contractor, therefore the provisions of the Revenue Act of 1918 imposing an additional tax in the years 1919, 1920, and 1921 on profits derived from "Government contracts" made between April 6, 1917, and November 11, 1918, was not intended to and did not apply to work performed pursuant to the mandatory orders of the President of the United States.

The claim is then made, and the evidence is shown to the extent it can be compiled, that these were not in any sense contracts or contractual money was not involved, so that the 80-percent rate in the 1917-18 war contracts should just be wiped out.

Senator VANDENBERG. I assume the Government denied that claim and subsequently was successful. Is that right?

Mr. RAUSHENBUSH. This is a claim made up by Mr. Montgomery, Senator, in this matter: Protest against income and profits tax deficiencies proposed for the years 1917 to 1921, inclusive; and the Government, in reply to your question, did throw out the contention, but Mr. Montgomery made this statement in a part of the brief:

It was clearly not the intention of Congress to tax at what are really penalty rates, income derived from the execution of the President's orders.

After making the point about these contracts not being contracts [continuing reading]:

Section 301 (c) of the Revenue Act of 1918 was inserted by the conference committee, and in explaining it to the House, the chairman of the Ways and Means Committee said:

"Though the 80-percent war-profits tax is eliminated for the next fiscal year—since there are no war profits for 1919-20—the conferees put in a provision extending the 80-percent war-profits tax for the calendar year 1919 to catch the profits that are derived in 1919 from war contracts made in 1918 and 1917, so that the profiteers will not get off with 80 percent eliminated after January 1, 1919."

Mr. Montgomery goes on:

The owners of shipyards who were prevented from undertaking lucrative commercial work and were commended to devote all their facilities to the production of vessels for the Government at prices stipulated by the Government can hardly be considered the profiteers the conference committee intended to reach.

That is the point, and the returns on the revenue agent's findings, now not on invested capital, according to any agreement, but on the revenue agent's findings show that for 1918 the company was getting a return of profit to invested capital, as the revenue agent found it, of 76.1 percent and in 1919 of 71.5 percent.

(Document marked "Exhibit 1561" and is included in the appendix.)

Senator VANDENBERG. How was the price fixed in one of these forced contracts?

Mr. RAUSHENBUSH. We have here one of those contracts included in the company's protest. It is a regular form contract. Mr. Ferguson can probably

give you the actual fixing of the price. It says "cost plus 10 percent", and the definitions of "cost" are given, including all taxes there. We had this discussed when New York Ship was here.

Senator VANDENBERG. Mr. Ferguson, when we are discussing this so-called "force contract", are we discussing the cost-plus-10-percent contracts?

Mr. FERGUSON. Some of them were cost plus 10 percent. They were all changed to cost plus a fixed fee. Some of them were cost plus a fixed fee in the first place. The only cost-plus-10-percent contracts which we ever completed was the first of a group of destroyers—

Senator CLARK. Was that during the war, Mr. Ferguson?

Mr. FERGUSON. Yes. The battle cruiser contracts were signed in 1916, and they were cost plus 10 percent but later on changed to cost plus a fixed fee of \$2,000,000. The battleship *Iowa* was cost plus a fixed fee from the beginning. A group of tankers we built for the Navy Department were cost plus a fixed fee, plus one-half of the savings under a certain price.

Senator VANDENBERG. This is after the war, is it not?

Mr. FERGUSON. No; this was during the war. It was during the war period. I do not remember just when the battleship *Iowa* contract was settled.

The first contracts provided that taxes of all kinds would be included as an item of the cost, before the war taxes were set. The later contracts, I am quite sure, showed that they included taxes except Federal profit taxes.

Senator VANDENBERG. The first contracts included income taxes and everything else?

Mr. FERGUSON. They included taxes of all kinds.

Senator VANDENBERG. What was there about a cost-plus-10-percent contract which so invaded the ordinary contractual prerogative that it ought not to be considered in ordinary tax practice?

Mr. FERGUSON. I take it—it is a legal question with which I am not acquainted—but I take it that being a Presidential order contract—

Senator VANDENBERG. I am not asking about the legal phase. I would not undertake to enter that field, either. I am talking about the practical phase. Do you not invite the inference that if you consider a cost-plus-10-percent contract an invasion of your ordinary contractual privileges, do you not invite the presumption that a 10-percent profit above all cost items is a great hardship, and a great invasion of your usual opportunity of doing a great deal better than that?

Mr. FERGUSON. No.

Senator VANDENBERG. It seems to me that you do. Go ahead, Mr. Raushenbush.

Mr. RAUSHENBUSH. The point that you were to accomplish by these protests which were laid before them by Mr. Montgomery and your learned attorneys and others was simply to reduce the taxes on all the Government work during the war, on the ground that it was a force contract? That is not to say that 10 percent was too much or too little, but that the taxes were too much. Was not that the point of it?

Mr. FERGUSON. I presume so.

Mr. RAUSHENBUSH. Then we turn to all the changes which were made, Mr. Ferguson, in your contracts. We find here a letter from you to Mr. Huntington, dated July 14, 1919, in which, in the second paragraph, you say:

We also discussed changing the battleships and battle cruisers to cost plus a fixed fee, and, although we reached no conclusions, I think it likely that we will do so. We would like to change the battle-cruiser contracts absolutely so as to get the date of the contracts out of the war period, and avoid the high tax on profits. The Secretary did not raise any particular objection to \$2,000,000 fixed fee on each of the two battle cruisers, and \$1,350,000 on each of the two battleships.

And it is very clearly stated, is it not, Mr. Ferguson [reading]:

We would like to change the battle-cruiser contracts absolutely so as to get the date of the contract out of the war period, and avoid the high tax on profits.

That was the point of changing all these contracts from a cost plus to a cost plus a fixed fee, was it not, and getting the date on them changed to get them out of the period when an 80-percent tax was put on contracts?

Mr. FERGUSON. Contracts were entered into for battle cruisers before the war. Then, after the war period, we changed to cost plus a fixed fee, and naturally, if we could and if they were not war work, were not done during the period of the war.

Mr. RAUSHENBUSH. You say—

so as to get the date of the contract out of the war period, and avoid the high tax on profits.

Mr. FERGUSON. Yes, sir.

Mr. RAUSHENBUSH. You are talking about Government contract work during the war. Then on December 17, 1919, in a letter to Mr. Huntington, you state:

Last Friday in Washington I went to see Secretary Glass, of the Treasury Department, at the suggestion of Secretary Daniels, in regard to the Federal tax on our two battle cruisers, the contracts for which were signed on May 25, 1917, or during the war period.

This was during the war period and not before or after. These were signed during the war period.

Mr. FERGUSON. I thought they were signed in 1916.

Mr. RAUSHENBUSH. You say to Mr. Huntington—

in regard to the Federal tax on our two battle cruisers, the contracts for which were signed on May 25, 1917, or during the war period. There is a special war excess-profit tax on Government contracts made during the war period, and before agreeing to any change in our contracts for the battle cruisers, we wanted to develop whether these cruisers were to be held by the Treasury Department to have been contracted for during the war period as the award and the agreements relative to the construction of these cruisers were actually settled before the war.

The Treasury Department officials appeared to be very willing to give us an opinion as soon as we could put up our case, which we will do with our income-tax returns for this year, if not before.

Then we go on to April 12, 1920, in a letter from you again to Mr. Huntington, on the second page, fourth paragraph:

We are engaged in shifting our two transports from a cost-plus-fixed-fee basis to a fixed-price basis, which will give us a greater profit than we would otherwise make, and I am quite sure will relieve us of a great deal of annoyance in having the Fleet Corporation auditors around the place.

Here are these transports for the Emergency Fleet Corporation?

Mr. FERGUSON. These were two transports we got for the Emergency Fleet Corporation on a cost-plus basis, and those were changed, at my suggestion, to a fixed-price basis, agreed upon between them and ourselves, and we made more than we would have made on the original contract, and the transports cost the Government about \$1,000,000 less apiece than other transports that were furnished on the cost-plus basis.

Mr. RAUSHENBUSH. Others not in your company?

Mr. FERGUSON. No; but in other companies.

Mr. RAUSHENBUSH. We hardly know the circumstances of the other companies.

Mr. FERGUSON. I am saying that we made more money and the Government saved \$1,000,000 apiece.

Mr. RAUSHENBUSH. At the time of the shifting you state that the shifting from a cost-plus fixed-fee basis to a fixed-price basis—

will give us a greater profit than we would otherwise make, and I am quite sure will relieve us of a great deal of annoyance in having the Fleet Corporation auditors around the place. These transports, or passenger ships as they will now be, are getting along very well and we will launch the first one in the summer. We have not yet shifted our 2-battleship and 2-battle-cruiser contracts from cost-plus-10-percent to cost-plus-fixed-fee basis as the Navy Department wants to do, for the reason that we have not been able so far to find out just how to do it and be safe.

What do you mean by "how to do it and be safe"?

Mr. FERGUSON. I do not remember what I meant.

Mr. RAUSHENBUSH (continuing reading):

I think that the best method would be to simply agree to a fixed fee as a change under the contract instead of 10 percent and have all the rest of the contract remain as it is.

You are still on the question of changing the base on those, are you not?

Mr. FERGUSON. No, sir; that means as you make changes under the contract, as was done, that a new contract was not made.

Mr. RAUSHENBUSH. Are you sure of that?

Mr. FERGUSON. A supplemental contract, but a new contract was not made, taking the cruisers out of the war period.

Mr. RAUSHENBUSH. Are you sure of that?

Mr. FERGUSON. Yes; I am quite sure.

Mr. RAUSHENBUSH. Mr. Branch?

Mr. BRANCH. That is correct.

Mr. RAUSHENBUSH. Then all these attempts came to nothing?

Mr. FERGUSON. It looks so.

Mr. RAUSHENBUSH. You kept after it year in and year out, apparently, explaining to Mr. Huntington in a letter of June 1, 1920:

Last week we changed out contract with the Shipping Board for the last two troop transports from a cost-plus-fixed-fee basis to a fixed-price basis. Our fee was to be \$350,000 for each ship plus one-half of the saving under a certain estimated price. We are now to get a little over \$6,100,000 per vessel, and we think we should make about \$750,000 profit on each vessel. We have canceled the former contract and written a new contract which we believe will take it out of the war period completely, and so we will not have to pay the extra tax on war profits on its since February 23, 1920, on these contracts. Mr. Palen negotiated this trade which I think was very advantageous from every point of view.

Then it goes on:

In regard to the two battle cruisers, we have tentatively agreed with the Navy Department, as previously discussed with you, to change these contracts from cost-plus-10-percent to cost-plus-a-fixed-fee basis, the fixed fee being agreed upon as \$2,000,000 per cruiser. For almost a year the Department has wanted us to write a new contract and particularly to change our old contract with regard to taxes. We have refused to do this and now will hold to our old contract, but simply agree in a letter to accept a fixed fee of \$2,000,000 for each vessel instead of 10 percent.

Why did the Navy Department want you to write a new contract there?

Do you remember that?

Mr. FERGUSON. I do not remember. Presumably to cut out taxes as an item of cost.

Senator VANDENBERG. This is after the war, is it not?

Mr. FERGUSON. Yes, sir.

Newport News met opposition from the Treasury in its attempt to shift profits to the post-war years in which tax rates were lower than in the war years (Feb. 12, 1935 p. 5296 seq).

Mr. RAUSHENBUSH. You were aware of the fact that the Treasury Department was opposed to your attempting to shift the profits out of the high war tax years into the lower post-war tax years, were you not?

Mr. BRANCH. That is true; we were conscious of it as it went along.

Mr. RAUSHENBUSH. You were not only conscious of it but you had acceptance of it because of this confidential report to the Treasury Department concerning this price?

Mr. BRANCH. I might say that I knew of the report, Mr. Raushenbush.

Mr. RAUSHENBUSH. I want to offer for the record "Confidential report of the internal-revenue agent examining the Newport News books, dated March 30, 1927", which I will show you [handing paper to witness].

(The document referred to was marked "Exhibit No. 1557" and is included in the appendix)

Mr. RAUSHENBUSH. I show you on the second page, the third paragraph, a comment on what seems to be this practice of shifting profits around to what the revenue agent thinks avoids the higher war taxes.

This, Mr. Chairman, is in point upon this question: If very high war taxes are put on, and this sort of practice is possible, then everybody who is taxed under a high rate will probably wait and do their best to postpone the settlement and postpone the taking of their profits until after the war is over, when everybody will think taxes will drop, as they did during the last war.

The paragraph reads:

About the time of closing the books each year many memoranda are not actually issued until January of the following year, and the auditor is told by Mr. Ferguson (dictated often by Mr. Gatewood) how to close certain long-term contracts. Particular reference is made to memorandum dated January 11, 1922, pertaining to 1921 closing, regarding contracts for hulls 261 and 262, which states "no change from present instructions." This memorandum bears initials of Mr. Gatewood. These are the contracts where \$2,283,474.88 profits were not reported until 1922, although contracts were fully paid and work had ceased for several months prior in 1921.

Mr. Gatewood and Mr. Ferguson should each be required to state under each why this large amount of income was not reported in 1920 and 1921, when only 10 percent of expenses was taken as profits each month in those years. Certainly at the end of 1920 they knew what percentage of the contract was completed and should have adjusted the profits in 1920 to show the proper income for 1920 as required by article 36 of regulations 62. Again, they should have restated their profits at the end of 1921 when the contract was actually closed. The same condition appears in many other contracts, which are detailed in my report in exhibit II.

I do not wish to accuse these gentlemen of any wrong intent, or even intimate such, but I cannot help but feel that such action was intentional, whatever the motive. But I have refrained from making any suggestions of wrongdoing in my report, but I hold that the income properly belongs in 1920 and 1921 and a penalty for negligence should be added for not restating same.

Another paragraph on the third sheet states:

Mr. McMurrin—

Was he the auditor at that time?

Mr. BRANCH. Yes, sir.

Mr. RAUSHENBUSH. Was he your predecessor, Mr. Branch?

Mr. BRANCH. Yes.

Mr. RAUSHENBUSH (reading):

Mr. McMurrin, the auditor, declined to come to the conference on March 12, 1927, stating that, as Mr. Gatewood had taken charge of the tax matters, he (Gatewood) should assume full responsibility. Mr. McMurrin stated that, if he (McMurrin) had been allowed to close the books, the profits would have been reported in accordance with the income-tax law, no matter what tax developed. I could not help noticing an apparent friction between Gatewood and the auditing department.

The letter then ends up:

The corporation is owned and controlled by wealthy people, fully able to pay the Federal taxes when properly determined, plus interest and penalties.

After consideration of this letter, it may be thought that more drastic action should be taken and fraud penalties.

That was the very thing you were talking about, was it not, Mr. Branch, and which the Treasury Department thought should be one way and you thought should be another?

Mr. BRANCH. Yes, sir.

Mr. RAUSHENBUSH. Do you want to comment on that, Mr. Ferguson?

Mr. FERGUSON. May I state in connection with 261 and 262, which were mentioned, that they were two oil ships, the largest ever built, for the Standard Oil Co. of New Jersey. These vessels were of new design and were much larger than any ships that had ever been built up to that time. The guarantee on those ships ran for 1 year after delivery.

The company was liable for the ships for a year. The income-tax people said that the profit should be taken at the time when the money was paid. We held that on account of the risk involved through a year's guarantee on a ship of a tremendous size, and different from any other oil ship, that we or anyone else had built up to that time, that we should be protected until our guarantee period should elapse.

In the case of other ships he refers to, they were two oil ships building for the A. G. W. I. interests. In that case the company became involved in financial difficulties. We kept the ships for 6 months. We accepted the bonds, which could not be sold, in payment for these ships. We did not wish to enter the profits on the ships until the bonds had been paid, or could be sold by us. The Treasury Department ruled that we had to take the profit when we accepted the bonds and could not wait until the bonds had been demonstrated to be good.

Mr. RAUSHENBUSH. There are some letters on that, Mr. Ferguson, which seem to include something more than the A. G. W. I. ships.

Senator BARBOUR. May I ask, if I may interrupt, were the bonds good?

Mr. FERGUSON. They were eventually paid off; yes, sir; and we took the profit when the notes represented by the bonds were paid.

Senator VANDENBERG. Did the postponement of the profits into subsequent years result in a tax advantage to the company in net result? Would it have resulted in a tax advantage?

Mr. FERGUSON. It would have but it did not.

Senator CLARK. How great a tax advantage, Mr. Ferguson? Can you tell us roughly what the difference would have been between the two constructions of the tax?

Mr. FERGUSON. I beg your pardon?

Senator CLARK. Can you tell us roughly what the difference in the tax would have been under the two constructions?

Mr. FERGUSON. I do not know.

Senator CLARK. Do you have anything which shows that, Mr. Raushenbush?

Mr. RAUSHENBUSH. I cannot work it out exactly, but there are several letters here showing definite attempts.

The CHAIRMAN. It would be quite interesting and the record should carry a completed study on that, showing just what the difference would be, if you will make note and have that prepared.

Mr. RAUSHENBUSH. All right, sir.

We have here a letter from Mr. Ferguson to Mr. H. E. Huntington, dated January 10, 1922. Mr. Huntington was the sole owner of the company, was he, Mr. Ferguson?

Mr. FERGUSON. He and his wife.

Mr. RAUSHENBUSH. He and his wife were the sole owners of the company?

Mr. FERGUSON. Yes, sir.

Mr. RAUSHENBUSH. It says in the second last paragraph:

In connection with the tax situation, we have decided not to take any of the profit we earned last year on the big naval ship work as we do not know at this time just what we will be called on to do, what disposition will be made of the hulls, or whether we will have to bid on them to finish them. * * * I am in hopes of working down our profits for last year to such a point where our taxes will not be so heavy, and legally we do not have to show profit for tax purposes until a job is completely finished and all of our responsibility in connection with it ceases.

I will call your attention to this:

I am in hopes of working down our profit for last year to such a point where our taxes will not be so heavy * * *.

Last year, being 1921, when the taxes were higher than 1922.

I offer that for the record.

(The letter referred to was marked "Exhibit No. 1558" and is included in the appendix)

Senator VANDENBERG. What is that letter?

Mr. RAUSHENBUSH. A letter from Mr. Ferguson to Mr. Huntington, and I was calling attention to a paragraph on the last page.

In addition to that, I call your attention to a letter of February 2, 1922, again to Mr. Huntington, signed by Mr. Ferguson. The third paragraph says:

In going over our tax situation in detail, we find that our taxes for last year will be very much less than I have heretofore indicated to you, as the two Standard Oil ships have guaranties which do not expire until the latter part of this year. It is also probable that we will not take profits for last year on any of the Government work which is canceled, as there is no way of telling what that profit will be.

That is a little more inclusive than the Standard Oil ships, is it not; postponing the profit taking on all Government work?

Mr. FERGUSON. The Government work had been suspended, or partially suspended, and there was no means of telling then what the profit would be.

Mr. RAUSHENBUSH. Do you know to what extent you had accepted it for 1921?

Mr. FERGUSON. The final settlement on the Government contract was made in 1925.

Mr. RAUSHENBUSH. On the canceled ships, as a result of the disarmament conference, you mean?

Mr. FERGUSON. Yes.

Mr. RAUSHENBUSH. The final settlement was made, but the arrangement, I thought you were going to say, was made in 1923. You knew you were going to get \$100,000 a month on that, did you not, from 1923 on?

Mr. FERGUSON. I do not remember that.

Mr. RAUSHENBUSH. We will come to that matter.

I call your attention further to a letter on the question of postponing profits of March 6, 1922, again addressed to Mr. Huntington [reading]:

Our tax return as made up for this year gives us a total Federal tax on income of only \$153,628.62. The reason for this is that we did not put in

the AGWI ships as they are still here awaiting final settlement. We wrote off an additional \$600,000 on the plant and did not put any profit on most of our Government work, as that is in the process of being canceled, and we do not know where we will land.

Mr. FERGUSON. What date was that?

Mr. RAUSHENBUSH. This letter is dated March 6, 1922.

Mr. FERGUSON. The Disarmament Conference met in 1921. It was finally approved and ratified about 1923. In the interim, when there was just a very small amount of work going on, we had no means of knowing what kind of a settlement the Government was going to make.

Mr. RAUSHENBUSH. We will just check the statement about the settlement to be made on the ships, Mr. Ferguson.

I want to call attention to the last part of this paragraph—

We did not put in the main profits of the Standard Oil ships as we have a 12 months' guarantee on these ships which does not expire until the latter part of this year. Of course this will make our taxes for the year 1922 very much larger than they would have been—

1922 was a lower tax year, 15 percent, was it not?

Mr. FERGUSON. Yes, sir.

Mr. RAUSHENBUSH. And 1921 was about 40 percent.

The letter goes on [reading]:

but under the circumstances I felt justified in keeping our taxes for 1921 as low as we legally could.

There was a letter indicating that what you were trying to do was to take the profits in the higher tax years and put them in the lower tax years?

Mr. FERGUSON. Yes.

Wines, liquors, cigars, etc., were charged into the wartime contracts as proper expense (Feb. 6, p. 5087):

Senator CLARK. Did that contract during the war include provision for assessing the services of your Chinese and Japanese representatives and for wines, liquors, and cigars which you actually put into the cost?

Mr. PARKER. It included all costs having to do with operating the business and wines and liquors in shipbuilding are just as necessary as steel in many cases.

Senator CLARK. Do I understand that the contract provided for under the Vinson bill should include wines, liquors, and cigars?

Mr. PARKER. Absolutely so.

Senator CLARK. That is very illuminating.

Senator VANDENBERG. In the case of those cost-plus contracts during the war, do I understand that the items which you included in cost, and which were subsequently eliminated, such as income taxes, and so forth, do I understand that you were authorized to include those at the time in the first instance?

Mr. PARKER. The contract, the first cost-plus contract, provided as one of the items of cost all taxes. That seemed to be authority to include income taxes.

The subject was raised a little later (Feb. 6, p. 5088):

Senator CLARK. Mr. Parker, I would like to have a little further explanation of your very surprising statement a little while ago that wines, liquors, and cigars were fully as important elements in the shipbuilding business as steel. Will you just explain why it happens that wines, liquors, and cigars are just as important in the manufacture of a ship as steel?

Mr. PARKER. Senator, if I would paint a picture of what the use of wines and liquors in the shipbuilding business is—

Senator CLARK. Since the Government has to pay for them, and then pay you an additional percentage of profits on top of them, I think that picture would be very interesting.

Mr. PARKER. All right. Wines and liquors have more to do with the building of the ship than just the champagne bottle that we push it overboard with or the few drinks that may be passed around on a trial trip, which Congressmen and Senators enjoy sometimes. [Laughter.]

In days of old when a trial was conducted, and I am sure we all remember the stories we read of the issuance of grog aboard ship, particularly in a time of stress, of storm, of extraordinary effort, that when a ship is required to go on trial, and you have the picture of 20 men throwing big, hand-picked coal in the furnaces, there are 5-gallon demijohns of liquor alongside them, and they have their drinks of beer and whisky just the same, and it is a matter of rule and routine and just as much a part of the business of operating a ship under these conditions as it is in a restaurant where the service is allowed.

Senator CLARK. Is there any more necessity for dealing out liquor and beer to these men on a trial trip than there is when the ship is in commission in the Navy? Of course, they are sweating from shoveling coal when the ship is on a regular cruise in the Navy, are they not? Is there any particular reason why they should get drunk on a trial trip any more than on a regular cruise? As a matter of fact, Mr. Parker, what this item of wines, liquors, and cigars amounts to is this, is it not: You go on a trial trip and the shipbuilding company is permitted to invite a large number of influential or distinguished people, some of whom may be Congressmen, Senators, or other Government officials, and a general jamboree is held by all, with fine, rich food and fine wines and liquors, and the Government not only pays the bill for that, for the purpose of making friends for the shipbuilding company, but also, under this program arrangement, has to pay you an additional amount for the privilege of allowing you to give a party? Is not that correct?

Mr. PARKER. Senator, when you go back to 1917 and 1918, that was the practice up to that time. That is 18 years ago. The practices which were in existence before the war were continued during that period, of course. But we did not run jamboree parties in naval vessels and never do. The only people on a naval vessel are the trial board and the representatives of the contractor and representatives of auxiliary manufacturers. There is no general jamboree on that.

Senator CLARK. I notice on naval vessels constructed after the war a very large item set down—I forget exactly when it was, but I referred to it when you were last here—a very large item for wines, liquors, and cigars in the construction of those vessels, set down as a part of the cost, on which the Government was required to pay an additional commission to you.

Mr. PARKER. They were Shipping Board vessels, Senator.

Senator CLARK. Whether they were naval vessels or Shipping Board vessels, the jamborees took place, did they not?

Mr. PARKER. They did.

Senator CLARK. You considered that part of the national-defense scheme, did you not, Mr. Parker, to have jamborees?

Mr. PARKER. Well, it certainly had a part of it. It was the first time that many of these Senators from the West and Congressmen from the West had ever seen a real ship in operation.

Senator CLARK. After having taken this pleasure trip, you felt they were better educated as to national defense, and more susceptible to suggestions of the New York Shipbuilding Co. and other members of the "big three"? Do I understand that to be your statement? As a matter of fact, that was the purpose of the trial trip, was it not, Mr. Parker?

Mr. PARKER. I would say that would be true from their attitude. They surely knew more about ships after that.

Senator CLARK. And also the shipbuilders, too, did they not; and had a wider education in the matter of wines and liquors?

Mr. PARKER. Yes, sir.

New York Ship did not give the Treasury the greatest degree of cooperation in its attempt to determine taxes. A report by Treasury officials illustrates one difficulty (Jan. 22, p. 4583 et seq.):

There is further description along the same line, and then it continues [reading]:

To verify the correctness of the taxpayer's returns, or books, it is most essential to procure the schedules referred to and to examine the computations of earned profit on each contract that was made by the taxpayer and appear thereon. Such schedules have been requested of the taxpayer, first over 3 weeks ago, and photostats thereof were promised by Mr. Norman F. Parker, assistant treasurer, almost daily after the first request.

Is that yourself, Mr. Parker?

Mr. PARKER. Yes, sir.

Mr. RAUSHENBUSH (continuing reading):

Last Saturday, on request again for the schedules, Mr. Parker informed us that he had been "stalling" and that we knew it, but that the corporation's counsel had advised him to delay giving the schedules to us. He called his counsel by telephone, a Mr. Orr, connected with White & Case, attorneys, while we were present, and explained the situation, and stated to Mr. Orr that he believed we were entitled to the schedules and should get them. Mr. Orr's advice, we were informed, was not to deliver them.

To date, the situation remains the same, the schedules have been refused on the advice of counsel, so we are informed by Mr. Parker and Mr. J. T. Wickersham, the treasurer.

The points raised by the Solicitor have developed other points that make it imperative, in the opinion of your examiners, after their investigation thus far, that a reexamination be made of the Taxpayer's books for the period extending from 1918 to 1921, inclusive.

Their investigation thus far, with the information we have been able to gather, results in an increase in income over income as determined by the revenue agent from Trenton, who made the last examination for the period 1918 to 1921, inclusive, of approximately \$8,000,000.

It is the positive opinion of your examiners, with the information gained thus far, that there should be recommended to the Commissioner that a reexamination be made of all of the taxpayer's books and records for the years 1918 to 1921, inclusive; and that the taxpayer should be duly notified under the provisions of section 1105 of the Revenue Act of 1926 that such investigation has been ordered.

That was just preliminary, Mr. Parker, was it not, to the examination which was made in great detail in 1926 that resulted in this increase in taxes?

Mr. PARKER. It was just at the beginning of that examination, as I recall it.

Mr. RAUSHENBUSH. Do you have any comment to make on the statement here that you had been "stalling" under the advice of your attorneys?

Mr. PARKER. None, except that that was true.

Miscellaneous items, such as securing business from Japan, were charged into the cost of Government contracts on war vessels (Feb. 6, 1935, p. 5082):

Mr. RAUSHENBUSH. Coming back, then, to this matter of the employment of Mr. Joyner, do you remember back that far, or have you ever had it called to your attention, the matter of a somewhat mysterious check for \$5,000 which he apparently received back there?

Mr. PARKER. What date, Mr. Raushenbush?

Mr. RAUSHENBUSH. That was back on December 31, 1920. There is an order here to make it out for expense, and Mr. Joyner writes Mr. Wickersham [reading]:

Inserted special on expense ship. If this is improper for your purposes, let me know. Mr. Neeland will tell you what the expense is for.

Mr. PARKER. What date is that, sir?

Mr. RAUSHENBUSH. Back in 1920. What was he doing for you at that time, if you remember, Mr. Parker?

Mr. PARKER. I do not recall. I checked Mr. Joyner back for the period—may I see that letter just a second?

Mr. RAUSHENBUSH. Yes, sir; 1920 to 1923 [handing paper to witness].

Mr. PARKER. That is right. I recall it.

Mr. RAUSHENBUSH. But you do not recall?

Mr. PARKER. I recall the amount and the purpose of it.

Mr. RAUSHENBUSH. What was the purpose of that?

Mr. PARKER. Mr. Joyner, as stated in my letter, was engaged to be the New York Shipbuilding Corporation representative for certain work, on a basis of salary and commission. Through his efforts we obtained a Japanese contract for the construction of a naval oil tanker, *Kamo-i*.

Senator CLARK. About when was that, Mr. Parker?

Mr. PARKER. About 1921 or 1922. The basis of his commission was not less than 5 percent of the net profits earned by the company on that particular contract. On the basis of the anticipated profits on the contract, he was paid \$5,000 commission in advance. That is the check to which you refer. He actually received, in final settlement, thirteen-thousand-some-odd dollars, which I have noted there.

Mr. RAUSHENBUSH. If that was a commission, what was the point of putting it in as an expense item? So that he could avoid the income tax on that? Is that the point of that?

Mr. PARKER. That is something I know nothing about.

Mr. RAUSHENBUSH. He definitely puts it in as an expense item [reading]:

Inserted special expense ship. If this is improper let me know. Mr.

Neeland will tell you what the expense is for.

Mr. PARKER. That was a matter of arrangement between Mr. Neeland and Mr. Wickersham, the then treasurer.

Mr. RAUSHENBUSH. It has nothing to do——

Senator CLARK. Did that expense item go into overhead, Mr. Parker?

Mr. PARKER. Yes, sir.

Senator CLARK. That was the Japanese representative about whom we were talking when you left here?

Mr. PARKER. Yes, sir.

Senator CLARK. In other words, the services in Japan in getting this tanker contract were partly charged up to the Government for overhead on the naval construction work which you were doing at that time?

Mr. PARKER. Yes, sir.

A considerable portion of the keels of ships authorized during the World War were not laid down until later. It was from this post-war construction, under war-time impetus, that the shipbuilders made considerable profits relatively free from high war-time taxes (Feb. 6, 1935, p. 5084).

Mr. RAUSHENBUSH. The question is not intended to cover in any way the cause of the delay, but the question is, rather, how it happened that after the war was all over on November 11, 1918, these ships whose keels were not laid at the time were then laid and continued and completed? Can you throw any light on that? You have explained quite satisfactorily that you had to build a yard, and that was the cause for that delay, but my question was the other one: Why, after the war was over, the contracts were not canceled, but instead you were given 10 destroyers to complete, and there were altogether 91 whose keels were laid subsequent to November 11, 1918. Can you throw any light on that at all?

Mr. PARKER. Not at all, except that we had a contract to build ships. The contract was not canceled, and we built them.

Mr. RAUSHENBUSH. I call the attention of the committee to the hearings in Navy Department appropriation bill, 1933, United States House hearings, Seventy-second Congress, on pages 66 and 67, in which these 91 destroyers, of which New York Ship had 10 whose keels were not laid until after the war, being ordered during the war, are listed, and offer for the record the statement just identified by Mr. Parker in reply to question 20.

(The document referred to was marked "Exhibit No. 1530" and is included in the appendix.)

Mr. RAUSHENBUSH. There is an illuminating comment on that, Mr. Chairman, by Admiral Pratt, who gives at least one reason why these destroyers, 91 destroyers, were built after the whole war was over [reading]:

Admiral PRATT. That seems like a very fair question. I cannot give you a real, practical, definite reason why, but I should say this: That if you start a big machine moving, such as this production is, it takes a certain amount of time before it gets slowed up and working normally; and I should think that that had about as much to do with it as anything. We just got swept into it, and before we could get our breath and stabilize and get together, there we were with our output.

The result of that is that there were 91 destroyers whose keels were not laid at all at the time of the armistice, but were begun afterward.

Senator CLARK. The result was we had 91 destroyers which we did not need?

New York Ship bought improvements made during the war by the Government at a cost of \$14,000,000 for \$500,000 (Jan. 21, 1935, p. 4538).

Mr. RAUSHENBUSH. That still does not quite answer my question. You did get from the Emergency Fleet Corporation about \$14,000,000 worth of property for about \$500,000, did you not, and that was the exchange price there?

Mr. PARKER. I won't say \$14,000,000 worth of property. We got the property which may have cost the Shipping Board \$14,000,000, but its worth was less than we paid for it.

Disallowances of Bethlehem Ship claims on war-time cost-plus contracts were discussed on February 26 (p. 5817 seq. (ex. 1642)).

Mr. RAUSHENBUSH. Mr. Shick, on these ships which you built for the Emergency Fleet Corporation in your various plants, we find some disallowances here which we have secured from the Shipping Board on these four plans, and I bring

up the matter not with any feeling that your company was unusual in this respect, because I do not think it was, but as to the way that, in the hurly-burly and excitement of war, with a great deal of pressure, things got done.

We find here a summary sheet, and several files have been examined after the audits by the Fleet Corporation auditors, and they make a request for a reaudit on various grounds.

I want to offer this for the record.

(The document referred to was marked "Exhibit No. 1642" and is included in the appendix.)

Mr. RAUSHEBUSH. File no. 35:

Alterations and Forgeries to Form a Basis for a Fictitious Base Rate.

No. 37:

Marine Auxiliaries Overcharge. Overcharges whereby Bethlehem attempted unjustly to defraud the Government.

No. 39:

Capital investment charged to Government. Attempt by Bethlehem to have the Government bear almost \$2,000,000 in the cost of capital investments charged to ship cost under the guise of overhead. The reaudit eliminated \$1,351,456.39 of this improper charge.

No. 41:

Interplant billings. Attempt of Bethlehem to gain a double profit on interplant work.

And there are some more of the same kind. Then we have the detailed sheets.

Mr. SHICK. Would you mind giving the total amount of these disallowances?

Mr. RAUSHEBUSH. Not at all.

Mr. SHICK. I mean the amount.

Mr. RAUSHEBUSH. I was going to read them from the plant sheets, \$2,218,404 is the total according to our figures.

Then they give the items yard by yard, and one of the interesting things here, Mr. Chairman, is that the Fleet Corporation totals their savings because of the reaudit, and then gives a final saving, which is a good deal less, and the only point there is that the cost of the audit, of policing the whole job, is often very considerable. Here on this Fore River sheet there is a total saving to the Emergency Fleet Corporation of \$253,000 plus, but the only saving really to the Emergency Fleet Corporation is \$135,000. The whole cost of auditing even a smaller job like this—a relatively small one—there is over \$100,000 plus, and so it goes all the way through.

It cost the Government an awful lot to make those \$2,218,000 savings.

On the Fore River plant the Emergency Fleet Corporation in exhibit A here claims \$253,370 plus savings. On the Sparrows Point plant, exhibit A, it is \$1,059,680. On the Moore plant it is \$531,385, and on the Harlan plant \$973,958.

Then they note the items that have been disallowed and consequently have been a saving to them, and summarize them.

There was dispute between the companies and the Treasury concerning their wartime income.

In the case of New York Ship the company reported net income 1917-21 of \$8,444,858. The revenue agents found \$24,296,957. The final compromise settlement was \$13,240,955 (Jan. 21, p. 4543) (exhibit 1420). This settlement was not made until 10 years after 1918.

On its wartime cost-plus contracts the disallowances made from the claims of the company 1917-21 were \$3,597,844 (Jan. 21, p. 4545).

During the war on the cost-plus contracts a 50-percent allowance was made for overhead and was paid by the Government. Revenue auditors calculated the actual overhead as \$2,152,976 less than that paid to the company by the Government (Jan. 21, p. 4551).

It was developed that a former Bethlehem official, Mr. J. W. Powell, left the company to head the Emergency Fleet Corporation. He received as a bonus from the company "a share in all the profits accruing from the contract covering the building of 137 destroyers for the United States Navy and all vessels built for the Emergency Fleet Corporation" (p. 5789 et seq., Feb. 26). He was later a witness

for Bethlehem Steel in a suit against it by the Emergency Fleet Corporation and later submitted a bill for 5 percent of the principal which the court found due to Bethlehem. At the time of the testimony he had not been paid any fee as a witness (Mr. Bromley). Mr. Powell referred to the possibility of there being no decision "for political reasons" on March 9, 1934 (exhibit 1639). His financial interest in the continuing contracts at issue in the suit was admitted.

Bethlehem Ship was able to profit on \$32,000,000 worth of facilities constructed by the Government at its own expense, according to the testimony of its officials (Feb. 27, 1935, p. 5807).

Senator VANDENBERG. What was the nature of your arrangement with the Government under which this \$32,000,000 was made available?

Mr. SCHICK. In the case at Squantum, which was a shipbuilding plant for the building of destroyers, the arrangement was that we go and engineer and build the facility and the Government would pay the bills, which they did. We turned over our organization and all our "know-how" to build this facility, and in building that facility all we did was order the material, do the engineering, and build the facility, and check the bills and approve the bills, and we turned the bills over to the Government and they paid for them.

Senator VANDENBERG. What was your compensation?

Mr. SHICK. We did not make anything out of that. Our compensation was supposed to come out of the profit which we would get from building those ships. If we did not build the ships and had not finished them before the war, we would not have got anything.

Senator CLARK. Then you took the facilities, after they had been constructed at Government expense, and operated them just as though they had been your facilities?

Mr. SHICK. No; those were the Government's facilities.

Senator CLARK. Yes; those were the Government's facilities, but you operated them just as though they were your own and took the earnings from those facilities?

Mr. SHICK. That was the understanding under the contract.

Senator CLARK. So that that was compensation for your building the facilities, the fact that you were going to be able to run them for your own profit afterward?

Mr. SHICK. Absolutely.

The question of the attitude toward wartime taxation of Bethlehem Steel Co., the owner of Bethlehem Shipbuilding Co., was considered with Mr. Eugene G. Grace, president, on the stand (Feb. 25, p. 5754, et seq.).

The CHAIRMAN. In another war—and we come now to a very important question, Mr. Grace—would your associates and yourself be willing to forego the bonuses which were paid to you and to them during the last war?

Mr. GRACE. That I could not tell. That is a question of the method of compensation in our corporation for services rendered. Our system of compensation is to have the individual interested in the results of the work which he performs.

Senator CLARK. Now, Mr. Grace, do you know of any reason why a man who is engaged in industry during a war, either as an executive or a riveter, or anything else you may take, any capacity you may be pleased to use, should be given a bonus as an incentive to extra effort, any more than a man who is in the Army?

Mr. GRACE. Only as it is human nature. I should say that in the production of a property, from my own experience in manufacturing, even if I were working for the Government on the basis that you have outlined, that I will be made major domo of our institution at an Army salary, to run it efficiently, to get efficiency, to get low costs, that I would want to place the proper interests of my workmen on an incentive basis for production.

Senator CLARK. A man who is engaged in military service during the war certainly takes more risks than the man engaged in manufacturing.

Mr. GRACE. Yes.

Senator CLARK. Whether he is a general, a colonel, or a private. He certainly puts in, as occasion may demand, overtime or anything else, and is certainly expected to give his very best effort.

Mr. GRACE. His services; that is true.

Senator CLARK. Without any particular remuneration of any sort except his ordinary pay and his patriotism and idea of doing a good job. Is there any essential difference between industry and military service which makes it necessary, as was done during the last war in some cases, for industrial plants to pay bonuses running into the hundreds of thousands of dollars for services?

Mr. GRACE. I should say that the incentive method of pay in industry is very effective and efficient, and I believe it applies in war just as well as any other time.

Senator CLARK. If a man is drafted, Mr. Grace, and is compelled to fight for the Old Flag for one dollar and a quarter a day, why should not a man engaged in the industrial end of the game—which I agree is very essential, whether he be an executive or a laboring man—also make some sacrifice for the Old Flag?

Mr. GRACE. Theoretically you are entirely right, of course, but can you get the same amount of production, the same amount of effective rendering of service, without the incentive feature put into it? I do not think so. That is all.

Senator CLARK. Of course, that is a matter of opinion, Mr. Grace.

Mr. GRACE. Yes, sir.

Senator CLARK. I do not know a thing about making steel, but I am very well satisfied if you will put an eagle on my shoulders I can get the boys to make steel during a war, and very good quality of steel during a war.

Mr. GRACE. Well, you probably can.

Senator BONE. Mr. Grace, taking your statement of a few minutes ago that there should be uniformity in the rules of the game of war, you were speaking then with respect to salaries. I mean you stated that if there was a horizontal reduction all around, that would be acceptable. But taking that principle, that there should be uniformity in the rules of the game of war, why, then, or how, then, can we justify paying enormous salaries and bonuses to one group—just pick out arbitrarily one group in society and reward them with hundreds of thousands of dollars a year, while all the other groups who are giving their best to the prosecution of the war are kept right on a dead level?

Mr. GRACE. Are you speaking of the man in the service?

Senator BONE. Yes.

Mr. GRACE. Versus the man in industry?

Senator BONE. No bonuses are paid to the men in the service.

The CHAIRMAN. They asked for one after it was all over with.

Senator BONE. They are still asking for it.

Mr. GRACE. And still asking for it. Whether it is advisable to discontinue your scheme of every day in respect to the reward for payment for services rendered in industry during war, during the war period, you must bear in mind that your men are all educated, developed, to be paid for their individual effort. They are with our institution. If I put Mr. Smith on this machine, and Mr. Jones on that machine, exactly identical in every respect, and they work 8 hours a day, and Mr. Smith produces twice as much as Mr. Jones, is not he entitled to more compensation? That is the theory of incentive.

Senator CLARK. If a man is called upon to go through barbed wire entanglements under heavy fire, he is doing more.

Mr. GRACE. But you do not have that scheme in every-day Army life.

Senator CLARK. I am not talking about the fellows who start in with a view of making the military profession their life work. I am talking about the fellows who might be working for your company, and were taken and drafted and were required for \$1.25 a day to crawl out through barbed-wire entanglements, under a barrage, and face the bombs and the poisonous gas and the bayonets of the enemy. They do not get any overtime, and they do not get any bonuses.

Mr. GRACE. No; but maybe we ought to stop and consider a little bit their method of pay.

Senator CLARK. Yes.

Mr. GRACE. The rates of pay which were given to the soldiers. I wonder if it is right to take a man from a \$5 a day job and put him in the Army at \$1 a day. I wonder if we had not better give that man his \$5, or something more, to go into Army service. Have we ever thought of that?

Senator CLARK. Yes; I have, and I am very much in favor of some such scheme.

Mr. GRACE. Maybe that is what we ought to do.

Senator CLARK. In any event, I think it would very much decrease the possibility of war and very much decrease the profits made by the munition manufacturers in the event of war.

Mr. GRACE. I am inclined to think maybe we should give more consideration to that end of it.

The CHAIRMAN. Mr. Grace, have you ever before protested that that was not done?

Mr. GRACE. Have I? No; I have not been a student of war.

The CHAIRMAN. Coming back to the original proposition, are we to understand that the Government got a larger service out of you by reason of the bonus which was paid to you during the war by your corporation?

Mr. GRACE. The Government got a larger service out of me?

The CHAIRMAN. Yes.

Mr. GRACE. For war purposes?

The CHAIRMAN. The Government got a larger service out of you by reason of your ability to draw a bonus, in addition to your salary, than it would have gotten out of you if you had had no bonus?

Mr. GRACE. I do not know how I can answer that question. I am employed on an incentive basis to perform my work. I should say that it has been an inspiration to me.

The CHAIRMAN. The bonus has?

Mr. GRACE. The bonus has been an inspiration in the work.

Senator CLARK. During the war?

The CHAIRMAN. Was it an inspiration to you during the war?

Mr. GRACE. Never thought of it in that time, naturally not.

The CHAIRMAN. Then, are we to draw the conclusion that the Government would have gotten the same service from you during the war, if you had had no bonus?

Mr. GRACE. If I was at the head of the Bethlehem Steel Co., at the most nominal salary, I should have done my best for it during the war and have rendered everything I had.

The CHAIRMAN. The bonus played no part in accomplishing what the United States was after in your individual case during the war?

Mr. GRACE. No; it certainly did not in my individual case.

Senator CLARK. Then the bonus was not really an incentive?

Mr. GRACE. I am talking about the bonus generally in the plan prevailing with the Bethlehem Steel Co.

Senator CLARK. Do you not think the rest of them are as patriotic as you are, and the rest of the men would do the same thing?

Mr. GRACE. Are you talking about these workingmen?

Senator CLARK. I am talking about your whole personnel.

Mr. GRACE. We would have to change our whole system of pay to our workingmen, if we eliminated the incentive for them. We will have to change the whole system of pay, and I should say that that would be very injurious in time of war for the effect it would have on them.

Senator CLARK. How much bonus did you get during the war?

Mr. GRACE. I do not know.

Senator CLARK. Have you any idea?

Mr. GRACE. Yes; it is all here, the whole bonus schedule, the entire bonus, I think.

Senator CLARK. \$1,386,000.

Mr. GRACE. In what year?

Senator CLARK. 1918. That seems to be the figure.

The CHAIRMAN. Before we look into 1918, would we not do well to start in with the bonus program for 1917?

Senator CLARK. I want to ask Mr. Grace one other question. Are you a member of the National Economy League?

Mr. GRACE. The National Economy League?

Senator CLARK. Yes, sir.

Mr. GRACE. I do not think so. I do not know whether I am or not.

Senator BONE. Do you belong to the Liberty League?

Mr. GRACE. Do I belong to the Liberty League? No; I think not.

Senator BONE. Any of your executives?

Mr. GRACE. I do not know. Certainly not active in it. I may belong to it.

Senator CLARK. The National Economy League, Mr. Grace, is an organization that was formed to oppose any compensation to veterans of the World War or any payment of a bonus.

Mr. GRACE. I do not think I am a member of it. I do not think I am.

Senator CLARK. Do you know whether your company has ever contributed to that organization?

Mr. GRACE. I am sure they have not.

The CHAIRMAN. In a letter addressed to your corporation by the committee, question 6 made request for information concerning bonus payments to officers and directors of Bethlehem Shipbuilding Corporation for the year 1917. The response, as submitted to us this morning, is as follows:

Bethlehem Shipbuilding Corporation, Ltd., was organized in October 1917 and began business on or about November 1, 1917. The information for the entire year is given below for the same officers and directors as was previously given for the year 1918, although during part of the year 1917 they acted in capacities other than as officers and directors of Bethlehem Shipbuilding Corporation, Ltd.

Bonuses paid for the year 1917 to officers of Bethlehem Steel Corporation, who were also officers of the Bethlehem Shipbuilding Corporation, Ltd., and of one or more of the other subsidiary companies of Bethlehem Steel Corporation, and who, respectively, received salaries of \$5,000 or more per annum:

E. G. Grace, president, \$1,501,532.

B. H. Jones, secretary and treasurer, \$250,255.

F. A. Shick, comptroller, \$200,205.

H. S. Snyder, vice president, \$350,357.

The committee has averaged these four payments and finds the average to be \$575,612.

I read on from the statement supplied by the corporation.

Bonuses paid during the year 1917 to other general officers of Bethlehem Ship Corporation, Ltd., who were also general officers of one or more of the other subsidiary companies, Bethlehem Steel Corporation, and who respectively received salaries of \$5,000 or more per year:

W. M. Tobias, purchasing agent, \$150,153.

A. Foster, assistant secretary and assistant treasurer, \$17,136.

J. W. Powell, vice president, \$70,793.

Bonuses paid during the year 1917 to other general officers and/or employees of Bethlehem Shipbuilding Corporation, Ltd., Fore River plant, and who respectively received salaries of \$5,000 or more per year:

S. W. Wakeman, general manager, \$4,279.

H. G. Smith, manager, \$18,492.

H. Brown, technical manager, \$15,028.

Now your exhibit, known as exhibit A, which was supplied the committee, revealing bonuses for the year 1918, reveals the following:

E. G. Grace, president, \$1,386,193.

H. S. Snyder, vice president, \$323,445.

B. H. Jones, secretary and treasurer, \$231,032.

F. A. Shick, comptroller, \$184,826.

R. E. McMath, assistant secretary, \$6,187.

E. B. Hill, treasurer, \$46,206.

H. E. Lewis, vice president, \$323,445.

J. N. Larkin, assistant to the president, \$9,113.

J. W. Powell, vice president, \$323,445.

A. Foster, assistant secretary and treasurer, \$36,714.

S. W. Wakeman, vice president, \$49,142.

H. G. Smith, manager, \$112,628.

H. Brown, technical manager, \$112,628.

A. W. Christian, manager of materials, \$7,834.

H. P. Phelps, standardization of plants, \$11,263.

R. Warriner, chief engineer, \$28,157.

H. P. Frear, naval architect, \$28,157.

And some few lesser ones. Let us make it complete, as there are only two more to read:

H. G. Hageman, mechanical engineer, \$5,529; and in the Fore River plant,

H. E. D. Gould, general superintendent and general manager, \$9,834.

Mr. Grace, in 2 years, according to these exhibits, your return in the form of bonus was \$2,887,725. Did the corporation or the Government get an additional service from you by reason of this \$2,800,000 bonus than it would have gotten if you had had no bonus at all?

Mr. GRACE. The method—I will have to answer that this way: The method of paying executives of the Bethlehem Steel Corporation was authorized by the stockholders on the basis that they would be paid a percentage of the profits accruing in conducting the business.

Senator CLARK. Mr. Grace, I do not think you have answered the chairman's question. Did this \$2,000,000, which you got, bring about any additional effort

on your part during the period of the war which you would not have given from patriotic motives, under your ordinary salary?

Mr. GRACE. I meant to say that that was not created for the purpose of incentive of service during wartime.

Senator CLARK. No, sir; but it was continued during the war?

Mr. GRACE. If you will go on, you will find it was existent prior to that, and it has been existent ever since.

Senator CLARK. Yes, sir; but most people during the period of the war in the United States were on a military footing and were prior to the war and during and after the war.

Mr. GRACE. That I do not know.

Senator CLARK. The chairman's question was as to whether this \$2,000,000 which you got personally brought about any additional incentive for the Government's purposes, turning out materials, than you would have made from patriotic motives on your ordinary salary?

Mr. GRACE. Certainly not.

The CHAIRMAN. What was your salary during those years?

Mr. GRACE. I think \$10,000.

The CHAIRMAN. We have a note here, \$12,000.

Mr. GRACE. Maybe 12. It was first 10 and then was increased to 12, and remained 12 throughout the subsequent years, where you have the record of the bonus there, Mr. Chairman. You will find a continuing record of our bonus, the results under our bonus scheme of compensation. I think that carries you all the way up to the present years. Is not that right?

The CHAIRMAN. That is right. For these 2 years, bringing this to a head, the total bonuses paid appear to have been in the neighborhood of \$6,000,000.

Mr. GRACE. Whatever those records show. I could not say.

The CHAIRMAN. We have not had a chance to add them accurately, but that seems to be roughly the figure.

Senator BONE. Mr. Grace, where do the odd dollars come in on the bonus? For instance, in the year 1918 your bonus was \$1,386,193. What are those bonuses predicated on? The profits?

Mr. GRACE. Profits of the corporation.

Senator BONE. In other words, they are a definite fraction of the profits of the corporation?

Mr. GRACE. Of the profits of the corporation, right.

These bonuses were not allowed as part of the costs on cost-plus contracts, according to testimony of F. A. Shick, comptroller of Bethlehem Steel (Feb. 25, p. 5760).

He also stated that the bonus system although set-up in 1904, was not authorized by the stockholders until April 3, 1917 (p. 5763).

Mr. Shick stated in reply to questioning by Senator Clark that the bonus system was in effect in connection with munitions for Russia and England before the United States entered the war (p. 5766).

Mr. Grace stated that he paid \$1,810,000 in taxes in 1917 and 1918, or 66 percent of his taxable income (Feb. 26, p. 5769.)

The question of why the Navy Department continued its wartime building after the armistice was raised on February 26 with Bethlehem officials (p. 5782 et seq.).

Senator BONE. Now, as one of the rather interesting, and what seems to a great many people to be a rather peculiar phase of war, of the last war, after the armistice the Government let a contract for the building of 97 destroyers. The war was over and many of these destroyers were prewar models, prewar design. Can you enlighten the committee as to why the Government let that contract?

Mr. GRACE. I cannot.

Senator BONE. Bethlehem Shipbuilding Co. got 44 of these destroyers. That is the case, is it not?

Mr. GRACE. I do not know how many. I know we built a lot of destroyers for the Government.

Senator BONE. Do you not know how many ships your company got out of this post-war program?

Mr. GRACE. I do not. I could not remember, but we built a lot of them. Did you say the contract was let after the war?

Senator BONE. After the armistice. The keels were laid after the armistice.

Mr. GRACE. There is quite a little difference between contracts and keels.

Senator BONE. Perhaps I misstated it. The ships were built and the keels were laid after the armistice. Instead of canceling those contracts and refraining from building those ships, the Government went ahead and had 97 of these destroyers built after the armistice. That is correct, is it not?

Mr. GRACE. That is a question for you to ask the Government, why they did it.

Senator BONE. I am wondering if you can give us any light on it.

Mr. GRACE. I cannot.

Senator BONE. Your company got 44 of these destroyers at a price totaling \$82,199,916. Is the Union outfit a subsidiary of Bethlehem?

Mr. GRACE. The Union Iron Works?

Senator BONE. Yes.

Mr. GRACE. It is a part of our shipbuilding organization.

Senator BONE. Where are they located?

Mr. GRACE. San Francisco.

Senator BONE. They got five of these destroyers, did they not?

Mr. GRACE. I do not know.

Senator BONE. The record indicates that they got five of them at a cost of \$8,341,059.

Mr. GRACE. Whatever the record says would naturally be true.

Senator BONE. For the 49 destroyers built by Bethlehem and its subsidiary or affiliate, the Government paid a total of \$90,540,975. That very astounding performance has interested a great many people and made them curious as to why the Government would actually have laid the keels and have the ships built for 97 destroyers.

Mr. GRACE. Maybe they did not have confidence the war was actually over. I do not know.

Senator BONE. It may be. It is hard for me to believe, but it may be that the Navy Department had heard vaguely that the war was over, after the armistice.

Mr. GRACE. It may be that they were preparing for another. I do not know what prompted them.

Senator BONE. There may be something in that idea. I would like to dally with the thought, anyhow.

Admiral Pratt, testifying at a hearing before the House Committee on Appropriations, was questioned about this particular construction. One of the Congressmen said he understood some of the destroyers had been laid down after the war came to an end. He says—

Why was it that, with the experience of mass production to which you referred a moment ago; with the realization that we were not just in desperate need to build destroyers at the rate of so many per month or per year—why was it that there was not at that time a slowing down, so as to take advantage of lessons of the war, and to accomplish, in building, the highest, instead of that which can be criticized when mass production is indulged in?

Admiral PRATT. That seems like a very fair question. I cannot give you a real, practical, definite reason why, but I should say this: That if you start a big machine moving, such as this production is, it takes a certain amount of time before it gets slowed up and working normally; and I should think that that had about as much to do with it as anything. We just got swept into it, and, before we could get our breath and stabilize and get together, there we were with our output.

In other words, the Navy Department could not catch its breath, and that it had plunged off into this program of building 97 destroyers because it could not slow down the momentum. Is there any better explanation which you can give us?

Mr. GRACE. Please do not ask me that question.

Senator BONE. You know, probably, more about this game, Mr. Grace, than anybody else in the country.

Mr. GRACE. But please do not ask me to interpret the policies of our Navy Department, my dear fellow.

Senator BONE. I do not want to embarrass you, but I would like to have you tell me outside.

Mr. GRACE. I really could not even tell you outside.

Senator BONE. I can believe that.

Mr. GRACE. I could not. As I say again, they may not have thought the war was over, or were preparing for another one. I cannot tell you.

Senator BONE. The total expenditure for these destroyers which were laid down and built after the war was \$181,247,022, of which your company got \$90,510,975, or about 50 percent. So you ought not to complain about the Navy Department's inability to understand its own program.

Mr. GRACE. You are not inferring that we encourage the Navy Department to go on and build something they did not want are you, I hope?

Senator BONE. Maybe you can explain whether you would or not.

Mr. GRACE. Encourage them to go on?

Senator BONE. Did you discourage them from going on?

Mr. GRACE. We had nothing to do with it. We executed the work the Navy Department wanted us to do, and we are very proud for having done it. The Navy Department had within itself the power, I assume, to cancel and stop work on those contracts. We were not down there asking them to continue the work. We had a contract or obligation with the United States Government, which we were conscientiously fulfilling and were proud of our performance under that.

Senator BONE. Let us get a little more light on this. These contracts were awarded, and when the armistice came and the ships had not been built, you got no word from the Navy Department canceling them, and you just went ahead with the construction?

Mr. GRACE. Certainly.

Senator BONE. Is that the picture?

Mr. GRACE. I assume it is the picture.

Senator BONE. What in this picture proves, or tends to prove, or tends to disprove, the suggestion on the part of the Navy Department that they wanted to keep private shipyards going and wanted to encourage them in every way? Do you think that experience would tend to bolster up the suggestions of the naval officials that they want to sustain the private shipyards?

Mr. GRACE. The picture which you have just given?

Senator BONE. Yes.

Mr. GRACE. I do not see that that has any bearing on it. I think that is a question, as to whether the Navy Department or the Government want private facilities available as to that class of work.

The war profits of Bethlehem Ship were discussed again on February 26, 1935 (p. 5777), in the course of which one report, by a Shipping Board examiner, spoke of the Bethlehem war contracts as "unconscionable and against public interest." The case was in litigation in 1935. The company representatives denied such charges entirely.

Senator BONE. Mr. Grace, there is a charge through this brief, through the report of the special examiner of the Shipping Board, that the Bethlehem Shipbuilding Corporation made unconscionable profits out of the Government during the war. If that be the case, and that is the charge solemnly made in a brief and in the pleadings of this case, whether the Government ought to, in the event of another war, subject itself to the possibility of a repetition of that sort of thing, is the point I want to raise. I know you think you did not make unconscionable profits.

Mr. GRACE. That is a question of opinion, of course. But, as I say, I see no reason—I do not mean the word "reason"—but I think we are in agreement that war should not be the vehicle for unconscionable profits. There is no question about that. There is a meeting of minds on that, without argument.

Senator BONE. In the report of Mr. Adamson, the special examiner, whose report was written in 1923, he uses this language:

Bethlehem's enormous profits may not aid in interpreting the language of contracts, but they do show that the Bethlehem contracts were unconscionable and against public interest.

Mr. GRACE. I think that is all being a part of the suit.

Senator BONE. He indicates in his report that there was almost \$50 per ton profit on one Bethlehem contract, and he contrasts the profits allowed to Bethlehem by Mr. Bullitt on three contracts, with profits allowed on contracts with other shipbuilders. In that respect he points out in contract 300 that Bethlehem's profit was \$49.59 per ton; contract no. 226, the profit was \$43.15 per ton.

Mr. GRACE. Have you Bethlehem's answer in respect to that? Have you the findings made by the referee, Mr. Bullitt, which you speak of, there? Have you the Bullitt report?

Senator BONE. I am referring to Bullitt's report right here.

Mr. GRACE. They are in Bullitt's finding?

Senator BONE. They are in Bullitt's finding. Contract 179, a profit of \$44.88 per ton, and the other shipbuilders represented in this report were J. F. Duthie & Co., I presume for a requisitioned ship, with a profit of \$10 per ton.

Mr. GRACE. I could not tell you.

Senator BONE. American Shipbuilding Co. contract, the profits were \$16.27 per ton. The American Shipbuilding Co.'s profit of \$16.27 per ton has been criticized. It is only one-third as much as Mr. Bullitt reports for Bethlehem on contract 300, and that calls for the statement which I made yesterday in this report of 20.5-percent profit to Bethlehem on ships built with Government funds. Again he refers to a statement by Admiral Bowles, manager of the Division of Steel Ship Construction, and G. S. Radford, manager of the Contract Division. This statement is made by them:

We wish to place on record the fact that the Bethlehem Shipbuilding Corporation's representatives have insisted on comparatively high prices for these vessels; that they have only with difficulty been persuaded to quote us on the types of ships referred to, and their attitude has been characterized by the arbitrary refusal to stand behind delivery dates * * *

While the prices we have agreed to with representatives of the Bethlehem Shipbuilding Corporation are not satisfactory to us, nevertheless they represent a material reduction from the prices quoted by that corporation. Realizing that the Nation will need these vessels, we have been actuated by the belief that further delay in placing the contracts should be eliminated, and we believe we have made the best compromise possible under very difficult conditions.

Why should the Bethlehem people quibble with the Government when war is on over the difference between profits which other companies were getting, or apparently getting, and the profit which you folks wanted?

Mr. GRACE. I cannot analyze the shipbuilding case for you. If you will read the Bethlehem side of it, like you are reading the Government side of it, you may find what the reasons were. If you want to go into that in complete detail, or if you want to go into it in detail, there is a man here prepared to do as much of that as you want, and knows the matter from beginning to end.

Senator BONE. Is not a part of that picture reflected in the fact that the Bethlehem Co.'s profits stepped up enormously during the war? Would not that be the answer?

Mr. GRACE. Bethlehem made a very efficient job of building ships. They may have been relatively cheap ships to the Government. If we made excellent cost in building them, the Government got the benefit of it through our prices, and you will probably find that our ships, when analyzed, were as cheap if not cheaper, to the Government than some of our competitors' ships.

Dividends paid by shipbuilding subsidiaries of Bethlehem Steel totaled \$60,498,529 (Feb. 26, p. 5811).

Mr. SHICK. We used the term "rental."

Mr. RAUSHENBUSH. How much was paid in dividends to the Bethlehem Steel by these various companies, would you say, Mr. Shick, by Bethlehem Shipbuilding Co. during those years, Fore River and Union Iron Works?

Mr. SHICK. It was our practice to have those companies practically pay out all their earning which were available, over to the Bethlehem Steel Corporation because the Bethlehem Steel Corporation was the one paying dividends to the stockholders. There was no reason leaving the earnings accumulate in those companies, so that they were paid over to the Bethlehem Steel Corporation.

Mr. RAUSHENBUSH. Do you have the dividends before you?

Mr. SHICK. I do not.

Mr. RAUSHENBUSH. Do you have them, Mr. Mitchell?

Mr. MITCHELL. I have them, as obtained from the revenue agent's working papers of the income-tax unit. He analyzed the surplus for the various years and according to the books the dividends paid were as follows:

Bethlehem Shipbuilding Corporation, Ltd., paid in 1919, \$1,782,500; in 1920 it paid \$1,705,000; and in 1921 it paid \$20,282,700, a total for the years 1917 to 1921 of \$23,770,200.

The Fore River Shipbuilding Corporation paid in 1917, \$90,000; in 1920, \$4,010,400; a total of \$4,100,400.

The Union Iron Works Co. in 1917 paid \$400,000; 1918, \$1,130,000; 1919, \$1,400,000; 1920, \$5,697,928.19; 1921, \$24,000,000; a total of \$32,627,928.19.

The total dividends paid by these three companies to Bethlehem Steel Co. amounted for those years to \$60,498,528.19.

One company had to be threatened during the war with commandeering before it undertook necessary plant construction (Jan. 21, 1935, p. 4538).

Mr. PARKER. I think the record will show in a number of letters where we did everything that was possible to avoid going into this program of plant construction along with ship construction.

The CHAIRMAN. How long from the time that the Government urged you to supervise the construction of that plant—how long was it before you complied?

Mr. PARKER. It was a very short while, Senator, because they said, "If you do not do it, we will commandeer your land and do it ourselves." So that it did not take very long for us to go along with them.

The CHAIRMAN. What time during the war was this?

Mr. PARKER. 1918.

Senator BONE. Was that to be a Government plant?

Mr. PARKER. That was to be a plant operated by the New York Shipbuilding Corporation management.

The CHAIRMAN. But the Government was to build it?

Mr. PARKER. The Government was to build it.

The CHAIRMAN. You were to supervise the building and you were to supervise the operations after it was completed?

Mr. PARKER. Yes, sir.

The CHAIRMAN. And yet the Government was forced to threaten commandeering?

Mr. PARKER. That is correct.

Further difficulties in preventing improper costs during war years were described by the district plant engineer of the Emergency Fleet Corporation (Jan. 22, p. 4589).

Mr. RAUSHENBUSH. During this discussion Mr. Freeman, the district plant engineer, refers to himself as "Mr. Freeman" instead of saying "I", because this is supposedly an official report.

After summarizing, in the first three paragraphs, his functions and his duties and obligations, he points out in paragraph 4 one of the few changes he made. That paragraph reads:

Mr. Freeman cut down the force from 35 to 10 at the New York Shipbuilding Corporation and also discovered that there was no check on maintenance at this yard, the cost of which was a cost against the ships in general overhead, and on some contracts an additional 10-percent profit was allowed. This matter was pointed out by Mr. Freeman and he was allowed to place four engineers on maintenance. A record of maintenance, month by month, by the New York Shipbuilding Corporation was kept in regular schedule, and at the date of Mr. Freeman starting activities had reached an amount of \$448,805 per month, which was charged against ship construction at a time when only the north yard was in operation, as the south yard had just gotten started.

Then he goes on to point out how he brought maintenance down from an amount of \$448,000 to \$91,000 plus.

The fifth paragraph reads:

Matters were brought somewhat to a head by the New York Shipbuilding Corporation receiving a letter dated February 20, 1920, from our resident engineer, in which their attention was called to the fact that they were doing considerable work in the yard and charging same to maintenance, which was an improper charge, as it was being done without authority, and 11 items were cited on which the work was going on at that time; and the said corporation was advised that we were requesting our resident auditors to withhold payment on these jobs until same were approved, if they were proper charges. On Wednesday, February 25, 1920, we were advised that Mr. Magoon, senior vice president of the New York Shipbuilding Corporation, was in conference in the home office of the Fleet Corporation; and one of the officers of the New York Shipbuilding Corporation at the yard stated

that he was afraid to call him up as he—Mr. Magoon—was in an awful temper about maintenance, resulting from our letter.

6. On the same day Mr. Magoon replied to our letter, stating that he was unable to find any ruling which required him to submit regular application for doing maintenance work for approval and that it was his present purpose to proceed with maintenance work under his usual procedure. On the same day the New York Shipbuilding Corporation wrote to Mr. Frick, manager of construction, Emergency Fleet Corporation, in which they state that the jurisdiction of the plant maintenance by the district engineer's department had been assumed as an extension of its duties in connection with plant construction and that they ask the Fleet Corporation in said letter to issue instructions that will relieve the New York Shipbuilding Corporation from all question of such supervision. It is to be noted that these letters were written the same day as the conference above referred to in the home office. Under date of February 28, Mr. Frick issued instructions to Mr. Miller to remove all engineers in his district whose work was confined strictly to maintenance.

Later, on however, that was changed.

I will now read from paragraph 7:

This department pointed out to various departments further irregularities that the New York Shipbuilding Corporation made in the matter of plant construction and charged to ships. In one case we discovered one of the old ways that had been there for 20 years had been remodeled from wooden construction to concrete construction at an expense of approximately \$126,000; same had been charged to ship construction and apparently had been paid as a ship cost. This was brought very forcibly before the auditing department; and said department, on their own initiative, made an estimate of the improper cost that had already been paid the New York Shipbuilding Corporation. An estimate of our share, amounting to \$750,000, had been improperly paid, and this amount was held up by the auditing department as made to the New York Shipbuilding Corporation. The Navy Department, hearing of this action, called a meeting and stated that inasmuch as they were paying 50 percent of the overhead, that they be allowed to see this list, as they also desired to hold up funds for improper payments, resulting in a similar amount being held up by the Navy Department on March 3.

The proposal to have adjusted-price contracts made the basis of wartime work was made by Mr. Homer, of Bethlehem, on February 28 (p. 5920).

Mr. HOMER. The thought has occurred to me in hearing your discussion the other day about what might be done to take the profits out of war contracts, excessive profits, that there is a possibility that the committee might want to give some thought to a plan of this kind as a basis for operating under a plan to take excessive profits out—

Senator BONE. Might it not be said—

Mr. HOMER. It is going at it another way.

Senator BONE. Pardon me. I did not mean to interrupt.

Mr. HOMER. I am talking more or less personally now, if you will pardon me. But going at it the other way, it seems to me that excessive profits in war are not caused by the deliberate attempt to make excess profits but they are usually by conditions which are unforeseen at the time that a contract is made.

One of the major factors in that condition is that the contractor has a fear that he is not adequately protected in taking a contract under conditions which are so variable and uncertain that he may lose a tremendous amount of money when he gets through.

If you can eliminate that fear, Senator, from a contract you have gone a long way, in my personal opinion, of taking the possibility or chance of excess profits out of contracts, munition contracts, or whatever you want, any contract, so far as that goes. That is just a suggestion. I do not know whether it is worth anything or not.

Senator BONE. It might be said by some, and perhaps with some slight justification, that even under this type of contract that the Government is the one who does the gambling on the contract.

Mr. HOMER. The Government will accept a certain amount of risk, but in the end it will probably save money because it is helping to take the risk of the subcontractor, to a certain extent. I do not believe that the Government

assumes all the risk. It does not. It does not assume all the risk under our present contracts, but it is an equitable means of adjusting things to suit conditions.

Later (p. 5921).

Mr. RAUSHENBUSH. Before we get off this question of your suggestion, Mr. Homer, about having this sort of a system apply to a wartime emergency, here you have, as I gather it, a system where the Government pays for material increases and pays for increases above a certain level.

Now, if that were done during the war, and all contracts were made that way, the Government doing the gambling on any price increases, what point would there be in a company getting any profit? The point of profit, as I understand it, is to compensate the company for risk, and what point would there be in keeping a profit arrangement like that, if the Government is going to take all the risk for which profit is usually given?

Mr. HOMER. In the first place, I do not agree with you that the Government takes all the risk.

Mr. RAUSHENBUSH. Just about all, does it not?

Mr. HOMER. You mean the Government assumes a certain part of the risk in the case of increases or decreases in prices of material and labor?

Mr. RAUSHENBUSH. That is right.

Mr. HOMER. That is not all in building a ship, Mr. Raushenbush. In the first place, there is no consideration being given to overhead expense of any kind whatsoever in this plan, and the contractor has to assume all the risk for that. It is merely an arbitrary basis which is taken, of 40 percent representing material and 30 percent representing labor and something representing the rest—30 percent.

Mr. RAUSHENBUSH. Let us talk about the rest of the 30 percent. Let us talk about the overhead, which is a part of it, and the rest of it is profit. The Government could allow, and does in fact now allow, a certain percentage of overhead, does it not?

Mr. HOMER. On what?

Mr. RAUSHENBUSH. On a ship.

Mr. HOMER. In what connection?

Mr. RAUSHENBUSH. You figure that in the Vinson Act it is supposedly a 10-percent limitation on profit, that the Government is going to allow a certain profit on that.

Mr. HOMER. We hope it will.

Mr. RAUSHENBUSH. Let us apply that to the situation which you suggested.

Mr. HOMER. And it is a legitimate part of cost, is what you mean?

Mr. RAUSHENBUSH. Your only risk, I take it, is in the element of overhead, which involves bonded indebtedness. There is no particular risk there.

Mr. HOMER. The only risk is bonded indebtedness?

Mr. RAUSHENBUSH. I am starting to subdivide the overhead, bonded indebtedness, taxes, and supervision. As I gathered it, roughly, what you are proposing is a system that the Government takes all the risk, that the plant will have none of the risk.

Mr. HOMER. Only a very small proportion of the risk.

Mr. RAUSHENBUSH. What is left is that on which private capital should get a profit?

Mr. HOMER. Do you not see that the Government does not take any risk in connection with the construction of the ship?

Mr. RAUSHENBUSH. You mean if it burns or is badly damaged?

Mr. HOMER. No; in building the ship you assume a risk, because you have got to construct something. You start off with nothing, and you finish with a ship, and it is supposed to be completed in accordance with the plans and specifications. You are assuming a certain risk, if you do not do it, are you not?

Mr. RAUSHENBUSH. Assuming a certain amount of competence on the part of the builders.

Mr. HOMER. Your engineering "know how", your organization all the way through, has to be suitable to do it, and you have to know how to do it, and you have to know how to do it within the cost which you have used as a basis for your estimate.

All this plan does is just to take away a certain part of that great risk which a contractor runs in the face of an inflation, or any other change in the economic conditions, which may change the basic factors on which he has established an estimate and his price, covering a contract over 3 years.

The matter of the war profits of Newport News led to some controversy. The Treasury cut the company's figure of invested capital for 1917 from \$10,000,000 to \$3,800,000 in conformance with regulations. The company did not accept this, and asked to have its taxes determined on a basis which did not involve the figure of invested capital. This was done. The tax dispute was not settled until 1931 (Feb. 12, 1935, p. 5292).

The income figures filed by the company varied greatly with the reports of the revenue agents (p. 5291). For example, in 1921 the company reported taxable income of \$1,366,765, and the revenue agents found \$4,043,000, an increase of 195 percent. The company reported its tax liability for that year as \$153,000. The revenue agents found \$1,663,830. The final settlement in compromise was \$1,303,000, more than nine times what the company reported (p. 5291).

The revenue agent, basing on the finding of an invested capital for 1917 of \$3,826,316 (disputed by the company) found a net taxable income of \$3,467,605, or 90.6 percent. In 1918, on the same Treasury basis (disputed by the company) the profit before taxes was 76.1 percent. In 1919 it was 71.5 percent. In 1920 it was 52.1 percent.

The company entered into the records figures tending to show the profits of the company for these years as (1917) 15.3 percent; (1918) 8.3 percent; (1919) 16.9 percent; (1920) 23.1 percent (p. 5284).

It was admitted by the company's president, Mr. Ferguson (p. 5295), that these figures could not be considered as income-tax figures, and that, based on the company's own returns to the Treasury, the profits were very considerably higher.

III. QUESTION OF EXTENT OF PLANT NECESSARY FOR WARTIME NEEDS

The question of the extent to which private industry must be used during any future war for the manufacture of arms, armaments, and implements of war is an important one. If it is impossible or undesirable because of high cost to build Government plants, and to purchase private plants sufficient to manufacture the necessary arms, ammunitions, and implements of war for wartime, the problem of wartime procurement is very different than if such Government plants can themselves produce sufficiently for wartime needs.

Representatives of the War Department offered to the Committee on December 21, 1934, figures prepared for the Sixty-fourth Congress, which indicated that it would cost \$496,000,000 for plants running on a one-shift basis to supply 1,000,000 men through the first year of war and equip part of a second million men. On a two-shift basis, apparently, the cost would be half, or \$248,000,000. On a three-shift basis the cost of plant might be upward of \$166,000,000.

With Army and Navy appropriations in 1936 running over \$900,000,000, the estimated cost of all the necessary plants (from \$166,000,000 to \$248,000,000) "to run 1,000,000 men through the first year of war, equip a second million men and run them through as much of that year's war as they will get into, and supply the necessary seacoast material", does not seem, comparatively, a disproportionate sum.

The War Department representatives also cited further figures from this estimate as to the cost of plants required "to run 1,000,000 men through the first year of war, equip 3,000,000 more men and run them through as much of the first year of war as they would get into, and supply the necessary seacoast material" on a one-shift basis, as \$927,000,000. On a two-shift basis, apparently, the cost would be half, or \$463,500,000. On a three-shift basis the cost of plant might be upward of \$309,000,000.

The War Department representatives stated that the plants estimated for in these estimates "would be capable of fully maintaining and supplying during the second and any succeeding year of wartime prices named." They qualified the figures by pointing out that present cost of construction might be higher than the old estimates, and that the estimates did not provide for tanks, armored cars, airplanes, or gas equipment.

The question immediately arises as to the policy of preparing for the wartime needs of an army of 2,000,000 men or 4,000,000 men. Apparently it is based on our World War experience, in which millions of troops were sent abroad to fight. If the national policy is to stand ready to send an army of similar size abroad again, the War Department's estimates of cost must be duly considered. If the national policy has altered as a result of experiences growing out of the World War, and the Nation stands ready only to support an army for use in continental America, the estimates must be subject to drastic

revision. Presumably the equipment of 1,000,000 men would be adequate for the defense of our shores or interests in continental America against any possibly conceivable attempt at invasion. In that case the first estimate, on a two-shift basis, of \$248,000,000 could be reduced by the armament thereof applicable to the second million men, and a figure of less than \$200,000,000 for the necessary plant to equip 1,000,000 men would probably be arrived at as a base.

In consideration of the national policy in regard to the sending abroad of millions of men, the recent technological development of warfare should be given due weight. Both submarines and airplanes have been improved greatly since the World War as threats to troop transports. The chances for the successful transportation of our troops through hostile waters has greatly decreased since 1918. Reversely, the chances for the successful transportation of troops into waters adjoining this Nation have decreased.

Decision on this matter will presumably wait upon an official statement of national policy. The committee meanwhile holds that under few, if any, imaginable circumstances will this Nation again be both willing and able to transport millions of troops to nations other than continental America, and that therefore the problem of the desirability of a Government monopoly of certain munitions resolves itself into providing adequate plant for peacetime and wartime supplies for any army of not more than 1,000,000 men.

Such plant can be provided in either of two ways. At present the War Department's plans are to use such Government arsenals as are now available and also to call upon certain industrial plants to devote themselves to the manufacture of such additional munitions as are necessary. The first of three ways of providing the necessary plant is to adopt and extend this plan, by increasing the amount of Government-owned plant so that it will provide fully for the peacetime needs of the Nation, and for a large share of the wartime needs, with the same provisions that the War Department now has for extending production into private plants for the rest of the wartime needs.

The second way is to provide for a governmental monopoly of certain munitions and to produce them both on a peacetime and a wartime basis. It is only in case this second way is chosen that a figure for plant approaching \$200,000,000 need be considered, and this should be subject to analysis in view of the figures developed before the committee by the engineers and accountants of the Interstate Commerce Commission.

Assuming that the first way is chosen, that of increasing the present arsenals and Navy yards so that they will provide fully for all the peacetime needs and a large share of the wartime needs of the Nation, the question is whether the War Department and Navy Department can expand production into new industries as easily and with as great an economy in time as they can at present expand production from a private plant manufacturing, for example, machine guns, into other private plants not having had any experience in manufacturing such guns. The relative merit of Government ownership of munitions plants as against private ownership, in the important matter of spreading into new industry in wartime, without loss of time, is not a matter of principle but of expansion. The Government's situation in respect to wartime needs is much the same whether the problem is to add to the present machine-gun monopoly now under the owner-

ship of Colt's Patent Rapid Firearms Co., located at Hartford, Conn., another private plant of equal size, and whether to add to a Government-owned machine-gun monopoly, located at Hartford, Conn., another private plant of equal size.

Again, at present, "there are not private facilities equipped for the quantity production of artillery and artillery ammunition." The problem of expansion into private industry in wartime would not change at all if governmental facilities were increased. The War Department representatives pointed out that many of the processes of manufacture of both artillery and artillery ammunition may be prepared with standard machines. "Both lend themselves readily to the production of component parts in different plants and later assembling at a central point." In other words, a large part of the expansion into private industry would represent no difficulties, and the purchase of the standard machines by the Government would be unnecessary. Since the estimate for plant and mobile artillery material of \$123,000,000 on a two-shift basis (\$246,000,000 on a one-shift basis) was the largest part, almost half, of the total estimate of \$248,000,000 (two-shift basis) a great reduction in this figure can be made by eliminating the purchase by the Government of the standard equipment necessary for machine, the great supply of shells, etc., necessary in wartime which could be done in already existing private plants. The War Department representatives expressed the opinion that this standard equipment, if purchased, "would mean that in the time of peace there would be standing idle several hundred million dollars worth of machinery." On that basis the cost of the assembling plant and of the war standard operations would be reduced to under \$23,000,000 on a two-shift basis (\$46,000,000 on a one-shift basis). With this arrangement the total necessary plant for running 1,000,000 men through a war would drop to under \$148,000,000.

IV. NAVAL SHIPBUILDING COSTS

A. NAVY DEPARTMENT FIGURES

In part 20 of the Committee's hearings, page 5567 seq. Capt. William G. DuBose, of the Bureau of Construction and Repair of the Navy Department, submitted to the committee certain information regarding comparative costs. The Navy Department had been requested by the committee to compile certain information on the last cruisers for which figures were available, those awarded in 1927 and 1929. He entered into the record (p. 5585) the costs to the Government of vessels built in Government navy yards and those built in private yards.

1927 cruisers.—Navy yards: *Louisville*, \$9,331,337; *Chicago*, \$9,635,747; average, \$9,483,542. Private yards: *Chester*, \$11,543,432; *Northampton*, \$11,689,975; *Houston*, \$11,596,146; *Augusta*, \$11,569,831; average, \$11,599,846. Average difference on 1927 cruisers, \$2,116,304.

1929 cruisers.—Navy yards: *New Orleans*, \$11,614,816; *Astoria*, \$10,401,977; *Minneapolis*, \$9,257,669; average, \$10,423,620. Private yards: *Portland*, \$11,971,794; *Indianapolis*, \$12,602,832; average, \$12,267,313. Average difference on 1929 cruisers, \$1,843,693.

According to these Navy Department figures these four cruisers built in private yards in 1927 cost the Government \$8,465,216 more than four cruisers built in navy yards would have cost, and the two cruisers of the 1929 type built in private yards in 1929 cost the Government \$3,687,386 more than two cruisers of that type built in navy yards would have cost. On the 1927-29 cruiser program, therefore, the private construction cost \$12,152,602 more than the navy yard costs, or enough to have built an additional cruiser of the 1927 type and still have a saving of \$2,669,060, or, instead, to have built an additional cruiser of the 1929 type and still have a saving of \$1,728,982.

The cost of inspection to the Government has not, in the Navy figures, been added to the cost of the ships constructed in private yards. The Secretary of the Navy informed the committee (Report on Naval Shipbuilding, p. 156) that the inspection of ships—private yards—had cost the Government \$3,769,493 from 1927 through 1934 which is at the rate of \$258,184 per \$10,000,000 planned expenditure. The committee estimated an additional cost to the Government for inspection of \$300,000 per cruiser actually built. Addition of this \$300,000 to the cost to the Government of the private-yard cruisers in 1927 would increase the advantage of the navy yards to an average of \$2,416,304 in 1927 and of \$2,143,693 in 1929. The savings on the six cruisers if they had been built in navy yards would be increased from \$12,152,602 to \$13,952,602.

B. INTERSTATE COMMERCE COMMISSION FIGURES

On February 6, 1936, the Chief of the Bureau of Valuation, of the I. C. C., Charles H. Spencer, entered into the record an analysis of the comparative costs to the Government of the three 1929 cruisers built in navy yards and one of those built in private yards in 1929, as of June 30, 1935, for hull and machinery (ex. 4403).

Navy yards: *New Orleans*, \$11,776,400; *Astoria*, \$10,477,727; *Minneapolis*, \$9,775,013; average, \$10,676,380. Private yards: *Indianapolis*, \$12,105,633. Average difference, \$1,429,253.

Mr. Spencer pointed out that the overheads on the three navy yard ships included large amounts for annual leave and holidays for labor, on the *New Orleans*, \$806,382; *Minneapolis*, \$545,594; *Astoria*, \$322,490; an average of \$558,000. He stated that the navy yards paid wage rates 20 percent higher than the private yards and also gave 30 days annual leave with pay during the construction of these cruisers, which leave has since been reduced to 15 days. This reduction would decrease the cost of navy-yard ships by same part, about half of the overhead of \$558,000 per cruiser for that purpose. If this reduction amounted to as much as \$500,000 per cruiser, the average difference would be increased in the future, since the reduction of leave, from \$1,429,253 in favor of the navy yards to \$1,929,253.

He stated that the above figures on costs of construction in the navy yards include depreciation, administrative expense, but did not include taxes (amounting on the *Indianapolis* to \$121,545.91) or insurance (amounting on the same cruiser to \$10,792.45) or advertising, rent of office in New York, personal and relief work, director's fees, legal fees, commissions and royalties, interest on funded debt, surety bonds (\$23,283.45). The depreciation charge on the *Indianapolis* was \$209,622 while the depreciation on the three navy yard ships was \$282,910; \$341,427; \$372,475.

The cost of the *Indianapolis* to the shipbuilding company was given as \$8,791,665, and the payments to the shipbuilding company (New York Shipbuilding) were given as \$11,788,728, the difference of almost \$3,000,000 being profit.

Similar figures for the *Chester*, awarded in 1927, and not a sister ship of the others, were given: Cost to the shipbuilding company, \$7,877,250; payments to the shipbuilding company, \$10,821,083; or almost \$3,000,000 difference, representing profit.

Mr. Spencer pointed out that if new machinery were installed in the navy yards the construction cost in them might be even lower than at present.

The committee believe that for every \$12,000,000 spent on cruisers in private yards the Government could save approximately \$2,000,000 by construction of the same cruisers in navy yards. By transferring the cruiser construction to the navy yards it would get one additional cruiser free for every six built.

V. COST OF ADEQUATE NAVAL FACILITIES

At the request of the committee the Interstate Commerce Commission investigated the cost of construction of adequate naval facilities and of certain munition plants. The study was under the direction of Mr. Charles H. Spencer, head valuation engineer, and of Mr. F. W. Amadon, his assistant. It covered a period of between 6 and 7 months and eight men were engaged on it during that time (testimony, Feb. 6, 1936).

Their study as respects shipbuilding showed:

Cost of minimum facilities.....	\$17, 604, 860
Cost of new machinery necessary.....	6, 000, 000
Total.....	23, 604, 860

These facilities would provide for construction in Government yards of a larger program even than now planned (1936). It allows for 4 major ships, 10 destroyers, and 3 submarines annually.

In view of the importance of this question and the careful study given to it by the branch of the Government most qualified in valuation work, the report is herewith incorporated in this report.

To: Special Committee Investigating the Munitions Industry, the
Honorable Gerald P. Nye, Chairman

Subject: Determination of costs of construction or purchase of sufficient Government ways to allow for a normal naval building and repair program

Herewith report prepared in accordance with arrangements whereby the Interstate Commerce Commission was to assign certain of its engineers to assist the Munitions Investigating Committee by making an appraisal of the probable cost to the Government of acquiring, through purchase or construction, sufficient shipbuilding facilities to carry on the construction of all combatant ships in a normal peacetime program.

In preparing this estimate the type and total number of each kind of ship adopted as typifying normal peace time requirements is of the utmost importance because the total of the estimate bears a direct relation to the program adopted. The building program under which the Government has been operating since 1933 does not offer a guide due to the fact that the types and number of ships authorized during this period have been dictated by treaty restrictions.

After considerable conference and study, the following annual program was adopted as a basis for an estimate, cognizant of the fact that some of the types of ships are not permissible today under the treaty governing the present building program:

ADOPTED ANNUAL BUILDING PROGRAM

- Keels for four major ships.
- Keels for ten destroyers.
- Keels for three submarines.

A program for the next two years conforming to treaty limitations would consist of twelve destroyers and six submarines each year.

Inquiry at the Navy Department disclosed the fact that the Government navy yards have a total of sixteen shipbuilding ways designed to accommodate the following types of ships:

	<i>Ways</i>
Major ships.....	7
Destroyers.....	6
Submarines.....	3
Total.....	16

There is a small distinction between a destroyer way and submarine way.

Tabulations in this report show ships under construction in Government navy yards far in excess of sixteen. This is accomplished by (1) building two or more small ships on a large way; (2) using dry docks as building ways.

Dry docks are built primarily for accommodating ships undergoing repairs and have not been considered shipbuilding facilities in this report. The absence of naval ships from the Atlantic coast has made the dry docks on the east coast available for new construction, but since repair facilities as well as new construction facilities must be provided, dry docks have been reserved for repairs and reconditioning.

The use of a large way for one or more small ships is obviously the proper procedure when only small ships are being built, but a large shipbuilding way suitable for a cruiser or battleship has excess facilities over the requirements of destroyer construction and the way is not used economically unless all facilities are employed.

All of the 16 ways in Government navy yards are not in condition at the present time to take a ship, but 16 has been adopted as the normal quota of Government shipbuilding ways and estimates have been built around this figure, and provision has been made in these estimates to recondition those out of repair.

Having established the number of ships to be laid down each year and the number of ways available on which to build the ships, the investigation resolved itself into an estimate of what part of the shipbuilding program the existing ways could handle and the probable cost of acquiring additional ways, if necessary.

The following tabulation shows available ways in Government navy yards, by types of ships accommodated and the number of ships adopted as a normal annual program:

	Ways in U. S. navy yards	Number of ships to be laid down annually
Major ships.....	7	4
Destroyers.....	6	10
Submarines.....	3	8

From this tabulation it is apparent that the program adopted exceeds the available ways in Government navy yards, and this deficiency is much more pronounced when adjustments are made, due to the fact that a major ship will be on the ways about two years, a destroyer one year, and a submarine one and one-half years.

With a program calling for four major ships a year, two years on the way and seven ways available, one additional major way is necessary.

In the case of ships of the destroyer class, ten laid down each year, one year on the ways, six ways available, four additional destroyer ways, or two additional double destroyer ways, are necessary.

Three submarines are to be built each year and with one and one-half year on the way, three ways available, two additional submarine ways are necessary.

Summing up the above requirements, the following are necessary:

One additional major ship way.

Four additional destroyer ship ways.

Two additional submarine ways.

Conferences with the Navy Department gave assurance that the present navy yard area can accommodate whatever additional building ways are necessary and, also, can provide space for increased shop facilities which may be necessary due to increasing the work load in the various yards. In order that the situation might be more clearly visualized, an inspection of the following navy yards was made during the month of September 1935:

Portsmouth Navy Yard.

Boston Navy Yard.

New York Navy Yard.

Philadelphia Navy Yard.

Norfolk Navy Yard.

The navy yards at Charleston, Puget Sound, and Mare Island were not visited.

All industrial facilities in each of the navy yards were visited. The purpose of the inspection was explained to the navy yard officials and they were requested to express an opinion as to the sufficiency of their present facilities and the probable necessary additional facilities in case new ways were placed in their yard. This inspection substantiated the assurances given by the Navy Department that the required expansion could be absorbed in active Government navy yards and that it would be unnecessary to look to private yards for additional ways.

Conditions existing in the various yards were closely observed in an endeavor to differentiate between additional facilities required due to obsolescence of existing plant and those due solely to proposed added work load to a yard on account of additional shipbuilding ways. An attempt has been made to limit the estimate to facilities due to more ships, but in many instances the dividing line is not sharply defined. Throughout the estimate there are cases where recommendations for additions have been included which are somewhat more embracing than the proposed increased work load to a yard would warrant, but there is no economy in operating a plant which is handicapped by insufficient facilities and in cases where an increase in the production of a whole yard would result from additional facilities somewhat greater than those made necessary by added work load, the entire additional facilities have been recommended.

Bearing in mind that the construction of the ships in the adopted normal program might involve the expenditure of one hundred and fifty million to two hundred million dollars annually, any savings in construction through the use of improved machinery and plant will be

a substantial amount. Specifications are becoming more exact, tolerance limits are being reduced, and in many instances an amount equaling the cost of a new shop or machine with its increased capacity could be saved in the construction of the ships in one year's program.

Another factor which has brought pressure to bear on the adequacy of navy yard facilities is the increase in the use of welding in ship construction in place of riveting, and estimates have been made for this change in operation in fitting out the yards for increased loads. One very apparent effect of the use of welding in place of riveting is evident in the large size units of a ship assembled prior to incorporating in the ship on the ways. The fabrication of these large sections is now carried on at various points throughout the yards, the only apparent requisite as to location of this fabrication being adequate service outlets for electricity and air, substantial foundations, and crane facilities to transfer the complete section within the reach of cranes serving the shipbuilding ways.

Sufficient space has been found in Government navy yards in which to locate shipbuilding facilities far in excess of the one additional major shipway, four destroyer ways, and two submarine ways, which are estimated necessary in conformity with the program. All existing navy yards, except New York, are capable of taking additional ways. This statement is based on personal observation of the navy yards at Portsmouth, Boston, New York, Philadelphia, and Norfolk, a study of the plan layouts of the navy yards at Charleston, Puget Sound, and Mare Island, and conference with the Navy Department.

At the present time considerable shipbuilding is in progress in the navy yards, especially on the east coast. The shipbuilding ways are full in all cases, except one, and ships are also under construction in dry docks at Boston, New York, Philadelphia, and Norfolk. The types of ships in these dry docks are destroyers, gunboats, and cruising cutters.

Some yards are considered principally construction yards, while others are classified as repair yards. Portsmouth Navy Yard represents a construction yard and Norfolk Navy Yard is an example of a large repair yard. At present the approximate disposition of the Norfolk Navy Yard work load is 65 percent destroyer construction (total of five), 15 percent ship repair, and 20 percent manufacturing of arresting gears, bombs, Diesel engines, paint, metal furniture, castings, et cetera.

The Boston Navy Yard is equipped with one destroyer way and one marine railway. Four destroyers are under construction here at the present time. The function of this yard is repair work, new construction, and conversion of commercial vessels in time of war.

The navy yards at New York and Philadelphia do repair work and new construction; also, various articles are manufactured at Philadelphia. These two yards are equipped to undertake battleship construction and are the only Government yards constructing cruisers at the present time.

The navy yard at Charleston has two destroyer ways and has not been heavily loaded in the past. Its present allotment is one gunboat, one cruiser cutter, and one destroyer. This yard is used for the construction of lighter ships of the auxiliary type.

All construction of ships at the Puget Sound Navy Yard is done in a building dock constructed for the purpose. This dock is listed as a

major ship way, although only ships of the destroyer class are allotted here. In addition to this building way, there are two dry docks in this yard.

At the Mare Island Navy Yard there is a cruiser way and destroyer or submarine way. No cruisers are allotted here, but two submarines are assigned, this being the only Government navy yard, except Portsmouth, engaged in submarine construction. There are two dry docks at Mare Island.

No attempt has been made to allocate the necessary additional ways to the various navy yards, but the types of ships built in the yards in the past indicate clearly in which direction expansion would go.

This study makes no provision for the construction of noncombatant auxiliary boats in Government navy yards.

The fullest cooperation has been offered by the Navy Department in the preparation of this report.

Summary of estimated cost to equip the Government navy yards to an annual capacity of 4 major ships, 10 destroyers, 3 submarines

Additional shipbuilding ways-----		\$2, 365, 000
Repairs to existing ways:		
Portsmouth-----	\$53, 000	
Philadelphia-----	445, 000	
Norfolk-----	350, 000	
New York-----	147, 860	
		995, 860
Additional facilities, exclusive of ways:		
Norfolk-----	490, 000	
Philadelphia-----	2, 787, 000	
New York-----	1, 200, 000	
Boston-----	1, 112, 000	
Portsmouth-----	220, 000	
Charleston-----	170, 000	
Puget Sound-----	2, 090, 000	
Mare Island-----	675, 000	
		8, 744, 000
Modernization of machine tools-----		5, 000, 000
Increased drafting room facilities-----		500, 000
		17, 604, 860

Estimated cost to provide sufficient shipbuilding ways in Government navy yards to annually lay down keels for 1 capital ship, 4 destroyers, 2 submarines

Estimated cost of a capital shipbuilding way, including pile foundations, excavation and dredging, concrete superstructure, crane runways, two 40-ton and four 10-ton bridge cranes, and service wiring and piping (average location): 1 at \$1,340,000-----	\$1, 340, 000
Estimated cost of double destroyer building ways, including pile foundations, excavation and dredging, concrete superstructure, 5 hammer-head cranes, and service lines (average location): 2 at \$325,000 each-----	650, 000
Estimated cost of a double submarine building way, including pile and concrete foundations, superstructure, crane runways, and cranes: 1 at \$375,000-----	375, 000
	2, 365, 000

TOTAL ESTIMATED COST TO PUT FIVE GOVERNMENT SHIPBUILDING WAYS IN CONDITION TO TAKE A BATTLESHIP

During October 1935 the navy yards at Norfolk, Philadelphia, and New York were requested to estimate the cost to revamp their large building ways to fit them for battleship construction. These three

yards are the only Government yards on the east coast with ways approaching battleship dimensions.

Norfolk Navy Yard.—At Norfolk there is a crane runway about 725 feet long, with the full quota of bridge cranes, suitable for a 600–700 ship, but at present the way is destroyer length only and has two destroyers laid down on it.

Philadelphia Navy Yard.—At Philadelphia there are two large ways with crane runway about 1,000 feet long and the necessary bridge cranes.

At the present time one of these ways has the light cruiser *Philadelphia* with hull about 33 percent complete, and the other way has two destroyers, *Cassin* and *Shaw*, which are to be launched Monday, October 28, 1935. The heavy cruiser *Wichita* will follow these two destroyers on the way.

New York Navy Yard.—At New York there are two large ways with crane runways about 725 feet long and the necessary bridge cranes.

On one of these ways is the light cruiser *Brooklyn*, with hull about 37 percent complete as of October 1, 1935, and on the other way is the light cruiser *Honolulu*, about 20 percent complete.

Estimated cost to put 1 large way at Norfolk Navy Yard in condition to take a battleship.....	\$350, 000
Estimated cost to put 2 large building ways at Philadelphia Navy Yard in condition to take battleships:	
Electric service.....	\$30, 000
Turret slab tracks.....	15, 000
2 additional fitting-out cranes.....	150, 000
	<hr/>
	195, 000
Estimated cost to put 2 large building ways at New York Navy Yard in condition to take battleships:	
Extend platforms, 2 at \$21,500.....	43, 000
Additional cost to widen way no. 1.....	38, 000
Crane repairs, elevators, walkways, floodlights, etc.:	
Way no. 1.....	34, 170
Way no. 2.....	32, 690
	<hr/>
	147, 860
Total estimated cost to put 5 ways in condition to take a battleship.....	692, 860

Comparative costs of preparing the ways in various navy yards in case only 1 or more battleships are laid down

Estimated cost to put 1 way in condition at Norfolk Navy Yard.....	\$350, 000
Estimated cost to put 2 ways in condition at Philadelphia Navy Yard.....	195, 000
Estimated cost to put 1 way in condition at New York Navy Yard.....	54, 190
Estimated cost to put second way in condition at New York Navy Yard.....	1 93, 670
	<hr/>
Total for 5 ways.....	692, 860

¹ 1 way at New York Navy Yard is slightly smaller than the other.

All of the above ways are in condition to take a cruiser, except the one at Norfolk where \$350,000 will have to be expended to fit this way for either a cruiser or a battleship.

In case the battleships exceed 725 feet in length, an additional estimated cost of \$200,000 may be necessary to extend platforms, crane runways, et cetera in some of the navy yards.

Estimated cost to repair the ways in Government navy yards which have not been maintained in working condition in recent years

Portsmouth Navy Yard: Repairs to Franklin ship house and submarine way.....	\$53, 000
Philadelphia Navy Yard: Construction of the superstructure of a double destroyer way, exclusive of hammer head cranes which are in place.....	250, 000
Norfolk Navy Yard: Extend the cruiser way to full cruiser or battleship way. This way at present is suitable for two destroyers only.....	1350, 000
Total.....	303, 000

¹ Included under cost to provide battleship ways.

Estimated cost of increased facilities, exclusive of building ways, considered necessary if all warships are constructed in Government navy yards

[Annual building program: 1 battleship, 1 aircraft carrier, 1 heavy cruiser, 1 light cruiser, 10 destroyers, 3 submarines]

Navy yard	Estimated cost	
	Plant	Tools
Portsmouth.....	\$220, 000	\$150, 000
Boston.....	1, 112, 000	560, 000
New York.....	1, 200, 000	950, 000
Philadelphia.....	2, 787, 000	1, 225, 000
Norfolk.....	490, 000	685, 000
Charleston.....	170, 000	350, 000
Mare Island.....	675, 000	430, 000
Puget Sound.....	2, 090, 000	650, 000
Total.....	8, 744, 000	5, 000, 000

CONSTRUCTION OF NEW WAYS FOR BATTLESHIPS, CRUISERS, DESTROYERS, AND SUBMARINES

The construction features of ways for battleships, destroyers, and submarines are quite different. The battleship and cruiser ways are very substantial structures and are served by bridge type cranes spanning the way, operating on structural steel runways, while the ways for destroyers and submarines, which are practically identical, are of lighter construction and are served by five or more revolving cranes of a fixed type, or two or more traveling cranes. The twin or double destroyer way shows an economy in crane requirements over the single destroyer way.

Standard designs for building ways have been developed by the Navy Department, utilizing wood or concrete construction, the first cost dictating which type shall be used. The concrete type should be built on account of its permanency and low maintenance costs.

The type and design of the overhead crane runways at Norfolk, Philadelphia, and New York vary only in length, thereby establishing what might be termed a "standard design", and it is estimated that this same design would be followed in case of additional major ship-building ways' being added.

With accepted designing for building ways, crane structures, and cranes, actual construction would follow closely the letting of contracts for extensions to existing ways and additional ways.

Estimated time to construct a major ship way to a state of completion sufficient to lay a keel is twelve months, while the time for a double destroyer or submarine way is eight months.

ESTIMATED TIME REQUIRED TO REPAIR EXISTING WAYS TO BRING THE QUOTA TO SIXTEEN

Norfolk Navy Yard.—The cruiser way in this yard was repaired during 1934, at a cost of about \$50,000, to take two destroyers. To make this way capable of taking a cruiser or battleship, it is estimated that it will cost an additional \$350,000. This involves lengthening, widening, and strengthening the entire way.

The rebuilding of the way beyond the section occupied by destroyers could proceed with destroyers on the way, but the way would be out of use during the time work was in progress on the section now occupied by two destroyers, a length of about 325 feet. It is estimated that the necessary repairs on this way to bring it to major ship capacity would render it unproductive from 4 to 6 months.

If it became necessary to lengthen the existing crane runway beyond the present 700 feet, this could be done at any time and would not interfere with the use of the building way.

Philadelphia Navy Yard.—The two cruiser ways with their service lines have been thoroughly reconditioned since 1929 at a cost of about \$575,000 and are in condition to take battleships, with the exception of a few minor repairs.

The destroyer way is out of repair and not in use. There are five 5- and 10-ton hammerhead cranes on the site of the way, which are serviceable, and it is estimated to cost \$250,000 to put this way in shape to take two destroyers. The way should be in condition to take a keel six months after letting contract for the repair work.

Portsmouth Navy Yard.—The submarine way in the Franklin ship house is out of repair and is not in use. It has not been used for ship construction during the past ten years. The Navy Department has taken no action on plans to recondition this structure, possibly because of the fact that additional ways have not been required under the present program of the Navy.

This location offers an additional way at a minimum cost. It is estimated that it will cost \$53,000 to make this way and crane structure serviceable. This work should be completed four months after letting the contract.

Ships being built at various Government navy yards exclusive of those whose keels have not been laid

Navy yard	September 1935	
	In dry docks	On ways
Norfolk.....	2 destroyers.....	3 destroyers.
Philadelphia.....	4 Coast Guard cutters.....	1 cruiser, 2 destroyers
New York.....	{ 1 gunboat.....	} 2 cruisers.
Boston.....	2 Coast Guard cutters.....	
Portsmouth ¹	2 destroyers (recently launched).....	Not used.
Charleston.....	None.....	2 submarines.
Puget Sound.....	None.....	1 gunboat, 1 cruiser cutter.
Mare Island.....	None.....	No ways here, 4 d. stroyers in building dock.
		2 destroyers.

¹ Also two submarines at fitting our piers, 78% and 91% complete.

Program 1935-36, allotment of ships

Type or class	Government yards	Private yards	Total
Aircraft carrier.....		Bethlehem Steel Co.....	1
Cruisers.....	New York.....	N. N. S. B. & D. D. Co.....	1
Destroyer leaders.....		Bath Iron Works.....	8
	(Boston.....		
	Philadelphia.....		
Destroyers.....	Norfolk.....	Bethlehem Steel Co. ¹	2
	Charleston.....	Federal Shipbuilding.....	8
	Puget Sound.....		
Submarines.....	Portsmouth.....	Electric Boat.....	8
	Mare Island.....		
Total.....	11	18	24

¹ Union plant, San Francisco.

	Total
Combatant ships contracted for in 1933, 1934, and 1935 program.....	86
Government navy yards.....	40
Private yards.....	46
Number of keels laid since 1933.....	57
Government navy yards.....	24
Private yards.....	33

Ships of the 1933, 1934, and 1935 program completed since 1933: None as of October 1935

Status of combatant ships in Government navy yards, including ships with keels laid and new ships assigned

Navy yard	Type of boat	Name	Number	Ship laid down	Date keel laid	Date launched	Percent of hull completed 10-1-35	Expected date of completion of ship
Norfolk.....	Destroyer.....	Tucker ¹	374	C. A. way.....	8-15-34		62.7	7-1-36
	do.....	Downs ¹	375	do.....	8-15-34		62.7	8-1-35
	do.....	Bagley.....	386	D. D. way.....	7-31-35		13.1	11-1-36
	do.....	Blue.....	387	Dry dock.....	9-25-35		11.8	2-1-37
	do.....	Helm.....	388	do.....	9-25-35		11.4	5-1-37
	do.....	do.....	405				0	
Philadelphia..	Cruiser.....	Philadelphia ¹	41	C. A. way.....	5-28-35		32.7	1-1-37
	Destroyer.....	Cassin ¹	372	do.....	10-1-34		51.9	5-1-36
	do.....	Shaw ¹	373	do.....	10-1-34		49.7	8-1-36
	Cruiser.....	Wichita.....	46				8.9	1-1-35
New York.....	Destroyer.....	do.....	404				0	
	Cruiser.....	Honolulu.....	48	C. A. way.....	9-10-35		19.5	10-1-37
	do.....	Brooklyn ¹	40	do.....	3-12-35		36.8	4-1-37
	Gunboat.....	Erie ¹	50	Dry dock.....	1-17-34		64.9	5-1-36
Boston.....	Cruiser.....	do.....	50				0	
	Destroyer.....	Conyngham ¹	371	Pier.....	9-19-34	9-14-35	54.5	10-1-35
	do.....	Case ¹	370	do.....	9-19-34	9-14-35	57.0	7-1-36
	do.....	Mugford.....	389				12.0	11-1-35
	do.....	Ralph Talbot ¹	390				12.0	2-1-37
	do.....	do.....	402				0	
Portsmouth..	do.....	403					0	
	Submarine.....	Porpoise ¹	172	Pier.....	10-27-33	6-20-35	61.3	2-1-35
	do.....	Pike ¹	173	do.....	12-20-33	9-12-35	78.4	5-1-36
	do.....	Plunger.....	179	Submarine way.....	7-17-35		15.3	2-1-37
	do.....	Pollack.....	180	do.....	10-1-35		14.2	5-1-37
	do.....	Snapper.....	185				0	
Puget Sound..	do.....	Stingray.....	186				0	
	Destroyer.....	Cushing ¹	376	Building dock.....	8-15-34		66.7	5-1-36
	do.....	Perkins ¹	377	do.....	11-15-34		60.8	8-1-36
	do.....	Patterson.....	392	do.....	7-23-35		8.5	11-1-36
	do.....	Jarvis.....	393	do.....	8-21-35		8.5	2-1-37
	do.....	do.....	408				0	
Mare Island..	do.....	Smith ¹	378	C. A. Way.....	10-27-34		48.0	7-1-36
	do.....	Preston ¹	379	do.....	10-27-34		44.9	10-1-36
	do.....	Henley.....	391				10.5	11-1-36
	Submarine.....	Pompano.....	181				5.8	5-1-37
Charleston....	do.....	Sturgeon.....	187				0	
	Destroyer.....	do.....	407				0	
	Gunboat.....	Charleston.....	51	Way.....	10-27-34		65.0	4-1-36

¹ 1933 contract; others since 1933.

In addition to the above ships, the following seven cruising cutters are under construction in navy yards, as follows:

Navy yard	Cruising cutters	Average per cent complete Oct. 1, 1935	Estimated average date of completion
Philadelphia.....	4	35.3	10- 1-36
New York.....	2	21.7	1- 1-37
Charleston.....	1	17.9	1-15-37

The expected dates of completion of ships are estimates made by the building yard.

Delays beyond dates shown probable on:

- Cruiser #41 (*Philadelphia*) at Philadelphia.
- Cruiser #48 (*Honolulu*) at New York.
- Submarine #172 (*Porpoise*) at Portsmouth.
- Submarine #181 (*Pompano*) at Mare Island.

Delays are also expected on the cutters at Philadelphia and New York.

APPROXIMATE DATES WHEN SHIPS ASSIGNED TO THE VARIOUS NAVY YARDS UNDER THE 1933, 1934, AND 1935 PROGRAM MAY BE LAUNCHED FROM THE BUILDING WAYS NOW IN REPAIR IN THESE YARDS

Norfolk Navy Yard:

- One double destroyer (cruiser) way.
- One destroyer way.
- Capacity, three destroyers.
- Keels not laid, two destroyers (#405 and #406).

The two destroyers on the cruiser way should be launched by December 1, 1935, having been laid down August 15, 1934, and reported 52.7 percent complete October 1, 1935. The two new destroyers, (#405 and #406), recently assigned to this yard, should be laid down on this way April 1936.

Inasmuch as no cruisers have been assigned to this yard, the fact that the cruiser way is not in a position to take a cruiser does not handicap this yard under the 1933-1935 program.

The destroyer (#386) on the destroyer way should be launched by August 1, 1936, and the two destroyers (#405 and #406) on the cruiser way, should be launched by April 1, 1937.

The Norfolk Navy Yard should be able to clear the ways of present assignments by April 1937, with ways available as follows:

- Destroyer way, single, August 1, 1936.
- Cruiser way, double destroyer, April 1937.

Philadelphia Navy Yard:

- Two cruiser ways; destroyer way out of repair.
- Capacity: Four destroyers or two cruisers.
- Keels not laid: One cruiser (#45) and one destroyer (#404).

Cruiser *Wichita* (#45) can follow the two destroyers (*Cassin* and *Shaw*) on the cruiser way about November 1, 1935, with the launching date about August 1, 1937.

Destroyer #404 can follow cruiser *Philadelphia* (#41) about August 1, 1936, and be launched about August 1, 1937.

The Philadelphia Navy Yard may have a way available for a cruiser about August 1, 1937, and may have a way available for a destroyer, not now assigned, alongside destroyer #404 about August 1, 1936.

If destroyer way is repaired, lay keel of destroyer #404 on this way, thereby making the way now occupied by cruiser *Philadelphia* available about August 1, 1936.

New York Navy Yard:

Two cruiser ways.

Capacity, two cruisers or four destroyers.

Keels now laid, two cruisers.

Keels not laid, one cruiser (#50).

The cruiser *Brooklyn*, now on one way, should be launched by January 1, 1937, at which time the new cruiser (#50) could be laid down, with a probable launching about December 1, 1938.

The cruiser *Honolulu* (#48) now on the ways, should be launched by June 1, 1937.

One way available June 1, 1937 for one cruiser or two destroyers.

One way available December 1, 1938, for one cruiser or two destroyers.

Boston Navy Yard:

One destroyer way, not now in use.

Capacity, one destroyer.

Keels not laid, two destroyers.

The destroyer way is not used for laying down ships under the present program.

The two destroyers (#370 and #371) launched September 14, 1935, were built in dry dock no. 2, and keels for two new destroyers (#389 and #390) were laid in dry dock no. 2 in October.

The two destroyers (#370 and #371) launched September 14, 1935, were in dry dock one year.

It would take the one destroyer way four years at least to accommodate the four destroyers assigned here.

One building way is available here now but the yard prefers to build in dry dock. The four destroyers assigned can be launched from the dry dock two years from now, or November 1, 1937.

Two destroyers placed in dry dock and one on way, releasing dry dock one year from now, or November 1, 1936, completing the fourth destroyer on building way two years hence, or November 1, 1937.

One way available for destroyer on November 1, 1937, based on building two of the present assigned destroyers in dry dock and two on the single way.

Portsmouth Navy Yard:

Two submarine ways.

Capacity, two submarines.

Keels not laid, two submarines.

Keels for two submarines have been laid recently, one on July 17, 1935, and one on October 1, 1935.

Based on the construction time of the *Porpoise* in this yard with fifteen months on the way, the two submarines on ways at present should be launched by March 1, 1937, and the two new submarines (#185 and #186) should be launched by August 1, 1938.

Two submarine ways available about August 1, 1938.

Puget Sound Navy Yard:

One building dock.

Capacity, one cruiser or four destroyers.

Keel not laid, one destroyer.

There are four destroyers in the building dock, two averaging 53 percent complete and two averaging 8.5 percent complete. The two averaging 53 percent complete (#376 and #377) are expected to be finished in May and August 1936, and should be in condition to launch about January 1, 1936.

The other two destroyers in the building dock (#392 and #393) may be launched about October 1, 1936.

This will make space available for two destroyers about January 1, 1936, but only one additional destroyer is assigned here. If this destroyer is laid in the building dock January 1, 1936, no ship larger than a destroyer may be laid down in this dock prior to February 1, 1937, and another destroyer cannot be laid until October 1, 1936, when destroyers #392 and #393 should be launched.

One destroyer way available January 1, 1936.

Three destroyer ways available October 1, 1936.

Mare Island Navy Yard:

One cruiser way.

One destroyer way (reconstructed into double way).

Capacity, one cruiser and two destroyers, or four destroyers.

Two destroyers on cruiser way.

One destroyer on destroyer way.

Keels not laid, two submarines.

The two destroyers (#378 and #379) should be launched by January 1, 1936, from cruiser way.

The keel for destroyer *Henley* (#391) was laid on reconstructed destroyer way October 10, 1935, and should be launched about January 1, 1937.

The submarine *Pompano* (#181) was reported 5.8 percent complete in September and 7.1 percent in October, but the keel had not been laid November 30, 1935. Lay keel for this submarine on cruiser way about January 1936, and launching about October 1937.

Lay keel for submarine *Sturgeon* (#187) alongside destroyer *Henley* about July 1936, launching about January 1938.

Charleston Navy Yard:

Two destroyer ways.

Capacity, two destroyers.

Gunboat #51 on one way.

Cruising cutter #71 on one way.

Keel not laid, destroyer #407.

The gunboat (#51) should be launched about November 15, 1935, and this will permit the keel of new destroyer (#407) being laid as soon as plans and material are ready about July 1936, and launching about July 1, 1937.

The keel for the cruising cutter (#71) laid August 15, 1935, should be off the way by August 15, 1936.

One way available August 15, 1936.

One way available July 1, 1937.

Approximate dates when ships assigned to the various navy yards under the 1933, 1934, and 1935 program may be launched from the building ways now in repair in these yards

SUMMARY

	Available	
Norfolk:		
Single destroyer way.....	Aug.	1, 1936
Cruiser (double destroyer) way.....	Apr.	1, 1937
Philadelphia:		
1 cruiser way.....	Aug.	1, 1937
1 cruiser way:		
1 destroyer.....	Aug.	1, 1936
1 destroyer.....	Aug.	1, 1937
If destroyer way is repaired, cruiser way will be available		
Aug. 1, 1936, for cruiser.		
New York:		
1 cruiser way.....	June	1, 1937
1 cruiser way.....	Dec.	1, 1938
Boston: 1 destroyer way.....	Nov.	1, 1937
Portsmouth: 2 submarine ways.....	Aug.	1, 1938
Puget Sound: ²		
1 destroyer way.....	Jan.	1, 1936
3 destroyer ways.....	Oct.	1, 1936
Mare Island:		
1 cruiser way.....	Oct.	1, 1937
1 destroyer way.....	Jan.	1, 1937
1 destroyer way.....	Jan.	1, 1938
Charleston:		
1 destroyer way.....	Aug.	15, 1936
1 destroyer way.....	July	1, 1937

¹ On basis of 2 destroyers in dry dock, 2 destroyers on way.

² Puget Sound has building dock accommodating 1 major ship or four destroyers.

Expected dates of completion of ships in 1933 and 1934 program now on ways in Government navy yards

	Destroy- ers	Subma- rines	Cruisers	Gunboats
Jan. 1936.....				
Feb. 1936.....		1 1		
March 1936.....				
April 1936.....				
May 1936.....	2	1		1
June 1936.....				
July 1936.....	3			
Aug. 1936.....	3			
Sept. 1936.....				
Oct. 1936.....	2			
Nov. 1936.....	4			
Dec. 1936.....				
Jan. 1937.....			1 1	
Feb. 1937.....	3	1		
March 1937.....				
April 1937.....			1	
May 1937.....	1	1 2		
June 1937.....				
July 1937.....				
Aug. 1937.....				
Sept. 1937.....				
Oct. 1937.....			1 1	
Nov. 1937.....				
Dec. 1937.....				
Jan. 1938.....			1	
Feb. 1938.....				
March 1938.....				
Total.....	18	5	4	2

¹ Reports indicate probable delays, extent indeterminate.

² (One.)

The Government building yards receiving the eleven awards for war ships under the 1935 program have not reported expected dates of completion.

Tabulation of the ship building ways in U. S. Government navy yards and possible expansion

U. S. Government shipyard	Class and symbol of naval vessel										Drydocks					
	Present existing ways					Expansion possible in existing yards without acquiring additional land					Graving		Building			
	Battle-ship (BB)	Aircraft-carrier (CV)	Cruiser (CL)	Destroyer (DL)	Submarine (SS)	Battle-ship (BB)	Aircraft-carrier (CV)	Cruiser (CL)	Destroyer (DL)	Submarine (SS)	Length	Width	Feet	Length	Width	Feet
1. Portsmouth.....					3								740	130	86	
2. Boston.....				1			1						373	86	114	
3. New York.....	2												738	114	98	
4. Philadelphia.....	2			1			1		18				417	113	656	
5. Norfolk.....	1			1			1						694	150	139	
6. Charleston.....				2									491	131	140	
7. Puget Sound.....	1			1				5					744	140	142	
8. Mare Island.....													344	86	86	
9. South Boston.....													490	130	136	
10. Squantum.....													722	136	144	
11. Pearl Harbor.....													1,011	144	76	
Total.....	7			6	3	1	2	3	36	26			665	76	622	134
													630	130	927	130
													809	145	(1)	(1)
													507	122		
													710	120		
													1,175	149		
													1,001	138		

¹ Building dock.

² Included as battleship way.

STATISTICAL DATA IN CONNECTION WITH U. S. NAVY YARDS IN WHICH SHIPS ARE BUILT; CORRECTED TO 1927

The data shown below is somewhat out of date in certain features such as square-foot and cubic-foot capacities of shop buildings but there has been only slight changes in other items since 1927. This tabulation presents a picture of the relative size of the industrial part of navy yards engaged in repair and new construction of ships.

The absence of pier area at Mare Island is due to the fact the body of water on which the navy yard is located—Mare Island Strait—is so narrow piers cannot extend beyond the wharf or bulkhead line.

Statistical data in connection with U. S. navy yards in which ships are built, corrected to 1927

Navy yard	Shop buildings		Standard gage rail-road tracks (miles)	Pier area (square feet)	Number Dry Docks	Berthing space (linear feet)	Condition of shipbuilding ways, as of September 1935, as regards rated capacity		Marine railway
	Square feet	Cubic feet					Serviceable	Not serviceable	
Portsmouth.....	798, 660	20, 209, 790	7. 6	216, 099	1	6, 770	2	1	0
Boston.....	704, 770	17, 256, 770	7. 3	344, 986	2	7, 370	1	-----	1
New York.....	1, 049, 830	33, 362, 203	12. 4	226, 489	4	14, 380	2	-----	0
Philadelphia.....	1, 563, 000	59, 626, 000	25. 4	557, 000	8	15, 440	2	1	0
Norfolk.....	1, 647, 115	60, 504, 898	16. 1	226, 025	6	7, 600	1	1	0
Charleston.....	315, 728	10, 149, 670	8. 6	141, 100	1	2, 285	2	-----	1
Puget Sound.....	608, 925	12, 100, 065	13. 5	306, 400	1 ³	33, 500	1	-----	1
Mare Island.....	1, 141, 098	38, 218, 755	17. 7	-----	2	11, 900	2	-----	0

¹ One is a building dock used for ship construction.

² Small boats only.

Comparison of the number of months allowed in contracts to build the various types of ships in Government and private shipbuilding yards

[Average time elapsing between date of contract and contract date of completion of 55 of the 86 ships in the 1933 and 1934 programs]

Type of ship	Unit: Months	
	Government navy yard	Private shipbuilding company
Cruiser:		
Heavy.....	38. 0	38. 5
Light.....	36. 0	37. 0
Destroyer:		
Heavy.....	-----	30. 6
Light.....	27. 5	26. 7
Submarine.....	28. 8	28. 2

Construction periods of various types of combatant ships

Type	Symbol	Time on ways	Total building time
Battleship.....	BB	24 months.....	42 months.
Aircraft carrier.....	CV	24 months.....	42 months.
Heavy cruiser.....	CA	24 months.....	38 months.
Light cruiser.....	CL	24 months.....	38 months.
Destroyer.....	DD	12 months.....	30 months.
Submarine.....	SS	18 months.....	30 months.
Gunboat.....	PG	12 months.....	30 months.
Coast Guard cutters.....	-----	12 months.....	24 months.

At the time of launching, ships are 60-70 percent completed.

Shipbuilding program 1933, 1934, and 1935—Total number of each type of ship contracted

Type of ship	Symbol	1933-34	1934-35	1935-36	Total
Battleship.....	BB	0	0	0	0
Aircraft carrier.....	CV	2		1	3
Cruiser:					
Heavy.....	CA	2	1		3
Light.....	CL	4	3	2	9
Destroyer leader.....	DL	8	2	3	13
Destroyer.....	DD	16	12	12	40
Submarine.....	SS	4	6	6	16
Total.....		36	24	24	84

In addition to above ships, there are two gunboats contracted in 1933.

Combatant ships contracted for—1930 to date

Combatant ships under contract since 1933:

Keels laid or to be laid:

In Government navy yards..... 40

In private shipyards..... 46

Total..... 86

Number of ships with keel laid as of Oct. 1, 1935:

Government yards..... 24

Private shipyards..... 33

Total..... 57

Number of ships launched as of Oct. 1, 1935:

Government yards..... 4

Private shipyards..... 5

Total..... 9

Ships completed under contract since 1933:

Government yards..... 0

Private shipyards..... 0

Total..... 0

Average percent of hull completed at time of laying of keel as evidenced by reports of hull completion of ships prior to laying of keel..... 10

Delay beyond contract date in completion of ships in Government and private yards

[Number of months between contract date of completion and estimated date of completion reported by building yards for ships on ways in October 1935]

	Government yards		Private yards	
	Number reporting	Lag months	Number reporting	Lag months
Heavy cruisers.....	1	0	2	0
Light cruisers.....	3	2.67	1	0
Submarines.....	5	0	5	2.0
Destroyers.....	18	2.22	16	1.63
Gunboats.....	2	2.50	None	
Aircraft carriers.....	None		2	5.0

From October 1935, progress report of ships in Government and private yards. These figures will change as dates of completion approach.

Estimated cost of shipbuilding ways

CRUISER AND BATTLESHIP WAY

ONE SHIP, LENGTH ABOUT 700'

File foundation: Excavation, dredging-----	\$200, 000
Superstructure: Concrete, reinforced-----	250, 000
Crane runway: Structural steel-----	500, 000
Cranes: 2, 40-ton; 4, 10-ton, overhead bridge type-----	140, 000
Services: Air, electricity, water, etc-----	250, 000
	1, 340, 000

DESTROYER AND SUBMARINE WAY

TWO SHIPS, LENGTH ABOUT 375'

File foundation: Excavation, dredging-----	\$60, 000
Concrete superstructure-----	80, 000
5 H. H. cranes, at \$25,000 (5, 10-ton, fixed tower)-----	125, 000
Services: Air, electricity, water, etc-----	60, 000
	325, 000

REQUIREMENTS OF SITES FOR NAVY YARDS

1. Situation upon a good harbor of sufficient size, depth, and accessibility for vessels of the largest size and draft.
2. A favorable position with respect to the principal lines of defense.
3. A local security from water attack due to position and natural surroundings.
4. Ample water frontage of sufficient depth and permanence and with currents of moderate rapidity.
5. A favorable position with respect to the lines of interior communication (by rail or otherwise) with the principal sources of supply.
6. That the character of the ground shall be suitable for the construction of excavated docks and basins and for heavy structures.
7. Proximity to centers of labor and supplies of material.
8. Healthfulness of the climate and its suitability for outdoor labor.
9. The existence in the vicinity of an ample supply of potable water.

The area should be suitable for eventual development and have an area of not less than 300 acres for the navy yard proper (the manufacturing yard).

Waterfront should be a straight line with a length of approximately 5,000 feet.

Elevation of approximately 5 to 10 feet above mean high water at waterfront with a level or slightly increasing elevation from the water.

Foundation conditions.—The soil should be of a character suitable for the construction of dry docks and buildings and to furnish foundations for heavy machinery.

Depth of water.—Depth at yard: The depth at the yard, including the entrance to the dry docks, the berthing spaces, and anchorage, should have a minimum depth at extreme low water of not less than 35 feet. It is very desirable that the depth should be 40 feet.

Depth to sea: The controlling depth to the sea should be not less than 35 feet at mean low water and, if practicable, 40 feet. Where

there is little range of tide, 45 feet would be preferable. Liberal allowance should be made for the effect of heavy seas and the "squat" of a vessel under way, reducing usable depth of water.

Tides and currents.—At the yard itself a reasonable rise and fall of tide is not objectionable.

A swift current is very undesirable.

Berthing.—Waterfront should be such that a total of approximately 20,000 linear feet can eventually be provided, preferably by a number of parallel piers of a length of not less than 1,000 feet.

Width of slips between piers should be not less than 300 feet and the piers 100 feet wide.

Dredging.—The original dredging necessary to obtain the prescribed depth is a matter affecting the cost of constructing the original yard, while the amount of annual dredging to maintain this depth is an operating expense.

Services necessary to provide at building ways.—Fire protection, fresh water, sewerage, compressed air, fuel oil (possibly), electricity for lighting, rivet heating, power, and welding. Outlets should be located at working spaces and ways convenient for service to any part of a ship.

Working and storage space.—Ample space should be provided for receiving and working material and for assembling it into larger units before placing.

These spaces are located generally at the head of the slip and on the normal route of material from storage spaces or shops to the building ways.

The area around the building way should have good drainage and a good working surface of hard earth, cinders, macadam, or other pavement.

ADDITIONAL DRAFTING ROOM FACILITIES NEEDED IF ALL COMBAT SHIPS ARE DESIGNED AND BUILT IN GOVERNMENT NAVY YARDS

Drafting and designing forces are maintained at the various Government navy yards and private shipbuilding yards. Designs are worked out and plans prepared and revised in these offices for ships under construction in yards located throughout the country, the work in any drafting office not being restricted to ships assigned to the yard in which the office is located.

In addition to the drafting offices in the navy yards, there is a central drafting office located at New York, where plans are prepared for ships at various navy yards.

Also, plans for many ships are prepared in private shipbuilding yards, such as the New York Shipbuilding Company, Newport News Shipbuilding and Dry Dock Company, Electric Boat Company, and the Fore River plant of the Bethlehem Steel Company.

At the Norfolk Navy Yard the number of draftsmen at the present time totals 108, divided as follows:

Work on which engaged:	<i>Number of draftsmen</i>
Construction and repair.....	50
Mechanical.....	39
Ordnance.....	5
Public Works.....	14
Total.....	108

During the period 1917-1918 about 150 men were accommodated in the drafting quarters now in use at Norfolk and no increase in space is considered necessary in case of expansion in this yard.

At the Philadelphia Navy Yard, additional space amounting to approximately 50 per cent of the present space is requested.

At the New York Navy Yard, where about four hundred draftsmen and designers are employed, no additional space is requested.

At the Portsmouth Navy Yard about seventy-five draftsmen are employed, and some additional space is requested.

The New York Shipbuilding Company, with three light cruisers and four heavy destroyers on its ways at present, has about three hundred and fifty draftsmen and designers.

In the event that warship construction is confined to Government navy yards, additional facilities housing the draftsmen in private yards will have to be provided. It is not necessary that the drafting force be located at the yard where construction is going on, although a small force is necessary at all points of construction.

Provided that all the designing and drafting be done in Government navy yards or at least by the Government, it is estimated that an expenditure of \$500,000 would enlarge present drafting room facilities in the navy yards and provide additional working quarters for draftsmen now employed at private yards. The location of this outside drafting force is optional because practically all the plans have to be reviewed and approved at Washington.

MACHINE TOOLS

A survey made by the Navy Department develops that the average age of machine tools in Government navy yards is about 19 years.

The estimated replacement value, exclusive of installation, of the machine tools in the eight navy yards actively engaged in building ships is somewhat in excess of 36 million dollars.

The average sum of \$1,211,811 has been expended yearly since 1930 for machine tools for replacements and additions.

An inspection of the machine tools in the east coast yards revealed crowded conditions and antiquated machines. Additional machine shop buildings have been estimated to relieve certain navy yards of their crowded condition, and an additional estimated sum of \$5,000,000 has been included to cover the cost of modern up-to-date machines with which to build the latest type warships. These ships, with their welded construction and heavy alloy-steel armor, require machines of the greatest capacity and accuracy; and while this is all due to the latest improvements in design and is in no sense attributable to the assumption that the Government may take over all warship construction, nevertheless this estimate must provide facilities to carry out the assumed program, and for this reason a part at least of the normal replacement costs of machines, which should follow year after year under an ordinary program, have been included in this estimate as a part of the cost of the plant required, to start on the program at once.

The Navy Department recommendation for the annual replacement of machine tools for the next five years is \$2,500,000, and this figure does not take into consideration the increased Government building program laid down in this report.

Initial cost of machines in each navy yard and calculated replacement value

	Replacement value exclusive of installation cost, machine tools, class 6 (few classes 4 and 5)	First cost of machine tools, class 6: From Paymaster General's report, 1934
Portsmouth.....	\$2, 586, 391. 90	\$2, 046, 196. 13
Boston.....	4, 199, 976. 49	3, 322, 766. 27
New York.....	6, 892, 400. 48	5, 452, 848. 43
Philadelphia.....	5, 745, 493. 27	4, 545, 489. 14
Norfolk.....	6, 471, 285. 81	5, 119, 898. 45
Charleston.....	1, 478, 828. 21	1, 169, 959. 03
Mare Island.....	4, 636, 908. 16	3, 668, 440. 00
Puget Sound.....	4, 623, 132. 40	3, 657, 541. 46
Pearl Harbor.....	1, 956, 965. 27	1, 547, 448. 79
Cavite.....	1, 348, 737. 46	1, 067, 039. 13
Total.....	39, 940, 124. 42	31, 597, 414. 83

Portable, loose, and hand tools not included above, which, when replaced, are charged to plant overhead. Average age of machine tools in continental yards, 19 years. Appraised value today of machinery and machine tools in above navy yards, \$5,529,487.

Funds expended for machine tools during past six years:

1930.....	\$1, 500, 000
1931.....	1, 500, 000
1932.....	960, 000
1933.....	200, 000
1934.....	1, 451, 220
1935.....	1, 231, 475
1936.....	1, 700, 000

No surplus machine tools, purchased during war, left for distribution to the yards. The above data taken from a recent report by Lieut. Commander Walker.

Total forces employed in U. S. navy yards, September 1935 and September 1918

Navy yard	Sept. 1935	Sept. 1918	Navy yard	Sept. 1935	Sept. 1918
Portsmouth.....	2, 400	5, 449	Norfolk.....	4, 300	8, 880
Boston.....	1, 970	9, 376	Charleston.....	1, 350	3, 532
New York.....	5, 900	15, 025	Mare Island.....	4, 600	7, 559
Philadelphia.....	6, 100	9, 001	Puget Sound.....	4, 450	6, 120

Figures for 1935 are total civilians.

Figures for 1918 (approximately war peak) are exclusive of clerks.

NUMBER OF NEW SHIPBUILDING WAYS NECESSARY TO BUILD ALL WARSHIPS IN GOVERNMENT NAVY YARDS

In a communication to the Senate Munitions Investigation Committee, the Navy Department advised that eight additional ways would be necessary for destroyer construction and five additional ways for submarine construction in the event all warships are built in Government navy yards. This estimate varies from the one attached, which covers the cost of one major ship way, four destroyer ways, and two submarine ways. The reason for the difference in the two estimates is as follows:

The basis of the Navy Department estimate is the tentative building program for the next two years laid down in accordance with treaty limitations. Under the treaty, the United States may build twenty-four destroyers and twelve submarines, and this number of ships has been divided equally in drawing up programs for 1936 and 1937—twelve destroyers and six submarines each year.

The Navy Department deducts the five existing destroyer ways from the total number of destroyers to be built each year (twelve) leaving seven, and allowing a year plus a small fraction over for construction of a destroyer, eight additional ways are necessary.

In figuring the number of new ways for submarines, the number of submarines (six) to be laid down each year was converted into number of building ways by multiplying by one and one-half inasmuch as a submarine occupies a way for this length of time. This results in nine ways necessary, and with a total of four existing ways—nine minus four equals five.

It should be noted that the Navy Department has not figured on any new major ship construction during the next two years and has made no use of any of the seven major shipbuilding ways for the construction of the ships under the 1936 and 1937 programs.

The attached estimate is predicated on the annual construction of four major ships, ten destroyers, and three submarines. The period of construction for each type of ship is the same as the Navy Department uses and in both estimates the total number of ways in navy yards is set at sixteen, although some are out of repair.

STANDARD DISPLACEMENT

The standard displacement of a ship is the displacement of the ship complete, fully manned, engined, and equipped ready for sea, including all armament and ammunition, equipment, outfit, provisions, and fresh water for crew, miscellaneous stores and implements of every description that are intended to be carried in war, but without fuel or reserve feed water on board.

The word "ton", in the present treaty, except in the expression metric tons, shall be understood to mean the ton of 2,240 pounds.

The standard displacement of a submarine is the surface displacement of the vessel complete (exclusive of the water in non-water-tight structure), fully manned, engined, and equipped ready for sea, including all armament and ammunition, equipment, outfit, provisions for crew, miscellaneous stores, and implements of every description that are intended to be carried in war, but without fuel, lubricating oil, fresh water or ballast water of any kind on board.

Each naval combatant vessel shall be rated at its displacement tonnage when in the standard condition. The word "ton", except in the expression metric tons, shall be understood to be the ton of 2,240 pounds.

SUITABLE GOVERNMENT LAND AREAS ON THE EASTERN SEABOARD CAPABLE OF DEVELOPMENT INTO SHIPBUILDING YARDS

A description of the shipbuilding facilities of the Navy on the eastern seacoast would not be complete without mention at least, of two locations entirely void of shipbuilding at present but with possibilities for considerable development.

One of these locations is the old Squantum Destroyer Base just south of Boston and the other is the area adjoining the South Boston drydock in Boston Harbor, both locations being in the same naval district as Boston Navy Yard.

Squantum Destroyer Base.—At Squantum there are no available ways in shape to use, but there are ten building ways designed for submarine or destroyer construction which might be put in shape to take ships of this character. The ways are of wood trestle construction, heavily braced and planked on the inboard end and pier construction at ground level on the outboard end. These ways are covered by saw-toothed type roof, glazed, and sidewalls entirely glazed. Small capacity cranes of about three tons serve these ways. These cranes would not be fit to repair at the present time and heavier cranes would be required if these ways were reconditioned for destroyer construction.

Large shop buildings are here, but in an unkept condition, the steel work remaining unpainted for many years. The buildings are not beyond repair, but a considerable sum would be necessary to recondition them. All machinery has been taken from the buildings and during the time we were on the premises, the dismantling of plate and angle crane runways and Building No. 24 was in progress. An old warehouse was being torn down, the salvaged material being used in the construction of other buildings for the use of the airway facilities at this point. The heavy cranes from plate storage yards were being salvaged for use in Boston Navy Yard.

Insofar as room and building layout are concerned, this area is well adapted for ship construction of the destroyer class. Thirty-five or more destroyers were built here during the war and the period immediately following, by the Bethlehem Shipbuilding Corporation.

In addition to the ten building ways there are the remains of what were six wet slips. These wet slips are about 50 feet wide, in groups of two with working platforms between, the entire number of slips being covered by a steel frame, glazed sidewall and roof structure. In 1932 fire destroyed the roof and working platforms and twisted the steel-roof structures to such an extent it would require a considerable sum to put this part of the plant in a working condition.

South Boston drydock area.—There are no building ways or shops on this site but there is ample space here for construction of the largest type of shipbuilding ways and the necessary shop buildings and appurtenances.

NAVY YARD, PORTSMOUTH

		<i>Tools</i>
Addition to Elect. Mfg. Shop #79, about 60% increase-----	\$150, 000	
Machine tools for above-----		\$100, 000
Enlarge foundry, 50%-----	70, 000	
Foundry equipment-----		50, 000
	220, 000	150, 000
	150, 000	
Total necessary-----	370, 000	
Desirable:		
Extension to ship fitter shop-----	150, 000	
Locomotive crane for weldments-----	20, 000	
Desirable-----	170, 000	

NAVY YARD, BOSTON

		<i>Tools</i>
New structural shop.....	\$750, 000	
Machine tools for structural shop.....		\$300, 000
Re-modeling old structural shop for pipe shop.....	25, 000	
Machine tools, additional for pipe shop.....		60, 000
Plate yard.....	35, 000	
Removal of trestle at end of ways.....	2, 000	
Extend and repair piers 5 and 6.....	300, 000	
Tools for machine shop, welding, etc.....		200, 000
	<u>1, 112, 000</u>	<u>560, 000</u>
	560, 000	
Total necessary.....	<u>1, 672, 000</u>	
Desirable:		
Improve power plant.....	280, 000	
Paint and oil storage.....	70, 000	
Desirable.....	<u>350, 000</u>	

NAVY YARD, NEW YORK

Covered welding platforms.....	\$300, 000	
Machine tools for structural shop.....		250, 000
1 additional pier.....	325, 000	
Enlarge machine shop.....	275, 000	
Tools for machine shop.....		300, 000
Remodel boiler shop, etc.....	300, 000	
Tools for boiler shop.....		200, 000
Welding equipment.....		200, 000
	<u>1, 200, 000</u>	<u>950, 000</u>
	950, 000	
Total necessary.....	<u>2, 150, 000</u>	
Desirable:		
Improve power plant.....	200, 000	
Fitting out crane, 350-ton.....	900, 000	
Miscellaneous building improvements.....	200, 000	
Desirable.....	<u>1, 300, 000</u>	

NAVY YARD, PHILADELPHIA

Increase plate and angle storage.....	\$350, 000	
Reserved material storehouse and crane.....	360, 000	
Heavy metals storehouse and crane.....	500, 000	
Cranes for pier 4.....	60, 000	
New sheet metal shop.....	365, 000	
Tools for sheet metal shop.....		100, 000
Enlarge machine shop.....	432, 000	
Tools for machine shop.....		400, 000
Lengthen and improve pier 5.....	250, 000	
Extension to copper and pipe shop.....	60, 000	
Tools for copper and pipe shop.....		100, 000
Additional 5-15 ton crane, pier 8.....	60, 000	
Enlarge electric shop.....	200, 000	
Tools for electric shop.....		100, 000
Miscellaneous small buildings, tracks, etc.....	50, 000	
Welding equipment.....		275, 000
Tools for structural shop.....		250, 000
Covered welding platforms.....	100, 000	
	<u>2, 787, 000</u>	<u>1, 225, 000</u>
	1, 225, 000	
Total necessary.....	<u>4, 012, 000</u>	
Desirable:		
New fitting out pier.....	800, 000	
Dry dock crane and track connection.....	225, 000	
Desirable.....	<u>1, 025, 000</u>	

MUNITIONS INDUSTRY

NAVY YARD, NORFOLK

		<i>Tools</i>
Extension of railroad tracks, roads, etc.....	\$50, 000	
Two traveling cranes, pier 3, and strengthening pier.....	200, 000	
Extension of machine shop.....	125, 000	
Tools for machine shop.....		\$325, 000
Welding equipment.....		90, 000
Miscellaneous small buildings.....	15, 000	
Welding bays at structural shop.....	100, 000	
Tools for structural shop.....		270, 000
	<u>490, 000</u>	
	685, 000	<u>685, 000</u>
Total necessary.....	<u>1, 175, 000</u>	
Desirable:		
New pier 1,000' long.....	1, 400, 000	
Dredging for same.....	300, 000	
Dry dock services building.....	75, 000	
Desirable.....	<u>1, 775, 000</u>	

NAVY YARD, CHARLESTON

Storehouse for reserved material.....	\$100, 000	
Connect the two building ways.....	20, 000	
Welding equipment.....		50, 000
Tools for machine shop.....		150, 000
Tools for extended structural shop.....		100, 000
Tools for boiler shop, etc.....		50, 000
Miscellaneous buildings and services.....	50, 000	
	<u>170, 000</u>	
	350, 000	<u>350, 000</u>
Total necessary.....	<u>520, 000</u>	
Desirable:		
Storehouse for heavy materials.....	50, 000	
Additional berthing and services.....	500, 000	
Desirable.....	<u>550, 000</u>	

NAVY YARD, MARE ISLAND

Improvements to distributing systems.....	\$300, 000	
Tools for machine shop.....		200, 000
Welding equipment.....		80, 000
Welding platforms.....	100, 000	
Tools for structural shop.....		150, 000
Service building south of Independence wharf.....	50, 000	
Submarine barracks facilities.....	50, 000	
Reserved materials storage.....	100, 000	
Storage for heavy materials.....	75, 000	
	<u>675, 000</u>	
	430, 000	<u>430, 000</u>
Total necessary.....	<u>1, 105, 000</u>	
Desirable:		
Quay wall extension north to submarine wharf.....	250, 000	
Interrupted quay wall south of Independence wharf..	350, 000	
Desirable.....	<u>600, 000</u>	

NAVY YARD, PUGET SOUND

		<i>Tools</i>
Reserved materials storehouse.....	\$75,000	
New combined smith and pipe shop.....	550,000	
Tools for smith and pipe shop.....		\$100,000
Enlarge foundry.....	315,000	
Tools for foundry.....		75,000
Railroad tracks, concrete roads, etc.....	100,000	
Welding equipment.....		75,000
Welding platforms.....	100,000	
Tools for structural shop.....		200,000
Tools for machine shop.....		200,000
Fitting out pier.....	950,000	
	<hr/>	
	2,090,000	650,000
	650,000	
	<hr/>	
Total necessary.....	2,740,000	
	<hr/>	
Desirable:		
Storage for heavy materials.....	200,000	
Tools storage at heads of piers.....	30,000	
	<hr/>	
Desirable.....	230,000	

SUMMARY

Estimated cost to equip the Government navy yards to an annual capacity of:	
1 battleship	
1 aircraft carrier	
1 heavy cruiser	
1 light cruiser	
10 destroyers	
3 submarines	
Estimated cost of the minimum facilities necessary.....	\$17,604,860
Estimated cost of additional fitting-out piers, cranes, berthing spaces, etc., facilities not absolutely necessary but desirable from the standpoint of economical operation.....	6,000,000
	<hr/>
Total.....	23,604,860

Respectfully submitted.

F. W. AMADON.
C. H. SPENCER.

WASHINGTON, D. C., December 23, 1935.

The Committee submits the foregoing findings of the experts from the Interstate Commerce Commission as being substantial.

VI. COSTS OF POWDER AND AMMUNITION

In regard to powder, ammunition ships, and ordnance materials generally it is very doubtful whether the War or Navy Departments have ever tried very hard to give the private companies any real amount of competition. This is extremely unlikely in view of the War and Navy Department attitudes that the private manufacturers must be kept in business. The report on naval shipbuilding (S. Rept. No. 944, 74th Cong.) contains testimony to the effect that the New York Navy Yard was not allowed to put in a competitive bid on the aircraft carrier *Ranger*, after the specifications on that ship had been revised, although the yard wanted to do so (p. 40). A du Pont report (hearings, pt. 16, p. 3959) quotes a discussion with General Ruggles of the Ordnance Department:

An order for 200,000 pounds 75mm FNH will be open to bids in a very short time. The specifications are intended to insure procurement from the du Pont Co. I mentioned the possibility of the naval powder factory as a competitor, possibly repeating our experiences relative to bids for 14-inch powder 2 years ago. General Ruggles does not anticipate a recurrence of that situation.

In connection with Frankford Arsenal, C. L. Reiersen, president of Remington Arms Co. wrote of a conference with General Ruggles (exhibit 1284)

He [Ruggles] says that if the cartridge companies are to do anything about getting any of this business—provided they want it—it should be done just as soon as possible. He pointed out that once they [Frankford] have gotten their production up to a point that will take care of their full requirements he will be powerless to give the cartridge companies any business as he much prefers to do * * *.

This attitude is further reflected in a letter from General Ruggles to Remington Arms Co. (exhibit 1287) in regard to the rejection of a lot of 1,000,800 rounds, part of an order for 10,000,000 rounds.

An examination of the data submitted in connection with the test of this particular lot of ammunition indicates that in the firings in the Browning water-cooled machine gun in the first test of 800 rounds, two bullets were lodged in the bore approximately three (3) and five (5) inches, respectively, from the breech end. On a retest of 1,800 rounds in the same machine gun, one (1) bullet was lodged in the bore approximately three (3) inches from the breech end. In other respects the ammunition appears to meet the specifications, although it is noted that the spread of the groups in the hang-fire test is in most cases considerably larger than those obtained with Frankford Arsenal ammunition.

The defect of having a bullet lodge in the bore when a cartridge is fired is a very serious one, in that it precludes the issue of this ammunition to the service. Cartridges of this type would be dangerous to fire in the service weapons and in our surveillance tests of the great quantity of ammunition left over from war production we would relegate ammunition of this type to the unserviceable class and would withdraw it from the hands of troops for breaking down.

The Ordnance Department greatly regret that the defect is not one that can be overcome by reworking the ammunition and, therefore, under the terms of the contract the ammunition cannot be accepted. It will, therefore, be necessary for your company to submit another lot of ammunition to replace that rejected. In this connection it will also be necessary for you to provide the powder for the additional lot since the Government has already furnished you powder.

The department realizes that you have limited, if any, outlet for this ammunition and it has been considering how it might help reduce the loss to your company by buying from you from time to time such amounts of this ammunition as might be used in its own tests at a price which would relieve you of some of the loss and still not increase the cost to the department of the tests to be made.

We have been considering the use of this ammunition in certain erosion and other tests of machine guns. You realize, of course, that the lodgement of a bullet in the bore of a machine gun would cause a failure of the gun to continue fire. With ordnance personnel posted as to the defect in this ammunition there would not be much danger because they can be warned not to resume fire until they have determined by inspection if the bullet is lodged in the bore, and, if so, to remove the bullet. This possibility of a cartridge being fired with a bullet already lodged in the bore is considered too great to permit the use of this ammunition except under the most carefully guarded conditions.

We are now in a position to say how much of this ammunition we might be able to buy for limited tests but are making a study to determine this as exactly as possible under the circumstances. We will let you know what the possibilities are within a short time. We can, of course, only agree to buy this ammunition from time to time as the possibility for using it arises.

After having determined the probable amounts of this ammunition which we may use in limited tests within the next few years, we will communicate with you further so that you may determine then whether it will be more profitable for you to hold the defective lot on the prospect of selling part of it from time to time to the Government at a reduced price or to break the lot down. In case you determine it will be to your advantage to hold the lot in store on the prospect of selling it from time to time to the Government, you will be in a position to quote us a price at which you will sell it to us. Under the circumstances we would be able to purchase the ammunition without advertising for competitive bids.

The lack of effective competition in regard to powder is illustrated by the following letter from the director of military sales of the du Pont Co. to its foreign representative, Col. W. N. Taylor (exhibit 1355).

JUNE 30, 1932.

*54—ESTHONIAN GOV'T.
MS-80-A
MS-64

Colonel W. N. TAYLOR,
16 Place Vendome, Paris, France.

DEAR SIR: We are attaching confirmation of your cable no. 991 and our reply no. 824. We have noted carefully your cable no. 991 indicating that Esthonia are requesting bids to be opened July 1932, on 15,000,000 cartridges, delivery specified in autumn 1933.

The competitive prices quoted by I. C. I. and Bofors disrupt our price schedule and made a noticeable differential in favor of the competitors insofar as made-up ammunition is concerned. You have advised that our maximum prices must be \$1.40 per kilogram c. i. f. England insofar as I. C. I. is concerned, which price includes 3% commission and \$1.50 per kilogram c. i. f. Belgium on sales to Fabrique Nationale, which price includes 5% commission.

Our cablegram has authorized you to quote these prices and naturally since they are considerably below our usual export schedule they must be considered our minimum figure. You must realize that our price schedule on rifle powder sales to the U. S. Government is 71 cents per pound f. o. b. Carney's Point, excluding boxes. The prices you have quoted figures, in the instance of sales to England, a gross selling price f. o. b. Carney's Point, including boxes, of 54½ cents and in the instance of Belgium a price of 57.6 cents, thereby reflecting a noticeable reduction.

Since our sales to the United States total approximately 700,000 pounds of rifle powder annually, we cannot take the chance of this reduced figure being divulged. Therefore, you must arrange some plan in submitting your proposal so that you will be absolutely satisfied that the prices quoted will be regarded with the utmost secrecy. We wish to make ourselves very emphatic on this point, and in the event you cannot work out the required arrangement or feel that our idea cannot be accomplished then we must advise you not to quote.

K. K. V. CASEY, Director.

This letter shows that prices of 54.5 cents a pound were quoted to England and 57.6 cents a pound to Belgium, although the price to the United States Government was 71 cents, and powder amounting to 700,000 pounds annually was being sold to the United States Government.

In 1928 various ammunition manufacturers were interested in discovering the Government's cost for manufacturing 30.06 caliber boat-tail cartridges in comparison with their own costs. This is a standard United States Infantry ammunition. The arrangement was that Frankford Arsenal would receive the information concerning the cost of manufacture in the private plants in exchange for its information on costs. This part of the arrangement was not carried out. Frankford Arsenal furnished its figures and received none in return.

The figures compiled by the manufacturers showed their costs to be much higher than those at Frankford Arsenal, even when items such as capital charges and taxes were added to Frankford costs.

(The discussion of this situation is contained in the hearings of the committee, pt. 16, p. 3948 seq. and exhibits 1283-1301).

The adjusted cost figures showed per thousand (exhibit 1294).

	Frankford Arsenal	Peters	Remington	Western	Winchester
Materials furnished by manufacturer.....	10.33	10.93	9.20	10.53	9.83
Materials furnished by Government.....	11.73	11.73	11.73	11.73	11.73
Labor.....	3.59	5.86	3.10	5.77	3.83
Factory burden.....	4.39	6.98	9.73	9.55	11.72
1 percent shrinkage.....	.18	.24	.22	.26	.25
Cost at factory.....	30.22	35.74	33.98	37.84	37.36
Administration expense.....	.83	.59	1.37	.74	1.39
Interest on plant investment and working capital.....	.82	.79	1.51	2.72	1.43
Total cost exclusive of profit.....	31.87	37.09	36.56	41.30	39.18
Profit 10 percent on above, less interest.....	3.11	3.63	3.54	3.86	3.83
Total cost including profit.....	34.98	40.72	40.40	45.16	43.06
Less cost of materials furnished by Government (net).....	23.25	28.99	28.67	33.43	31.33
Selling price less 10 percent (profit) on United States material.....	1.17	1.17	1.17	1.17	1.17
Net selling price.....	22.08	27.82	27.50	32.26	30.16
Add 5 percent for rejections.....	1.10	1.39	1.38	1.61	1.51
Net selling price.....	23.18	29.21	28.88	33.87	31.67

Deducting only two items from Frankford Arsenal figures (but leaving items for taxes, depreciation, administrative expense in overhead) not actually paid out by Frankford Arsenal, but added by manufacturers for comparison: Interest on plant and working capital \$0.82; profit \$1.94 (\$3.11 less \$1.17), total \$2.76. The net selling prices of the companies and the arsenal are:

	Percent
Frankford Arsenal.....	20.43
Peters.....	29.21
Remington.....	28.88
Western.....	33.87
Winchester.....	31.67
Higher than Frankford:	
Peters.....	42.9
Remington.....	41.3
Western.....	65.7
Winchester.....	55.0
Average.....	51.2

Before deduction of these two unpaid items, but leaving in estimated costs for depreciation, administrative expense, overhead, and taxes, the companies are higher than Frankford by: 26.0, 24.5, 46.1, 35.3 percent; average, 32.9 percent.

These figures, available to the manufacturers, were not presented to the Committee of the House of Representatives in 1932, but some older figures, taken in 1926 by an accident employed by the ammunition industry, were offered instead (exhibit 1300). This was a better investigating Government competitive with private business. The War Department, of course, had not been supplied with the munitions companies' figures, in spite of the agreement, and would therefore not Shanin the evidence. The companies proposed that Frankford Arsenal go out of the business of producing ammunition, although in the same statement (exhibit 1300) they described Frankford Arsenal as having—

new and up-to-date machinery was installed by the Government for increasing the production capacity of and reducing costs at Frankford Arsenal. Machines were rearranged and extensive conveying systems were installed. An excellent job of mechanical engineering resulted in elimination of operations and labor which, with the increased production now totaling about 300,000 rounds per day, brought the costs at Frankford, when figured by their system of accounting, far below anything that a commercial manufacturer could attain.

They neglected to say that when Frankford was figured on the companies' own methods of accounting, including taxes, depreciation, etc., the companies were still 32.9 percent above Frankford, and leaving out profit and interest were 51.2 percent above Frankford.

Remington Arms Co. later furnished the committee with estimates tending to show that its cost of manufacturing 10,000,000 rounds would be (less material furnished by the Government) \$23.62 per thousand compared to \$19.14 for Frankford Arsenal. However, this was before profit or investment, and on September 3, 1927, Remington had bid \$30 per thousand on 10,000,000 rounds.

VII. COST OF MACHINE-GUN PLANT

The Interstate Commerce Commission engineers presented figures showing that the cost of constructing machine-gun facilities equal to those now available to the Government at the Hartford plant of the Colt's Patent Fire Arms Manufacturing Co. would be (Feb. 6, 1936, exhibit 4407):

	Cost, new	Cost, less depreciation
Plant and land.....	\$5,715,987	\$2,587,159
Patterns, tools, etc.....	2,941,429	2,941,426
Automobiles, furniture, etc.....	158,000	158,000
Total.....	8,815,413	5,686,585

The cost of building an entirely new plant would be \$8,815,413. The cost of acquiring a plant in no better condition than the present plant would be approximated by the figure \$5,686,585.

No figures were compiled on possible costs of patents.

Colt's furnished the Army 97 percent of the small arms purchased from private manufacturers in recent years (exhibit 440).

VIII. COST OF AIRPLANE FACILITIES

The Interstate Commerce Commission engineers presented figures showing that the cost of constructing airplane production facilities equal to those now available to the Government in the Pratt-Whitney Aircraft Co. (engines and propellers) the Chance Corporation (bodies) and United Airports, Inc. (testing field), would be (Feb. 6, 1936, exhibits 4404, 4405, 4406):

	Cost new	Cost less de- preciation
Engines and propellers.....	\$3,020,891	\$4,929,653
Bodies.....	1,358,071	1,179,621
Testing field and equipment.....	1,072,165	993,632
Total.....	8,451,127	7,093,905

The cost of building an entirely new plant would be \$8,451,127. The cost of acquiring a plant in the condition of the present plant would be approximated by the figure \$7,093,905.

No figures were compiled on possible costs of patents.

IX. COST OF POWDER PLANT

In Interstate Commerce Commission engineers presented figures showing that the cost of constructing powder manufacturing facilities equal to those at the Carney's Point plant of the du Pont Co. would be (Feb. 6, 1936, exhibit 4410):

Cost new (plant, equipment and land)-----	\$2, 563, 085
Add: Acid plant-----	1, 075, 000
Total-----	3, 638, 085
Cost less depreciation-----	1, 334, 100
Add: Acid plant-----	1, 075, 000
Total-----	2, 409, 100

The cost of building a new plant would be \$3,638,085. The cost of acquiring a plant in the condition of the present plant would be approximated by the figure \$2,409,100.

The Carney's Point plant furnishes 99.4 percent of the Army's cannon powder and 98.6 percent of the small-arms powder and some amount of powder for the Navy.

No figures were compiled on possible costs of patents.

Figures on the Navy Department's investment in its plant at Indianhead, Md., were given as: Cost new (excluding land), \$4,-234,186. Cost less depreciation, \$2,025,871. This investment includes acid plants.

X. ARMOR PLATE PLANT

(Steel company figures)

Officials of the three steel companies now supplying the Navy with armor plate prepared for the committee figures on the investment in their plants devoted to armor plate. These figures were not checked by committee accountants for lack of funds (Feb. 7, 1936).

	Capacity, light armor plate	Original investment of value
	<i>Tons</i>	
Bethlehem Steel Co.-----	3, 000	\$7, 193, 439
Midvale Co.-----	5, 000	6, 236, 000
Carnegie Steel Co.-----	9, 000	6, 303, 672

XI. PRICES OF PROJECTILES, GUN FORGINGS, ARMOR PLATE

(Steel company figures)

The existence of three companies being awarded contracts for projectiles, gun forgings, and armor plate does not necessarily mean that a competitive price situation exists among them. On naval ordnance order 272, the bids were, in 1930 (exhibit 4494): Carnegie, \$560 per ton (turret armor); Midvale, \$690; Bethlehem, \$670.

On this award Carnegie, according to its own figures made 57.9 percent profit. The Carnegie officials were questioned whether their prices had dropped to the Government after these high profits had been made on this contract. (Transcript Feb. 7, 1936, p. 13746 et seq.) It developed that the official whose duty it was to enter bids stated that he did not know of the profits.

Question. When you make the bids, do you not know how much profit you have made on an earlier bid of the same character?

Answer. (Mr. Cooney). No; I cannot say that I do.

Question. How can you draw bids without knowing how you would come out on them on similar operations?

Answer. (Mr. Cooney). By comparison with other prices, competitors' prices.

It seems clear that when one company can make a profit of \$203.14 per ton at \$560 per ton and that the other companies bid \$130 and \$110 above the low bid, there is no great competition in that instance. In spite of these profits, by 1933 Carnegie was bidding \$585 on turret armor instead of \$560.

A very brief examination of three of the largest suppliers of armor plate and projectiles was held on February 7, 1936. It developed that these companies, in the normal course, had destroyed their files for the war years. The examination was confined to a few matters, the first dealing with the cost of each company's plant available for Navy Department work.

Bethlehem Steel Co., officials¹ put the original cost of their investment in armor plant at \$7,193,439, which had not been reduced by any depreciation. They stated the capacity of such a plant at 3,000 gross tons of light armor plate. At present this plant is also used for heavy gun forgings and heavy shaft forgings. The company officials doubted that a new plant with equal capacity could be built for less than the original cost of this plant.

The company sold from 1925 to 1934, inclusive, steel amounting to \$4,745,874 to Newport News Shipbuilding Co., \$5,204,243 to New York Shipbuilding Co., and \$14,799,011 to Bethlehem Shipbuilding Co., as well as about one million dollars' worth to other shipbuilding companies. For these years it furnished armor plate, gun forgings, and projectiles to the Navy Department in the amount of \$7,246,175 as well as a considerable amount of steel for the navy yards.

¹ Transcript of hearings, Feb. 7, 1936, p. 13551.

Bethlehem had many war contracts with foreign belligerents during the war outside of those made through the agency of J. P. Morgan & Co. Through that agency there were \$40,839,065 in contracts with the French and \$58,436,286 in contracts with the British.¹

Bethlehem submitted costs and profits on certain armor plate contracts, preparing the costs and profit figures especially for the committee and using the principles the company expected to use on contracts under the Vinson Act. One contract showed a profit of 6.58 percent, another 21.91 percent, another 5.89 percent, another 2.21 percent. The figures were not checked by the committee's accountants, nor was the system used for depreciation or general expense. In many cases depreciation was higher than the cost of the material.

Certain contracts for gun forgings showed a profit over cost of 28.27 percent, 18.47 percent, and 18.09 percent.

Reminded of the testimony of Mr. Eugene Grace in 1917 that a plant running 23 percent capacity would produce armor plate costing \$499 per ton, while a plant running 100 percent would produce it for \$315, the Bethlehem officials were asked concerning the possibility of a similar reduction in cost in case their plant was operated at 100 percent capacity. (From the time the cruiser building started in 1927 through 1934 the plant operated at 25 percent capacity² on Government business and an additional 10 percent on commercial steel.) The witness admitted the possibility of much lower cost on full-time production.³ Mr. Johnstone testified that a great decrease in cost of production does not necessarily reflect itself in similar lower costs to the Government—

because you never know until after the event, after the passage of perhaps a period of 4 or 5 years, whether you are actually going to operate at 15 percent or 50 percent.⁴

Question. Does it therefore follow that when you get more orders, as you have in recent years, and your plants fill up to a larger extent, the Government therefore gets a big cut in the price of these things?⁵

Mr. JOHNSTONE. It does not reflect itself automatically.

Question. It far from reflects itself, does it not, during recent years, when your plants have all been more full than before?

Mr. JOHNSTONE. That is right.

Certain contracts for projectiles showed a profit over cost of 13.42 percent, a loss of 4.89 percent, a profit of 8.92 percent, a loss of 14.09 percent, a loss of 5.72 percent, a profit of 49.55 percent. None of these figures were checked by the committee, and the difficulty of such check for purposes of the Vinson Act limiting profits of Navy supplies to 11.1 percent was admitted:⁶

Mr. RAUSHENBUSH. We have not been able to check any of these costs; as I gather it, that would be a hard thing for anybody to come in from the outside and do without following every job practically through the factory. Is not that true?

Mr. JOHNSTONE. Certainly. Over a 10-year period to take each particular contract and to build up the small items that naturally go into any of these totals—

Mr. RAUSHENBUSH. You would practically have to follow it through from beginning to end?

¹ Ex. 4414.

² Transcript of hearings, Feb. 7, 1936, p. 13569.

³ *Ibid.*, p. 13570.

⁴ *Ibid.*, p. 13581.

⁵ *Ibid.*, p. 13582.

⁶ Transcript of hearings, Feb. 7, 1936, pp. 13573-13575.

Mr. JOHNSTONE. Certainly.

Mr. RAUSHENBUSH. I do not quite see how you people managed to put these figures together of the old contracts like that without following them through.

Mr. JOHNSTONE. We spent probably 2 or 3 months with four or five men assembling these figures.

Mr. RAUSHENBUSH. Going through the past records?

Mr. JOHNSTONE. That is right. These, of course, were just a few typical contracts, and they were most of them within the last 5 or 6 years, as I recall it.

Mr. RAUSHENBUSH. Coming back to the Vinson Act, a given contract of yours might take 2 years to go through the mill, in some cases 3 years, perhaps. During the time it is going through, as I understand it, there is no Treasury official or no Navy Department official standing there next to your own cost accountants to watch the thing go through the mill?

Mr. SHICK. That is true.

Mr. RAUSHENBUSH. So at the end of the period when they want to check on the figures for the purpose of the Vinson Act, they would either have to run a complete audit of the kind that had taken you so long or completely take your word on it?

Mr. SHICK. We will have figures to show what our cost was, hereafter.

Mr. RAUSHENBUSH. So far as checking it up, they would just take your figures?

Mr. JOHNSTONE. It will be a good deal more simple, probably, in the future than it has been in the past, because the figures would be necessarily useful or necessary in connection with the Vinson Act contracts and be kept accordingly.

The Midvale Co. was known until 1915 as the Midvale Steel Co. In 1915 its stock was acquired by the Midvale Steel & Ordnance Co. In 1923 this company was acquired by the Bethlehem Steel Co. except for the old Midvale plant at Nicetown, Pa. This plant has been operated since 1923 as the Midvale Co. About 61 percent of this company's stock has been acquired by the Baldwin Locomotive Co. The chief line of the company is special forgings. From 1930 on about 20 percent of the production has been for the military services.¹

The company estimated that the value of its plant used for armor plate was \$6,236,000.² This is a figure before depreciation. A new plant, built exclusively for armor plate, might be so arranged that the cost of operation would be less than in the present plant.³ This plant can produce approximately 5,000 tons of light armor plate. Since 1929 the company has sold armor plate to the Navy Department costing the Government \$5,115,428,⁴ gun forgings costing \$3,685,842, and projectiles costing \$3,183,373.

On a selected list of orders covering all three classes, costing the Government \$5,982,386, Midvale calculated a cost of production of \$5,429,291 and a profit of \$553,095, or over 10 percent of cost. Depreciation charged to these contracts was \$1,157,591.⁵ The depreciation of the plant for the idle years (1922 to 1929, the years of the disarmament agreement) was included in the calculation on the cost of the orders sold to the Government from 1929 on.⁶

Question. So that all during the period when we were not building ships, the cost of that naval limitation got paid for later on when we did start building ships? Is that not right?

¹ Transcript of hearings, Feb. 7, 1936, p. 13593.

² Ex. 4415.

³ Transcript of hearings, p. 12590.

⁴ Ex. 4416.

⁵ Ex. 4419.

⁶ Transcript of hearings, p. 13605.

Mr. MILLIKEN. It is true that we carried our depreciation against the amount of business that we received. That is the only way we could get a return for this part of the cost.

No witnesses could testify as to the evidence introduced into the banking hearings consisting of letters signed by A. C. Dinkie, then president of Midvale Steel & Ordnance Co. indicating that that company was delaying orders on United States production during the war and giving British order the preference,¹ or concerning the higher prices apparently charged to the United States for howitzers.

Exhibits 4422-4428 indicate that Midvale Steel & Ordnance Co. kept from the Government the information in its possession that the cost of pig iron to it was \$51.29 per ton while informing the Government that the cost was actually \$75 per ton, and as a result of this misinformation was allowed to receive a much higher price than it otherwise would have received on an order of 13,500 14-inch projectiles. The company, knowing the truth, nevertheless continuously informed the Government that the price of this raw material was 46 percent higher than it actually was. On the basis of estimated costs for such shells² with pig iron at \$50 and at \$75 the Government's loss on this misinformation seems to have been about \$300,000 on this order.

Data on Army and Navy armor-piercing projectiles³ compiled on June 5, 1920 indicate that the cost of the shells (exclusive of amortization) was \$230 on 12-inch shells sold to the Government for \$380; \$300 on 14-inch shells sold to the Government for \$580, and \$551 on 16-inch shells sold to the Government for \$900. According to this tabulation the profit on these 35,800 shells seems to have been \$8,935,900.

Evidence was introduced that the three big armor-plate companies consulted together before accepting contracts in 1919.⁴

Costs for Navy turbines for New York shipyards and William Cramp & Sons were given, showing costs of about one-fourth of the sales prices.⁵ The Navy became interested in the costs.⁶ William Cramp & Sons informed Midvale that the Compensation Board was authorizing a price of 52.25 cents per pound, as compared with the Midvale figure of 84.95 cents per pound, and asked for a statement of costs to justify the higher price in case Midvale persisted in claiming it.⁷ The Midvale auditor suggested accepting the 52.25 cents to avoid further controversy.⁸ (The actual costs as shown in exhibit 4432 were from 18.29 cents to 32.25 cents.) Mr. Milliken, the auditor, stated that these were manufacturing costs.⁹

Close relations between the armor-plate companies during the war years were evidenced in exhibits 4438 et seq. Mr. Neale, of Midvale, noted that Mr. Balsinger, of Carnegie, informed him that he would quote \$520 on a certain armor plate order "no delivery." This was the price later quoted.¹⁰ Exhibit 4440 indicates that the companies agreed among themselves as to division of Government orders. The

¹ Transcript of hearings, Feb. 7, 1936, p. 13613.

² Ex. 4429.

³ Ex. 4430.

⁴ Ex. 4431.

⁵ Exs. 4432, 4433.

⁶ Ex. 4434.

⁷ Ex. 4435.

⁸ Ex. 4436.

⁹ Transcript of Hearings, p. 13625.

¹⁰ Ex. 4441.

discussion of price in advance of bidding is evidenced in exhibit 4442. Further interchange of information is seen in exhibit 4443 from Balsinger, of Carnegie, to Dinkie, of Midvale. The armor plate companies seemed to know about Navy plans before the Secretary of the Navy did.¹ The companies wanted to get new prices for light armor for the cruisers after the war.² The question of readvertising bids or modifying the old awards was involved. A Navy officer was quoted as saying:

What difference does it make to you if you get what you want no matter how it is done.³

In a conference with Navy officials the three armor-plate companies refused to take the prices proposed by the Navy, and asked for \$60 extra per ton for light armor, "which had been agreed upon by the other steel manufacturers."⁴

The Navy was interested during the war in the cost of gun forgings, and requested that, prior to an extension order, Midvale's accounts be opened to Government auditors.⁵ The Midvale auditor replied that—

in view of the fact that our costs are much lower than the estimate on which sale prices were established, it would seem advisable not to have our costs examined.⁶

The costs for the forgings, which Mr. Milliken stated were manufacturing costs, were 34.13 cents per pound on 3-inch rough forgings, 23.01 cents per pound on 4-inch rough forgings, and 23.44 cents per pound on 5-inch rough forgings.⁷ The company offered to accept a reduction of 1 cent per pound.⁸

Summaries of orders compiled by Midvale show that from 1923 to 1928 the Midvale and Bethlehem awards from Navy Ordnance were constantly close, in 1928 totaling \$2,080,669 for Midvale and \$2,044,999 for Bethlehem.⁹

Midvale sales of munitions included gun forgings from 1924 on, projectiles from 1927 on and armor plate from 1930 on, totaling \$9,648,896.¹⁰ There were also sales to the shipbuilding companies.¹¹

Friendly relations between Carnegie and Midvale Steel and Ordnance were indicated in a letter from Balsinger to Dinkie.¹² Midvale was interested in finding ways by which the bidding of arsenals and Navy yards might be avoided.¹³ One bid in 1926 on four thousand 14-inch projectiles shows Midvale bidding \$102 and the Naval Gun Factory bidding \$68. On a quantity of two thousand and five hundred 5-inch projectiles Midvale bid \$27.58 and Frankford Arsenal \$14.95. On three thousand and one hundred 6-inch projectiles in 1926 Midvale bid \$69.75 and Frankford \$31.74.

The Carnegie Steel Co. is a subsidiary of the United States Steel Co. It furnished the committee with figures showing that the orig-

¹ Ex. 4444.

² Transcript of Hearings, p. 13623.

³ Ex. 4445.

⁴ Ex. 4446.

⁵ Ex. 4448.

⁶ Ex. 4449.

⁷ Ex. 4450.

⁸ Ex. 4451.

⁹ Ex. 4455.

¹⁰ Ex. 4456.

¹¹ Ex. 4457.

¹² Ex. 4497.

¹³ Exs. 4498-4404.

inal cost of its armor plate plant was \$4,970,672 plus a real-estate value of \$364,000 and auxiliary equipment cost was \$975,000.¹

Cost of armor plate plant.....	\$4, 970, 672
Real-estate value.....	364, 000
Auxiliary equipment.....	975, 000
Total.....	6, 309, 672

This plant has an annual capacity of 9,000 tons of light armor plate.¹

U. S. Steel Products Co. showed contracts with the British Government, through J. P. Morgan & Co., of \$62,514,546 from 1915 to 1917² and \$52,781,486 with the French.

Sales of steel to various shipbuilding companies, both for the commercial and naval ships, amounted to \$29,389,055 from 1925 to 1934.

Armor plate contracts with the Navy Department totaled \$2,362,204 from 1930-35. Contracts for special-treatment steel with the Navy Department totaled \$10,152,076 for 1926 to 1935.³

Selected armor plate contracts showed, according to the company's figures, as follows:

	Cost	Proceeds	Profit	Percent	Profit per ton
NOD-272.....	\$226, 124	\$357, 093	\$130, 669	57. 9	\$203. 14
NOD-331.....	149, 399	214, 318	64, 919	43. 4	166. 72
NOD-432.....	161, 455	144, 903	43, 418	42. 7	159. 23

These profits, according to the company's auditors were after material and plant expense, general expense, taxes, and depreciation,⁴ Contract 272 was for conning tower armor and turret armor, class B, in 1930. Carnegie's bids for conning tower armor dropped \$10 in 1933 from the 1930 bid of \$610. Turret armor, class B, rose from \$560 in 1930 and 1931 to \$585 in 1934 and \$595 in 1936.

Contract 331 was for turret armor, class B, in 1931 at \$560 per ton. The company bid and received awards for this class of armor for \$585 in 1934 and \$595 in 1935.

Contract 432 was, according to the company's exhibit for several classes of armor in 1933, being \$545 on class B turret armor. Other bids in 1934 and 1935 show bids of \$585 and \$595 on this class.⁵

Carnegie officials were questioned whether their prices had dropped to the Government after these high profits had been made on individual contracts.⁶ It developed that the official who made the bids stated that he did not know of the profits.

Question. When you make the bids, do you not know how much profit you have made on a earlier bid of the same character?

Mr. COONEY. No; I cannot say that I do.

Question. How can you draw bids without knowing how you would come out on them on similar operations?

Mr. COONEY. By comparison with other prices, competitor's prices.

¹ Ex. 4460.

² Ex. 4462.

³ Ex. 4466.

⁴ Ex. 4468, 4469.

⁵ Ex. 4473.

⁶ Transcript of Hearings, p. 13746 seq.

It was developed that on the contract on which Carnegie made 57.9 percent profit, Bethlehem bid \$130 a ton above Carnegie and Midvale bid \$110 above Carnegie.¹

The company furnished a typical mill cost make-up for protective deck plates shows the total cost of the ingots as \$45,983 per ton, of rolled slabs \$62,177, of rolled plates at \$80,276, and of rolled protective deck plates as \$126,168.²

It showed figures on three major steel commodities used in shipbuilding from 1925 to 1934, inclusive.³

	Gross tons shipped	Proceeds	Material and plant expense	General expense
Heavy structural shapes.....	790, 127	\$30,968, 257.00	\$27,934, 010.00	\$964, 599.00
Rate per ton.....		39.19	35.35	1.22
Universal plates.....	904, 172	34,358, 198.00	39,889, 815.00	1,027, 655.00
Rate per ton.....		38.00	34.16	1.14
Sheared plates.....	2, 680, 919	99, 168, 705.00	95, 020, 353.00	3, 140, 407.00
Rate per ton.....		38.42	36.82	1.22

	Taxes	Depreciation	Total cost	Profit (+) and loss (-)
Heavy structural shapes.....	\$303,395.00	\$1,770,292.00	\$30,972,296.00	-\$4,039.00
Rate per ton.....	.38	2.24	39.20	-.01
Universal plates.....	312,728.00	1,957,132.00	34,187,330.00	+170,863.00
Rate per ton.....	.35	2.16	37.81	+.19
Sheared plates.....	918,838.00	5,610,383.00	104,690,011.00	+5,521,306.00
Rate per ton.....	.36	2.17	40.56	+2.14

The company's files showed a compilation of material for armament purposes made by Carnegie for 1924 to July 1934. It totaled 125,854 tons.⁴

In the winter of 1934 the War Department, according to G. Elkins Knable, manager of Carnegie Steel Co., signing himself as "Lt. Col., Ord. Res.", the War Department was offering the steel companies more favorable contracts for wartime than they had previously considered.⁵ The imminence of the Senate munitions inquiry seems to have held up the discussion.⁶ In 1934 Carnegie Steel Co. officials outlined the objections to any act limiting profits to 10 percent.⁷

A compilation made for the president of the U. S. Steel Corporation showed that from 1925 to 1934 (six months) the production of "armaments for war purposes" was—⁸

	Tons
American Bridge Co.....	9,274
American Sheet and Tin Plate.....	5,364
Carnegie Steel.....	135,854
Columbia Steel.....	3,406
Illinois Steel.....	2,100
Lorain Steel.....	481
National Tube.....	9,609
Total.....	156,088

¹ Transcript of Hearings, Feb. 7, 1936, p. 13740.

² Ex. 4471.

³ Ex. 4472.

⁴ Ex. 4475.

⁵ Ex. 4478.

⁶ Ex. 4479.

⁷ Ex. 4480.

⁸ Ex. 4492.

Abstracts of bids for armor plate, projectiles and gun forgings were submitted as exhibits 4494, 95, 96.

The relationship between the bids, awards, costs, and profits was not entered into by the Committee further for lack of staff to check figures.

Crucible Steel Co. reported sale of projectiles to the United States Government between 1927 and 1935 of \$6,431,447. The projectile orders began in 1929.

XII. PRICES AT GOVERNMENT PLANT

Frankford Arsenal (Philadelphia) does not offer a yardstick to the bids of the private steel companies on armor plate or gun forgings, but does offer one, in some cases, on projectiles. Evidence introduced tended to show that on the advertisements for material over \$200,000 in value, Frankford Arsenal underbid the steel companies with fair regularity (Exhibit 4495). Bethlehem officials pointed out that in some cases that company had underbid Frankford, and furnished a list of other bids, which, however, was incomplete. A tabulation was thereupon made showing all projectile bids on which Frankford Arsenal bid at all. It shows that Frankford was lower than all steel companies in 35 out of 71 items in the years 1926-35. When the cost of Government inspection of 6.6 percent is added, Frankford production cost the Government less in 48 out of 71 items.

Year	Item	Bethlehem		Midvale	Crucible		Tredegar	Frankford, Government
		Bid	With inspection costs		Bid	With inspection costs		
1926	14' target			\$102.00				\$68.00
	6' Comm			69.75				31.74
	5' Comm			27.58				14.95
	5' Ill			24.60				12.76
	5' AA			26.73				13.62
1928	3', 50 Cal., Ill	\$4.75						5.26
	3', 25 Cal., Ill	4.75						5.52
1929	5', 25 Cal., AA	9.26						8.93
	5', 25 Cal., Ill	9.45						8.97
1930	4' Ill	7.37	\$7.85					7.49
	3' 23 Ill	4.49	7.78					4.56
	5' AA., Com	8.33	8.87					8.74
1931	5' AA., Com	7.63						8.14
	5' AA., Com	7.81	8.32					8.07
	5' Ill	8.05			\$8.00	\$8.52		8.03
1932	5' AA., Com	6.35						6.89
	3' Ill	3.34						2.43
	5' AA., "A"	16.45						19.66
	5' AA., "B"	16.63						19.69
	5' AA., "C"	16.68						19.66
	5' AA	16.60						10.94
1933	5'/25 AA	7.55			7.11	7.57		7.49
	5'/25 AA	7.50			7.09	7.55		7.43
	5'/25 Ill	7.36	7.84					7.64
	5'/38 AA	7.25						7.73
	5'/38 Ill	7.21						7.64
	3' Ill	3.84						2.89
	5'/38 AA	6.25	6.67					6.43
	5'/38 Ill	6.53						6.32
	5'/25 Ill	6.41						6.17
	6' Com	39.00						35.34
	6' Ill	44.00						32.44
	5'/38 Ill	7.21						6.97
	5'/25 Ill	7.36						6.80
	5'/38	6.74						7.30

Year	Item	Bethlehem		Midvale	Crucible		Tredegar	Frankford, Government
		Bid	With inspection costs		Bid	With inspection costs		
1934	8"/55 drill	\$75.00		\$78.00			\$62.18	\$20.00
	3" field gun	7.40						4.47
	3" field gun	4.19						3.81
	5"/25 AA	8.20						7.04
	4"/50 Ill.	9.25						8.33
	3"/23 Ill.	4.10						2.99
	5"/25 AA	6.90	\$(7.35)					8.34
	5"/38 AA	6.80						8.52
	5"/38 Ill.	7.89	(8.40)					8.27
	4"/50 Ill.	9.25						8.64
3"/23 Ill.	4.10						3.79	
1935	5"/25 AA	6.60						7.78
	5"/25 Ill.	8.55						7.74
	5"/38 AA	6.70						8.31
	5"/38 Ill.	8.75						8.14
	1" AA							.60
	1" AA							.60
	5"/38							16.87
	5"/28					\$17.50		16.81
	5"/38					17.50		16.93
	5"/38	16.50	17.58					16.61
	5"/38 AA	8.59						8.24
	5"/25 AA	8.10						7.84
	5"/51 Ill.	9.00						7.97
	5"/38 Ill.	9.25						8.05
	4"/50 Ill.	9.25						8.05
	3"/23 Ill.	4.00						3.48
	5"/25 AA	7.10						7.67
	5"/38 Com.	7.79						8.49
	5"/25 AA	6.95						8.13
	5"/38 AA	7.74				7.70		8.47
	5"/38 AA	7.82				7.75		8.53
	6" Com.	28.00				24.95		36.49
5"/38 Com.	16.40				13.90		15.97	
5"/25 Ill.	8.85				8.30	\$8.84	8.74	
5"/38 Ill.	8.45				8.00		8.78	

In 1926 the Frankford bids were about half of the Midvale bids. After this, Bethlehem became the main bidder against Frankford until Crucible reentered the field in 1935. When Frankford was not bidding the Tredegar Co., in many cases, heavily underbid the other steel companies (exhibit 4495).

The bids do not indicate costs, except roughly, since it is the Government's policy to encourage the steel companies to continue in production of war material, and this may have had an effect on the bids offered by Frankford Arsenal. It is to be noticed, in this connection, that almost without exception where Tredegar, Bliss, or, in cases, Crucible entered the bidding, Frankford simply did not bid at all.

On the two bids in 1926, the Government saved a considerable sum through the existence of Government plants. The first bid (exhibit 4495) was for 4,000 14-inch target projectiles, awarded to the Naval Gun Factory at \$68 over Midvale at \$102, the saving of \$34 per shell amounted to \$136,000.

The second bid in 1926 was:

	Number	Frankford	Midvale	Saving per shell	Total saving
6" Comm.....	3,100	\$31.74	\$69.75	\$38.01	\$117,831
5" Comm.....	2,500	14.95	27.58	12.63	81,575
5" Ill.....	7,500	12.76	24.60	11.84	88,800
5" A.A.....	19,000	13.62	26.73	13.11	249,090
Total.....					487,296

Frankford has not bid on heavy projectiles over 6 inch, and the Naval Gun Factory has bid rarely.

The bidding on the heavier projectiles has been:

	Bethlehem	Midvale	Tredegar	Crucible	Naval Gov't Factory	Frankford Arsenal
1926						
14" target.....		\$102.00			\$68.00	
6" Comm.....		69.75				\$31.74
1927						
14" target.....		111.50	\$74.25			
8" Comm.....	\$144.25	147.50		\$139.00		
14" target.....	69.96	101.50				
1928						
8" target.....	67.85	48.25				
14" target.....	65.71	81.03	57.79			
8" target.....	36.23	36.53				
1929						
14" target.....	57.00		51.06			
8" drill.....	150.75	90.70		29.80		
8" Comm.....	146.00	152.00		143.50		
1931						
14" target.....	47.60	81.75	44.23			
8" target.....	24.74	27.40	22.00			
8" drill.....	75.00		37.15			
8" Comm.....	142.50	146.25				
1932						
14" target.....	81.00	59.75				
8" target.....	16.50	20.18				
1933						
8"/55 drill.....	75.00		56.29			
14" target.....	45.00	60.52	43.23			
8" target.....	19.50	22.35		19.42		
1934						
8"/55 drill.....	75.00	78.00	62.18			

There is, of course, little question that a plant tooled up for a given size of standard projectile, and receiving a stream of orders could produce them more cheaply than a plant only receiving occasional orders.

The War Department's only analysis of the price situation was made by the Kernan Board in 1916 (S. Doc. No. 664, 64th Cong., 2d sess.). In that report was contained an exhibit showing that

arsenal costs were lower than private-plant manufacture by 18.6 percent (exhibit F). On certain items the saving by arsenal production was very considerable.

Articles purchased	Cost		Saving	Per cent
	Contract	Arsenal		
Field-artillery carriages, etc.....	\$545,966	\$380,906	\$165,060	43
Cannon powder.....	249,730	173,706	76,024	42
12" projectiles (700 pound).....	171,605	95,410	76,195	80
12" projectiles (600 pound).....	199,536	119,952	79,584	67
.30 cal. cartridges.....	315,680	217,120	98,560	45
Automatic pistols.....	760,624	619,839	140,785	23
Field-artillery shells.....	606,517	449,174	157,342	35
.45 cal. pistol cartridges.....	19,470	16,410	3,060	19
.30 cal. cartridges.....	2,864,900	2,397,600	467,300	19
Field-artillery shells and fuzes.....	5,381,039	4,890,676	490,363	10
Optical instruments.....	26,855	24,553	2,302	9.6
.38 cal. revolver cartridges.....	11,670	12,390	-720	-6

According to these figures on one order for \$100,000,000 of material of this character the saving through arsenal production would be \$18,600,000.

To the cost of material produced in the private plants should be added a charge for inspection paid for by the Government. The Kernan Board in 1916 estimated this to be 6.6 percent.

XIII. SURPLUS WAR SUPPLIES

The War Department sells material which it no longer needs at open competitive sales. Testimony concerning the activities of some of the second-hand dealers engaged in purchasing such material was presented before the House Military Affairs Committee in 1935 and 1936. The material may be used or it may be unused. No adequate figures have been secured on the original cost of the material sold by the Department. Much of it consisted of supplies accumulated during the World War, which later deteriorated. Testimony was given before the committee that millions of pounds of powder produced at Old Hickory had deteriorated. Some of this was sold. Some of it was exchanged for new powder, the chemical companies using the old powder for commercial purposes.

Information furnished by the War Department showed that material acquired at a very considerable cost had been sold for very little (exhibit 4838).

The testimony of Mr. Henry F. Butts, in command of the ballistic bureau of the New York Police Department (Feb. 15, 1936) indicated that occasionally the guns sold as scrap metal by the Quartermaster's Department are repaired and converted to the use of gangsters. He stated that in New York City there have been six killings by Thompson submachine guns, and that the department has confiscated 15 to 20 of them and that four of the Browning machine rifles had been confiscated. He testified that of the 15,000 Thompson submachine guns manufactured only 6 or 7 thousand are left. "Up to 5 years ago they did not have any regulation on that gun. You could walk into a store in New York City and purchase a Thompson submachine gun when you could not get a .38 Colt revolver."

Mr. Thomas I. Todarelli, formerly assistant United States attorney for the southern district of New York testified (Feb. 19, 1936) that in 1931 a group of Cuban revolutionaries had bought from Francis Bannerman & Sons, in addition to many rifles, 200 Vickers machine guns, 22 Lewis machine guns, and 2 Browning automatic rifles. From I. Silverman Bros., a New York firm, they bought 22 Lewis machine guns. Much of this material was sent to R. F. Sedgley, in Philadelphia, for repairs. He stated that both Bannerman and Sedgley had promised to notify the Department of Justice if attempts were made to purchase arms, and that both people had failed to do so when the arms were actually purchased. "Had Sedgley, therefore, lived up to his promise to notify the Government, it might have been possible for the Government to have nipped this plan in the bud at that time. The fact of the matter is, however, that he failed to do so, and that also led us to believe that he was aware of the fact that these firearms were destined for the Cuban revolution."

Mr. Jacob Paley, of New York City, testified (Feb. 19, 1936) that he occasionally purchased Government supplies and salvage materials. In 1933 he purchased from the Schenectady depot a lot of

286,000 pounds of scrap steel and brass which consisted largely of "mutilated" Marlin machine guns for about \$1,516. The inventory showed that this consisted of 3,334 Marlin machine guns and 500 Hotchkiss machine guns. These were, he stated, unused. Their original cost to the Government was "around \$700", or a total cost to the Government of over \$2,000,000. The cost to him was 12 cents apiece. Of the Marlin machine guns, 2,030 were stored in New York City with Lucke-Kiffe Co. He did not authorize Lucke-Kiffe to quote them for sale, but they did so. They have refused to deliver them to him. One hundred guns were shipped to Sedgley in Philadelphia.

XIV. RECOMMENDATIONS

In its Report on Activities and Sales of Munitions Companies (Rept. No. 944, pt. 3, 74th Cong., 2d sess.) the committee stated:

"The members of the Committee are all agreed that, in view of these findings, it is essential that the worst of these practices be stopped if it is possible to stop them, and that the nature of the foreign practices of American munitions companies and their profits on contracts for the military services of the United States should be strictly limited and controlled.

"The Committee majority (Senators Nye, Clark, Pope, Bone) recommends Government ownership of facilities adequate for the construction of all warships by the United States Navy Department, also all gun forgings, projectiles, and armor plate, and of facilities adequate for the production of powder, rifles, pistols, and machine guns necessary for the United States War Department.

"It does so because it believes that regulation is easily evaded, and cites the Committee's unanimous findings on the profit limitation in the Vinson Act of 1934 incorporated in the Committee's Report on Naval Shipbuilding. It is convinced that a thorough examination of the books of the naval contractors subject to that act will show greatly increased overhead and other methods of increasing apparent costs.

"It does so also because any control over the foreign affairs of the companies, which is essential to the estoppel of present practices, will, in effect, amount to control of management, and cannot be effected successfully under the private ownership of these companies.

"It does so also because of its findings that during the World War the munitions companies insisted throughout on their pound of flesh in the form of high profits for their production, and did not let their patriotism stand in the way of their 'duty as trustees' to the stockholders.

"In making its recommendations for Government ownership of certain facilities the Committee majority believes that the War and Navy Departments can produce from their own ranks or employ sufficiently able technicians to operate these plants successfully.

"The Committee majority has noted the pressure on the service departments by the munitions and shipbuilding companies for orders and for help in foreign sales and for help in opposition to embargoes and other disarmament measures, and wishes the Army and Navy to be the masters in their own house, and free from outside pressure.

"The Committee majority believes that the manufacture of the material which it is proposed to have the Government manufacture (powder, projectiles, guns, armor plate, gun forgings, and naval vessels) can be carried on and improved on satisfactorily by the staff of the War and Navy Departments, and that the mobilization of the war-munitions industries in wartime for the wartime production

of some or all of the necessary munitions can be carried out in the same way it is now proposed to do. Salaries for technicians should be made comparable with those in private industry. The Government plants should, in the event that new construction instead of purchase is decided upon, be located as close as possible to the present plants so that there may be a minimum of labor dislocation.

"The Committee majority believes the national defense will be greatly aided by the estoppel of the practice of selling American military inventions abroad, which can be accomplished effectively only in this manner.

"The Committee majority points out that the Government services already manufacture half of the naval vessels, their guns, their rifles, their ammunition, and, in the case of the Navy, their powder, and sees no change in principle to extend the present practice in regard to this material to the same or other material. If the Navy can manufacture powder, the Army can do so as well. The Army has made important contributions to machine-gun development and has at present no benefit of competition when it wishes to purchase machine guns. The Army has shown its ability in the development of the 75 field piece. The aircraft industry is at present exempted from these recommendations, although it is almost entirely dependent on Government orders or indirect subsidies, because airplane and engine construction are still rapidly developing arts and in that way different from the somewhat more standard articles for which it is proposed to have the Government acquire facilities.

"The Committee also recommends that the War Department be given sufficient appropriations to acquire the jigs, tools, and dies necessary for installation in private plants in time of war for the manufacture of munitions.

"The plan as proposed by the Committee majority looks forward to an adequate munitions plant to supply the peacetime needs only of the Army and Navy, and procurement by the military services of sufficient tools and equipment so that installation of them in private plants may be undertaken in time of war. This will be done under regulation or even in the absence of regulation upon the outbreak of war. It does not plan large munitions plants. In a later report on Government costs, figures will be presented to show that the Navy could enlarge its facilities to produce all the ships necessary for a considerable naval race at a cost for those facilities of as little as \$23,600,000, including sufficient machinery to modernize the yards and produce ships even more efficiently than at present.

"The Committee majority does not see any danger to overproduction in Government plans since the manufacture of the Army's guns and rifles and the Navy's powder and ships have not, according to any service officials, resulted in overloading the services with matériel.

"At present the munitions companies charge into their costs to the Government all the overhead of idle plant, with resultant high costs to the Government. Carnegie Steel Co. made profits, according to its own figures, of 57.9, 43.4, and 42.7 percent on three typical Navy contracts between 1930 and 1934. Yet on the contract on which 57.9 percent profit was made, Bethlehem Steel Co. had bid \$130 a ton above Carnegie and Midvale had bid \$110 a ton above Carnegie. It was admitted by the steel companies that their prices included overhead for idle time. (Compare Report on Government costs.)

MUNITIONS INDUSTRY

The Committee majority believes that the idle plant should be brought into use and the own overhead can be cut down by its use.

"The Committee majority recommends strict control to profits and foreign and domestic activities for those industry not included in Government ownership.

"The Committee minority (Senators George, Va Barbour), supporting all other findings of the committee the complete nationalization of certain defense commodities it doubts the advantage from the standpoint of (1) its disarmament, (2) its effect upon essential national defense, its effect upon Government costs. The Committee minority believes that if large Government plants are erected to provide these commodities there will be inevitable local, political pressure to maintain these plants at full capacity production regardless of actual defense needs, and the result will be to encourage armament rather than disarmament. The Committee minority believes that if all production be thus concentrated in Government plants, furthermore, there will be no adequate corollary reliance, through private manufacture, in the event of a war emergency unless the nationalized facilities are maintained at a needlessly extravagant and dangerous rate during peacetime. The Committee minority believes, on the other hand, that unless these facilities are kept on a full-time production basis during peace years the unit cost of production will increase to a point which will create higher costs to the Government than would be available through normal, private purchase. This could be another impulse to armament rather than disarmament through anxiety to maintain maximum arms production in order to maintain minimum costs. In other words, the Committee minority believes that the public welfare, from the standpoint of peace, defense, and economy, can be better served by rigid and conclusive munitions control than by nationalization, except in a few isolated instances."



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