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Internal Revenue Bulletin

Cumulative Bulletin 1953–2

JULY–DECEMBER 1953

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INTERNAL REVENUE BULLETIN

CUMULATIVE BULLETIN 1953-2

July–December 1953



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INTRODUCTION

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for the announcement of official Internal Revenue rulings, and for the publication of Treasury Decisions, Executive orders, legislation, and court decisions pertaining to Internal Revenue matters.

It is the policy of the Service to publish in the Bulletin all substantive and procedural rulings of importance or general interest, the publication of which is considered necessary to promote a uniform application of the laws administered by the Service. It is also the policy to publish all rulings which revoke, modify, amend, or affect any published ruling. Rulings relating solely to matters of internal management are not published. The rulings are prepared in the various divisions of the National Office, including the Office of the Chief Counsel for the Internal Revenue Service. All published rulings have received the consideration and approval of the Chief Counsel.

Revenue Rulings reported in the Bulletin do not have the force and effect of Treasury Department Regulations (including Treasury Decisions), but are published to provide precedents to be used in the disposition of other cases, and may be cited and relied upon for this purpose. However, since each published ruling represents the conclusion of the Service as to the application of the law to the entire state of facts involved, Revenue officers and others concerned are cautioned against reaching the same conclusion in other cases unless the facts and circumstances are substantially the same. In applying rulings published in the Bulletin, personnel of the Service will, of course, consider the effect of subsequent legislation, regulations, court decisions, and rulings.

Each ruling is designated as a "Revenue Ruling" and should be cited by reference to the Bulletin and page where reported. Thus, Revenue Ruling No. 119 should be cited as "Rev. Rul. 119, C. B. 1953–2, 95." Rulings are keyed to the applicable sections of the Internal Revenue Code and regulations.

Internal Revenue Cumulative Bulletin 1953–2, contains all rulings, decisions, and legislation pertaining to Internal Revenue matters published in the biweekly Internal Revenue Bulletins 14 to 26, inclusive, for the period July 1 to December 31, 1953. It also contains a cumulative list of announcements relating to decisions of The Tax Court of the United States, published in those Bulletins.

This Cumulative Bulletin is printed in three parts. The rulings under the Internal Revenue Code are printed as Part I (A.—Income tax under Regulations 118, B.—Under all other laws and regulations), rulings pertaining to administrative matters are printed as Part II, and miscellaneous matters are printed as Part III.

ABBREVIATIONS

The following abbreviations in current use and formerly used will appear in material published in the Bulletin:

A, B, C, etc.—The names of individuals.
A. T.—Alcohol and tobacco tax ruling.
B. T. A.—Board of Tax Appeals.
C. B.—Cumulative Bulletin.
Ct. D.—Court decision.
D. C.—Treasury Department circular.
E. O.—Executive Order.
E. T.—Estate and gift tax ruling.
Em. T.—Employment tax ruling.
G. C. M.—Chief Counsel's memorandum (formerly General Counsel's memorandum).
I. R. B.—Internal Revenue Bulletin.
I. R. C.—Internal Revenue Code.
IR-Mim.—Published IR-Mimeograph.
I. T.—Income tax ruling.
M, N, X, Y, Z, etc.—The names of corporations, places, or businesses according to context.
M. T.—Miscellaneous tax ruling.
Mim.—Published Mimeograph.
P. L.—Public Law.
Rev. Rul.—Revenue Ruling.
S. T.—Sales tax ruling.
T. C.—The Tax Court of the United States.
T. D.—Treasury Decision.
x and y are used to represent certain numbers, and when used with the word "dollars" represent sums of money.

THE TAX COURT OF THE UNITED STATES

CUMULATIVE LIST OF ANNOUNCEMENTS RELATING TO DECISIONS OF THE TAX COURT OF THE UNITED STATES PUBLISHED IN THE INTERNAL REVENUE BULLETIN FROM JULY 1, 1953, TO DECEMBER 31, 1953, INCLUSIVE

It is the policy of the Internal Revenue Service to announce in the Internal Revenue Bulletin at the earliest practicable date the determination of the Commissioner to acquiesce or not to acquiesce in a decision of the Tax Court of the United States which disallows a deficiency in tax determined by the Commissioner to be due. Notice that the Commissioner has acquiesced or nonacquiesced in a decision of the Tax Court relates only to the issue or issues decided adversely to the Government. Decisions so acquiesced in should be relied upon by officers and employees of the Internal Revenue Service as precedents in the disposition of other cases. (No announcements are made in the Bulletin with respect to memorandum opinions of the Tax Court.)

The Commissioner acquiesces in the following decisions:

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[1] Nonacquiescence published in Cumulative Bulletin 1952-1, page 5, withdrawn.

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[2] Nonacquiescence published in Cumulative Bulletin 1951-2, page 5, withdrawn.

[3] Acquiescence relates only to issues of whether respondent properly reconstructed gross profit for 1949 by use of gross markup method, and whether petitioner is liable for fraud penalty for 1949 under sec. 293(b) of the Internal Revenue Code.

[4] Not applicable to transfers occurring after the enactment of sec. 804 of the Revenue Act of 1932, 47 Stat. 280 (1932).

[5] Acquiescence relates only to whether casualty losses and losses from sale of racehorses are ordinary losses or capital losses.

[6] Acquiescence relates only to whether Gregory Run Coal Co. is entitled to deduction for "overriding royalties," and whether the basis for depreciation of a tipple was its cost or its basis in the hands of the transferor.

[7] Gift tax decision.

[8] Estate tax decision.

[9] Acquiescence relates only to whether certain transfers by decedent, prior to her death, were made in contemplation of death.

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[10] Nonacquiescence published in Cumulative Bulletin 1953-1, page 7, withdrawn.
[11] Estate tax decision.
[12] Nonacquiescence published in Cumulative Bulletin 1949-2, page 4, withdrawn.
[13] Acquiescence relates only to whether petitioner may deduct the fair market value of capital stock distributed to its employees as compensation for services.
[14] Acquiescence relates to all issues except whether certain debts incurred by petitioner in 1943 and 1944 are includible as part of invested capital within the meaning of sec. 719 of the Internal Revenue Code, and whether respondent erred in determining petitioner's inadmissible assets.

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[15] Nonacquiescence published in Cumulative Bulletin 1951-2, page 5, withdrawn.
[16] Estate tax decision.
[17] Acquiescence relates only to whether casualty losses and losses from sale of racehorses are ordinary losses or capital losses.
[18] Not applicable to transfers occurring after the enactment of sec. 804 of the Revenue Act of 1932, 47 Stat. 280 (1932).
[19] Estate tax decision.
[20] Acquiescence relates only to whether Gregory Run Coal Co. is entitled to deduction for "overriding royalties," and whether the basis for depreciation of a tipple was its cost or its basis in the hands of the transferor.

ACQUIESCENCES—Continued

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[21] Nonacquiescence published in Cumulative Bulletin 1948-1, page 4, withdrawn.

The Commissioner does NOT acquiesce in the following decisions:

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Hargis, J. F., estate of	26474	19	842
Hargis, Mary M., estate of	26475	19	842
Hargis, Ruth	31695	19	842
Home Title Guaranty Co	20631	15	637
Hutchinson, Florence E., et al., trustees and transferees of estate of Lillie G. Hutchinson [1] [2]	23856 23857 23858	20	749
Hutchinson, Lillie G., estate of [1] [2]	23856 23857 23858	20	749
L			
Luton, Joe B	32533	18	1153
P			
Pacific Affiliate, Inc.[3]	12836	18	1175
R			
Rivera, Clotilde Santiago, estate of [1]	36335	19	271

[1] Estate tax decision.

[2] Nonacquiescence relates only to whether face amounts of insurance contracts which decedent, during her lifetime, assigned to her sons, are includible in her estate as transfers to take effect at her death.

[3] Nonacquiescence relates to whether certain debts incurred by petitioner in 1943 and 1944 are includible as part of invested capital within the meaning of sec. 719 of the Internal Revenue Code, and whether respondent erred in determining petitioner's inadmissible assets.

PART I.—RULINGS AND DECISIONS

A.—INCOME TAX UNDER REGULATIONS 118

INTERNAL REVENUE CODE

CHAPTER 1.—INCOME TAX

SUBCHAPTER B.—GENERAL PROVISIONS

PART II.—COMPUTATION OF NET INCOME

SECTION 22(a).—GROSS INCOME: GENERAL DEFINITION

REGULATIONS 118, SECTION 39.22(a)-1: What included in gross income. Rev. Rul. 231

INTERNAL REVENUE CODE

Where in accordance with a prearranged plan a taxpayer provides the means for a security dealer to purchase a controlling interest in the stock of a corporation and transfer such interest to the taxpayer, a dividend declared and paid at a time when the dealer is the record owner of the stock is includible in the gross income of the taxpayer.

Advice is requested whether a security dealer who acquires stock of a corporation pursuant to an agreement to sell such stock to a third party ex-dividend, should include in gross income the dividends which are distributed while he is the record owner of such stock.

A taxpayer interested in obtaining the physical properties of a corporation, but deterred by the large undistributed earned surplus of such corporation, entered into an agreement with a security dealer for the purchase of the stock thereof ex-dividend. Under the terms of the agreement the taxpayer agreed to invest up to a certain amount provided that (1) acquisition of at least 85 percent of the stock could be obtained and (2) the surplus could be reduced prior to acquisition. It was also agreed that the taxpayer would make funds available to the security dealer to buy the stock and that the dealer would declare itself a dividend and transfer the stock to the taxpayer-purchaser at its cost less the dividend received, and plus a fee of $1 per share of stock. Over 90 percent of the outstanding stock of the corporation was thus acquired. While the affairs of the corporation were in the hands of the dealer, new directors were appointed and a large dividend was distributed. The sale price of the stock to the purchaser was reduced by the amount of the dividend received by the dealer.

It is a well established fact that the substance rather than the form of a transaction is to be regarded for Federal income tax purposes and that taxation is more concerned with the actual command over the property taxed than over refinements of ownership. *Charles A. Corliss* v. *Frank K. Bowers*, 281 U. S. 376, Ct. D. 188, C. B. IX-1, 254 (1930). In the instant case, it appears that the purchaser made available the funds with which the stock was acquired; that the broker had no real interest in the dividend but was bound by the terms of the agreement to reduce the sales price of the stock by the amount of such dividend; and that the only benefits that could inure to the broker under the agreement was a fixed commission per share of stock transferred to the purchaser. Accordingly, it is held that the dividend is includible in the gross income of the taxpayer under section 22(a) of the Internal Revenue Code.

REGULATIONS 118, SECTION 39.22(a)-1: What included in gross income. (Also Section 39.22(a)-20; Section 115(c), Section 39.115(c)-1.) — Rev. Rul. 255

INTERNAL REVENUE CODE

Commissions payable to a corporation in liquidation constitute taxable income to such corporation where, prior to the date of filing the certificate of dissolution and prior to the date on which the right to receive the commissions was assigned to its sole stockholder, the corporation had performed all of the services required to earn the commissions.

Advice is requested whether commissions payable to a corporation in liquidation constitute taxable income to such corporation where prior to the date of filing the certificate of dissolution and prior to the date on which the right to receive the commissions was assigned to its sole stockholder, the corporation had performed all the services required to earn the commissions.

The taxpayer corporation was engaged in business as a commission broker. Under established procedure, the taxpayer secured orders from customers in its territory. These orders were then communicated to the seller for its approval as to terms of payment and delivery. Such approval was usually prompt and preceded the formal execution of the order between the customer and the taxpayer. After an order was executed and submitted to the seller the taxpayer had no further duties to perform in earning its commissions from the seller. The acceptance of an order by the seller completed the corporation's services. The actual payment of the commissions by the seller usually followed soon after the goods were shipped by the seller. It had been the consistent practice of the taxpayer to accrue as income from commissions at the close of each year, the commissions due it on goods shipped by the sellers within the year, payment for which had not been received within the year.

The corporation, which reported its income on the accrual basis, made a distribution of certain of its assets, including accounts receivable, pursuant to a stockholder's resolution to liquidate the corporation and distribute its assets to its sole stockholder. At the time of the distribution there were outstanding various unfilled orders, executed

by the corporation and certain customers which had been approved and accepted by the seller but with respect to which the goods involved had not been shipped. The right to receive the commissions on these orders was assigned to the sole stockholder as part of the distribution in the liquidation of the corporation under section 115(c) of the Internal Revenue Code and the sole stockholder treated the proceeds of the liquidation to the extent that they exceeded the basis of his stock as capital gain. No contention was made that the right to collect these commissions was worth less than full value. It is contended, however, that, since these commissions receivable were assigned to the sole stockholder before the goods were shipped by the seller, they were not accrued prior to the assignment in liquidation and therefore did not constitute corporate income and were not taxable as such.

Notwithstanding the provisions of section 39.22(a)-20 of Regulations 118, that a corporation realizes no gain or loss from the mere distribution of its assets in kind in partial or complete liquidation, a corporation is taxable on income earned up to the time of liquidation although such income has not been received. (See *Jud Plumbing and Heating, Inc., et al.* v. *Commissioner*, 5 T. C. 127, affirmed, 153 Fed. (2d) 681; *Standard Paving Co., et al.* v. *Commissioner*, 13 T. C. 425; *Floyd et al.* v. *Scofield*, 193 Fed. (2d) 594.)

In discussing this issue, the United States Court of Appeals for the Fifth Circuit in the case of Jud Plumbing and Heating, Inc., *supra*, used the following language:

> A corporation being a separate legal entity, its net earnings, whether ascertained or not, belong to it, and the tax upon unexempt income in each taxable year is chargeable to it, * * * and this liability cannot be discharged by the simple expedient of dissolution and turning over of all its assets, including current and unreported income, to its sole stockholder, even though such corporation receives no money consideration for the transfer of such income. It is the actuality of income rather than its disposition that is important in determining the tax consequence.

In *Morris Cohen* v. *Commissioner*, 15 T. C. 261, acquiescence, C. B. 1951-1, 1, it was held that compensation derived from past personal services is taxable to the one who performed the services whether or not he actually receives the compensation or transfers the right to receive it before it is paid. In the case of *Helvering* v. *Paul R. G. Horst*, 311 U. S. 112, Ct. D. 1472, C. B. 1940-2, 206, the Supreme Court of the United States said "But the rule that income is not taxable until realized has never been taken to mean that the taxpayer, even on a cash receipts basis, who has fully enjoyed the benefit of the economic gain represented by his right to receive income, can escape taxation because he has not himself received payment of it from his obligor."

Since the acceptance by the seller completed the corporation's services in obtaining the orders, the commissions due the taxpayer from the seller had been earned by the corporation prior to dissolution. The right to receive these commissions from the seller had been determined and this income represented compensation for services actually rendered by the corporation. It is immaterial that the receipt of the commissions had to await the shipment of the goods. The assignment to its sole stockholder of the right to receive this earned income was ineffectual to relieve the corporation from the tax thereon. The transfer of assets in a corporate liquidation cannot divert taxability of income already earned any more than does an assignment of such

income. *United States* v. *Lynch*, 192 F. (2d) 718, certiorari denied, 343 U. S. 934.

In view of the foregoing, it is held that commissions payable to a corporation in liquidation constitute taxable income to such corporation where, prior to the date of filing the certificate of dissolution and prior to the date on which the right to receive the commissions was assigned to its sole stockholder, the corporation had performed all of the services required to earn the commissions.

REGULATIONS 118, SECTION 39.22(a)–5: Gross income from business. (Also Section 117(k), Section 39.117(k)–1.) Rev. Rul. 217

INTERNAL REVENUE CODE

Trees marketed as Christmas trees do not constitute "timber" within the meaning of section 117(k) of the Internal Revenue Code, and an election may not be made to treat the cutting of such trees as a sale or exchange of timber in which any gain realized may be treated as long-term capital gain. The proceeds from the sale of Christmas trees constitute ordinary income.

SECTION 22(b).—GROSS INCOME: EXCLUSIONS FROM GROSS INCOME

REGULATIONS 118, SECTION 39.22(b)(2)–2: Annuities.

INTERNAL REVENUE CODE

Payments under an annuity contract received as consideration for the transfer of real estate. (See Rev. Rul. 239, p. 53.)

REGULATIONS 118, SECTION 39.22(b)(4)–4: Interest upon United States obligations. Rev. Rul. 268

INTERNAL REVENUE CODE

Interest received by United States citizens on obligations issued by the General Supplies Administration, a division of the Puerto Rican Department of Agriculture and Commerce, is exempt from Federal income tax.

Advice is requested whether interest received by citizens of the United States on obligations issued by the General Supplies Administration of Puerto Rico, a division of the Puerto Rican Department of Agriculture and Commerce, is exempt from Federal income tax under section 22(b)(4) of the Internal Revenue Code.

The General Supplies Administration of Puerto Rico was created as an agency of the executive branch of the Government of Puerto Rico by the Insular Supplies Act of 1942 (Act No. 228 of the Legislature of Puerto Rico). The act entrusted to the Administration various economic stabilization functions including: (*a*) the provision of

an adequate supply of staple commodities, (*b*) price controls and rationing, and (*c*) various related and supplementary functions.

In 1950 the functions of the Administration were transferred to the Puerto Rican Department of Agriculture and Commerce in accordance with a reorganization plan promulgated by the Governor of Puerto Rico pursuant to the Reorganization Act of 1949. The Administration ceased to exist as a separate agency and became a division of the Department of Agriculture and Commerce, under the direction of the Commissioner of Agriculture and Commerce.

Section 22(b) of the Internal Revenue Code provides in part:

EXCLUSIONS FROM GROSS INCOME.—The following items shall not be included in gross income and shall be exempt from taxation under this chapter:

* * * * * * *

(4) TAX-FREE INTEREST.—Interest upon * * * (C) the obligations of the United States or its possessions. * * *

For the purposes of section 22(b)(4) of the Code, Puerto Rico is a "possession" of the United States. Section 4(a) of the Public Debt Act of 1941, C. B. 1941–1, 546, which terminated the exemption feature of obligations issued by the United States and agencies and instrumentalities thereof, provided that for the purposes of such termination:

* * * a possession of the United States * * * and any political subdivision thereof, and any agency or instrumentality of any one or more of the foregoing, shall not be considered as an agency or instrumentality of the United States.

The exemption provision of section 22(b)(4)(C) of the Code has remained in effect with respect to obligations of possessions of the United States. See section 39.22(b)(4)–4(b) of Regulations 118.

In view of the foregoing, it is held that interest received by United States citizens from obligations issued by the General Supplies Administration, a division of the Puerto Rican Department of Agriculture and Commerce, is exempt from Federal income tax under section 22(b)(4) of the Code.

Rev. Rul. 256

INTERNAL REVENUE CODE

The disability retirement pay of a member of the uniformed services who is retired under section 402 of the Career Compensation Act of 1949 (63 Stat. 802) and who is also entitled to the benefits of the Pay Readjustment Act of 1942 (56 Stat. 359) because of service in the military forces of the United States prior to November 12, 1918, is excludable from the gross income of the recipient under section 22(b)(5) of the Internal Revenue Code only to the extent of the pay he would have received if such pay were computed on the basis of percentage of disability. The amount received in excess thereof is includible in gross income and is subject to withholding of income tax at the source under section 1622 of the Code.

Advice is requested relative to the status for Federal income tax purposes of disability retirement pay received by members of the uniformed services who elect under section 402 of the Career Compensation Act of 1949 (63 Stat. 802) to have their retirement pay com-

puted on the basis of percentage of disability and who are also entitled to the benefits of the Pay Readjustment Act of 1942 (56 Stat. 359) because of service in the military forces of the United States prior to November 12, 1918.

In the case under consideration an officer of the United States Navy was transferred to the Naval Reserve Retired List in September 1951. He received gross monthly retirement pay of $2x$ dollars which, since it was computed on the basis of years of service, was taxable. In February 1953 the records were corrected to show that as of his retirement date he was placed on the temporary disability retired list with a disability rating of 30 percent in accordance with the Career Compensation Act, *supra*. Pursuant to the provisions of section 402 of that act, he elected to receive retirement pay of $3x$ dollars per month based on percentage of disability rather than $2x$ dollars per month based on years of service. In May 1953, since he had served in the Navy prior to November 12, 1918, his account was further adjusted, pursuant to the Pay Readjustment Act of 1942, *supra*, retroactive to the retirement date, to a gross monthly rate of $5x$ dollars, which is 75 percent of the active duty pay of an officer of his rank and years of service.

Section 22(b)(5) of the Internal Revenue Code provides in part as follows:

> (b) EXCLUSIONS FROM GROSS INCOME.—The following items shall not be included in gross income and shall be exempt from taxation under this chapter [ch. 1 of the Code]:
>
> * * * * * * *
>
> (5) COMPENSATION FOR INJURIES OR SICKNESS.— * * * amounts received as a pension, annuity, or similar allowance for personal injuries or sickness resulting from active service in the Armed Forces of any country;

Paragraph 4 of section 15 of the Pay Readjustment Act of 1942, *supra*, provides as follows:

> The retired pay of any officer of any of the services mentioned in the title of this Act who served in any capacity as a member of the military or naval forces of the United States prior to November 12, 1918, hereafter retired under any provision of law, shall, unless such officer is entitled to retired pay of a higher grade, be 75 per centum of his active duty pay at the time of his retirement.

Section 402(h) of the Career Compensation Act of 1949, *supra*, provides as follows:

> That part of the disability retirement pay computed on the basis of years of active service which is in excess of the disability retirement pay that a member would receive if such disability pay were computed on the basis of percentage of disability shall not be deemed to be a pension, annuity, or similar allowance for personal injuries or sickness resulting from active service in the armed service in the Armed Forces of any country within the meaning of section 22(b)(5) of the Internal Revenue Code, as amended.

In 31 Comp. Gen. 28 and 31 Comp. Gen. 213, the Comptroller General held that both regular and reserve members of the uniformed forces placed on the temporary or permanent disability retired list on and after October 1, 1949, in conformity with the provisions of section 402 of the Career Compensation Act of 1949 are entitled to the benefits of paragraph 4 of section 15 of the Pay Readjustment Act of 1942 so as to have their retired pay computed at the rate of three-fourths of the active duty pay of the grade in which they were serving at the time of retirement.

Section 402(h) of the Career Compensation Act, *supra*, prescribes what portion of the payments under this act will be exempt from Federal income tax under section 22(b)(5) of the Code. Under section 402(h) the exemption is limited to that portion of the disability retirement pay that would have been received if such pay were computed on the basis of percentage of disability. Thus the tax exemption benefit of section 22(b)(5) of the Code does not apply to that part of the disability retirement pay that a member receives which is in excess of the pay that he would have received if it had been computed on the basis of percentage of disability, whether such excess payment is due to the computation of retirement pay on the basis of years of active service, or by reason of some other provision of law, such as, in the instant case, paragraph 4 of section 15 of the Pay Readjustment Act of 1942.

In view of the foregoing, it is held that the retirement pay of members of the uniformed services entitled to the benefits of the Pay Readjustment Act of 1942, to the extent it exceeds the retirement pay computed on a percentage of disability basis under the provisions of the Career Compensation Act of 1949, constitutes taxable income for Federal income tax purposes, is includible in the gross income of the recipient in the year of receipt, and is subject to withholding of income tax at the source under section 1622 of the Code. In the instant case, the difference between $5x$ dollars and $3x$ dollars is not exempt from Federal income tax under section 22(b)(5) of the Internal Revenue Code.

Although this ruling holds certain portions of such retirement pay are taxable and subject to the withholding of income tax at the source under section 1622 of the Code, under the authority of section 3791(b) of the Code, withholding of the tax shall not be required with respect to any such payments made prior to January 1, 1954. However, the recipients are required to report such income in their returns for the year of receipt.

Rev. Rul. 257

INTERNAL REVENUE CODE

Nonoccupational disability benefits paid under article 9 of the New York workmen's compensation law are not excludable from the gross income of the recipients as amounts received "under workmen's compensation acts" within the purview of section 22(b)(5) of the Internal Revenue Code.

Advice is requested whether nonoccupational disability benefits paid under article 9 of the New York workmen's compensation law, generally known as the disability benefits law, are excludable from the gross income of the recipients as amounts received "under workmen's compensation acts" within the purview of section 22(b)(5) of the Internal Revenue Code.

Section 22(b)(5) of the Code provides in part:

(b) EXCLUSIONS FROM GROSS INCOME.—The following items shall not be included in gross income and shall be exempt from taxation under this chapter [ch. 1 of the Code]:

* * * * * * *

(5) COMPENSATION FOR INJURIES OR SICKNESS.—Except in the case of amounts attributable to (and not in excess of) deductions allowed under section 23(x) in any prior taxable year, amounts received, * * * under workmen's compensation acts, as compensation for personal injuries or sickness * * *.

Workmen's compensation acts have not been understood to encompass anything other than occupational disability or injuries. The fact that New York for its own reasons placed its nonoccupational benefits provisions within the confines of its workmen's compensation law is not determinative of what is or is not workmen's compensation for purposes of section 22(b)(5) of the Code. If such nonoccupational disability benefits were regarded as workmen's compensation within the ambit of section 22(b)(5) of the Code, those States which require the payment of similar benefits but which do not identify their statutes as workmen's compensation acts would be treated differently than New York, although there is no factual difference between the statutes or the benefits.

In view of the foregoing, it is held that nonoccupational disability benefits paid pursuant to article 9 of the New York workmen's compensation law are not excludable from the gross income of the recipients as amounts received "under workmen's compensation acts" within the purview of section 22(b)(5) of the Code. *Cf.* Rev. Rul. 208, page 102, this Bulletin, and Rev. Rul. 209, page 104, this Bulletin.

Rev. Rul. 269

INTERNAL REVENUE CODE

Permanent disability retirement benefits received from the Teachers' Retirement System of the State of Illinois constitute accelerated retirement pay for length of service and are not excludable from gross income as accident or health insurance under section 22(b)(5) of the Internal Revenue Code. That part of the System which provides for temporary disability benefits constitutes a plan of insurance within the meaning of section 22(b)(5) of the Code, and payments received thereunder are excludable from gross income. The exclusions from gross income under section 22(b)(5) is available even though the system is a trust qualified under section 165(a).

Advice is requested whether permanent disability retirement and temporary disability benefits received under the Teachers' Retirement System of the State of Illinois are excludable from gross income under section 22(b)(5) of the Internal Revenue Code.

The State of Illinois has created by statute and placed under the administration of a board of trustees a teachers' retirement system which provides member public school teachers, who meet specified requirements, with death, age retirement, permanent disability, and temporary disability benefits in specified amounts and for specified periods of time. Illinois Revised Statutes (1951), chapter 122, article 25 (Teachers' Retirement System).

The statute provides that upon the application of a member or of his employer any member who has had 10 or more years of creditable

service and who is not entitled to an age retirement allowance may be retired for physical disability and receive a permanent disability retirement benefit. (Sec. 25–54.) Under the provisions of the statute the permanent disability benefit is closely attuned to age retirement. Such benefit is primarily based on the actuarial equivalent of the accumulated contributions of the retiring member at the time of his or her retirement plus a stated percentage of the annuity the member would have been provided at the minimum age at which the member would have been eligible for age retirement. (Sec. 29–55.)

The statute provides further that a member public school teacher who is not entitled to either an age retirement or to a disability retirement benefit, who has been engaged in teaching or in other specified occupations for at least 5 years, and who has been a contributor to the system for at least 1 year after July 1, 1947, may, upon application, be granted a temporary disability benefit. The amount of the temporary disability benefit is equal to 40 percent of the member's most recent salary at the time disability occurred, payable in monthly installments at an annual rate of 40 percent of the most recent annual contract salary of the member at the date of disability. In addition to the temporary disability benefit, disabled members receive credit in lieu of normal contributions which they would otherwise have made. (Sec. 25–56.1.)

Member teachers help to finance the system by contributing a percentage of their salaries. The State of Illinois annually contributes enough money to make the estimated credits to the various funds in the system equal the estimated charges. The funds of the system are separate from normal State funds. The payment of the required State contributions, the creation and maintenance of proper balances in the various funds, the crediting of regular interest, and the payment of all pensions, annuities, retirement allowances, death benefits, refunds and other benefits granted under the provisions of, or assumed by, this retirement system in connection with the administration and operation thereof are also made obligations of Illinois by the statute. If a member ceases to be a teacher for any cause other than death, he is entitled to a refund of his contribution to the system, less any refunds previously made, without interest.

Section 22(b)(5) of the Internal Revenue Code provides in part for the exclusion from gross income of "amounts received, through accident or health insurance or under workmen's compensation acts, as compensation for personal injury or sickness, plus the amount of any damages received whether by suit or agreement on account of such injury or sickness."

Retirement pay for length of service or age is not excludable from gross income under section 22(b)(5) of the Code. (See I. T. 3428, C. B. 1940–2, 60.) In the system under consideration, there is a close relationship between the permanent disability retirement and the age retirement benefits. The amount of the permanent disability benefit is closely attuned to that for age retirement. Only those members who are ineligible for normal age retirement can apply for the permanent disability retirement benefit. And, as a general rule, a member must have at least 10 years of creditable service to receive the

permanent disability benefit. It is accordingly held that the permanent disability retirement provided by the Teachers' Retirement System of the State of Illinois is an accelerated retirement provision and is not exempt from Federal income tax as health or accident insurance under section 22(b)(5) of the Code.

With respect to that part of the system which provides for the payment of temporary disability benefits, it is to be noted that the mere existence of a compulsory benefits statute does not, in itself, transform its benefits into insurance for purposes of section 22(b)(5) of the Code. (See I. T. 4107, C. B. 1952–2, 73.) However, the temporary disability benefits part of the system has other features that combine to make it a plan of insurance. A genuinely independent fund administered by a board of trustees separate from the regular governmental establishment of Illinois pays the benefits. The monies necessary to provide the benefits are derived from member teachers as well as from the State. Member teachers possess fixed rights against the system and the State. Eligibility for benefits does not depend on age or a long period of service but on a relatively short period of service and disability. And the benefits, which equal predetermined amounts are based not on employee or employer contributions, like the permanent disability retirement pensions, but on a percentage of salary. It is accordingly held that the part of the Teachers' Retirement System which provides for temporary disability benefits constitutes a plan of insurance within the meaning of section 22(b)(5) of the Code, and payments received thereunder are excludable from the gross income of the recipients. *Cf.* Rev. Rul. 209, page 104, this Bulletin.

The system is a trust qualified under section 165(a) of the Code despite the fact that the temporary disability benefits are excludable from gross income under section 22(b)(5). A benefit excludable under section 22(b)(5) may be provided by a trust without automatically preventing its qualification under section 165(a). Although a plan otherwise qualifying under section 165(a) may devote so great a part of its funds to the provision of sickness or injury benefits as to prevent its qualification under section 165(a), the temporary disability benefits in the instant case are not that large in relation to the other benefits provided. See Regulations 118, section 39.23(p)-1. Therefore, the exclusion of section 22(b)(5) supersedes the taxing provision of 165(b) so far as the temporary disability benefits are concerned. However, the permanent disability retirement benefits will be taxed as prescribed by section 165(b) of the Code, which requires that the pension be taxed as if it were an annuity under section 22(b)(2) of the Code. Contributions by members to the system will be treated under section 22(b)(2) as the cost of the annuity. Since credits towards age and disability retirement pensions made on behalf of an employee by the system during a period of temporary disability are not taxable as income, they will not constitute a part of the cost of the annuity.

SECTION 22(d).—GROSS INCOME: [INVENTORIES—ELECTIVE METHOD]

REGULATIONS 118, SECTION 39.22(d)–1: Last-in first-out inventories. Rev. Rul. 238

INTERNAL REVENUE CODE

Price indexes for July 1953 published by the Bureau of Labor Statistics on September 2, 1953, for use by department stores employing the retail inventory and elective inventory methods.

The following price indexes for July 1953 published by the Bureau of Labor Statistics on September 2, 1953, for use by department stores employing the retail inventory and elective inventory methods, are accepted by the Internal Revenue Service pursuant to Treasury Decision 5605, C. B. 1948–1, 16, and Mimeograph 6244, C. B. 1948–1, 21, for appropriate application to inventories for taxable years of 12 months ended on June 30, 1953, and July 31, 1953.

Bureau of Labor Statistics, department store inventory price indexes, by department groups

[January 1941=100]

Group	July 1952	July 1953	Percent change from July 1952 to July 1953
I. Piece goods, domestics and draperies	204.2	203.3	−0.4
II. Shoes	210.8	212.1	+0.6
III. Ladies' underwear	174.7	172.7	−1.1
IV. Ladies' outerwear and girls' wear	179.5	179.2	−0.2
V. Men's and boys' wear	203.4	201.6	−0.9
VI. Furniture and bedding	205.3	210.4	+2.5
VII. Homefurnishings	190.0	195.8	+3.1
VIII. Major appliances and electrical goods	159.0	157.8	−0.8
IX. Notions and toilet articles	160.4	163.8	+2.1
X. Ladies' accessories	170.6	170.6	0
Total, Groups I, II, III, IV, V, IX, and X	189.5	189.3	−0.1
Total, Groups VI, VII, and VIII	186.6	190.6	+2.1
Store total	188.5	189.6	+0.6

REGULATIONS 118, SECTION 39.22(d)–7: Involuntary liquidation and replacement.

INTERNAL REVENUE CODE

Interim allowance in respect of overpayment of tax. (See Rev. Rul. 241, p. 85.)

SECTION 23(a).—DEDUCTIONS FROM GROSS INCOME: EXPENSES

REGULATIONS 118, SECTION 39.23(a)–1: Business expenses. Rev. Rul. 168

INTERNAL REVENUE CODE

A penalty payment made by a taxpayer to his mortgagee to obtain a release from the mortgage on property used in his trade or business,

in order to secure a new loan from another source, is deductible by the taxpayer in the year of payment or accrual, depending on the taxpayer's method of reporting income.

REGULATIONS 118, SECTION 39.23(a)-15: Nontrade or nonbusiness expenses.

INTERNAL REVENUE CODE

Election with respect to the treatment of certain administrative expenses of an estate for Federal income tax purposes. (See Rev. Rul. 240, p. 79.)

SECTION 23(e).—DEDUCTIONS FROM GROSS INCOME: LOSSES BY INDIVIDUALS

REGULATIONS 118, SECTION 39.23(e)-1: Losses by individuals. Rev. Rul. 286

INTERNAL REVENUE CODE

Only that part of a loss resulting from the sale of property used for both personal and income-producing purposes that can be allocated to the income-producing portion of the property constitutes a loss within the meaning of section 23(e) of the Internal Revenue Code. In determining the gain or loss on the sale, there must be an actual allocation of the amounts which represent cost, selling price, depreciation allowed or allowable, and selling expenses to the respective portions of property in the same manner as if there were two separate transactions. The example set forth below, assuming that 80 percent of the property or 80 percent of its use is allocable to income-producing purposes, will best serve to illustrate the method of computation:

		Income-producing	*Personal*
Selling price of property		$36,000	$9,000
Cost of property	$48,000		12,000
Less adjustment for depreciation	12,000		
Adjusted basis		36,000	
Gain or (loss)		—0—	(3,000)
Less expense of sale		2,400	600
Net Gain or (loss)		(2,400)	(3,600)

As a result of the foregoing allocation, the net loss of $2,400 applicable to the income-producing portion of the property would be deductible from the gross income of the individual, subject to the provisions of section 117 of the Internal Revenue Code, and the net loss of $3,600 applicable to personal use, would not be allowable as a deduction under section 23(e) of the Code. See section 39.23(e)(1) of Regulations 118.

SECTION 23(k).—DEDUCTIONS FROM GROSS INCOME: BAD DEBTS

REGULATIONS 118, SECTION 39.23(k)-5: Reserve for bad debts. — Rev. Rul. 211

INTERNAL REVENUE CODE

An election of either the reserve for bad debts method or the specific chargeoff method of treating bad debt losses sustained by a mutual savings bank may be made in any taxable year beginning after December 31, 1951, but not later than the first taxable year in which the bank sustained actual bad debts. This is true irrespective of whether a deduction for such bad debts was taken in a Federal income tax return. See Section 39.23(k)-1 of Regulations 118 with respect to permission for changing the method of treating bad debts.

SECTION 23(m).—DEDUCTIONS FROM GROSS INCOME: DEPLETION

REGULATIONS 118, SECTION 39.23(m)-1: Depletion of mines, oil and gas wells, other natural deposits, and timber; depreciation of improvements.

INTERNAL REVENUE CODE

Processes included in mining with respect to calcium carbonates and shale mined for use in the manufacture of cement. (See Rev. Rul. 290, p. 41.)

SECTION 23(q).—DEDUCTIONS FROM GROSS INCOME: CHARITABLE AND OTHER CONTRIBUTIONS BY CORPORATIONS

REGULATIONS 118, SECTION 39.23(q)-1: Contributions or gifts by corporations. — Rev. Rul. 287

INTERNAL REVENUE CODE

> Where a corporation's net income for a taxable year has been reduced due to a net operating loss carryback, its charitable deductions under section 23(q) of the Internal Revenue Code must be revised to an amount which does not exceed 5 percent of the taxpayer's net income after application of the carryback.

Advice is requested as to the deduction for contributions allowable for Federal income tax purposes under section 23(q) of the Internal Revenue Code, where the net income of a corporation for the taxable year has been subsequently reduced due to a net operating loss carryback under the provisions of section 122 of the Code.

Section 23(q) of the Code provides that in computing net income, in the case of a corporation, there shall be allowed as deductions contributions or gifts payment of which is made within the taxable year to or for the use of the types of organizations described therein, limited to an amount which does not exceed 5 percent of the tax-

payer's net income as computed without the benefit of the deduction for contributions.

Section 23(s) of the Code also provides that in computing net income there shall be allowed as deductions for any taxable year beginning after December 31, 1939, the net operating loss deduction under section 122 of the Code. Under section 122 of the Code the benefit of a net operating loss is granted through the medium of a carryback or a carryover to other taxable years, in a specified sequence.

Since the percentage limitation for contribution deductions is, in the case of a corporation, based on net income and the net operating loss deduction is one of the deductions to be taken in arriving at net income, it follows that in computing the income for a year to which a net operating loss deduction is applicable, the charitable contribution deduction must be revised to meet the percentage limitation of section 23(q) of the Code after the application of the net operating loss deduction. This conclusion is in accord with the principles set forth in I. T. 3733, C. B. 1945, 119, IR-Mim. 43, C. B. 1952-2, 112 and *Edward C. Thayer et ux.* v. *Commissioner*, 12 T. C. 795, acquiescence C. B. 1950-1, 5.

Accordingly, it is held that where a corporation's net income for a taxable year has been reduced due to a net operating loss carryback, its charitable deductions under section 23(q) of the Internal Revenue Code must be revised to an amount which does not exceed 5 percent of the taxpayer's net income after application of the carryback.

SECTION 23(aa).—DEDUCTIONS FROM GROSS INCOME: OPTIONAL STANDARD DEDUCTION

REGULATIONS 118, SECTION 39.23(aa)-1: Standard deduction. — Rev. Rul. 280

INTERNAL REVENUE CODE

Where a taxpayer claims no itemized deductions and makes an election under section 23(aa)(1) of the Internal Revenue Code to take the standard deduction in computing his Federal income tax, and where his adjusted gross income for the taxable year is subsequently reduced by application of a net operating loss carryback, the claimed standard deduction for such year is also subject to revision and should be corrected on the basis of the adjusted gross income after allowance of the net operating loss carryback. (See Rev. Rul. 287, p. 21.)

SECTION 25.—CREDITS OF INDIVIDUAL AGAINST NET INCOME

REGULATIONS 118, SECTION 39.25-2: Credits of individuals for purpose of normal tax and surtax. — Rev. Rul. 220

INTERNAL REVENUE CODE

Where a divorced husband, in violation of a court order, fails to make payments of "child support" for a calendar year, but pays the

arrearage in a subsequent year, the amount thereof does not constitute support of the child furnished by the husband, either for the year in which such payments were in arrears or for the year in which the arrearage was paid, but constitutes a reimbursement to the divorced wife for support of the child furnished by her during the period such payments were in arrears. (See *Thomas Lovett et ux.* v. *Commissioner*, 18 T. C. 477, acquiescence, C. B. 1952-2, 2.)

REGULATIONS 118, SECTION 39.25-2: Credits of individuals for purpose of normal tax and surtax. Rev. Rul. 235

INTERNAL REVENUE CODE

In determining who furnished over half of the support of a "dependent" in a situation where several members of a household contribute to the support of the household, consideration should be given to the amount actually used in supporting the various members of the household. Expenses which are equally applicable to the support of each member of the household should be allocated equally among all such members.

The actual expenses incurred in connection with a house owned by a taxpayer in which lodging is furnished to his parent, and not the fair rental value of such house, should be taken into account in determining whether a taxpayer furnished over half of the parent's support.

Advice is requested relative to the manner of determining who furnished over half of the support of a "dependent" in a situation where several members of a household contribute to the support of such household. Advice is also requested whether the fair rental value of a house owned by a taxpayer in which lodging is furnished to his parent may be taken into account in determining whether the parent qualifies as a dependent of the taxpayer for Federal income tax purposes.

Section 25(b)(3) of the Internal Revenue Code provides that the term "dependent" means any person within certain specified relationships to the taxpayer (including the father or mother of the taxpayer) over half of whose support, for the calendar year in which the taxable year of the taxpayer begins, was received from the taxpayer. Section 39.25-2(e) of Regulations 118 provides that whether or not over half of a person's support, for the calendar year in which the taxable year of the taxpayer begins, was received from the taxpayer shall be determined by reference to the amount of expense incurred by the taxpayer for such support.

The Revenue Service considers that the term "support" generally includes such items of expenses as the cost of board, lodging, clothing, education, medical and dental care, and other similar expenses. However, in determining the amount of support furnished in the form of lodging to such a closely related person, reference must be made to the actual expense of furnishing the lodging involved and not to the value of the lodging furnished. Accordingly, it is held that the fair rental value of a house owned by a taxpayer in which lodging is furnished to a dependent parent (whether or not the parent lives with the taxpayer) may not be taken into account in determining whether over half of that parent's support was furnished by the taxpayer. The types of expenses which may be included in determining the cost of

furnishing lodging to a dependent are such items as property taxes, mortgage interest, property insurance, and ordinary repairs. Depreciation and expenditures properly chargeable to capital account, including payments on the principal amount of a mortgage, may not be included for the purpose of such determination.

By the same token, where the taxpayer and his dependent parent live in a house owned and furnished by the parent, the fair rental value of the house is not to be taken into account in determining whether the taxpayer has furnished more than half of the parent's support for purposes of the credit for a dependent under section 25(b) of the Code.

These cases are to be distinguished from those where the taxpayer (or the dependent, as the case may be) furnishes lodging in a *rented* home. In such a situation, since it is an item of actual expense, the rent paid for the living accommodations should be included in determining whether more than half of the dependent's support was furnished by the taxpayer.

In situations in which a taxpayer and one or more members of a household are contributing toward the support of the household jointly, consideration should be given to the amount actually used in supporting the various members of the household in determining which member of the household is entitled to the credit for the dependents involved. In the absence of an actual record of the expenses relating to the support of each member of the household, a pro rata portion of the aggregate of such expenses may be allocated to each member. Once the cost of supporting each member of the household is determined, the amount used by the taxpayer for his own support should be subtracted from the amount which he contributed. The remainder will be the amount which the taxpayer actually contributed toward the support of other members of the household, and unless he is able to show otherwise, it will be presumed that such remainder was used equally for the support and maintenance of each of the other members. However, if the taxpayer can show that the amount contributed by him which is not required for his own support is for the support of a particular member of a family group, his right to an exemption will be determined accordingly.

The following examples will serve to illustrate the application of the foregoing:

(1) A taxpayer and his parent live in a house owned by the taxpayer. The expenses of the taxpayer for such items as property tax, mortgage interest, insurance, etc., amount to $400 for the year. The parent receives a nontaxable pension of $40 per month. The annual food bill amounts to $1,200 per year toward the purchase of which the parent contributes $480. Miscellaneous household expenses paid by the taxpayer amount to $400. The total cost of maintaining the household including food, taxes, interest, etc., is $2,000, of which $480 is furnished by the parent and the remaining $1,520 by the taxpayer. In the absence of specific records showing the actual use of these funds toward the support of the taxpayer and his parent, half of the $2,000 ($1,000) is allocated to the support of each person. Since the taxpayer has contributed $1,520 to the support of the household, $1,000 of which is allocable to support of himself, there is a balance of $520

which he has contributed toward the support of his parent. The support of the parent amounted to $1,000. Since the taxpayer contributed $520 toward the support of the parent, he is entitled to claim the parent as a dependent for Federal income tax purposes.

(2) The taxpayer and his parent live in a house which is owned and furnished by the parent. The parent had taxable income of $400, the entire amount of which was used to pay taxes, interest on mortgage, and insurance on the house. The taxpayer paid all other expenses of maintaining the household, including the cost of food, etc., which totaled $1,300. There were no other support expenses involved. The total cost of maintaining the household was $1,700, half of which ($850) is allocable to the support of each member of the household. Deducting $850 for the support of the taxpayer from the $1,300 paid by him leaves a remainder of $450 contributed by the taxpayer to the support of his parent. Since the $450 contributed by the taxpayer toward the support of his parent is more than half of the $850 required for the parent's support, he is entitled to claim the parent as a dependent.

(3) The taxpayer and his mother and father live in a house owned by the taxpayer's father. The father and mother have no taxable income but have a sizable savings account. The taxpayer contributed $1,400 toward the expenses of the household. The father paid taxes, insurance, and interest on mortgage on the house in the amount of $400. The mother employed a maid and paid her $900 for the year. Assuming that there were no other expenses, the aggregate cost of maintaining the household is $2,000, one-third of which ($900) is allocable to the support of each of the three individuals. The taxpayer and his mother each have contributed $900 toward the support of themselves. The taxpayer has contributed $500 ($1,400−$900) toward the support of the father. Since the taxpayer furnished more than half of the support of his father he is entitled to claim him as a dependent.

(4) A taxpayer and his sister live with their mother in a house owned and furnished by their mother. The mother paid taxes, insurance, etc., on the house in the amount of $400. The taxpayer contributed $1,100 toward food and other household expenses. The sister paid the salary of the maid in the amount of $600 and the expenses of clothing, dental, and medical care required by her mother in the amount of $500. Total cost of maintaining the household was $2,100, of which the taxpayer contributed $1,100, his sister $600, and the mother $400. The $500 for clothing, dental, and medical care for the mother, paid by the sister, is not includible in the cost to be allocated equally among the three individuals, since it constitutes support for the mother only. Of the $2,100 spent, $700 is allocable to the support of the taxpayer, his sister, and the mother. Of the $1,100 contributed by the taxpayer toward the household expenses, $400 ($1,100−$700) constitutes support for other members of the household. The taxpayer's sister contributed only $600 toward household expenses, therefore $100 ($700−$600) of the taxpayer's

contribution constitutes support of his sister and $300 ($700−$400) thereof constitutes support of his mother. The total support of the mother amounts to $1,200 ($700 pro rata portion of the household expenses and $500 clothing, dental, and medical expenses paid by the taxpayer's sister) of which the taxpayer furnished $300, the sister furnished $500, and the mother furnished $400. Since neither the taxpayer nor his sister furnished over half of the support of their mother, neither of them is entitled to claim her as a dependent.

SECTION 26(h).—CREDITS OF CORPORATIONS: CREDIT FOR DIVIDENDS PAID ON CERTAIN PREFERRED STOCK

REGULATIONS 118, SECTION 39.26(h)-1: Credit for dividends paid on preferred stock of public utilities. Rev. Rul. 228

INTERNAL REVENUE CODE

In the case of a public utility company which has nonutility income, no apportionment of the dividends paid credit allowed under section 26(h) of the Internal Revenue Code will be made where the nonutility income is less than 20 percent of total income, irrespective of the method used in determining such total income.

Advice is requested relative to the determination of the credit for dividends paid on preferred stock of public utilities provided under section 26(h) of the Internal Revenue Code in a case where the public utility has income derived from utility and nonutility sources.

Section 26(h)(1) of the Code provides for a credit for dividends paid on certain preferred stock of public utilities. Section 26(h)(2) of the Code defines a "public utility" as a corporation "engaged in the furnishing of telephone service or in the sale of electric energy, gas, or water * * *".

A question arises as to the computation of the dividends paid credit in the case of a corporation which is engaged in one of the four types of businesses enumerated in section 26(h) of the Code and is also engaged in some other business that does not fall within any of the enumerated categories. Since the statute itself is silent with respect to nonutility activities, the position might be taken that section 26(h) of the Code should be interpreted to allow the credit only in cases where the corporation is engaged solely in selling or furnishing the specified services because there is no provision for allowance of the credit to corporations engaged in other than public utility business. However, this position would result in denying the credit where as little as 5 to 10 percent of the total income was from nonutility activities. On the other hand, the position might be taken that the credit should be allowed in full to any corporation although its income from utility sources does not exceed 1 percent of its total income. However, a construction of the statute which would lead to unreasonable and extreme results should be avoided. *American Trucking Association* v. *United States*, (1940) 310 U. S. 534. Accordingly, an apportionment formula which allocates the dividends paid credit upon a basis of utility and nonutility income avoids extreme results and

attains a reasonable and practical interpretation of section 26(h) of the Code.

In view of the foregoing, it is believed appropriate to allow a credit for dividends paid in an amount equal to the ratio which the total income from utility sources bears to total income from all sources. The allocation may be made upon the basis of gross income or gross receipts, whichever method results in the higher credit. Where such an allocation reaches an inequitable result and the books of the company are so kept that the net income can be readily determined (particularly where they are required by governmental bodies for rate making or other purposes), the allocation may be made upon the basis of net income. However, no apportionment of the dividends paid credit allowed under section 26(h) of the Code will be made where the nonutility income is less than 20 percent of the total income, irrespective of the method used in determining such total income. (Compare section 448 of the Code where a regulated public utility is defined for excess-profits tax purposes as a corporation with 80 percent or more of its income derived from certain regulated services.)

PART IV.—ACCOUNTING PERIODS AND METHODS OF ACCOUNTING

SECTION 43.—PERIOD FOR WHICH DEDUCTIONS AND CREDITS TAKEN

REGULATIONS 118, SECTION 39.43–2: When charges deductible. Rev. Rul. 288

(Also Section 131(d), Section 39.131(d)–1.)

INTERNAL REVENUE CODE

Income taxes paid to a foreign country by a domestic corporation, which reports its income from a long-term contract on the completed contract basis for United States income tax purposes and is required to report such income on the percentage of completion basis for foreign income tax purposes, may be taken into account by the corporation for the year in which the contract is completed in determining its United States income tax liability.

Advice is requested relative to the year in which a deduction under section 23(c) or a credit under section 131(a) of the Internal Revenue Code may be taken by a taxpayer for income taxes paid to a foreign country under the facts and circumstances outlined below.

The taxpayer is a corporation organized under the laws of Delaware. Its entire income for the next 3 years will be from the performance of services in a foreign country under a single contract. Such income constitutes income from sources outside of the United States. The taxpayer desires to report the income from the contract on the completed contract basis for United States income tax purposes, but for the purposes of the income taxes of the foreign country income from the contract must be reported and the income tax thereon paid annually, measured by the income attributable to the work performed during such year.

With respect to the treatment of the income tax paid to the foreign country and for purposes of the United States income tax, the cor-

poration has the option of taking a deduction of the tax under section 23(c) of the Code or of claiming a credit against its United States income tax under section 131(b) of the Code. Since the taxpayer intends to report the income from the contract in the year the contract is completed, the question arises whether the income taxes paid to the foreign country on an annual basis may be carried as a deferred item and taken into account in determining its United States income tax liability for the year in which the contract is completed.

Section 43 of the Code provides that deductions and credits shall be taken for the taxable year in which "paid or accrued" or "paid or incurred," depending upon the method of accounting upon the basis of which the net income is computed, unless in order to clearly reflect the income the deductions or credits should be taken as of a different period. Section 39.42-4 of Regulations 118 permit making returns of income on the long-term contract basis on the theory that income can be determined only when the project is completed. Where such method of reporting is adopted, all expenditures properly allocable to the contract are to be deducted from gross income at that time.

Since the income taxes to be paid to the foreign country are properly allocable to the income to be derived from carrying out and completing the long-term contract, such taxes which are paid to the foreign country should be allocated to the contract and treated as a part of the total deferred expenditures to be deducted from the gross income derived from the contract. (*Cf.* I. T. 3434, C. B. 1940-2, 90, and *D. L. Wheelock* v. *Commissioner*, 10 B. T. A. 540.) Accordingly, on its return for the year in which the contract is completed, the corporation may include as a deduction under section 23(c) of the Code the combined amounts of income taxes paid to the foreign country with respect to the income in question.

In keeping with the theory of section 43 of the Code, section 39.131(d)-1 of Regulations 118 provides that if under the provisions of section 39.43-1 of Regulations 118 an amount otherwise constituting gross income for the taxable year from sources without the United States is, owing to monetary, exchange, or other restrictions imposed by a foreign country, not includible in gross income of the taxpayer for such year, the credit for income taxes imposed by such foreign country with respect to such amount shall be taken proportionately in any subsequent taxable year in which such amount or portion thereof is includible in gross income. To the same effect is section 39.43-1 of Regulations 118.

The factual pattern prevailing in the case of using the completed contract method of reporting income derived from foreign sources is similar in all essential respects to that prevailing in the blocked income issue. Thus, in both cases, a taxpayer may be required to account annually and pay a tax to the foreign country on income earned therein. In both cases the effect of the foreign operations is not reflected in gross income for Federal income tax purposes and such operations remain incomplete until the occurrence of that event resulting in the realization of income. Blocked income is considered realized in the year the foreign currency restrictions are lifted, whereas income derived from the performance of a long-term contract, and reported

on the completed contract method, is considered realized in the year such contract is completed.

In order to give full effect to the underlying principle of the foreign tax credit, namely, that a domestic taxpayer is not to be subjected to double taxation on income earned abroad, and in accordance with the concept set forth in section 39.131(d)-1 of Regulations 118, in reporting income on the completed contract basis, the foreign tax credit provisions of section 131(a) of the Code should follow the income into the taxable year in which it is realized, that is, the year in which the contract is completed.

Accordingly, it is held that if the taxpayer elects to take the benefits of section 131(a) of the Code, the amount of income tax paid to the foreign country during each calendar year, measured by the work performed during each such calendar year, may be claimed as a credit against its United States income tax, to the extent provided by section 131(b) of the Code, in the year in which the contract is completed. This ruling does not apply where a corporation elects to report its income from a long-term contract on the percentage of completion method.

SECTION 44.—INSTALLMENT BASIS

REGULATIONS 118, SECTION 39.44-1: Sale of personal property on installment plan. (Also Section 39.44-5.) Rev. Rul. 234

INTERNAL REVENUE CODE

An agreement between the taxpayer and a publisher for the preparation and delivery of a literary composition at a specified future date constitutes an executory contract to sell a manuscript. The sale will occur on the date the manuscript is delivered and assigned to the publisher. Payment for the manuscript will be made over a period of years and such sale will qualify as a casual sale of personalty on the installment basis within the purview of section 44(b) of the Internal Revenue Code.

Advice is requested regarding the Federal income tax consequences of an agreement between a publisher and a taxpayer, who is not an author by profession, for the preparation and delivery of a literary composition by the taxpayer under the conditions described below.

The agreement between the taxpayer-author and the publisher in the instant case provides that the author will complete and deliver within a certain period of time a final manuscript of a literary composition, together with suitable material from which illustrations can be made. Simultaneously with the delivery of such manuscript and materials, the author has agreed to grant and assign to the publisher all rights of every kind in and to the composition, including the right to obtain statutory copyrights thereof and renewals or extensions of such copyrights in the name of the publisher. The agreement indicates the minimum and maximum number of words desired for the composition and the general subject to be covered thereby. The author represents and warrants that he will be the author and sole proprietor of the composition, that the composition will not have been previously published, and that it will not contain libelous or otherwise unlawful material.

The agreement also provides that the price to be paid for the rights in and to the composition is 120x dollars. On the date the manuscript is delivered, the purchaser will pay 20x dollars to the author and deliver to him four noninterest bearing promissory notes of 25x dollars each, maturing in each of 4 succeeding years. The agreement specifically provides that the author shall be an independent contractor and shall not act as the agent of the publisher. It also includes certain elections which permit the publisher to terminate the agreement in the event of a breach of contract by the author or his inability to complete the composition because of death or other disability. The author agreed not to make or permit the publication of any material, which may be considered to be in any material way in competition with his composition, until the expiration of a certain period of time after publication by the publisher.

At the time the contract was entered into, the author received a loan of 10x dollars from the publisher. This loan is to be repaid to the publisher on or before a fixed date which is prior to the date of delivery of the manuscript except that in the event of death or incapacity, repayment will be made only under certain specified conditions relating to the receipt of proceeds by the author or his estate from the subject matter of the literary composition.

The primary question to be determined is whether, under the terms of the agreement between the publisher and the author, the transaction constitutes a casual sale of personal property which may be returned on the installment basis under the provisions of section 44(b) of the Internal Revenue Code.

A literary composition is recognized as property in the Internal Revenue Code. See section 117(a)(1) of the Internal Revenue Code. Such property is considered to be personal property. G. C. M. 236, C. B. VI-2, 27 (1927); I. T. 2735, C. B. XII-2, 131 (1933).

Under the provisions of section 44(b) of the Internal Revenue Code, in the case of casual sales of personal property, if the selling price exceeds $1,000, and the initial payments received in cash or other property, other than evidence of indebtedness of the purchaser, during the taxable period of the sale, do not exceed 30 percent of the selling price, the gain realized from such sale may be reported on the installment basis.

Under the installment basis, there is reportable as income in any taxable year only that proportion of the installment payments actually received in that year which the gross profit realized or to be realized when payment is completed, bears to the total contract price.

Section 44(d) of the Internal Revenue Code, reads in part as follows:

(d) GAIN OR LOSS UPON DISPOSITION OF INSTALLMENT OBLIGATIONS.—If an installment obligation is satisfied at other than its face value or distributed, transmitted, sold, or otherwise disposed of, gain or loss shall result to the extent of the difference between the basis of the obligation and (1) in the case of satisfaction at other than face value or a sale or exchange—the amount realized, or (2) in case of a distribution, transmission, or disposition otherwise than by sale or exchange—the fair market value of the obligation at the time of such distribution, transmission, or disposition. Any gain or loss so resulting shall be considered as resulting from the sale or exchange of the property in respect of which the installment obligation was received. The basis of the obligation shall be the excess of the face value of the obligation over an amount equal to the income which would be returnable were the obligation satisfied in full.

This subsection shall not apply to the transmission at death of installment obligation if there is filed with the Commissioner, at such time as he may by regulation prescribe, a bond in such amount and with such sureties as he may deem necessary, conditioned upon the return as income, by the person receiving any payment on such obligations, of the same proportion of such payment as would be returnable as income by the decedent if he had lived and had received such payment. * * *

An executory contract to sell is to be distinguished from a sale of property. In the case of *Charles W. Dahlinger* v. *Commissioner*, 51 Fed. (2d) 662, Ct. D. 414, C. B. X-2, 337 (1931) certiorari denied, 284 U. S. 673, involving the question of the year in which a sale was consummated, the United States Circuit Court of Appeals for the Third Circuit in affirming the decision of the Board of Tax Appeals, 20 B. T. A. 176, referred to the following statements applied by the Board of Tax Appeals to show the distinction between a contract to sell and a sale:

A contract to sell goods is a contract whereby the seller agrees to transfer the property in goods to the buyer for a consideration called the price.

A sale of goods is an agreement whereby the seller transfers the property in goods to the buyer for a consideration called the price. (Williston on Sales, vol. 1, sec. 1.)

Williston proceeds as follows:

The distinction is often expressed by the terms "executory" and "executed" sales. Whether a bargain between parties is a contract to sell or an actual sale depends upon whether the property in the goods is transferred. If it is transferred, there is a sale, an executed sale, even though the price be not paid.

Based upon the above facts, it is held, as follows:

(1) The agreement entered into by and between the author and the publisher constitutes an executory contract to sell a manuscript at a future date. A sale of the manuscript will occur on the date the manuscript is delivered and assigned to the publisher by the author. Such sale will qualify as a casual sale of personalty on the installment basis within the purview of section 44(b) of the Code.

(2) Except as provided in paragraph 3, below, the loan of $10x$ dollars received by the author on the effective date of the agreement will not be subject to Federal income tax.

(3) The loan received by the author and not theretofore repaid, will be includible in the author's gross income as ordinary income in the taxable year in which the agreement is terminated if the author fails to complete and deliver the manuscript on or before the agreed date by reason of his death or disability, and if the publisher elects to terminate the agreement, except that if such termination occurs after the death of the taxpayer the amount of the loan shall be includible in the gross income of the taxpayer's estate as ordinary income.

(4) The payment of $20x$ dollars received by the author pursuant to the agreement upon the delivery and assignment of the manuscript will be the "initial payment" referred to in section 44(b) of the Code. The taxable portion of such payment, computed in accordance with the provisions of section 44(a) of the Code, will be includible in gross income as ordinary income in the taxable year in which the manuscript is delivered and assigned to the publisher. The loan of $10x$ dollars which the publisher

made to the author is not considered to be the "initial payment" for the reason that, on the basis of the facts represented, it is determined to constitute a loan rather than an advance. The repayment thereof is independent of the delivery of the manuscript, for which a separate date was provided, and the loan is required to be repaid whether or not the manuscript is delivered. The only condition under which repayment is not required is the death or other disability of the author prior to delivery of the manuscript, but even in such case the manuscript, or, if not completed, the author's working papers with respect thereto, will serve as security for the loan since the author or, in the event of his death, his estate is required to repay the portion of the loan represented by any proceeds received from the subject matter of the composition involved.

(5) The promissory notes delivered to the author pursuant to the agreement upon the delivery of the manuscript will be "installment obligations," within the meaning of section 44 of the Code.

(6) The taxable portion of payments received by the author in full satisfaction of the promissory notes so delivered to him, as computed in accordance with the provisions of section 44(a) of the Code, will be includible in gross income as ordinary income in the taxable year in which such payments are received.

(7) If any of such promissory notes so delivered to the author are satisfied at other than face value or are sold or exchanged, the excess of the amount realized over the basis of such note will constitute ordinary income computable under the provisions of section 44(d) of the Code, in the taxable year in which such amounts are realized.

(8) If any of such promissory notes so delivered to the author are distributed, transmitted, or disposed of otherwise than by sale or exchange, the excess of the fair market value of such note as of the time of such distribution, transmission, or disposition, over its basis, will constitute ordinary income computable under the provisions of section 44(d) of the Code, in the taxable year in which such distribution, transmission, or disposition occurs. However, if any of such promissory notes are transmitted at his death, no gain on account of such transmission will be required to be reported as income in his final Federal income tax return, provided there is filed with the Commissioner the bond prescribed in section 44(d) of the Code.

(9) The cost of producing the manuscript will constitute the basis thereof for the purpose of computing the gain realized from the sale.

REGULATIONS 118, SECTION 39.44-5: Gain or loss upon disposition of installment obligations. Rev. Rul. 267

INTERNAL REVENUE CODE

Installment obligations received as part of the selling price of property held in joint tenancy by a husband and wife become the property of the surviving spouse when one tenant dies and are not transmitted at death within the meaning of section 44(d) of the Internal Revenue Code. However, the provisions of section 44(d)

of the Code are applicable where property not held in joint tenancy is sold and the resulting profit is reported on a joint return or where the property to which the obligations are attributable is the community property interest of the deceased spouse.

Advice is requested relative to the application of section 44(d) of the Internal Revenue Code to installment obligations held by a taxpayer after the death of his or her spouse where the property to which the obligations are attributable was (1) held in joint tenancy, (2) not held in joint tenancy but the sale and resulting profits of such property were reported on joint returns, and (3) community property.

Section 44(d) of the Internal Revenue Code, relating to gain or loss upon disposition of installment obligations provides, in part, as follows:

If an installment obligation is satisfied at other than its face value or distributed, transmitted, sold, or otherwise disposed of, gain or loss shall result to the extent of the difference between the basis of the obligation and (1) in the case of satisfaction at other than face value or a sale or exchange—the amount realized, or (2) in the case of a distribution, transmission, or disposition otherwise than by sale or exchange—the fair market value of the obligation at the time of such distribution, transmission, or disposition. * * * This subsection shall not apply to the transmission at death of installment obligations if there is filed with the Commissioner, at such time as he may by regulation prescribe, a bond in such amount and with such sureties as he may deem necessary, conditioned upon the return as income, by the person receiving any payment on such obligations, of the same proportion of such payment as would be returnable as income by the decedent if he had lived and had received such payment. * * *

Where a capital asset is held under State law by a husband and wife in joint tenancy, each is considered as being seized of the entire estate in his own right. When one joint tenant dies his or her interest does not pass to the survivor but merely ceases and all rights in such property continue in the surviving joint tenant by right of survivorship. See G. C. M. 6677, C. B. VIII–2, 172; I. T. 1635, C. B. II–1, 19; I. T. 3754, C. B. 1945, 143; I. T. 3785, C. B. 1946–1, 98; *Fannie E. Lang* v. *Commissioner*, 289 U. S. 109, Ct. D. 662, C. B. XII–1, 171; and *Helen G. Carpenter* v. *Commissioner*, 27 B. T. A. 282. Inasmuch as the installment obligation was received as part of the selling price of a capital asset held in joint tenancy by a husband and wife, it follows that such obligation was held by the husband and wife as joint tenants in the same manner as the property sold and that upon the death of one spouse the other takes the whole interest in the installment obligation by right of survivorship. Accordingly, it is held that in such case there is no transmission at death of the installment obligations within the meaning of section 44(d) of the Internal Revenue Code for the purpose of the filing of a bond. Therefore the surviving spouse should report as capital gain for Federal income tax purposes the total outstanding balance of profit to be realized on the sale as and when realized through payments on the installment obligation made by the obligor.

Where property not held in joint tenancy is sold, the reporting of such sale on a joint return combining the incomes and deductions of both husband and wife has no effect on the ownership of property. The spouses although filing a joint return continue to retain title to their respective properties. Accordingly, on the assumption that a husband dies possessed of an installment obligation, it is held that any gain resulting from the disposition or satisfaction thereof, computed

in accordance with section 44(d) of the Code, would be reportable as income in the return of the decedent for the year of his death, unless there is filed with the Commissioner a bond, in such amount and with such securities as he may deem necessary, conditioned upon the return as income, by any person receiving any payment on such obligation, of the same proportion of such payment as would have been reportable as income by the decedent if he had lived and received such payment.

Where a surviving spouse has one-half interest in an installment obligation received as part of the selling price of community property, that part of the income attributable to such interest received during the period of administration of the estate of the deceased spouse, who died while domiciled in a community property state, is taxable to the surviving spouse for Federal income tax purposes. See G. C. M. 25008, C. B. 1946-2, 49. That part of the gain attributable to the interest of the decedent spouse in the installment obligation would be reportable in the final return of the decedent. However, if an election is made by the administrator of the estate, legatee, or next of kin of the decedent to receive the benefit of section 44(d) of the Code, the income attributable to the interest of the decedent would be reportable by the recipient of such income in accordance with the provisions of such section provided the required bond is filed with the Commissioner.

PART V.—RETURNS AND PAYMENT OF TAX

SECTION 58(d).—DECLARATION OF ESTIMATED TAX BY INDIVIDUALS: TIME AND PLACE FOR FILING

REGULATIONS 118, SECTION 39.58(d)-1: Time and place for filing declarations.

INTERNAL REVENUE CODE

Time for filing declaration and making payment of estimated tax. (See Rev. Rul. 292, p. 82.)

SUBCHAPTER C.—SUPPLEMENTAL PROVISIONS

SUPPLEMENT B.—COMPUTATION OF NET INCOME

SECTION 112(b).—RECOGNITION OF GAIN OR LOSS: EXCHANGES SOLELY IN KIND

REGULATIONS 118, SECTION 39.112(b)(3)-(5): Statutory provisions; recognition of gain or loss; exchanges solely in kind; stock for stock on reorganization; gain of corporation; transfer to corporation controlled by transferor.

INTERNAL REVENUE CODE

"Split-off" form of reorganization. (See Rev. Rul. 289, p. 37.)

REGULATIONS 118, SECTION 39.112(b)(6)-1: Distributions in liquidation of subsidiary corporation.

INTERNAL REVENUE CODE

Transfer of appreciated assets to parent corporation. (See Rev. Rul. 259, p. 55.)

REGULATIONS 118, SECTION 39.112(b)(11)-1: Certain distributions of stock on reorganization. (Also Section 112(g), Section 39.112(g)-1.) Rev. Rul. 270

INTERNAL REVENUE CODE

Tax consequences of a proposed spin-off reorganization of a bank wherein the two branch offices of the bank will be transferred to new corporations.

Advice is requested with respect to the tax consequences of a proposed reorganization of a California bank under the circumstances set forth below:

The B Corporation is an old California banking corporation with a main banking office and two branch offices. It has only common stock outstanding. For important business reasons B's officers and directors desire to incorporate B's two branch banking offices as separate corporations. Under California law B would not be permitted to transfer the branch offices to new corporations without declaring a "dividend." B proposes to declare a "dividend" (as that term is used in California law) to its shareholders of certain cash, real estate, furniture, fixtures, bonds, and loans that are attributable to the business of the branch offices. However, B will segregate the "dividend" into two funds and will transfer such funds on behalf of its stockholders directly to two new corporations, and no stockholder will be entitled to receive any of the assets declared as a "dividend." The two new corporations will each have an authorized capital of 50,000 shares of common stock, and will issue all of their stock pro rata to B's stockholders. B will also transfer directly to the new corporations assets equivalent to the deposits and other liabilities attributable to the business of its branch offices in consideration of the assumption of such liabilities by the new corporations. B's stockholders represent that they have no present intention of disposing of any of the stock of the new or old corporations or of liquidating any of the corporations.

Section 112(b)(11) of the Internal Revenue Code provides:

> (11) DISTRIBUTION OF STOCK NOT IN LIQUIDATION.—If there is distributed, in pursuance of a plan of reorganization, to a shareholder of a corporation which is a party to the reorganization, stock (other than preferred stock) in another corporation which is a party to the reorganization, without the surrender by such shareholder of stock, no gain to the distributee from the receipt of such stock shall be recognized unless it appears that (A) any corporation which is a party to such reorganization was not intended to continue the active conduct of a trade or business after such reorganization, or (B) the corporation whose stock is distributed was used principally as a device for the distribution of earnings and profits to the shareholders of any corporation a party to the reorganization.

Section 112(g)(1)(D) of the Code defines a reorganization to include "a transfer by a corporation of all or a part of its assets to another corporation if immediately after the transfer the transferor or

its shareholders or both are in control of the corporation to which the assets are transferred, * * *".

On the basis of the above facts it is held that the proposed transaction will constitute reorganizations within the meaning of section 112(g)(1)(D) of the Code, and that pursuant to section 112(b)(11) of the Code the stockholders of B Corporation will realize no gain or loss on receipt of the stock of the new corporations. In accordance with section 113(a)(23) of the Code the stockholders will determine their basis in the stock of the three corporations after the reorganizations by allocating their adjusted basis in the old stock at the time of the reorganizations among the old and new stocks on the basis of the fair market value of the three stocks at such time. The earnings and profits of the old corporation will be allocated among the old and new corporations in accordance with Regulations 118, section 39.115(a)-3.

REGULATIONS 118, SECTION 39.112(b)(11)-1: Certain distributions of stock on reorganization.

INTERNAL REVENUE CODE

"Spin-off" form or reorganization. (See Rev. Rul. 289, p. 37.)

SECTION 112(f).—RECOGNITION OF GAIN OR LOSS: INVOLUNTARY CONVERSION

REGULATIONS 118, SECTION 39.112(f)-1: Involuntary conversion where disposition of the converted property occurred after December 31, 1950. Rev. Rul. 271

(Also Section 117(j), Section 39.117(j)-1.)

INTERNAL REVENUE CODE

Where a State turnpike bisects a taxpayer's farmland in such manner as to deny cattle access to water, shade, and grazing area, the expenditure of proceeds received as severance damages to restore the usability of the farm (as in making water and shade available to cattle) will constitute the acquisition of property similar or related in service or use to the property involuntarily converted within the meaning of section 112(f) of the Code. To the extent that the unexpended portion of the severance damages exceeds the basis of the remaining property, gain will be recognized subject to the limitations provided by section 117(j) of the Internal Revenue Code.

Advice is requested whether, upon condemnation by a State of a strip of land through a taxpayer's farm, the expenditure of proceeds received as severance damages for the purpose of placing the farm in the same operating condition as it was prior to condemnation will constitute the acquisition of property similar or related in service or use to the property involuntarily converted. Advice is also requested with respect to the taxability of any gain resulting from the receipt of such damages.

In the instant case, a State turnpike commission condemned a strip of land through the taxpayer's farm for the purpose of constructing a turnpike. The turnpike will bisect the farm and separate the cattle barns from water and pasture land. To restore the farm to an efficient

operating condition it will be necessary to dig wells for water purposes, clear certain wooded areas, drain swampland, erect fences and sheds, and plant shade trees. The State paid the taxpayer certain amounts in connection with the acquisition of its right-of-way, among which were severance damages.

Section 112(f) of the Internal Revenue Code provides, in part, and subject to conditions stated therein, that if property is compulsorily or involuntarily converted as a result of its condemnation after December 31, 1950, and the taxpayer purchases other property similar or related in service or use to the property so converted, at the election of the taxpayer the gain shall be recognized only to the extent that the amount realized upon such conversion exceeds the cost of such other property.

In the instant case the severance damages are separate and apart from other damages paid as a result of the condemnation, and represent compensation for conversion of the taxpayer's right to use his farm property in the manner and for the purpose for which it was acquired. Such damages are analogous to the proceeds of property insurance; they represent compensation for damage to the property.

It is held that the expenditure of the severance damages in digging wells for water purposes, clearing certain wooded areas, draining swamplands, erecting fences and sheds, and planting shade trees to restore the usability of the farm constitutes the acquisition of property similar or related in service or use to the property involuntarily converted within the meaning of section 112(f) of the Code, and that if the conditions of section 112(f) are otherwise satisfied only the portion of such damages not so expended should be applied in the reduction of the basis of the retained portion of the property. See G. C. M. 23698, C. B. 1943, 340. To the extent that the unexpended portion of such damages exceeds the basis of the retained property, gain will be recognized subject, however, to the limitations provided in section 117(j) of the Internal Revenue Code.

SECTION 112(g).—RECOGNITION OF GAIN OR LOSS: DEFINITION OF REORGANIZATION

REGULATIONS 118, SECTION 39.112(g)-1: Purpose and scope of exception of reorganization exchanges.

INTERNAL REVENUE CODE

Circumstances which constitute a reorganization. (See Rev. Rul. 270, p. 35.)

REGULATIONS 118, SECTION 39.112(g)-2: Definition of terms. Rev. Rul. 289

(Also Section 112(b), Sections 39.112(b)(3)-(5), 39.112(b)(11)-1.)

INTERNAL REVENUE CODE

Under a plan of reorganization a going corporation transferred part of its assets to a new corporation in exchange for all the stock of the

new corporation. Immediately thereafter the stock of the new corporation was distributed *pro rata* among the stockholders of the old corporation in exchange for a portion of their stock in the old corporation (a transaction commonly called a "split-off"). *Held*, such a transaction constitutes a "reorganization" as that term is defined by section 112(g)(1)(D) of the Internal Revenue Code, with respect to which no gain or loss will be recognized to the shareholders under section 112(b)(3) of the Code, provided the requirements of control, continuity of interest, and business purpose are satisfied. (*Cf. Chester E. Spangler et ux.* v. *Commissioner*, 18 T. C. 976, acquiescence, C. B. 1953-1, 6.)

The "split-off" form of reorganization is to be distinguished from the "spin-off" type which occurs when a part of the assets of a going corporation are transferred to a new corporation and the stock in the latter is distributed to the shareholders of the old corporation without a surrender of stock by the stockholders. "Spin-off" reorganizations are governed by the provisions of section 112(b)(11) of the Code.

SECTION 113(a).—ADJUSTED BASIS FOR DETERMINING GAIN OR LOSS: BASIS [UNADJUSTED] OF PROPERTY

REGULATIONS 118, SECTION 39.113(a)(15)-1: Basis of property received by a corporation in complete liquidation of another corporation.

INTERNAL REVENUE CODE

Basis of appreciated assets transferred to parent corporation upon liquidation of wholly-owned subsidiary. (See Rev. Rul. 259, p. 55.)

SECTION 113(b).—ADJUSTED BASIS FOR DETERMINING GAIN OR LOSS: ADJUSTED BASIS

REGULATIONS 118, SECTION 39.113(b)(1)-4: Adjusted basis; mutual savings banks, building and loan associations, and cooperative banks. Rev. Rul. 216

INTERNAL REVENUE CODE

> Mutual savings banks, building and loan associations, and cooperative banks subject to Federal income tax for taxable years beginning after December 31, 1951, may amortize mortgage acquisition costs on a composite basis by employing a composite rate based on the relationship which the aggregate credits to principal of an institution's mortgage loan account over a representative period of years bears to the aggregate of the yearly balance of such mortgage loan account over the same period.

Advice is requested whether mutual savings banks, building and loan associations, and cooperative banks subject to Federal income tax for taxable years beginning after December 31, 1951, may amortize mortgage acquisition costs on a composite basis by employing a composite rate based on the relationship which the aggregate credits to principal of an institution's mortgage loan account over a repre-

sentative period of years bears to the aggregate of the yearly balances of such mortgage loan account over the same period.

The instant taxpayer has proposed a method for the amortization of mortgage acquisition costs, referred to by the taxpayer as the New York Method, for use by mutual savings banks, building and loan associations and cooperative banks for taxable years after December 31, 1951. It is contemplated that the representative period of years to be used under this method will vary with different banking institutions but that in each case it will be ascertained in the light of the particular institution's loan experience, the complexion of its loan account and all other appropriate and relevant factors; the aim being to select a period sufficiently representative to permit the inference that the experience of such period is indicative of future loan operations.

Under the method proposed, the balance in the mortgage loan account of a given bank for each of the years in the representative period would be ascertained as of the beginning of such year. To that would be added one-half of the new mortgage loans made during such year, in order to properly reflect and weigh the year's addition to the loan account. Secondly, in respect of each of the years during the representative period, the total credits to principal of the mortgage account during such year would be ascertained. These total credits to principals include all payments of principal on mortgage loans, credits arising as a result of foreclosure, and credits arising from compromise payments and chargeoffs. The percentage which the aggregate credits to principal over the period bears to the aggregate of the yearly mortgage loan account balances would then be ascertained and divided into 100 to obtain an expression in years. The example set forth below will best serve to illustrate the application of this method.

Year	Balance mortgage loan account at beginning of year	One-half of additions during year	Column 2 plus column 3	Total credits to principal
1942	$100,000	$2,000	$102,000	$5,000
1943	99,000	5,000	104,000	6,000
1944	103,000	4,000	107,000	6,000
1945	105,000	9,000	114,000	11,000
1946	112,000	6,000	118,000	14,000
1947	110,000	7,000	117,000	9,000
1948	113,000	10,000	123,000	8,000
1949	125,000	8,000	133,000	15,000
1950	126,000	9,000	135,000	16,000
1951	128,000	8,000	136,000	14,000
Totals			1,189,000	104,000
	Percentage 8.75 percent or 11.43 years			

It is proposed that the composite rate thus obtained could be used for the purpose of amortizing the bank's mortgage acquisition costs until such time as significant changes in its loan operations, loan experience, or complexion of its loan account indicate that such rate is no longer applicable or appropriate.

The following table, in which the average period of payment has been rounded out to 11 instead of 11.43 years, shows the amount of the unamortized acquisition costs on December 31, 1951, and the

amount of the amortization of those costs to be taken as a deduction for income tax purposes in 1952.

Year	Total acquisition costs	Basis Value Dec. 31, 1951		Amortization for 1952	
		Fraction	Value	Fraction	Value
1941	$2,000	1/22	90.91	1/22	90.91
1942	2,040	3/22	278.18	1/11	185.44
1943	2,080	5/22	472.73	1/11	189.10
1944	2,140	7/22	680.91	1/11	194.54
1945	2,280	9/22	932.73	1/11	207.28
1946	2,360	11/22	1,180.00	1/11	214.54
1947	2,340	13/22	1,382.72	1/11	212.72
1948	2,460	15/22	1,677.27	1/11	223.64
1949	2,660	17/22	2,055.45	1/11	241.82
1950	2,700	19/22	2,331.82	1/11	245.46
1951	2,720	21/22	2,596.36	1/11	247.28
	25,780		13,679.09		2,252.73

Section 39.113(b)(1)-4 of Regulations 118 provides in part as follows:

The adjustments to the cost or other basis of property provided in section 113(b) and section 39.113(b)(1)-1 to section 39.113(b)(1)-3, inclusive, are applicable in the case of a mutual savings bank not having capital stock represented by shares, a domestic building and loan association, and a cooperative bank without capital stock organized and operated for mutual purposes and without profit, although such institutions were exempt from tax for taxable years beginning before January 1, 1952. * * *

* * * * * * *

In the case of a mortgage purchase, acquired, or originated at a premium, where the principal of such mortgage is payable in installments, adjustments to the basis of the premium must be made for all taxable years (whether or not the institution was exempt from tax during such years) in which installment payments are received. Such adjustments may be made on an individual mortgage basis or on a composite basis by reference to the average period of payments of the mortgage loans of such institution. For the purpose of this adjustment, the term "premium" includes the excess of the acquisition value of the mortgage over its maturity value. The acquisition value of the mortgage is the cost including buying commissions, attorneys' fees, or brokerage fees, but such value does not include amounts paid for accrued interest.

The regulations cited above make it clear that adjustment to the basis of mortgage acquisition costs may be made on a composite basis by reference to the average payments of the mortgage loans. What constitutes the average period of payments is a question of fact to be determined in the case of the individual taxpayer. No particular method for adjusting mortgage acquisition costs on a composite basis is prescribed in the regulations. The method outlined above appears to be one which would reasonably determine the adjusted basis of mortgage acquisition costs as of the beginning of the first taxable year beginning after December 31, 1951, and the amount of yearly amortization thereafter.

In view of the foregoing, it is held that the method proposed in the instant case for the amortization of mortgage acquisition costs by mutual savings banks, building and loan associations, and cooperative banks is a permissible method under section 39.113(b)(1)-4 of Regulations 118.

SECTION 114.—BASIS FOR DEPRECIATION AND DEPLETION

REGULATIONS 118, SECTION 39.114-1: Basis for allowance of depreciation and depletion. (Also Section 23(m), Section 39.23 (m)-1.) Rev. Rul. 290

INTERNAL REVENUE CODE

Determination of the processes properly included in mining under section 114(b)(4)(B) of the Internal Revenue Code, with respect to calcium carbonates and shale mined for use in the manufacture of cement.

Advice is requested concerning the position of the Internal Revenue Service on the determination of the processes properly included in mining with respect to calcium carbonates and shale mined for use in the manufacture of cement.

It is the position of the Internal Revenue Service that calcium carbonates and shale, mined for use in the cement industry, are not customarily sold in the form of the crude mineral product, and that, therefore, under section 39.23(m)(1)(f) of Regulations 118, crushing and grinding are considered "ordinary treatment processes" in the computation of gross income from the property for percentage depletion purposes. Blending with other material after crushing and grinding, such as that occurring at the kiln feed bins, is excluded from "ordinary treatment processes," but where mixing of the calcium carbonates.and shale occurs before or during crushing and grinding, it will be considered as incidental to such processes.

The gross income for percentage depletion purposes must of course be computed separately with respect to each component mineral, notwithstanding any such mixing. The net income for purposes of the limitation on percentage depletion should also be computed separately for each component mineral unless the minerals are produced from the same "property." See Revenue Ruling 76, C. B. 1953-1, 176.

In view of the specific detailed listing in section 114(b)(4)(A) of the Internal Revenue Code, percentage depletion is not allowable on clay used in the manufacture of cement unless the clay so used definitely comes within one of the specific classifications in that section.

SECTION 115(c).—DISTRIBUTIONS BY CORPORATIONS: DISTRIBUTIONS IN LIQUIDATION

REGULATIONS 118, SECTION 39.115(c)-1: Distributions in liquidation.

INTERNAL REVENUE CODE

Commissions assigned by corporation in liquidation. (See Rev. Rul. 255, p. 10.)

SECTION 116.—EXCLUSIONS FROM GROSS INCOME

REGULATIONS 118, SECTION 39.116-1: Earned income from sources without the United States. Rev. Rul. 291

INTERNAL REVENUE CODE

Income tax liability of United States citizens resident or physically present in foreign countries for taxable years beginning on or after January 1, 1951.

SECTION 1. PURPOSE.

The primary purpose of this Revenue Ruling is to provide assistance and guidance to United States citizens, residing or physically present in foreign countries, in the preparation of their Federal income tax returns. The Revenue Ruling relates only to the tax problems peculiar to such citizens and is intended to supplement information issued by the Internal Revenue Service for taxpayers generally. Therefore, in the preparation of their Federal income tax returns and other forms, such citizens should follow the instructions issued in connection with the forms insofar as they are applicable.

SEC. 2. AUTHORITY.

The right of the United States to impose income tax upon its citizens, wherever resident, is based on citizenship. Generally speaking, United States citizens residing or physically present in foreign countries are taxable in the same manner as those residing within the United States, unless they can satisfy the requirements of section 116(a) of the Internal Revenue Code. If the citizen meets either the "foreign residence" test or the "presence in a foreign country" test provided by section 116(a) of the Code, he may, for taxable years beginning on or after January 1, 1951, exclude from gross income amounts received as "earned income" for personal services rendered without the United States.

SEC. 3. SCOPE.

This Revenue Ruling applies to taxable years beginning on or after January 1, 1951. It does *NOT* apply to taxable years beginning prior to January 1, 1951; nor to citizens performing civilian or military services for the United States or for any agency or instrumentality thereof. Compensation for personal services performed by a citizen as an employee of the United States, or any agency or instrumentality thereof, is required to be included in gross income regardless of where the services are performed.

SEC. 4. EXCLUSION UNDER SECTION 116(a)(1) BASED UPON BONA FIDE RESIDENCE IN FOREIGN COUNTRIES.

.01 *General.*—A United States citizen may exclude from gross income under section 116(a)(1) of the Code, his "earned income" (as defined in sec. 7 of this Rev. Rul.) if:

(a) He has been a bona fide resident of a foreign country or countries for an uninterrupted period which includes an entire taxable year; *and*

(b) Such earned income is:

(1) Received on or after January 1, 1951;

(2) For personal services rendered outside the United States;

(3) Attributable to such uninterrupted period; *and*

(4) Not paid by the United States or any agency or instrumentality thereof.

All of these requirements must be met by the citizen in order to claim the exclusion from gross income. For example, a privately employed citizen was a bona fide resident of a foreign country for an uninterrupted period beginning July 1, 1950, and ending June 30, 1952, and files his returns on the calendar year basis. He may exclude from gross income the amount of compensation received on or after January 1, 1951, for personal services rendered abroad if such amount is attributable to the period July 1, 1950, to June 30, 1952. (He may not apply the exclusion to any compensation received in 1950, since under the law in effect for that year an exclusion from gross income was allowable for 1950 only if the taxpayer was a bona fide resident of the foreign country during the "entire taxable year.")

.02 *Period of residence prior to January 1, 1951.*—The period during which the citizen was a bona fide resident of a foreign country or countries prior to January 1, 1951, may be taken into account in determining whether he had been a bona fide resident of a foreign country or countries for an uninterrupted period of at least an entire taxable year. For instance, a privately employed citizen, who files his returns on the calendar year basis, was a bona fide resident of a foreign country for an uninterrupted period beginning July 1, 1949, and ending October 31, 1951. Under section 116(a)(1) of the Code, as amended by the Revenue Act of 1951, the taxpayer may exclude the "earned income" attributable to such period and received on or after January 1, 1951, since his period of bona fide foreign residence includes an entire taxable year (1950).

.03 *Bona fide foreign residence.*—No specific rule can be stated for determining whether a United States citizen is a bona fide resident of a foreign country, since it involves his intentions with respect to the length and nature of his stay. The intention of the taxpayer to establish a bona fide residence in a foreign country may be evidenced by words and acts, but where they conflict, more emphasis will be placed on the acts than on the words. Generally, a citizen who goes to a foreign country for a definite purpose, which is of a temporary nature, and who returns to the United States after it has been accomplished, is not a bona fide resident of such foreign country. However, if his purpose is of such a nature that an extended and indefinite stay may be necessary for its accomplishment, and to that end he establishes residence in the foreign country, he may be a bona fide resident of such foreign country for Federal income tax purposes. For example, American citizens who go to foreign countries to work on construction projects, which are obviously of a temporary nature, cannot be classified as bona fide residents of such countries for the purposes of section 116(a)(1) of the Code, even though they remain abroad for an entire taxable year or longer. (For information as to whether the "earned income" attributable to such personal services rendered abroad is excludable under the "presence in a foreign country" exclusion, see sec. 5 of this Rev. Rul.) However, citizens of the United States who are permanently assigned to foreign divisions of business concerns

and who establish and maintain their residence in a foreign country or countries for a period of indefinite duration may be classified as bona fide residents of a foreign country or countries for the purposes of section 116(a)(1) of the Code.

.04 *Temporary absence from foreign country.*—Once bona fide residence in a foreign country or countries has been established, temporary visits to the United States or elsewhere on vacation or business trips will not necessarily deprive the citizen of his status as a bona fide resident of a foreign country. Such absences must not be unreasonable in length, there must be full intention on the part of the individual to return to his foreign post, and there must be substantial evidence that the foreign residence has not been relinquished. Long periods of time spent in the United States or any possessions thereof would be considered as evidence that the citizen had relinquished bona fide residence in a foreign country.

SEC. 5. EXCLUSION UNDER SECTION 116(a)(2) BASED ON PRESENCE IN A FOREIGN COUNTRY.

.01 *General.*—A citizen of the United States may exclude from gross income under section 116(a)(2) of the Code, amounts constituting "earned income" (as defined in sec. 7 of this Rev. Rul.) if:

(a) He is present in a foreign country or countries during a total of at least 510 full days during any period of 18 consecutive months; *and*

(b) Such earned income is:

(1) Received on or after January 1, 1951;

(2) For personal services rendered outside the United States;

(3) Attributable to such 18-month period; *and*

(4) Not paid by the United States or any agency or instrumentality thereof.

All of these requirements must be met in order for the citizen to qualify for the exclusion. The excluded gross income may be attributable to any 18 consecutive-month period during which the citizen is in a foreign country or countries for 510 full days. For example, a citizen of the United States, privately employed, arrives in a foreign country on August 3, 1952, and remains there continuously until his departure therefrom on December 27, 1953, a period during which he is present in the foreign country 510 full days. The citizen may exclude from gross income the "earned income" from sources without the United States that is attributable to any 18 consecutive-month period which includes the above 510 full days, notwithstanding that the citizen was actually present in the foreign country for a period of less than 18 months. For example, the exclusion would be applicable but not limited to the following 18-month periods: An 18-month period which commences August 4, 1952, and ends February 3, 1954; an 18-month period which commences June 28, 1952, and ends December 27, 1953; or an 18-month period which commences July 1, 1952, and ends December 31, 1953.

.02 *Limitation on amount excludable.*—There is no limitation upon the amount of earned income received during the period January 1, 1951, through December 31, 1952, which may be excluded from gross income under section 116(a)(2) of the Code. However, for taxable years ending after December 31, 1952, but only with respect to amounts

received after such date, the amount excluded from gross income under the provisions of such section shall not exceed $20,000 in those cases in which the 18-month period includes the entire taxable year. In those cases in which the 18-month period does not include the entire taxable year, the $20,000 annual limitation shall be prorated in the following manner: The amount excluded from gross income under such section for such taxable year shall not exceed an amount which bears the same ratio to $20,000 as the number of days in the part of the taxable year within the 18-month period bears to the total number of days in such year. For example, a taxpayer was present in a foreign country 510 full days during the 18-month period ending June 30, 1953, during which the requirements of section 116(a)(2) of the Code were satisfied. During the calendar year 1952 he received $26,000 and during the period January 1, 1953, through June 30, 1953, he received $13,000 as salary. If the taxpayer reported on a calendar year basis, the entire $26,000 received during 1952 would be excludable, but only $9,917.81 (181/365 of $20,000) would be excludable in 1953. The balance of $3,082.19 would be includible in the taxpayer's gross income for 1953. A special rule is applicable to a fiscal year beginning in 1952 and ending in 1953. (There is no limitation upon the amount of "earned income" which may be excluded from gross income under sec. 116(a)(1) of the Code.)

.03 *Computation of 510 full days presence in foreign country.*—In computing the minimum of 510 full days presence in a foreign country or countries, all separate periods of such presence during the 18-month period are to be aggregated. For the purpose of section 116(a)(2) of the Code, if an individual travels from one place in a foreign country to another place in the same country, or to a place in another foreign country, and if such travel extends over a period of less than 24 hours and does not involve travel within the United States or any possession thereof, such individual shall not be deemed outside a foreign country during the period of such travel. The 510 full days need not be consecutive, but may be interrupted by periods during which the citizen is not present in a foreign country. Time spent in a foreign country in the employment of the United States Government will count toward satisfaction of the 510 full-day requirement, even though amounts paid by such Government are not excludable from gross income. The period during which the citizen was present in a foreign country, or countries, prior to January 1, 1951, may be taken into account in determining whether such citizen is present in a foreign country or countries during at least 510 full days during any 18-month period. However, the income attributable to the period prior to January 1, 1951, is not excludable from gross income under section 116(a)(2) of the Code if received before such date, since the exclusion is applicable only to taxable years beginning on or after January 1, 1951.

.04 *Computation of 18-month period.*—The 18 consecutive-month period may be part of a longer period of presence in a foreign country and need not commence with the citizen's day of arrival therein or terminate with the day of his departure therefrom. For example, a citizen who arrives in a foreign country on January 1, 1952, and finally departs therefrom on February 14, 1954, may not be present in such country for 510 full days during the 18-month period commencing with January 1, 1952, and ending with the close of June 30, 1953, be-

cause of his visits to the United States during such period. However, he may satisfy the 510 full-day requirement during the 18-month period commencing with February 15, 1952, and ending with the close of August 14, 1953. In such event, the exclusion will apply to income attributable to the latter period, but not to income attributable to the period commencing with January 1, 1952, and ending with the close of February 14, 1952. The exclusion is applicable as long as there is a continuing period throughout which the citizen satisfies the requirement of 510 full days presence in a foreign country or countries during an 18-month period.

.05 *Definition.*—The term "full day" means a continuous period of 24 hours commencing from midnight and ending with the following midnight. The term "18 consecutive months" means any 18-month period commencing with the beginning of any day of any month and ending with the close of the day preceding the corresponding day in the succeeding 18th month; or if there is no such corresponding day, with the close of the last day of the succeeding 18th month. For example, the period July 3, 1951, through January 2, 1953, and the period July 1, 1951, through December 31, 1952, would both be periods of "18 consecutive months." The term "foreign country" includes only territory under the sovereignty of a government other than that of the United States; it does not include the territories (Hawaii and Alaska) or the possessions of the United States.

SEC. 6. INCOME RECEIVED WITHIN POSSESSIONS OF THE UNITED STATES.

Income derived from possessions of the United States may, under certain circumstances, be excluded from gross income in accordance with the provisions of section 116(1) and section 251 and, in some rare instances, under section 116(a) of the Internal Revenue Code. Generally, section 116(a) of the Code has no application to citizens of the United States performing personal services or engaged in a trade or business within the possessions. However, a citizen who has qualified for the "foreign residence" or "presence in a foreign country" exclusion under section 116(a) of the Code may exclude earned income attributable to a period he is temporarily present in a possession during such qualifying period. For example: A privately employed citizen arrived in Brazil on December 31, 1950, and remained there continuously until May 25, 1952, a period during which he qualified for the "presence in a foreign country" exclusion. (See sec. 5 of this Rev. Rul.) On May 25, 1952, he left Brazil for a temporary assignment in the Panama Canal Zone, a possession of the United States, where he remained until July 15, 1952, when he returned to the United States for a permanent assignment. The citizen may exclude from gross income under section 116(a)(2) of the Code the earned income attributable to the period beginning January 1, 1951, and ending June 30, 1952, without limitation as to amount if received before January 1, 1953, since he was present in a foreign country for 510 full days during such 18-month period and such income was for personal services rendered outside the United States. He may not exclude the earned income attributable to the period July 1 to July 15, 1952, since he did not qualify for the "presence in a foreign country" exclusion for an 18-month period which included such period. For purposes of this section, some of the more important possessions are the Panama Canal Zone, Guam,

American Samoa, Wake, Midway Islands, Puerto Rico, and the Virgin Islands.

SEC. 7. EARNED INCOME.

.01 *Compensation for personal services rendered.*—The term "earned income" means wages, salaries, professional fees, and other amounts received as compensation for personal services actually rendered. It does not include such income as dividends, other distributions of corporate earnings or profits, gambling gains, interest, rents, or gains or profits from dealing in real or personal property. For example, where a citizen performs personal services for a corporation in which he owns stock, "earned income" means only such portion of any income received from the corporation which represents a *reasonable allowance as compensation for the personal services actually rendered.* The entire amount received as professional fees by a citizen engaged in a professional occupation, such as a doctor or lawyer, may be treated as "earned income" even though he employs assistants in the performance of the services, if the patients or clients are those of the citizen and look to him as the person responsible for the services rendered, and capital is not a material income-producing factor.

.02 *Profit from trade or business.*—If a citizen is engaged in a trade or business, either as sole proprietor or as a member of a partnership, in which both personal services and capital are material income-producing factors, a reasonable allowance as compensation for the personal services actually rendered by him shall be considered to be "earned income," but the amount which may be treated as "earned income" from such trade or business may not exceed 20 percent of his share of the net profits therefrom. To illustrate: A citizen qualifying for the "foreign residence" exclusion operates a retail sales outlet in a foreign country. Since capital is a material income-producing factor in the business, not more than 20 percent of the net profits from the business may be treated as "earned income" and excluded. The balance of the profits must be included in gross income for Federal income tax purposes.

SEC. 8. SOURCE OF INCOME.

For the purpose of section 116(a) of the Code, the place where personal services are performed is considered to be the source of the income for such services, irrespective of the place where payment is made. Therefore, if "earned income" is attributable to a period in which the citizen satisfies either the "foreign residence" test or the "presence in a foreign country" test, the amounts of such income received for personal services rendered outside the United States may be excluded from gross income, subject to the limitations set forth in section 5.02 of this Revenue Ruling, even though received within the United States. Compensation for personal services rendered within the United States is taxable and is not excludable from gross income, regardless of the place where payment is made. For example, a United States citizen, who is a bona fide resident of a foreign country, returns to the United States on a business trip. The compensation for the services rendered while in the United States is taxable and includible in gross income, even though payment for such services may be received by the taxpayer after his return to the foreign country.

SEC. 9. INCOME RECEIVED IN FOREIGN CURRENCY.

The income reported on a Federal income tax return must be expressed in terms of United States dollars. Where income is actually or constructively received in foreign currency, the computation in terms of United States dollars must be based on the rate of exchange at the time of receipt by the citizen, or when credited to his account in the foreign country, even though not actually converted into United States currency at that time. (In the case of Blocked Foreign Income see sec. 10 of this Rev. Rul.)

SEC. 10. BLOCKED FOREIGN INCOME.

Generally, all income (other than that excludable by law) of United States citizens from sources within a foreign country or countries, whether in terms of United States dollars or foreign currencies, is includible in gross income for Federal income tax purposes, notwithstanding the fact that under the laws or regulations of the foreign country or countries conversion of such foreign income into United States dollars, or into other money or property which is readily convertible into United States currency, may be blocked. The citizen must include the blocked income in his gross income when such income is either actually or constructively received or is credited to his account in the foreign country, unless he takes affirmative action to elect to defer the reporting of such income until it ceases to be blocked. If he wishes to make such election and defer the income taxes otherwise due on such income, he must comply with the procedural requirements of the Internal Revenue Service relating to blocked foreign income, including the filing, with his regular return, of a tentative return reflecting such blocked income, but on which no tax is computed. Details of the requirements are published in the Internal Revenue Bulletins. See Mimeograph 6475, C. B. 1950-1, 50, as amended by Mimeograph 6494, C. B. 1950-1, 54, and Mimeograph 6584, C. B. 1951-1, 19. Income ceases to be blocked and is includible in gross income when it is convertible, or has been converted, into United States dollars or into other money or property which is convertible into United States currency; or the citizen uses the income for his personal expenditures; or disposes of it by way of gift, bequest, devise or inheritance, or in some other manner.

SEC. 11. FILING OF INCOME TAX RETURNS.

.01 *Gross income.*—A citizen of the United States, wherever resident, who has gross income of $600 or more (other than income excluded by law) during the taxable year must file an income tax return, regardless of his marital status, the number of his dependents, or the amount of his deductions. For example, a citizen who qualifies for the "foreign residence" exclusion files his return on a calendar year basis. For the year 1952 he received a salary of $10,000 for services performed in a foreign country, dividends of $500 from a foreign corporation, and interest of $200 from investments in foreign countries. The citizen must file a return for such year since he had gross income of $600 or more exclusive of the salary of $10,000 excludable under the provisions of section 116(a)(1) of the Code. A self-employed citizen not meeting the above requirements may nevertheless be required to file a return for purposes of the self-employment tax if he is engaged in a trade or business as defined in section 481 of the

Code, and has net earnings of $400 or more from self-employment. (See sec. 12 of this Rev. Rul.)

.02 *Deductions.*—Any expenses, losses, and other deductions which are attributable to income properly excluded under section 116(a) are not allowable as deductions in a Federal income tax return. For example, a salesman residing and traveling abroad, who properly excluded from gross income under section 116(a) of the Code income earned abroad, may not deduct in his Federal income tax return traveling and other expenses incurred by him in earning such excluded income. Expenses, losses, and other deductions which cannot be identified as being attributable exclusively to either includible or excludable income but are attributable to both must be allocated or apportioned.

.03 *Income taxes paid to foreign countries.*—If a citizen is required to include in his income tax return, Form 1040, income from foreign sources on which income taxes to a foreign country or countries are paid or accrued, he may claim credit for such foreign income taxes against his United States income tax in accordance with the provisions of section 131 of the Internal Revenue Code, *provided* he does not claim the standard deduction or compute his tax by the use of the tax table on page 4 of the return. The foreign tax credit should be claimed on the line provided therefor (line 10 of the 1953 Form 1040) at the bottom of page 3 of the return. The method of computing the foreign tax credit allowable under section 131 of the Code is explained on Form 1116, which must be filed with the income tax return by every taxpayer claiming credit under that section. If credit is claimed under section 131 of the Code and a redetermination of the taxpayer's foreign income tax liability discloses that he has overpaid or underpaid such tax, he should immediately notify the Commissioner of Internal Revenue in order that appropriate adjustment may be made of the foreign tax credit claimed on his Federal income tax return. As an alternative to claiming the foreign income tax as a direct *credit* against his United States income tax, the taxpayer may claim the amount of income taxes paid to a foreign country or countries as a *deduction* on page 3 of Form 1040 in computing his net income, provided he itemizes his deductions. In most cases, however, it will be to the taxpayer's advantage to claim foreign income taxes as a credit against the Federal tax under section 131 of the Code. Taxpayers who claim the foreign *income* taxes either as a credit or as a deduction may not also have the benefit of the standard deduction.

.04 *Where right to exemption not yet established.*—If a citizen employed abroad has not been there long enough to qualify for exemption under either the "foreign residence" rule or the "presence in a foreign country" rule at the time his income tax return is due to be filed, he must either include the compensation in his gross income and pay the Federal tax due thereon, or obtain an extension of time for the filing of his return. (See par. .06 of this section.) If he elects to include the compensation in his gross income, he may, after he has met the statutory requirements for exemption and within the statutory period, file an amended return or a claim on Form 843 for refund or credit of any tax thus overpaid. For example, a citizen was a bona fide resident of a foreign country from November 1, 1952, through January 31, 1954, during which period he performed personal services abroad. He

would be required to include in his 1952 return, filed on the calendar year basis, all income for the year, including the "earned income" received during the period November 1, 1952, through December 31, 1952, since he had not met the requirements of section 116(a)(1) of the Code as of the due date for the filing of such return. However, since the requirements of that section would be met as of December 31, 1953, he would then be entitled to a refund or credit of any overpayment of tax resulting from the exclusion of the "earned income" received during the period November 1, 1952, through December 31, 1952, and a claim on Form 843 or amended return should then be filed.

.05 *Due date for filing returns.*—Citizens of the United States who, on March 15, are residing or traveling outside of the United States, and who file their returns on the calendar year basis, are automatically allowed an extension of time until June 15 for filing the return for the preceding taxable year. Similarly, an extension of 3 months is granted to fiscal year taxpayers. A taxpayer who takes advantage of this extension must attach to his return a statement showing that he was residing or traveling outside the United States on the due date (March 15, for calendar year taxpayers) and he must pay interest at the rate of 6 percent per annum on the unpaid tax, if any, from the due date until paid.

.06 *Extensions of time for filing returns.*—An extension of time for filing income tax returns may be granted for more than 6 months in the case of citizens of the United States who are abroad. A citizen desiring an extension of time, in addition to the 3 months automatically granted, for filing his return until after the completion of the qualifying period under section 116(a) of the Code should make application therefor with the district director of internal revenue with whom the return is required to be filed. The application must be in writing, properly signed by the taxpayer or his duly authorized agent, and must be made before the due date for filing the return with respect to which the extension is requested. The application should set forth the facts relied upon to justify the extension of time requested and should include a statement as to the earliest date the taxpayer expects to be in a position to determine whether he will be entitled to the exclusion provided by section 116(a) of the Code.

SEC. 12. SELF-EMPLOYMENT TAX.

A citizen of the United States, wherever resident, who has net earnings from self-employment of $400 or more from a trade or business carried on by him or from a partnership of which he is a member, is subject to the self-employment tax. Such citizen is required to file a return on Form 1040 for the purpose of reporting the self-employment tax even though he has no income tax liability. A schedule for the computation of the tax is provided on page 3 of separate Schedule C (Form 1040) and instructions for its completion are shown on page 4 of the schedule. The term "trade or business" as used herein includes all self-employment activities of the citizen, except those specifically excluded by law. Some of the self-employment activities specifically excluded by law are the practice of certain professions, such as the medical, accounting and legal professions; or services as a minister or

member of a religious order; or farming; or real estate rentals, except rentals received in the course of a trade or business as a real estate dealer. For a complete list of the excluded activities, see "EXCLUSIONS" on page 4 of separate Schedule C (Form 1040).

SEC. 13. DECLARATION OF ESTIMATED TAX.

.01 *Who must file.*—Every citizen of the United States must file a declaration of estimated tax on Form 1040-ES for the taxable year if he expects to receive during such year (exclusive of income exempt from tax) either (a) gross income in excess of $100 not subject to withholding, provided his total gross income is expected to amount to $600 or more; or (b) wages subject to withholding in excess of $4,500 plus $600 for each exemption to which he is entitled. Specific instructions for the preparation and filing of the declaration are printed on the Form 1040-ES and, with the exceptions mentioned herein, should be followed by citizens outside the United States.

.02 *Due date for filing declarations.*—The declaration is required to be filed on or before the 15th day of the third month of the taxable year for which it is made. However, a citizen traveling or residing in a foreign country on the due date for filing the declaration is allowed an extension of time to and including the 15th day of the sixth month of the taxable year (June 15, for the calendar year taxpayers) for filing the declaration and payment, without interest, of all installments of estimated tax then due.

SEC. 14. WHERE RETURNS AND DECLARATIONS SHOULD BE FILED.

Income tax returns and declarations of estimated tax should be filed with the district director of internal revenue for the district in which the taxpayer's legal residence or principal place of business in the United States is located, or if he has no legal residence or place of business in the United States, with the District Director of Internal Revenue, Baltimore 2, Maryland, U. S. A.

SEC. 15. PENALTIES.

Citizens of the United States residing or present in foreign countries are liable, to the same extent as taxpayers within the United States, for all the penalties and additions to the tax imposed by law, including penalties and additions to the tax in respect of declarations and payments of estimated tax.

SEC. 16. WHERE FORMS MAY BE OBTAINED.

Necessary forms for the filing of returns, declarations, and/or claims may be obtained from any district director of internal revenue, or from most United States Embassies and Consulates.

SEC. 17. CORRESPONDENCE.

Any taxpayer desiring additional information concerning this Revenue Ruling, or information relating to the law, regulations, or procedures applicable to taxable years beginning on or before December 1, 1950, should address a communication to the Commissioner of Internal Revenue, Attention: Assistant Commissioner (Technical), Washington 25, D. C.

REGULATIONS 118, SECTION 39.116-4: Exclusion of certain cost-of-living allowances. Rev. Rul. 237

INTERNAL REVENUE CODE

Territorial cost-of-living allowances paid to certain civilian employees of the Government of the United States stationed in Territories and possessions of the United States, pursuant to section 207 of the Independent Offices Appropriation Act of 1949, as amended, 62 Stat. 194 and 1205, are excludable from gross income and exempt from Federal income tax under the provisions of section 116(j) of the Internal Revenue Code.

Advice is requested whether territorial cost-of-living allowances paid to certain civilian employees of the Government of the United States stationed in Territories and possessions of the United States, under the provisions of section 207 of the Independent Offices Appropriation Act of 1949, approved April 20, 1948, 62 Stat. 194, as amended by section 104 of the Supplemental Independent Offices Appropriation Act of 1949, approved June 30, 1948, 62 Stat. 1205, are excludable from gross income and exempt from Federal income tax under the provisions of section 116(j) of the Internal Revenue Code.

Section 207 of the Independent Offices Appropriation Act of 1949, as amended, *supra*, provides in pertinent part as follows:

Any appropriations or funds available to the executive departments, independent establishments, and wholly owned Government corporations for the payment of salaries and compensation to persons stationed outside the continental United States or in Alaska whose rates of basic compensation are fixed by statute, shall be available for the payment of additional compensation to such persons, based on living costs substantially higher than in the District of Columbia, or conditions of environment which differ substantially from conditions of environment in the States and warrant additional compensation as a recruitment incentive, or both such factors: *Provided*, That such additional compensation, except as otherwise specifically authorized by law, shall be paid only in accordance with regulations prescribed by the President * * *.

Pursuant to this act, the President on September 16, 1948, issued Executive Order 10,000, 3 CFR, 1948 Supp. page 202, promulgating regulations to which the statute refers. Among other things, the order provides for payment of additional compensation to certain employees of the Government who are stationed in Territories or possessions of the United States. The payments are of two types, (1) a "territorial post differential," authorized for service at posts having conditions of environment which differ substantially from conditions of environment in the States and warrant additional compensation as a recruitment incentive, and (2) a "territorial cost-of-living allowance," authorized for service at posts where living costs are substantially higher than in the District of Columbia.

Section 116(j) of the Internal Revenue Code excludes from gross income:

In the case of a clerk or employee in the Foreign Service of the United States, amounts received as cost-of-living allowances under authority of section 3, as amended, of the Act of February 23, 1931; and in the case of an ambassador, minister, diplomatic, consular, or Foreign Service officer, amounts received as post allowances under the authority of section 12, as amended and renumbered, of the Act of May 24, 1924; and in the case of other civilian officers or employees of the Government of the United States stationed outside continental United States, amounts received as cost-of-living allowances in accordance with regulations approved by the President.

From the foregoing it is apparent that the cost-of-living payments provided for Government employees stationed in the Territories and possessions by section 207 of the Independent Offices Appropriation Act of 1949, as amended, *supra*, based on living costs substantially higher than in the District of Columbia, are clearly distinguishable from the payments for environmental factors authorized in that statute. Furthermore, the Civil Service Commission regulations issued under authority of Executive Order 10,000, *supra*, define the cost-of-living payments here considered as "territorial cost-of-living allowances." See 5 CFR 350.1(e). Such classification appears to bring the instant payments squarely within the purview of section 116(j) of the Code as "amounts received as cost-of-living allowances in accordance with regulations approved by the President." The recipients thereof are "stationed outside continental United States," since section 39.116–4 of Regulations 118 provides that for purposes of section 116(j) the term "continental United States" includes only the States of the Union and the District of Columbia.

It is accordingly held that territorial cost-of-living allowances paid to certain civilian employees of the Government of the United States stationed in Territories and possessions of the United States, pursuant to section 207 of the Independent Offices Appropriation Act of 1949, as amended, 62 Stat. 194 and 1205, are excludable from gross income and exempt from Federal income tax under the provisions of section 116(j) of the Internal Revenue Code. *Cf.* I. T. 3807, C. B. 1946–2, 67, and G. C. M. 24162, C. B. 1944, 266.

SECTION 117(a).—CAPITAL GAINS AND LOSSES: DEFINITIONS

REGULATIONS 118, SECTION 39.117(a)-1: Meaning of terms. Rev. Rul. 239

(Also Section 22(b), Section 39.22(b)(2)-2.)

INTERNAL REVENUE CODE

> The "consideration paid" for an annuity contract executed by an individual in exchange for real property is the fair market value of the real property at the time of the transfer. The annuity payments received under the contract constitute ordinary income to the extent of 3 percent of the fair market value of the real property at the time of the transfer until the aggregate of that portion of the payments which is not taxable under section 22(b)(2) of the Internal Revenue Code equals the fair market value of the property transferred. After such time the payments are taxable in full as ordinary income.
>
> After the total of that part of the annuity payments which is not taxed under section 22(b)(2) of the Code equals the adjusted basis of the real property, subsequent payments, to the extent that they exceed 3 percent of the fair market value of the property, are taxable as gain from the sale of such property until the total of the payments so taxed equals the excess of the fair market value of the real property over the adjusted basis thereof.

Advice is requested relative to the treatment for Federal income tax purposes of monthly payments received by the taxpayer under the circumstances outlined below.

In the instant case, the taxpayer transferred certain real property

valued at $40,000 in consideration of the agreement of the purchaser, an individual, to pay her $2,000 per year for the remainder of her life and after her death to make similar payments to her daughter for life. The adjusted basis of the property at the time of the transfer was $5,600. The evidence does not indicate that any part of the property was transferred as a gift.

In *J. Darsie Lloyd* v. *Commissioner*, 33 B. T. A. 903, acquiescence C. B. 1950-2, 3, and *Commissioner* v. *Estate of Bertha F. Kann*, 174 Fed. (2d) 357, it is held that no taxable gain is realized at the time of the transfer of property to an individual in exchange for the promise of such individual to make annuity payments to the transferor. It does not follow from the Lloyd and Kann cases that an annuitant may not be liable for a capital gains tax where the amount received under an annuity contract exceeds the annuitant's adjusted basis for the property transferred therefor. In *Estate of C. V. Hill* v. *Maloney*, 58 Fed. Supp. 164, where the decedent had transferred shares of stock to a syndicate organized by his sons in return for a down payment and an annuity, it was held that the payments received to the extent of the cost of the shares to the decedent constituted a return of capital, but that the excess of the amounts received (up to the value of the stock) over such cost was subject to tax as capital gain. The court further held that the amounts received in the form of annuity payments (the amounts received after the down payment) were subject to tax pursuant to section 22(b)(2) of the Revenue Act of 1936. The court reasoned that what the decedent did was the equivalent of selling his stock for cash and using the proceeds to purchase an annuity contract.

In the instant case it is held that the payments received under the contract constitute annuity payments under section 22(b)(2) of the Code, for which the "consideration paid" is the fair market value of the real property at the time of the transfer. Accordingly, the annual payments of $2,000 constitute ordinary income to the extent of 3 percent of the fair market value of the real property (3 percent of $40,000=$1,200) at the time of the transfer until the aggregate of that portion of the payments which is not taxed under section 22(b)(2) of the Code ($800 per annum) equals the fair market value of the property transferred. After such time the payments are taxable in full as ordinary income. It is further held that after the total of that part of the annuity payments which is not taxed under section 22(b)(2) of the Code equals the adjusted basis of the real property ($5,600), subsequent payments, to the extent that they exceed 3 percent of the fair market value of the property, are taxable as gain from the sale of such property until the total of the payments so taxed equals the excess of the fair market value of the property at the time of the transfer over the adjusted basis thereof. During the first 50 years $1,200 (3 percent of $40,000) of each annual payment of $2,000 is taxable as ordinary income under section 22(b)(2) of the Code. The remaining $800 of each annual payment is excludable from gross income during the first 7 years such payments are received. In the 8th to 50th years, inclusive, $800 of each annual payment is includible in gross income subject to the capital gains provisions of section 117 of the Code. After the 50th year the full annuity payment of $2,000 per year is taxable as ordinary income.

SECTION 117(j).—CAPITAL GAINS AND LOSSES: GAINS AND LOSSES FROM INVOLUNTARY CONVERSION AND FROM THE SALE OR EXCHANGE OF CERTAIN PROPERTY USED IN THE TRADE OR BUSINESS

REGULATIONS 118, SECTION 39.117(j)-1: Gains and losses from involuntary conversions and from the sale or exchange of certain property used in the trade or business.
(Also Section 112(b), Section 39.112(b)(6)-1; Section 113(a), Section 39.113(a)(15)-1; Section 3760, Section 39.3760-1.)

Rev. Rul. 259

INTERNAL REVENUE CODE

Where appreciated assets are distributed to a parent corporation in complete liquidation of a wholly-owned subsidiary which is indebted to the parent, the Internal Revenue Service will not take the position that the subsidiary realizes gain by reason of the appreciation of the assets applied in payment of the indebtedness, provided that the parent executes a closing agreement that is duly approved under section 3760 of the Internal Revenue Code stating that the basis of the subsidiary's assets in the hands of the parent will be the same as the subsidiary's basis in such assets.

I. T. 4109, C. B. 1952-2, 138, modified.

Advice is requested whether gain must be recognized, in accordance with I. T. 4109, C. B. 1952-2, 138, to a wholly-owned subsidiary corporation, which is indebted to its parent, upon the distribution of appreciated assets to the parent in a complete liquidation within the meaning of section 112(b)(6) of the Internal Revenue Code, where the parent agrees that the basis of the subsidiary's assets in the hands of the parent will be the same as the basis of such assets in the hands of the subsidiary immediately prior to the liquidation.

I. T. 4109, *supra*, holds that assets distributed to the parent corporation upon complete liquidation of a wholly-owned subsidiary corporation which is indebted to the parent must first be applied, at their fair market value, against the indebtedness to the parent, and if appreciated assets are so applied, the subsidiary realizes taxable gain to the extent of such appreciation. The remaining assets, if any, of the subsidiary distributed to the parent fall within the purview of section 112(b)(6) of the Code, provided the requirements of that section are met.

In view of the administrative difficulties incident to a strict application of the rule set forth in I. T. 4109, and in the interest of an orderly and efficient administration of the internal revenue laws, in cases to which I. T. 4109 would otherwise apply, the Internal Revenue Service will not take the position that the subsidiary realizes gain on the liquidation by reason of the application of appreciated assets to its indebtedness, if the parent corporation executes a closing agreement that is duly approved under the provisions of section 3760 of the Code stating that the basis of the subsidiary's assets in the hands of the parent will be the same as the basis of such assets in the hands of the subsidiary immediately prior to the liquidation.

However, in all cases where the parent's basis in the indebtedness of a solvent subsidiary is less than the face value thereof, it will be held that the parent realizes gain in the satisfaction of the indebtedness in

the liquidation measured by the difference between the basis of the indebtedness and its face value. (*Cf. Houston Natural Gas Corporation* v. *Commissioner*, 9 T. C. 570, affirmed 173 Fed. (2d) 461.)
I. T. 4109, C. B. 1952-2, 138, modified.

REGULATIONS 118, SECTION 39.117(j)-1: Gains and losses from involuntary conversions and from the sale or exchange of certain property used in the trade or business.

INTERNAL REVENUE CODE

Severance damages received upon condemnation by a State of a strip of land through a farm. (See Rev. Rul. 271, p. 36.)

SECTION 117(k).—CAPITAL GAINS AND LOSSES: GAIN OR LOSS IN THE CASE OF TIMBER OR COAL

REGULATIONS 118, SECTION 39.117(k)-1: Gain or loss upon the cutting and disposal of timber and the disposal of coal.

INTERNAL REVENUE CODE

Cutting and disposal of Christmas trees. (See Rev. Rul. 217, p. 12.)

SUPPLEMENT C.—CREDITS AGAINST TAX

SECTION 131(a).—TAXES OF FOREIGN COUNTRIES AND POSSESSIONS OF UNITED STATES: ALLOWANCE OF CREDIT

REGULATIONS 118, SECTION 39.131(a)-1: Analysis of credit for taxes. Rev. Rul. 272

INTERNAL REVENUE CODE

The tax imposed under the Haitian tax law of September 19, 1951, whether on the so-called "fixed rate basis" or on the actual net income determined under the provisions thereof, falls within the United States concept of an income tax and is allowable as a credit against United States income tax to the extent provided by section 131 of the Internal Revenue Code. No tax is imposed by the law of October 8, 1949, and thus, no basis exists therein for a credit under section 131 of the Code.

Advice is requested whether taxes paid under the Haitian laws of October 8, 1949, and September 19, 1951, qualify as income taxes within the purview of section 131 of the Internal Revenue Code.

The word "income" as defined in chapter I, article 1 of the Haitian law of September 19, 1951, covers any earnings, profit or income resulting from work; any earnings from personal property or real estate, any profit obtained from trade, business or industry, salaries

(including bonuses and gifts), profits obtained from agriculture, rentals or income, interest on capital, and any other periodical earnings.

All individuals, associations, companies, and enterprises, whether partnerships or not, obtaining an income by one of the above means are subject to the payment of the tax. The income may be composed of industrial and commercial profits and the amounts constituting an individual income, "taxed separately or of one or the other." The tax is payable on the above-mentioned income earned in Haiti regardless of the location of the establishment and even though the payee does not reside in that country.

In chapter III provision is made for certain individuals and enterprises to be taxed on a "fixed rate basis." The fixed rate income is calculated by multiplying by 5 the yearly rental value of the buildings and lands which such taxpayers occupy for their trade or industries or as otherwise provided in this chapter.

Under chapter IV, a tax is imposed on all stock corporations, companies and partnerships, or individual enterprises conducting a trade or industry in Haiti upon the basis of their net profit during the financial year as determined from the balance sheet. The net taxable profit is defined as the amount by which the income derived by a taxpayer during the financial year exceeds the usual expenses and charges in the administration and operation of the enterprise during the taxable period before deduction of reserves for amortization, repayment, or repurchase of bonds, and other amounts to be paid from the authorized capital. The expenses constituting the usual expenses and charges which are deductible from the gross income in view of determining the net taxable profit are the professional disbursements which are justified, customary, and necessary and which have a direct connection with the particular trade or industry of the taxpayer or are inherent in this trade or industry.

Chapter V of the Haitian law provides that persons receiving salaries, those employed by business firms, civil servants, and those who exercise a profession or have any lucrative noncommercial occupation, moneylenders, persons with private income, and all those who have an income not originating from industrial or commercial activities are subject to the tax on personal income. The estimated annual rental of houses received as gifts represents taxable income. Dividends are subjected to a tax of 5 percent which is withheld at the source and such dividends are not included in the personal income tax return. Also included in personal income are gross gifts, bonuses, gross income from investments, interest, pensions, and gross rentals (less one-third in lieu of deductions for depreciation, taxes, insurance, repairs) and any other income. Professional people who are self-employed and who also pay their tax on a fixed rate basis "will deduct" this tax from their personal income tax return.

Provision is made for the allowance of personal exemptions in the case of unmarried individuals, married couples, and dependents; and in lieu of deductions from personal income of contributions, taxes and imposts, insurance, or losses from fire, a 10 percent general deduction not to exceed a stated amount is allowed from the individual's adjusted income as explained in the law. Interest, professional expenses, and medical expenses to the extent specified are deductible.

Section 131 of the Internal Revenue Code provides in part as follows:

"(a) ALLOWANCE OF CREDIT.—If the taxpayer chooses to have the benefits of this section, the tax imposed by this chapter [chapter I of the Code] * * * shall be credited with:

"(1) CITIZENS AND DOMESTIC CORPORATIONS.—In the case of a citizen of the United States and of a domestic corporation, the amount of any income * * * taxes paid or accrued during the taxable year to any foreign country * * *"

In order for a tax paid or accrued to a foreign country to be allowable as a credit against United States income tax under section 131 of the Code, *supra*, it must be shown that the tax imposed by the foreign law is an income tax within the United States concept of that term, or is a tax in lieu of an income tax.

It is held that the tax imposed under the Haitian tax law of September 19, 1951, whether on the so-called "fixed rate basis" or on the actual net income determined under the provisions thereof, falls within the United States concept of an income tax and is allowable as a credit against United States income tax to the extent provided by section 131 of the Internal Revenue Code. *Cf. Herbert Ide Keen* v. *Commissioner*, 15 B. T. A. 1243, acquiescence, C. B. IX-1, 28 (1930). No tax is imposed by the law of October 8, 1949, and therefore, no question arises as to the credit under section 131 with respect to this law.

REGULATIONS 118, SECTION 39.131(a)-1: Analysis of credit for taxes. Rev. Rul. 273

INTERNAL REVENUE CODE

The withholding tax on royalties imposed by the Government of Japan, under the provisions of article 1, paragraph 2, item 6 of the Japanese income tax law falls within the United States concept of an income tax and is allowable as a credit against United States income tax to the extent provided by section 131 of the Internal Revenue Code.

SECTION 131(d).—TAXES OF FOREIGN COUNTRIES AND POSSESSIONS OF UNITED STATES: YEAR IN WHICH CREDIT TAKEN

REGULATIONS 118, SECTION 39.131(d)-1: When credit for taxes may be taken.

INTERNAL REVENUE CODE

Period in which credit for foreign taxes may be taken by taxpayer reporting income from sources outside the United States on the completed contract basis, for United States income tax purposes, and on the percentage of completion basis for the purposes of the foreign taxes. (See Rev. Rul. 288, p. 27.)

SUPPLEMENT D.—RETURNS AND PAYMENT OF TAX

SECTION 143.—WITHHOLDING OF TAX AT SOURCE

REGULATIONS 118, SECTION 39.143–1: T. D. 6047
Withholding tax at source.
(Also Section 144, Section 39.144–1.)

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 7.—TAXATION PURSUANT TO TREATIES.—SUBPART—CANADA

Release or refund of excess tax withheld, and exemption from, or reduction in rate of, withholding under sections 143 and 144 of the Internal Revenue Code in the case of residents of Canada and of corporations organized under the laws of Canada, as affected by the income tax convention and protocol between the United States and Canada proclaimed by the President of the United States of America on June 17, 1942, and amended by the supplementary convention between such Governments proclaimed by the President on November 29, 1951.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

On August 6, 1953, there was published in the Federal Register (18 F. R. 4620) a notice of proposed rulemaking containing withholding regulations with respect to the income tax convention between the United States and Canada, signed March 4, 1942, as modified and supplemented by the supplementary convention between such Governments, signed June 12, 1950. No objection to the rules proposed having been received, the regulations set forth below are hereby adopted:

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7.51. Exempt organizations.
7.52. Release of excess tax withheld at source.
7.53. Addressee not actual owner.
7.54. Return of tax withheld and information to be furnished in ordinary course.
7.55. Beneficiaries of a domestic estate or trust.
7.56. Refund of excess tax withheld prior to 1954.
7.57. Prior regulations.

SEC. 7.45. INTRODUCTORY.—The income tax convention and protocol between the United States and Canada, signed March 4, 1942, and proclaimed by the President of the United States on June 17, 1942, as modified and supplemented by the supplementary convention between such Governments, signed June 12, 1950, and proclaimed by the President on November 29, 1951, hereinafter referred to as the convention, provides in part as follows, effective for taxable years beginning on or after January 1, 1951:

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ARTICLE VI A

Pensions (including Government pensions) and life annuities derived from within one of the contracting States by a resident of the other contracting State shall be exempt from taxation in the former State.

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ARTICLE X

Income derived from sources within one of the contracting States by a religious, scientific, literary, educational, or charitable organization of the other contracting State shall be exempt from taxation in the State from which the income is derived if, within the meaning of the laws of both contracting States, such organization would have been exempt from income tax.

ARTICLE XI

1. The rate of income tax imposed by one of the contracting States, in respect of income derived from sources therein, upon individuals residing in, or corporations organized under the laws of, the other contracting State, and not having a permanent establishment in the former State, shall not exceed 15 percent for each taxable year.

2. Notwithstanding the provisions of paragraph 1 of this Article, income tax in excess of 5 percent shall not be imposed by one of the contracting States in respect of dividends paid by a subsidiary corporation organized under the laws of such State, or of a political subdivision thereof, to a parent corporation organized under the laws of the other contracting State, or of a political subdivision thereof: Provided, however, That this paragraph shall not apply if the competent authority in the former State is satisfied that the corporate relationship between the two corporations has been arranged or is maintained primarily with the intention of taking advantage of this paragraph.

3. Notwithstanding the provisions of Article XXII of this convention, paragraph 1 or paragraph 2, or both, of this Article, may be terminated without notice on or after the termination of the three-year period beginning with the effective date of this convention by either of the contracting States imposing a rate of income tax in excess of the rate of 15 percent prescribed in paragraph 1 or in excess of the rate of 5 percent prescribed in paragraph 2.

* * * * * * *

ARTICLE XII

1. Dividends and interest paid by a corporation organized under the laws of Canada to a recipient, other than a citizen or resident of the United States of America or a corporation organized under the laws of the United States of America, shall be exempt from all income taxes imposed by the United States of America.

2. Dividends and interest paid by a corporation organized under the laws of the United States of America whose business is not managed and controlled in Canada to a recipient, other than a resident of Canada or a corporation whose business is managed and controlled in Canada, shall be exempt from all taxes imposed by Canada.

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ARTICLE XIII A

1. A resident or corporation organized under the laws of Canada deriving from sources within the United States of America rentals from real property may elect for any taxable year to be subject to the tax imposed by the United States of America on a net basis as if such resident or corporation were engaged in trade or business within the United States of America through a permanent establishment therein during such taxable year.

2. Rentals from real property derived from sources within Canada by an individual or corporation resident in the United States of America shall receive tax treatment by Canada not less favorable than that accorded under section 99, The Income Tax Act, as in effect on the date on which this Article goes into effect.

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ARTICLE XIII C

Royalties for the right to use copyrights or in respect of the right to produce or reproduce any literary, dramatic, musical, or artistic work (but not inclusive of rents or royalties in respect of motion picture films) derived from sources within one of the contracting States by a resident or corporation or other entity of the other contracting State not engaged in trade or business in the former State through a permanent establishment shall be exempt from tax imposed by such former State.

* * * * * * *

ARTICLE XVIII

The competent authorities of the two contracting States may prescribe regulations to carry into effect the present convention within the respective States and rules with respect to the exchange of information.

The competent authorities of the two contracting States may communicate with each other directly for the purpose of giving effect to the provisions of the present convention.

* * * * * * *

ARTICLE XIX

With a view to the prevention of fiscal evasion, each of the contracting States undertakes to furnish to the other contracting State, as provided in the succeeding Articles of this convention, the information which its competent authorities have at their disposal or are in a position to obtain under its revenue laws insofar as such information may be of use to the authorities of the other contracting State in the assessment of the taxes to which this convention relates.

The information to be furnished under the first paragraph of this Article, whether in the ordinary course or on request, may be exchanged directly between the competent authorities of the two contracting States.

ARTICLE XX

1. The competent authorities of the United States of America shall forward to the competent authorities of Canada as soon as practicable after the close of each calendar year the following information relating to such calendar year:

The names and addresses of all persons whose addresses are within Canada and who derive from sources within the United States of America dividends, interest, rents, royalties, salaries, wages, pensions, annuities, or other fixed or determinable annual or periodical profits and income, showing the amount of such profits and income in the case of each addressee.

* * * * * * *

ARTICLE XXI

1. If the Minister in the determination of the income tax liability of any person under any of the revenue laws of Canada deems it necessary to secure the cooperation of the Commissioner, the Commissioner may, upon request, furnish the Minister such information bearing upon the matter as the Commissioner is entitled to obtain under the revenue laws of the United States of America.

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ARTICLE XXII

This convention and the accompanying protocol which shall be considered to be an integral part of the convention shall be ratified and the instruments of ratification shall be exchanged at Washington as soon as possible.

This convention and protocol shall become effective on the first day of January 1941. They shall continue effective for a period of three years from that date and indefinitely after that period, but may be terminated by either of the contracting States at the end of the three-year period or at any time thereafter provided that, except as otherwise specified in the case of Article XI, at least six months prior notice of termination has been given, the termination to become

effective on the first day of January following the expiration of the six-month period.

* * * * * * *

PROTOCOL

At the moment of signing the convention for the avoidance of double taxation, and the establishment of rules of reciprocal administrative assistance in the case of income taxes, this day concluded between the United States of America and Canada, the undersigned plenipotentiaries have agreed upon the following provisions and definitions:

1. The taxes referred to in this convention are:

(a) for the United States of America: the Federal income taxes, including surtaxes, and excess-profits taxes.

(b) for Canada: the Dominion income taxes, including surtaxes, and excess-profits taxes.

2. In the event of appreciable changes in the fiscal laws of either of the contracting States, the Governments of the two contracting States will consult together.

3. As used in this convention:

(a) the terms "person," "individual," and "corporation," shall have the same meanings, respectively, as they have under the revenue laws of the taxing State or the State furnishing the information, as the case may be;

(b) the term "enterprise" includes every form of undertaking, whether carried on by an individual, partnership, corporation or any other entity;

(c) the term "enterprise of one of the contracting States" means, as the case may be, "United States enterprise" or "Canadian enterprise";

(d) the term "United States enterprise" means an enterprise carried on in the United States of America by an individual resident in the United States of America, or by a corporation, partnership or other entity created or organized in or under the laws of the United States of America, or of any of the States or Territories of the United States of America;

(e) the term "Canadian enterprise" is defined in the same manner mutatis mutandis as the term "United States enterprise";

(f) the term "permanent establishment" includes branches, mines and oil wells, farms, timberlands, plantations, factories, workshops, warehouses, offices, agencies and other fixed places of business of an enterprise, but does not include a subsidiary corporation. The use of substantial equipment or machinery within one of the contracting States at any time in any taxable year by an enterprise of the other contracting State shall constitute a permanent establishment of such enterprise in the former State for such taxable year.

When an enterprise of one of the contracting States carries on business in the other contracting State through an employee or agent established there, who has general authority to contract for his employer or principal or has a stock of merchandise from which he regularly fills orders which he receives, such enterprise shall be deemed to have a permanent establishment in the latter State.

The fact that an enterprise of one of the contracting States has business dealings in the other contracting State through a commission agent, broker, or other independent agent or maintains therein an office used solely for the purchase of merchandise shall not be held to mean that such enterprise has a permanent establishment in the latter State.

4. The term "Minister," as used in this convention, means the Minister of National Revenue of Canada or his duly authorized representative. The term "Commissioner," as used in this convention, means the Commissioner of Internal Revenue of the United States of America, or his duly authorized representative. The term "competent authority," as used in this convention, means the Commissioner and the Minister and their duly authorized representatives.

5. The term "United States of America," when used in a geographical sense, includes only the States, the Territories of Alaska and Hawaii, and the District of Columbia. The term "Canada" when used in a geographical sense means the Provinces, the Territories, and Sable Island.

6. The term "subsidiary corporation" as used in Article XI of this convention means a corporation 95 percent of whose shares (other than Directors' qualifying shares) having full voting rights are beneficially owned by another corporation, provided that (except in the case of a corporation the chief business of which is

the making of loans) ordinarily not more than one-quarter of the gross income of such subsidiary corporation is derived from interest and dividends other than interest and dividends received from its subsidiary corporations.

7. (a) The term "rentals and royalties" referred to in Article II of this convention shall include rentals or royalties arising from leasing real or immovable, or personal or movable property or from any interest in such property, including rentals or royalties for the use of, or for the privilege of using, patents, copyrights, secret processes and formulae, goodwill, trade marks, trade brands, franchises and other like property;

(b) the term "interest," as used in this convention, shall include income arising from interest-bearing securities, public obligations, mortgages, hypothecs, corporate bonds, loans, deposits and current accounts;

(c) the term "dividends," as used in this convention, shall include all distributions of the earnings or profits of corporations.

8. The term "pensions" referred to in Article VI A of this convention means periodic payments made in consideration for services rendered or by way of compensation for injuries received.

9. The term "life annuities" referred to in Article VI A of this convention means a stated sum payable periodically at stated times, during life, or during a specified number of years, under an obligation to make the payments in consideration of a gross sum or sums paid by the recipient or under a contributory retirement plan.

10. The term "permanent establishment" as used in Article XI of this convention, shall not be deemed to include an office used solely for the purchase of merchandise.

11. The provisions of the present convention shall not be construed to restrict in any manner any exemption, deduction, credit or other allowance accorded by the laws of one of the contracting States in the determination of the tax imposed by such State.

12. The citizens of one of the contracting States residing within the other contracting State shall not be subjected to the payment of more burdensome taxes than the citizens of such other State.

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As used in this Treasury Decision, any term defined in the convention shall have the meaning so assigned to it; any term not so defined shall have the meaning which such term has under the Internal Revenue Code.

SEC. 7.46. DIVIDENDS.—(*a*) *General.*—The rate of United States income tax upon dividends derived from sources within the United States and received in taxable years beginning on or after January 1, 1951, by a nonresident alien (including a nonresident alien individual, fiduciary, and partnership) who is a resident of Canada, or by a corporation organized under the laws of Canada, shall not exceed 15 percent of the gross amount thereof for each taxable year under the provisions of Article XI of the convention if such alien or corporation at no time during the taxable year in which such dividends are derived has a permanent establishment in the United States. As to what constitutes a permanent establishment, see paragraphs (3) (f) and (10) of the protocol.

Thus, if a nonresident alien individual who is a resident of Canada performs personal services within the United States during the taxable year, but has at no time during such a year a permanent establishment within the United States, he is entitled to the reduced rate of tax with respect to dividends derived in that year from United States sources, as provided in Article XI of the convention, even though under the provisions of section 211(b) of the Internal Revenue Code he has engaged in trade or business within the United States during such year by reason of his having rendered personal services therein.

For provisions pertaining to dividends derived from sources within the United States by exempt organizations, see section 7.51.

(*b*) *Dividends paid by related corporation.*—Under the provisions of Article XI(2) of the convention, dividends derived from sources within the United States and paid by a corporation organized under the laws of the United States, or of a political subdivision thereof, to a parent corporation organized under the laws of Canada, or of a political subdivision thereof, which beneficially owns at the time the dividend is paid 95 percent or more of the shares (other than directors' qualifying shares) of the paying corporation which have full voting rights are, when received in taxable years beginning on or after January 1, 1951, subject to United States income tax at a rate not in excess of 5 percent if (1) ordinarily not more than 25 percent of the gross income of the paying corporation for the 3-year period immediately preceding the taxable year in which the dividend is paid consists of dividends and interest (other than dividends and interest received by such paying corporation from its own subsidiary corporations, if any), (2) the Commissioner of Internal Revenue is satisfied that the relationship between the paying corporation and the parent corporation has not been arranged or maintained primarily with the intention of securing the reduced rate of 5 percent, and (3) the parent corporation at no time during the taxable year in which such dividends are derived has a permanent establishment in the United States. The condition set forth under (1) above (relating to the character of the income) shall not apply, however, in the case of a paying corporation the chief business of which is the making of loans.

Any domestic corporation which claims or contemplates claiming that dividends paid or to be paid by it are subject to such rate not in excess of 5 percent shall file the following information with the Commissioner of Internal Revenue as soon as practicable: (1) the date and place of its organization; (2) the number of outstanding shares of stock of the domestic corporation having voting power and the voting power thereof; (3) the person or persons beneficially owning such stock of the domestic comporation and their relationship to the Canadian corporation; (4) the amount of the gross income by years of the domestic corporation for the 3-year period immediately preceding the taxable year in which the dividend is paid; (5) the amount of interest and dividends by years included in the gross income of the domestic corporation, and the amount of interest and dividends by years received by such corporation from its own subsidiary corporations, if any; and (6) the relationship between the domestic corporation and the Canadian corporation deriving the dividend from sources within the United States.

As soon as practicable after such information is filed, the Commissioner will determine whether the dividends concerned fall within the scope of the provisions of Article XI(2) of the convention and may authorize the release or refund of excess tax withheld with respect to dividends which come within such provisions. For additional requirements respecting the refund of excess tax withheld prior to 1954, see section 7.56.

In any case in which the Commissioner has notified the domestic corporation that the dividends fall within the scope of the provisions

of Article XI(2) of the convention, the reduced withholding rate of 5 percent, to the extent withholding of United States income tax is required, shall apply to any dividends subsequently paid by such corporation to the Canadian corporation, unless the stock ownership of the domestic corporation, or the character of its income, materially changes; or unless the Commissioner determines that the relationship between the two corporations concerned is being maintained primarily with the intention of securing the reduced rate of tax. In such instance, if such change in stock ownership or character of income occurs, the domestic corporation shall promptly notify the Commissioner of the then existing facts with respect thereto. The continued application of the rate not in excess of 5 percent is also dependent upon the continued fulfillment of condition (3) of the first paragraph of (*b*) of this section.

(*c*) *Effect of address in Canada on withholding in the case of dividends.*—For the purpose of withholding of United States income tax in the case of dividends every nonresident alien (including a nonresident alien individual, fiduciary, and partnership) whose address is in Canada shall be deemed by United States withholding agents to be a nonresident alien who is a resident of Canada not having a permanent establishment in the United States; and every foreign corporation whose address is in Canada shall be deemed by such withholding agents to be a corporation organized under the laws of Canada and not having a permanent establishment in the United States.

(*d*) *Rate of withholding.*—Withholding at source in the case of dividends derived from sources within the United States and paid on or after January 1, 1954, to nonresident aliens (including a nonresident alien individual, fiduciary, and partnership) and to foreign corporations, whose addresses are in Canada, shall be at the rate of 15 percent in every case except that in which, prior to the date of payment of such dividends, (1) the Commissioner of Internal Revenue has notified (i) the domestic corporation (pursuant to paragraph (*b*) of this section) that such dividends fall within the scope of the provisions of Article XI(2) of the convention or (ii) the withholding agent that the reduced rate of withholding shall not apply, or (2) the withholding agent has received the letter of notification prescribed in section 7.51(*b*).

The preceding provisions respecting the application of the reduced withholding rate in the case of dividends paid to nonresident aliens and foreign corporations with addresses in Canada are based upon the assumption that the payee of the dividend is the actual owner of the capital stock from which the dividend is derived and consequently is the person liable to United States income tax upon such dividend. As to action by the recipient who is not the owner of the dividend, see section 7.53.

The rate at which United States tax has been withheld from any dividend paid at any time after the expiration of the thirtieth day after the date on which this Treasury Decision is published in the Federal Register to any person whose address is in Canada at the time the dividend is paid shall be shown either in writing or by appropriate stamp on the check, draft, or other evidence of payment, or on an accompanying statement.

In the case of dividends paid on or after January 1, 1951, by a corporation organized under the laws of Canada no withholding of United States income tax is required. See Article XII(1) of the convention.

(*e*) *Definition of dividend.*—Under paragraph 7(c) of the protocol, the term "dividends," as used in the convention, includes all distributions of the earnings or profits of corporations.

SEC. 7.47. INTEREST.—(*a*) *General.*—The rate of United States income tax upon interest on bonds, securities, notes, debentures, or on any other form of indebtedness, including interest on obligations of the United States, obligations of instrumentalities of the United States, and mortgages and bonds secured by real property, which is derived from sources within the United States and received in taxable years beginning on or after January 1, 1951, by a nonresident alien (including a nonresident alien individual, fiduciary, and partnership) who is a resident of Canada, or by a corporation organized under the laws of Canada, shall not exceed 15 percent of the gross amount thereof for each taxable year under the provisions of Article XI of the convention if such alien or corporation at no time during the taxable year in which such interest is derived has a permanent establishment in the United States. As to what constitutes a permanent establishment, see paragraphs 3(f) and 10 of the protocol.

For provisions pertaining to interest derived from sources within the United States by exempt organizations, see section 7.51.

(*b*) *Application of reduced rate at source.*—To secure the reduced rate of United States income tax at source in the case of coupon bond interest, the nonresident alien who is a resident of Canada or the corporation organized under the laws of Canada shall for each issue of bonds file Form 1001-C in duplicate when presenting the interest coupons for payment. This form shall be signed by the owner of the interest, trustee, or agent and shall show the name and address of the obligor, the name and address of the owner of the interest, and the amount of the interest. It shall contain a statement that the owner (1) is a resident of Canada, or is a corporation organized under the laws of Canada, and (2) has no permanent establishment in the United States.

The reduction in the rate of United States income tax contemplated by Article XI of the convention, insofar as it concerns coupon bond interest, is applicable only to the owner of the interest. The person presenting the coupon or on whose behalf it is presented shall, for the purpose of the reduction in tax, be deemed to be the owner of the interest only if he is, at the time the coupon is presented for payment, the owner of the bond from which the coupon has been detached. If the person presenting the coupon or on whose behalf it is presented is not the owner of the bond, Form 1001, and not Form 1001-C, shall be executed.

The original and duplicate of Form 1001-C shall be forwarded by the withholding agent to the District Director of Internal Revenue, Audit Division, Alien Returns Section, Baltimore 2, Maryland, with the quarterly return on Form 1012. See section 39.143-7 of this chapter [Regulations 118]. Form 1001-C shall be listed on Form 1012.

For general provisions pertaining to the use, without reference to the provisions of the convention, of ownership certificate, Form 1001,

by nonresident aliens and nonresident foreign corporations, see section 39.143–4 and section 39.143–6 of this chapter.

To secure the reduced rate of United States income tax at source in the case of interest, other than coupon bond interest, the nonresident alien who is a resident of Canada or the corporation organized under the laws of Canada shall file Form 1001A–C in duplicate with the withholding agent in the United States. This form shall be signed by the owner of the interest, trustee, or agent and shall show the name and address of the obligor and the name and address of the owner of the interest. It shall contain a statement that the owner (1) is a resident of Canada, or is a corporation organized under the laws of Canada, and (2) has no permanent establishment in the United States.

Form 1001A–C shall be filed with the withholding agent for each successive 3-calendar-year period during which such interest is paid. For this purpose, the first such period shall commence with the beginning of the calendar year in which such income is first paid on or after January 1, 1954. Each such form filed with any withholding agent shall be filed not later than 20 days preceding the date of the first payment within each successive period, or, if that is not possible because of special circumstances, as soon as possible after such first payment. Once such a form has been filed in respect of any 3-calendar-year period, no additional Form 1001A–C need be filed in respect thereto unless the Commissioner of Internal Revenue notifies the withholding agent that another such form shall be filed by the taxpayer. If, after filing such form, the taxpayer ceases to be eligible for the benefit of Article XI of the convention, he shall promptly notify the withholding agent by letter in duplicate. When any change occurs in the ownership of the interest as recorded on the books of the payer, the reduction in rate of withholding of United States income tax shall no longer apply unless a Form 1001A–C is duly executed and filed with the withholding agent by the new owner of record of such interest.

The duplicate of each Form 1001A–C (and letter) shall be immediately forwarded by the withholding agent to the District Director of Internal Revenue, Audit Division, Alien Returns Section, Baltimore 2, Maryland.

In the case of interest paid on or after January 1, 1951, by a corporation organized under the laws of Canada no withholding of United States income tax is required. See Article XII(1) of the convention.

(*c*) *Definition of interest.*—Under paragraph 7(b) of the protocol, the term "interest," as used in the convention, includes income arising from interest-bearing securities, public obligations, mortgages, hypothecs, corporate bonds, loans, deposits, and current accounts.

SEC. 7.48. COPYRIGHT ROYALTIES.—(*a*) *General.*—Royalties for the right to use copyrights or in respect of the right to produce or reproduce any literary, dramatic, musical, or artistic work which are derived from sources within the United States and received in taxable years beginning on or after January 1, 1951, by a nonresident alien (including a nonresident alien individual, fiduciary, and partnership) who is a resident of Canada, or by a Canadian corporation or other entity, are exempt from United States tax under the provisions of Article

XIII C of the convention if such alien, corporation, or other entity at no time during the taxable year in which such royalties are derived is engaged in trade or business within the United States through a permanent establishment situated therein. Such royalties are, therefore, not subject to the withholding of United States tax at source. As to what constitutes a permanent establishment, see paragraph 3(f) of the protocol.

The provisions of this section shall have no application to rents or royalties in respect of motion picture films. For provisions pertaining to royalties derived from sources within the United States by exempt organizations, see section 7.51.

(*b*) *Application of exemption from withholding.*—To avoid withholding of United States tax at the source in the case of the royalties to which paragraph (*a*) is applicable, the nonresident alien who is a resident of Canada, or the Canadian corporation or other entity, shall file Form 1001A-C in duplicate with the withholding agent in the United States. The provisions of section 7.47(*b*) relating to the execution, filing, and effective period of such form with respect to interest are equally applicable with respect to the income falling within the scope of this section.

The duplicate of each Form 1001A-C (and letter) shall be immediately forwarded by the withholding agent to the District Director of Internal Revenue, Audit Division, Alien Returns Section, Baltimore 2, Maryland.

SEC. 7.49. NATURAL RESOURCE ROYALTIES, REAL PROPERTY RENTALS, SALARIES, WAGES, EMOLUMENTS, ETC.—(*a*) *General.*—Under Article XI of the convention the rate of United States income tax imposed upon natural resource royalties, real property rentals, salaries, wages, emoluments, premiums, compensations, remunerations, and other gains, profits, and income (other than gains, profits, and income otherwise exempt from United States income tax under the convention) which are derived from sources within the United States and received in taxable years beginning on or after January 1, 1951, by a nonresident alien (including a nonresident alien individual, fiduciary, and partnership) who is a resident of Canada, or by a corporation organized under the laws of Canada, shall not exceed 15 percent of the gross amount of such items for each taxable year if such alien or corporation at no time during the taxable year in which such items are derived has a permanent establishment in the United States. As to what constitutes a permanent establishment, see paragraphs 3(f) and 10 of the protocol.

For the application of the reduced rate of United States income tax at source with respect to dividends and interest, see sections 7.46 and 7.47, respectively. For the application of the exemption from United States tax at source with respect to copyright royalties, pensions, and life annuities, see sections 7.48 and 7.50, respectively. For provisions pertaining to income derived from sources within the United States by exempt organizations, see section 7.51.

(*b*) *Application of reduced rate at source.*—To secure the reduced rate of United States income tax at source in the case of the items of income to which paragraph (*a*) is applicable, the nonresident alien who is a resident of Canada or the corporation organized under the laws of Canada shall file Form 1001A-C in duplicate with the with-

holding agent in the United States. The provisions of section 7.47(*b*) relating to the execution, filing, and effective period of such form with respect to interest are equally applicable with respect to the income falling within the scope of this section.

The provisions of this paragraph shall have no application in the case of wages paid to nonresident aliens who are residents of Canada and who enter and leave the United States at frequent intervals. See section 405.102(g) of this chapter [Regulations 116]. The provisions of section 39.143–3 of this chapter [Regulations 118] relating to the allowance of the exemptions under section 25(b) on a prorated basis, when determining the tax to be withheld at source with respect to remuneration for labor or personal services performed within the United States by a nonresident alien, shall have no application when a Form 1001A–C has been filed with the withholding agent pursuant to this paragraph with respect to such remuneration.

The duplicate of each Form 1001A–C (and letter) shall be immediately forwarded by the withholding agent to the District Director of Internal Revenue, Audit Division, Alien Returns Section, Baltimore 2, Maryland.

SEC. 7.50. PENSIONS AND LIFE ANNUITIES.—(*a*) *General.*—Private and Government pensions, and life annuities, derived from sources within the United States and received in taxable years beginning on or after January 1, 1951, by a nonresident alien individual who is a resident of Canada are exempt from United States tax under the provisions of Article VI A of the convention. Such items of income are, therefore, not subject to the withholding of United States tax at source.

(*b*) *Application of exemption from withholding.*—To avoid withholding of United States tax at source in the case of the items of income to which paragraph (*a*) is applicable, the nonresident alien individual who is a resident of Canada shall notify the withholding agent by letter in duplicate that such income is exempt from United States tax under the provisions of Article VI A of the convention. The letter of notification shall be signed by the owner of the income, shall show the name and address of both the payer and the owner of the income, and shall contain a statement that the owner, an individual, is neither a citizen nor a resident of the United States but is a resident of Canada.

If such letter is also to be used as authorization for the release, pursuant to section 7.52(*a*), of excess tax withheld from such items of income, it shall also contain a statement that the owner was, at the time when the income was received from which the excess tax was withheld, neither a citizen nor a resident of the United States but was a resident of Canada.

This letter shall constitute authorization for the payment of such items of income without withholding a United States tax at source unless the Commissioner of Internal Revenue subsequently notifies the withholding agent that the tax shall be withheld with respect to payments of such items of income made after receipt of such notice. If, after filing a letter of notification, the owner of the income ceases to be eligible for the exemption from United States tax provided by the convention in respect to such income, he shall promptly notify the withholding agent by letter in duplicate. When any change occurs in the

ownership of such income as recorded on the books of the payer, the exemption from withholding of United States tax shall no longer apply unless a letter of notification is duly executed and filed with the withholding agent by the new owner of record of such income.

Each letter of notification, or the duplicate thereof, shall be immediately forwarded by the withholding agent to the District Director of Internal Revenue, Audit Division, Alien Returns Section, Baltimore 2, Maryland.

(*c*) *Definition of pensions and life annuities.*—Under paragraph 8 of the protocol, the term "pensions," as used in Article VI A of the convention, means periodic payments made in consideration for services rendered or by way of compensation for injuries received.

Under paragraph 9 of the protocol, the term "life annuities," as used in Article VI A of the convention, means a stated sum payable periodically at stated times, during life, or during a specified number of years, under an obligation to make the payments in consideration of a gross sum or sums paid by the recipient or under a contributory retirement plan.

SEC. 7.51. EXEMPT ORGANIZATIONS.—(*a*) *General.*—Income derived from sources within the United States and received in taxable years beginning on or after January 1, 1951, by a religious, scientific, literary, educational, or charitable organization of Canada is exempt from United States tax under the provisions of Article X of the convention if, within the meaning of the laws of both the United States and Canada, such organization would have been exempt from income tax.

Paragraph 11 of the protocol provides that the provisions of the convention shall not be construed to restrict in any manner any exemption, deduction, credit, or other allowance accorded by the laws of one of the contracting States in the determination of the tax imposed by such State. In view of the provisions of such paragraph, the provisions of section 101 of the Internal Revenue Code, relating to exemptions from tax on corporations, apply to every Canadian organization coming within the scope of that section and otherwise qualifying for the exemption granted by Article X of the convention, regardless of whether Canada recognizes such organization as exempt from income taxes imposed by its own laws.

In view of the above, fixed or determinable annual or periodical income derived from sources within the United States by a nonresident Canadian organization which qualifies for the exemption granted by Article X of the convention is not subject to the withholding of United States tax at source.

(*b*) *Application of exemption from withholding.*—To avoid withholding of United States tax at source in the case of fixed or determinable annual or periodical income derived from sources within the United States, other than coupon bond interest, the nonresident Canadian organization which qualifies for the exemption from United States tax shall notify the withholding agent by letter in duplicate that such income is exempt from United States tax under the provisions of Article X of the convention. The letter of notification shall be signed by the owner of the income, trustee, or agent and shall show the name and address of the obligor and the name and address of the owner of the income. It shall contain a copy of the determination of the Commissioner of Internal Revenue that such organization is

exempt from taxation under chapter 1, relating to the income tax, of the Internal Revenue Code and a statement that the owner of the income (1) is a Canadian organization and (2) has at no time during the current taxable year been engaged in trade or business within the United States. This letter shall constitute authorization for the payment of such income to such organization without withholding of United States tax at source.

The provisions of section 7.47(*b*) relating to the filing and effective period of Form 1001A–C prescribed therein with respect to interest are equally applicable with respect to the letter of notification prescribed herein.

Each letter of notification, or the duplicate thereof, shall be immediately forwarded by the withholding agent to the District Director of Internal Revenue, Audit Division, Alien Returns Section, Baltimore 2, Maryland.

To avoid withholding of United States tax at source in the case of coupon bond interest, the nonresident Canadian organization which qualifies for the exemption from United States tax granted by Article X of the convention shall inscribe on each copy of the Form 1001–C required by section 7.47(*b*) a notation substantially as follows: "As this organization, which is not engaged in trade or business within the United States, has been held to be exempt from taxation under chapter 1 of the Internal Revenue Code by the Commissioner of Internal Revenue under date of _____ __, 19__, the interest on this certificate is not subject to withholding of United States tax." The organization shall give therewith the date of the official letter in which the organization was held to be so exempt.

Form 1001–C, when so used to substantiate an exemption from withholding of United States tax, need not be listed on Form 1012 when forwarded to the district director pursuant to section 7.47(*b*).

To the extent not inconsistent herewith, the provisions of section 7.47(*b*) relating to Form 1001 and Form 1001–C are equally applicable under this paragraph.

SEC. 7.52. RELEASE OF EXCESS TAX WITHHELD AT SOURCE.—(*a*) *General.*—In order to give the convention effective application at the earliest practicable date, the exemptions from, and reductions in the rate of, withholding of United States tax at source granted by this Treasury Decision are hereby made effective beginning January 1, 1954, contingent upon compliance with the applicable provisions of section 7.46 through section 7.51.

In the case of dividends derived from sources within the United States and paid to a nonresident alien (including a nonresident alien individual, fiduciary, and partnership) or to a foreign corporation, whose address at the time of payment was in Canada, if United States income tax at the statutory rate (30 percent as of the date of approval of this Treasury Decision) has been withheld from such dividends on or after January 1, 1954, there shall be released (except as provided in paragraphs (*b*) and (*c*)) by the withholding agent and paid over to the person from whom it was withheld an amount which is equal to the amount obtained by subtracting 15 percent of such dividends from the tax so withheld.

In the case of every taxpayer whose address at the time of payment was in Canada and who furnishes to the withholding agent Form

1001A-C in accordance with section 7.47(*b*), section 7.48(*b*), and section 7.49(*b*), if United States income tax at the statutory rate (30 percent as of the date of approval of this Treasury Decision) or at 15 percent has been withheld on or after January 1, 1954, from the items of income in respect of which such form is prescribed in such sections, there shall be released by the withholding agent and paid over to the person from whom it was withheld—

(1) in the case of copyright royalties and the like, an amount equal to the tax so withheld from such items; and

(2) in the case of other items of income (other than dividends, pensions, life annuities, and coupon bond interest), an amount which is equal to the amount obtained by subtracting 15 percent of such items in the aggregate from the tax so withheld from such items.

In the case of every taxpayer whose address at the time of payment was in Canada and who furnishes to the withholding agent Form 1001-C clearly marked "SUBSTITUTE" and executed in accordance with section 7.47(*b*), if United States income tax at the statutory rate (28 percent or 30 percent, as the case may be, as of the date of approval of this Treasury Decision) has been withheld from coupon bond interest on or after January 1, 1954, there shall be released (except as provided in paragraph (*b*)) by the withholding agent and paid over to the person from whom it was withheld an amount which is equal to the difference between the amount of such interest multiplied by the higher of such statutory rates (30 percent as of the date of approval of this Treasury Decision) and 15 percent of such interest. One such substitute form shall be filed in duplicate with respect to each issue of bonds and will serve with respect to that issue to replace all Forms 1001 previously filed by the taxpayer in the calendar year in which the excess tax was withheld and with respect to which such excess is released.

The original and duplicate of such substitute Form 1001-C shall be forwarded by the withholding agent to the District Director of Internal Revenue, Audit Division, Alien Returns Section, Baltimore 2, Maryland, with the quarterly return on Form 1012. See section 39.143-7 of this chapter. Such substitute Form 1001-C shall be listed on Form 1012.

In the case of every taxpayer whose address at the time of payment was in Canada and who furnishes to the withholding agent the letter of notification prescribed in section 7.50(*b*) as authorization for the release of excess tax withheld, if United States tax at the statutory rate (30 percent as of the date of approval of this Treasury Decision) or at 15 percent has been withheld on or after January 1, 1954, from Government pensions, private pensions, or life annuities, there shall be released by the withholding agent and paid over to the person from whom it was withheld an amount equal to the tax so withheld from such items.

The provisions of this section (other than paragraph (*d*)) shall have no application to excess tax withheld at source which has been paid by the withholding agent to the district director of internal revenue pursuant to section 39.143-7 of this chapter.

(*b*) *Exempt organizations.*—In the case of every exempt organization whose address at the time of payment was in Canada and which

furnishes to the withholding agent a letter of notification in accordance with section 7.51(*b*), if United States tax at the statutory rate (30 percent as of the date of approval of this Treasury Decision) or at 15 percent has been withheld on or after January 1, 1954, from fixed or determinable annual or periodical income derived from sources within the United States, there shall be released (except in the case of coupon bond interest) by the withholding agent and paid over to the organization from which it was withheld an amount equal to the tax so withheld, if the date on which the Commissioner of Internal Revenue has held such organization to be exempt from taxation under chapter 1 is not subsequent to the date on which payment of such income was made.

In the case of every exempt organization whose address at the time of payment was in Canada and which furnishes to the withholding agent Form 1001-C clearly marked "SUBSTITUTE" and executed in accordance with section 7.47(*b*) and section 7.51(*b*), if United States tax has been withheld from coupon bond interest on or after January 1, 1954, there shall be released by the withholding agent and paid over to the organization from which it was withheld an amount equal to the tax so withheld, if the date on which the Commissioner of Internal Revenue has held such organization to be exempt from taxation under chapter 1 is not subsequent to the date on which payment of such interest was made. One such substitute form shall be filed in duplicate with respect to each issue of bonds and will serve with respect to that issue to replace all Forms 1001 previously filed by the taxpayer in the calendar year in which the excess tax was withheld and with respect to which such excess is released.

The original and duplicate of such substitute Form 1001-C shall be forwarded by the withholding agent to the District Director of Internal Revenue, Audit Division, Alien Returns Section, Baltimore 2, Maryland, with the quarterly return on Form 1012. See section 39.143-7 of this chapter. Such substitute Form 1001-C need not be listed on Form 1012.

(*c*) *Dividends paid by related corporation.*—In the case of every domestic corporation receiving notification from the Commissioner of Internal Revenue under the provisions of section 7.46(*b*) that dividends paid or to be paid by it fall within the scope of the provisions of Article XI(2) of the convention, if United States income tax in excess of the applicable rate of 5 percent has been withheld on or after January 1, 1954, from dividends which come within the scope of such provisions, the withholding agent shall, if so authorized in such notification, release and pay over to the corporation from which it was withheld the excess tax withheld with respect to such dividends.

(*d*) *Amounts withheld before 1954.*—For provisions respecting the refund of excess tax withheld during calendar years prior to 1954, see section 7.56.

SEC. 7.53. ADDRESSEE NOT ACTUAL OWNER.—(*a*) *General.*—If the recipient in Canada of any dividend from sources within the United States, with respect to which United States income tax at the reduced rate of 15 percent has been withheld at source pursuant to section 7.46(*d*), is a nominee or representative through whom such dividend flows to a person other than one described in section 7.46(*a*) as being entitled to such reduced rate, such recipient in Canada shall withhold an additional amount of United States income tax equivalent to the

United States income tax which would have been withheld if the convention had not been in effect (30 percent of such dividend as of the date of approval of this Treasury Decision) minus the 15 percent which has been withheld at the source.

In any case in which a fiduciary or partnership with an address in Canada receives, otherwise than as a nominee or representative, a dividend from sources within the United States with respect to which United States income tax at the reduced rate of 15 percent has been withheld at source pursuant to section 7.46(*d*), if a beneficiary of such fiduciary or a partner in such partnership is not entitled to the reduced rate of tax granted by Article XI of the convention, the fiduciary or partnership shall withhold an additional amount of United States income tax with respect to the portion of such dividend included in such beneficiary's share of the distributed or distributable income, or in such partner's distributive share of the income, of such fiduciary or partnership, as the case may be. The amount of the additional tax is to be calculated in the same manner as under the immediately preceding paragraph of this section.

If any amount of United States income tax is released pursuant to section 7.52(*a*) by the withholding agent in the United States with respect to a dividend paid to such a person (nominee, representative, fiduciary, or partnership) with an address in Canada, the latter shall also withhold from such released amount any additional amount of United States income tax, otherwise required to be withheld by the preceding provisions of this section in respect of such dividend, in the same manner as if at the time of payment of such dividend United States income tax at the rate of only 15 percent had been withheld at source therefrom.

Nothing in this Treasury Decision shall be deemed to prevent the application of section 7.511, relating to Canadian withholding agents, of Treasury Decision 5532 [C. B. 1946-2, 73], approved August 23, 1946 [26 CFR 7.511].

(*b*) *Returns filed by Canadian withholding agents.*—The amounts so withheld by such withholding agents in Canada during the year 1954 and each subsequent calendar year during which the convention is in effect shall be forwarded, after being converted into United States dollars, to the District Director of Internal Revenue, Baltimore 2, Maryland, U. S. A., on or before March 15 of the following year, together with United States return Form 1042 on which shall be listed the names, addresses, and other information required on such form in respect to the persons from whom such additional amounts have been withheld by such agents in Canada.

SEC. 7.54. RETURN OF TAX WITHHELD AND INFORMATION TO BE FURNISHED IN ORDINARY COURSE.—(*a*) *Return of tax withheld.*—In addition to making the annual return on Form 1042 prescribed by section 39.143-7 of this chapter, every United States withholding agent shall make and file in duplicate with the district director of internal revenue an information return on Form 1042 Supplement, with respect to Canadian addresses, for the calendar year 1954 and each subsequent calendar year during which the convention is in effect.

There shall be reported on such Form 1042 Supplement all items of fixed or determinable annual or periodical income derived from

sources within the United States and paid to nonresident aliens (including nonresident alien individuals, fiduciaries, and partnerships) and to nonresident foreign corporations (including exempt organizations), whose addresses at the time of payment were in Canada, including (1) such items of income as are required to be listed on Form 1042, (2) such items of income as constitute interest required to be listed on Form 1012, and (3) such items of income upon which, in accordance with this Treasury Decision, no withholding of United States tax is required; except that any of such items which constitute wages subject to withholding of United States tax pursuant to section 1622, Internal Revenue Code, and interest in respect of which Form 1001–C or substitute Form 1001–C has been filed in duplicate with the withholding agent are not required to be reported on such Form 1042 Supplement.

(*b*) *Information to be furnished in ordinary course.*—In compliance with the provisions of Articles XIX and XX of the convention the Commissioner of Internal Revenue will transmit to the Minister of National Revenue of Canada, as soon as practicable after the close of the calendar year 1954 and of each subsequent calendar year during which the convention is in effect, the following information relating to such preceding calendar year:

(1) The duplicate copy of each available Form 1042 Supplement filed pursuant to paragraph (*a*) of this section; and

(2) The duplicate copy of each available ownership certificate, Form 1001–C, filed pursuant to section 7.47(*b*) or section 7.51(*b*), and substitute Form 1001–C, filed pursuant to section 7.52(*a*) or section 7.52(*b*), in connection with coupon bond interest.

SEC. 7.55. BENEFICIARIES OF A DOMESTIC ESTATE OR TRUST.—A nonresident alien who is a resident of Canada and who is a beneficiary of a domestic estate or trust shall be entitled to the exemption from, or reduction in the rate of, United States tax granted by Articles XI, XII, and XIII C of the convention with respect to dividends, interest, copyright royalties, and other gains, profits, and income, to the extent such item or items are included in his share of the distributed or distributable income of such estate or trust, provided that he otherwise satisfies the requirements of these respective articles. In order to be entitled in such instance to the exemption from, or reduction in the rate of, withholding of United States tax such beneficiary must otherwise satisfy such requirements and shall, where applicable, execute and submit to the fiduciary of such estate or trust in the United States the Form 1001A–C prescribed in section 7.47(*b*), section 7.48(*b*), and section 7.49(*b*).

SEC. 7.56. REFUND OF EXCESS TAX WITHHELD PRIOR TO 1954.—If United States income tax withheld at the source prior to 1954 from dividends, interest, copyright royalties and the like, natural resource royalties, real property rentals, salaries, wages, pensions, life annuities, or other gains, profits, and income, is in excess of the tax imposed by chapter 1 (relating to the income tax) of the Internal Revenue Code, as modified by the convention, a claim by the taxpayer for the refund of any overpayment resulting therefrom shall be made under section 322 of the Internal Revenue Code by filing Form 843 together with Form 1040NB, Form 1040B, Form 1120, Form

1120NB, or other appropriate return, whichever is applicable, or with an amended return.

The taxpayer's total gross income from sources within the United States shall be disclosed on the return. In the event that securities are held in the name of a person other than the actual or beneficial owner, the name and address of such person shall be furnished with the claim. There shall also be included in such claim for refund:

(*a*) A statement that, at the time when the item or items of income were derived from which the excess tax was withheld, (1) the taxpayer was neither a citizen nor a resident of the United States but was a resident of Canada, or, in the case of a corporation, (2) the taxpayer was a corporation organized under the laws of Canada; and

(*b*) A statement that the taxpayer at no time during the taxable year in which such income was derived had a permanent establishment in the United States.

If, however, the taxpayer is an individual who during the taxable year derived from sources within the United States income which consists exclusively of pensions or life annuities entitled to the benefit of Article VI A of the convention, the statement specified in (*b*) above shall not be required.

If the taxpayer is an exempt organization claiming the benefit of Article X of the convention, the statement specified in (*b*) above shall not be required, but such organization shall include with such claim a copy of the Commissioner's determination referred to in section 7.51(*b*) and shall indicate whether it was engaged in trade or business within the United States at any time during the taxable year in which the income concerned was derived.

As to additional information required in the case of a Canadian corporation claiming the benefit of the 5 percent rate on dividends paid by a domestic corporation, see section 7.46(*b*).

SEC. 7.57. PRIOR REGULATIONS.—Except to the extent necessary for the application of section 7.511 of Treasury Decision 5532 [26 CFR 7.511], the provisions of Treasury Decision 5157 [C. B. 1942–2, 137], approved June 27, 1942 [26 CFR 7.10 through 7.17], are hereby superseded as the respective provisions of this Treasury Decision become effective.

(This Treasury Decision is issued under the authority contained in secs. 62 and 3791 of the Internal Revenue Code (53 Stat. 32, 467; 26 U. S. C. 62, 3791) and Article XVIII of the income tax convention and protocol between the United States and Canada, signed March 4, 1942, and proclaimed by the President of the United States on June 17, 1942.)

JUSTIN F. WINKLE,
Acting Commissioner of Internal Revenue.

Approved November 5, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register November 10, 1953, 8:52 a. m.)

REGULATIONS 118, SECTION 39.143-7: Return and payment of tax withheld. T. D. 6055

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 7.—TAXATION PURSUANT TO TREATIES

Exchange of information under income tax conventions

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

SEC. 7.1. EXCHANGE OF INFORMATION.—(*a*) *Form 1042 Supplement.*—For the calendar year 1953 and subsequent calendar years every United States withholding agent shall make and file with the district director of internal revenue for the district in which the withholding agent is located an information return on Form 1042 Supplement with respect to each foreign country which has, or will have, entered into an income tax convention with the United States, if such convention provides for the mutual exchange of information and if the Commissioner of Internal Revenue determines that such return is required in the case of such country.

Form 1042 Supplement shall be filed simultaneously with the Form 1042 prescribed by section 39.143-7 of this chapter. A separate return shall be made on Form 1042 Supplement in duplicate with respect to each such country as the Commissioner of Internal Revenue shall designate, and there shall be reported thereon all items of fixed or determinable annual or periodical income derived from sources within the United States and paid to nonresident aliens (including nonresident alien individuals, fiduciaries, and partnerships) and to nonresident foreign corporations, whose addresses at the time of payment were in such country, including such items of income upon which United States tax has not been withheld at source because of the income tax convention with such country; except that any of such items which constitute wages subject to withholding of United States tax pursuant to section 1622, Internal Revenue Code, and interest in respect of which an ownership certificate other than Form 1001, such as Form 1001-D, Form 1001-IR, or Form 1001-UK, or the substitute thereof, has been filed in duplicate with the withholding agent is not required to be reported on such Form 1042 Supplement.

As soon as practicable after the close of the calendar year 1953 and subsequent calendar years during which the income tax convention between the United States and such country is in effect, the Commissioner of Internal Revenue will transmit to the appropriate authority designated in the convention with such country the duplicate copy of each available Form 1042 Supplement filed pursuant to this section in respect to such country for such preceding calendar year.

Form 1042B, Form 1042C, Form 1042D, Form 1042E, and Form 1042F, which are currently prescribed under this part as information returns for use under the income tax convention between the United States and Canada, France, the United Kingdom, the Netherlands,

and Switzerland, respectively, will not be required for 1953 and subsequent years.

(*b*) *Form 1042.*—For the calendar year 1953 and subsequent calendar years every United States withholding agent shall report on Form 1042 all such items of income, otherwise required to be reported thereon pursuant to section 39.143–7 of this chapter, upon which United States tax has not been withheld at source because of any income tax convention which is in effect between the United States and a foreign country. There shall also be reported on such form interest on registered bonds with respect to which an exemption certificate, such as Form 1001 A–D, or an exemption or reduced rate certificate, such as Form 1001 A–S, has been filed with the withholding agent.

(*c*) *Prior regulations.*—The provisions of this section shall apply notwithstanding any regulation to the contrary which has been approved prior to the date on which this Treasury Decision is published in the Federal Register.

Because this Treasury Decision is basically in accordance with procedures now being followed by withholding agents, it is hereby found that it is unnecessary to issue this Treasury Decision with notice and public procedure thereon under section 4(a) of the Administrative Procedure Act, approved June 11, 1946, or subject to the effective date limitation of section 4(c) of that act.

(This Treasury Decision is issued under the authority contained in secs. 62 and 3791 (53 Stat. 32, 467; 26 U. S. C. 62, 3791) of the Internal Revenue Code and in the provisions relating to exchange of information which are found in the respective income tax conventions between the United States and the foreign countries here concerned.)

T. Coleman Andrews,
Commissioner of Internal Revenue.

Approved December 1, 1953.

M. B. Folsom,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register December 7, 1953, 8:48 a. m.)

SECTION 144.—PAYMENT OF CORPORATION INCOME TAX AT SOURCE

Regulations 118, Section 39.144–1: Witholding in the case of nonresident foreign corporation.

INTERNAL REVENUE CODE

Release or refund of excess tax withheld, and exemption from, or reduction in rate of, withholding in the case of residents of Canada and of corporations organized under the laws of Canada, as affected by the income tax convention and protocol between the United States and Canada. (See T. D. 6047, p. 59.)

REGULATIONS 118, SECTION 39.144-1: Withholding in the case of nonresident foreign corporation.

INTERNAL REVENUE CODE

Interest derived from earnings of ships under a foreign flag. (See Rev. Rul. 274, p. 81.)

SUPPLEMENT E.—ESTATES AND TRUSTS

SECTION 162.—NET INCOME

REGULATIONS 118, SECTION 39.162-1: Income of estates and trusts. (Also Section 23(a), Section 39.23(a)-15; Section 812(b), Section 81.29, Regulations 105.) — Rev. Rul. 240

INTERNAL REVENUE CODE

Treatment of the deduction for executor's commissions and attorney's fees for Federal estate tax and income tax purposes in view of the provisions of section 162(e) of the Internal Revenue Code.

Advice is requested relative to the treatment for Federal estate tax and income tax purposes of the deduction for executor's commissions and attorney's fees in view of the provisions of section 162(e) of the Code under the circumstances hereinafter described.

In the first case the decedent died on October 1, 1948, and on the estate tax return for his estate filed on November 10, 1949, deductions were claimed under Schedule J of the return for executor's commissions and attorney's fees in the amount of $100x$ dollars. Of this amount $50x$ dollars had been paid at the time of the internal revenue agent's examination of the estate tax return. The amounts paid in 1949, totaling $85x$ dollars, were not claimed as deductions in the fiduciary income tax return originally filed for that year. In August of 1951, the representatives of the estate filed a statement with the internal revenue agent waiving the right to deductions in the estate tax return for the executor's commissions and attorney's fees which were paid in 1949 and elected to claim the deductions for such amounts in the fiduciary income tax return for that year.

Section 162 of the Internal Revenue Code, relating to the computation of net income of estates and trusts, provides in part as follows:

SEC. 162. NET INCOME.

The net income of the estate or trust shall be computed in the same manner and on the same basis as in the case of an individual, except that—

* * * * * * *

(e) Amounts allowable under section 812(b) as a deduction in computing the net estate of a decedent shall not be allowed as a deduction under section 23, except subsection (w), in computing the net income of the estate unless there is filed, within the time and in the manner and form prescribed by the Commissioner, a statement that the items have not been claimed or allowed as deductions under section 812(b) and a waiver of the right to have such items allowed at any time as deductions under section 812(b).

This section was added by the Revenue Act of 1942 and its purpose was the prevention of a double deduction. Under a strict interpreta-

tion of the statute the words "claimed or allowed" might be construed to mean that an item could not be allowed as a deduction in computing the net income of an estate if the item had been "claimed" as a deduction in computing gross estate. Such an interpretation would not give proper effect to the phrase as a whole or to the intent of Congress. It would make the need for the word "allowed" questionable, since, except in unusual circumstances, a deduction would not be allowed unless it has in some way been "claimed," either on the original return or by information presented prior to audit of the return. It is not believed that it was intended that the taxpayer's privilege of election should be restricted to the extent of making a mere "claim" for deduction irrevocable in all circumstances. A proper interpretation of the statute does not require a conclusion that a mere claim of deduction for estate tax purposes, or a claim plus the fact that the payment has been made, constitutes a binding election. The purpose and language of the statute will be served if an estate is permitted such leeway in the adjustment of allowable deductions between the estate tax return and the fiduciary return as is compatible with efficient administration and the prevention of a double deduction.

Accordingly, notwithstanding that deductions were claimed on the estate tax return of the decedent as filed and that some of the amounts had been paid, the estate is not precluded from deducting such amounts for income tax purposes provided, at the time the required statement and waiver are filed, such amounts have not been allowed as deductions for estate tax purposes, and provided the taxpayer takes such action as is necessary to make it clear that the same amounts are not currently being claimed as deductions on the estate tax return.

In the second case the testator died on January 4, 1949, and on the estate tax return filed on March 1, 1950, no deduction was taken for executor's commissions and attorney's fees, it being stated in Schedule J of the return that these deductions were to be taken for income tax purposes. Thereafter, a fiduciary income tax return was filed, in which income of $5x$ dollars was reported and administrator's commissions and attorney's fees totaling $15x$ dollars were claimed as deductions, showing net income as minus $10x$ dollars. A statement was filed with this fiduciary return and any right to claim them as estate tax deductions was waived. The beneficiaries of the estate in their individual income tax returns reported no distribution of income of the decedent and were advised that they could not claim the excess of the administration costs over the income of the estate as individual deductions.

The statement on Schedule J of the estate tax return that the deductions will be taken on the income tax return and the mere "claim" of the deductions on the fiduciary income tax return are not irrevocable. The deduction could not be allowed under section 23 of the Code in computing net income of the estate until the statement and waiver are filed. Under section 39.162–1, Regulations 118, such statement and waiver are not required to be filed with the income tax return, but may be filed at any time prior to the expiration of the statutory period of limitation applicable to the income tax return in which the deduction is sought. However, after the statement and waiver are filed with respect to a particular item of administration expense, the deduction cannot be transferred and allowed under section

812(b) of the Code in computing the net estate, because under the terms of section 162(e) of the Code the waiver operates as a relinquishment of the right to have the items allowed *at any time* as deductions under section 812(b) of the Code.

In the event that administrative expenses are such that they would be allowable for either income or estate tax purposes, the taxpayer may allocate the expenses to either the estate tax return or the income tax return for the year in which payment is made, or to both in such proportions as he desires, provided there is no duplication of deduction and provided the terms of section 162(e) of the Code are complied with. *Cf.* I. T. 4048, C. B. 1951-1, 39.

SUPPLEMENT I.—FOREIGN CORPORATIONS

SECTION 231.—TAX ON FOREIGN CORPORATIONS

REGULATIONS 118, SECTION 39.231-3: Exclusion of earnings of foreign ships or aircraft from gross income. (Also Section 144, Section 39.144-1.) — Rev. Rul. 274

INTERNAL REVENUE CODE

Interest on temporary short-term investments purchased with surplus cash by a foreign corporation engaged in the shipping business, and held in a United States bank, does not constitute earnings derived from the operation of a ship or ships documented under the laws of a foreign country within the meaning of section 231(d) of the Internal Revenue Code, and withholding of tax from such interest income is required under section 144 of the Code.

Advice is requested whether interest received on short-term investments of surplus cash held in a United States bank for the account of a foreign corporation engaged in the business of operating ships represents "earnings derived from the operation of a ship or ships documented under the laws of a foreign country" within the meaning of section 231(d) of the Internal Revenue Code and, accordingly, not subject to withholding of tax under section 144 of the Code.

G. C. M. 4859, C. B. VII-2, 73 (1928), holds that interest received by a British corporation on moneys held temporarily in United States banks, which represent surplus working cash arising and collected in the United States from the business of shipping, is regarded as being included in the term "earnings derived from the operation of a ship or ships" within the meaning of the revenue acts in effect at that time and consequently exempt from United States income tax.

The exemption provisions of such acts with respect to the earnings of ships of a foreign corporation are now embodied in section 231(d) of the Internal Revenue Code which reads as follows:

(d) EXCLUSIONS.—The following items shall not be included in gross income of a foreign corporation and shall be exempt from taxation under this chapter:

(1) SHIPS UNDER FOREIGN FLAG.—Earnings derived from the operation of a ship or ships documented under the laws of a foreign country which grants an equivalent exemption to citizens of the United States and to corporations organized in the United States;

Under the rationale of G. C. M. 4859, *supra*, interest is exempt under section 231(d) of the Code if it is derived from current assets used in the operation of the shipping business and held on current account for immediate disbursement or pending remittance to the foreign country.

As distinguished from the foregoing, interest earned in the United States by a foreign shipping corporation on temporary short-term investments such as United States Treasury notes and certificates purchased with surplus working cash, is not considered as interest received from current assets used in the operation of a shipping business and therefore such interest does not represent earnings derived from the operation of ships.

Accordingly, it is held that interest on temporary short-term investments purchased with surplus cash by a foreign corporation engaged in the shipping business, and held in a United States bank, does not constitute earnings derived from the operation of a ship or ships documented under the laws of a foreign country within the meaning of section 231(d) of the Internal Revenue Code, and withholding of tax from such interest income is required under section 144 of the Code.

SUPPLEMENT M.—INTEREST AND ADDITIONS TO THE TAX

SECTION 294.—ADDITIONS TO THE TAX IN CASE OF NONPAYMENT

REGULATIONS 118, SECTION 39.294–1: Additions to the tax. Rev. Rul. 292

(Also Section 58(d), Section 39.58(d)–1.)

INTERNAL REVENUE CODE

Where a taxpayer on a calendar year basis failed to file a declaration of estimated tax which he was required to file on or before March 15, June 15, or September 15 of the taxable year, but on or before the following January 15 he files a final return for the taxable year and at the time of such filing pays in full the amount of tax shown to be due thereon, and the total tax reported on that return (with certain exceptions) is not less than 80 percent of his correct tax liability, he is liable for the additions to the tax imposed by section 294(d)(1)(A) of the Code for failure to file a timely declaration (unless such failure is shown to the satisfaction of the Commissioner to be due to reasonable cause and not to willful neglect), but is not liable for the addition to the tax provided in section 294(d)(2) of the Code for substantial underestimate of estimated tax.

However, sections 3809 and 145 of the Code provide for criminal penalties in the case of any person who willfully makes and subscribes to a false return, statement, or other document; or who willfully fails to make a return or declaration, or to pay any estimated tax or tax at the time required by law or regulations.

Advice is requested relative to the application of the additions to the tax provided in section 294(d) of the Internal Revenue Code where a taxpayer on a calendar year basis failed to file a declaration of estimated tax which he was required to file on or before March 15, June 15, or September 15 of the taxable year, but on or before January 15

of the succeeding year he files a final return and pays in full the amount of tax shown to be due on that return.

Section 58 of the Code provides in part as follows:

(a) REQUIREMENT OF DECLARATION.—Every individual (other than an estate or trust and other than a nonresident alien with respect to whose wages, as defined in section 1621(a), withholding under subchapter D of chapter 9 is not made applicable, but including every alien individual who is a resident of Puerto Rico during the entire taxable year) shall, at the time prescribed in subsection (d), make a declaration of his estimated tax for the taxable year if—

(1) his gross income from wages (as defined in section 1621) can reasonably be expected to exceed the sum of $4,500 plus $600 with respect to each exemption provided in section 25(b); or

(2) his gross income from sources other than wages (as defined in section 1621) can reasonably be expected to exceed $100 for the taxable year and his gross income to be $600 or more.

* * * * * * *

(d) TIME AND PLACE FOR FILING.—

(1) IN GENERAL.—The declaration required under subsection (a) shall be filed on or before March 15 of the taxable year, except that if the requirements of section 58(a) are first met.

(A) after March 1 and before June 2 of the taxable year, the declaration shall be filed on or before June 15 of the taxable year, or

(B) after June 1 and before September 2 of the taxable year, the declaration shall be filed on or before September 15 of the taxable year, or

(C) after September 1 of the taxable year, the declaration shall be filed on or before January 15 of the succeeding taxable year.

(2) AMENDMENT OF DECLARATION.—An individual may make amendments of a declaration filed during the taxable year under this subsection, under regulations prescribed by the Commissioner with the approval of the Secretary. If so made, such amendments may be filed on or before the fifteenth day of the last month of any quarter of the taxable year subsequent to that in which the declaration was filed and in which no previous amendment has been filed, except that in the case of an amendment filed after September 15 of the taxable year, it may be filed on or before January 15 of the succeeding taxable year. Declarations and amendments thereof shall be filed with the collector specified in section 53(b)(1).

(3) RETURN AS DECLARATION OR AMENDMENT.—If on or before January 15 of the succeeding taxable year the taxpayer files a return, for the taxable year for which the declaration is required, and pays in full the amount computed on the return as payable, then, under regulations prescribed by the Commissioner with the approval of the Secretary—

(A) If the declaration is not required to be filed during the taxable year, but is required to be filed on or before such January 15, such return shall, for the purposes of this chapter, be considered as such declaration; and

(B) If the tax shown on the return (reduced by the credits under sections 32 and 35) is greater than the estimated tax shown in a declaration previously made, or in the last amendment thereof, such return shall, for the purposes of this chapter, be considered as the amendment of the declaration permitted by paragraph (2) to be filed on or before such January 15.

Section 60(c) of the Code provides that in the case of a taxable year beginning on any date other than January 1, there shall be substituted, for the months specified in section 58, the months which correspond thereto. The taxpayer in the instant situation is on a calendar year basis, but the conclusions reached hereinafter are equally applicable to taxpayers on a fiscal year basis, with appropriate substitution of months.

Section 294(d)(1) of the Code provides for additions to the tax for failure (A) to file a timely declaration of estimated tax or (B) to

pay within the time prescribed installments of estimated tax declared, "unless such failure is shown to the satisfaction of the Commissioner to be due to reasonable cause and not to willful neglect."

The purpose of such legislation is to require individuals (whose wages or other income exceed the amounts specified in section 58(a) of the Code, *supra*) to file timely and reasonably accurate declarations of estimated tax, and to pay installments of such declared estimated tax within the time prescribed in section 59(a) of the Code—with provisions for additions to the tax for failure to file timely declarations or to pay timely installments of declared estimated tax.

It is held that where a taxpayer on a calendar year basis failed to file a declaration of estimated tax which he was required to file on or before March 15, June 15, or September 15 of the taxable year, but on or before January 15 of the succeeding year he files a final return for the taxable year and at the time of such filing pays in full the amount of tax shown to be due thereon, and the total tax reported on that return (with certain exceptions) is not less than 80 percent of the tax imposed for that year, the taxpayer is liable for the additions to the tax for delinquency in filing a declaration of estimated tax provided in section 294(d)(1)(A) of the Code (unless such delinquency is shown to the satisfaction of the Commissioner to be due to reasonable cause and not to willful neglect), but he is not liable for the addition to the tax for substantial underestimate of estimated tax provided in section 294(d)(2) of the Code. While there is no provision in the Code (except in the case of farmers, as to whom see section 60(a) of the Code), for filing a timely declaration of estimated tax on or before January 15 following a calendar taxable year for which filing of such a declaration during the year was required under Code section 58(d)(1), *supra*, and, hence, no provision therein for considering a final return filed for that taxable year on or before January 15 of the succeeding year to be a timely declaration, it was obviously contemplated by Congress that delinquent declarations would be filed, since additions to the tax are provided for such delinquencies in section 294(d)(1)(A) of the Code. Even though the Code does not provide that such a final return shall be considered as a delinquent declaration of estimated tax, it would be unrealistic not to consider it as such, since it satisfies on or before January 15 of the succeeding taxable year a further requirement which obviates the necessity for filing a delinquent declaration. Under such circumstances, to which the instant rule will be strictly confined, a final return filed on or before such date will also be considered as a delinquent declaration of estimated tax.

However, attention is invited to section 3809 of the Code which provides for penalties of fine or imprisonment, or both, in the case of any person who willfully makes and subscribes any return, statement, or other document, which contains or is verified by a written declaration that it is made under the penalties of perjury, and which he does not believe to be true and correct as to every material matter, and to section 145 of the Code which provides for penalties of fine or imprisonment, or both, in the case of any person required to pay any estimated tax or tax, or to make a return or declaration, who willfully fails to pay such estimated tax or tax, or to make such return or declaration, at the time or times required by law or regulations.

SECTION 322.—REFUNDS AND CREDITS

REGULATIONS 118, SECTION 39.322-3: Claims for refund by taxpayers. Rev. Rul. 230

INTERNAL REVENUE CODE

Where an offer submitted by the husband and wife in compromise of unpaid income taxes, for which they were jointly and severally liable, is rejected, the check for the reimbursement of the amount tendered should be drawn in their joint names, even though payment on the offer was made with funds personally borrowed by the husband and the taxpayers were later divorced. Any disagreement between the copayees as to the endorsement of the check is a matter that should be settled between themselves.

REGULATIONS 118, SECTION 39.322-3: Claims for refund by taxpayers. Rev. Rul. 241*
(Also Section 22(d), Section 39.22(d)-7.)

INTERNAL REVENUE CODE

Interim allowance in respect of overpayment of tax under section 22(d)(6) of the Internal Revenue Code.

1. Com.-Mim. Coll. No. 6361 dated February 7, 1949, C. B. 1949-1, 126, established a program in respect of interim allowances of 75 percent of claimed overpayments of tax under section 22(d)(6) of the Internal Revenue Code, relating to involuntary liquidation of LIFO inventories in taxable years beginning after December 31, 1940, and prior to January 1, 1948, and replacement of such inventories prior to January 1, 1951.

2. Public Law 919 approved January 11, 1951, C. B. 1951-1, 179, extended the replacement period provided for in section 22(d)(6) of the Code with respect to involuntary liquidations occurring in years beginning after December 31, 1940, and prior to January 1, 1948, to January 1, 1953, and added subparagraph (F) to that section.

3. Under subparagraph (F) thus added to section 22(d)(6) of the Code, treatment similar to that provided in that section for taxable years beginning after December 31, 1940, and prior to January 1, 1948, is provided with respect to involuntary liquidations occurring in taxable years ending after June 30, 1950, and prior to January 1, 1954, and replacement of such liquidations in years ending prior to January 1, 1956. Subparagraph (F) of section 22(d)(6) of the Code as added by Public Law 919 was also amended by section 306 of the Revenue Act of 1951 to permit replacements to which that subparagraph would otherwise be applicable to be first treated as replacements of involuntary liquidations occurring in taxable years beginning after December 31, 1940, and prior to January 1, 1948.

4. The administrative provisions set forth in Com.-Mim. Coll. No. 6361 establishing an interim or accelerated refund program of 75

*Originally issued as IR-Mimeograph 282, dated September 16, 1953.

percent of the net reduction in taxes attributable to adjustments in connection with involuntary liquidations of LIFO inventories during taxable years beginning after December 31, 1940, and prior to January 1, 1948, and to replacements of such inventories in taxable years ending prior to January 1, 1951 (also applicable, following the enactment of Public Law 919, *supra*, to replacements in taxable years ending prior to January 1, 1953), are hereby extended to apply to cases subject to the provisions of section 22(d)(6) of the Code, as amended, in which involuntary liquidations occurred in taxable years ending after June 30, 1950, and prior to January 1, 1954, and in which the replacements were made in a subsequent taxable year ending prior to January 1, 1956.

5. Taxpayers entitled to the benefits of section 22(d)(6) of the Code and who desire an interim allowance in respect to any overpayment of tax under the provisions of such section must file an "Application for Interim Allowance in Respect of Overpayment of Taxes under Section 22(d)(6) of the Internal Revenue Code," Form 7013. Such application should set forth fully and clearly all of the information and data substantiating the taxpayer's representations that an interim allowance in respect of an overpayment of tax should be made as a result of involuntary liquidations and replacements. Applications must be filed, under oath, with the district director of internal revenue for the district in which assessment was made or tax paid. District directors are instructed to transmit, without delay, such applications, together with a certification as to assessment and payment of tax to the Assistant Commissioner (Operations), Internal Revenue Service, Washington 25, D. C., for the attention of the Collection Accounting Branch of the Collection Division which will make the adjustments authorized herein. In those cases in which involuntary liquidations occurred in more than 1 year, separate applications must be filed for each year. There must be attached to each application two copies of a duly executed "Agreement as to Interim Allowance in Respect of Overpayment of Tax under Section 22(d)(6) of the Internal Revenue Code," Form 7014. In connection with the financial statement referred to in item 9 of the application form, district directors should furnish any information in their possession or which had been called to their attention bearing on the wisdom of effecting an interim adjustment.

SUBCHAPTER E.—TAX ON SELF-EMPLOYMENT INCOME

SECTION 481.—DEFINITIONS

REGULATIONS 118, SECTION 39.481-2: Self-employment income. Rev. Rul. 275

INTERNAL REVENUE CODE

Optical services performed by members of a partnership in connection with the optometry business of the partnership, which holds itself out to the public as "jewelers and optometrists," may under some circumstances be integrated with the profession of optometry, where some of the members are optometrists, and excluded from the

self-employment tax under section 481(c)(5) of the Internal Revenue Code; however, the income from the jewelry department may not be so integrated.

Advice is requested as to the manner in which the distributive shares of the income from a partnership doing business as jewelers and optometrists should be computed for the purpose of determining the amount of "self-employment income" of the partners.

In the instant case a partnership operates a jewelry store and an optical department, and holds itself out to the public as jewelers and optometrists. One of the partners is licensed by the State as an optometrist and devotes approximately 95 percent of his time to the practice of optometry and to the performance of services as an optician. The other partners operate the jewelry store with only a portion of their time spent in performing services in connection with the optical department. The profits of both departments are divided equally among the partners at the end of the year.

Section 481 of the Internal Revenue Code provides in part as follows:

(a) NET EARNINGS FROM SELF-EMPLOYMENT.—The term "net earnings from self-employment" means the gross income derived by an individual from any trade or business carried on by such individual, less the deductions allowed by this chapter [chapter I] which are attributable to such trade or business, plus his distributive share (whether or not distributed) of the ordinary net income or loss, as computed under section 183, from any trade or business carried on by a partnership of which he is a member; * * *

(b) SELF-EMPLOYMENT INCOME.—The term "self-employment income" means the net earnings from self-employment derived by an individual * * * during any taxable year beginning after December 31, 1950; except that such term shall not include—

(1) That part of the net earnings from self-employment which is in excess of: (A) $3,600, minus (B) the amount of the wages paid to such individual during the taxable year; or

(2) The net earnings from self employment, if such net earnings for the taxable year are less than $400. * * *

(c) TRADE OR BUSINESS.—The term "trade or business" when used with reference to self-employment income or net earnings from self-employment, shall have the same meaning as when used in section 23, except that such term shall not include—

* * * * * * *

(5) The performance of service by an individual in the exercise of his profession as a * * * optometrist * * * or the performance of such service by a partnership.

Section 39.481-3 of Regulations 118 provides in effect that the nature of the services performed by the partnership as such and not the nature of the services contributed to the partnership by an individual member thereof determines whether any partner's distributive share of partnership income constitutes self-employment income. I. T. 4097, C. B. 1952-2, 208, holds that the distributive share of income of a member of a partnership which is engaged in the practice of dentistry, even though such a member is not a dentist, does not constitute self-employment income within the meaning of section 481(b) of the Internal Revenue Code.

Section 481(c)(5) of the Code excludes from the term "trade or business," when used with reference to net earnings from self-employment, the performance of service by an individual or a partnership in the exercise of certain professions, one of which is that of an optometrist.

It is not uncommon for persons practicing one of the excluded professions either as individuals or as partners, to engage, in addition, in sideline activities not in themselves so excluded. There is of course no precise rule for determining whether any such activity constitutes the practice of the excluded profession inasmuch as the answer in each case must be ascertained from all the surrounding facts and circumstances.

In general, however, the sideline activity will be regarded as incidental to the practice of the excluded profession if the former is a normal extension of such profession and can reasonably be embraced therein. In that case the net earnings from the sideline activity must be integrated with those arising from the practice of the excluded profession. On the other hand, if the activity in issue is not incidental to such profession the net earnings from each must be segregated and only those attributable to the excluded profession can be exempt from the tax on self-employment income. The segregation or integration of net earnings from each one of multiple enterprises for self-employment tax purposes is not subject to the taxpayer's election.

Opticians are not among those excluded professions enumerated in section 481(c)(5) and optical services as such do not come within the exclusion. A properly licensed optometrist, however, who examines eyes and prescribes glasses and charges for these services might perform optical services to the extent that he furnishes the glasses in accordance with his prescriptions and fits them. In such a case the performance of the optical services, together with any other optical service which may evolve from such activity as an optometrist is incidental to the practice of his profession as an optometrist and the entire income from both would come within the exclusion.

The circumstances in the instant case disclose that the partners hold themselves out to the public as "jewelers" and "optometrists" and that the services performed by them in the optical department are incidental to the services performed by them in the practice of optometry. Since the performance of the optical services is not a separate trade or business, the net earnings therefrom must be integrated with those arising from the practice of optometry. However, the services performed by the members of the firm in the operation of the jewelry department constitute a "trade or business" within the meaning of section 481(c) of the Code.

Accordingly, no part of the distributive shares of income derived by the partners from the optical department of the partnership should be included in computing their net earnings for the purpose of the tax on self-employment income. However, the distributive shares of the partnership income, to the extent provided by section 481(b) of the Code which are attributable to income from the jewelry department constitute net earnings from self-employment.

REGULATIONS 118, SECTION 39.481–3: Trade or business. Rev. Rul. 276

INTERNAL REVENUE CODE

The professions specifically designated in section 481(c)(5) of the Internal Revenue Code as being exempt from the tax on self-employment income are to be given their commonly accepted meaning. Such exemption applies only if the individual meets the legal

requirements, if any, for practicing his profession in the place where the service is performed.

Advice is requested whether a particular activity not in itself one of the professions enumerated in section 481(c)(5) of the Internal Revenue Code, may in some circumstances be regarded as incidental to and thus constituting a part of such a profession so that the income therefrom is exempt from self-employment tax.

For taxable years beginning after December 31, 1950, section 480 of the Code imposes a tax upon the self-employment income of every individual. In general, self-employment income consists of the net earnings derived by an individual (other than a nonresident alien) from a "trade or business" carried on by him as sole proprietor, or by a partnership of which he is a member, subject to certain exclusions, exceptions, and limitations.

Section 481(c)(5) of the Code excludes from the term "trade or business," for purposes of such tax, the performance of service by an individual in the exercise of his profession as a physician, lawyer, dentist, osteopath, veterinarian, chiropractor, naturopath, optometrist, Christian Science practitioner, architect, certified public accountant, accountant registered or licensed as an accountant under State or municipal law, full-time practicing public accountant, funeral director, or professional engineer.

Only those professions specifically designated in section 481(c)(5) of the Code are excluded from the term "trade or business," and the performance of services by an individual cannot constitute the exercise of an excluded profession unless he meets the legal requirements, if any, for the practice of such profession in the place where the services are performed. Furthermore, the statutory designations of the excluded professions are to be given their commonly accepted meanings. For example, the term "physician" as it is used in that section means an individual who is legally qualified to practice medicine and the term may not be extended by administrative action to include an individual who has been licensed solely to practice chiropody. Thus services of a character normally performed by a chiropodist can constitute a part of an excluded trade or business within the scope of section 481(c)(5) when they are performed by a physician incidental to the exercise of his profession as such but not when they are performed by an individual who is not a physician but is engaged in the practice of chiropody.

The Internal Revenue Service has had occasion to consider whether certain activities may be considered to qualify as a profession exempt from self-employment tax. While under some circumstances activities not in themselves constituting the practice of a profession might be regarded as such when performed incidental to the practice of a profession, it may be said that the performance of service as a chiropodist, landscape architect, masseuse, patent attorney (not legally qualified to practice law), pharmacist, physical-therapist technician, physiotherapist, podiatrist, registered anesthetist, registered land surveyor, or sculptor does not generally qualify as the practice of a profession exempt from the tax on self-employment income under section 481(c)(5) of the Code. *Cf.* Rev. Rul. 275, page 86.

CHAPTER 36.—COLLECTION

SUBCHAPTER F.—CLOSING AGREEMENTS AND COMPROMISES

SECTION 3760.—CLOSING AGREEMENTS

REGULATIONS 118, SECTION 39.3760-1: Closing agreements relating to tax liability in respect of internal revenue taxes.

INTERNAL REVENUE CODE

Closing agreement upon liquidation of wholly-owned subsidiary. (See Rev. Rul. 259, p. 55.)

B.—UNDER ALL OTHER LAWS AND REGULATIONS

INTERNAL REVENUE CODE

CHAPTER 1.—INCOME TAX

SUBCHAPTER B.—GENERAL PROVISIONS

PART I.—RATES OF TAX

SECTION 15.—SURTAX ON CORPORATIONS

REGULATIONS 111, SECTION 29.15-2: Disallowance of surtax exemption and minimum excess-profits credit. T. D. 6024

(Also Section 29.15-1; Section 204, Section 29.204-1; Section 231, Section 29.231-1; Section 431, Section 40.431-1, Regulations 130.)

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 29 AND PART 40

Disallowance of surtax exemption and minimum excess-profits credit under section 15(c) of the Internal Revenue Code.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

On January 3, 1953, notice of proposed rulemaking was published in the Federal Register (18 F. R. 81) to conform Regulations 111 [26 CFR, pt. 29] and Regulations 130 [26 CFR, pt. 40] to section 15(c) of the Internal Revenue Code, as added by section 121(f) of the Revenue Act of 1951, approved October 20, 1951. After consideration of all such relevant matter as was presented by interested persons relating to the rules proposed, the amendments to Regulations 111 and 130 set forth below are hereby adopted.

REGULATIONS 111 [26 CFR, PT. 29]

PARAGRAPH 1. The following is inserted immediately after section 29.15-1 [26 CFR 29.15-1]:

SEC. 121. INCREASE IN RATE OF CORPORATION NORMAL TAX [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

* * * * * * *

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(f) AMENDMENT OF SECTION 15.—Section 15 (relating to surtax on corporations) is hereby amended to read as follows:

"SEC. 15. SURTAX ON CORPORATIONS.

* * * * * * *

"(c) DISALLOWANCE OF SURTAX EXEMPTION AND MINIMUM EXCESS PROFITS CREDIT.—If any corporation transfers, on or after January 1, 1951, all or part of its property (other than money) to another corporation which was created for the purpose of acquiring such property or which was not actively engaged in business at the time of such acquisition, and if after such transfer the transferor corporation or its stockholders, or both, are in control of such transferee corporation during any part of the taxable year of such transferee corporation, then such transferee corporation shall not for such taxable year (except as may be otherwise determined under section 129(b)) be allowed either the $25,000 exemption from surtax provided in subsection (b) or the $25,000 minimum excess profits credit provided in the last sentence of section 431, unless such transferee corporation shall establish by the clear preponderance of the evidence that the securing of such exemption or credit was not a major purpose of such transfer. For the purposes of this subsection, control means the ownership of stock possessing at least 80 per centum of the total combined voting power of all classes of stock entitled to vote or at least 80 per centum of the total value of shares of all classes of stock of the corporation. In determining the ownership of stock for the purpose of this subsection, the ownership of stock shall be determined in accordance with the provisions of section 503, except that constructive ownership under section 503(a)(2) shall be determined only with respect to the individual's spouse and minor children. The provisions of section 129(b), and the authority of the Secretary under such section, shall, to the extent not inconsistent with the provisions of this subsection, be applicable to this subsection. This subsection shall not apply to any taxable year with respect to which the tax imposed by subchapter D of this chapter is not in effect."

SEC. 125. EFFECTIVE DATE [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

The amendments made by this part [sections 121 to 125, inclusive] shall be applicable only with respect to taxable years beginning after March 31, 1951, and to taxable years beginning on January 1, 1951, and ending on December 31, 1951 * * * For treatment of taxable years (other than the calendar year 1951) beginning before April 1, 1951, and ending after March 31, 1951, see section 131.

SEC. 29.15-2. DISALLOWANCE OF SURTAX EXEMPTION AND MINIMUM EXCESS-PROFITS CREDIT.—(*a*) *In general.*—If one corporation transfers after December 31, 1950, all or part of its property (other than money) to another corporation, neither the $25,000 exemption from surtax provided in section 15(b) nor the $25,000 minimum excess-profits credit provided in section 431 shall be allowed the transferee if—

(1) the transferee was created for the purpose of acquiring such property, or

(2) the transferee was not actively engaged in business at the time of the acquisition, and

(3) after such transfer the transferor or its stockholders, or both, are in control of the transferee during any part of the taxable year of the transferee,

unless—

(4) the transferee establishes by the clear preponderance of the evidence that the securing of either such exemption or such credit or both was not a major purpose of such transfer, or

(5) the Commissioner allows such exemption or such credit pursuant to the authority provided in section 15(c) and section 129(b).

(*b*) *Purpose of section 15(c).*—The purpose of section 15(c) is to prevent avoidance or evasion of the surtax on corporation surtax net income imposed by section 15(b) or of the excess-profits tax imposed by section 430. It is not intended, however, that section 15(c) be interpreted as delimiting or abrogating any principle of law established by judicial decision, or any existing provisions

of the Internal Revenue Code, such as sections 45 and 129, which have the effect of preventing the avoidance or evasion of income or excess-profits taxes. Such principles of law and such provisions of the Code, including section 15(c), are not mutually exclusive, and in appropriate cases they may operate together or they may operate separately.

The provisions of section 129(b) and the authority of the Commissioner thereunder, to the extent not inconsistent with the provisions of section 15(c), are applicable to cases covered by section 15(c). Pursuant to the authority provided in section 129(b), the Commissioner may allow to the transferee any part of a surtax exemption or minimum excess-profits credit for a taxable year for which such exemption or credit would otherwise be disallowed under section 15(c); or he may apportion such exemption or credit among the corporations involved (see section 29.129–4). For example, Corporation A transfers on January 1, 1952, all its property to Corporations B and C in exchange for all the stock of such corporations. Immediately thereafter, Corporation A is dissolved and its stockholders become the sole stockholders of Corporations B and C. Assuming that Corporations B and C are unable to establish by the clear preponderance of the evidence that the securing of the surtax exemption provided in section 15(b) or the minimum excess-profits credit provided in section 431, or both, was not a major purpose of the transfer, the Commissioner, nevertheless, has authority under sections 15(c) and 129(b) to allow one such exemption and credit and to apportion such exemption and credit between Corporations B and C.

For the purpose of section 15(c) and this section, a corporation maintaining an office for the purpose of preserving its corporate existence is not considered to be "actively engaged in business" even though such corporation may be deemed to be "doing business" for other purposes. Similarly, for the purpose of section 15(c) and this section, a corporation engaged in winding up its affairs, prior to an acquisition to which section 15(c) is applicable, is not considered to be "actively engaged in business."

(c) *Meaning and application of the term "control".*—For the purpose of section 15(c) and this section, the term "control" means the ownership of stock possessing either (1) at least 80 percent of the total combined voting power of all classes of stock entitled to vote, or (2) at least 80 percent of the total value of shares of all classes of stock of the corporation. In determining whether stock possessing at least 80 percent of the total combined voting power of all classes of stock entitled to vote is owned, all classes of such stock shall be considered together; it is not necessary that 80 percent of each class of voting stock the corporation shall be considered together; it is not necessary that 80 percent of the total value of shares of all classes of stock is owned, all classes of stock of the corporation shall be considered together; it is not necessary that 80 percent of the value of shares of each class be owned. The fair market value of a share shall be considered as the value to be used for the purpose of this computation.

The ownership of stock shall be determined in accordance with the provisions of section 503 and the regulations thereunder, except that constructive ownership under section 503(a)(2) shall be determined only with respect to the individual's spouse and minor children. For example, in addition to stock held directly or under an option to purchase, an individual is deemed to own stock held directly or indirectly by or for his spouse or minor children, and also to own a proportionate part of the stock owned by a corporation, partnership, estate, or trust in which he holds an interest as a shareholder, partner, or beneficiary.

Disallowance of the exemption and credit under section 15(c) is not limited to the taxable year of the transferee corporation in which the transfer of property occurs. Section 15(c) provides for the disallowance of the exemption and credit for any taxable year, whether the taxable year in which the transfer of property occurs or any subsequent taxable year of the transferee corporation, if, during any part of such year, the transferor corporation or its stockholders, or both, are in control of the transferee corporation. Thus, if Corporation D on January 1, 1951, transfers a part of its property to Corporation E, a corporation not actively engaged in business at the time of the acquisition of such property, in exchange for 60 percent of the voting stock of Corporation E, and, thereafter, during a later taxable year with respect to which section 15(c) is applicable, acquires an additional 20 percent of the voting stock of Corporation E, Corporation D, by reason of such later acquisition, is considered to be in control of Corporation E as of the time of such acquisition for the purpose of section 15(c). Accordingly, Corporation E will be disallowed the surtax exemption and minimum excess-profits credit for the taxable year in which the later acquisition of

stock occurred and for each taxable year thereafter in which the requisite control continues, unless Corporation E establishes by the clear preponderance of the evidence that the securing of such exemption or credit, or both, was not a major purpose of the transfer of the property in 1951.

In determining, for the purpose of section 15(c), whether a corporation, its stockholders, or both, are in control of a transferee corporation, it is not necessary that the stock be acquired on or after January 1, 1951. Thus, if Corporation F on June 1, 1950, owns 70 percent of the voting stock of Corporation G, and thereafter, on January 2, 1951, Corporation F acquires an additional 10 percent of such stock, control within the meaning of section 15(c) is acquired by Corporation F on January 2, 1951.

(*d*) *Nature of transfer.*—A transfer made by any corporation of all or part of its assets, whether or not such transfer qualifies as a reorganization under section 112(g), is within the scope of section 15(c), except that section 15(c) does not apply to a transfer of money only. For example, the transfer of cash for the purpose of expanding the business of the transferor corporation through the formation of a new corporation is not a transfer within the scope of section 15(c), irrespective of whether the new corporation uses the cash to purchase from the transferor corporation stock in trade or similar property.

(*e*) *Purpose of transfer.*—In determining, for the purpose of section 15(c), whether the securing of the exemption from surtax or the minimum excess-profits credit constituted "a major purpose" of the transfer, all circumstances relevant to the transfer shall be considered. For disallowance of the surtax exemption and minimum excess-profits credit under section 15(c), it is not necessary that the obtaining of either such credit or exemption or both have been the sole or principal purpose of the transfer of the property. It is sufficient if it appears, in the light of all the facts and circumstances, that the obtaining of such exemption or credit, or both, was one of the major considerations that prompted the transfer. Thus, the securing of the surtax exemption or the minimum excess-profits credit may constitute "a major purpose" of the transfer, notwithstanding that such transfer was effected for a valid business purpose and qualified as a reorganization within the meaning of section 112(g). The taxpayer's burden of establishing by the clear preponderance of the evidence that the securing of either such exemption or credit or both was not "a major purpose" of the transfer may be met, for example, by a showing that the obtaining of such exemption, or credit, or both, was not a major factor in relationship to the other consideration or considerations which prompted the transfer.

(*f*) *Taxable years to which applicable.*—Section 15(c) and this section are applicable to a taxable year which is the calendar year 1951 and to taxable years beginning after March 31, 1951, and are also applicable in the computation of the tax for certain fiscal years; however, such sections do not apply to any taxable year with respect to which the excess-profits tax imposed by subchapter D of chapter 1 of the Internal Revenue Code is not in effect. For treatment of taxable years beginning after June 30, 1950, and before April 1, 1951, and ending after March 31, 1951 (other than the calendar year 1951), see section 29.108–6. For treatment of taxable years beginning before April 1, 1954, and ending after March 31, 1954, see section 29.108–9. For computation of the excess-profits tax for certain fiscal years, see section 40.430–2(b)(2) and (c) of Regulations 130.

PAR. 2. Section 29.15–1, as amended by Treasury Decision 5950 [C. B. 1952–2, 32], approved December 2, 1952 [26 CFR 29.15–1], is further amended by adding at the end of the third paragraph of (*b*) of the section the following:

See, however, section 29.15–2, as to the circumstances under which the $25,000 exemption from surtax for the calendar year 1951 and certain taxable years beginning after March 31, 1951, may be disallowed in whole or in part.

PAR. 3. Section 29.204–1, as amended by Treasury Decision 5950 [26 CFR 29.204–1], is further amended by adding after the seventh sentence of the last paragraph of the section the following:

For the circumstances under which the $25,000 exemption from surtax for the calendar year 1951 and certain taxable years beginning after March 31, 1951, may be disallowed in whole or in part, see section 29.15–2.

PAR. 4. Section 29.231–1, as amended by Treasury Decision 5950 [26 CFR 29.231–1], is further amended by adding at the end of the third paragraph of (*b*) of the section the following:

See, however, section 29.15–2, as to the circumstances under which the $25,000 exemption from surtax for the calendar year 1951 and certain taxable years beginning after March 31, 1951, may be disallowed in whole or in part.

REGULATIONS 130 [26 CFR, PT. 40]

PAR. 5. Section 40.431–1 [26 CFR 40.431–1] is amended by adding at the end thereof the following:

See, however, section 15(c) and the regulations thereunder, as to the circumstances under which the $25,000 minimum excess-profits credit may be disallowed in whole or in part in the case of transfers of property (other than money) on or after January 1, 1951, between related corporations. For treatment of taxable years beginning before April 1, 1951, and ending after March 31, 1951 (other than the calendar year 1951), see section 40.430–2(b)(2). For treatment of taxable years beginning before July 1, 1953, and ending after June 30, 1953, see section 40.430–2(c).

(This Treasury Decision is issued under the authority contained in secs. 62 and 3791 of the Internal Revenue Code (53 Stat. 32, 467; 26 U. S. C. 62, 3791).)

T. COLEMAN ANDREWS,
Commissioner of Internal Revenue.

Approved June 25, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register June 30, 1953, 8:53 a. m.)

PART II.—COMPUTATION OF NET INCOME

SECTION 22(a).—GROSS INCOME: GENERAL DEFINITION

REGULATIONS 111, SECTION 29.22(a)–1: What included in gross income. Rev. Rul. 119

INTERNAL REVENUE CODE

The discount at which a "Twelve Year Dollar Savings Bond" of the State of Israel is originally issued constitutes interest which is taxable as ordinary income under section 22(a) of the Internal Revenue Code when realized upon redemption; it does not represent an amount received upon retirement of the bond within the meaning of section 117(f) of the Code.

Advice is requested as to the treatment, for Federal income tax purposes, of the discount upon original issuance of a "Twelve Year Dollar Savings Bond" of the State of Israel when realized upon redemption thereof.

The bonds in question are general non-interest-bearing obligations of the State of Israel issued in registered form and in eight denominations ranging from $50 to $10,000. The maturity value of each bond appears on the face thereof and is equal to 150 percent of the amount for which issued, e. g., a $50 bond matures at $75 and a $10,000 bond at $15,000. Each bond bears an issue date as of the first day of the

month during which issued, and each bond matures within 12 years of the issue date. On the reverse side of each bond is a "Schedule of Appreciation" indicating the amount at which the bond may be redeemed during each half-year period between the issue date and maturity. The bonds are nontransferable and nonassignable except in certain special instances. Prior to maturity, they are redeemable at the option of the bearer only in Israel and in Israeli currency at the then official rate of exchange. The estate of a deceased owner has the option, within 2 years of the owner's death, of redeeming the bonds in this country for United States legal tender. The bonds may be redeemed on or after May 1, 1956, at the option of the State of Israel.

The bonds appear to be similar to United States savings bonds, Series E, issued under the Second Liberty Bond Act, as amended, in that they are non-interest-bearing obligations issued at a discount. The Second Liberty Bond Act, as amended, provides that the increment in value represented by the difference between the issue price paid and the redemption value received, whether at or before maturity, shall be considered as interest. (See par. 1 of Mim. 6327, C. B. 1948–2, 12.)

In the case of an original purchaser of a United States Treasury bill issued prior to March 1, 1941, which purchaser holds it until maturity, the entire amount of the discount at which the bill was issued is considered interest which is exempt as such from Federal income tax. If the bill is sold before maturity, the amount of the discount is, for purposes of the income tax computation, to be apportioned among the holders according to the periods of their holdings. (See T. D. 4276, C. B. VIII–2, 83 (1929).) The amount of discount at which Treasury bills are issued on or after March 1, 1941, is considered as interest which is not tax exempt, and the principles of Treasury Decision 4276, *supra*, are applicable with respect to proration and apportionment of discount among the original and other holders according to their respective holding periods. (See I. T. 3486, C. B. 1941–2, 76.)

Since about 1920, discount realized on retirement of State and municipal obligations in the hands of the original purchaser has been treated by the Bureau as interest, the theory being that discount is an amount paid in lieu of interest. (See G. C. M. 1455, C. B. VI–1, 87 (1927), and rulings cited therein, which G. C. M. was partially revoked by G. C. M. 10452, C. B. XI–1, 18 (1932), as to other issues.) It was also the position of the Bureau as early as 1923 that an amount in excess of the discount at which issued (the difference between the original discount and the greater discount at which subsequently purchased) realized by the holder upon retirement of an obligation of a political subdivision of a State is to be treated as taxable income, not as tax-free interest. (See I. T. 1637, C. B. II–1, 36 (1923).) Subsequently, the principles of Treasury Decision 4276, *supra*, were applied to State and municipal securities issued at a discount in order to make the discount apportionable among the original and all subsequent purchasers according to the periods of their holdings, the same as interest on interest-bearing obligations. (See I. T. 2629, C. B. XI–1, 20 (1932), and G. C. M. 10452, *supra*.) The position taken by

the Bureau in the above-cited rulings has been consistently maintained with regard to characterizing discount as interest and treating the excess over discount (and ordinary interest, if any) realized upon retirement as taxable income. However, after the enactment of section 117(f) of the Internal Revenue Code, the excess over discount has been consistently taxed as capital gain rather than ordinary gain. (See G. C. M. 21890, C. B. 1940–1, 85.) Therefore, only the excess of the amount realized from a State or municipal bond, less discount from the date of acquisition, and ordinary interest, if any, over the cost or other basis of the bond is the amount received upon retirement taxable as capital gain under section 117(f) of the Code.

In view of the foregoing, it is believed that no legal distinction for Federal income tax purposes can be made between discount received on the retirement at or prior to maturity of a State or municipal obligation, or on a United States savings bond, Series E, and discount received on retirement at or prior to maturity of a "Twelve Year Dollar Savings Bond" of the State of Israel. Accordingly, it is held that the discount at which a "Twelve Year Dollar Savings Bond" of the State of Israel is originally issued constitutes interest which is taxable as ordinary income under section 22(a) of the Code when realized upon redemption; it does not represent an amount received upon retirement of the bond within the meaning of section 117(f) of the Code.

In the case of *Commissioner* v. *George Peck Caulkins*, 144 Fed. (2d) 482, affirming the Tax Court decision, 1 T. C. 656, acquiescence, C. B. 1944, 5, the court held that the excess of the amount received by the taxpayer, pursuant to a contract with Investors Syndicate over the aggregate payments made by him for an Accumulative Installment Certificate, constituted capital gain, and stated that the certificate in question was " 'an evidence of indebtedness' similar to a bond or debenture and hence falls within the statutory group governed by section 117(f)." This decision should be limited precisely to what was there decided under the particular facts of that case. It would be inappropriate to apply the decision to any other case unless the facts and circumstances conform to those stated in the published decision of the Tax Court in the Caulkins case.

REGULATIONS 111, SECTION 29.22(a)-1: What included in gross income. Rev. Rul. 129

INTERNAL REVENUE CODE

Payments received by a lessee-sublessor which are attributable to an assignment of subsisting subleases on leased property, in connection with a reassignment of the basic ground lease to the lessor, are includible in the gross income of the lessee-sublessor as ordinary income.

Advice is requested as to the tax treatment, for Federal income tax purposes, of payments received by a lessee-sublessor which are attributable to the assignment of subsisting subleases on the leased property in connection with a reassignment of the basic ground lease to the lessor.

In the instant case after acquisition of an existing lease on land the M Company improved the site by the erection of various buildings and other structures and entered into numerous subleases, rental agreements, and other contracts for occupancy or use of the buildings, room facilities, and space. Later by virtue of a purchase and sales agreement the M Company agreed to "sell, convey, assign, and transfer" to the lessors of such land all right, title, and interest in the leasehold. Title and interest in the leasehold include rights, title, and interest in all subleases, rental agreements, and contracts for occupancy or use of space, and all rentals or revenues to be derived therefrom. All of the subleases, agreements, and contracts expire within a period of 2 years, at which time the M Company's lease also expires.

Section 22 of the Internal Revenue Code provides in part as follows:

(a) GENERAL DEFINITION.—"Gross income" includes gains, profits, and income derived from * * * rent * * * or gains or profits and income derived from any source whatever. * * *

In *Walter M. Hort* v. *Commissioner*, 313 U. S. 28, Ct. D. 1502, C. B. 1941-1, 319, it was held that an amount received by a lessor in consideration of a cancellation of a lease of real estate is to be taxed as ordinary income for it "involved nothing more than the relinquishment of the right to future rental payments in return for a present substitute payment and possession of the leased premises." The court reasoned that the definition of gross income reaches the rent paid prior to cancellation just as it embraces subsequent payments in the event the lease is never canceled; that simply because the lease is "property" the amount received for its cancellation is not a return of capital; and that where an amount is essentially a substitute for rental payments which section 22(a) expressly characterizes as gross income, it must be regarded as ordinary income and it is immaterial that for some purposes the contract creating the right to such payments may be treated as "property" or "capital." (See *General Artists Corporation* v. *Commissioner*, decided by U. S. Court of Appeals, 2d Circuit, July 7, 1953; *Commissioner* v. *Starr Bros.*, decided by U. S. Court of Appeals, 2d Circuit, May 29, 1953.)

The facts in the instant case fall within the rule set forth in *Walter M. Hort* v. *Commissioner*, *supra*. The payments to the lessee-sublessor are essentially a substitute for rental payments owing the lessee-sublessor from the sublessee.

Accordingly, it is held that payments received by a lessee-sublessor which are attributable to an assignment of subsisting subleases on leased property, in connection with a reassignment of the basic ground lease to the lessor, are includible in the gross income of the lessee-sublessor as ordinary income.

REGULATIONS 111, SECTION 29.22(a)-1: What included in gross income.

INTERNAL REVENUE CODE

Amounts contributed by taxpayer for purpose of rehabilitating employees after major disaster. (See Rev. Rul. 131, p. 112.)

REGULATIONS 111, SECTION 29.22(a)-1: What included in gross income.

INTERNAL REVENUE CODE

Treatment of the amount paid by life insurance companies for accrued dividends with respect to capital stock purchased. (See Rev. Rul. 198, p. 221.)

REGULATIONS 111, SECTION 29.22(a)-2: Compensation for personal services. (Also Section 1621, Section 405.101, Regulations 116.) Rev. Rul. 130

INTERNAL REVENUE CODE

Employees' contributions assumed and paid by employers, which contributions are required of employees under article 9 (known as the disability benefits law) of the New York workmen's compensation law, are not includible in the gross income of covered employees and are not subject to withholding of income tax at the source on wages.

I. T. 4010, C. B. 1950-1, 30, and I. T. 4075, C. B. 1952-1, 13, modified.

Further consideration has been given to the holding in I. T. 4010, C. B. 1950-1, 30, to the effect that contributions required of employees under article 9 of the New York workmen's compensation law which are assumed and paid by employers are includible in the gross income of the employees and are subject to withholding of income tax at the source on wages under section 1622 of the Internal Revenue Code.

Under section 209 of the New York workmen's compensation law, every covered employer is given the right to require contributions from his employees toward the cost of providing nonoccupational disability benefits for employees. However, subdivision 4 of section 211 of such law provided for an exception in the case of such an approved plan which was in existence on the effective date of the article (April 13, 1949) and did not require contributions from the employees. Chapter 134 of the New York Laws of 1952, *supra*, amended article 9 to provide that in the case of new plans, as well as in the case of plans in existence on April 13, 1949, the obligation of employees to contribute to the payment of the cost of the benefits should be as provided in the plan rather than as provided in the statute. In I. T. 4075, C. B. 1952-1, 13, it is held that in the case of approved plans which were in existence when article 9 became effective, and under such plans contributions are not required of employees, there is no receipt of income by the employees upon the employer providing for the payment of the disability benefits.

Upon further consideration it is held that employees' contributions assumed and paid by employers, which contributions are required of employees under article 9 (known as the disability benefits law) of the New York workmen's compensation law, are not includible in the gross income of covered employees and are not subject to withholding of income tax at the source under section 1622 of the Internal Revenue Code. I. T. 4010, C. B. 1950-1, 30, is modified to the extent that it holds that contributions required of employees under the New York workmen's compensation law which are assumed and paid by employers are includible in the gross income of employees and are subject

to withholding of income tax at the source on wages under section 1622 of the Internal Revenue Code. I. T. 4075, C. B. 1952–1, 13, is modified to eliminate therefrom any reference to I. T. 4010.

REGULATIONS 111, SECTION 29.22(a)–3: Compensation paid other than in cash.

INTERNAL REVENUE CODE

Premiums paid by an employer on individual accident insurance policies purchased for each of its salesmen. (See Rev. Rul. 210, p. 114.)

REGULATIONS 111, SECTION 29.22(a)–5: Gross income from business. (Also Section 23(a), Sections 29.23(a)–1, 29.23(a)–4; Section 23(c), Section 29.23(c)–2.) T. D. 6028

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 29.—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1941

Regulations 111 amended to permit inclusion of certain items in the cost of acquisition or production, rather than business expense.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

On December 20, 1952, a notice of proposed rulemaking was published in the Federal Register (17 F. R. 11656) to conform certain provisions of Regulations 111 [26 CFR, pt. 29] to acceptable accounting practices. After careful consideration of all relevant matter presented by persons interested in the rules proposed, the amendments to Regulations 111 set forth below are hereby adopted.

PARAGRAPH 1. Section 29.22(a)–5 is amended by striking out the second sentence and inserting in lieu thereof the following:

In determining gross income, subtractions should not be made for depletion allowances based on discovery value or percentage of income, selling expenses, or losses, or for other items not ordinarily used in computing cost of goods sold.

PAR. 2. Section 29.23(a)–1, as amended by Treasury Decision 6006 [C. B. 1953–1, 30], approved April 10, 1953, is amended further as follows:

(A) By striking from the first sentence the words "except the classes of items which are deductible under sections 23(b) to 23(z), inclusive, and the regulations thereunder", and inserting in lieu thereof the following: "except items which are used as the basis for a deduction or a credit under provisions of law other than subsection (a) of section 23."

(B) By inserting after the seventh sentence, which names certain items included in business expenses, the following sentence:

No such item shall be included in business expenses, however, to the extent that it is used by the taxpayer in computing the cost of property included in its

inventory or used in determining the gain or loss basis of its plant, equipment, or other property.

PAR. 3. Section 29.23(a)–4 is amended by striking out the first sentence and inserting in lieu thereof the following:

The cost of incidental repairs which neither materially add to the value of the property nor appreciably prolong its life, but keep it in an ordinarily efficient operating condition, may be deducted as expense, provided the cost of acquisition or production or the gain or loss basis of the taxpayer's plant, equipment, or other property, as the case may be, is not increased by the amount of such expenditures.

PAR. 4. Section 29.23(c)–2, as amended by Treasury Decision 5371 [C. B. 1944, 80], approved May 11, 1944, is further amended by striking out the second sentence and inserting in lieu thereof the following:

The fact that any such tax is not deductible as a tax under section 23(c) for a taxable year beginning after December 31, 1943, does not prevent (a) a deduction therefor under section 23(a) provided it represents an ordinary and necessary expense paid or incurred during the taxable year by a corporation or an individual in carrying on any trade or business, or, in the case of an individual, for the production or collection of income, or for the management, conservation, or maintenance of property held for the production of income, or (b) the inclusion of such tax paid or incurred during the taxable year by a corporation or an individual as a part of the cost of acquisition or production in the trade or business, or, in the case of an individual, as a part of the cost of property held for the production of income with respect to which such tax is paid or incurred.

(This Treasury Decision is issued under the authority contained in secs. 62 and 3791 of the Internal Revenue Code (53 Stat. 32, 467; 26 U. S. C. 62, 3791).)

T. COLEMAN ANDREWS,
Commissioner of Internal Revenue.

Approved July 6, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register July 10, 1953, 8:46 a. m.)

REGULATIONS 111, SECTION 29.22(a)–5: Gross income from business. Rev. Rul. 141

INTERNAL REVENUE CODE

In determining the amount of gross income of manufacturing, merchandising, or mining businesses, the amount of depreciation and depletion based on cost, incurred in connection with the production or acquisition of goods or materials, may be included in the cost of such items.

Advice is requested with respect to the application and significance of the amendment to section 29.22(a)–5, of Regulations 111, by Treasury Decision 6028 promulgated July 7, 1953, page 100, this Bulletin, which removed the prohibition against the subtraction of depreciation and depletion based on cost in determining gross income of manufacturing, merchandising, or mining businesses.

Prior to its amendment section 29.22(a)–5 of Regulations 111 provided that, in determining gross income, subtractions should not be made for depreciation, depletion, selling expenses, or losses, or for

items not ordinarily used in computing the cost of goods sold. The regulations as amended permit a subtraction of amounts for depreciation or depletion based on costs incurred in connection with the production of goods or materials in determining gross income. The regulations, accordingly, now conform to accepted principles of cost accounting and are consistent with the provisions of sections 29.22(c)–2 and 3 of Regulations 111, with respect to the valuation of inventories.

The amendment merely permits the subtraction of depreciation and cost depletion in determining gross income in accordance with accepted accounting practice in the particular trade or business and does not require such subtraction. Any change by a taxpayer from the method consistently used in the past with respect to the treatment of such items in determining gross income constitutes a change in accounting method which requires the consent of the Commissioner in accordance with section 29.41–2 of Regulations 111.

In those cases where subtractions for depreciation and cost depletion are properly included in the costs of goods or materials produced in determining gross income, such items and amounts should be set forth in detail in schedule C of the individual return, Form 1040, or in a supplementary schedule supporting item 2 of the partnership return, Form 1065, or accompanying schedule A of the corporation return, Form 1120.

SECTION 22(b).—GROSS INCOME: EXCLUSIONS FROM GROSS INCOME

Rev. Rul. 208

INTERNAL REVENUE CODE

Benefits received under a self-insured plan which complies with the New York State disability benefits law providing a system of cash benefits payable to employees disabled as a result of nonoccupational injuries or sickness are excludable from the gross income of the recipients as accident or health insurance under section 22(b)(5) of the Internal Revenue Code where the benefits are paid entirely from an independent fund consisting solely of contributions and the earnings from the contributions of employees.

Advice is requested, in view of I. T. 4107, C. B. 1952–2, 73, whether nonoccupational disability benefits received by employees under a self-insured plan established by an employer and approved by the appropriate State agency as conforming to the requirements of article 9 (known as the disability benefits law) of the New York workmen's compensation law, are excludable from the gross income of the recipients as accident or health insurance under section 22(b)(5) of the Internal Revenue Code, where the benefits are paid entirely from an independent fund consisting solely of contributions and the earnings derived from the contributions of employees.

I. T. 4107, *supra*, provides that self-insured plans established by employers which provide for the payment of sickness or accident disability benefits to their employees, and which are not in themselves plans of insurance within the purview of section 22(b)(5) of the Code, do not become plans of insurance merely by virtue of compliance with State disability benefits statutes and approval by the appropriate State agencies.

The New York State disability benefits law provides in pertinent part that each employee is required to contribute to the cost of provid-

ing disability benefits by means of a payroll deduction in the amount of one-half of 1 percent of the wages paid to him on and after July 1, 1950, but not in excess of 30 cents per week. The law provides that in collecting employee contributions through payroll deductions the employer shall act as the agent of his employees and shall use the contributions only to provide disability benefits as required by the law. To the extent that the employer does not provide for the payment of benefits by insuring with the State fund or with another insurance carrier, he shall keep the contributions of his employees as trust funds separate and apart from all other funds of the employer. (Sec. 209.) Every employer is required to contribute the cost of providing disability benefits in excess of the contributions collected from his employees. (Sec. 210.)

In the instant case the employer, under a self-insured plan approved by the appropriate State agency, collects from the weekly wages of its employees in the State of New York the statutory amounts which each employee is required to contribute to the cost of providing the disability benefits. Such amounts are, pursuant to the State law, deposited in a special bank account. No deposits other than the contributions of employees are made to this account and the funds in the account are used for the sole purpose of paying New York State disability benefits. The benefits paid are the minimum amounts required under the statute. Although the employer is obligated under the law to contribute as much as is necessary to meet the cost of providing disability benefits when they exceed employee contributions, the employer has thus far neither deposited any of its own funds in the special bank account nor used any of its own money to pay any benefits, the contributions of the employees having been the exclusive source of all benefits paid.

Section 22(b)(5) of the Code provides in part as follows:

> (b) EXCLUSIONS FROM GROSS INCOME.—The following items shall not be included in gross income and shall be exempt from taxation under this chapter [chapter 1 of the Code]:
>
> * * * * * * *
>
> (5) COMPENSATION FOR INJURIES OR SICKNESS.—Except in the case of amounts attributable to (and not in excess of) deductions allowed under section 23(x) in any prior taxable year, amounts received, through accident or health insurance or under workmen's compensation acts, as compensation for personal injuries or sickness * * *

An examination of the facts in the instant case reveals the existence of insurance within the meaning of section 22(b)(5), *supra*. (See G. C. M. 23511, C. B. 1943, 86.) The benefits paid pursuant to the State law are based in part on regular wages (the maximum limit being an arbitrary amount) but the period during which the benefits are payable does not depend on the employee's length of service. The benefits are paid out of employee contributions with no indication that the employer expects to contribute to the cost of the benefits within the foreseeable future. Furthermore, the contributions of the employees are paid into a bank account which, since it contains employee contributions, must be maintained as a trust fund apart from the moneys of the employer under the law. The benefits are paid from this same account.

In view of the foregoing, it is held that benefits received under a self-insured plan which complies with the New York State disability

benefits law providing a system of cash benefits payable to employees disabled as a result of nonoccupational injuries or sickness are excludable from the gross income of the recipients as accident or health insurance under section 22(b)(5) of the Internal Revenue Code where the benefits are paid entirely from an independent fund consisting solely of contributions and the earnings derived from the contributions of employees.

The conclusion reached herein does not constitute an acceptance of the decision in the case of *Arnold W. Epmeier* v. *United States*, 199 Fed. (2d) 508.

Rev. Rul. 209

INTERNAL REVENUE CODE

A self-insured plan established by an employer in compliance with the New York State disability benefits law providing for the payment of nonoccupational disability benefits to its employees under which (1) the benefits paid are based on length of service rather than degree of disability, (2) employees make no contributions to the plan or other payments similar to premiums, and (3) there is no trust or other separate entity into which the employer pays his contributions and from which employees receive benefits, is not a plan of insurance within the purview of section 22(b)(5) of the Internal Revenue Code since there is nothing to distinguish the benefit payments under the plan from continuation of regular compensation in whole or in part during periods of disability.

Advice is requested whether self-insured plans established by an employer in compliance with the New York State disability benefits law providing for the payment of nonoccupational disability benefits to its employees constitute plans of accident or health insurance within the purview of section 22(b)(5) of the Internal Revenue Code so that the benefits received thereunder may be excluded from the gross income of the recipients.

The taxpayer has three nonoccupational disability benefits plans for its employees, each of which has been approved by the Workmen's Compensation Board of the State of New York as complying with the requirements of the disability benefits law of that State. (Article 9 of the New York workmen's compensation law.) Under the first plan, the taxpayer pays, pursuant to the terms of a collective bargaining agreement, disability benefits equal to regular compensation to regular employees covered by that agreement for a period of time based on length of service. The second plan covers regular employees not within the collective bargaining unit. It provides that an employee disabled as a result of nonoccupational injuries or sickness, shall receive as disability benefits 1 week's pay at his regular rate and an additional week's pay for each additional year of service after the first year. The third plan applies to temporary employees not covered by the first two and provides for the payment of minimum statutory benefits.

Employees covered by these plans are not required to contribute to the cost of providing the disability benefits. The taxpayer has not established a trust or an independent entity into which contributions are made and from which benefits are paid. The taxpayer has not entered into any contract with an insurance carrier to provide the disability benefits.

Section 22(b)(5) of the Internal Revenue Code provides in part as follows:

(b) EXCLUSIONS FROM GROSS INCOME.—The following items shall not be included in gross income and shall be exempt from taxation under this chapter [chapter 1 of the Code]:

* * * * * * *

(5) COMPENSATION FOR INJURIES OR SICKNESS.—Except in the case of amounts attributable to (and not in excess of) deductions allowed under section 23(x) in any prior taxable year, *amounts received, through accident or health insurance* * * * as compensation for personal injuries or sickness * * * [Italics supplied.]

I. T. 4107, C. B. 1952–2, 73, provides that self-insured plans established by employers which provide for the payment of sickness or accident disability benefits to their employees, and which are not in themselves plans of insurance within the purview of section 22(b)(5) of the Code, do not become plans of insurance merely by virtue of compliance with State disability benefits statutes and approval by the appropriate State agencies. Neither the existence of a contractual obligation, such as the collective bargaining agreement pursuant to which the first plan in the instant case was established, nor the fact that the plan operates under statutory requirements which are essentially equivalent to contractual obligations, is by itself enough to make the plan one of insurance for purposes of section 22(b)(5). Something more than a contract or statutory obligation is required. See I. T. 4107, *supra*, and G. C. M. 23511, C. B. 1943, 86.

An examination of the facts in the instant case does not reveal the existence of insurance within the meaning of section 22(b)(5), *supra*. The employees make no contributions to the plan or any other payments similar to premiums for the disability benefits provided under the plans. The benefits under the first and second plans are based on the regular wages or salaries of the covered employees and the duration of the benefits is based on the length of employment rather than the degree of disability. In the third plan, the statutory benefit is based on a percentage of regular compensation except that an arbitrary maximum is fixed; the period during which benefits are paid under this plan depends on length of disability except that an arbitrary maximum is fixed. Furthermore, there is an absence of any trust or independent entity into which the employer pays his contributions under any of the plans and from which the employees receive benefits when disabled, *cf.* Rev. Rul. 208, page 102, this Bulletin. Thus, although there is a contract or an analogous obligation in each of the plans in the instant case, there is nothing to distinguish the benefits payments received thereunder from the continuation of regular compensation in whole or in part during a period of disability.

It is accordingly held that the plans of the instant taxpayer are not plans of insurance within the meaning of section 22(b)(5) of the Internal Revenue Code. Benefits received thereunder after December 31, 1952, are includible in the gross income of the recipients and are subject to withholding of income tax at the source on wages under section 1622 of the Code.

I. T. 4107, *supra*, modified I. T. 4000, C. B. 1950–1, 21, I. T. 4015, C. B. 1950–1, 23, and I. T. 4060, C. B. 1951–2, 11, which had held that disability benefits paid under sertain plans established pursuant to State law in New Jersey, California, and New York, were excludable

from gross income under section 22(b)(5) of the Code. Those payments are no longer so excluded merely on the basis that the plans under which paid complied with State disability benefit statutes and were approved by appropriate State agencies. I. T. 4107, *supra*, provided that the conclusion stated therein would not be applied with respect to disability payments received prior to January 1, 1953, under the types of plans there involved. Prior to the issuance of I. T. 4107, *supra*, some employers submitted their plans to the Internal Revenue Service for a specific determination as to whether their individual plans constituted plans of insurance for the purpose of section 22(b)(5) in accordance with I. T. 4000, *supra*, I. T. 4015, *supra*, or I. T. 4060, *supra*. Such employers, to the extent not heretofore specifically notified by the Revenue Service, are hereby notified of the effect of I. T. 4107, *supra*, and that, accordingly, withholding of income tax in such cases shall, pursuant to the authority contained in section 3791(b) of the Code, be required with respect to payments made on and after November 1, 1953.

REGULATIONS 111, SECTION 29.22(b)(1)-2: Death payment by employer—amounts paid by reason of the death of an employee. T. D. 6020

(Also Sections 29.22(b)(2)-2, 29.22(b)(2)-5; Section 113(a), Section 29.113(a)(5)-1; Section 165, Section 29.165-6.)

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 29.—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1941

Regulations 111 amended to conform to section 302, Revenue Act of 1951, relating to payments to beneficiaries of deceased employees, and section 303 thereof, relating to joint and survivor annuities.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

On November 14, 1952, notice of proposed rulemaking with respect to amendments to conform Regulations 111 to section 302 of the Revenue Act of 1951 (Public Law 183, 82d Cong.), approved October 20, 1951, relating to the exclusion from gross income of certain death benefits paid by employers to beneficiaries of deceased employees, and section 303 thereof, relating to the taxability of amounts received by a surviving annuitant under a joint and survivor annuity, was published in the Federal Register (17 F. R. 10411). After consideration of all such relevant matter as was presented by interested persons regarding the rules proposed, the amendments to Regulations 111 [26 CFR, pt. 29] set forth below are hereby adopted:

PARAGRAPH 1. There is inserted immediately preceding section 29.22(b)(1)-1 the following:

SEC. 302. PAYMENTS TO BENEFICIARIES OF DECEASED EMPLOYEES [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

(a) AMENDMENT OF SECTION 22(b)(1).—Section 22(b)(1) (relating to exclusion of life insurance proceeds from gross income) is hereby amended to read as follows:

"(1) LIFE INSURANCE, ETC.—Amounts received—

"(A) under a life insurance contract, paid by reason of the death of the insured; or

"(B) under a contract of an employer providing for the payment of such amounts to the beneficiaries of an employee, paid by reason of the death of the employee;

whether in a single sum or otherwise (but if such amounts are held by the insurer, or the employer, under an agreement to pay interest thereon, the interest payments shall be included in gross income). The aggregate of the amounts excludible under subparagraph (B) by all the beneficiaries of the employee under all such contracts of any one employer may not exceed $5,000."

(b) EFFECTIVE DATE.—The amendment made by this section shall be applicable with respect to taxable years beginning after December 31, 1950.

PAR. 2. Immediately following section 29.22(b)(1)-1, as amended by Treasury Decision 5515 [C. B. 1946-1, 26], approved May 16, 1946, there is inserted the following new section which represents the basic provisions of regulations regarding the interpretation of section 302 of the Revenue Act of 1951:

SEC. 29.22(b)(1)-2. DEATH PAYMENT BY EMPLOYER—AMOUNTS PAID BY REASON OF THE DEATH OF AN EMPLOYEE.—Amounts, not in excess of $5,000, paid by an employer in pursuance of an express contract, to the estate or to a beneficiary (individual, partnership, trust, or corporation) of an employee, including a former employee, by reason of the employee's death shall be excluded from the gross income of such beneficiary if received during a taxable year beginning after December 31, 1950. Where such death payments are made by more than one employer, including former employers of the decedent, a $5,000 exclusion applies separately to amounts receivable from each employer or former employer of the decedent. Where the aggregate payments by an employer, under an express contract, to the beneficiaries of the deceased employee exceed $5,000, the $5,000 exclusion shall be proportioned among the beneficiaries in the same proportion as the amount payable to or received by each under such contract bears to the total death payment the employer is contractually obligated to make. It is immaterial whether the proceeds are received in a single sum or otherwise. If, however, the proceeds are held by an employer under an agreement to pay interest thereon, the interest payment must be included in gross income.

Example (1). The M Corporation, the employer of A, who died on November 30, 1950, was liable under an express contract to pay a death payment of $15,000 to the beneficiaries of A, to be distributed as follows; $5,000 to the widow of A; $2,500 each to the parents of A; and $1,000 each to the five children of A. Each of the beneficiaries of A, except his widow, received such payment in a lump sum in January 1951. The widow of A elected to receive her share of the death payment in monthly installments of $100 beginning with the month of January 1951. All of the beneficiaries filed income tax returns on a calendar year basis. Apportioning the $5,000 exclusion in the same proportions as the total death payments the employer is contractually obligated to make, the widow of A shall exclude $1,666.67 of the monthly payments made to her (one-third of $5,000); each of A's parents shall exclude $833.33 of his or her death payment (one-sixth of $5,000); and each of the five children shall exclude $333.33 (one-fifteenth of $5,000). In the case of the widow, $1,200 of her monthly payments shall be excluded from her income tax return for the year 1951 and the balance of $466.67 from her return for the year 1952.

Example (2). H died on July 1, 1951. At the time of his death he was employed by the A Corporation, which was liable under an express contract to pay a death payment of $2,500 to W, his widow. The B Corporation, a former employer of H, was also liable under an express contract to pay a death payment of $5,000 to W. The $7,500 receivable by W from the A and B Corporation is excludable from her gross income.

Where a payment is made on account of the death of an employee by a welfare fund or a trust, including a pension trust exempt under section 165(a), in pursuance of an agreement entered into by an employer of the deceased employee, the payment shall be considered to have been made by the employer for the purpose of this section. Any part of a death payment which is attributable to the contributions of the employee shall be disregarded in determining the amount paid by an employer.

An express contract requiring payment by an employer to the beneficiaries of a deceased employee by reason of the latter's death shall be deemed to exist only if (1) the employer and employee had entered into a written contract, not revoked before the employee's death, which required such payment or (2) the employer had an established plan (or program having the effect of a plan) making provision for such payments in the case of his employees generally, or for a class or classes of his employees. In the latter case, the contract will be deemed to exist between the employer and the members of the class or classes of employees to whom the plan applies, provided such plan had been communicated to such employees and had not been rescinded prior to the death of the employee to whom the particular death payment relates. Communication of an employer's plan or program to his employees may be made in different ways, such as by publicizing or distributing to the employees concerned notice of the resolution approved by the board of directors which created the plan, or by distributing to the employees a booklet containing an explanation of the plan and the rights of their beneficiaries thereunder.

The exclusion from gross income provided by this section is limited solely to those amounts paid by or on behalf of an employer which, by the terms of the contract with the employee or by the provisions of the plan providing for such payments, are specifically designated and intended as a death payment, paid only by reason of the death of the employee. The exclusion does not apply to amounts with respect to which the deceased employee possessed, immediately prior to his death, a nonforfeitable right to receive the amounts while living. See section 29.165–7. Amounts to which the exclusion is not applicable include, among others, such items as uncollected salary, payments for unused leave, and amounts paid by or on behalf of an employer to the survivor of a deceased retired employee as a survivor's annuity, as to which see section 29.22(b)(2)–2.

Example (3). A, who was a participant under the B Company pension plan, retired on December 31, 1951. He had made no contributions to the plan. Upon his retirement he became entitled to a monthly income of $100 payable for life, 120 months certain. A died in October 1952 having received 10 monthly payments of $100 each. His widow became entitled to 110 monthly payments representing the balance of the payments certain. No exclusion from gross income may be made by A's widow under this section since the employee's right to the monthly payments was nonforfeitable from the date of his retirement.

Example (4). The trustee of the C Corporation profit-sharing plan was required under the provisions of the plan to pay to the beneficiary of B, an employee of the C Corporation who died on July 1, 1952, the benefit due on account of the death of B. The provisions of the profit-sharing plan gave each participating employee in case of voluntary termination of employment a 10 percent vested interest in the amount accumulated in his account for each year of participation in the plan but, in case of death, the entire credit to the participant's account would be paid to his beneficiary.

At the time of the death of B he had been a participant for 3 years and the accumulation in his account was $8,000. After his death this amount was paid to his beneficiary. At the time of the death of B the amount distributable to him on account of voluntary termination of employment was $2,400 (30 percent of $8,000). The difference of $5,600 ($8,000 minus $2,400), payable to the beneficiary of B only by reason of the death of B, is considered an amount payable solely by reason of B's death. Accordingly, $5,000 may be excluded from the gross income of the beneficiary receiving such payment.

Example (5). The X Corporation instituted a retirement plan for its employees, the cost thereof being borne entirely by the corporation. The plan provided, in part, as follows: If, after 10 years of service, an employee left the employ of the corporation, either voluntarily or involuntarily, before retirement, a percentage of the reserve provided for the employee in the pension trust fund would be paid the employee as follows: 10 to 15 years of service, 25 percent; 15 to 20 years of service, 50 percent; 20 to 25 years of service, 75 percent; 25 years of service or over, 100 percent. The plan further provided that if an employee died

before reaching retirement age, his beneficiary would receive a percentage of the reserve provided for the employee in the retirement fund, on the same basis as shown in the preceding sentence. Y, an employee of the X Corporation for 17 years, died while in the employ of the corporation before retirement. His beneficiary received $7,500, an amount equal to 50 percent of the reserve provided for Y's retirement. No exclusion from gross income may be made by the beneficiary with respect to such payment since Y, prior to his death, had a nonforfeitable right to the payment.

PAR. 3. There is inserted immediately preceding section 29.22(b)-(2)-1 the following provisions of the Revenue Act of 1951:

SEC. 303. JOINT AND SURVIVOR ANNUITIES [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

(a) AMENDMENT OF SECTION 22(b)(2).—Section 22(b)(2) is amended by adding at the end thereof the following new subparagraph:

"(C) Joint and Survivor Annuities.—For purposes of subparagraphs (A) and (B) of this paragraph, where amounts are received by a surviving annuitant under a joint and survivor's annuity contract and the basis of such survivor annuitant's interest is determined under section 113(a)(5) the consideration paid for such survivor's annuity shall be considered to be an amount equal to such basis."

* * * * * * *

(c) EFFECTIVE DATES.—The amendments made by this section shall be applicable to taxable years ending after December 31, 1950.

PAR. 4. Section 29.22(b)(2)-2, as amended by Treasury Decision 5684 [C. B. 1949-1, 50], approved January 7, 1949, is further amended as follows:

(A) By inserting immediately after the first paragraph the following:

If, in the case of amounts received under a joint and survivor's annuity, the value of any part of the survivor's interest is required to be included in the gross estate of a decedent annuitant dying after December 31, 1950, under the provisions of section 811 (whether or not such estate exceeds $60,000 so as to require the filing of an estate-tax return under section 937), the basis of such interest to the survivor annuitant is considered to be the value of the life annuity to the survivor at the time of the decedent's death as determined under section 113(a)(5). Such valuation shall be substituted, effective upon the date of death of the first annuitant, in lieu of the consideration previously used, if any, for purposes of determining the taxable amounts of the annuity payments received after such date of death. Likewise, the amount of consideration determined in accordance with this rule shall, with respect to survivor annuity payments made after the death of the first annuitant, be substituted for the amount of consideration, if any, that may be recovered without inclusion in gross income.

(B) By adding the following examples after example (3) thereof:

Example (4). H and W on August 1, 1947, each contributed $90,000 toward the purchase of a joint and survivor's annuity of $12,000 a year, payable in monthly installments. On August 15, 1952, H died. There is includible in his estate under the provisions of section 811 the amount of $30,000 attributable to the decedent's interest in the annuity contract. The value of the annuity payments to be received by W subsequent to H's death (i. e., the cost of providing an annuity of $12,000 a year during the remaining life of W) is determined, under the provisions of section 113(a)(5), to be $60,000. This amount is deemed to be the consideration paid by W, effective August 15, 1952, for the annuity payments to be received by her subsequent to that date. Therefore, of the monthly payments made to W following H's death, W shall include the sum of $150, being such portion of the installment as is not in excess of 3 percent of $60,000 (the consideration deemed to have been paid) divided by 12. The full amount of the annuity will not become includible in gross income until $60,000 shall have been recovered.

Example (5). H, an employee of the M Corporation, retired on January 1, 1952. Under the company's retirement plan H was entitled, upon retirement, to elect to receive a life annuity of $2,400 annually or a reduced annuity with a provision that his wife would receive $1,200 annually during her lifetime if he should predecease her. The M Corporation inaugurated its retirement plan in 1949 and paid the entire cost of all annuities. H elected to take the reduced annuity. He died on November 1, 1952, and thereafter his wife W received $1,200 annually in equal monthly installments. By reason of H's election to accept a reduced annuity with survivor payments for his widow, there is includible in his estate under the provisions of section 811 the amount of $12,000. This is the same valuation, as determined under section 113(a)(5), placed on the annuity payments received by W subsequent to H's death. Therefore, W shall include in her gross income with respect to each monthly annuity payment received subsequent to November 1, 1952, the sum of $30, being such portion of the installment as is not in excess of 3 percent of $12,000 (the consideration deemed to have been paid) divided by 12. The full amount of the annuity payments will not become includible in gross income until $12,000 of the annuity payments received after H's death shall have been excluded from income. It is immaterial that H had no cost basis with respect to his annuity and had to include the full amount thereof in his gross income.

PAR. 5. Section 29.22(b)(2)-5, as amended by Treasury Decision 5853 [C. B. 1951-2, 90], approved August 29, 1951, is further amended by striking the first sentence of the third paragraph thereof and substituting the following:

Except as provided in section 29.22(b)(2)-2 with respect to joint and survivor annuity payments received subsequent to the death of an annuitant who died after December 31, 1950, if upon the death of a retired employee, the widow or other beneficiary of such retired employee is paid, in accordance with the terms of the annuity contract relating to the deceased employee, an annuity or other death benefit, the amounts received by or made available to her shall be included in her income to the extent that they would have been included in the income of the deceased employee had he lived and received such payments.

PAR. 6. There is inserted immediately preceding section 29.113(a)(5)-1 the following:

SEC. 303. JOINT AND SURVIVOR ANNUITIES [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

* * * * * * *

(b) AMENDMENT OF SECTION 113(a)(5).—Section 113(a)(5) is amended by adding at the end thereof the following: "For the purposes of this paragraph, the survivor's interest in a joint and survivor's annuity shall be considered to be property 'acquired by bequest, devise, or inheritance' from the decedent if the death of the decedent was after December 31, 1950, and if the value of any part of such interest was required to be included in determining the value of the decedent's gross estate under section 811."

(c) EFFECTIVE DATES.—The amendments made by this section shall be applicable to taxable years ending after December 31, 1950.

PAR. 7. Section 29.113(a)(5)-1, as amended by Treasury Decision 5687 [C. B. 1949-1, 9], approved February 16, 1949, is further amended by adding at the end thereof the following:

(*h*) *Joint and survivor annuities.*—If, with respect to an annuitant who dies after December 31, 1950, the value of any part of a survivor's interest in a joint and survivor's annuity is required to be included in the gross estate of the deceased annuitant (whether or not such estate exceeds $60,000 so as to require the filing of an estate tax return under section 937), the basis of such interest to the survivor annuitant is considered to be the value at the time of the decedent's death. As to the taxability of survivor annuity payments in accordance with this rule, see section 29.22(b)(2)-2.

PAR. 8. Section 29.165-6, as amended by Treasury Decision 5853, is further amended as follows:

(A) By striking the first sentence of the third paragraph and substituting in lieu thereof the following:

Except as provided in section 29.22(b)(2)-2, if pension or annuity payments are continued after the death of a retired employee to his beneficiary, such beneficiary will be required to include such pension or annuity payments in income to the same extent that the deceased employee would have been required to include such payments in income had he lived to receive such payments.

(B) By adding at the end thereof the following new paragraph:

See also section 29.22(b)(1)-2 as to the limited exclusion from income of death benefits made by or on behalf of an employer in pursuance of an express contract and paid by reason of the death of an employee.

(This Treasury Decision is issued under the authority contained in secs. 62 and 3791 of the Internal Revenue Code (53 Stat. 32, 467; 26 U. S. C. 62, 3791).)

O. GORDON DELK,
Acting Commissioner of Internal Revenue.

Approved June 17, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register June 19, 1953, 8:51 a. m.)

REGULATIONS 111, SECTION 29.22(b)(2)-2: Annuities.

INTERNAL REVENUE CODE

Benefits received as an "annuity" that vary in amount with an increase or decrease in the market value of the assets from which such benefits are paid, or vary with the fluctuations of a specified and generally recognized cost-of-living index. (See Rev. Rul. 185, p. 202.)

REGULATIONS 111, SECTION 29.22(b)(2)-5: Employees' annuities. Rev. Rul. 181

(Also Section 147, Section 29.147-2; Section 1426, Section 408.227, Regulations 128; Section 1621, Section 405.101, Regulations 116.)

INTERNAL REVENUE CODE

An amount paid by an employer exempt from Federal income tax under section 101(6) of the Internal Revenue Code as an insurance premium for the purchase of an annuity contract of the type referred to in section 22(b)(2)(B) of the Code is not required to be included in the income of the employee for whom the annuity is purchased. The employee will be taxed upon the basis of the amounts he actually receives under the annuity contract and at the time he receives such annuity payments. The payment of the insurance premium by the employer does not fall within the meaning of the term "wages" as defined in section 1621 of the Code or section 1426(a)(3) of the Federal Insurance Contributions Act. Therefore, such payment is not subject to withholding either for Federal employment or income tax purposes. The employer is not required to file an information return, Form 1099, under section 147 of the Code, with respect to such payment.

REGULATIONS 111, SECTION 29.22(b)(2)-5: Employees' annuities.

INTERNAL REVENUE CODE

Regulations 111 amended. (See T. D. 6033, p. 203.)

REGULATIONS 111, SECTION 29.22(b)(2)-5: Employees' annuities.

INTERNAL REVENUE CODE

Benefits received under an annuity contract purchased for an employee by an employer exempt under section 101(6) of the Internal Revenue Code. (See Rev. Rul. 185, p. 202.)

SECTION 22(n).—GROSS INCOME: DEFINITION OF "ADJUSTED GROSS INCOME"

REGULATIONS 111, SECTION 29.22(n)-1: Adjusted gross income.

INTERNAL REVENUE CODE

Transportation expenses of employees working on a temporary construction project located at a distance from their regular place of employment. (See Rev. Rul. 190, p. 303.)

SECTION 23(a).—DEDUCTIONS FROM GROSS INCOME: EXPENSES

REGULATIONS 111, SECTION 29.23(a)-1: Business expenses. Rev. Rul. 131
(Also Section 29.23(a)-13; Section 22(a), Section 29.22(a)-1.)

INTERNAL REVENUE CODE

Amounts contributed by the taxpayer to promote the rehabilitation of its employees and their families who sustained injuries or damages in a tornado are deductible as ordinary and necessary business expenses under section 23(a)(1)(A) of the Internal Revenue Code. Since such contributions are not related to services rendered but are based solely on need, they do not constitute income to the employees for Federal income tax purposes.

Advice is requested relative to the status, for Federal income tax purposes, of amounts contributed by the instant taxpayer to promote the rehabilitation of its employees and their families, who were injured or sustained damages to their property as a result of a tornado.

The taxpayer corporation is one of the largest employers in the disaster area. Most of its employees, who lived in residential communities hardest hit by the tornado, suffered immediate losses including lives of family members, injuries, and severe property damage extending, in some instances, to the complete destruction of their homes. Hundreds of automobiles and other items of personal property were either completely or partially destroyed. A disaster committee was created immediately after the disaster, by a resolution of the board of directors of the corporation, to assist in the rehabilitation of its em-

ployees and their families. A fund tentatively set at 500x dollars was established from which contributions are to be made to employees and their families and pensioners. No payment from the fund is to be made by the committee for injuries resulting from any act of the corporation nor for any injuries normally occurring in the course of employment. The payments, which are to be made to employees who are not directors or officers of the corporation, are for purposes of rehabilitation not actually compensated for by insurance or other sources, and are to be made without regard to length or type of service.

Section 23(a)(1)(A) of the Internal Revenue Code provides in part that in computing net income there shall be allowed as deductions "All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, * * *." Section 29.23(a)-13 of Regulations 111 provides in pertinent part that "Donations to organizations other than those described in section 23(q) which bear a direct relationship to the corporation's business and are made with a reasonable expectation of a financial return commensurate with the amount of the donation may constitute allowable deductions as business expenses."

The maintenance of the goodwill of a community in which a business enterprise has its establishment, is of prime importance to the enterprise because of the effect on its progress and on its income. Moreover, since the community is generally the source of labor supply, a vital consideration is the morale of the employees in their own community. These and like considerations lead to the conclusion that amounts expended by way of rehabilitation of employees for injuries and damages sustained in a major disaster have a direct bearing on the retention of the employer's goodwill and the morale of the employees, which in turn are essential to the successful conduct of the business. It is accordingly held that such amounts, expended or properly accrued, will be allowable as ordinary and necessary business expenses under section 23(a)(1)(A) of the Internal Revenue Code. (See *Corning Glass Works* v. *Lucas*, 37 Fed. (2d) 798; *Sugarland Industries* v. *Commissioner*, 15 B. T. A. 1265, acquiescence, C. B. VIII-2, 50; and *Slaymaker Lock Co.* v. *Commissioner*, 18 T. C. 1001, acquiescence, page 6, this Bulletin.)

The instant contributions, which are not related to services rendered and are not measured by length of service or type of employment, are to be made to employees, not including directors and officers, who because of their relationship with the corporation turn naturally to it for help. Such contributions, measured solely by need, are considered gratuitous and spontaneous. The objective of the corporation is to try to place the employees in the same economic position, or as near to it as possible, which they had before the casualty. In the light of these considerations, it is held that the payments in question do not come within the concept of gross income under the provisions of section 22(a) of the Code and therefore should not be included in the gross income of the recipients for Federal income tax purposes.

In computing casualty loss deductions, the recipients of the rehabilitation payments should take them into consideration to the extent that such amounts are used by them as reimbursement for or replacement of property damaged or destroyed, in addition to reimbursement from other sources. If the reimbursements should exceed the recipient's

basis in the property prior to the casualty, the amount of the excess cannot be used to increase the basis of the property.

REGULATIONS 111, SECTION 29.23(a)-1: Business expenses. Rev. Rul. 210
(Also Section 22(a), Section 29.22(a)-3.)

INTERNAL REVENUE CODE

An employer purchased an individual accident insurance policy for each of its salesmen and will continue to pay the premiums thereon. Such policies provide an accidental death benefit and weekly indemnity for total disability. The employer retained no incident of ownership in the policies and the employees have full rights, benefits, and privileges thereunder, including the right to name the beneficiary. *Held*, (1) the premiums paid by the employer on the individual accident insurance policies purchased for its salesmen are allowable deductions under section 23(a)(1)(A) of the Internal Revenue Code, and (2) the premiums paid on such policies constitute taxable income to the salesmen under section 22(a) of the Code.

REGULATIONS 111, SECTION 29.23(a)-1: Business expenses.

INTERNAL REVENUE CODE

Regulations 111 amended. (See T. D. 6028, p. 100.)

REGULATIONS 111, SECTION 29.23(a)-1: Business expenses.

INTERNAL REVENUE CODE

Amount contributed by taxpayer corporation for purpose of constructing a hospital building to be used by its employees. (See Rev. Rul. 160, below.)

REGULATIONS 111, SECTION 29.23(a)-1: Business expenses.

INTERNAL REVENUE CODE

Transportation expenses of employees working on a temporary construction project located at a distance from their regular place of employment. (See Rev. Rul. 190, p. 303.)

REGULATIONS 111, SECTION 29.23(a)-13: Corporate contributions. Rev. Rul. 160
(Also Section 29.23(a)-1.)

INTERNAL REVENUE CODE

An amount contributed by a corporation to its Employees' Hospital Association for the purpose of constructing a hospital building to be used by its employees is deductible as an ordinary and necessary business expense under section 23(a)(1)(A) of the Internal Revenue Code.

Advice is requested whether an amount contributed by the taxpayer corporation to its Employees' Hospital Association for the construction of a new hospital building, title and complete ownership of which will be in the association, is deductible as an ordinary and necessary business expense under section 23(a) of the Internal Revenue Code.

In the instant case the Employees' Hospital Association, an unincorporated association of the taxpayer corporation's employees, exempt from Federal income tax under the provisions of section 101(8) of the Code, operates the present hospital, which is owned by the taxpayer corporation, for the benefit of its members who are entitled to medical, surgical, and hospital services without charge. The association derives its income from assessments on the corporation's officers and employees who are required to become members of the association and revenue from outside patients. Dependents of members are treated at less than the regular rates to nonmembers. Since there are no other hospitals located in the community nor within a radius of 50 miles, outside patients are admitted to the hospital, but are required to pay regular hospital rates. The association also assumes a responsibility to the various welfare organizations in that part of the State for the care and treatment of indigent patients. The present hospital facilities have been found to be inadequate for the proper care of the corporation's employees. Accordingly, the association has purchased from the corporation at current market values, the vacant land adjoining the present hospital for the purpose of constructing a new hospital building thereon. The corporation has contributed to the association an amount of money estimated as necessary to construct such building, however, that contribution was less than 3 percent of net income after taxes. Title and complete ownership of the new building will be in the association. The question presented is whether the amount contributed by the corporation is deductible from the gross income of the corporation as an ordinary and necessary business expense under the provisions of section 23(a) of the Code.

Section 23(a)(1)(A) of the Code provides in part that in computing net income there shall be allowed as deductions "All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, * * *." Section 29.23(a)-13 of Regulations 111 provides in pertinent part that "Donations to organizations other than those described in section 23(q) which bear a direct relationship to the corporation's business and are made with a reasonable expectation of a financial return commensurate with the amount of the donation may constitute allowable deductions as business expenses."

The courts have consistently allowed deductions for cash contributions made by taxpayers in the interest of securing additional hospital facilities which tend to promote the general well-being and welfare of their employees. In the case of *Sugarland Industries* v. *Commissioner*, 15 B. T. A. 1265, acquiescence, C. B. VIII-2, 50, where similar circumstances were involved, the Board of Tax Appeals held that the taxpayer was entitled to deduct the full amount of its contribution for the erection of a hospital as an ordinary and necessary business expense pursuant to section 234(a)(1) of the Revenue Act of 1918, which corresponds to section 23(a)(1)(A) of the Code cited above.

In determining that this amount represented an ordinary and necessary expense of the business, the Board pointed out that the taxpayer in making the expenditure made it "* * * as a business proposition wherein the expenditure represented a consideration for a benefit flowing directly to it and as an incident to its business."

Similar conclusions were reached by the courts in other cases where the facts were analogous to those in the instant case. (See *Corning Glass Works* v. *Lucas*, 37 Fed. (2d) 798; *Appeal of Poinsett Mills*, 1 B. T. A. 6; acquiescence, C. B. VIII-2, 42, *Franklin Mills* v. *Commissioner*, 7 B. T. A. 1290, acquiescence, C. B. VIII-2, 18; *Weil Clothing Co.* v. *Commissioner*, 13 T. C. 873, acquiescence, C. B. 1950-1, 5; and *Slaymaker Lock Co.* v. *Commissioner*, 18 T. C. 1001, acquiescence, p. 6, this Bulletin. See also I. T. 2653, C. B. XI-2, 94.)

In view of the foregoing, it is held that an amount contributed by a corporation to its Employees' Hospital Association for the purpose of constructing a hospital building for the use of its employees, title and complete ownership of the hospital building to be in the association, is deductible as an ordinary and necessary business expense under section 23(a)(1)(A) of the Internal Revenue Code.

REGULATIONS 111, SECTION 29.23(a)-13: Corporate contributions.

INTERNAL REVENUE CODE

Amounts contributed by taxpayer for purpose of rehabilitating employees after major disaster. (See Rev. Rul. 131, p. 112.)

SECTION 23(c).—DEDUCTIONS FROM GROSS INCOME: TAXES GENERALLY

REGULATIONS 111, SECTION 29.23(c)-1: Taxes. Rev. Rul. 142

INTERNAL REVENUE CODE

The tax on spiritous distilled liquors imposed by section 18-85 of the General Statutes of North Carolina of 1943, as amended, constitutes a retail sales tax within the meaning of section 23(c)(3) of the Internal Revenue Code, and to the extent that such tax is added to the sales price of the liquor and paid by the purchaser (other than in connection with his trade or business) it is deductible by him in arriving at his net income for Federal income tax purposes.

The taxes imposed on fortified wines and those on beer, ale, etc., by sections 18-85.1 and 18-81, respectively, of the above statutes, as amended, are imposed upon the manufacturer, distributor, or retailer and are not retail sales taxes within the meaning of section 23(c)(3) of the Internal Revenue Code. However, such taxes may be deducted under section 23(c)(1) of the Code by the manufacturer, distributor, or retailer who purchases and affixes the tax stamps, crowns, or lids to the containers in which such beverages are sold.

REGULATIONS 111, SECTION 29.23(c)-1: Taxes. Rev. Rul. 192

INTERNAL REVENUE CODE

The Pennsylvania State cigarette stamp tax imposed by the Cigarette Tax Act, 72 P. S. sections 3154–3167 (Purdon's Pennsylvania Statutes Annotated), is not a tax upon the retailer or upon the consumer and may not be deducted by the consumer, for Federal income tax purposes, under section 23(c) of the Internal Revenue Code.

REGULATIONS 111, SECTION 29.23(c)-2: Federal duties and excise taxes.

INTERNAL REVENUE CODE

Regulations 111 amended. (See T. D. 6028, p. 100.)

SECTION 23(d).—DEDUCTIONS FROM GROSS INCOME: TAXES ON SHAREHOLDER PAID BY CORPORATION

REGULATIONS 111, SECTION 29.23(d)-1: Tax on bank or other stock.

INTERNAL REVENUE CODE

Double allowance of Pennsylvania tax imposed on bank shares. (See Ct. D. 1762, p. 439.)

SECTION 23(e).—DEDUCTIONS FROM GROSS INCOME: LOSSES BY INDIVIDUALS

REGULATIONS 111, SECTION 29.23(e)-5: Losses of farmers.

INTERNAL REVENUE CODE

Loss of livestock due to natural causes. (See Rev. Rul. 195, p. 169.)

SECTION 23(f).—DEDUCTIONS FROM GROSS INCOME: LOSSES BY CORPORATIONS

REGULATIONS 111, SECTION 29.23(f)-1: Losses by corporations. Ct. D. 1761

INCOME TAX—INTERNAL REVENUE CODE—DECISION OF COURT

1. GROSS INCOME—DEDUCTIONS—CAPITAL LOSS—ASSOCIATED PRESS MEMBERSHIP—DIMINUTION IN VALUE BY REASON OF SUPREME COURT DECISION.

Taxpayer, a publisher of a newspaper and a member of the Associated Press, did not sustain a deductible capital loss under section 23(f) of the Internal Revenue Code by reason of the decision of the Supreme Court of the United States in the case of *Associated Press* v. *United States*, 326 U. S. 1, which held illegal, under the Sherman Anti-Trust Act, the bylaws of the Associated Press which granted taxpayer as a member thereof an exclusive membership in the association and the exclusive right to Associated Press services in the community. Although it may be conceded that the decision by the

Supreme Court effected a diminution in value of the Associated Press membership, the present membership still enables the taxpayer to receive all the services therefrom that it received before such decision. So long as the membership is being retained and used in the business, in the same way, for the same purposes and with the same beneficial results, it cannot be said to have no value.

2. DECISION AFFIRMED.

Decision of The Tax Court of the United States, 18 T. C. 86 (1952) affirmed.

3. CERTIORARI DENIED.

Petition for certiorari denied on June 15, 1953.

UNITED STATES COURT OF APPEALS, TENTH CIRCUIT

The Reporter Publishing Company, Inc., petitioner, v. *Commissioner of Internal Revenue, respondent*

On petition to review the decision of The Tax Court of the United States

Before BRATTON, HUXMAN, and MURRAH, United States Circuit Judges

[January 30, 1953]

OPINION

HUXMAN, Circuit Judge.

The question presented for our consideration is whether the appellant taxpayer sustained a deductible capital loss for income tax purposes by reason of the decision of the Supreme Court of the United States in *Associated Press* v. *United States*, 326 U. S. 1, holding illegal the bylaws of the Associated Press granting to appellant as a member thereof an exclusive membership in the association and the exclusive right to Associated Press services in its community. The Tax Court in a decision review by the full court unanimously held that no deductible loss was sustained and the taxpayer has appealed.

On March 1, 1940, taxpayer purchased the assets of the Independence Daily Reporter, a daily newspaper published at Independence, Kansas, for a total consideration of $150,000. A bond issue was necessary to finance the purchase of the paper. Included in the assets was a membership in the Associated Press which was valued by the engineer for the brokerage firm handling the bond issue at $70,735. The Associated Press membership under the bylaws existing at that time entitled the taxpayer to the exclusive news gathering facilities of the Associated Press. Without appellant's consent, no competing paper in its territory could obtain such a membership and the benefits flowing therefrom. The taxpayer assigned a value of $79,734.67 to the Associated Press membership on its books.

In its decision the Supreme Court held that the bylaws of the Associated Press relating to the conditions under which new members might be admitted in territory where a newspaper held such a membership were illegal because they unlawfully restrained trade in violation of the Sherman Anti-Trust Act.[1] The effect of the decision was to prohibit any restriction upon a new membership based solely upon the status of the new member with respect to competition with an existing membership.

Following the decision by the Supreme Court, the taxpayer reduced the value of its membership on its books from $79,734.67 to $50,000 and took in its income tax return for the fiscal year in question a deduction of the difference of $29,734.67 from its gross income as a loss sustained in that year, resulting from such decision. The Commissioner disallowed the deduction and imposed resulting deficiencies in tax. Before the Tax Court the taxpayer took the position that the decision of the Supreme Court completely destroyed the value of the capital asset consisting of the Associated Press membership; that its total value as reflected on its books should have been deducted and that the tax accountant who prepared the return failed to take the full deduction because he did not realize the legal effect of the decision. That was its position before the Tax Court and was the theory on which the case was tried and decided and that is the position it takes on this appeal.

[1] 26 Stat. 209, 15 U. S. C. A. 1, et seq.

There is no dispute in the applicable principles of income tax law relating to capital gains and capital losses or to the factors that must exist before one is chargeable with a capital gain or may take the benefit of a capital loss as a deduction from gross income. A taxpayer is not chargeable with a capital gain resulting from an enhanced value of a capital asset while it is still being used in the business; neither may he take a deduction from gross income because of the diminution in value of such an asset while it is still a part of the business and is being used in the business. Since there is no conflict in the decisions with respect to these principles of law, citing numerous decisions in support thereof would be superfluous and add nothing of value to the opinion.

Section 29.23(e)-1 promulgated under the Internal Revenue Code and made applicable to corporations by section 29.23(f)-1 provides that "losses for which an amount may be deducted from gross income must be evidenced by closed and completed transactions, fixed by identifiable events, bona fide and actually sustained during the taxable period for which allowed. Substance and not mere form will govern in determining deductible losses." And section 29.23(e)-3 so far as material provides that when "the usefulness in the business of some or all of the assets is suddenly terminated, so that the taxpayer discontinues the business or discards such assets permanently from use in such business, he may claim as loss for the year in which he takes such action the difference between the basis * * * and the salvage value of the property."

These regulations implementing the statute make it clear that before one may take a capital loss deduction the capital asset must be liquidated, generally by sale, or in event by some definitely identifiable event or, if its usefulness in the business has been destroyed and it is not sold, it must be permanently discarded from use in the business.

Since deductions from gross income are matters of legislative grace, one who seeks the benefit thereof must bring himself clearly within the statute or an effective regulation authorizing the deduction.[2] In line with these principles it has been held consistently that a deduction under the statute and regulation in question may be claimed only when there is a closed transaction during the taxable year, generally evidenced by a sale of the asset or abandonment of the asset as completely worthless.[3]

For the purpose of the opinion, it may be conceded that the decision by the Supreme Court effected a diminution in value of the Associated Press membership. It is no doubt much less desirable since the holder thereof may no longer prevent a competitor from having such a membership. But this is a far cry from saying that it is valueless. The present membership still enables the taxpayer to receive all the services therefrom that he received before the decision by the Supreme Court. If it did not hold this membership, it would be seriously handicapped in the conduct of its business. If it did not hold such membership and applied for one, it would be required to pay an initial charge in addition to the regular charges for the services furnished and, if the taxpayer sold his business and transferred the membership with it, the purchaser likewise would be entitled to full benefits of the membership without the payment of initial fees, which otherwise would be required. There are other elements of value in the ownership of this membership which need not, however, be spelled out because in any event appellant has not brought itself within the statutory provisions entitling it to the claimed deduction. The best evidence of value is found in the fact that appellant continues to use the membership in the same way and with the same benefits as before the decision by the Supreme Court. If the membership had no value or utility, it would be a simple matter to surrender it and eliminate it entirely from the business. Then appellant would be entitled to the claimed deduction. But so long as the membership is being retained and used in the business, in the same way, for the same purposes and with the same beneficial results, it cannot be said to have no value.

We think the conclusions reached by us find support in the case of *Consolidated Freight Lines* v. *Commissioner*, 101 F. 2d 813 [Ct. D. 1421, C. B. 1939-2, 206]. There the monopolistic rights of a certificate of public convenience and necessity for which a valuable consideration had been paid were conferred by statute. A

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[2] *Interstate Transit Lines* v. *Commissioner*, 319 U. S. 590 [Ct. D. 1586, C. B. 1943, 1016]; *Commissioner of Internal Revenue* v. *Thompson* (10th Cir.), 193 F. 2d 586 [Ct. D. 1744, C. B. 1952-1, 26]; *Chicago Mines Co.* v. *Commissioner* (10th Cir.), 164 F. 2d 785; *Hales-Mullaly* v. *Commissioner* (10th Cir.), 131 F. 2d 509.

[3] *Pugh* v. *Commissioner*, 49 F. 2d 76; *Commissioner* v. *McCarthy*, 129 F. 2d 84; In re Rae's Estate, 147 F. 2d 204; *Louisiana Land and Exploration Co.* v. *Commissioner*, 161 F. 2d 842.

statute subsequent to the purchase of the certificate abolished and wiped out the monopolistic features of the certificate. It was contended, as here, that this destroyed the value of the certificate and entitled the taxpayer to a capital loss deduction. While the facts are not identical with the facts in this case, we think the court's conclusion that the destruction of the monopoly resulted only in a diminution of value of the certificate is equally applicable here.

Affirmed.

SECTION 23(k).—DEDUCTIONS FROM GROSS INCOME: BAD DEBTS

REGULATIONS 111, SECTION 29.23(k)-5: Reserve for bad debts. — Rev. Rul. 182

INTERNAL REVENUE CODE

A building and loan association which, pursuant to section 313 of the Revenue Act of 1951, is subject to income tax for taxable years beginning after December 31, 1951, has surplus, undivided profits, and reserves at the beginning of a given taxable year aggregating less than 12 percent of its total withdrawable accounts outstanding at the year's end. After having allocated the requisite amounts out of total income to meet operating expenses and pay dividends on withdrawable savings accounts, it credited the balance (1) to reserves established solely for the purpose of absorbing losses, and (2) to undivided profits available for dividend distribution. The amounts credited to the reserve for absorbing losses are mandatory under Federal and State statutes, regulations, or supervisory orders, and the balance, credited to undivided profits, comprises an amount which, if otherwise credited as an addition to the reserve for losses or as a credit to a reserve maintained for bad debts, would be permissive under such statutes, regulations, or orders. *Held*, the amount of income so allocated to undivided profits under circumstances not foreclosing its availability for dividend distribution will not be deemed to have been credited to the bad debt reserve or similar accounts referred to in section 29.23(k)-5(b)(3) of Regulations 111, and such amount is not deductible from gross income. Additional credits to reserves of the type contemplated in section 29.23(k)-5(b)(3)(ii) furnish additional protection against loss to the depositors or owners of withdrawable accounts and are treated as deductions for income tax purposes. Accordingly, the amount of income allocated to undivided profits is subject to Federal income tax and, under the circumstances here indicated, constitutes net income for the purpose of computing the 5 percent limitation on charitable and other contributions allowable as a deduction under section 23(q) of the Internal Revenue Code.

SECTION 23(m).—DEDUCTIONS FROM GROSS INCOME: DEPLETION

REGULATIONS 111, SECTION 29.23(m)-1: Depletion of mines, oil and gas wells, other natural deposits, and timber; depreciation of improvements. — T. D. 6031

(Also Section 114, Section 29.114-1; Section 453, Section 40.453-2, Regulations 130.)

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 29 AND PART 40

Regulations 111 and Regulations 130 amended to conform to section 319 of the Revenue Act of 1951, and to Public Law 594 (82d Cong., 2d sess.).

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

On October 29, 1952, notice of proposed rulemaking with respect to amendments conforming the income tax and excess-profits tax regulations to section 319 of the Revenue Act of 1951, approved October 20, 1951, and to Public Law 594, Eighty-second Congress, second session, approved July 21, 1952, was published in the Federal Register (17 F. R. 9745). After consideration of such relevant suggestions as were presented by interested persons regarding the proposals, the following amendments to Regulations 111 [26 CFR, pt. 29] and Regulations 130 [26 CFR, pt. 40] are hereby adopted:

REGULATIONS 111

PARAGRAPH 1. Section 29.23(m)–1(*f*), as amended by Treasury Decision 6021, approved June 18, 1953 [26 CFR 29.23(m)–1(f)], is further amended as follows:

(A) By inserting in (3) of the fifth paragraph thereof immediately after the word "sintering" the following "(agglomerating by incipient fusion)";

(B) By substituting in (4) of the fifth paragraph thereof the word "minerals" for the word "ores" which precedes the phrase "which are not customarily sold";

(C) By substituting in (4) of the fifth paragraph thereof the word "mineral" for the word "ore" which appears at the end of the first sentence; and

(D) By inserting immediately following the fifth paragraph thereof the following new undesignated paragraphs:

In addition, the processes listed below are not included in the term "ordinary treatment processes" unless such processes are (i) otherwise provided for in (1), (2), (3), or (4) above; (ii) necessary or incidental to the processes provided for in (1), (2), (3), or (4) above; or (iii) necessary to bring the ores or minerals into condition or form suitable for shipment (for example, the agglomeration of concentrates):

(A) treatment effecting a chemical change,
(B) blending with other material,
(C) thermal action,
(D) fine pulverization, pressing into shape, or molding.

For the purposes of (3) and (4) above, the terms "concentration" or "concentrating" mean the process of eliminating waste or of separating two or more minerals or ores.

PAR. 2. Section 29.23(m)–3, as amended by Treasury Decision 5645, approved July 20, 1948 [26 CFR 29.23(m)–3], is further amended by substituting for the heading and first two sentences of the first paragraph the following:

SEC. 29.23(m)-3. COMPUTATION OF DEPLETION OF MINES AND OTHER NATURAL DEPOSITS (OTHER THAN THOSE IN RESPECT OF WHICH PERCENTAGE DEPLETION IS ALLOWABLE) ON BASIS OF DISCOVERY VALUE.—The basis on which depletion is to be computed in the case of mines and other natural deposits (other than those in respect of which depletion is allowed on the basis of percentage of income under section 29.23(m)-5) discovered by the taxpayer after February 28, 1913, is the fair market value of the property at the date of discovery or within 30 days thereafter, if such mines or deposits were not acquired as the result of purchase of a proven tract or lease, and if the fair market value of the property is materially disproportionate to cost. Such basis may not be used in the case of the mines or deposits listed under section 29.23(m)-5 for any period in respect to which depletion on the basis of percentage of income is allowable.

PAR. 3. Section 29.23(m)-5, as amended by Treasury Decision 5645 [26 CFR 29.23(m)-5], is further amended as follows:

(A) By substituting for the heading and the first sentence of the first paragraph the following:

SEC. 29.23(m)-5. COMPUTATION OF DEPLETION BASED ON PERCENTAGE OF INCOME IN CASE OF CERTAIN MINES OR OTHER NATURAL DEPOSITS.—In the case of the mines or other natural deposits listed hereinafter, a taxpayer may deduct for depletion under section 114(b)(4)(A) amounts equal to the following percentages of the gross income from the property during the periods indicated below:

Mine or deposit	*Percent*	*Taxable years beginning after*
Aplite	15	(1)
Asbestos	10	(1)
Barite	15	Dec. 31, 1943
Bauxite	15	Dec. 31, 1946
Bentonite	15	Do.
Beryl	15	Dec. 31, 1943
Borax	15	(1)
Bromine	5	(1)
Brucite	10	(1)
Calcium carbonates	10	(1)
Calcium chloride	5	(1)
Clam shell	5	(1)
Clay, ball	15	Dec. 31, 1941
Clay, brick and tile	5	(1)
Clay, china	15	Dec. 31, 1946
Clay, refractory and fire	15	(1)
Clay, sagger	15	Dec. 31, 1941
Coal	5	Do.
Coal	10	(1)
Diatomaceous earth	15	(1)
Dolomite	10	(1)
Feldspar	15	Dec. 31, 1943
Fluorspar	15	Dec. 31, 1941
Fuller's earth	15	(1)
Garnet	15	(1)
Gilsonite	15	Dec. 31, 1946
Granite	5	(1)
Graphite, flake	15	Dec. 31, 1942
Gravel	5	(1)
Lepidolite	15	Dec. 31, 1943
Limestone, chemical grade	15	(1)
Limestone, metallurgical grade	15	(1)
Magnesite	10	(1)
Magnesium carbonates	10	(1)
Magnesium chloride	5	(1)
Marble	5	(1)
Metal mines	15	Dec. 31, 1941
Mica	15	Dec. 31, 1943

Mine or deposit	Percent	Taxable years beginning after
Oyster shells	5	(1)
Perlite	10	(1)
Phosphate rock	15	Dec. 31, 1946
Potash	15	Dec. 31, 1943
Pumice	5	(1)
Pyrophillite	15	Dec. 31, 1946
Quartzite	15	(1)
Rock asphalt	15	Dec. 31, 1941
Sand	5	(1)
Scoria	5	(1)
Shale	5	(1)
Slate	5	(1)
Sodium chloride	5	(1)
Spodumene	15	Dec. 31, 1943
Stone	5	(1)
Sulphur	23	Dec. 31, 1941
Talc	15	Dec. 31, 1943
Thenardite	15	Dec. 31, 1946
Tripoli	15	(1)
Trona	15	Dec. 31, 1946
Vermiculite	15	Dec. 31, 1943
Wollastonite	10	(1)

[1] Effective January 1, 1951. For taxable years beginning before January 1, 1951, and ending after December 31, 1950, see below.

Such deduction shall not in any case exceed 50 percent of the net income of the taxpayer (computed without allowance for depletion) from the property.

By inserting immediately following the first paragraph the following new paragraph:

For the purposes of this section, the minerals indicated below shall have the following meanings:

Borax	Any boron material including that contained in brines.
Bromine	Bromine if obtained from brine wells.
Calcium carbonates	Miscellaneous limestones and other calcium carbonate rocks (not specifically provided for at a 5 percent or 15 percent rate of percentage allowance) such as cement rock and limestone used or sold for use in soil treatment. This classification does not include rock or minerals used or sold for use as ballast, road making, concrete aggregates, or other purposes for which chemical composition is not a major requirement.
Calcium chloride	Calcium chloride if produced from brine wells.
Clay, brick, and tile	Clay used or sold for use in the manufacture of common brick, drain and roofing tile, sewer pipe, flower pots and kindred products (other than clay specifically identified as a clay for which a 15 percent rate of percentage allowance is provided).

Coal	All coal including lignite.
Limestone, chemical grade	Limestone used or sold for use in the chemical trades.
Limestone, metallurgical grade	Limestone used or sold for use in the production of metals.
Magnesium chloride	Magnesium chlorides if produced from brine wells.
Phosphate rock	Any phosphate ore.
Pumice	All pumice including pumicite.
Scoria	All scoria produced from natural deposits.
Stone	All common dimension, crushed or broken stone within the ordinary meaning of these terms.
Thenardite	All sodium sulfate minerals, including those contained in brine.
Trona	All sodium carbonate minerals including those contained in brine.

(C) By inserting immediately following the last paragraph the following new paragraphs:

In the case of a taxpayer whose taxable year began before January 1, 1951, and ended after December 31, 1950, and who became entitled to percentage depletion, or an increase therein, or whose basis for depletion changed on January 1, 1951, the allowance for depletion for the taxable year under this section is an amount equal to the sum of:

(1) That portion of a tentative allowance computed under the provisions of this section (without regard to the amendments to section 114(b)(4) effective January 1, 1951), which the number of days in such taxable year prior to January 1, 1951, bears to the total number of days in such taxable year; plus

(2) That portion of a tentative allowance computed under the provisions of this section as though the amendments to section 114(b)(4), effective January 1, 1951, were applicable to the entire taxable year, which the number of days in such taxable year after December 31, 1950, bears to the total number of days in such taxable year.

For taxable years ending after December 31, 1950, percentage depletion is not allowable with respect to any disposal of coal to the extent that such disposal is treated as a sale of coal under section 117(k)(2).

PAR. 4. Section 29.23(m)-8 [26 CFR 29.23(m)-8] is amended by substituting for the first sentence of the first paragraph the following:

No revaluation of a property whose value as of any specific date has been determined and approved will be made or allowed during the continuance of the ownership under which the value was so determined and approved, except in the case of a subsequent discovery of nonmetallic minerals in respect to which depletion is not allowed on the basis of percentage of income under section 29.23(m)-4 or 5, or of misrepresentation or fraud or gross error as to any facts known on the date as of which the valuation was made.

PAR. 5. Section 29.23(m)-10(*d*), as amended by Treasury Decision 5645 [26 CFR 29.23(m)-10(d)] is further amended to read as follows:

(d) In lieu of the treatment provided for in paragraphs (*a*) and (*b*) above, the owner of an economic interest in minerals in respect of which depletion is allowed on the basis of percentage of income under section 29.23(m)-4 or 5 may take as a depletion deduction in respect of any bonus or advanced royalty from the property for the taxable year or period for which such deduction is allowable under such section an amount computed on the basis of the percentages applicable as indicated in such sections; but the deduction shall not in any case exceed 50 percent of the net income of the taxpayer (computed without allowance for depletion) from the property.

PAR. 6. Section 29.23(m)-13(*a*), as amended by Treasury Decision 5645 [26 CFR 29.23(m)-13(a)] is amended by substituting for so much of the first paragraph as precedes (1), the following:

(*a*) There shall be attached to the return of every taxpayer who claims depletion on the basis of percentage of income under section 29.23(m)-4 or 5, a statement containing the following information with respect to every property for which percentage depletion is allowable:

PAR. 7. Section 29.23(m)-14(*a*), as amended by Treasury Decision 5645 [26 CFR 29.23(m)-14(a)] is further amended by substituting for the heading and so much of paragraph (*a*) as precedes the last sentence thereof the following:

SEC. 29.23(m)-14. DISCOVERY OF MINES OR OTHER NATURAL DEPOSITS (EXCEPT THOSE IN RESPECT OF WHICH PERCENTAGE DEPLETION IS ALLOWABLE UNDER SECTION 29.23(m)-5).—(*a*) To entitle a taxpayer to a valuation of his property, for the purposes of depletion allowances, by reason of the discovery of a mine or minerals (other than those in respect of which percentage depletion is allowable under section 29.23(m)-4 or 5), it must appear that the mine or minerals were not acquired as the result of the purchase of a proven tract or lease; also the discovery must be made by the taxpayer after February 28, 1913, and must result in the fair market value of the property becoming disproportionate to cost. For the purposes of this section, mines or minerals shall not be entitled to valuation upon the basis of discovery for any taxable year or period in respect to which percentage depletion is allowable under section 29.23(m)-4 or 5.

PAR. 8. There is inserted immediately preceding section 29.114-1 [26 CFR 29.114-1] the following:

SEC. 319. PERCENTAGE DEPLETION [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

(a) ALLOWANCE OF PERCENTAGE DEPLETION.—So much of paragraph (4) of section 114(b) as precedes the last sentence of subparagraph (A) is hereby amended to read as follows:

"(4) PERCENTAGE DEPLETION FOR COAL AND METAL MINES AND FOR CERTAIN OTHER MINES AND NATURAL MINERAL DEPOSITS.—

"(A) In General.—The allowance for depletion under section 23(m) in the case of the following mines and other natural deposits shall be—

"(i) in the case of sand, gravel, slate, stone (including pumice and scoria), brick and tile clay, shale, oyster shell, clam shell, granite, marble, sodium chloride, and, if from brine wells, calcium chloride, magnesium chloride, and bromine, 5 per centum,

"(ii) in the case of coal, asbestos, brucite, dolomite, magnesite, perlite, wollastonite, calcium carbonates, and magnesium carbonates, 10 per centum,

"(iii) in the case of metal mines, aplite, bauxite, fluorspar, flake graphite, vermiculite, beryl, garnet, feldspar, mica, talc (including pyrophyllite), lepidolite, spodumene, barite, ball clay, sagger clay, china clay, phosphate rock, rock asphalt, trona, bentonite, gilsonite, thenardite, borax, fuller's earth, tripoli, refractory and fire clay, quartzite, diatomaceous earth, metallurgical grade limestone, chemical grade limestone, and potash, 15 per centum, and

"(iv) in the case of sulfur, 23 per centum,

of the gross income from the property during the taxable year, excluding from such gross income an amount equal to any rents or royalties paid or incurred by the taxpayer in respect of the property."

(b) TECHNICAL AMENDMENT.—So much of paragraph (2) of section 114(b) as precedes "discovered by the taxpayer after February 28, 1913" is hereby amended to read as follows:

"(2) DISCOVERY VALUE IN THE CASE OF MINES.—In the case of mines (except mines in respect of which percentage depletion is allowable under paragraph (4) of this subsection)".

(c) EFFECTIVE DATE.—The amendments made by this section shall be applicable only with respect to taxable years beginning after December 31, 1950.

PUBLIC LAW 594, EIGHTY-SECOND CONGRESS, APPROVED JULY 21, 1952

SEC. 5. Section 319(c) of the Revenue Act of 1951 is amended to read as follows:

"(c) EFFECTIVE DATE.—The amendments made by this section shall be effective on and after January 1, 1951."

PAR. 9. Section 29.114–1, as amended by Treasury Decision 5645 [26 CFR 29.114–1], is further amended to read as follows:

SEC. 29.114–1. BASIS FOR ALLOWANCE OF DEPRECIATION AND DEPLETION.—The basis upon which exhaustion, wear and tear, obsolescence, and depletion will be allowed in respect of any property is the same as is provided in section 113(a), adjusted as provided in section 113(b), for the purpose of determining the gain from the sale or other disposition of such property, except that as provided in section 29.23(m)–21 in the case of the cutting of timber which is considered to be a sale or exchange of such timber under section 117(k)(1), the basis shall be the fair market value of such timber as of the first day of the taxable year in which it is cut; and except as provided in section 29.23(m)–3 relating to depletion based on discovery value, in section 29.23(m)–4 relating to percentage depletion in the case of oil and gas wells; in section 29.23(m)–5 relating to percentage depletion in the case of certain minerals with respect to the applicable taxable years or effective date specified therein, and in sections 23(cc)(3) and 23(ff)(4) relating to basis for depletion for taxable years ending after December 31, 1950.

REGULATIONS 130

PAR. 10. Section 40.453–2(h) of Regulations 130 [26 CFR 40.453–2(h)] is amended by adding at the end thereof the following:

The nonmetallic minerals referred to in sections 453(a)(13) and 453(b)(2) and (4) shall be given the meanings set forth in section 29.23(m)–5 of Regulations 111.

PAR. 11. Section 40.453–2(j)(3) of Regulations 130, as amended by Treasury Decision 6004 [26 CFR 40.453–2(j)(3)], is amended as follows:

(A) By inserting in (C) of subdivision (iii) immediately after the word "sintering" the following: "(agglomerating by incipient fusion)";

(B) By substituting in (D) of subdivision (iii) the words "minerals" for the word "ores" which precedes the phrase "which are not customarily sold";

(C) By substituting in (D) of subdivision (iii) the word "mineral" for the word "ore" which appears at the end of the first sentence; and

(D) By inserting immediately following subdivision (iii) the following new undesignated paragraphs:

In addition, the processes listed below are not included in the term "ordinary treatment processes" unless such processes are (*a*) otherwise provided for in (A), (B), (C), or (D) above; (*b*) necessary or incidental to the processes provided for in (A), (B), (C), or (D) above; or (*c*) necessary to bring the ores or minerals into condition or form suitable for shipment (for example, the agglomeration of concentrates):

(*1*) treatment effecting a chemical change,
(*2*) blending with other material,
(*3*) thermal action,
(*4*) fine pulverization, pressing into shape or molding.

For the purposes of (C) and (D) above, the terms "concentration" or "concentrating" mean the process of eliminating waste or of separating two or more minerals or ores.

(This Treasury Decision is issued under the authority contained in secs. 23(m) and 62 of the Internal Revenue Code (53 Stat. 14, 32; 26 U. S. C. 23(m), 62).)

T. COLEMAN ANDREWS,
Commissioner of Internal Revenue.

Approved July 14, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register July 17, 1953, 8:50 a. m.)

REGULATIONS 111, SECTION 29.23(m)-1: Depletion of mines, oil and gas wells, other natural deposits, and timber; depreciation of improvements.

INTERNAL REVENUE CODE

Regulations 111 amended. (See T. D. 6021, p. 169.)

REGULATIONS 111, SECTION 29.23(m)-1: Depletion of mines, oil and gas wells, other natural deposits, and timber; depreciation of improvements.

INTERNAL REVENUE CODE

Processes which may be considered mining processes in the case of low-grade iron ores. (See Rev. Rul. 184, p. 158.)

SECTION 23(o).—DEDUCTIONS FROM GROSS INCOME: CHARITABLE AND OTHER CONTRIBUTIONS

REGULATIONS 111, SECTION 29.23(o)-1: Contributions or gifts by individuals. Rev. Rul. 162

INTERNAL REVENUE CODE

Furnishing blood for a transfusion, or to a blood bank is analogous to the rendering of a personal service by the donor rather than a contribution of "property" and the fair market value of blood donated by an individual to a charitable institution is not deductible as a charitable contribution under section 23(o) of the Internal Revenue Code.

Advice is requested whether the fair market value of blood donations made to a charitable institution is deductible as a charitable contribution under section 23(o) of the Internal Revenue Code.

Section 23(o) of the Internal Revenue Code provides in part that in computing net income there shall be allowed as deductions, in the case of an individual, contributions or gifts payment of which is made within the taxable year to or for the use of a corporation, trust, or community chest, fund, or foundation organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, etc., of an amount not in excess of 20 percent of the taxpayer's

adjusted gross income. Section 29.23(o)–1, of Regulations 111, promulgated under section 23(o) of the Code, provides that if the contribution or gift is other than money, the basis for calculation of the amount thereof shall be the fair market value of the property at the time of the contribution or gift.

Accordingly, allowable deductions are confined to donations of money and of things which are generally thought of as being comprehended by the term "property" as distinguished from the value of services rendered. It has been a long established policy of the Internal Revenue Service not to allow a deduction for the value of services rendered to charitable institutions. See O. D. 712, C. B. 3, 188 (1920). The Comptroller General of the United States in considering the question of reimbursement for blood transfusions has ruled that a blood transfusion involves the rendering of a personal service by the donor rather than the sale of a commodity. See 5 Comp. Gen. 658 and 888.

In view of the foregoing, it is held that furnishing blood for a transfusion or to a blood bank is analogous to the rendering of a personal service by the donor rather than a contribution of "property" and the fair market value of blood donated by an individual to a charitable institution is not deductible as a charitable contribution under section 23(o) of the Internal Revenue Code.

REGULATIONS 111, SECTION 29.23(o)–1: Contributions or gifts by individuals. Rev. Rul. 194

INTERNAL REVENUE CODE

Where a taxpayer irrevocably transfers property to a trust to be held for a period of 10 years and 10 days for the benefit of a charitable foundation meeting the requirements of section 23(o)(2) of the Internal Revenue Code, the taxpayer is entitled to a deduction of the present value of the property interest which she contributed to the trust, subject to the limitations provided by section 23(o) of the Code.

Advice is requested whether an individual is entitled to a deduction under section 23(o) of the Internal Revenue Code for transfers which she made to a trust to be held by the trust for a period of 10 years and 10 days for the benefit of a charitable foundation.

In the instant case the grantor irrevocably transferred shares of common stock to a trust to be held for the benefit of a charitable foundation for a period of 10 years and 10 days. At the expiration of that period of time, the stock will be returned to the grantor (or her estate in the event of her death) as her absolute property. The trust instrument provides that during the existence of the trust all the income from the corpus thereof shall belong absolutely to the foundation. The income of the trust is not taxable to the grantor under the provisions of Regulations 111, section 29.22(a)–21. The foundation is exempt under section 101(6) of the Code as a charitable organization.

Section 23 of the Internal Revenue Code provides in part as follows:

In computing net income there shall be allowed as deductions:

* * * * * * *

(o) CHARITABLE AND OTHER CONTRIBUTIONS.—In the case of an individual, contributions or gifts payment of which is made within the taxable year to or for the use of:

* * * * * * *

(2) a corporation, trust, or community chest, fund, or foundation, created * * * organized and operated exclusively for religious, charitable * * * purposes. * * *

* * * * * * *

to an amount which in all the above cases combined does not exceed 20 per centum of the taxpayer's adjusted gross income. * * *

The phrase "for the use of" as used in section 23(o)(2) of the Internal Revenue Code is intended to convey a meaning similar to "in trust for" and, where the beneficiary of a trust meets the requirements of that section, the value of the interest transferred in trust is deductible by the grantor in the manner and to the extent therein provided. See I. T. 37037, C. B. 1945, 114, and the case of *John Danz, et al.* v. *Commissioner*, 18 T. C., 454, acquiescence C. B. 1952-2, 1.

Accordingly, it is held that where a taxpayer irrevocably transfers property to a trust to be held for a period of 10 years and 10 days for the benefit of a charitable foundation meeting the requirements of section 23(o)(2) of the Internal Revenue Code, the taxpayer is entitled to a deduction of the present value of the property interests which she contributed to the trust, subject to the limitations provided by section 23(o) of the Code.

SECTION 23(p).—DEDUCTIONS FROM GROSS INCOME: CONTRIBUTIONS OF AN EMPLOYER TO AN EMPLOYEES' TRUST OR ANNUITY PLAN AND COMPENSATION UNDER A DEFERRED-PAYMENT PLAN

REGULATIONS 111, SECTION 29.23(p)-1: Contributions of an employer to an employees' trust or annuity plan and compensation under a deferred-payment plan—In general.

INTERNAL REVENUE CODE

Regulations 111 amended. (See T. D. 6033, p. 203.)

REGULATIONS 111, SECTION 29.23(p)-9: Contributions of an employer under an employees' annuity plan that meets the requirements of section 165(a)—Application of section 23(p)(1)(B).

INTERNAL REVENUE CODE

Pension plans which provide benefits that vary in amount with an increase or decrease in the market value of the assets from which such benefits are paid, or which provide benefits that vary with the fluctuations of a specified and generally recognized cost-of-living index. (See Rev. Rul. 185, p. 202.)

SECTION 23(x).—DEDUCTIONS FROM GROSS INCOME: MEDICAL, DENTAL, ETC., EXPENSES

REGULATIONS 111, SECTION 29.23(x)-1: Medical, dental, etc., expenses. Rev. Rul. 143

Amounts paid psychologists who are qualified and authorized under State law to practice psychology for services rendered by them in connection with the diagnosis, cure, mitigation, treatment, or prevention of disease, or for the purpose of affecting any structure or function of the body, constitute expenses paid for medical care within the meaning of section 23(x) of the Internal Revenue Code and may be deducted in computing net income for Federal income tax purposes, to the extent provided therein.

SECTION 23(z).—DEDUCTIONS FROM GROSS INCOME: AMOUNTS REPRESENTING TAXES AND INTEREST PAID TO COOPERATIVE APARTMENT CORPORATION

REGULATIONS 111, SECTION 29.23(z)-1: Amounts representing taxes and interest paid to cooperative apartment corporation. — Rev. Rul. 120

INTERNAL REVENUE CODE

A tenant-stockholder of a cooperative apartment corporation is not deprived of a deduction for his proportionate share of the corporation's interest and real estate taxes under section 23(z) of the Internal Revenue Code solely by reason of a special issue, pursuant to section 213 of the National Housing Act, of preferred stock to the Commissioner of the Federal Housing Administration in a nominal amount not exceeding $100.

Advice is requested whether a tenant-stockholder of a cooperative apartment corporation is deprived of a deduction for his proportionate share of the corporation's interest and real estate taxes under section 23(z) of the Internal Revenue Code solely by reason of a special issue, pursuant to section 213 of the National Housing Act, of preferred stock to the Commissioner of the Federal Housing Administration in a nominal amount not exceeding $100.

Section 23(z) of the Internal Revenue Code provides that in computing net income a tenant-stockholder may deduct amounts paid or accrued to a cooperative apartment corporation to the extent that such amounts represent his proportionate share of real estate taxes and interest paid or incurred by the corporation with respect to the apartment building or the land on which it is situated. In defining a cooperative apartment corporation section 23(z)(2) of the Code provides in part as follows:

> (A) COOPERATIVE APARTMENT CORPORATION.—The term "cooperative apartment corporation" means a corporation—
>
> (i) having one and only one class of stock outstanding, * * *

Under the provisions of section 213 of the National Housing Act, as added by Public Law 475, enacted by the Eighty-first Congress, 64 Stat., 48, the Federal Housing Administration is authorized to insure mortgages covering property held by nonprofit cooperative housing corporations, the permanent occupancy of the dwellings of which is restricted to members of such cooperatives. The common stock of such corporation is owned and held by the cooperative corporation members. Section IV of the Federal Housing Administration rules and regulations, governing section 213 of the National Housing Act, provides that the Certificate of Incorporation, or other instru-

ment under which the mortgagor corporation is created, will provide for the issuance of:

* * * certain shares of special stock (or other evidence of a beneficial interest in the mortgagor) which stock or interest will acquire majority voting rights in the event of default under the mortgage or violation of provisions of the charter, but only for a period coexistent with the duration of such default or violation. Such special stock or interest issued to the Commissioner * * * shall be in sufficient amount to constitute under the laws of the particular State a valid class of stock or interest and shall be issued in consideration of the payment by the Commissioner of not exceeding in the aggregate $100. * * *

Pursuant to the rules and regulations issued under section 213, the Federal Housing Administrator has issued a "Model Form of Certificate of Incorporation." Under the "Model Form of Certificate of Incorporation" the preferred stock outstanding is to be redeemed by the corporation at par after the termination of the contract of mortgage insurance and, when so redeemed, shall be retired and canceled.

The "preferred stock" issued to the Commissioner in the specified amount of $100 par value under such circumstances is issued for the purpose of granting to the Commissioner the right to acquire majority voting rights in the corporate mortgagor in the event of a default under the mortgage or a violation of the charter. The Commissioner does not make an investment in the corporation as a "shareholder." Under the charter, the "preferred stock," costing the nominal sum of $100, is created as a security device that protects the Commissioner as the insurer of the mortgage debt. That the preferred stock is not an equity interest is evident from the charter provision that the "preferred stock" is to be redeemed at par upon termination of the contract of mortgage insurance covering any indebtedness of the corporation. Assurance that the "preferred stock" will only be used as a security device is provided by making the shares nontransferable to anyone other than the Commissioner or his nominees, and redeemable, upon satisfaction of the indebtedness, only for cancellation and retirement.

The general purpose of section 23(z) of the Internal Revenue Code is to place the tenant-stockholders of a cooperative apartment in the same position as the owner of a dwelling house so far as deductions for interest and taxes are concerned. There is no reason to believe that when Congress imposed the restrictive single classification of stock under section 23(z)(2)(A)(i) of the Code that it intended that a special classification of preferred stock, issued solely as a security device, would constitute a class of stock so as to deprive tenant-stockholders of the common stock of the benefits conferred by section 23(z) of the Code. The purpose of the condition is to restrict the benefits of section 23(z) of the Code to bona fide cooperative apartment corporations. (S. Rept. No. 1631 on the Revenue Bill of 1942, C. B. 1942-2, 504, at pp. 546 and 577.)

In view of the foregoing, it is held that preferred stock issued pursuant to section 213 of the National Housing Act by a cooperative apartment corporation to the Commissioner of the Federal Housing Administration in a nominal amount not exceeding $100, is issued for the purpose of creating a security device on the mortgage debt of the corporation. Since it does not represent an equity interest in the corporation, such special stock should not be treated as a "class of

stock" within the meaning of section 23(z)(2)(A)(i) of the Internal Revenue Code. For the purpose of such section of the Code a corporation which has one and only one class of stock outstanding in addition to preferred stock held solely by the Commissioner will qualify as a "cooperative apartment corporation" if it satisfies all the other conditions of section 23(z)(2)(A) of the Code, in which case its tenant-stockholders will be entitled to deductions in their individual income tax returns for their proportionate share of the corporation's interest and taxes under section 23(z)(1) of the Code.

SECTION 23(cc).—DEDUCTIONS FROM GROSS INCOME: DEVELOPMENT OF MINES

REGULATIONS 111, SECTION 29.23(cc)-1: Mine development expenditures. T. D. 6023

(Also Sections 29.23(m)-1, 29.23(m)-2, 29.23(m)-15, 29.23(m)-17, 29.23(ff)-1; Section 24, Section 29.24-2; Section 113(b), Section 29,113(b)(1)-1.)

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 29.—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1941

Regulations 111 amended to conform to sections 309 and 342 of the Revenue Act of 1951.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

On November 6, 1952, notice of proposed rulemaking with respect to amendments conforming the income tax regulations to sections 309 and 342 of the Revenue Act of 1951, approved October 20, 1951, was published in the Federal Register (17 F. R. 9985). After consideration of such relevant suggestions as were presented by interested persons regarding the proposals, the following amendments to Regulations 111 [26 CFR, pt. 29] are hereby adopted:

PARAGRAPH 1. Section 29.23(m)-1(*g*), as amended by Treasury Decision 5458 [C. B. 1945, 45], approved June 15, 1945 [26 CFR 29.23(m)-1(g)], is further amended by changing the term "development costs properly charged to expense" appearing in the first sentence to read as follows: "development costs properly charged to expense or allowable as deductions under section 23(cc)".

PAR. 2. Section 29.23(m)-2 [26 CFR 29.23(m)-2] is amended as follows:

(A) By amending the first sentence thereof and the bracketed matter immediately following that sentence to read as follows:

The basis upon which depletion, other than discovery depletion or percentage depletion, is to be allowed in respect of any property is the basis provided for in section 113(a), adjusted as provided in section 113(b) for the purpose of determining the gain upon the sale or other disposition of such property, except that with respect to taxable years ending after December 31, 1950, the amount of expenditures treated as deferred expenses under sections 23(cc)(2) and 23(ff)(2) shall be disregarded in determining such adjusted basis (see sections 29.113(a)-1 to 29.114-1 inclusive, and sections 29.23(cc)-1 and 29.23(ff)-1 of these regulations); and

(B) By inserting immediately after the word "depreciation" in the fourth paragraph the following: ", through deferred expenses,".

PAR. 3. Section 29.23(m)-15 [26 CFR 29.23(m)-15] is amended as follows:

(A) By changing the heading thereof to read as follows: "SEC. 29.23(m)-15. ALLOWABLE CAPITAL ADDITIONS IN CASE OF MINES.—(*a*) *General.*";

(B) By deleting (*b*) which immediately precedes the beginning of the second paragraph; and

(C) By adding immediately following the second paragraph the following new paragraph:

(*b*) *Special rules for taxable years ending after December 31, 1950.*—Sections 23(cc) and 23(ff) contain special provisions for treatment of expenditures for certain exploration and development costs (other than for acquisition or improvement of depreciable property) with respect to ores and minerals other than oil or gas. See sections 29.23(cc)-1 and 29.23(ff)-1 of these regulations.

PAR. 4. Section 29.23(m)-17 [26 CFR 29.23(m)-17] is amended by adding at the end thereof the following new paragraph:

(*h*) For taxable years ending after December 31, 1950, sections 23(cc) and 23(ff) provide special rules for treatment of depreciation allowances with respect to the exploration and development of a mine or other natural deposit other than oil or gas. See sections 29.23(cc)-1 and 29.23(ff)-1.

PAR. 5. There is inserted immediately following section 29.23(bb)-1 [26 CFR 29.23(bb)-1] the following:

SEC. 309. EXPENDITURES IN THE DEVELOPMENT OF MINES [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

(a) DEDUCTION OF EXPENDITURES.—Section 23 (relating to deductions from gross income) is hereby amended by adding at the end thereof the following new subsection:

"(cc) DEVELOPMENT OF MINES.—

"(1) IN GENERAL.—Except as provided in paragraph (2), all expenditures paid or incurred during the taxable year for the development of a mine or other natural deposit (other than an oil or gas well) if paid or incurred after December 31, 1950, and after the existence of ores or minerals in commercially marketable quantities has been disclosed. This subsection shall not apply to expenditures for the acquisition or improvement of property of a character which is subject to the allowance for depreciation provided in section 23(l), but allowances for depreciation shall be considered, for the purposes of this subsection, as expenditures.

"(2) ELECTION OF TAXPAYER.—At the election of the taxpayer, made in accordance with regulations prescribed by the Secretary, expenditures described in paragraph (1) paid or incurred during the taxable year shall be treated as deferred expenses and shall be deductible on a ratable basis as the units of produced ores or minerals benefited by such expenditures are sold. In the case of such expenditures paid or incurred during the development stage of the mine or deposit, the election shall apply only with respect to the excess of such expenditures during the taxable year over the net receipts during the taxable year from the ores or minerals produced from such mine or deposit. The election under this paragraph, if made, must be for the total amount of such expenditures, or the total amount of such excess, as the case may be, with respect to the mine or deposit, and shall be binding for such taxable year.

"(3) ADJUSTED BASIS OF MINE OR DEPOSIT.—The amount of expenditures which are treated under paragraph (2) as deferred expenses shall be taken into account in computing the adjusted basis of the mine or deposit, except that such amount and the adjustments to basis provided in section 113(b)(1)(J), shall be disregarded in

determining the adjusted basis of the property for the purpose of computing a deduction for depletion under section 114."

* * * * * * *

(d) EFFECTIVE DATE.—The amendments made by this section shall be applicable to taxable years ending after December 31, 1950.

SEC. 29.23(cc)-1. MINE DEVELOPMENT EXPENDITURES.—(*a*) *Allowance of deduction.*—Effective only with respect to taxable years ending after December 31, 1950, section 23(cc)(1) provides for a deduction from gross income of all expenditures for the development of a mine or other natural deposit (other than an oil or gas well) paid or incurred by the taxpayer after December 31, 1950, and after the existence of ores or minerals in commercially marketable quantities has been disclosed subject to the following rules. The deduction is not allowable with respect to expenditures for the acquisition or improvement of property of a character subject to allowance for depreciation under section 23(l). However, allowances for depreciation shall be considered for the purposes of this section as expenditures for development to the extent allocable to development. Such development expenditures are deductible under section 23(cc)(1) (notwithstanding the provisions of section 29.23(m)-15 of these regulations) whether paid or incurred by the taxpayer while the mine or deposit is in the development or while in the production stage.

For the purposes of this section, expenditures thus described include only those which, except for this section, would not qualify as a deduction for the taxable year. For treatment of certain exploration expenditures see section 23(ff) and section 29.23(ff)-1. In general, the provisions of this section are applicable only to costs paid or incurred by the taxpayer in respect of development undertaken (directly or through a contract) by the taxpayer and do not apply, for example, to such costs of development undertaken by other persons as may be reflected in the acquisition cost paid or incurred by the taxpayer for wholly or partially developed property.

As to the deductibility of expenditures attributable to a grant or loan made to a taxpayer by the United States for the encouragement of the exploration, development, or mining of critical and strategic minerals, see section 22(b)(15).

(*b*) *Election to defer.*—A taxpayer entitled to the deduction under section 23(cc)(1) may, in lieu of taking such deduction in the year when the expenditures for development were paid or incurred, elect under section 23(cc)(2) to treat such expenditures as deferred expenses to be deducted ratably as the units of the produced ore or minerals benefited by the expenditures are sold. In the case of such expenditures paid or incurred while the mine or deposit is in the development stage, the election is applicable only in respect of the excess of such expenditures paid or incurred during the taxable year over the net receipts during the taxable year from the ore or minerals produced from the mine or deposit. The amount of such expenditures not in excess of net receipts from the ore or mineral for the taxable year while the mine or deposit is in the development stage shall be deductible in full. (See section 29.23(m)-15(*a*) of these regulations for description as to when a mine will be considered to have passed from a development to a production stage.)

The amount of the deduction allowable during the taxable year is an amount A, which bears the same ratio to B (the total deferred development expenditures for a particular mine or deposit reduced by the amount of such expenditures deducted in prior taxable years) as C (the number of units of the ore or mineral benefited by such expenditures sold during the taxable year) bears to D (the number of units of ore or mineral benefited by such expenditures remaining as of the taxable year). For the purposes of this proportion, the "number of units of ore or mineral benefited by such expenditures remaining as of the taxable year" is the number of units of ore or mineral benefited by the deferred development expenditures remaining at the end of the year to be recovered from the mine or deposit (including units benefited by such expenditures recovered but not sold) plus the number of units benefited by such expenditures sold within the taxable year. The principles outlined in section 29.23(m)-9 of these regulations are applicable in estimating the number of units remaining as of the taxable year and the number of units sold during the taxable year. The estimate is subject to revision in accordance with that section in the event it is ascertained as the result of operations or development that the remaining units are materially greater or less than the number of units remaining from a prior estimate. Sections 29.23(e)-3 and 29.23(f)-1 of these regulations contain rules relating to the treatment of losses resulting from abandonment.

If the taxpayer has paid or incurred expenditures of the character described herein, has made the election to defer such expenditures, and thereafter leases the developed property retaining a royalty interest therein, he shall be allowed the ratable deduction indicated in the foregoing paragraph.

The election referred to in this paragraph shall be made for each mine or deposit by a clear indication on the return or by a statement filed with the director of internal revenue with whom the return was filed not later than 6 months after the filing of the return for the taxable year to which such election is applicable, or, in case the return for the taxable year to which such election is applicable is filed on or before March 15, 1953, by a statement in writing to that effect filed with the director of internal revenue with whom the return was filed on or before September 15, 1953. If such an election is made by the taxpayer, such election must be for the total amount of all such expenditures during the taxable year while the mine or deposit is in the producing stage. If the mine or deposit is in the development stage, such election must be for all of the excess of such expenditures over the net receipts during the taxable year from the ore or mineral produced. The election shall be binding for the taxable year in respect to which the election was made.

PAR. 6. There is inserted immediately following section 23(ee) which follows section 29.23(dd)-1 [26 CFR 29.23(dd)-1] the following:

SEC. 342. DEDUCTION OF EXPENDITURES FOR MINE EXPLORATION [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

(a) DEDUCTION OF MINE EXPLORATION EXPENDITURES.—Section 23 (relating to deductions from gross income) is hereby amended by adding at the end thereof the following new subsection:

"(ff) DEDUCTION OF EXPLORATION EXPENDITURES.—

"(1) IN GENERAL.—In the case of expenditures paid or incurred during the taxable year for the purpose of ascertaining the existence, location, extent, or quality of any deposit of ore or other mineral, and paid or incurred prior to the beginning of the development stage of the mine or deposit, so much of such expeditures as does not exceed $75,000. This subsection shall apply only with respect to the amount of such expenditures which, but for this subsection, would not be allowable as a deduction for the taxable year. This subsection shall not apply to expenditures for the acquisition or improvement of property of a character which is subject to the allowance for depreciation provided in section 23(l), but allowances for depreciation shall be considered, for the purposes of this subsection, as expenditures paid or incurred. In no case shall this subsection apply with respect to amounts paid or incurred for the purpose of ascertaining the existence, location, extent, or quality of any deposit of oil or gas.

"(2) ELECTION OF TAXPAYER.—If the taxpayer elects, in accordance with regulations prescribed by the Secretary, to treat as deferred expenses any portion of the amount deductible for the taxable year under paragraph (1), such portion shall not be deductible under paragraph (1) but shall be deductible on a ratable basis as the units of produced ores or minerals discovered or explored by reason of such expenditures are sold. An election made under this paragraph for any taxable year shall be binding for such year.

"(3) LIMITATION.—This subsection shall not apply to any amounts paid or incurred in any taxable year if in any four preceding years the taxpayer, or any individual or corporation who has transferred to the taxpayer any mineral property under circumstances which make the provisions of paragraph (7), (8), (11), (13), (15), (17), (20), or (22) of section 113(a) applicable to such transfer, has either (A) been allowed a deduction under paragraph (1) of this subsection or (B) made the election provided under paragraph (2) of this subsection.

"(4) ADJUSTED BASIS OF MINE OR DEPOSIT.—The amount of expenditures which are treated under paragraph (2) as deferred expenses shall be taken into account in computing the adjusted basis of the mine or deposit, but such amounts, and the adjustments to basis pro-

vided in section 113(b)(1)(M) shall be disregarded in determining the adjusted basis of the property for the purpose of computing a deduction for depletion under section 114."

* * * * * * *

(c) EFFECTIVE DATE.—The amendments made by this section shall be applicable to taxable years ending after December 31, 1950.

SEC. 29.23(ff)-1. DISCOVERY OR EXPLORATION EXPENDITURES.—(*a*) *Allowance of deduction.*—Subject to the limitation prescribed in (*c*) hereinafter, section 23(ff)-1 provides with respect to taxable years ending after December 31, 1950, for a deduction from gross income of expenditures for ascertaining the existence, location, extent, or quality of any deposit of ore or other mineral (other than oil or gas) paid or incurred by the taxpayer prior to the beginning of the development stage. The expenditures thus described include only those which, except for this section, would not qualify as a deduction for the taxable year and do not include expenditures for the acquisition or improvement of property of a character which is subject to the allowance for depreciation provided for in section 23(l). However, allowances for depreciation shall be considered for the purposes of this section as expenditures paid or incurred. For the purposes of this section, such expenditures do not include expenditures paid or incurred after the existence of ores or minerals in commercially marketable quantities has been disclosed. For treatment of development expenditures see section 23(cc) and section 29.23(cc)-1. In general, the provisions of this section are applicable only to costs paid or incurred by the taxpayer in respect of exploration or discovery undertaken (directly or through contract) by the taxpayer and do not apply, for example, to such costs of exploration or discovery undertaken by other persons as may be reflected in the acquisition cost paid or incurred by the taxpayer for the property.

As to the deductibility of expenditures attributable to a grant or loan made to a taxpayer by the United States for the encouragement of the exploration, development, or mining of critical and strategic minerals, see section 22(b)(15).

(*b*) *Election to defer.*—A taxpayer entitled to the deduction under section 23(ff)(1) may, in lieu of taking such deduction to which he is entitled in the year when the expenditures for discovery or exploration were paid or incurred, elect under section 23(ff)(2) to treat any portion of such deductible expenditures as deferred expenses to be deducted ratably as the units of produced ores or minerals discovered or explored by reason of such expenditures are sold.

The amount of the deduction allowable during the taxable year is an amount A, which bears the same ratio to B (the total deferred discovery or exploration expenditures reduced by the amount of such expenditures deducted in prior taxable years) as C (the number of units of the produced ore or mineral sold during the taxable year) bears to D (the number of units of ore or mineral remaining as of the taxable year). For the purposes of this proportion, the "number of units of ore or mineral remaining as of the taxable year" is the number of units of ore or mineral remaining at the end of the year to be recovered from the mines or deposits benefited by such expenditures (including units recovered but not sold) plus the number of units sold within the taxable year. The principles outlined in section 29.23(m)-9 of these regulations are applicable in estimating the number of units remaining as of the taxable year and the number of units sold during the year. The estimate is subject to revision in accordance with that section in the event it is ascertained as the result of further discovery, development or operations that the remaining units are materially greater or less than the units remaining from a prior estimate. Sections 29.23(e)-3 and 29.23(f)-1 of these regulations contain rules relating to the treatment of losses resulting from abandonment.

If the taxpayer has paid or incurred expenditures of the character described herein, has made the election to defer such expenditures and thereafter leases the mine or deposit benefited by such expenditures retaining a royalty interest therein, he shall be allowed the ratable deduction in the foregoing paragraph.

The election referred to in this paragraph shall be made by a clear indication on the return or by a statement filed with the director of internal revenue with whom the return was filed not later than 6 months after the filing of the return for the taxable year to which such election is applicable, or, in case the return for the taxable year to which such election is applicable is filed on or before March 15, 1953, by a statement in writing to that effect filed with the director of internal revenue with whom the return was filed on or before September 15,

1953. In such statement, the taxpayer shall disclose the amount to be deferred, and the name, location, extent, and nature of the mineral deposit to which the election relates. The election shall be binding for the taxable year in respect to which the election was made.

(c) *Limitation.*—The deduction described in (a) above is allowable only for the amount of all such expenditures paid or incurred by the taxpayer in the taxable year as does not exceed $75,000. Amounts otherwise allowable as deductions without reference to this section (except allowances for depreciation) are not to be taken into account in determining this limitation. The limitation applies to all such described expenditures of the taxpayer and is not a total amount allowable with respect to each mine or deposit. No deduction under section 23(ff)(1) or election under section 25(ff)(2) may be taken or exercised if in any 4 preceding years (not necessarily consecutive years) the taxpayer, or any individual or corporation who has transferred to the taxpayer any mineral or ore property under circumstances which make the provisions of paragraph (7), (8), (11), (13), (15), (17), (20), or (22) of section 113(a) applicable to such transfer, has been allowed a deduction or elected to treat such expenditures as deferred expenses under section 23(ff)(1) or section 23(ff)(2), respectively. Thus, under such circumstances, no deduction under section 23(ff)(1) or election under section 23(ff)(2) may be taken or exercised after the combined deductions and elections so taken or exercised by one or more transferors and the taxpayer equal four. For the purposes of the preceding sentence, a deduction and an election availed of in any taxable year by a particular taxpayer or transferor shall be considered as having been taken or exercised only once.

Example (1). Assume that a taxpayer who has never claimed the benefits of section 22(ff) received in 1956 a mineral deposit from X Corporation upon a distribution in complete liquidation of the latter under conditions which would make the provisions of section 113(a)(15) applicable in determining the basis of the property in the hands of the taxpayer, and that during the year 1955 X Corporation expended $60,000 for exploration expenditures which X Corporation elected to treat as deferred expenses. On the basis of these facts the taxpayer may deduct or defer for any three (not necessarily consecutive) subsequent taxable years similar expenditures made in those years not to exceed $75,000 in any year. Where the amount expended in any taxable year is less than $75,000 the difference, if any, may not be carried over or back to other taxable years.

Example (2). Assume the same facts stated in example (1) except that, prior to acquisition by the taxpayer of the deposit from Corporation X in 1956, Corporation X had acquired the deposit in 1954 in a similar distribution from Y Corporation which, in the years 1952 and 1953, deducted exploration costs paid in respect of an entirely different deposit in the amounts of $30,000 and $50,000 respectively. Under these circumstances, the taxpayer may deduct or defer exploration expenditures paid or incurred for only 1 taxable year in an amount not in excess of $75,000.

PAR. 7. There is inserted immediately preceding section 29.24–1 [26 CFR 29.24–1] the following:

SEC. 309. EXPENDITURES IN THE DEVELOPMENT OF MINES [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

* * * * * * *

(c) TECHNICAL AMENDMENT.—Section 24(a)(2) (relating to items not deductible) is hereby amended by adding after the word "estate" the following: ", except expenditures for the development of mines or deposits deductible under section 23(cc)".

(d) EFFECTIVE DATE.—The amendments made by this section shall be applicable to taxable years ending after December 31, 1950.

PAR. 8. Section 29.24–2, as amended by Treasury Decision 5513 [C. B. 1946–1, 61], approved May 16, 1946 [26 CFR 29.24–2], is further amended as follows:

(A) By inserting immediately after the heading the following: —(a) *Expenditures except nondepreciable mine development expenditures.*—

(B) By adding at the end thereof the following:

(*b*) *Nondepreciable expenditures for mine development.*—Section 23(cc) provides that certain expenditures (not subject to depreciation allowance under section 23(l)) paid or incurred by the taxpayer for mine development after December 31, 1950, may be deducted or treated as deferred expenses. For the rules governing treatment of such expenditures see section 23(cc) and section 29.23(cc)-1.

PAR. 9. There are inserted immediately preceding section 29.113(b)(1)-1 [26 CFR 29.113(b)(1)-1] the following:

SEC. 309. EXPENDITURES IN THE DEVELOPMENT OF MINES [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

* * * * * * *

(b) ADJUSTED BASIS FOR DETERMINING GAIN OR LOSS UPON SALE OR EXCHANGE.—Section 113(b)(1) (relating to adjusted basis of property) is hereby amended by adding at the end thereof the following subparagraph:

"(J) for amounts allowed as deductions as deferred expenses under section 23(cc)(2) (relating to certain expenditures in the development of mines) and resulting in a reduction of the taxpayer's taxes under this chapter, but not less than the amounts allowable under such section for the taxable year and prior years."

* * * * * * *

(d) EFFECTIVE DATE.—The amendments made by this section shall be applicable to taxable years ending after December 31, 1950.

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SEC. 342. DEDUCTION OF EXPENDITURES FOR MINE EXPLORATION [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

* * * * * * *

(b) ADJUSTED BASIS FOR DETERMINING GAIN OR LOSS UPON SALE OR EXCHANGE.—Section 113(b)(1) (relating to adjusted basis of property) is hereby amended by adding at the end thereof the following:

"(M) for amounts allowed as deductions as deferred expenses under section 23(ff)(2) (relating to certain exploration expenditures) and resulting in a reduction of the taxpayer's taxes under this chapter, but not less than the amounts allowable under such section for the taxable year and prior years."

(c) EFFECTIVE DATE.—The amendments made by this section shall be applicable to taxable years ending after December 31, 1950.

PAR. 10. Section 29.113(b)(1)-1, as amended by Treasury Decision 6006 [C. B. 1953-1, 30], approved April 10, 1953 [26 CFR 29.113(b)(1)-1], is further amended by adding at the end thereof the following:

With respect to taxable years ending after December 31, 1950, the basis shall also be adjusted to take into account the amount of expenditures for development and exploration of mines or mineral deposits treated as deferred expenses under sections 23(cc)(2) and 23(ff)(2). The basis so adjusted shall be reduced by the amount of such expenditures allowed as deductions under such sections which results in a reduction of the taxpayer's liability for income tax but not less than the amounts allowable under such sections for the taxable year and prior years. For example, if a taxpayer purchases unexplored and undeveloped mining property for $1,000,000 and at the close of the development stage has incurred exploration and development costs of $9,000,000 treated as deferred expenses, the basis of such property at such time for computing gain or loss will be $10,000,000. Assuming that the taxpayer in this example has operated the mine for several years and has deducted allowable percentage depletion in the amount of $2,000,000 and has deducted allowable deferred

exploration and development expenditures of $2,000,000, the basis of the property in the taxpayer's hands for purposes of determining gain or loss if sold will be $6,000,000.

(This Treasury Decision is issued under the authority contained in sec. 62 of the Internal Revenue Code (53 Stat. 32; 26 U. S. C. 62), and secs. 23(cc) and 23(ff) of the Internal Revenue Code (65 Stat. 486, 515; 26 U. S. C. 23(cc) and 23(ff)).)

T. COLEMAN ANDREWS,
Commissioner of Internal Revenue.

Approved June 23, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register June 25, 1953, 8:51 a. m.)

SECTION 24.—ITEMS NOT DEDUCTIBLE

REGULATIONS 111, SECTION 29.24-2: Capital expenditures.

INTERNAL REVENUE CODE

Regulations 111 amended. (See T. D. 6023, p. 132.)

REGULATIONS 111, SECTION 29.24-6: Losses from sales or exchanges between certain classes or persons.

INTERNAL REVENUE CODE

Deduction by wife, where community property is invested by husband in a partnership, of one-half of husband's share of partnership loss where husband is precluded from deducting his share of such loss. (See Rev. Rul. 121, p. 209.)

PART IV.—ACCOUNTING PERIODS AND METHODS OF ACCOUNTING

SECTION 42.—PERIOD IN WHICH ITEMS OF GROSS INCOME INCLUDED

REGULATIONS 111, SECTION 29.42-1: When included in gross income. Rev. Rul. 169

INTERNAL REVENUE CODE

Income resulting from a retroactive increase in temporary airmail rates, accrues, for Federal income tax purposes, in the year in which the Civil Aeronautics Board issues an order providing for such increase. Pending final determination of airmail rates by the Board, compensation will be accrued at the airmail rates in effect at the end of the taxable year for which such income is being reported for Federal income tax purposes.

I. T. 3961, C. B. 1949-2, 35, revoked.

Advice is requested as to the year of accrual of income resulting from a retroactive increase in temporary airmail rates, granted by an order of the Civil Aeronautics Board fixing permanent airmail

rates with respect to transportation of airmail during prior taxable years.

In I. T. 3851, C. B. 1947–1, 32, it was held that income from retroactive increases in permanent airmail rates accrues in the year in which the Board issues its final order providing for such increases. This ruling cited and followed Law Opinion 1086, C. B. I–1, 87, (1922), in which additional compensation granted railway mail carriers by order of the Interstate Commerce Commission for services performed in 1916 and 1917 was held to accrue in the year 1919, the year in which the Commission's order was issued. I. T. 3961, C. B. 1949–2, 35, holds that income from retroactive increases in temporary airmail rates accrues for the years during which the services are rendered. The principal factual difference between the two rulings is that I. T. 3961 involved a retroactive increase in temporary airmail rates, whereas I. T. 3851 involved a retroactive increase in permanent airmail rates.

It is believed that the rules governing accrual of retroactive increases in permanent airmail rates are equally applicable to the treatment of retroactive increases in temporary airmail rates. Accordingly, it is held that I. T. 3851, *supra*, is applicable to retroactive increases in both temporary and permanent airmail rates. I. T. 3961, *supra*, is hereby revoked.

Pending final determination of airmail rates by the Board, compensation will be accrued at the airmail rates in effect at the close of the taxable year for which such income is being reported for Federal income tax purposes. Adjustments for changes in airmail rates will be made upon the return for the year in which an order is issued by the Board changing such airmail rates.

Pursuant to the authority contained in section 3791(b) of the Internal Revenue Code, this ruling will not be applied with respect to retroactive increases in temporary airmail rates granted by an order of the Board promulgated prior to August 31, 1953.

REGULATIONS 111, SECTION 29.42–1: When included in gross income. Rev. Rul. 214

INTERNAL REVENUE CODE

Application of Revenue Ruling 62, C. B. 1953–1, 71, relating to amounts credited to insured banks under section 7(d) of the Federal Deposit Insurance Act, to taxable years ended prior to January 1, 1953.

Revenue Ruling 62, C. B. 1953–1, 71, holds that amounts credited to insured banks under section 7(d) of the Federal Deposit Insurance Act by the Federal Deposit Insurance Corporation are includible in the gross income of the bank, on the cash receipts and disbursements basis, for its taxable year or years in which and to the extent each such credit is applicable toward payment of a deposit-insurance assessment or assessments or is refundable or assignable. Each such credit, being ultimately realized by the bank in full, is includible in its gross income, on the accrual basis, in entirety for its taxable year in which it is definitely advised by the Corporation of the amount thereof.

Since the Federal Deposit Insurance Corporation did not determine

until 1952 that insured banks were entitled as a matter of right to the full amount of the credit and also since Revenue Ruling 62 was not published until April 27, 1953, the Internal Revenue Service, pursuant to authority contained in section 3791(b) of the Internal Revenue Code, will not require the application of the ruling for taxable years ended prior to January 1, 1953, if for such prior years a bank had a different method for reflecting the credit. However, this will not preclude such a bank from adopting or using the method provided in Revenue Ruling 62 beginning with a taxable year ended prior to January 1, 1953.

SECTION 43.—PERIOD FOR WHICH DEDUCTIONS AND CREDITS TAKEN

REGULATIONS 111, SECTION 29.43-2: When charges deductible. Rev. Rul. 170

INTERNAL REVENUE CODE

Intangible drilling and development costs prepaid by a taxpayer, who keeps his accounts and files his returns on the cash basis and elects to treat such costs as expenses, constitute an allowable deduction only for the taxable year in which the drilling and developing services are actually rendered.

Advice is requested whether intangible drilling and development costs prepaid by a taxpayer, who keeps his accounts and files his returns on the cash basis and elects to treat such costs as expense, constitute an allowable deduction for the year in which payment was made or for the year in which the drilling and development services were actually rendered.

In the instant case, the taxpayer acquired a lease on certain land for the purpose of drilling an oil well. In November of 1951, the taxpayer orally accepted a bid of the M Company to do the drilling. On December 31, 1951, the taxpayer executed a formal agreement for the drilling of the well. The agreement provided for the payment of a specified amount per foot of well drilled, plus a specified amount per foot of hole cored. Pursuant to a provision in the agreement, the taxpayer paid the M Company, on December 31, 1951, the sum of $95x$ dollars as "payment for the work to be performed and materials to be furnished" under the agreement. The agreement also provided that upon completion of the contract the taxpayer would pay any additional amount due in excess of the $95x$ dollars already paid, and if the final contract price was less than $95x$ dollars the M Company would refund the excess to the taxpayer. Drilling of the well began during January 1952, and by March 1952 oil production had started. The evidence submitted does not indicate that in other years the taxpayer followed a consistent practice of prepaying drilling or development expenses and claiming a deduction therefor in the year of payment.

Section 29.23(m)-16 of Regulations 111 provides in part that a taxpayer may, at his option, elect to treat intangible drilling and development costs of the type here involved as an expense, deductible from gross income, or as a charge to his capital account. That section does not specify when such intangible costs may be deducted.

Accordingly, it is necessary to refer to section 23(a)(1)(A) of the Internal Revenue Code to determine when they may be deducted. Section 23(a)(1)(A) of the Code provides in part that in computing net income there shall be allowed as deductions:

> All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered * * *.

Under the provisions of section 23(a)(1)(A), *supra*, the taxpayer is not entitled to a deduction in his return filed for the taxable year 1951 for the payment made in that year, unless the intangible drilling and development costs were an "ordinary and necessary" expense in 1951, and were not compensation for personal services. If the costs constitute compensation for personal services, they are deductible only in the year in which the personal services were actually rendered, namely, in 1952.

The contract between the taxpayer and the M Company required the company to perform services. The M Company provided such equipment as was necessary for the drilling of the well. The money paid by the taxpayer to the M Company in the taxable year 1951 constituted compensation for services and rental for the equipment that the contractor employed in performing the services. The contract was an executory one calling for future performance by the M Company. When it was made the only immediate effect was the incidence of the obligations of the parties to keep their contract. The measure of such an obligation is not the contract price, but the response in damages for its breach. (See *Hallack & Howard Lumber Co.* v. *Commissioner*, 18 B. T. A. 954, in which case it was held that an expense for services was deductible by an accrual basis taxpayer in the year in which the services were performed and not in the previous year when the contract for such services was made.) It would follow, therefore, that the payment made by the taxpayer in the taxable year 1951, simultaneously with the making of the contract, was merely an advance payment for work to be performed in the future.

In *Galatoire Bros.* v. *Lines*, 23 Fed. (2d) 676, T. D. 4138, C. B. VII-1, 229, the court held that a lessee may not deduct advance rental payments in the year in which the rental payments are made. The statute applicable in that case allowed a deduction for "the necessary expenses actually paid in carrying on any business or trade." In *Commissioner* v. *Boylston Market Association*, 131 Fed. (2d) 966, Ct. L. 1573, C. B. 1943, 1024, the court held that prepaid insurance premiums were not "an ordinary and necessary business expense" in the year in which prepaid in the case of a taxpayer on the cash basis. (See also G. C. M. 23587, C. B. 1943, 213.) In *D. K. McColl* v. *Commissioner* (B. T. A. Memo. Op., Docket 95834, Jan. 11, 1941) the taxpayer was denied a deduction in the year of payment where the services were rendered in a subsequent year.

Accordingly, it is held that the intangible drilling and development costs here involved constitute an allowable deduction for the taxable year 1952, the year in which the drilling and development services were rendered, and not for 1951, the year in which payment therefor was made.

REGULATIONS 111, SECTION 29.43-2: When charges deductible. Rev. Rul. 183

INTERNAL REVENUE CODE

Determination of year in which embezzlement losses are deductible for Federal income and excess-profits tax purposes in the light of the opinion of the Supreme Court of the United States in the cases of *Martha L. Alison* v. *The United States of America* and *The United States of America* v. *Stevenson-Chislett, Inc.*, 344 U. S. 167, Ct. D. 1754, C. B. 1953-1, 39.

Advice is requested whether embezzlement losses occurring over a period of several years are properly deductible in the years in which the embezzlement occurred or in the year the losses were discovered and their amounts ascertained.

On December 8, 1952, the Supreme Court of the United States, in its decision in the cases of *Martha L. Alison* v. *The United States of America* and *The United States of America* v. *Stevenson-Chislett, Inc.*, 344 U. S. 167, Ct. D. 1754, C. B. 1953-1, 39, stated, "Whether and when a deductible loss results from an embezzlement is a factual question, a practical one to be decided according to the surrounding circumstances * * *. An inflexible rule is not needed; the statute does not compel it."

Section 29.43-2 of Regulations 111 provides that a loss from theft or embezzlement occurring in 1 year and discovered in another is ordinarily deductible for the year in which sustained. On the basis of that provision, it has been the policy to allow a deduction for a loss from an embezzlement occurring in 1 year or over a period of several years and discovered in a later year only in the year or years in which the embezzlement actually occurred, limiting the deduction each year to the amount of the loss occurring in that year. Generally, that policy will continue to be followed. However, in view of the above-mentioned decision, an exception to that policy will be applicable in those cases in which it is impossible from the facts and circumstances involved to identify the year or years in which the embezzlements actually occurred and to ascertain the amount thereof in such year or years. Likewise, in other special factual cases where the embezzlement is not discovered for many years because of the secret maneuvers of the embezzler and the facts reveal that undue hardship or injustice would result if the loss were allowed only in the years the embezzlements occurred, it is believed that the loss may properly be allowed in the year in which it is discovered and the amount thereof ascertained.

It should be understood, however, that this exception does not provide taxpayers with an option to select the taxable year in which the deduction of the loss is to be allowed for tax purposes. The selection of the year in which to claim such a deduction should be made in accordance with actual facts and circumstances, as explained above.

REGULATIONS 111, SECTION 29.43-2: When charges deductible. Rev. Rul. 258

(Also Section 113(b), Section 29.113(b)(1)-1; Section 125, Section 29.125-1; Section 201, Section 29.201-9.)

Mortgage loans insured by the Federal Housing Administration do not constitute "bonds" within the meaning of section 125 of the Internal Revenue Code, and, therefore, the amortization of bond premiums provided therein is not applicable to premiums paid for such loans.

Premiums paid for such loans by life insurance companies may be amortized by them, under section 201(e) of the Code, over the period from the date of acquisition to maturity or the earliest interest payment date at which payable, or such other payment date, prior to maturity, specified in the security as may be selected by them.

Premiums paid by banks for such loans constitute a part of purchase price, but, in view of their nature, are deductible in proportionate amounts in each taxable year as payments of loan principal are received. In the event of sale or exchange of such a loan, adjustment must be made of its gain or loss basis for the portion or portions of the premium thereon previously deductible (and for any portions deducted in excess of amounts deductible in taxable years barred from adjustment of tax liability.)

Advice has been requested regarding the treatment, for Federal income tax purposes, of premiums paid by banks and insurance companies upon purchasing Federal Housing Administration insured mortgage loans from original lenders.

Such mortgages are made initially to a "mortgagee approved by the Administrator as responsible and able to service the mortgage properly" (secs. 203(b)(1) and 603(b)(1) of the National Housing Act, as amended), and loans secured by such mortgages, thereupon insured, were purchased from the original lenders at a "premium" (i. e., at a price in excess of the principal amount of the mortgage notes). It appears that such premiums were paid primarily in view of these mortgage loans being insured and serviced.

For Federal income tax purposes, under the Internal Revenue Code and regulations, except where special provision is made, premiums paid upon the purchase of securities constitute to the purchaser a part of the purchase price or cost of the security. (See *New York Life Insurance Company* v. *Edwards*, 271 U. S. 109, T. D. 3872, C. B. V-1, 305 (1926).) Such special provisions are contained in section 125 of the Internal Revenue Code, relating to amortizable bond premiums, and section 201 of the Code, relating to the tax on life insurance companies.

Section 125 of the Code generally provides for the amortization of bond premiums, but only in the case of any "bond" as defined in subsection (d) thereof, namely, any bond, debenture, note or certificate, or other evidence of indebtedness issued by any corporation and bearing interest (including any like obligation issued by a government or political subdivision thereof) with interest coupons or in registered form. Since Federal Housing Administration insured mortgage loans are not issued by either a corporation, a government, or a political subdivision thereof, such loans are not "bonds" for the purposes of that section and, therefore, its provisions do not apply to premiums on such loans.

Section 201(e) of the Code provides for certain adjustments on account of amortization of premiums and accrual of discount on bonds, notes, debentures, or other evidences of indebtedness held by a life insurance company. Section 29.201-9 of Regulations 111 provides

for amortization of the premium on such bonds and notes over the period from the date of their acquisition to their maturity or earliest interest payment date, if payable at such date, or such other payment date, prior to maturity, specified in the security as may be selected by the life insurance companies. The service has held that such provision in the regulations for premium amortization is applicable to Federal Housing Administration insured mortgage loans.

Under the present statute, premiums paid by banks on Federal Housing Administration insured mortgage loans constitute to them a part of the purchase price paid therefor and, as such, are not deductible from gross income when paid. However, since such premiums appear to have been paid primarily in view of these mortgage loans being insured and serviced, and the loans are payable in installments, the Service has held that the banks may deduct for each taxable year the same proportion of the total premium as the payment on principal of a loan during the year bears to its principal (face) amount when purchased. Should such a loan be paid prior to maturity, the portion of the total premium which, under the above-stated rule, was not previously deductible (and was not deducted in any taxable year barred from adjustment of tax liability) is deductible for the taxable year in which the loan is paid. In the event of sale or exchange of such a loan, adjustment must be made of its gain or loss basis for the portion or portions of the premium previously deductible (and for any portions deducted in excess of amounts deductible in taxable years barred from adjustment of tax liability). See section 113(b) of the Code; also G. C. M. 19367, C. B. 1937–2, 115, and G. C. M. 23587, C. B. 1943, 213. As provided in section 29.113(b)(1)–1 of Regulations 111, "Adjustments must always be made to eliminate double deduction or their equivalent."

SECTION 44.—INSTALLMENT BASIS

REGULATIONS 111, SECTION 29.44–5: Gain or loss upon disposition of installment obligations. (Also Section 112(b), Section 29.112(b)(6)–3; Section 112(f), Section 29.112(f)–3; Section 131, Section 29.131–3.) T. D. 6041

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 29.—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1941

Miscellaneous changes in procedure in connection with the transfer of certain functions to district directors of internal revenue.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

Regulations 111 [26 CFR, pt. 29] are amended as follows:

PARAGRAPH 1. Section 29.44–5 (relating to gain or loss upon disposition of installment obligations), as amended by Treasury Decision 5334 [C. B. 1944, 160], approved February 28, 1944, is further amended by inserting immediately after the second sentence of the second paragraph from the end thereof the following new sentence:

On and after September 1, 1953, the functions of the Commissioner with respect to such bonds shall be performed by the district director of internal revenue for the internal revenue district in which the last return of the decedent is filed, and any bond filed on or after such date shall be filed with such district director.

PAR. 2. Section 29.112(b)(6)-3 (relating to liquidations covering more than 1 taxable year) is amended as follows:

(A) By striking from the first sentence of paragraph (*b*) thereof the words "for transmittal to the Commissioner".

(B) By striking the first sentence of paragraph (*c*) thereof and inserting in lieu thereof the following:

For each of the taxable years which falls wholly or partly within the period of liquidation, the recipient corporation may be required to file a bond, the amount of which shall be fixed by the district director of internal revenue.

(C) By inserting at the end of paragraph (*c*) thereof the following sentence:

On and after September 1, 1953, the functions of the Commissioner with respect to such bonds shall be performed by the district director of internal revenue for the internal revenue district in which the return was filed, and any bond filed on or after such date shall be filed with such district director.

PAR. 3. Section 29.112(f)–3(*c*) (relating to involuntary conversion where disposition of the converted property occurred after December 31, 1950), as added by Treasury Decision 5991 [C. B. 1953–1, 146], approved February 17, 1953, is hereby amended by striking that part of the third paragraph which follows the first sentence and inserting in lieu thereof the following:

Such application shall be made prior to the expiration of the 1 year after the close of the first taxable year in which any part of the gain from the conversion is realized, and shall contain all of the details in connection with the involuntary conversion. Such application, if made prior to September 1, 1953, shall be made to the Commissioner, or, if made on or after September 1, 1953, shall be made to the district director of internal revenue for the internal revenue district in which the return is filed for the first taxable year in which any of the gain from the involuntary conversion is realized. No extension of time shall be granted pursuant to such application unless the taxpayer can show reasonable cause for not being able to replace the converted property within the required period of time.

PAR. 4. Section 29.131–3 (relating to conditions of allowance of credit for taxes paid other than to the United States), as amended by Treasury Decision 5947 [C. B. 1952–2, 145], approved November 19, 1952, is further amended by inserting after the last sentence of the third paragraph thereof the following new sentence:

On and after September 1, 1953, the functions of the Commissioner with respect to such bonds shall be performed by the district director of internal revenue, and any bond filed on or after such date shall be filed with the district director.

Because this Treasury Decision merely changes the designation of the official with whom certain bonds and applications for extension must be filed, and relieves certain taxpayers from the requirement of filing bonds, it is found that it is unnecessary to issue such Treasury Decision with notice and public procedure thereon under section 4(a) of the Administrative Procedure Act, approved June 11, 1946, or subject to the effective date limitation of section 4(c) of said act.

(This Treasury Decision is issued under the authority contained in sec. 3791 of the Internal Revenue Code (53 Stat. 467; 26 U. S. C. 3791).)

T. COLEMAN ANDREWS,
Commissioner of Internal Revenue.

Approved September 9, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register September 14, 1953, 8:49 a. m.)

SECTION 46.—CHANGE OF ACCOUNTING PERIOD

REGULATIONS 111, SECTION 29.46-1: Change of accounting period. T. D. 6035

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 29.—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1941

Section 29.46-1 of Regulations 111 amended to provide that taxpayers may make a change of accounting period under certain circumstances without obtaining the prior approval of the Commissioner.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

Section 29.46-1 of Regulations 111 [26 CFR, pt. 29], as amended by Treasury Decision 5614 [C. B. 1948-1, 50], approved May 11, 1948, is further amended as follows:

(A) By changing the heading thereof to read as follows: "CHANGE OF ACCOUNTING PERIOD.—(*a*) *Short taxable years ending prior to July 1, 1953.*"

(B) By revising the second and third sentences thereof to read as follows:

However, if the short taxable year for which a return would be required to effect the change ends after July 31, 1943, but not later than June 30, 1953, such taxpayer shall, before using the new period for income tax purposes, secure the consent of the Commissioner, and application for permission to change the accounting period shall be made direct to the Commissioner on Form 1128 at least 60 days prior to the close of the short taxable year for which a return would be required to effect the change. If a change of accounting period of a subsidiary is required for income tax purposes under section 24.14 of Regulations 129 [26 CFR, pt. 24], the information required on Form 1128 shall be furnished by the subsidiary at or before the time of filing the consolidated income tax return.

(C) By adding at the end thereof the following:

(*b*) *Short taxable years ending after June 30, 1953.*—(1) *General.*—A change of accounting period for income tax purposes requiring a return for a short taxable year ending after June 30, 1953, is authorized, except where inconsistent with section 41, requiring the use of the calendar year basis in certain specific cases, and except as provided in subparagraph 2 of this paragraph, and no application for such change need be filed. To make such a change the taxpayer shall file a tax return on or before the 15th day of the 3d full calendar month following the close of the short taxable year accompanied by a statement that it is

made under the authorization conferred by this section. Once a change of accounting period has been made, the taxpayer shall thereafter make his returns and compute his net income on the basis of the new accounting period.

(2) *Cases in which approval of change of accounting period is required.*—The prior approval of the Commissioner will be required before a taxpayer may change his accounting period if any of the following conditions exist:

(i) At any time within the 5 calendar years ending with the calendar year which includes the beginning of the short taxable year required to effect the change of accounting period the taxpayer has changed his accounting period for income tax purposes. For the purpose of this subparagraph a change of accounting period for income tax purposes by a partnership shall be considered as a change by each member thereof and a change by any member shall be deemed to be a change by the partnership. Likewise, a change of accounting period for income tax purposes by a trust shall be considered as a change by each beneficiary thereof and a change by a beneficiary shall be deemed to be a change by the trust.

(ii) The short taxable year required to effect the change of accounting period ends more than 3 months and less than 9 months after the close of the accounting period used by the taxpayer for purposes of filing his income tax return for the previous full taxable year.

(iii) The taxpayer's net income for the short taxable year required to effect the change of accounting period, as annualized in the manner provided in section 29.47-2, is less than 80 percent of the net income of the taxpayer for the full taxable year immediately preceding such short taxable year.

The application of certain of the foregoing provisions is illustrated by the following example:

Example. X files his income tax returns on a calendar year basis. He desires to change his accounting period during the year 1954 in order to file his returns on a fiscal year basis ending March 31. X has not previously changed his accounting period. His income for the period January 1 through March 31, 1954, when annualized in accordance with section 29.47-2, equals at least 80 percent of his net income for the calendar year 1953. X is authorized to change his accounting period by filing, on or before June 15, 1954, a tax return for the short taxable year beginning January 1 and ending March 31, 1954. Thereafter X shall make his annual returns and compute his net income on the basis of a fiscal year ending March 31.

Had X preferred, he could have changed to a fiscal year basis ending the last day of January, February, September, October, or November. However, if X had elected to change to a fiscal year accounting period ending on the last day of April, May, June, July, or August, the prior approval of the Commissioner would be required since such a change would result in a return for a short taxable year ending more than 3 months and less than 9 months after the close of the accounting period regularly used by X.

Where prior approval of a change of accounting period is required, application shall be filed on Form 1128 with the Commissioner of Internal Revenue, Washington, D. C., on or before the 15th day following the close of the short taxable year for which a return would be required to effect the change of accounting period. In general, an application for a change of accounting period will be approved where the taxpayer establishes valid business reasons for making such change. A change of accounting period intended to be made primarily for the purpose of effecting a tax saving shall not be allowed except where such tax saving results from the application of section 12(d), the so-called "income splitting" provision, in the case where a husband and wife adopt the same accounting period in order to file a joint return and no other reason appears which is considered sufficient by the Commissioner for denying such permission.

(3) *Change of accounting period by a subsidiary corporation filing a consolidated return.*—The foregoing provisions of this paragraph have no application in the case of a subsidiary corporation required to change its accounting period because it has elected to file consolidated returns. (See sec. 24.14, Regulations 129.) In such a case, if a change of accounting period is made on or after July 1, 1953, the corporation shall complete Form 1128 and forward it to the director of internal revenue with whom the consolidated return is to be filed at or before the time of filing of such consolidated return.

Because this Treasury Decision makes only procedural changes in net effect relieving restrictions, it is found unnecessary to issue such

Treasury Decision with notice and public procedure thereon under section 4(a) of the Administrative Procedure Act, approved June 11, 1946, or subject to the effective date limitation of section 4(c) of said act.

(This Treasury Decision is issued under the authority contained in secs. 62 and 3791 of the Internal Revenue Code (53 Stat. 32, 467: 26 U. S. C. 62, 3791).)

T. COLEMAN ANDREWS,
Commissioner of Internal Revenue.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register August 3, 1953, 8:52 a. m.)

PART V.—RETURNS AND PAYMENT OF TAX

SECTION 53.—TIME AND PLACE FOR FILING RETURNS

REGULATIONS 111, SECTION 29.53-1: Time for filing returns. Rev. Rul. 215
(Also Section 56, Section 29.56-1.)

INTERNAL REVENUE CODE

A corporation which has satisfied or made provision for all of its liabilities and distributed all of its assets prior to the end of its annual accounting period has completed liquidation thereby effecting a *de facto* dissolution and must file its Federal income tax return and pay its tax on or before the 15th day of the third full month following such liquidation unless a later date for filing the return is permitted by the Commissioner. The corporation may elect, however, to pay the tax in installments in accordance with section 56(b) of the Code. O. D. 692, C. B. 3, 286 (1920), is inapplicable with respect to taxable years beginning after December 31, 1941.

Advice is requested relative to the time for filing a Federal income tax return and payment of the tax by a corporation which liquidated prior to the end of its normal annual accounting period.

Section 47(g) of the Internal Revenue Code provides as follows:

(g) RETURNS WHERE TAXPAYER NOT IN EXISTENCE FOR TWELVE MONTHS.—In the case of a taxpayer not in existence during the whole of an annual accounting period ending on the last day of a month, or, if the taxpayer has no such annual accounting period or does not keep books, during the whole of a calendar year, the return shall be made for the fractional part of the year during which the taxpayer was in existence.

Section 48 of the Code, defining certain terms used in chapter 1 of the Code, provides in part as follows:

(a) TAXABLE YEAR.—* * * "Taxable year" means, in the case of a return made for a fractional part of a year under the provisions of this chapter or under regulations prescribed by the Commissioner with the approval of the Secretary, the period for which such return is made.

Section 29.52-1 of Regulations 111 provides that a corporation having an existence during any portion of a taxable year is required to make a return. If a corporation was not in existence throughout an

annual accounting period (either calendar year or fiscal year), the corporation is required to make a return for that fractional part of a year during which it was in existence. A corporation is not in existence after it ceases business and dissolves, retaining no assets, whether or not under State law it may thereafter be treated as continuing as a corporation for certain limited purposes connected with winding up its affairs, such as for the purpose of suing and being sued. If the corporation has valuable claims for which it will bring suit during this period, it has retained assets, and it continues in existence.

Section 29.53-1 of Regulations 111 provides that, in general, returns of income must be filed on or before the 15th day of the third full calendar month following the close of the taxable year. However, in the case of a return for a fractional part of a year, the Commissioner may, upon a showing by the taxpayer of unusual circumstances, prescribe a later time for the filing of the return. Such section further provides that a corporation going into liquidation during any taxable year may, upon the completion of such liquidation, prepare a return for that year covering its income for the part of the year during which it was engaged in business and may immediately file such return with the collector (now district director).

In view of the foregoing, it is held that a corporation which has satisfied or made provision for all of its liabilities and distributed all of its assets prior to the end of its annual accounting period has completed liquidation thereby effecting a *de facto* dissolution and must file its Federal income tax return and pay its tax on or before the 15th day of the third full month following such liquidation unless a later date for filing the return is permitted by the Commissioner. See I. T. 3871, C. B. 1947-2, 62. The corporation may elect, however, to pay the tax in installments in accordance with section 56(b) of the Code. O. D. 692, C. B. 3, 286 (1920), is inapplicable with respect to taxable years beginning after December 31, 1941.

SECTION 55.—PUBLICITY OF RETURNS

Rev. Rul. 132

INTERNAL REVENUE CODE

The Bureau is without authority to permit the blanket inspection of Federal estate and gift tax returns by State officials or by branches of the Government other than the Treasury Department.

Advice is requested whether properly designated State officials or representatives of branches of the Government other than the Treasury Department may be permitted to make blanket inspections of Federal estate and gift tax returns.

The inspection of Federal estate and gift tax returns and related papers by States and by branches of the Government, other than the Treasury Department, is governed by the provisions of T. D. 4929, C. B. 1939-2, 91, as amended by T. D. 4991, C. B. 1940-2, 92.

Subpart C of T. D. 4929, relating specifically to estate and gift tax returns, provides in part as follows:

SEC. 463C.20. *General.*—Estate tax returns and notices and gift tax returns, filed under the Internal Revenue Code, shall be treated as privileged communications and shall not be inspected nor their contents disclosed except as hereinafter provided.

* * * * * * *

SEC. 463C.23. *Inspection by State officials.*—A return or notice may be exhibited, or information contained therein may be disclosed, to an officer of any State, for official use in connection with an estate, inheritance, legacy, succession, gift, or other tax of the State, provided a like cooperation is given by the State to the Commissioner or his representatives for use in the administration of the Federal tax laws. Such officer may also be permitted to inspect schedules, lists, and other statements designed to be supplemental to or to become a part of, the original return, and other records and reports which contain information included or required by statute to be included in the return.

Subpart D, relating to general provisions, provides in part as follows:

SEC. 463C.30. *Scope.*—The following provisions, unless otherwise stated, are applicable to all returns referred to in subparts B and C of these regulations.

SEC. 463C.31. *Permission to inspect.*—The Commissioner, upon written application setting forth fully the reason for the request, may grant permission for the inspection of returns in accordance with these regulations.

* * * * * * *

SEC. 463C.33. (*a*) *Inspection by branch of Government other than Treasury Department.*—Except as provided in 463C.34, if the head of an executive department (other than the Treasury Department), or of any other establishment of the United States Government, desires to inspect or to have some other officer or employee of his branch of the service inspect a return in connection with some matter officially before him, the inspection may, in the discretion of the Secretary of the Treasury, be permitted upon written application to him by the head of such executive department or other Government establishment. The application shall be signed by such head and shall show in detail why the inspection is desired, the name and address of the taxpayer who made the return, and the name and official designation of the person it is desired shall inspect the return. The information obtained under this section and section 463C.32 may be used as evidence in any proceeding, conducted by or before any department or establishment of the United States, or to which the United States is a party.

Section 463.33(*b*) of T. D. 4929, as amended by T. D. 4991, provides for inspection of income returns by representatives of the District of Columbia and the several Territories in the discretion of the Commissioner of Internal Revenue. Under this section blanket inspections of income returns have been authorized in order to permit properly designated officials of the District of Columbia and the several territories to inspect income returns under a method of procedure similar to that provided for inspection by the States. Under section 29.55(b)–1 of Regulations 111 States are allowed to make blanket inspections of income returns but there are no provisions in the Internal Revenue Code or regulations authorizing blanket inspection of Federal estate and gift tax returns by State officials. Section 463C.23 of T. D. 4929, which deals with the inspection of individual Federal estate and gift tax returns by State officials, has not been interpreted as authorizing blanket inspection of such returns.

In view of the foregoing it is held that although sections 463C.23 and 463C.33(*a*) of T. D. 4929, *supra*, authorize the inspection of Federal estate and gift tax returns by State officials and branches of the Government other than the Treasury Department, such inspection is limited to specific cases and does not extend to blanket inspection of such returns.

INTERNAL REVENUE CODE

Processing by district directors of certain applications to inspect returns and related papers.

1. Effective August 24, 1953, the Audit Division in the National Office discontinued the processing of applications to inspect returns and related documents retained for permanent filing in district directors' offices (or requests for copies of such returns and related documents) which are submitted to the Commissioner pursuant to the provisions of Treasury Decision 4929, C. B. 1939-2, 91, as amended by Treasury Decision 5019, C. B. 1940-2, 95, Treasury Decision 4945, C. B. 1939-2, 97, as amended by Treasury Decision 5808, C. B. 1950-2, 38, and Treasury Decision 5138, C. B. 1942-1, 99, by the applicants listed in paragraph 2 below of this Revenue Ruling. All such applications on hand and not in process in the Audit Division on the effective date, or received after that date, will be forwarded to district directors for disposition. Any such applications submitted to district directors will be handled by them in the same manner as if addressed to the Commissioner and forwarded to the district directors for handling.

2. The processing of applications referred to in paragraph 1 of this Revenue Ruling apply only with respect to applications submitted by the applicants listed below:

a. RETURNS UNDER CHAPTERS 1 AND 2, INTERNAL REVENUE CODE.

(1) *Individual returns.*—(*a*) The maker of a separate return;

(*b*) Either spouse for whom a joint return was made, upon satisfactory showing of such relationship;

(*c*) The administrator, executor, trustee, or guardian of the estate of the maker of a separate return or of a spouse for whom a joint return was made, if such maker or spouse is deceased or has become legally incompetent;

(*d*) An heir at law, next of kin, or beneficiary under the will of a deceased person who shows that he has a material interest which will be affected by information contained in the return of the decedent;

(*e*) A receiver or trustee in bankruptcy, if the property of the person who made the return is in the hands of such receiver or trustee; or

(*f*) The duly constituted attorney in fact of any of the foregoing.

(2) *Partnership returns.*—(*a*) An individual who was a member of the partnership during any part of the time covered by the return upon satisfactory showing of such membership;

(*b*) The administrator, executor, trustee, or guardian of the estate of a member during any part of the time covered by the return who has died or become legally incompetent;

(*c*) An heir at law, next of kin, or beneficiary under the will of the deceased member who shows that he has a material interest which will be affected by information contained in the return;

(*d*) A receiver or trustee, if the property of the partnership is in the hands of such receiver or trustee in bankruptcy; or

(*e*) The duly constituted attorney in fact of any of the foregoing.

(3) *Estate returns.*—(*a*) The administrator, executor, or trustee of such estate;

(*b*) An heir at law, next of kin, or beneficiary under the will of the decedent for whose estate the return is made, upon a showing of a material interest which will be affected by information contained in the return;

(*c*) The administrator, executor, trustee, or guardian of the estate of an heir at law, next of kin, or beneficiary under a will who has died or become legally incompetent, upon a showing of a material interest which will be affected by information contained in the return; or

(*d*) The duly constituted attorney in fact of any of the foregoing.

(4) *Trust returns.*—(*a*) The trustee or trustees, jointly or severally;

(*b*) Any individual who was a beneficiary of the trust during any part of the time covered by the return upon satisfactory showing that he was such beneficiary;

(*c*) The administrator, executor, trustee, or guardian of the estate of a beneficiary during any part of the time covered by the return who has died or has become legally incompetent;

(*d*) An heir at law, next of kin, or beneficiary under the will of the deceased beneficiary upon a showing of a material interest which will be affected by information contained in the return; or

(*e*) The duly constituted attorney in fact of any of the foregoing.

(5) *Corporation returns.*—(*a*) Any person designated by action of its board of directors, or other similar governing body, upon submission of satisfactory evidence of such action;

(*b*) Any officer or employee upon written request to the Commissioner, signed by any principal officer and attested by the secretary, or other officer, under the corporate seal, if any;

(*c*) The duly constituted attorney in fact of the corporation;

(*d*) In the case of a corporation which has since been dissolved, by any person who might have inspected at date of dissolution;

(*e*) A receiver or trustee, if the property of the corporation is in the hands of such receiver or trustee in bankruptcy, or by the duly constituted attorney in fact of such receiver or trustee; or

(*f*) A bona fide shareholder of record owning 1 percent or more of the outstanding stock. No power of attorney in

this respect may be accepted, since the privilege to a shareholder is personal and may not be delegated to another.

b. RETURNS UNDER CHAPTERS 3 AND 4, INTERNAL REVENUE CODE.

(1) *Estate tax returns.*—(*a*) The executor, or his successor in office, or his duly constituted attorney in fact; or

(*b*) Any other person having a material interest in ascertaining any fact disclosed by the return, or in obtaining information as to payment of the tax.

(2) *Gift tax returns.*—(*a*) The donor or his duly authorized attorney in fact; or

(*b*) Any other person having a material interest in ascertaining any fact disclosed by the return, or in obtaining information as to payment of the tax.

c. RETURNS UNDER CHAPTERS 7, 12, 21, 30, SUBCHAPTER C OF CHAPTER 9, AND SUBCHAPTER A OF CHAPTER 29, INTERNAL REVENUE CODE.

(1) Same classes of applicants listed in paragraph 2a, above, covering returns under chapters 1 and 2 of the Code.

3. Applicants entitled to inspect returns may be furnished copies thereof and may also inspect, and receive copies of, information returns, schedules, etc., designated to be supplemental to or become part of returns, as well as records and reports relating to the returns. The policy with respect to what documents may be inspected is generally as follows:

a. If the inspection of returns and the furnishing of copies of returns is authorized, schedules, information returns, protests, briefs, face of claims, waivers, and other statements or documents designed to be supplemental to or become part of the return, may also be inspected and copies furnished.

b. Examiners' reports may be inspected and copies furnished to the extent that such reports have previously been furnished to the taxpayers; therefore, the transmittal letter portion of a revenue agent's report, or a separate confidential report, which contains information for Service use only, may not be inspected or copies furnished.

c. Conference reports may not be inspected or copies furnished with the exception of the pages showing recomputation of tax liability.

d. Work papers of examiners, engineers' reports, cover letters of the reports in which opinions are expressed, reports of special agents, and interoffice communications, may not be inspected or copies furnished, unless specific authorization is given by the Commissioner.

e. Inspection of claims for refund and furnishing of copies will be limited to the face of the claim only, since the back of the claim contains Service records. Typed copies of office copies of certificates of overassessment may be furnished; no *photostat copies* of certificates of overassessment are to be made.

4. Copies of returns, etc., may be certified by district directors and assistant regional commissioners (Appellate) only as provided in T. D. 5808, *supra*. All other requests for certified copies of documents will be handled by the Audit Division in the National Office.

5. In submitting the applications within the purview of this Revenue Ruling, all the evidentiary requirements of the Treasury Decisions cited in paragraph 1 must be complied with. Inspections are permitted only in the presence of designated internal revenue officers.

SECTION 56.—PAYMENT OF TAX

REGULATIONS 111, SECTION 29.56-1: Date on which tax shall be paid.

INTERNAL REVENUE CODE

Time for payment of tax shown to be due on corporation return filed for a fractional part of a year. (See Rev. Rul. 215, p. 149.)

SUBCHAPTER C.—SUPPLEMENTAL PROVISIONS

SUPPLEMENT A.—RATES OF TAX

SECTION 101.—EXEMPTIONS FROM TAX ON CORPORATIONS

Rev. Rul. 133

INTERNAL REVENUE CODE

The revocation of the tax-exempt status, for taxable years beginning after December 31, 1951, of certain banks and building and loan associations by the Revenue Act of 1951, does not affect the exemption from Federal income taxes of national farm loan associations which are still entitled to exemption under section 101(15) of the Internal Revenue Code.

Advice is requested whether the revocation of the tax-exempt status, for taxable years beginning after December 31, 1951, of certain banks and building and loan associations by the Revenue Act of 1951, affects the exemption from Federal income taxes of national farm loan associations under section 101(15) of the Internal Revenue Code.

Section 101(15) of the Internal Revenue Code which provides for the exemption from Federal tax of certain corporations, reads as follows:

(15) Corporations organized under Act of Congress, if such corporations are instrumentalities of the United States and if, under such Act, as amended and supplemented, such corporations are exempt from Federal income taxes;

Section 313 of the Revenue Act of 1951 repealed the exemption, under section 101(15) of the Internal Revenue Code, of Federal savings and loan associations for taxable years beginning after December 31, 1951, by amending section 5(h) of the Home Owners' Loan Act of 1933, as amended, 48 Stat. 128. However, such amendment does not affect national farm loan associations, which are exempt from Federal tax pursuant to section 26 of the Federal Farm Loan Act, 39 Stat. 360, as amended, which provides in part as follows:

Every Federal land bank and every national farm loan association, including the capital and reserve or surplus therein and the income derived therefrom, shall be exempt from Federal, State, municipal, and local taxation, except taxes

upon real estate held, purchased, or taken by said bank or association under the provisions of sections 761 and 781 of this title. * * *

Accordingly, it is held that the revocation of the tax-exempt status, for taxable years beginning after December 31, 1951, of certain banks and building and loan associations by the Revenue Act of 1951, does not affect the exemption from Federal income taxes of national farm loan associations which are still entitled to exemption under section 101(15) of the Internal Revenue Code.

SECTION 102.—SURTAX ON CORPORATIONS IMPROPERLY ACCUMULATING SURPLUS

REGULATIONS 111, SECTION 29.102-4: Computation of undistributed section 102 net income.

INTERNAL REVENUE CODE

Regulations 111 amended. (See T. D. 6021, p. 169.)

SUPPLEMENT B.—COMPUTATION OF NET INCOME

SECTION 112(b).—RECOGNITION OF GAIN OR LOSS: EXCHANGES SOLELY IN KIND

REGULATIONS 111, SECTION 29.112(b)(6)-3: Liquidations covering more than one taxable year.

INTERNAL REVENUE CODE

Regulations 111 amended. (See T. D. 6041, p. 145.)

SECTION 112(f).—RECOGNITION OF GAIN OR LOSS: INVOLUNTARY CONVERSION

REGULATIONS 111, SECTION 29.112(f)-3: Involuntary conversion where disposition of the converted property occurred after December 31, 1950.

INTERNAL REVENUE CODE

Regulations 111 amended. (See T. D. 6041, p. 145.)

SECTION 112(n).—RECOGNITION OF GAIN OR LOSS: GAIN FROM SALE OR EXCHANGE OF RESIDENCE

REGULATIONS 111, SECTION 29.112(n)-1: Gain from sale or exchange of residence.

INTERNAL REVENUE CODE

Deficiency interest on recognized gain from sale of taxpayer's principal residence. (See Rev. Rul. 112, p. 226.)

SECTION 113(a).—ADJUSTED BASIS FOR DETERMINING GAIN OR LOSS: BASIS (UNADJUSTED) OF PROPERTY

REGULATIONS 111, SECTION 29.113(a)(5)-1: Basis of property acquired by bequest, devise, or inheritance.

INTERNAL REVENUE CODE

Regulations 111 amended. (See T. D. 6020, p. 106.)

REGULATIONS 111, SECTION 29.113(a)(5)-1: Basis of property acquired by bequest, devise, or inheritance.

INTERNAL REVENUE CODE

Effect of a change in partnership interests upon the basis of such interests and of partnership assets. (See Rev. Rul. 144, p. 212.)

REGULATIONS 111, SECTION 29.113(a)(5)-1: Basis of property acquired by bequest, devise, or inheritance.

INTERNAL REVENUE CODE

Basis of an annuity to a survivor annuitant. (See Rev. Rul. 158, p. 259.)

REGULATIONS 111, SECTION 29.113(a)(13)-1: Property contributed in kind by a partner to a partnership.

INTERNAL REVENUE CODE

Regulations 111 amended. (See T. D. 6037, p. 213.)

REGULATIONS 111, SECTION 29.113(a)(13)-1: Property contributed in kind by a partner to a partnership.

INTERNAL REVENUE CODE

Effect of a change in partnership interests upon the basis of such interests and partnership assets. (See Rev. Rul. 144, p. 212.)

REGULATIONS 111, SECTION 29.113(a)(14)-1: Property acquired prior to March 1, 1913.

INTERNAL REVENUE CODE

Regulations 111 amended. (See T. D. 6021, p. 169.)

SECTION 113(b).—ADJUSTED BASIS FOR DETERMINING GAIN OR LOSS: ADJUSTED BASIS

REGULATIONS 111, SECTION 29.113(b)(1)–1: Adjusted basis: General rule.

INTERNAL REVENUE CODE

Determination of gain or loss on the sale or exchange of a Federal Housing Administration insured mortgage loan for which a premium has been paid. (See Rev. Rul. 258, p. 143.)

REGULATIONS 111, SECTION 29.113(b)(1)–1: Adjusted basis: General rule.

INTERNAL REVENUE CODE

Regulations 111 anmeded. (See T. D. 6023, p. 132.)

SECTION 114.—BASIS FOR DEPRECIATION AND DEPLETION

REGULATIONS 111, SECTION 29.114–1: Basis for allowance of depreciation and depletion. (Also Section 23(m), Section 29.23(m)–1.) Rev. Rul. 184

INTERNAL REVENUE CODE

Processes which may be considered to be mining processes in the case of low-grade iron ores for the purpose of determining gross income for the computation of percentage depletion.

Advice is requested whether certain processes applied in the case of low-grade iron ores may be considered to be mining processes for the purpose of determining gross income from the property for the computation of percentage depletion.

Low-grade iron ores are first ground or, if necessary, pulverized to free ferrous particles from nonferrous particles. If the ferrous particles at this stage are magnetic, separation from the nonferrous particles may be accomplished by magnetic forces. If the ferrous particles are not magnetic, a so-called "magnetic roast" may be applied which reduces such particles to a magnetic state, thereby making magnetic separation possible. This so-called "magnetic roast" is not a true roast, such as that excluded from the mining processes by section 114(b)(4)(B)(iv) of the Internal Revenue Code, which is an oxidizing process. It is a closely controlled thermal process carried on in a reducing atmosphere, and it removes some of the oxygen from the nonmagnetic particles.

Other processes may also be applied. When the separation of ferrous and nonferrous particles is carried on by wet processes, such as flotation or heavy media, it may be necessary to remove as much of the reagents or media and water as practicable, by filtration or equivalent processes. If the concentrates so obtained are of shipping grade and form, they may be loaded and shipped. If not, sintering or some substantially equivalent process may be applied to bring the concen-

trates to shipping grade and form. Pelletizing, nodulizing, extruding, and briquetting may be considered as equivalent to sintering, provided they accomplish no more than to agglomerate the concentrates to suitable shipping form.

It is held that the grinding or pulverizing necessary to free the ferrous particles from the nonferrous particles, the reducing treatment (magnetic roast) when it precedes magnetic concentration, the various concentration processes and such processes as filtering and drying incidental thereto, and such agglomerating processes as pelletizing, nodulizing, extruding, or briquetting, when substantially equivalent to sintering, are ordinary treatment processes normally applied by mine owners or operators within the intent of section 114(b)(4)(B).

REGULATIONS 111, SECTION 29.114-1: Basis for allowance of depreciation and depletion.

INTERNAL REVENUE CODE

Regulations 111 amended. (See T. D. 6031, p. 120.)

SECTION 115.—DISTRIBUTIONS BY CORPORATIONS

REGULATIONS 111, SECTION 29.115-9: Distribution in redemption or cancellation of stock taxable as a dividend. T. D. 6019

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 29.—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1941

Regulations 111 amended to conform to sections 208 and 209 of the Revenue Act of 1950 and section 320 of the Revenue Act of 1951.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

On May 8, 1952, notice of proposed rulemaking was published in the Federal Register (17 F. R. 4240) conforming Regulations 111 [26 CFR, pt. 29] to section 208 (relating to treatment of certain redemptions of stock as dividends) and section 209 (relating to redemption of stock to pay death taxes) of the Revenue Act of 1950, approved September 23, 1950, and to section 320 of the Revenue Act of 1951, approved October 20, 1951. After consideration of all such relevant matter as was presented by interested persons relating to the rules proposed, the amendments to Regulations 111 set forth below are hereby adopted.

PARAGRAPH 1. There is inserted immediately preceding section 29.115-1 [26 CFR 29.115-1] the following:

SEC. 208. TREATMENT OF CERTAIN REDEMPTIONS OF STOCK AS DIVIDENDS [REVENUE ACT OF 1950, APPROVED SEPTEMBER 23, 1950].

(a) AMENDMENT OF SECTION 115(g).—Section 115(g) (relating to redemption of stock) is hereby amended to read as follows:

"(g) REDEMPTION OF STOCK.—

"(1) IN GENERAL.—If a corporation cancels or redeems its stock (whether or not such stock was issued as a stock dividend) at such time and in such manner as to make the distribution and cancellation or redemption in whole or in part essentially equivalent to the distribution of a taxable dividend, the amount so distributed in redemption or cancellation of the stock, to the extent that it represents a distribution of earnings or profits accumulated after February 28, 1913, shall be treated as a taxable dividend.

"(2) REDEMPTION THROUGH USE OF SUBSIDIARY CORPORATION.—If stock of a corporation (hereinafter referred to as the issuing corporation) is acquired by another corporation (hereinafter referred to as the acquiring corporation) and the issuing corporation controls (directly or indirectly) the acquiring corporation, the amount paid for the acquisition of the stock shall constitute a taxable dividend from the issuing corporation to the extent that the amount paid for such stock would have been considered, under paragraph (1), as essentially equivalent to a taxable dividend if such amount had been distributed by the acquiring corporation to the issuing corporation and had been applied by the issuing corporation in redemption of its stock. For the purposes of this paragraph, control means the ownership of stock possessing at least 50 per centum of the total combined voting power of all classes of stock entitled to vote or at least 50 per centum of the total value of shares of all classes of stock of the corporation."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall be applicable to taxable years ending after August 31, 1950, but shall apply only with respect to amounts received after such date.

SEC. 209. REDEMPTION OF STOCK TO PAY DEATH TAXES [REVENUE ACT OF 1950, APPROVED SEPTEMBER 23, 1950].

(a) CERTAIN DISTRIBUTIONS NOT TREATED AS DIVIDENDS.—Section 115(g) (relating to redemptions of stock) is hereby amended by adding at the end thereof the following:

"(3) REDEMPTION OF STOCK TO PAY DEATH TAXES.—The provisions of this subsection shall not apply to such part of any amount so distributed with respect to stock the value of which is included in determining the value of the gross estate of a decedent in accordance with section 811, as is distributed after such decedent's death and within the period of limitations for the assessment of estate tax provided in section 874(a) (determined without the application of section 875) or within 90 days after the expiration of such period, and as is not in excess of the estate, inheritance, legacy, and succession taxes (including any interest collected as a part of such taxes) imposed because of such decedent's death: *Provided*, That the value of the stock in such corporation for estate tax purposes comprises more than 50 per centum of the value of the net estate of such decedent."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall be applicable to taxable years ending on or after the date of the enactment of this Act, but shall apply only to amounts distributed on or after such date.

SEC. 320. REDEMPTION OF STOCK TO PAY DEATH TAXES [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

(a) AMENDMENT OF SECTION 115(g)(3).—Section 115(g)(3) (relating to redemption of stock to pay death taxes) is hereby amended by striking out "50 per centum of the value of the net estate" and inserting in lieu thereof "35 per centum of the value of the gross estate".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall be applicable to taxable years ending on or after the date of the enactment of this Act, but shall apply only to amounts distributed on or after such date.

PAR. 2. Section 29.115-9 [26 CFR 29.115-9] is amended as follows:

(A) By striking from the heading thereof "DIVIDEND.—" and by inserting in lieu thereof "DIVIDEND.—(*a*) *In general.*"

(B) By inserting at the end of such section the following:

(*b*) *Redemption of stock through use of subsidiary corporation.*—If stock of one corporation (hereinafter referred to as the "issuing corporation") is acquired from a shareholder of such corporation by another corporation (hereinafter referred to as the "acquiring corporation"), and if the issuing corporation controls, directly or indirectly, the acquiring corporation, the amount paid for such stock if received by the shareholder after August 31, 1950, may constitute a taxable dividend to such shareholder. For the purpose of this paragraph, the issuing corporation is deemed to control the acquiring corporation if it owns, directly or indirectly, stock possessing 50 percent or more of the total combined voting power of all classes of stock of the acquiring corporation entitled to vote or 50 percent or more of the total value of shares of all classes of stock of such corporation.

Where stock of one corporation is acquired by another corporation and the issuing corporation controls the acquiring corporation, the amount paid for the stock shall be treated, under section 115(g), as though such amount had first been distributed to the issuing corporation and immediately thereafter had been distributed by such corporation in redemption of such stock, to the shareholders from whom such stock was acquired. If and to the extent a distribution by the issuing corporation under such circumstances would be treated as essentially equivalent to the distribution of a taxable dividend under the principles of (*a*) of this section, the amount paid by the acquiring corporation shall be considered a dividend to the shareholder from the issuing corporation.

(c) *Redemption of stock to pay death taxes.*—Section 115(g)(3) of the Internal Revenue Code provides that in certain cases a distribution in cancellation or redemption of stock, the value of which is included in determining the value of the gross estate of a decedent, shall not be treated as a dividend under section 115(g). Section 115(g)(3) is applicable only with respect to distributions in cancellation or redemption of stock made on or after September 23, 1950. In the case of such distributions made on or after September 23, 1950, and before October 20, 1951, section 115(g)(3) applies only where the distribution is with respect to stock of a corporation the value of whose stock in the gross estate of the decedent, for the purpose of the Federal estate tax, is an amount in excess of 50 percent of the value of the net estate of such decedent. For the purpose of the preceding sentence the term "net estate of the decedent" means the net estate as computed for purposes of the additional estate tax imposed by section 935 of the Code. In the case of distributions made on or after October 20, 1951, section 115(g)(3) applies only where the distribution is with respect to stock of a corporation the value of whose stock in the gross estate of the decedent for purposes of the Federal estate tax is an amount in excess of 35 percent of the gross estate of such decedent.

For the purpose of section 115(g)(3), the term "gross estate" means the gross estate as computed in accordance with section 811 of the Code. See sections 81.10 to 81.28, inclusive, and 81.38 of Regulations 105.

In determining whether the estate of the decedent is comprised of stock of a corporation of sufficient value to satisfy the percentage requirements of section 115(g)(3) the total value, in aggregate, of all classes of stock of a corporation includible in the gross estate is taken into account. Thus, if the gross estate of the decedent, valued for purposes of the Federal estate tax at $1,000,000, includes common stock of Corporation A valued at $250,000, preferred stock of Corporation A valued at $110,000, preferred stock of Corporation B valued at $370,000, and common stock of Corporation C valued at $50,000, section 115(g)(3) is applicable to distributions, after October 20, 1951, in cancellation or redemption of either common or preferred stock of Corporation A (comprising $360,000/$1,000,000 or 36 percent of the gross estate) or preferred stock of Corporation B, (comprising $370,000/$1,000,000 or 37 percent of the gross estate) but not to distributions in cancellation or redemption of stock of Corporation C (comprising only 5 percent of the gross estate).

Section 115(g)(3) applies to distributions made after the death of the decedent and prior to the expiration of the 3-year period of limitations for the assessment of estate tax provided in section 874(a) (determined without the application of any provision of law extending or suspending the running of such period of

limitations) or within 90 days after the expiration of such period. Since the period for assessment of estate tax prescribed in section 874(a) is a period of three years after the filing of the estate tax return, section 115(g)(3) applies only to distributions made not later than three years and 90 days after the filing of the estate tax return.

While section 115(g)(3) will most frequently have application in the case where stock is cancelled or redeemed from the executor or administrator of an estate, the section is also applicable to distributions in cancellation or redemption of stock included in the decedent's gross estate and held at the time of the redemption by any person who acquired the stock by any of the means comprehended by the subdivisions of section 811, including the heir, legatee, or donee of the decedent, a surviving joint tenant, surviving spouse, appointee, or taker in default of appointment, or a trustee of a trust created by the decedent. Thus, section 115(g)(3) may apply with respect to a distribution in cancellation or redemption of stock from a donee to whom the decedent has transferred stock in contemplation of death where the value of such stock is included in the decedent's gross estate under section 811(c)(1)(A). Similarly, section 115(g)(3) may apply to the redemption of stock from a beneficiary of the estate to whom an executor has distributed the stock pursuant to the terms of the will of the decedent. However, section 115(g)(3) is not applicable to the case where stock is redeemed from a stockholder who has acquired the stock by gift or purchase from any person to whom such stock has passed from the decedent.

The total application of section 115(g)(3) with respect to stock included in the gross estate of any decedent can never exceed the amount of the estate, inheritance, legacy, and succession taxes (including any interest collected as a part of such taxes) imposed because of the decedent's death. In determining whether the total distributions in redemption of such stock made within the period of time prescribed in section 115(g)(3) exceed the amount of such taxes and interest, account shall be taken of all such distributions without regard to whether any distribution would be treated as a dividend were it not for section 115(g)(3).

For the purpose of section 115(g)(3), the Federal estate tax or any other estate, inheritance, legacy, or succession tax shall be ascertained after the allowance of any credit, relief, discount, refund, remission, or reduction of tax.

The sole effect of section 115(g)(3) is to exempt from tax as a dividend a distribution to which such section is applicable when made in redemption of stock includible in a decedent's gross estate. Such section does not, however, in any other manner affect the principles set forth in (*a*) of this section. Thus, if stock of a corporation is owned equally by A, B, and the C estate, and the corporation redeems one-half of the stock of each shareholder, the determination of whether the distributions to A and B are essentially equivalent to dividends shall be made without regard to the effect which section 115(g)(3) may have upon the taxability of the distribution to the C estate.

(This Treasury Decision is issued under the authority contained in secs. 62 and 3791 of the Internal Revenue Code (53 Stat. 32, 467; 26 U. S. C. 62, 3791).)

O. GORDON DELK,
Acting Commissioner of Internal Revenue.

Approved June 12, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register June 17, 1953, 3:54 a. m.)

SECTION 116.—EXCLUSIONS FROM GROSS INCOME

REGULATIONS 111, SECTION 29.116-1: Earned income from sources without the United States. T. D. 6039

(Also Section 147, Section 29.147-3.)

TITLE I—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 29.—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1941

Regulations 111 amended to conform to section 321 of the Revenue Act of 1951 and to section 204 of the Technical Changes Act of 1953.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

On December 13, 1952, there was published in the Federal Register (17 F. R. 11341) a notice of proposed rulemaking to conform Regulations 111 [26 CFR, pt. 29] to section 321 of the Revenue Act of 1951, relating to earned income from sources without the United States, approved October 20, 1951. After consideration of all such relevant matter as was presented by interested persons regarding the rules proposed, the amendments set forth below, including such supplemental amendments as are necessary to conform Regulations 111 to section 204 of the Technical Changes Act of 1953 [p. 508, this Bulletin], approved August 15, 1953, are hereby adopted:

PARAGRAPH 1. There is inserted immediately preceding section 29.116-1 the following:

SEC. 321. EARNED INCOME FROM SOURCES WITHOUT THE UNITED STATES [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

(a) EXCLUSION FROM GROSS INCOME.—Section 116(a) (relating to earned income from sources without the United States) is hereby amended by striking out paragraphs (1) and (2) and inserting in lieu thereof the following:

"(1) BONA FIDE RESIDENT OF FOREIGN COUNTRY.—In the case of an individual citizen of the United States, who establishes to the satisfaction of the Secretary that he has been a bona fide resident of a foreign country or countries for an uninterrupted period which includes an entire taxable year, amounts received from sources without the United States (except amounts paid by the United States or any agency thereof) if such amounts constitute earned income (as defined in paragraph (3)) attributable to such period; but such individual shall not be allowed as a deduction from his gross income any deductions properly allocable to or chargeable against amounts excluded from gross income under this paragraph.

"(2) PRESENCE IN FOREIGN COUNTRY FOR 17 MONTHS.—In the case of an individual citizen of the United States, who during any period of 18 consecutive months is present in a foreign country or countries during at least 510 full days in such period, amounts received from sources without the United States (except amounts paid by the United States or any agency thereof) if such amounts constitute earned income (as defined in paragraph (3)) attributable to such period; but such individual shall not be allowed as a deduction from his gross income any deductions properly allocable to or chargeable against amounts excluded from gross income under this paragraph."

* * * * * * *

(c) EFFECTIVE DATES.—The amendment made by subsection (a) shall be applicable to taxable years beginning after December 31, 1950. * * *

SEC. 204. EARNED INCOME FROM SOURCES WITHOUT THE UNITED STATES [TECHNICAL CHANGES ACT OF 1953, APPROVED AUGUST 15, 1953].

(a) AMENDMENT OF SECTION 116(a)(2).—Section 116(a)(2) (relating to exclusion from gross income of earned income from sources without the United States) is hereby amended by adding at the end thereof the following new sentences:

"If the 18-month period includes the entire taxable year, the amount excluded under this paragraph for such taxable year shall not exceed $20,000. If the 18-month period does not include the entire taxable year, the amount excluded under this paragraph for such taxable year shall not exceed an amount which bears the same ratio to $20,000 as the number of days in the part of the taxable year within the 18-month period bears to the total number of days in such year."

* * * * * * *

(c) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply with respect to taxable years ending after December 31, 1952, but only to amounts received after such date. In the case of any taxable year beginning in 1952 and ending in 1953 the exclusion of amounts received after December 31, 1952, shall not exceed an amount which is the same proportion of $20,000 as the number of days in such taxable year after December 31, 1952, is of 365 days. * * *

PAR. 2. Section 29.116-1, as amended by Treasury Decision 5373 [C. B. 1944, 143], approved May 23, 1944, is further amended as follows:

(A) By revising so much thereof as precedes the first sentence thereof to read as follows:

SEC. 29.116-1. EARNED INCOME FROM SOURCES WITHOUT THE UNITED STATES.—*(a) Resident of a foreign country.*

(B) By inserting immediately after "December 31, 1942," in the first sentence thereof "and before January 1, 1951,".

(C) By deleting from the first paragraph thereof the last two sentences, which commence with the words "However, once bona fide residence" and "Whether the individual citizen", respectively.

(D) By inserting after the first paragraph thereof the following new paragraphs:

For taxable years beginning after December 31, 1950, amounts constituting earned income as defined in section 116(a)(3) shall be excluded from gross income in the case of an individual citizen of the United States who establishes to the satisfaction of the Commissioner that he has been a bona fide resident of a foreign country or countries for an uninterrupted period which includes an entire taxable year, if such amounts are (1) from sources without the United States, (2) attributable to such uninterrupted period, and (3) not paid by the United States or any agency or instrumentality thereof. The exemption from tax thus provided is applicable to such amounts as are attributable to that portion of an uninterrupted period of bona fide foreign residence which falls within a taxable year during the course of which the citizen begins or terminates bona fide residence in a foreign country, provided that such period includes at least 1 entire taxable year. If attributable to an uninterrupted period in respect of which the citizen qualifies for the exemption from tax thus provided, the amounts shall be excluded from gross income irrespective of when they are received, if received in taxable years beginning after December 31, 1950. The period during which the citizen was a bona fide resident of a foreign country or countries prior to the commencement of his first taxable year beginning after December 31, 1950, may be taken into account in determining whether such citizen has been a bona fide resident of a foreign country or countries for an uninterrupted period which includes an entire taxable year.

Though the period of bona fide foreign residence must, in the application of either of the above rules, be continuous and uninterrupted, once bona fide residence in a foreign country or countries has been established, temporary visits to the United States or elsewhere on vacation or business trips will not necessarily deprive the citizen of his status as a bona fide resident of a foreign country. Whether the individual citizen of the United States is a bona fide resident of a foreign country shall be determined by the application, to the extent feasible,

of the principles of sections 29.211-2, 29.211-3, 29.211-4, and 29.211-5, relating to what constitutes residence or nonresidence, as the case may be, in the United States in the case of an alien individual.

(E) By inserting immediately after "December 31, 1941," in the first sentence of the second paragraph thereof "and before January 1, 1951,".

(F) By adding at the end of the third paragraph thereof, which commences with the words "In any case in which any amount", the following new sentence:

The apportionment and allocation of such expenses, losses, or deductions as between income from sources within, and income from sources without, the United States shall be determined in accordance with the principles of section 119 and the regulations thereunder.

(G) By adding at the end thereof the following new matter:

An amount constituting earned income as defined in section 116(a)(3) which is derived from sources without the United States shall not be included in gross income solely because it is received within the United States, since the place of receipt is immaterial in determining whether any items shall be excluded from gross income under the provisions of section 116(a). No amounts received for services performed within the United States shall be excluded from gross income by such section. For the allocation or segregation as between sources within, and sources without, the United States in the case of compensation for labor or personal services, see section 119 and the regulations thereunder.

Any return filed before the completion of the period necessary to qualify a citizen for the exemption under section 116(a) shall be filed without regard to the exemption provided by that section, but claim for credit or refund of any overpayment of tax may be filed if the taxpayer subsequently qualifies for the exemption under section 116(a). A taxpayer desiring an extension of time (in addition to that granted by section 29.53-3) for filing the return until after the completion of the qualifying period under section 116(a) shall make application therefor with the district director of internal revenue, setting forth the facts relied upon to justify the extension of time requested and including a statement as to the earliest date he expects to be in a position to determine whether he will be entitled to the exclusion provided by section 116(a). An extension of time may be granted for more than 6 months in the case of taxpayers who are abroad. For extensions of time for filing returns, see section 53(a)(2) and section 29.53-2.

In estimating his gross income for the purpose of making a declaration of estimated tax for any taxable year beginning after December 31, 1950, a citizen of the United States is not required to take into account income which it is reasonable to believe will be excluded from gross income under the provisions of section 116(a) and the regulations thereunder.

The term "foreign country" means territory under the sovereignty of a government other than that of the United States. It does not include a possession or Territory of the United States.

(*b*) *Presence in a foreign country.*—For taxable years beginning after December 31, 1950, amounts constituting earned income as defined in section 116(a)(3) shall be excluded from gross income in the case of an individual citizen of the United States who during any period of 18 consecutive months is present in a foreign country or countries during a total of at least 510 full days, if such amounts are (1) from sources without the United States, (2) attributable to such period, and (3) not paid by the United States or any agency or instrumentality thereof. If attributable to a period of 18 consecutive months in respect of which the citizen qualifies for the exemption from tax thus provided, the amounts shall be excluded from gross income irrespective of when they are received, if received in taxable years beginning after December 31, 1950.

For taxable years ending before January 1, 1953, there is no limitation upon the amount which may be excluded from gross income pursuant to the preceding paragraph. For taxable years ending after December 31, 1952, but only with respect to amounts received after such date, the amount excluded from gross income under the provisions of section 116(a)(2) shall not exceed $20,000 if

the 18-month period includes the entire taxable year. If the 18-month period does not include the entire taxable year, the amount excluded from gross income under such section for such taxable year shall not exceed an amount which bears the same ratio to $20,000 as the number of days in the part of the taxable year within the 18-month period bears to the total number of days in such year. In the case of a fiscal year beginning in 1952 and ending in 1953 the exclusion of amounts received after December 31, 1952, shall not exceed the lesser of the amount determined under the two preceding sentences or an amount which is the same proportion of $20,000 as the number of days in such taxable year after such date is of 365 days. There is no limitation as to the total amount of the exclusion for amounts received prior to January 1, 1953, in the case of such a fiscal year.

The period during which the citizen was present in a foreign country or countries prior to the commencement of his first taxable year beginning after December 31, 1950, may be taken into account in determining whether such citizen is present in a foreign country or countries during at least 510 full days during any period of 18 consecutive months.

Any return filed before the completion of the period necessary to qualify a citizen for the exemption under section 116(a) shall be filed without regard to the exemption provided by that section, but claim for credit or refund of any overpayment of tax may be filed if the taxpayer subsequently qualifies for the exemption under section 116(a). A taxpayer desiring an extension of time (in addition to that granted by section 29.53-3) for filing the return until after the completion of the qualifying period under section 116(a) shall make application therefor with the district director of internal revenue, setting forth the facts relied upon to justify the extension of time requested and including a statement as to the earliest date he expects to be in a position to determine whether he will be entitled to the exclusion provided by section 116(a). An extension of time may be granted for more than 6 months in the case of taxpayers who are abroad. For extensions of time for filing returns, see section 53(a)(2) and section 29.53-2.

In estimating his gross income for the purpose of making a declaration of estimated tax for any taxable year beginning after December 31, 1950, a citizen of the United States is not required to take into account income which it is reasonable to believe will be excluded from gross income under the provisions of section 116(a) and the regulations thereunder.

The provisions of paragraph (*a*) hereof respecting the disallowance of certain deductions, the definition of earned income, the source of income, and the immateriality of the place of receipt of amounts constituting earned income are equally effective in the application of this paragraph.

The term "foreign country" means territory under the sovereignty of a government other than that of the United States and includes the airspace over such territory. It does not include a possession or Territory of the United States.

The exclusion granted by section 116(a)(2) applies to income attributable to any period of 18 consecutive months during which the citizen satisfies the 510 full-day requirement, even though such period constitutes a part of a longer period of presence in a foreign country or countries. For this purpose, the term "18 consecutive months" means any period of such duration, that is, any period commencing with the beginning of any day of a calendar month and terminating (1) with the close of the day which precedes that day in the eighteenth succeeding calendar month numerically corresponding to the day of the period's beginning, or, if there is no such corresponding day, (2) with the close of the last day of such eighteenth succeeding month. Such period need not necessarily commence with the day of arrival in a foreign country, nor terminate with the day of departure therefrom. In no event will the 510 full-day requirement be prorated over a period of less than 18 consecutive months.

Thus, a citizen who arrives in a foreign country on January 1, 1952, makes several return trips to the United States, and then finally departs from the foreign country on February 14, 1954, may not be present in such country for 510 full days during the 18-month period commencing with January 1, 1952, and ending with the close of June 30, 1953, because of his visits to the United States during such period, but may satisfy the 510 full-day requirement during the 18-month period commencing with February 15, 1952, and ending with the close of August 14, 1953. In such event, the exclusion will apply to income attributable to the latter period, but not to income attributable to the period commencing with January 1, 1952, and ending with the close of February 14,

1952. For such purpose, it is assumed that no part of the period ending with the close of February 14, 1952, is included in any 18-month period during which the 510 full-day requirement is satisfied. Furthermore, the mere fact that the 510 full-day requirement has been satisfied with respect to the period ending with the close of August 14, 1953, does not mean that income earned thereafter will be excluded under section 116(a)(2) unless such income is attributable to another 18-month period during which there is compliance with the 510 full-day requirement. Thus, the 510 full-day requirement cannot be prorated over the 6-month period commencing with August 15, 1953, and ending with the close of February 14, 1954, in order to determine whether the exclusion allowed by section 116(a)(2) applies to income attributable to such 6-month period. Therefore, assuming that the citizen is present in the foreign country 170 full days (⅓ of 510 full days) during such 6-month period (⅓ of 18 consecutive months), the exclusion will not be applicable to income attributable to any part of such 6-month period if no part thereof is included in any 18-month period during which the 510 full-day requirement is satisfied.

The term "full day" means, not any 24-consecutive-hour period, but a continuous period of 24 hours commencing from midnight and ending with the following midnight. In computing the minimum of 510 full days of presence in a foreign country or countries, all separate periods of such presence during the period of 18 consecutive months are to be aggregated. The 510 full days need not be consecutive, but may be interrupted by a number of short periods during which the citizen is not present in a foreign country. Time spent in a foreign country in the employment of the United States Government will count toward satisfaction of the 510 full-day requirement, even though amounts paid by such Government are not exempt from tax under section 116(a)(2).

In each of the following examples it is assumed that the facts are such that the limitations upon the amount to be excluded, which were added by section 204 of the Technical Changes Act of 1953, are not applicable.

Example (1). On February 1, 1953, Mr. White, a citizen of the United States privately employed, arrived in Puerto Rico on a business assignment. Upon completion of the assignment he departed for a new assignment in Venezuela. On June 1, 1953, at 9 a. m. he arrived in Venezuela, where he remained until 2 p. m. on October 25, 1954, at which time he departed for another assignment in Puerto Rico. On January 10, 1955, he left Puerto Rico for a new assignment in the United States. During the 18-month period commencing with April 25, 1953, and ending with the close of October 24, 1954, the taxpayer was in a foreign country an aggregate of 510 full days; in addition, during the 18-month period commencing with June 2, 1953, and ending with the close of December 1, 1954, he was in a foreign country an aggregate of 510 full days. The exemption from tax granted by section 116(a)(2) will thus apply to income attributable to the entire period which commences with April 25, 1953, and ends with the close of December 1, 1954, a period of approximately 19 consecutive months.

Example (2). At 2 p. m. on January 18, 1952, Mr. Brown, a citizen of the United States privately employed, arrived in England on a business trip from the United States. On May 19, 1952, at 10 p. m. he departed from England by steamer and arrived in the United States on May 25, 1952. After spending a period therein on official business, he left the United States by steamer on June 9, 1952, and arrived in France at 3 p. m., June 14, 1952. At 8 a. m. on February 3, 1953, he departed from France by airplane for a brief visit to Puerto Rico, arriving there on February 4; and thence went to England, arriving there at 1 a. m. on February 12, 1953, where he remained until midnight, July 18, 1953, at which time the 510 full-day requirement was satisfied in respect of the period of 18 consecutive months which began with January 19, 1952. Mr. Brown continued his presence in England, not leaving such country until 5 a. m. on November 18, 1953, at which time he departed for the United States. During the 18-month period commencing with January 19, 1952, and ending with the close of July 18, 1953, the taxpayer was in a foreign country or countries an aggregate of 510 full days; in addition, during the 18-month period commencing with June 16, 1952, and ending with the close of December 15, 1953, he was in a foreign country or countries an aggregate of 510 full days. The exemption from tax granted by section 116(a)(2) will thus apply to income attributable to the entire period which commences with January 19, 1952, and ends with the close of December 15, 1953. The computation with respect to each period may be illustrated as follows:

First 18 month period (Jan. 19, 1952 through July 18, 1953)	*Full days in foreign country*
Jan. 19, 1952 to May 18, 1952	121
May 19, 1952 to June 14, 1952	0
June 15, 1952 to Feb. 2, 1953	233
Feb. 3, 1953 to Feb. 12, 1953	0
Feb. 13, 1953 to July 18, 1953	156
Total full days	510

Second 18 month period (June 16, 1952 through Dec. 15, 1953)	*Full days in foreign country*
June 16, 1952 to Feb. 2, 1953	232
Feb. 3, 1953 to Feb. 12, 1953	0
Feb. 13, 1953 to Nov. 17, 1953	278
Nov. 18, 1953 to Dec. 15, 1953	0
Total full days	510

Example (3). On March 6, 1952, at 3 p. m. Mr. Green, a citizen privately employed, arrived in Cuba where he remained until 9 p. m., June 25, 1952, at which time he departed from Cuba for a short business trip to Puerto Rico. Upon completion of his negotiations in that possession, he departed for Mexico, arriving there at 2 p. m. on July 24, 1952, where he remained until 10 a. m., August 22, 1953, at which time he departed from such country for a vacation in the United States. He arrived again in Mexico at 9 a. m. on September 5, 1953, where he remained until 8 a. m., January 1, 1954, at which time he departed from such country for a new assignment in the United States. During the 18-month period commencing with March 7, 1952, and ending with the close of September 6, 1953, the taxpayer was in a foreign country or countries an aggregate of 504 full days; during the 18-month period commencing with July 1, 1952, and ending with the close of December 31, 1953, he was in a foreign country an aggregate of 510 full days. The exemption from tax granted by section 116(a)(2) will thus not apply to income attributable to any part of the period beginning with March 6, 1952, and ending with the close of June 30, 1952; it will apply to income attributable to the period commencing with July 1, 1952, and ending with the close of December 31, 1953. The computation with respect to each period may be illustrated as follows:

First 18 month period (Mar. 7, 1952 through Sept. 6, 1953)	*Full days in foreign country*
Mar. 7, 1952 to June 24, 1952	110
June 25, 1952 to July 24, 1952	0
July 25, 1952 to Aug. 21, 1953	393
Aug. 22, 1953 to Sept. 5, 1953	0
Sept. 6, 1953	1
Total full days	504

Second 18 month period (July 1, 1952 through Dec. 31, 1953)	*Full days in foreign country*
July 1, 1952 to July 24, 1952	0
July 25, 1952 to Aug. 21, 1953	393
Aug. 22, 1953 to Sept. 5, 1953	0
Sept. 6, 1953 to Dec. 31, 1953	117
Total full days	510

PAR. 3. Section 29.147-3, as amended by Treasury Decision 5907, [C. B. 1952-1, 107] approved May 29, 1952, is further amended as follows:

(A) By inserting immediately after "without the United States made" in (*e*) of the first paragraph thereof "before January 1, 1951,".

(B) By inserting immediately preceding the last paragraph thereof the following:

(*n*) Payments representing earned income for services rendered without the United States made on or after January 1, 1951, to a citizen of the United States, if it is reasonable to believe that such amounts will be excluded from gross income under the provisions of section 116(a) and the regulations thereunder.

(This Treasury Decision is issued under the authority contained in secs. 62 and 3791 (53 Stat. 32, 467; 26 U. S. C. 62, 3791) of the Internal Revenue Code.)

O. GORDON DELK,
Acting Commissioner of Internal Revenue.

Approved August 27, 1953.

H. CHAPMAN ROSE,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register August 31, 1953, 8:54 a. m.)

REGULATIONS 111, SECTION 29.116–1: Earned income from sources without the United States.

INTERNAL REVENUE CODE

Okinawa is a foreign country. (See Rev. Rul. 199, p. 225.)

SECTION 117.—CAPITAL GAINS AND LOSSES

REGULATIONS 111, SECTION 29.117–7: Gains and losses from involuntary conversions and from the sale or exchange of certain property used in the trade or business. (Also Section 23(e), Section 29.23(e)–5.) — Rev. Rul. 195

INTERNAL REVENUE CODE

Where livestock held by a taxpayer for draft, breeding, or dairy purposes, and held for 12 months or more from the date of acquisition, is subsequently killed by a destructive force, such as lightning, or by order of governmental authority (because of disease), any loss sustained thereby constitutes a loss from involuntary conversion within the purview of section 117(j) of the Internal Revenue Code. However, if the death of such livestock is the result of natural causes, such as old age or sickness, the loss constitutes an ordinary business loss. See section 23(e) of the Code and section 29.23(e)–5 of Regulations 111.

REGULATIONS 111, SECTION 29.117–8: Gain or loss upon the cutting and disposal of timber and the disposal of coal. (Also Sections 29.117–3, 29.117–7; Section 23(m), Section 29.23(m)–1; Section 102, — T. D. 6021

Section 29.102-4; Section 113(a), Section 29.113(a)(14)-1; Section 481, Section 29.481-1.)

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 29.—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1941

Regulations 111 amended to conform to section 325 of the Revenue Act of 1951.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

On December 4, 1952, notice of proposed rulemaking conforming Regulations 111 [26 CFR, pt. 29] to section 325 of the Revenue Act of 1951, approved October 20, 1951, was published in the Federal Register (17 F. R. 10969). No objection to the rules proposed having been received, the amendments set forth below are hereby adopted.

PARAGRAPH 1. Section 29.23(m)-1, as amended by Treasury Decision 5461 [C. B. 1945, 284], approved July 9, 1945 [26 CFR 29.23(m)-1], is further amended as follows:

(A) By amending the second sentence of the second paragraph thereof to read as follows:

However, no depletion deduction shall be allowed the owner with respect to any timber or coal which such owner has disposed of under any form of contract by virtue of which he retains an economic interest in such timber or coal, if such disposal is considered a sale of timber or coal under section 117(k)(2) of the Code.

(B) By adding at the end of (*f*) thereof the following paragraph:

Rents and royalties paid or incurred by a taxpayer with respect to coal shall be excluded from the "gross income from the property" without regard to the treatment under section 117(k)(2) of such rents and royalties in the hands of the recipient.

PAR. 2. Section 29.102-4, as amended by Treasury Decision 5989 [C. B. 1953-1, 119], approved February 16, 1953 [26 CFR 29.102-4], is further amended by inserting immediately preceding the last paragraph thereof the following paragraph:

In determining "section 102 net income", section 117(k)(2), in the case of coal, shall have no application. See section 29.117-8(*c*).

PAR. 3. Section 29.113(a)(14)-1, as amended by Treasury Decision 5394 [C. B. 1944, 274], approved July 27, 1944 [26 CFR 29.113(a)(14)-1], is further amended by inserting in the second sentence of the second paragraph thereof after "determination of loss upon timber" the following: "or coal".

PAR. 4. There is inserted immediately preceding section 29.117-1 [26 CFR 29.117-1] the following:

SEC. 325. TAX TREATMENT OF COAL ROYALTIES [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

(a) DEFINITION OF PROPERTY USED IN THE TRADE OR BUSINESS.—Section 117(j)(1) (relating to the definition of property used in the trade or business) is hereby amended by adding after the word "timber" in the second sentence thereof the following: "or coal".

(b) GAIN OR LOSS UPON CERTAIN DISPOSALS OF TIMBER OR COAL.—Section 117(k)(2) (relating to the disposal of timber) is hereby amended to read as follows:

"(2) In the case of the disposal of timber or coal (including lignite), held for more than 6 months prior to such disposal, by the owner thereof under any form or type of contract by virtue of which the owner retains an economic interest in such timber or coal, the difference between the amount received for such timber or coal and the adjusted depletion basis thereof shall be considered as though it were a gain or loss, as the case may be, upon the sale of such timber or coal. Such owner shall not be entitled to the allowance for percentage depletion provided for in section 114(b)(4) with respect to such coal. This paragraph shall not apply to income realized by the owner as a co-adventurer, partner, or principal in the mining of such coal. The date of disposal of such coal shall be deemed to be the date such coal is mined. In determining the gross income, the adjusted gross income, or the net income of the lessee, the deductions allowable with respect to rents and royalties shall be determined without regard to the provisions of this paragraph. This paragraph shall have no application, in the case of coal, for the purposes of applying section 102 or subchapter A of chapter 2 (including the computation under section 117(c)(1) of a tax in lieu of the tax imposed by section 500)."

(c) CLERICAL AMENDMENT.—The heading to section 117(k) (relating to the gain or loss upon the cutting of timber) is hereby amended to read as follows: "(k) GAIN OR LOSS IN THE CASE OF TIMBER OR COAL.—".

* * * * * * *

(f) EFFECTIVE DATE.—* * * the amendments made by this section shall be applicable only with respect to taxable years ending after December 31, 1950 (whether the contract was made on, before, or after such date), but shall apply only with respect to amounts received or accrued after such date.

PAR. 5. Section 29.117-3 as amended by Treasury Decision 5951 [C. B. 1952-2, 81], approved December 2, 1952 [26 CFR 29.117-3], is further amended by adding at the end thereof the following:

Where amounts are received or accrued after December 31, 1950, from the disposal of coal to which the provisions of section 117(k)(2) are applicable, the computation under section 117(c)(1) of a tax in lieu of the tax imposed by section 500 shall be made without regard to section 117(k)(2); that is, the partial tax under section 117(c)(1)(A), insofar as it involves the tax under section 500, is computed without regard to section 117(k)(2).

PAR. 6. Section 29.117-7 as amended by Treasury Decision 5980 [C. B. 1953-1, 65], approved February 3, 1953 [26 CFR 29.117-7], is further amended by adding after the word "timber" in (iii) of (*a*)(1) thereof, the phrase ", or disposal of coal,".

PAR. 7. Section 29.117-8, as added by Treasury Decision 5394, approved July 27, 1944 [26 CFR 29.117-8], is amended as follows:

(A) By amending the heading to read as follows:

SEC. 29.117-8. GAIN OR LOSS UPON THE CUTTING AND DISPOSAL OF TIMBER AND THE DISPOSAL OF COAL.—

(B) By adding at the end thereof the following:

(*c*) *Gain or loss upon the disposal of coal.*—With respect to taxable years ending after December 31, 1950, but only with respect to amounts received or accrued after such date, if a taxpayer disposes of coal (including lignite), held for more than 6 months prior to such disposal, under any form or type of contract whereby he retains an economic interest in such coal, the difference between the amount received for such coal and the adjusted depletion basis thereof under section 114(b)(1) shall be considered to be a gain or loss upon the sale of such coal.

The adjusted depletion basis under section 114(b)(1), for the purpose of this section, includes adjustments for development and exploration expenditures and for deductions under section 113(b)(1) (J) and (M). For the purpose of this section, the date of disposal of the coal shall be deemed to be the date the coal is mined. If the coal has been held for more than 6 months on the date that it is mined, it is immaterial that it had not been held for more than 6 months on the date of the contract. For the purpose of section 117(j), such coal shall be considered to be property used in the trade or business, along with other property of the taxpayer used in the trade or business as defined in section 117(j)(1). Whether gain or loss resulting from the disposition of the coal will be deemed to be gain or loss resulting from the sale of a capital asset held for more than 6 months will depend upon the application of section 117(j) to that and other transactions of the taxpayer.

There shall be no allowance for percentage depletion provided for in section 114(b)(4) with respect to amounts received any part of which is considered to be received from the sale of coal under section 117(k)(2). In computing the gross income, adjusted gross income, or the net income of the lessee, the deductions allowable with respect to rents and royalties shall be determined without regard to the provisions of section 117(k)(2). Section 117(k)(2) shall have no application with respect to amounts received by a taxpayer as a coadventurer, partner, or principal in the mining of coal.

To the extent any advance payments are treated, under section 117(k)(2) as received from the sale of coal for any taxable year, and the grant of the coal rights for which such payments are made expires, terminates, or is abandoned in a later taxable year before the coal which has been paid for has been mined, the grantor shall recompute the tax liability for the prior taxable year and treat such payments to such extent as not received from the sale of the coal; such recomputation should be in the form of an "amended return" if necessary.

PAR. 8. There is inserted immediately preceding section 29.481-1 [26 CFR 29.481-1] the following:

SEC. 325. TAX TREATMENT OF COAL ROYALTIES [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

* * * * * * *

(d) TECHNICAL AMENDMENT.—Section 481(a)(4) is hereby amended by striking out "cutting or disposal of timber" and inserting in lieu thereof "cutting of timber, or the disposal of timber or coal,".

* * * * * * *

(f) EFFECTIVE DATE.—* * * the amendments made by this section shall be applicable only with respect to taxable years ending after December 31, 1950 (whether the contract was made on, before, or after such date), but shall apply only with respect to amounts received or accrued after such date.

PAR. 9. Section 29.481-1, as added by Treasury Decision 5855 [C. B. 1951-2, 141], approved September 13, 1951 [26 CFR 29.481-1], is amended by adding after "timber," in (c)(4)(ii) thereof, the phrase "or disposal of coal,".

(This Treasury Decision is issued under the authority contained in secs. 62 and 3791 of the Internal Revenue Code (53 Stat. 32; 26 U. S. C. 62, 3791).)

T. COLEMAN ANDREWS,
Commissioner of Internal Revenue.

Approved June 18, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register June 23, 1953, 8:50 a. m.)

REGULATIONS 111, SECTION 29.117-10: Gains and losses from certain short sales of capital assets. Rev. Rul. 154

INTERNAL REVENUE CODE

Certain bonds traded in on the New York Stock Exchange are convertible, at the option of the holder, into common stock of the issuing corporation. The market price of the bonds tends to fluctuate in direct relation to the market price of the stock. At times, however, there is a slight difference in the relative market prices of the bonds and stock. When the price of the bonds is down, in relation to the price of the stock, members of the Exchange buy the bonds at the market price and as nearly simultaneously as possible sell the stock into which the bonds are convertible. The bonds purchased are then converted and the stock so received is used to close the sale. These transactions are known as arbitrage operations. *Held*, sales of stock in the manner described constitute short sales within the purview of section 117 (l) of the Internal Revenue Code.

REGULATIONS 111, SECTION 29.117-13: Gain from sale or exchange of certain property between spouses or between an individual and a controlled corporation. T. D. 6022

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 29.—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1941

Regulations 111 amended to conform to section 328 of the Revenue Act of 1951.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

On November 22, 1952, notice of proposed rulemaking with respect to amendments to conform Regulations 111 to section 328 of the Revenue Act of 1951, approved October 20, 1951, relating to treatment of gain on sales of certain property between spouses and between an individual and a controlled corporation, was published in the Federal Register (17 F. R. 10649). No objections to the proposed rules having been received, the amendments to Regulations 111 [26 CFR, pt. 29] set forth below are hereby adopted:

PARAGRAPH 1. There is inserted immediately preceding section 29.117-1 the following:

SEC. 328. TREATMENT OF GAIN ON SALES OF CERTAIN PROPERTY BETWEEN SPOUSES AND BETWEEN AN INDIVIDUAL AND A CONTROLLED CORPORATION [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

(a) DISALLOWANCE OF CAPITAL GAIN TREATMENT.—Section 117 (relating to capital gains and losses) is hereby amended by adding at the end thereof the following new subsection:

"(o) GAIN FROM SALE OF CERTAIN PROPERTY BETWEEN SPOUSES OR BETWEEN AN INDIVIDUAL AND A CONTROLLED CORPORATION.—

"(1) TREATMENT OF GAIN AS ORDINARY INCOME.—In the case of a

sale or exchange, directly or indirectly, of property described in paragraph (2)—

"(A) between a husband and wife; or

"(B) between an individual and a corporation more than 80 per centum in value of the outstanding stock of which is owned by such individual, his spouse, and his minor children and minor grandchildren;

any gain recognized to the transferor from the sale or exchange of such property shall be considered as gain from the sale or exchange of property which is neither a capital asset nor property described in subsection (j).

"(2) SUBSECTION APPLICABLE ONLY TO SALES OR EXCHANGES OF DEPRECIABLE PROPERTY.—This subsection shall apply only in the case of a sale or exchange of property by a transferor which in the hands of the transferee is property of a character which is subject to the allowance for depreciation provided in section 23(l)."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall be applicable with respect to taxable years ending after April 30, 1951, but shall apply only with respect to sales or exchanges made after May 3, 1951.

PAR. 2. There is added after section 29.117-12, as added by Treasury Decision 6013 [C. B. 1953-1, 195], approved May 25, 1953, the following new section:

SEC. 29.117-13. GAIN FROM SALE OR EXCHANGE OF CERTAIN PROPERTY BETWEEN SPOUSES OR BETWEEN AN INDIVIDUAL AND A CONTROLLED CORPORATION.—Section 117(o) provides that any gain recognized to the transferor from the sale or exchange, directly or indirectly, between a husband and wife or between an individual and a controlled corporation, of property which, in the hands of the transferee, is property of a character subject to the allowance for depreciation provided in section 23(l) (including such property with respect to which a deduction for amortization is allowable under section 23(t)) shall be considered as gain from the sale or exchange of property which is neither a capital asset nor property described in section 117(j). This rule is applicable for taxable years ending after April 30, 1951, but only with respect to sales or exchanges made after May 3, 1951. For the purpose of section 117(o), a corporation is controlled when more than 80 percent in value of all outstanding stock of the corporation is owned (whether legal ownership or beneficial ownership) by the taxpayer, his spouse, and his minor children and minor grandchildren. For the purpose of this rule, the terms "children" and "grandchildren" include stepchildren and legally adopted children. The provisions of section 117(o) are applicable whether the property be transferred from the corporation to the shareholder or from the shareholder to the corporation.

(This Treasury Decision is issued under the authority contained in secs. 62 and 3791 of the Internal Revenue Code (53 Stat. 32, 467; 26 U. S. C. 62, 3791).)

T. COLEMAN ANDREWS,
Commissioner of Internal Revenue.

Approved June 19, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register June 23, 1953, 8:51 a. m.)

REGULATIONS 111, SECTION 29.117-14: Capital gains treatment of certain termination payments. T. D. 6036

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 29.—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1941

Regulations 111 amended to conform to section 329 of the Revenue Act of 1951 relating to capital gains treatment of certain termination payments to employees.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

On November 15, 1952, notice of proposed rulemaking regarding amendments to conform Regulations 111 [26 CFR, pt. 29] to section 329 of the Revenue Act of 1951, approved October 20, 1951, relating to capital gains treatment of certain termination payments to employees, was published in the Federal Register (17 F. R. 10465). After consideration of all relevant matter presented by interested persons regarding the rules proposed, the amendments to Regulations 111 set forth below are hereby adopted.

PARAGRAPH 1. There is inserted immediately preceding section 29.117-1 the following:

SEC. 329. RECEIPTS OF CERTAIN TERMINATION PAYMENTS BY EMPLOYEE [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

(a) TAXABILITY TO EMPLOYEE AS CAPITAL GAIN.—Section 117 of the Internal Revenue Code is hereby amended by adding at the end thereof the following subsection:

"(p) TAXABILITY TO EMPLOYEE OF TERMINATION PAYMENTS.—Amounts received from the assignment or release by an employee, after more than twenty years' employment, of all his rights to receive, after termination of his employment and for a period of not less than five years (or for a period ending with his death), a percentage of future profits or receipts of his employer shall be considered an amount received from the sale or exchange of a capital asset held for more than six months, if such rights were included in the terms of the employment of such employee for not less than twelve years, and if the total of the amounts received for such assignment or release are received in one taxable year and after the termination of such employment."

(b) EFFECTIVE DATE.—The amendment made by this section shall be applicable with respect to taxable years beginning after December 31, 1950.

PAR. 2. There is inserted immediately after section 29.117-13, as added by Treasury Decision 6022, p. 173, this Bulletin, approved June 19, 1953, the following new section:

SEC. 29.117-14. CAPITAL GAINS TREATMENT OF CERTAIN TERMINATION PAYMENTS.—For taxable years beginning after December 31, 1950, certain amounts received by an employee pursuant to the assignment or release by the employee of all his rights to receive, after termination of his employment and for a period of not less than 5 years or for a period ending with his death, a percentage of future profits or receipts of his employer, that is, profits or receipts attributable to a period subsequent to termination of employment, shall, under the provisions of section 117(p), be considered and treated as an amount received from the sale or exchange of a capital asset held for more than 6 months. The provisions of section 117(p) shall have application to such payments only if the following conditions are met:

(1) The employee was employed by the employer, in whose future profits or receipts the employee has an interest, for a period of more than 20 years prior to the assignment or release by the employee of his rights in such future profits or receipts,

(2) The full rights of the employee to the percentage of the future profits or receipts of such employer, which rights are the subject of the assignment or release, were incorporated in the terms of the contract of employment between the employee and the employer for a period of at least 12 years,

(3) The assignment or release was made after the termination of the employee's employment with such employer,

(4) The assignment or release conveyed all the rights of the employee in the future profits or receipts of such employer and conveyed no other rights of the employee, and

(5) The total amount to which the employee became entitled pursuant to the assignment or release was received by the employee after the termination of his employment with such employer and in 1 taxable year of the employee.

It is immaterial whether the contract of employment is oral or written provided the prescribed conditions are met. The requirement that the assignment or release be made after the termination of the employee's employment contemplates a complete and bona fide termination of the relationship of employer and employee and not merely, for example, a termination of such relationship under the particular contract or contracts of employment pursuant to which the employee acquired his rights in the future profits or receipts of the employer. The contract need not expressly provide that the employee shall share in the future profits or receipts of the employer for a minimum period of 5 years. However, if the contract does not expressly so provide and the assignment or release is made prior to the expiration of 5 years following the termination of employment, the terms of the contract considered in conjunction with the facts in the particular situation must establish that the rights of the employee to a percentage of future profits or receipts, in all probability, will extend to a period of not less than 5 years from the date of termination of employment or for a period ending with his death. Section 117(p) has application only to an assignment or release made by the employee who acquired the right to a percentage of future profits or receipts of the employer, and has no application to amounts received other than as payment for assignment or release of such right. Section 117(p) has no effect upon the determination of the income tax of the employer making the payment to the employee.

(This Treasury Decision is issued under the authority contained in secs. 62 and 3791 of the Internal Revenue Code (53 Stat. 32, 467; 26 U. S. C. 62, 3791).)

T. Coleman Andrews,
Commissioner of Internal Revenue.

Approved August 4, 1953.

M. B. Folsom,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register August 7, 1953, 8:52 a. m.)

SECTION 122.—NET OPERATING LOSS DEDUCTION

Regulations 111, Section 29.122-4: Computation of net operating loss carryovers and net operating loss carrybacks. (Also Section 322, Section 29.322-7.) — Rev. Rul. 218

INTERNAL REVENUE CODE

Net operating losses carried back or carried over to a particular taxable year are considered to be applied in reduction of the net income of such year in the order of the taxable years from which such losses are carried over or carried back, beginning with the loss for the earliest taxable year, without regard to the statute of limitations. (See secs. 29.122-1, 29.122-4 of Regulations 111.) Thus, where a taxpayer failed to avail itself of a 1946 net operating loss carryover on its 1947 return and later sustained a net operating loss in 1949 which is carried back

to 1947, that net operating loss is absorbed in the year 1947 only to the extent of the net income remaining after application of the 1946 net operating loss carryover. Where the period in which a timely claim for refund or credit of 1947 tax, based on a net operating loss carryover from 1946, has expired but a timely claim for refund or credit with respect to the 1949 net operating loss carryback has been filed, the amount of the refund or credit which can be made may not exceed the overpayment attributable to the 1949 net operating loss carryback. (See sec. 29.322-7, Regulations 111; G. C. M. 9800, C. B. X-2, 271 (1931).) In determining the net income for 1947 against which the net operating loss carryback for 1949 may be applied, such income must be first reduced by the net operating loss carryover from 1946 which was available as a deduction from 1947 income.

SECTION 124B.—AMORTIZATION DEDUCTION FOR GRAIN STORAGE FACILITIES

Rev. Rul. 227

INTERNAL REVENUE CODE

The amortization deduction allowable under section 124B of the Internal Revenue Code may be taken in respect of a grain storage facility for which a certificate under section 124A(e) was made provided that the certificate is canceled by the certifying authority prior to the making of any election to take the amortization deduction allowable under section 124A(a) with respect to such facility.

Advice is requested whether the amortization deduction under section 124B of the Internal Revenue Code is allowable in the case of a grain storage facility for which a certificate was issued under section 124A(e) but which certificate was later canceled by the certifying authority prior to the making of any election to take the amortization allowable under section 124A(a) with respect to such facility.

Section 124B(d) provides that the term "grain storage facility" shall not include any facility any part of which is an emergency facility under section 124A.

The issuance of a certificate under section 124A(e) with respect to any structure will not prevent the classification of such structure as a "grain storage facility" within the meaning of section 124B(d), nor the allowance of the deduction provided by section 124B(a) with respect to such structure, provided that, prior to making any election to take the amortization deduction allowable under section 124A(a) with respect to such structure, such certificate has been canceled by the certifying authority.

SECTION 125.—AMORTIZABLE BOND PREMIUM

REGULATIONS 111, SECTION 29.125-1: In general.

INTERNAL REVENUE CODE

Premiums paid for Federal Housing Administration insured mortgage loans. (See Rev. Rul. 258, p. 143.)

SECTION 126.—INCOME IN RESPECT OF DECEDENTS

REGULATIONS 111, SECTION 29.126-1: Inclusion in gross income of income in respect of a decedent.
(Also Section 811, Section 81.13, Regulations 105.)

Rev. Rul. 196

INTERNAL REVENUE CODE

The amount received by the estate of a decedent-employee upon the surrender to the employer of options to purchase employer's stock is compensatory income the right to which was acquired by the estate from the decedent within the purview of section 126 of the Internal Revenue Code.

The amount of the difference between the fair market value of the employer's stock, as of the applicable valuation date for Federal estate tax purposes, and the price at which such stock could have been purchased under the options is includible in the decedent's gross estate. The estate is entitled to the allowable deduction for the estate tax paid on account of the value of the options in accordance with the provisions of section 126(c).

Advice is requested as to the Federal income tax consequences in respect to the amount received by the estate of a deceased employee upon the surrender to the employer corporation of unexercised options to purchase stock, and whether the value of such options should be included in the gross estate of the decedent for Federal estate tax purposes.

In the instant case, the employer corporation adopted a plan which was approved by its board of directors and stockholders, under which plan various employees were granted options to purchase stock of the corporation. The options may only be exercised by an employee at a time when he is employed by the corporation, except in the case of his retirement with the consent of the employer. The options are not transferable except in the event of the optionee's death while an employee, in which case the options pass to the decedent's estate, heirs, legatees, or next of kin, and if the proper party, within a certain period after the optionee's death, requests the corporation to do so, it will purchase any unexercised options at a price per share not greater than the amount by which the closing price of the corporation's shares of the stock on the New York Stock Exchange, on the day last preceding the date of such purchase, exceeds the option price per share. At the date of death of the optionee in the case under consideration, he held unexercised options covering a large number of shares, which options passed to his legal representative.

I. T. 3795, C. B. 1946-1, 15, holds that if an employee receives an option on or after February 26, 1945, to purchase stock of the employer corporation and the employee transfers such option for consideration in an arm's-length transaction, the employee realizes taxable income by way of compensation on the date he receives such consideration to the extent of the value of such consideration. Accordingly, if the option in the instant case had been transferred to the employer corporation by the employee, he would have realized taxable income by way of compensation to the extent of the consideration received. Section 130A of the Code, relating to the treatment of restricted stock

options, does not apply to cases where options are transferred by the employee.

Section 126(a)(1)(A) of the Internal Revenue Code provides that all amounts to which a decedent is entitled as gross income and which are not includible in computing his net income for his last taxable year or any prior taxable year, shall be included, when received, in the gross income of the estate of the decedent or of the person receiving such amounts if such amounts are received in a taxable year ending after December 31, 1942. (Sec. 29.126-1 of Regulations 111.) Section 126(a) provides that the right to receive an amount shall be treated in the hands of the estate as if it had been acquired by the estate in the transaction by which the decedent acquired such right, and that the amount includible in gross income shall have the character in the hands of the estate as it would have had in the hands of the decedent had he received such income.

In the Tax Court decision in *Estate of Edgar V. O'Daniel* v. *Commissioner*, 10 T. C. 631, affirmed, 173 Fed. (2d) 966, involving the payment of a bonus under a plan in which the decedent had participated, the court stated "The amount here in question was not earned by the estate by virtue of its own activity or investments, but was income earned by the decedent. It was paid for services rendered by him to his employer and was received by the petitioner, as his representative, solely because of services rendered by him. It remained income when received by the estate. The right of the estate to receive it was acquired from, by reason of the death of, the decedent within the purpose and intended meaning of section 126(a)(1)(A)." In the instant case, the options represented income earned by the decedent-employee as a result of services rendered by him, although unrealized until such options were surrendered for a consideration. Accordingly, the right of the estate to realize earned income is derived from the decedent-employee upon acquisition of the option by the estate, and, therefore, such option constitutes a right to income in respect of the decedent within the meaning of section 126(a)(1)(A) of the Code.

Section 811 of the Internal Revenue Code provides that there shall be included in the gross estate of a decedent the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated, except real property situated outside of the United States. Options to purchase stock are includible in the gross estate of a decedent, at the fair market value thereof. Since the instant case is governed by section 126 of the Code, the provisions of section 113(a)(5) with respect to the basis of property acquired by bequest, devise, or inheritance do not apply to the amounts received by the estate. (Sec. 29.126-1 of Regulations 111.) However, the estate is allowed a deduction for the estate tax paid on account of the value of the options in accordance with the provisions of section 126(c) of the Code.

In view of the foregoing, it is held that the amount received by the estate of a decedent-employee upon the surrender to the employer of options to purchase employer's stock is compensatory income the right to which was acquired by the estate from the decedent within the purview of section 126 of the Internal Revenue Code. The amount of the difference between the fair market value of the employer's stock, as of the applicable valuation date for Federal estate tax purposes, and

the price at which such stock could have been purchased under the options is includible in the decedent's gross estate. The estate is entitled to the allowable deduction for the estate tax paid on account of the value of the options in accordance with the provisions of section 126(c) of the Code.

SECTION 130.—LIMITATION ON DEDUCTIONS ALLOWABLE TO INDIVIDUALS IN CERTAIN CASES

REGULATIONS 111, SECTION 29.130–1: Limitation on deductions allowable to individuals in certain cases. Rev. Rul. 155

(Also Section 182, Section 29.182–1.)

INTERNAL REVENUE CODE

Application of section 130 of the Code to a trade or business carried on in the form of a partnership.

Advice is requested as to whether section 130 of the Internal Revenue Code is applicable in cases where the trade or business of the individual is carried on in the form of a partnership. If so, advice is also requested as to whether the $50,000 loss test provided by section 130 should be applied to the operating results of the partnership or only to the individual partner's distributive share of the partnership loss.

Section 130(a) of the Internal Revenue Code provides as follows:

> If the deductions (other than taxes and interest) allowable to an individual (except for the provisions of this section) and attributable to a trade or business carried on by him for five consecutive taxable years have, in each of such years, exceeded by more than $50,000 the gross income derived from such trade or business, the net income of such individual for each of such years shall be recomputed. For the purpose of such recomputation in the case of any such taxable year, such deductions shall be allowed only to the extent of $50,000 plus the gross income attributable to such trade or business, except that the net operating loss deduction, to the extent attributable to such trade or business shall not be allowed.

Section 181 of the Code provides, as follows:

> SEC. 181. PARTNERSHIP NOT TAXABLE.—Individuals carrying on business in partnership shall be liable for income tax only in their individual capacity.

In view of the foregoing provisions of section 130 of the Code, such section applies only to a trade or business carried on by an individual taxpayer. Where an individual is a member of a partnership, the partnership business is the individual's business to the extent of his proportionate interest in such business. It is believed that this view is consistent with the purpose of section 130 of the Code.

Accordingly, it is held that section 130 is applicable to a trade or business carried on in the form of a partnership by individuals. However, as section 130 is applicable only if an individual's loss from a trade or business carried on by him is in excess of $50,000, it is further held that such section should be applied to a business of an individual operated in partnership form only where the individual partner's distributive share of a partnership loss is in excess of $50,000, exclusive of interest and taxes.

With respect to a trade or business operated by an individual in the form of a bona fide partnership, this ruling, pursuant to the authority of section 3791(b) of the Internal Revenue Code, shall be applied without retroactive effect to any taxable year of an individual in which there are included partnership losses attributable to the partnership's first taxable year ending after this Revenue Ruling is published, except that, if with the application of this ruling the immediate succeeding taxable year or any subsequent taxable year of such individual would be the 5th consecutive taxable year, which would bring into operation the provisions of section 130, then this ruling shall be applicable to all of such 5 consecutive years. For example, assume that both the partner and the partnership report on the basis of a calendar year. In such case, if as of December 31, 1953, the partner's distributive share of the partnership losses exceeds $50,000 for each of 5 consecutive years, the ruling will not apply with respect to such series of years. If, however, as of December 31, 1954, the partner's distributive share of the partnership losses exceeds $50,000 for each of 5 consecutive taxable years, the ruling will be applied with respect to such series of years.

REGULATIONS 111, SECTION 29.130-1: Limitation on deductions allowable to individuals in certain cases. Rev. Rul. 219

INTERNAL REVENUE CODE

The application of section 130 of the Code to certain situations arising in the oil and gas business.

Advice is requested whether, for the purpose of section 130 of the Internal Revenue Code, (1) the income or losses from the sale of an oil or gas property constitute income "derived from" or losses "attributable" to the oil and gas business; (2) income from oil and gas royalties should be included in the gross income of the oil and gas business; and (3) the word "deductions" includes intangible drilling costs and losses due to worthlessness or abandonment of oil or gas properties.

Section 130(a) of the Code provides as follows:

If the deductions (other than taxes and interest) allowable to an individual (except for the provisions of this section) and attributable to a trade or business carried on by him for five consecutive taxable years have, in each of such years, exceeded by more than $50,000 the gross income derived from such trade or business, the net income of such individual for each of such years shall be recomputed. For the purpose of such recomputation in the case of any such taxable year, such deductions shall be allowed only to the extent of $50,000 plus the gross income attributable to such trade or business, except that the net operating loss deduction, to the extent attributable to such trade or business shall not be allowed.

With respect to the first question, it is held that, for the purpose of section 130 of the Code, gains from the sale of oil or gas properties belonging to the business should be included in the gross income derived from the business and losses from such sales should be included in the deductions attributable to the business. If by virtue of section 117(j) of the Code gains from the sale of such properties are treated for tax purposes as gains from the sale of capital assets, then for years to which the Revenue Act of 1951 applies the whole of said gains are includible in gross income for the purposes of section 130, but the deductions attributable to the trade or business for the purpose of sec-

tion 130 include the deduction provided by section 117(b) of the Code that is attributable to such gross income. For prior years only one-half of such gains are includible in gross income. See *United States* v. *Helen W. Benedict et al.*, 338 U. S. 692, Ct. D. 1730, C. B. 1950–1, 70.

With respect to the second question, it is held that income from oil and gas royalties may be included as part of the gross income of the oil and gas business, it being understood that allowable deductions attributable to such royalties should likewise be taken into account in applying section 130.

With respect to the third question, it should be noted that in its use of the word "deductions" the language of section 130 is definite and unqualified. It does not distinguish between different types of deductions. When it has been determined that a deduction, other than taxes and interest, is allowable to an individual and is attributable to a trade or business carried on by him for 5 consecutive taxable years the law is specific in requiring that it be taken into account in determining whether the deductions have exceeded the gross income by more than $50,000.

The deduction for intangible drilling costs is allowable under the provisions of section 23 of the Code and section 29.23(m)–16 of Regulations 111. Deductions for losses due to worthlessness or abandonment of properties used in a trade or business by an individual are allowable under section 23(e) of the Code. Accordingly, it is held that deductions for intangible drilling costs and losses due to worthlessness or abandonment of oil or gas properties are "deductions" within the meaning of section 130.

REGULATIONS 111, SECTION 29.130–1: Limitation on deductions allowable to individuals in certain cases. Rev. Rul. 221

INTERNAL REVENUE CODE

Application of section 130 of the Code to a trade or business carried on in more than one form such as an individual proprietorship and a partnership or two or more partnerships.

Advice is requested whether for the purpose of determining what constitutes a trade or business under section 130 of the Internal Revenue Code all of an individual's income or losses from partnership interests in a particular business, such as the cattle business or the oil business, are to be consolidated and combined with income or losses from the individual's personal operations in the same line of activity.

It is recognized that an individual may be engaged in several trades or businesses. However, the provisions of section 130 of the Code apply to a particular trade or business carried on by an individual. As stated in Rev. Rul. 155, on page 180, this Bulletin, a business carried on in partnership is considered to be the business of the individual partners. It follows that if a business of the individual partner is the cattle business or the oil business, he may be carrying on that business in more than one partnership. He may be the partner of A in one partnership and the partner of B in another but he is carrying on only one business for the purpose of section 130. In addition to being a member of one or more partnerships engaged, for example, in the cattle business he may also be carrying on that business as an individual pro-

prietor. For the purposes of section 130 all of such activities are but one trade or business. Accordingly, it is held that where a particular business of an individual is conducted in one or more forms such as a partnership, joint venture, or individual proprietorship, the individual's share of the profits and losses from each business unit must be aggregated to determine the applicability of section 130 of the Code.

See Rev. Rul. 155, page 180, this Bulletin, as to the nonretroactive effect of section 130 of the Code to an individual's share of profits and losses from a partnership.

SUPPLEMENT C.—CREDITS AGAINST TAX

SECTION 131.—TAXES OF FOREIGN COUNTRIES AND POSSESSIONS OF UNITED STATES

REGULATIONS 111, SECTION 29.131–1: Analysis of credit for taxes.

INTERNAL REVENUE CODE

Okinawa is a foreign country. (See Rev. Rul. 199, p. 225.)

REGULATIONS 111, SECTION 29.131–3: Conditions of allowance of credit.

INTERNAL REVENUE CODE

Regulations 111 amended. (See T. D. 6041, p. 145.)

SUPPLEMENT D.—RETURNS AND PAYMENT OF TAX

SECTION 141.—CONSOLIDATED RETURNS

REGULATIONS 110, SECTION 33.31(c)(6): Consolidated excess-profits credit carryover. (Also Section 33.31(b)(47) of Regulations 110, and Section 24.31(b)(21) of Regulations 129.) Rev. Rul. 222

INTERNAL REVENUE CODE

In applying the limitation contained in section 33.31(c)(6) of Regulations 110, the same principle is to be followed as is followed in computing the limitation imposed by section 33.31(b)(47)(iii) of such regulations. Under the rule of section 33.31(b)(47)(iii) an unused excess-profits credit is adjusted, in the later year to which it may be carried, to the extent that it is beneficially allowable in intervening years. This same rule is equally applicable to section 33.31(c)(6) since the limitation, in each instance, has the same purpose. This purpose is to prevent the offsetting of a member's unused excess-profits credit from a separate return year against that portion of the consolidated excess-profits net income attributable to other members of the group. Thus, where an affiliated group filed a consolidated return for 1944 in which the consolidated excess-profits credit

was computed under the general average method, such group is entitled to carryback and include in its 1944 consolidated unused excess-profits credit adjustment the 1946 unused excess-profits credit of one of its subsidiaries, computed in the subsidiary's separate return under the growth formula, to the extent of the 1944 consolidated excess-profits net income attributable to that subsidiary and not previously offset by any excess-profits credit attributable to that subsidiary.

REGULATIONS 129, SECTION 24.11: Consolidated returns for subsequent years. Rev. Rul. 152

INTERNAL REVENUE CODE

Affiliated corporations which filed consolidated Federal income tax returns for prior years may, notwithstanding the filing of such returns, elect to file separate Federal income tax returns with respect to the first return due to be filed after July 16, 1953, the date of the enactment of Public Law No. 125, Eighty-third Congress, first session, page 473, this Bulletin.

Section 141(a) of the Internal Revenue Code provides in part that the making of a consolidated return shall be upon the condition that all corporations which were members of the affiliated group consent to all the consolidated return regulations prescribed under section 141(b) prior to the last day prescribed by law for the filing of such returns.

Section 24.11(a) of Regulations 129 provides that if a consolidated return is made for any taxable year, a consolidated return must be made for each subsequent taxable year during which the affiliated group remains in existence unless certain conditions are met. One such condition set forth in clause (2) is that, subsequent to the exercise of the election to make consolidated returns, chapter 1 of the Internal Revenue Code to the extent applicable to corporations, or the consolidated return regulations which have been consented to, have been so amended as to make less advantageous to affiliated groups as a class the continued filing of consolidated returns, regardless of the effective date of such amendment.

It is held that chapter 1 of the Internal Revenue Code has been so amended by Public Law No. 125, Eighty-third Congress, first session, page 473, this Bulletin, as to make less advantageous to affiliated groups as a class the continued filing of consolidated returns, within the meaning of section 24.11(a) of Regulations 129. Accordingly, affiliated groups which filed consolidated returns in prior years, may elect to file separate returns with respect to the first return due to be filed after July 16, 1953, the date of the enactment of Public Law No. 125.

Rev. Rul. 17, C. B. 1953–1, 227, is hereby modified to the extent that it is inconsistent with the foregoing.

REGULATIONS 129, SECTION 24.31(a)(90): Consolidated unused excess-profits credit.

INTERNAL REVENUE CODE

Regulations 129 amended. (See T. D. 6046, p. 231.)

REGULATIONS 129, SECTION 24.31(b)(20): Computations under section 448.

INTERNAL REVENUE CODE

Qualification of the Securities and Exchange Commission as an "appropriate regulatory body." (See Rev. Bul. 123, p. 235.)

SECTION 143.—WITHHOLDING OF TAX AT SOURCE

REGULATIONS 111, SECTION 29.143-1: Withholding tax at source. T. D. 6030
(Also Section 144, Section 29.144-1.)

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 7.—TAXATION PURSUANT TO TREATIES.—SUBPART—FINLAND, REGULATIONS EFFECTIVE JANUARY 1, 1953

Release or refund of excess tax withheld, and exemption from, or reduction in rate of, withholding under sections 143 and 144 of Internal Revenue Code in the case of residents of Finland and of Finnish corporations, as affected by the income tax convention between the United States and the Republic of Finland proclaimed by the President of the United States on December 22, 1952.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

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SECTION 7.700. INTRODUCTORY.—The income tax convention between the United States and Finland, signed March 3, 1952, proclaimed by the President of the United States on December 22, 1952, and effective for taxable years beginning on or after January 1, 1952, hereinafter referred to as the convention, provides in part as follows:

ARTICLE I

(1) The taxes referred to in this convention are:
(a) In the case of the United States of America: The Federal income tax, including surtaxes and excess profits taxes.
(b) In the case of Finland: The State (National) income tax.
(2) The present convention shall also apply to any other taxes of a substantially similar character imposed by either contracting State subsequently to the date of signature of the present convention.

ARTICLE II

(1) As used in this convention:

(a) The term "United States" means the United States of America, and when used in a geographical sense includes only the States, the Territories of Alaska and Hawaii, and the District of Columbia.

(b) The term "Finland" means the Republic of Finland.

(c) The term "permanent establishment" means a branch office, factory, warehouse or other fixed place of business, but does not include the casual and temporary use of merely storage facilities, nor does it include an agency unless the agent has and exercises a general authority to negotiate and conclude contracts on behalf of an enterprise or has a stock of merchandise from which he regularly fills orders on its behalf. An enterprise of one of the contracting States shall not be deemed to have a permanent establishment in the other State merely because it carries on business dealings in such other State through a bona fide commission agent, broker or custodian acting in the ordinary course of his business as such. The fact that an enterprise of one of the contracting States maintains in the other State a fixed place of business exclusively for the purchase of goods or merchandise shall not of itself constitute such fixed place of business a permanent establishment of such enterprise. The fact that a corporation of one contracting State has a subsidiary corporation which is a corporation of the other State or which is engaged in trade or business in the other State shall not of itself constitute that subsidiary corporation a permanent establishment of its parent corporation.

(d) The term "enterprise" includes every form of undertaking whether carried on by an individual, partnership, corporation, or any other entity.

(e) The term "enterprise of one of the contracting States" means, as the case may be, "United States enterprise" or "Finnish enterprise".

(f) The term "United States enterprise" means an enterprise carried on in the United States by a resident or partnership of the United States or by a United States corporation or other entity; the term "United States corporation or other entity" means a corporation or other entity created or organized in the United States or under the law of the United States or of any State or Territory of the United States.

(g) The term "Finnish enterprise" means an enterprise carried on in Finland by a resident or partnership of Finland or by a Finnish corporation or other entity; the term "Finnish corporation or other entity" means a corporation or other entity created or organized in Finland or under Finnish law.

(h) The term "competent authorities" means, in the case of the United States the Commissioner of Internal Revenue as authorized by the Secretary of the Treasury; and in the case of Finland, the Taxation Department of the Ministry of Finance.

(2) In the application of the provisions of the present convention by one of the contracting States any term not otherwise defined shall, unless the context otherwise requires, have the meaning which such term has under the tax laws of that State.

* * * * * * *

ARTICLE VI

(1) The rate of United States tax on dividends derived from a United States corporation by a resident or corporation or other entity of Finland, not engaged in trade or business in the United States through a permanent establishment therein, shall not exceed 15 percent: provided that such rate of tax shall not exceed 5 percent if such Finnish corporation controls, directly or indirectly, at least 95 percent of the entire voting power in the corporation paying the dividend, and not more than 25 percent of the gross income of such paying corporation is derived from interest and dividends, other than interest and dividends from its own subsidiary corporation. Such reduction of the rate to 5 percent shall not apply if the relationship of the two corporations has been arranged or is maintained primarily with the intention of securing such reduced rate.

(2) The rate of Finnish tax on dividends derived from a Finnish corporation by a resident or corporation or other entity of the United States, not engaged in trade or business in Finland through a permanent establishment therein, shall

not exceed 15 percent: provided that such rate of tax shall not exceed 5 percent if such United States corporation controls, directly or indirectly, at least 95 percent of the entire voting power in the corporation paying the dividend, and not more than 25 percent of the gross income of such paying corporation is derived from interest and dividends, other than interest and dividends from its own subsidiary corporation. Such reduction of the rate to 5 percent shall not apply if the relationship of the two corporations has been arranged or is maintained primarily with the intention of securing such reduced rate. For the purposes of this paragraph the combined Finnish tax on such dividends and the Finnish property tax on the capital stock of a Finnish corporation owned by such resident or corporation of other entity shall not exceed an amount computed at such rates as applied to dividends, if any, so derived.

ARTICLE VII

(1) Interest on bonds, securities, notes, debentures, or on any other form of indebtedness derived from sources within one of the contracting States by a resident or corporation or other entity of the other contracting State, not having a permanent establishment in the former State, shall be exempt from tax by such former State.

(2) Bonds, bank deposits and trade balances beneficially owned by a resident or corporation or other entity of the United States shall be exempt from the Finnish property tax.

ARTICLE VIII

Royalties for the right to use copyrights or in respect of the right to produce or reproduce any literary, dramatic, musical, or artistic work (but not inclusive of rents or royalties in respect of motion picture films) derived from sources within one of the contracting States by a resident or corporation or other entity of the other contracting State, not engaged in trade or business in the former State through a permanent establishment therein, shall be exempt from tax imposed by such former State.

ARTICLE IX

(1) Income from real property (not including interest derived from mortgages and bonds secured by real property) and royalties in respect of the operation of mines, quarries, or other natural resources, shall be taxable only in the contracting State in which such property, mines, quarries, or other natural resources are situated.

(2) A resident or corporation or other entity of one of the contracting States deriving any such income from sources within the other contracting State may, for any taxable year, elect to be subject to the tax of such other contracting State as if such resident or corporation or other entity were engaged in trade or business within such other contracting State through a permanent establishment therein during such taxable year.

ARTICLE X

* * * * * * *

(2) Private pensions and life annuities derived from within one of the contracting States and paid to individuals residing in the other contracting State shall be exempt from taxation in the former State.

(3) The term "pensions", as used in this Article, means periodic payments made in consideration for services rendered or by way of compensation for injuries received.

(4) The term "life annuities" as used in this Article means a stated sum payable periodically at stated times during life, or during a specified number of years, under an obligation to make the payments in return for adequate and full consideration in money or money's worth.

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ARTICLE XII

(1) Dividends and interest paid by a Finnish corporation shall be exempt from United States tax except where the recipient is a citizen, resident or corporation or other entity of the United States.

(2) Dividends and interest paid by a United States corporation shall be exempt from Finnish tax except where the recipient is a resident or corporation or other entity of Finland.

* * * * * * *

ARTICLE XVII

The competent authorities of the contracting States shall exchange such information (being information available under the respective taxation laws of the contracting States) as is necessary for carrying out the provisions of the present convention or for the prevention of fraud or the administration of statutory provisions against tax avoidance in relation to the taxes which are the subject of the present convention. Any information so exchanged shall be treated as secret and shall not be disclosed to any person other than those concerned with the assessment and collection of the taxes which are the subject of the present convention. No information shall be exchanged which would disclose any trade secret or trade process.

ARTICLE XVIII

Each of the contracting States may collect taxes, which are the subject of this convention, imposed by the other contracting State (as though such tax were a tax imposed by the former State) as will ensure that the exemption or reduced rate of tax granted under the present convention by such other State shall not be enjoyed by persons not entitled to such benefits.

ARTICLE XIX

The State to which application is made for information or assistance shall comply as soon as possible with the request addressed to it except that such State may refuse to comply with the request for reasons of public policy or if compliance would involve violation of a trade, business, industrial, or professional secret or trade process.

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ARTICLE XXI

(1) The provision of this convention shall not be construed to deny or affect in any manner the right of diplomatic and consular officers to other or additional exemptions now enjoyed or which may hereafter be granted to such officers.

(2) The provisions of the present convention shall not be construed to restrict in any manner any exemption, deduction, credit or other allowance accorded by the laws of one of the contracting States in the determination of the tax imposed by such State.

(3) Should any difficulty or doubt arise as to the interpretation or application of the present convention, or its relationship to conventions between one of the contracting States and any other State, the competent authorities of the contracting States may settle the question by mutual agreement.

ARTICLE XXII

(1) The competent authorities of the two contracting States may prescribe regulations necessary to interpret and carry out the provisions of this convention. With respect to the provisions of this convention relating to exchange of information and mutual assistance in the collection of taxes, such authorities may, by common agreement, prescribe rules concerning matters of procedure, forms of application and replies thereto, conversion of currency, disposition of amounts collected, minimum amounts subject to collection and related matters.

(2) The competent authorities of the two contracting States may communicate with each other directly for the purpose of giving effect to the provisions of this convention.

ARTICLE XXIII

(1) The present convention shall be ratified and the instruments of ratification shall be exchanged at Helsinki as soon as possible. It shall have effect for the taxable years beginning on or after the first day of January of the year in which such exchange takes place.

(2) The present convention shall continue effective for a period of five years and indefinitely after that period, but may be terminated by either of the contracting States at the end of the five-year period, or at any time thereafter, provided that at least six months' prior notice of termination has been given and, in such event, the present convention shall cease to be effective for the taxable years beginning on or after the first day of January next following the expiration of the six-month period.

* * * * * * *

As used in this Treasury Decision, any term defined in the convention shall have the meaning so assigned to it; any term not so defined shall, unless the context otherwise requires, have the meaning which such term has under the Internal Revenue Code.

SEC. 7.701. DIVIDENDS.—(*a*) *General.*—The rate of United States tax imposed by the Internal Revenue Code upon dividends derived from a domestic corporation and received in taxable years beginning on or after January 1, 1952, by a nonresident alien (including a nonresident alien individual, fiduciary, and partnership) who is a resident of Finland, or by a Finnish corporation or other entity, shall not exceed 15 percent under the provisions of Article VI of the convention if such alien, corporation, or other entity at no time during the taxable year in which such dividends are derived has engaged in trade or business within the United States through a permanent establishment situated therein. As to what constitutes a permanent establishment, see Article II(1)(c) of the convention.

Thus, if a nonresident alien individual who is a resident of Finland performs personal services within the United States during the taxable year, but has at no time during such year a permanent establishment within the United States, he is entitled to the reduced rate of tax with respect to dividends derived in that year from a domestic corporation, as provided in Article VI of the convention, even though under the provisions of section 211(b) of the Internal Revenue Code he has engaged in trade or business within the United States during such year by reason of his having performed personal services therein.

(*b*) *Dividends paid by related corporation.*—Under the proviso of Article VI(1) of the convention, dividends derived from a domestic corporation by a Finnish corporation which controls, directly or indirectly, at the time the dividend is paid 95 percent or more of the entire voting power in the corporation paying the dividend are, when received in taxable years beginning on or after January 1, 1952, subject to United States tax at a rate not in excess of 5 percent if (1) not more than 25 percent of the gross income of the paying corporation for the 3-year period immediately preceding the taxable year in which the dividend is paid consists of dividends and interest (other than dividends and interest received by such paying corporation from its own subsidiary corporations, if any), (2) the relationship between the paying corporation and the Finnish corporation has not been arranged or maintained primarily with the intention of securing the reduced rate of 5 percent, and (3) the Finnish corporation at no time during the taxable year in which such dividends are derived has engaged in trade or business within the United States through a permanent establishment situated therein.

Any domestic corporation which claims or contemplates claiming that dividends paid or to be paid by it are subject to a rate not in excess of 5 percent shall file the following information with the Com-

missioner of Internal Revenue as soon as practicable: (1) the date and place of its organization; (2) the number of outstanding shares of stock of the domestic corporation having voting power and the voting power thereof; (3) the person or persons beneficially owning such stock of the domestic corporation and their relationship to the Finnish corporation; (4) the amount of the gross income by years of the domestic corporation for the 3-year period immediately preceding the taxable year in which the dividend is paid; (5) the amount of interest and dividends by years included in the gross income of the domestic corporation, and the amount of interest and dividends by years received by such corporation from its own subsidiary corporations, if any; and (6) the relationship between the domestic corporation and the Finnish corporation deriving the dividend.

As soon as practicable after such information is filed, the Commissioner will determine whether the dividends concerned fall within the scope of the proviso of Article VI(1) of the convention and may authorize the release or refund of excess tax withheld with respect to dividends which come within such proviso. For additional requirements respecting the refund of excess tax withheld during 1952, see section 7.710.

In any case in which the Commissioner has notified the domestic corporation that the dividends fall within the scope of the proviso of Article VI(1) of the convention, the reduced withholding rate of 5 percent, to the extent withholding of United States tax is required, shall apply to any dividends subsequently paid by such corporation and derived by the Finnish corporation, unless the stock ownership of the domestic corporation, or the character of its income, materially changes; or unless the Commissioner determines that the relationship between the two corporations concerned is being maintained primarily with the intention of securing the reduced rate of tax. In such instance, if such change in stock ownership or character of income occurs, the domestic corporation shall promptly notify the Commissioner of the then existing facts with respect thereto. The continued application of the rate not in excess of 5 percent is also dependent upon the continued fulfillment of condition (3) of the first paragraph of (*b*) of this section.

(*c*) *Effect of address in Finland on withholding in the case of dividends.*—For the purpose of withholding of United States tax in the case of dividends every nonresident alien (including a nonresident alien individual, fiduciary, and partnership) whose address is in Finland shall be deemed by United States withholding agents to be a nonresident alien who is a resident of Finland not engaged in trade or business within the United States through a permanent establishment situated therein; and every foreign corporation whose address is in Finland shall be deemed by such withholding agents to be a Finnish corporation not engaged in trade or business within the United States through a permanent establishment situated therein.

(*d*) *Rate of withholding.*—Withholding at source in the case of dividends derived from a domestic corporation and paid on or after January 1, 1953, to nonresident aliens (including a nonresident alien individual, fiduciary, and partnership) and to foreign corporations, whose addresses are in Finland, shall be at the rate of 15 percent in every case except that in which, prior to the date of payment of such

dividends, the Commissioner of Internal Revenue has (1) pursuant to (*b*) of this section notified the domestic corporation that such dividends fall within the scope of the proviso of Article VI(1) of the convention or (2) notified the withholding agent that the reduced rate of withholding shall not apply.

The preceding provisions respecting the application of the reduced withholding rate in the case of dividends paid to nonresident aliens and foreign corporations with addresses in Finland are based upon the assumption that the payee of the dividend is the actual owner of the capital stock from which the dividend is derived and consequently is the person liable to United States tax upon such dividend. As to action by the recipient who is not the owner of the dividend, see section 7.707.

The rate at which United States tax has been withheld from any dividend paid at any time after the expiration of the 30th day after the date on which this Treasury Decision is published in the Federal Register to any person whose address is in Finland at the time the dividend is paid shall be shown either in writing or by appropriate stamp on the check, draft, or other evidence of payment, or on an accompanying statement.

In the case of dividends paid on or after January 1, 1952, by a Finnish corporation no withholding of United States tax is required. See Article XII(1) of the convention.

SEC. 7.702. INTEREST.—(*a*) *General.*—Interest on bonds, securities, notes, debentures, or on any other form of indebtedness, including interest on obligations of the United States, obligations of instrumentalities of the United States, and mortgages and bonds secured by real property, which is derived from sources within the United States and received in taxable years beginning on or after January 1, 1952, by a nonresident alien (including a nonresident alien individual, fiduciary, and partnership) who is a resident of Finland, or by a Finnish corporation or other entity, is exempt from United States tax under the provisions of Article VII of the convention if such alien, corporation, or other entity at no time during the taxable year in which such interest is derived has a permanent establishment in the United States. Such interest is, therefore, not subject to the withholding of United States tax at source. As to what constitutes a permanent establishment, see Article II(1)(c) of the convention.

(*b*) *Application of exemption from withholding.*—To avoid withholding of United States tax at source in the case of coupon bond interest the nonresident alien who is a resident of Finland, or the Finnish corporation or other entity, shall for each issue of bonds file Form 1001–FIN in duplicate when presenting the interest coupons for payment. This form shall be signed by the owner of the interest, trustee, or agent and shall show the name and address of the obligor, the name and address of the owner of the interest, and the amount of the interest. It shall contain a statement that the owner (1) is a resident of Finland, or is a Finnish corporation or other entity, and (2) has no permanent establishment in the United States.

The exemption from United States tax contemplated by Article VII of the convention, insofar as it concerns coupon bond interest, is applicable only to the owner of the interest. The person presenting the coupon or on whose behalf it is presented shall, for the purpose

of the exemption from tax, be deemed to be the owner of the interest only if he is, at the time the coupon is presented for payment, the owner of the bond from which the coupon has been detached. If the person presenting the coupon or on whose behalf it is presented is not the owner of the bond, Form 1001, and not Form 1001–FIN, shall be executed.

The original and duplicate of Form 1001–FIN shall be forwarded by the withholding agent to the Commissioner of Internal Revenue, Uniform Audit Branch, Alien Returns Section, Washington 25, D. C., with the quarterly return on Form 1012, as provided in section 29.143–7 of this chapter with respect to Form 1001. Form 1001–FIN need not be listed on Form 1012.

For general provisions pertaining to the use, without reference to the provisions of the convention, of ownership certificate, Form 1001, by nonresident aliens and nonresident foreign corporation, see section 29.143–4 and section 29.143–6 of this chapter [26 CFR 29.143–4 and 29.143–6].

To avoid withholding of United States tax at source in the case of interest, other than coupon bond interest, the nonresident alien who is a resident of Finland, or the Finnish corporation or other entity, shall notify the withholding agent by letter in duplicate that such income is exempt from United States tax under the provisions of Article VII of the convention. The letter of notification shall be signed by the owner of the interest, trustee, or agent and shall show the name and address of the obligor and the name and address of the owner of the interest. It shall contain a statement (1) that the owner is neither a citizen nor a resident of the United States but is a resident of Finland, or, in the case of a corporation or other entity, (2) that the owner is a Finnish corporation or other entity; and, in addition, a statement that the owner has at no time during the current taxable year had a permanent establishment in the United States.

This letter of notification, which shall constitute authorization for the payment of such interest without withholding of United States tax at source, shall be filed with the withholding agent for each successive 3-calendar-year period during which such income is paid. For this purpose, the first such period shall commence with the beginning of the calendar year in which such income is first paid on or after January 1, 1953. Each such letter filed with any withholding agent shall be filed not later than 20 days preceding the date of the first payment within each successive period, or, if that is not possible because of special circumstances, as soon as possible after such first payment.

If such letter is also to be used as authorization for the release, pursuant to section 7.706(*a*), of excess tax withheld from interest, other than coupon bond interest, it shall also contain a statement that, at the time when the interest was derived from which the excess tax was withheld, (1) the owner was neither a citizen nor a resident of the United States but was a resident of Finland, or, in the case of a corporation or other entity, (2) the owner was a Finnish corporation or other entity; and, in addition, a statement that the owner at no time during the taxable year in which such interest was derived had a permanent establishment in the United States.

Once a letter has been filed in respect of any 3-calendar-year period, no additional letter need be filed in respect thereto unless the Commissioner of Internal Revenue notifies the withholding agent that an additional letter shall be filed by the taxpayer. If, after filing a letter of notification, the taxpayer ceases to be eligible for the exemption from United States tax provided by the convention in respect to such interest, he shall promptly notify the withholding agent by letter in duplicate. When any change occurs in the ownership of the interest as recorded on the books of the payer, the exemption from withholding of United States tax shall no longer apply unless a letter of notification is duly executed and filed with the withholding agent by the new owner of record of such interest.

Each letter of notification, or the duplicate thereof, shall be immediately forwarded by the withholding agent to the Commissioner of Internal Revenue, Uniform Audit Branch, Alien Returns Section, Washington 25, D. C.

In the case of interest paid on or after January 1, 1952, by a Finnish corporation no withholding of United States tax is required. See Article XII(1) of the convention.

SEC. 7.703. COPYRIGHT ROYALTIES.—(*a*) *General.*—Royalties for the right to use copyrights or in respect of the right to produce or reproduce any literary, dramatic, musical, or artistic work which are derived from sources within the United States and received in taxable years beginning on or after January 1, 1952, by a nonresident alien (including a nonresident alien individual, fiduciary, and partnership) who is a resident of Finland, or by a Finnish corporation or other entity, are exempt from United States tax under the provisions of Article VIII of the convention if such alien, corporation, or other entity at no time during the taxable year in which such royalties are derived has engaged in trade or business within the United States through a permanent establishment situated therein. Such royalties are, therefore, not subject to the withholding of United States tax at source. As to what constitutes a permanent establishment, see Article II(1)(c) of the convention.

The provisions of this section shall have no application to rents or royalties in respect of motion picture films.

(*b*) *Application of exemption from withholding.*—To avoid withholding of United States tax at source in the case of the royalties to which (*a*) of this section is applicable, the nonresident alien who is a resident of Finland, or the Finnish corporation or other entity, shall notify the withholding agent by letter in duplicate that such royalties are exempt from United States tax under the provisions of Article VIII of the convention. The provisions of section 7.702(*b*) relating to the execution, filing, and effective period of the letter of notification prescribed therein with respect to interest, including its use for the release of excess tax withheld, are equally applicable with respect to the income falling within the scope of this section.

Each letter of notification, or the duplicate thereof, shall be immediately forwarded by the withholding agent to the Commissioner of Internal Revenue, Uniform Audit Branch, Alien Returns Section, Washington 25, D. C.

SEC. 7.704. NATURAL RESOURCE ROYALTIES AND REAL PROPERTY RENTALS.—The convention does not change the rate of United States

tax imposed pursuant to sections 211 and 231 of the Internal Revenue Code upon natural resource royalties and real property rentals. The withholding of United States tax with respect to such items derived from sources within the United States by nonresident aliens who are residents of Finland, or by Finnish corporations or other entities, is not changed by the convention. See sections 143(b) and 144 of the Internal Revenue Code and Article IX of the convention.

SEC. 7.705. PENSIONS AND LIFE ANNUITIES.—(*a*) *General.*—Private pensions and life annuities, as defined in Article X (3) and (4) of the convention, derived from sources within the United States and paid in taxable years beginning on or after January 1, 1952, to a nonresident alien individual who is a resident of Finland are exempt from United States tax under the provisions of Article X(2) of the convention. Such items of income are, therefore, not subject to the withholding of United States tax at source.

(*b*) *Application of exemption from withholding.*—To avoid withholding of United States tax at source in the case of the items of income to which (*a*) of this section is applicable, the nonresident alien individual who is a resident of Finland shall notify the withholding agent by letter in duplicate that such income is exempt from United States tax under the provisions of Article X of the convention. The letter of notification shall be signed by the owner of the income, shall show the name and address of both the payer and the owner of the income, and shall contain a statement that the owner, an individual, is neither a citizen nor a resident of the United States but is a resident of Finland.

If such letter is also to be used as authorization for the release, pursuant to section 7.706(*a*), of excess tax withheld from such items of income, it shall also contain a statement that the owner was, at the time when the income was paid from which the excess tax was withheld, neither a citizen nor a resident of the United States but was a resident of Finland.

This letter shall constitute authorization for the payment of such items of income without withholding of United States tax at source unless the Commissioner of Internal Revenue subsequently notifies the withholding agent that the tax shall be withheld with respect to payments of such items of income made after receipt of such notice. If, after filing a letter of notification, the owner of the income ceases to be eligible for the exemption from United States tax provided by the convention in respect to such income, he shall promptly notify the withholding agent by letter in duplicate. When any change occurs in the ownership of such income as recorded on the books of the payer, the exemption from withholding of United States tax shall no longer apply unless a letter of notification is duly executed and filed with the withholding agent by the new owner of record of such income.

Each letter of notification, or the duplicate thereof, shall be immediately forwarded by the withholding agent to the Commissioner of Internal Revenue, Uniform Audit Branch, Alien Returns Section, Washington 25, D. C.

SEC. 7.706. RELEASE OF EXCESS TAX WITHHELD AT SOURCE.—(*a*) *General.*—In order to give the convention effective application at the earliest practicable date, the exemptions from, and reductions in rate of, withholding of United States tax at source granted by this Treas-

ury Decision are hereby made effective beginning January 1, 1953, contingent upon compliance with the applicable provisions of section 7.701 through section 7.705.

In the case of dividends derived from a domestic corporation and paid to a nonresident alien (including a nonresident alien individual, fiduciary, and partnership) or to a foreign corporation, whose address at the time of payment was in Finland, where United States tax at the statutory rate (30 percent as of the date of approval of this Treasury Decision) has been withheld from such dividends on or after January 1, 1953, there shall be released (except as provided in (*b*) of this section) by the withholding agent and paid over to the person from whom it was withheld an amount which is equal to the amount obtained by substracting 15 percent of such dividends from the tax so withheld.

In the case of every taxpayer whose address at the time of payment was in Finland and who furnishes to the withholding agent the letter of notification prescribed in section 7.702(*b*), section 7.703(*b*), and section 7.705(*b*) as authorization for the release of excess tax withheld, where United States tax at the statutory rate (30 percent as of the date of approval of this Treasury Decision) has been withheld on or after January 1, 1953, from interest (other than coupon bond interest), copyright royalties and the like, and from private pensions and life annuities as defined in Article X, there shall be released by the withholding agent and paid over to the person from whom it was withheld an amount equal to the tax so withheld from such items.

In the case of every taxpayer whose address at the time of payment was in Finland and who furnishes to the withholding agent Form 1001–FIN clearly marked "SUBSTITUTE" and executed in accordance with section 7.702(*b*), where United States tax at the statutory rate (28 percent or 30 percent, as the case may be, as of the date of approval of this Treasury Decision) has been withheld from coupon bond interest on or after January 1, 1953, there shall be released by the withholding agent and paid over to the person from whom it was withheld an amount equal to the tax so withheld from such interest. One such substitute form shall be filed in duplicate with respect to each issue of bonds and will serve with respect to that issue to replace all Forms 1001 previously filed by the taxpayer in the calendar year in which the excess tax was withheld and with respect to which such excess is released.

The original and duplicate of substitute Form 1001–FIN shall be forwarded by the withholding agent to the Commissioner of Internal Revenue, Uniform Audit Branch, Alien Returns Section, Washington 25, D. C., with the quarterly return on Form 1012, as provided in section 29.143–7 of this Chapter with respect to Form 1001. Substitute Form 1001–FIN need not be listed on Form 1012.

The provisions of this section shall have no application to excess tax withheld at source which has been paid by the withholding agent to the district director of internal revenue pursuant to section 29.143–7 of this chapter.

(*b*) *Dividends paid by related corporation.*—In the case of every domestic corporation receiving notification from the Commissioner of Internal Revenue under the provisions of section 7.701(*b*) that dividends paid or to be paid by it fall within the scope of the proviso of

Article VI(1) of the convention, where United States tax in excess of the applicable rate of 5 percent has been withheld on or after January 1, 1953, from dividends which come within the scope of such proviso, the withholding agent shall, if so authorized in such notification, release and pay over to the corporation from which it was withheld the excess tax withheld with respect to such dividends.

(*c*) *Amounts withheld during 1952.*—For provisions respecting the refund of excess tax withheld during the calendar year 1952, see section 7.710.

SEC. 7.707. ADDRESSEE NOT ACTUAL OWNER.—(*a*) *General.*—If the recipient in Finland of any dividend from a United States corporation, with respect to which United States tax at the reduced rate of 15 percent has been withheld at source pursuant to section 7.701(*d*), is a nominee or representative through whom such dividend flows to a person other than one described in section 7.701(*a*) as being entitled to such reduced rate, such recipient in Finland shall withhold an additional amount of United States tax equivalent to the United States tax which would have been withheld if the convention had not been in effect (30 percent of such dividend as of the date of approval of this Treasury Decision minus the 15 percent which has been withheld at the source.

In any case in which a fiduciary or partnership with an address in Finland receives, otherwise than as a nominee or representative, a dividend from a United States corporation with respect to which United States tax at the reduced rate of 15 percent has been withheld at source pursuant to section 7.701(*d*), if a beneficiary of such fiduciary or a partner in such partnership is not entitled to the reduced rate of tax granted by Article VI(1) of the convention, the fiduciary or partnership shall withhold an additional amount of United States tax with respect to the portion of such dividend included in such beneficiary's share of the distributed or distributable income, or in such partner's distributive share of the income, of such fiduciary or partnership, as the case may be. The amount of the additional tax is to be calculated in the same manner as under the immediately preceding paragraph.

If any amount of United States tax is released pursuant to section 7.706(*a*) by the withholding agent in the United States with respect to a dividend paid to such a person (nominee, representative, fiduciary, or partnership) with an address in Finland, the latter shall also withhold from such released amount any additional amount of United States tax, otherwise required to be withheld by the preceding provisions of this section in respect of such dividend, in the same manner as if at the time of payment of such dividend United States tax at the rate of only 15 percent had been withheld at source therefrom.

(*b*) *Returns filed by Finnish withholding agents.*—The amounts so withheld pursuant to (*a*) of this section by such withholding agents in Finland shall be deposited, without converting such amounts into United States dollars, with the Finnish Taxation Department of the Ministry of Finance on or before the 15th day after the close of the quarter of the calendar year in which such withholding in Finland occurs. Each withholding agent making such deposit shall render therewith the appropriate Finnish form as prescribed by the Taxation Department of the Ministry of Finance. That Department has arranged that the amounts so deposited will be remitted by draft in

United States dollars to the District Director of Internal Revenue, Baltimore, Maryland, U. S. A., on or before the end of the calendar month in which the deposits are made, such draft to be accompanied by the Finnish form rendered by the withholding agents in Finland in connection with such deposits.

SEC. 7.708. INFORMATION TO BE FURNISHED IN ORDINARY COURSE.—In compliance with the provisions of Article XVII of the convention the Commissioner of Internal Revenue will transmit to the Finnish Taxation Department of the Ministry of Finance, as soon as practicable after the close of the calendar year 1953 and of each subsequent calendar year during which the convention is in effect, the following information relating to such preceding calendar year:

(*a*) The name and address of each person, whose address as disclosed on each available Form 1012 and Form 1042 is in Finland, deriving from sources within the United States dividends, interest, rent, royalties, salaries, wages, pensions, annuities, and other fixed or determinable annual or periodical income; and the amount of such income as disclosed on such form with respect to each such person; and

(*b*) The duplicate copy of each available ownership certificate, Form 1001–FIN, filed pursuant to section 7.702(*b*), and substitute Form 1001–FIN, filed pursuant to section 7.706(*a*), in connection with coupon bond interest.

To facilitate compliance with Article XVII of the convention, every United States withholding agent shall report on Form 1042 for the calendar year 1953 and each subsequent calendar year, in addition to the items of income required to be listed on such form pursuant to section 29.143–7 of this chapter, all other items of fixed or determinable annual or periodical income derived from sources within the United States and paid to nonresident aliens (including nonresident alien individuals, fiduciaries, and partnerships) and to nonresident foreign corporations, whose addresses at the time of payment were in Finland, including such items of income upon which, in accordance with this Treasury Decision, no withholding of United States tax is required; except that any item of interest in respect of which Form 1001–FIN or substitute Form 1001–FIN has been filed in duplicate with the withholding agent is not required to be reported on such form.

SEC. 7.709. BENEFICIARIES OF A DOMESTIC ESTATE OR TRUST.—A nonresident alien who is a resident of Finland and who is a beneficiary of a domestic estate or trust shall be entitled to the exemption from, or reduction in the rate of, United States tax granted by Articles VI, VII, VIII, and XII of the convention with respect to dividends, interest, and copyright royalties and the like, to the extent such item or items are included in his share of the distributed or distributable income of such estate or trust. In order to be entitled in such instance to the exemption from, or reduction in the rate of, withholding of United States tax such beneficiary must otherwise satisfy the requirements of these respective articles of the convention and shall, where applicable, execute and submit to the fiduciary of such estate or trust in the United States the appropriate letter of notification prescribed in section 7.702(*b*) and section 7.703(*b*).

SEC. 7.710. REFUND OF EXCESS TAX WITHHELD DURING 1952.—If United States tax withheld at the source during the year 1952 from dividends, interest, copyright royalties and the like, pensions, or life annuities is in excess of the tax imposed by chapter 1 (relating to the income tax) of the Internal Revenue Code, as modified by the convention, a claim by the taxpayer for the refund of any overpayment shall be made under section 322 of the Internal Revenue Code by filing Form 843 together with Form 1040NB, Form 1040NB-a, Form 1040B, Form 1120, or Form 1120NB, whichever is applicable, or with an amended return.

The taxpayer's total gross income from sources within the United States, including every item of capital gain subject to tax under the provisions of section 211(a)(1)(B) or 211(c) of the Internal Revenue Code, shall be disclosed on the return. In the event that securities are held in the name of a person other than the actual or beneficial owner, the name and address of such person shall be furnished with the claim. There shall also be included in such claim for refund:

(*a*) A statement that, at the time when the item or items of income were derived (or "paid," in the case of private pensions and life annuities) from which the excess tax was withheld, (1) the taxpayer was neither a citizen nor a resident of the United States but was a resident of Finland, or, in the case of a corporation or other entity, (2) the taxpayer was a Finnish corporation or other entity; and

(*b*) A statement that the taxpayer at no time during the taxable year in which the income was derived was engaged in trade or business within the United States through a permanent establishment situated therein.

If, however, the taxpayer is an individual who during the taxable year derived from sources within the United States income which consists exclusively of pensions or life annuities entitled to the benefit of Article X of the convention, the statement specified in (*b*) above shall not be required.

As to additional information required in the case of a Finnish corporation claiming the benefit of the 5 percent rate on dividends paid by a domestic corporation, see section 7.701(*b*).

Because it is necessary to bring into effect at the earliest practicable date the rules of this Treasury Decision respecting release or refund of excess tax withheld, and exemption from, or reduction in rate of, withholding of tax, it is hereby found that it is impracticable to issue this Treasury Decision with notice and public procedure thereon under section 4(a) of the Administrative Procedure Act, approved June 11, 1946, or subject to the effective date limitation of section 4(c) of that Act.

(This Treasury Decision is issued under the authority contained in secs. 62 and 3791 (53 Stat. 32, 467; 26 U. S. C. 62, 3791) of the Internal Revenue Code and in Article XXII of the convention.)

T. COLEMAN ANDREWS,
Commissioner of Internal Revenue.

Approved July 10, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register July 15, 1953, 8:52 a. m.)

SECTION 144.—PAYMENT OF CORPORATION INCOME TAX AT SOURCE

REGULATIONS 111, SECTION 29.144-1: Withholding in the case of nonresident foreign corporations.

INTERNAL REVENUE CODE

Release or refund of excess tax withheld, and exemption from, withholding in case of Finnish corporations, as affected by the reciprocal income tax convention between the United States and Finland. (See T. D. 6030, p. 185.)

SECTION 147.—INFORMATION AT SOURCE

REGULATIONS 111, SECTION 29.147-2: Return of information as to payments to employees. Rev. Rul. 134

INTERNAL REVENUE CODE

The report which an airline captain is required to file at the conclusion of each flight identifying the members of his crew, the plane, the trip, and indicating the number of hours the crew was away from their base station, by which the airline computes the amount of the expense reimbursement of the pilot at the hourly and per diem rates provided for under a union agreement relative to the compensation and other employment conditions of pilots in the employ of the airline does not constitute an accounting of ordinary and necessary expense incurred in the business of the employer within the meaning of Mimeograph 5947, C. B. 1945, 235, and such reimbursements not subject to withholding, are required to be reported by the employer on Form 1099.

Advice is requested whether the time report which an airline captain is required to file with his employer for the purpose of computing the pilot's reimbursement expenses constitutes an accounting of ordinary and necessary expense incurred in the business of the employer within the meaning of Mimeograph 5947, C. B. 1945, 235.

Section 29.147-2 of Regulations 111, provides that if an employee receiving an allowance as an advance or reimbursement of expenses is paid an aggregate (in wages plus allowances) of $600 or more in a calendar year, his allowances not subject to withholding must be reported by the employer on Form 1099, in addition to the usual reporting of wages subject to withholding on Form W-2.

Mimeograph 5947, *supra*, dated November 19, 1945 was issued for the purpose of clarifying the provisions of section 29.147-2 of Regulations 111, as amended by Treasury Decision 5480, C. B. 1945, 234, with respect to the reporting on Form 1099 of advances or reimbursed expenses. It relieves an employer of reporting on Form 1099 "advances or reimbursements for expenses" with respect to which detailed expense accounts are submitted to the employer by the employee showing that the expenses are ordinary and necessary expenses incurred in the business of the employer.

In accordance with the terms of a union agreement pilots of an airline company receive certain hourly allowances for absences for operations away from the base and for attendance at the company's

training school. In addition pilots in international operations receive per diem allowances to cover miscellaneous expenses. A paragraph of the agreement specifically provides that the stated amounts are intended to reimburse pilots for only reasonable actual expenses. The amounts are determined exactly upon the number of hours or fractions thereof of the absences from base.

The report prepared by the captain at the conclusion of a trip indicates the number of hours away from base and serves as a basis for computation by the company of reimbursements at the hourly and per diem rates. However, such report does not show that the expenses were actually incurred by the employees in the business of the employer.

Accordingly, the report which an airline captain is required to file at the conclusion of each flight identifying the members of his crew, the plane, the trip, and indicating the number of hours the crew was away from their base station, by which the airline computes the amount of the expense reimbursement of the pilot at the hourly and per diem rates provided for under a union agreement relative to the compensation and other employment conditions of pilots in the employ of the airline does not constitute an accounting of ordinary and necessary expense incurred in the business of the employer within the meaning of Mimeograph 5947, C. B. 1945, 235, and such reimbursements not subject to withholding, are required to be reported by the employer on Form 1099.

REGULATIONS 111, SECTION 29.147-2: Return of information as to payments to employees.

INTERNAL REVENUE CODE

Premium paid on "Employees' Annuities" by an employer exempt from Federal income tax under section 101(6) of the Internal Revenue Code. (See Rev. Rul. 181, p. 111.)

REGULATIONS 111, SECTION 29.147-2: Return of information as to payments to employees.

INTERNAL REVENUE CODE

Transportation allowances paid to employees working on a temporary construction project located at a distance from their regular place of employment. (See Rev. Rul. 190, p. 303.)

REGULATIONS 111, SECTION 29.147-3: Cases where no return of information required.

INTERNAL REVENUE CODE

Regulations 111 amended. (See T. D. 6039, p. 162.)

SECTION 148.—INFORMATION BY CORPORATIONS

REGULATIONS 111, SECTION 29.148-1: Return of information as to payments of dividends. T. D. 6042

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 29.—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1941

Regulations 111 amended with respect to the requirements for filing information returns reporting dividends paid by savings and loan associations and similar organizations for calendar years after 1952.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

Section 29.148-1 of Regulations 111 [26 CFR, pt. 29], as amended by Treasury Decision 5914 [C. B. 1952-2, 169], approved June 24, 1952, is further amended as follows:

(A) By striking out the last sentence of (*b*) which reads as follows: "In the case of a building and loan association, a cooperative bank, a homestead association, a credit union, a savings and loan association, or a corporation described in section 101 (10), (11), (12), or (13), making a payment of a dividend or a distribution to any shareholder, the information returned on Forms 1096 and 1099 shall be rendered only in the case of payments amounting to $100 or more during the calendar year."

(B) By inserting in lieu of such last sentence the following:

In the case of a corporation described in section 101 (10), (11), (12), or (13), making a payment of a dividend or a distribution to any shareholder, the information return on Forms 1096 and 1099 shall be rendered only in the case of payments amounting to $100 or more during the calendar year. In the case of a savings and loan association, a cooperative bank, a homestead association, a credit union, or a building and loan association an information return is required to be filed with respect to dividends or distributions to a shareholder only if an information return would have been required under the provisions of section 29.147-1 had the dividends or distributions been payments of interest, except that, for years prior to 1953, such an organization is required to file an information return where the payments to a shareholder amount to $100 or more during the calendar year.

Because the purpose of this Treasury Decision is to reduce the burden of filing information returns with respect to payments made by certain organizations for calendar years after 1952, it is found that it is unnecessary to issue this Treasury Decision with notice and public precedure thereon under section 4(a) of the Administrative Procedure Act, approved June 11, 1946, or subject to the effective date limitation of section 4(c) of said act.

(This Treasury Decision is issued under the authority contained in secs. 62, 148, and 3791 of the Internal Revenue Code (53 Stat. 32, 65, 467; 26 U. S. C. 62, 148, 3791).)

T. COLEMAN ANDREWS,
Commissioner of Internal Revenue.

Approved September 16, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register September 18, 1953, 8:49 a. m.)

SECTION 165.—EMPLOYEES' TRUSTS

REGULATIONS 111, SECTION 29.165–1: Employees' trusts. (Also Section 22(b), Sections 29.22(b)(2)–2, 29.22(b)(2)–5; Section 23(p), Section 29.23(p)–9.)

Rev. Rul. 185

INTERNAL REVENUE CODE

A pension plan which otherwise meets the requirements of section 165(a) of the Internal Revenue Code (or section 23(p)(1)(B) of the Code if a nontrusteed plan is involved) and which provides benefits that vary with the increase or decrease in the market value of the assets from which such benefits are payable, or which vary with the fluctuations of a specified and generally recognized cost-of-living index, will be recognized as a plan providing for "definitely determinable" benefits within the meaning of section 29.165–1(*a*) of Regulations 111. Similar benefits received under an annuity contract purchased for an employee by an employer exempt under section 101(6) of the Code will be recognized as "annuity" payments within the meaning of section 22(b)(2)(B) of the Code. Also, amounts received which vary in the manner specified and which otherwise meet the requirements of section 22(b)(2)(A) or section 22(b)(2)(C) of the Code will be considered amounts received as an annuity within the meaning of those sections.

Sol. Op. 160, C. B. III–2, 60 (1924), modified.

Advice is requested whether (1) a pension plan, in all other respects meeting the requirements of section 165(a) of the Internal Revenue Code (or the requirements of section 23(p)(1)(B) thereof if a trust is not involved), will fail of qualification under the applicable Code section or (2) the payments under an annuity contract purchased for an employee by an employer exempt under section 101(6) of the Code will fail to be recognized as an "annuity" within the meaning of section 22(b)(2)(B) of the Code, solely on the ground that the benefits provided by such plan or contract will vary in dollar amount from time to time to the extent of (*a*) the increase or decrease, percentage-wise, in the market value of the assets from which such benefits are to be paid or (*b*) the variation in a specified and generally recognized cost-of-living index or correction factor by which each benefit under the plan or contract, after determination of the amount thereof in accordance with all other provisions of the plan or contract, shall be increased or decreased in amount before it is paid.

Section 29.165–1(*a*) of Regulations 111 provides, in part, that, to be entitled to exemption under section 165(a) of the Code, a trust "must be formed and availed of solely to aid in the proper execution of a [stock bonus, pension, or profit-sharing] plan which is a definite written program and arrangement communicated to the employees." A pension plan is defined therein as one "established and maintained by an employer primarily to provide systematically for the payment of *definitely determinable* benefits to his employees over a period of years, usually for life, after retirement." (Italics supplied.) Benefits under a pension plan are "definitely determinable" only if funds

arising from forfeitures are used to reduce the amount of contributions by the employer and the amounts payable from time to time can be determined actuarially (in advance or at the time of payment).

A pension plan recognized as otherwise meeting the requirements of section 165(a) of the Code (including the requirements of section 23(p)(1)(B) of the Code, if a nontrusteed plan is involved) but which provides

(1) benefits payable, *not* on the basis of a fixed number of dollars per month for the life of the annuitant, as provided by the more or less standard form of money purchase, fixed benefit or unit benefit type of plan, but on the basis of a definitely determinable number of "shares" or "units" of interest in the total assets from which the benefit is to be paid, with the dollar amount of the benefit payable varying from time to time to the extent of any variation in the market value (as of the date of the benefit payment, or as of a specified date preceding the date of payment by *not more* than 1 year) of such total assets, or

(2) benefits definitely determinable as to amount, in accordance with methods generally acceptable in the standard forms or types of pension plans, but subject to increase or decrease in amount at the time of payment to the extent, if any, but only to such extent, of the fluctuation up or down of a specified and generally recognized cost-of-living index,

will be recognized as a plan providing for "definitely determinable" benefits within the meaning of section 29.165–1(*a*) of Regulations 111. Similar benefits under an "annuity contract * * * purchased for an employee by an employer exempt under section 101(6)" of the Code will be recognized as "annuity" payments within the meaning of section 22(b)(2)(B) of the Code. Also, amounts received which vary in the manner specified and which otherwise meet the requirements of section 22(b)(2)(A) or section 22(b)(2)(C) of the Code will be considered "amounts received under an annuity contract" within the meaning of those sections. Sol. Op. 160, C. B. III–2, 60 (1924), modified by G. C. M. 26595, C. B. 1950–2, 16, is hereby further modified to the extent that it is inconsistent with the foregoing.

REGULATIONS 111, SECTION 29.165–6: Taxability of beneficiary under a trust which meets the requirements of section 165(a). (Also Section 29.165–1; Section 22(b), Section 29.22(b)(2)–5; Section 23(p), Section 29.23(p)–1.) T. D. 6033

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 29.—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1941

Regulations 111 amended to conform to section 335 of the Revenue Act of 1951 and Public Law 589 (82d Cong.) [C. B. 1952–2, 364] relating to taxation of beneficiaries of certain trusts exempt under section 165(a) of the Internal Revenue Code, and to section 343 of the Revenue Act of 1951, relating to treatment of full-time life insurance salesmen as employees for certain purposes.

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TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

On November 11, 1952, notice of proposed rulemaking regarding amendments to conform Regulations 111 [26 CFR, pt. 29] to section 335 of the Revenue Act of 1951 and Public Law 589 (82d Cong.) [C. B. 1952-2, 364], approved July 17, 1952, relating to taxation of beneficiaries of certain trusts exempt under section 165(a) of the Internal Revenue Code, and to section 343 of the Revenue Act of 1951, relating to treatment of full-time life insurance salesmen as employees for certain purposes, was published in the Federal Register (17 F. R. 10262). After consideration of all relevant matter presented by interested persons regarding the rules proposed, the amendments to Regulations 111 set forth below are hereby adopted.

PARAGRAPH 1. Section 29.22(b)(2)-5, as amended by Treasury Decision 6020 [p. 106, this Bulletin], approved June 17, 1953, is further amended by adding at the end thereof the following:

As to inclusion of full-time life insurance salesmen within the class of persons considered to be employees, see section 3797(a)(20), as added by section 343 of the Revenue Act of 1951, set forth immediately preceding section 29.3797-1.

PAR. 2. Section 29.23(p)-1, as amended by Treasury Decision 5666 [C. B. 1948-2, 34], approved November 2, 1948, is further amended by adding immediately after the second sentence thereof the following new sentence:

(As to inclusion of full-time life insurance salesmen within the class of persons considered to be employees, see section 3797(a)(20), as added by section 343 of the Revenue Act of 1951, set forth immediately preceding section 29.3797-1.)

PAR. 3. There is inserted immediately preceding section 29.165-1 the following:

SEC. 335. EMPLOYEES' TRUSTS [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

(a) AMENDMENT OF SECTION 165(b).—Section 165(b) (relating to taxability of beneficiary on distributions from an employees' trust) is hereby amended by adding at the end thereof the following new sentence: "Where such total distributions include securities of the employer corporation, there shall be excluded from such excess the net unrealized appreciation attributable to that part of the total distributions which consists of the securities of the employer corporation so distributed. The amount of such net unrealized appreciation and the resulting adjustments to basis of the securities of the employer corporation so distributed shall be determined in accordance with regulations which shall be prescribed by the Secretary. For purposes of this subsection, the term 'securities' means only shares of stock and bonds or debentures issued by a corporation with interest coupons or in registered form, and the term 'securities of the employer corporation' includes securities of a parent or subsidiary corporation (as defined in section 130A(d) (2) and (3)) of the employer corporation."

(b) EFFECTIVE DATE.—The amendment made by this section shall be applicable with respect to distributions made after December 31, 1950.

PUBLIC LAW 589 (82d CONG., 2d SESS.), APPROVED JULY 17, 1952

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 165(b) of the Internal Revenue Code (relating to employee stock purchase

plans) is hereby amended by adding at the end thereof the following: "In no event shall the amount actually distributed or made available to any distributee include net unrealized appreciation in securities of the employer corporation attributable to the amount contributed by the employee. Such net unrealized appreciation and the resulting adjustments to basis of such securities shall also be determined in accordance with regulations which shall be prescribed by the Secretary."

SEC. 2. The amendment made by this Act shall be applicable with respect to taxable years beginning after December 31, 1951.

PAR. 4. Section 29.165-1, as amended by Treasury Decision 5422 [C. B. 1944, 318], approved December 13, 1944, is further amended by adding after the second sentence thereof the following new sentence:

As to inclusion of full-time life insurance salesmen within the class of persons considered to be employees, see section 3797(a)(20), as added by section 343 of the Revenue Act of 1951, set forth immediately preceding section 29.3797-1.

PAR. 5. Section 29.165-6, as amended by Treasury Decision 6020, is further amended as follows:

(A) By changing the heading to read: "TAXABILITY OF BENEFICIARY UNDER A TRUST WHICH MEETS THE REQUIREMENTS OF SECTION 165 (a).—(*a*). *In general.*"

(B) By inserting immediately after the second sentence thereof the following new sentence:

(For rules providing for exclusion from income in the year of distribution of amounts representing unrealized appreciation in the value of securities of the employer corporation, see (*b*) of this section.)

(C) By inserting immediately preceding the last sentence of the next to the last paragraph of such section the following:

See, however, (*b*) of this section for rules relating to exclusion from such excess of amounts representing net unrealized appreciation in the value of securities of the employer corporation distributed after December 31, 1950.

(D) By adding at the end of such section the following:

(*b*) *Distributions including securities of the employer corporation.*—(1) *In general.*—If a trust exempt under section 165(a) makes a distribution to a distributee, and such distribution includes securities of the employer corporation, there shall be excluded for purposes of computing the amount of such distribution includible in the distributee's income in the year of distribution net unrealized appreciation in such securities to the following extent:

(i) If the distribution is made after December 31, 1950, and constitutes a total distribution to which the rules of the next to the last paragraph of (*a*) of this section are applicable, the amount to be excluded is the entire net unrealized appreciation attributable to that part of the total distribution which consists of securities of the employer corporation; and

(ii) If the distribution is made in a taxable year of the distributee beginning after December 31, 1951, and is other than a total distribution to which the next to the last paragraph of (*a*) of this section is applicable, the amount to be excluded is that portion of the net unrealized appreciation in the securities of the employer corporation which is attributable to the amount considered to be contributed by the employee to the purchase of such securities.

The amount of net unrealized appreciation which is excludable under the rules of (i) and (ii) shall not be included in the basis of the securities in the hands of the distributee at the time of distribution for purposes of determining gain or loss on subsequent disposition. In the case of a total distribution the amount of net unrealized appreciation which is not included in the basis of the securities in the hands of the distributee at the time of distribution shall be considered to the extent realized in a subsequent taxable transaction as a gain from the sale or exchange of a capital asset held for more than 6 months. However, if the net gain realized by the distributee exceeds the amount of the net unrealized

appreciation, such excess shall constitute a long-term or short-term capital gain depending upon the holding period of the securities in the hands of the distributee.

For purposes of section 165(b) and of this section, the term "securities" means only shares of stock and bonds or debentures issued by a corporation with interest coupons or in registered form, and the term "securities of the employer corporation" includes securities of a parent or subsidiary corporation (as defined in section 130A(d) (2) and (3), relating to employee stock options) of the employer corporation.

(2) *Determination of net unrealized appreciation.*—The amount of net unrealized appreciation in securities of the employer corporation which are distributed by the trust is to be determined by reference to the cost or other basis to the trust of such securities and by reference to the market value of such securities at the time of distribution. Thus, if a distribution consists in part of securities which have appreciated in value and in part of securities which have depreciated in value, the net unrealized appreciation shall be considered to consist of the net increase in value of all of the securities included in the distribution. For this purpose, two or more distributions made by a trust to a distributee in a single taxable year of the distributee shall be treated as a single distribution.

The determination of the cost or other basis to the trust of a distributed security of the employer corporation, for purposes of determining net unrealized appreciation thereon, shall be made in accordance with whichever of the following rules is applicable:

(i) If a security was, at the time of purchase by, or contribution to, the trust, earmarked for the account of a particular employee so that the cost or other basis of such security to the trust is reflected in the account of such employee, such cost or other basis shall be used.

(ii) If as of the close of each taxable year of the trust (or other specified period of time not in excess of 12 consecutive calendar months) the trust allocates among the accounts of participating employees all securities acquired by the trust during the period (exclusive of securities unallocated under a plan providing for allocation in whole shares only), the cost or other basis to the trust of any securities allocated as of the close of a particular allocation period shall be the average cost or other basis to the trust of all securities of the same type which were purchased or otherwise acquired by the trust during such allocation period. (For purposes of determining the average cost to the trust of securities included in a subsequent allocation, the actual cost to the trust of the securities unallocated as of the close of a prior allocation period shall be deemed to be the average cost or other basis to the trust of securities of the same type allocated as of the close of such prior allocation period.)

(iii) In a case where neither (i) nor (ii) is applicable, if the trust fund, or a specified portion thereof, is invested exclusively in one particular type of security of the employer corporation, and if during the period the distributee participated in the plan none of such securities has been sold except for the purpose of paying benefits under the trust or for the purpose of enabling the trustee to obtain funds with which to exercise rights which have accrued to the trust, the cost or other basis to the trust of all securities distributed to such distributee shall be the total amount credited to the account of such distributee (or such portion thereof as was available for investment in such securities) reduced by the amount available for investment but uninvested on the date of distribution. (If at the time of distribution to a particular distributee a portion of the amount credited to his account is forfeited, appropriate adjustment shall be made with respect thereto in determining the cost or other basis to the trust of the securities distributed.)

(iv) In all other cases, there shall be used the average cost or other basis to the trust of all securities of the employer corporation of the type distributed to the distributee which the trust has on hand at the time of the distribution, or which the trust had on hand on a specified inventory date which date does not precede the date of distribution by more than 12 calendar months. If a distribution includes securities of the employer corporation of more than one type, the average cost or other basis to the trust of each type of security distributed shall be determined. The average cost to the trust of securities of the employer corporation on hand on a specified inventory date (or on hand at the time of distribution) shall be computed on the

basis of their actual cost, considering the securities most recently purchased to be those on hand, or by means of a moving average calculated by subtracting from the total cost of securities on hand immediately preceding a particular sale or distribution an amount computed by multiplying the number of securities sold or distributed by the average cost of all securities on hand preceding such sale or distribution. These methods of computing average cost may be illustrated by the following examples:

Example (1). A, a distributee who makes his income tax returns on the basis of a calendar year, receives on August 1, 1952, in a total distribution, to which the next to the last paragraph of (*a*) of this section is applicable, 10 shares of class D stock of the employer corporation. On July 1, 1952 (the specified inventory date of the trust) the trust had on hand 80 shares of class D stock. The average cost of the 10 shares distributed, on the basis of the actual cost method, is $100 computed as follows:

Shares	Purchase date	Cost per share	Total cost
20	June 4, 1952	$101	$2,020
40	Jan. 10, 1951	102	4,080
20	Oct. 20, 1950	95	1,900
80			$8,000

Example (2). B, a distributee who makes his income tax returns on the basis of a calendar year, receives on October 30, 1952, in a total distribution, to which the next to the last paragraph of (*a*) of this section is applicable, 20 shares of class E stock of the employer corporation. The specified inventory date of the trust is the last day of each calendar year. The trust had on hand on December 31, 1950, 1,000 shares of class E stock of the employer corporation. During the calendar year 1951 the trust distributed to four distributees a total of 100 shares of such stock and acquired, through a number of purchases, a total of 120 shares. The average cost of the 20 shares distributed to B, on the basis of the moving average method, is $52 computed as follows:

	Shares	Total cost	Average cost
On hand December 31, 1950	1,000	$50,000	$50
Distributed during 1951 at average cost of $50	100	5,000	
	900	45,000	
Purchased during 1951	120	8,040	
On hand December 31, 1951	1,020	53,040	52

(3) *Unrealized appreciation attributable to employee contributions.*—In any case in which it is necessary to determine the amount of net unrealized appreciation in securities of the employer corporation which is attributable to contributions made by an employee:

(i) The cost or other basis of the securities to the trust and the amount of net unrealized appreciation shall first be determined in accordance with the rules in (*b*) (2) of this section;

(ii) The amount contributed by the employee to the purchase of the securities shall be solely the portion of his actual contributions to the trust properly allocable to such securities, and shall not include any part of the increment in the trust fund expended in the purchase of the securities;

(iii) The amount of net unrealized appreciation in the securities distributed which is attributable to the contributions of the employee shall be that proportion of the net unrealized appreciation determined under the rules of (*b*) (2) of this section which the contributions of the employee properly allocable to such securities bear to the cost or other basis to the trust of the securities;

(iv) If a distribution consists solely of securities of the employer corporation, the contributions of the employee expended in the purchase of such

securities shall be allocated to the securities distributed in a manner consistent with the principles set forth in (*b*)(2) (i), (ii), (iii), or (iv) of this section, whichever is applicable, that is, the amount of the employee's contribution which can be identified as having been expended in the purchase of a particular security shall be allocated to such security, and the amount of such contribution which cannot be so identified shall be allocated ratably among the securities distributed. If a distribution consists in part of securities of the employer corporation and in part of cash or other property, appropriate allocation of a portion of the employee's contribution to such cash or other property shall be made unless such allocation is inconsistent with the terms of the plan or trust.

Example. A trust distributes 10 shares of stock issued by the employer corporation each of which has an average cost to the trust of $100, consisting of employee contributions in the amount of $60 and employer contributions in the amount of $40, and on the date of distribution has a fair market value of $180. The portion of the net unrealized appreciation attributable to the contributions of the employee with respect to each of the shares of stock is $18 computed as follows:

(1) Value of one share of stock on distribution date		$180
(2) Employee contributions	$60	
(3) Employer contributions	40	
(4) Total contributions		100
(5) Net unrealized appreciation		80
(6) Portion of net unrealized appreciation attributable to employee contributions, 60/100 (amount of employee contributions (item 2) over total contributions (item 4)) of $80 (item 5)		48

For the purpose of determining gain or loss to the distributee in the year or years in which any share of stock referred to in the preceding example is sold or otherwise disposed of in a taxable transaction, the basis of each such share in the hands of the distributee at the time of the distribution by the trust will be $132 computed as follows:

(*a*) Employee contributions	$60
(*b*) Employer contributions (taxable as ordinary income in the year the securities were distributed)	40
(*c*) Portion of net unrealized appreciation attributable to employer contributions (item (5) minus item (6)) (taxable as ordinary income in the year the securities were distributed)	32
(*d*) Basis of stock	132

(4) *Change in exempt status of trust.*—For principles applicable in making appropriate adjustments if the trust was not exempt for 1 or more years prior to the year of distribution, see (*a*) of this section.

PAR. 6. There is inserted immediately preceding section 29.3797-1 the following:

SEC. 343. DEFINITION OF EMPLOYEE [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

(a) AMENDMENT OF SECTION 3797(a).—Section 3797(a) is amended by adding at the end thereof the following new paragraph:

"(20) EMPLOYEE.—For the purpose of applying the provisions of chapter 1 with respect to contributions to or under a stock bonus, pension, profit-sharing, or annuity plan, and with respect to distributions under such a plan or by a trust forming part of such plan, the term 'employee' shall include a full-time life insurance salesman who is considered an employee for the purpose of subchapter A of chapter 9, or, in the case of services performed before January 1, 1951, who would be considered an employee if his services were performed during 1951."

(b) EFFECTIVE DATE.—The amendment made by this section shall be applicable with respect to taxable years beginning after December 31, 1938.

The amendments made to Regulations 111 by paragraphs 1, 2, 4, and 6 are hereby made applicable to taxable years beginning after December 31, 1938, and before January 1, 1942, such years being covered by Regulations 103 [26 CFR, pt. 19].

(This Treasury Decision is issued under the authority contained in secs. 62 and 3791 of the Internal Revenue Code (53 Stat. 32, 467; 26 U. S. C. 62, 3791) and under the authority contained in sec. 165(b) of the Internal Revenue Code, as amended by sec. 335 of the Revenue Act of 1951 and by Public Law 589, 82d Cong. (65 Stat. 507, 66 Stat. 766; 26 U. S. C. 165(b)).)

JUSTIN F. WINKLE,
Acting Commissioner of Internal Revenue.

Approved July 27, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register July 30, 1953, 8:51 a. m.)

REGULATIONS 111, SECTION 29.165-6: Taxability of beneficiary under a trust which meets the requirements of section 165(a).

INTERNAL REVENUE CODE

Regulations 111 amended. (See T. D. 6020, p. 106.)

SUPPLEMENT F.—PARTNERSHIPS

SECTION 181.—PARTNERSHIP NOT TAXABLE

REGULATIONS 111, SECTION 29.181-1: Partnerships.

INTERNAL REVENUE CODE

Regulations 111 amended. (See T. D. 6037, p. 213.)

SECTION 182.—TAX OF PARTNERS

REGULATIONS 111, SECTION 29.182-1: Distributive share of partners. (Also Section 24, Section 29.24-6.) Rev. Rul. 121

INTERNAL REVENUE CODE

Where community property is invested by the husband in a partnership, the wife, who under the laws of the State of Washington has a vested interest in the community property equal to that of her husband, is not precluded by section 24(b) of the Internal Revenue Code from deducting in her separate Federal income tax return one-half of her husband's share of a partnership loss resulting from the sale of certain depreciable assets by the partnership to a corporation in which the husband owned directly or indirectly more than 50 percent of the stock.

Advice is requested whether, under the circumstances stated herein, the taxpayer, whose husband is a member of a partnership in the State of Washington, a community property State, is entitled to deduct in her separate Federal income tax return one-half of her husband's share of a partnership loss resulting from the sale of depreciable assets by the partnership to a corporation in which the husband owned directly or indirectly more than 50 percent of the stock.

In the instant case the husband of the taxpayer was a member of a partnership in the State of Washington. His capital investment in the partnership was made with community funds. The partnership incurred a loss with respect to certain depreciable assets it sold to a corporation in which the taxpayer's husband, together with his mother, sister, and three brothers, owned directly or indirectly 73.55 percent of the stock. The taxpayer's husband was precluded, under section 24(b)(1)(B) of the Internal Revenue Code from deducting his share of the partnership loss in his separate return for the year in which the sale was made. The taxpayer seeks to deduct in her separate return one-half of her husband's share of the partnership loss inasmuch as she does not own, directly or indirectly, 50 percent of the stock of the corporation.

In the State of Washington a wife has a vested interest in the community property equal to that of her husband. The husband, the manager of the community property, is also the agent of the community. (See *Burns Poe* v. *H. G. Seaborn*, 282 U. S. 101, Ct. D. 259, C. B. IX-2, 202 (1930); in re: *Coffey's Estate*, 195 Wash. 379, 81 Pac. (2d), 283.) All property acquired after marriage in the State of Washington is presumed to be community property. (In re: *Brown's Estate*, 124 Wash. 273, 214 Pac. 10; *Seaton* v. *Smith et ux.*, 186 Wash. 447, 58 Pac. (2d), 830.) The fact that community property is also part of property operated by a partnership does not affect the wife's vested community interest in such property. (*Milton A. Black* v. *Commissioner*, 114 Fed. (2d) 355.)

Section 181 of the Internal Revenue Code provides that individuals carrying on business in partnership shall be liable for income tax only in their indivdual capacity. Each partner, in computing his net income, is required by section 182 of the Code to report his distributive share of the gain or loss of the partnership, whether distributed to him or not.

Section 29.182-1 of Regulations 111, relating to the distributive share of partners, provides in part as follows:

> (b) If separate returns are made by the husband and wife domiciled in a community property State, and the husband only is a member of a partnership, the part of his distributive share of gains and losses of the partnership from sales or exchanges of capital assets or the part of his distributive share of ordinary net income or ordinary net loss, which is, or is derived from, community property should be reported by the husband and by the wife in equal proportions * * *.

From the foregoing it appears that, in cases involving community income, the tax is imposed on the individual partner only to the extent of his ownership of the income. The community property contributed to the partnership by the taxpayer's husband continued to be community property and the taxpayer had a vested interest therein. In selling the property from which the loss in the instant case arises,

the husband, in taking part in such sale, acted in a dual capacity, that is, as agent of the community with respect to the community interest and as a partner with respect to the partnership interest. Therefore, upon sale of the property at a loss it follows that there was also a loss by the community. Although the taxpayer was not a partner in the partnership, she must share the profits and losses of the partnership equally with her husband because of the community relationship. Such profits and losses would not come to her from or through her husband, but are derived directly from the community.

In *Arizona Publishing Company* v. *Commissioner*, 9 T. C. 85, a similar problem was involved. In that case a corporation sustained a loss on the sale of certain real property to one of its stockholders. Such stockholder owned 27 percent of the corporation's outstanding stock as community property with his wife. However, for the purpose of section 24(b)(1)(B) of the Code, he owned directly or indirectly an additional 27 percent of the corporate stock held as community property by his sister and brother-in-law. The court held that since the sale of the real property was to a community estate, the portion of the loss attributable to the property sold to the stockholder was not deductible under section 24(b) of the Code. The portion of the loss attributable to the other one-half of the property was held deductible because that half of the property was considered as having been sold to the stockholder's wife and her actual and constructive ownership of the corporate stock represented only the stock directly owned by her and the stock directly owned by her husband which was less than 50 percent of the total outstanding stock of the corporation. It is believed that the principle of the Arizona Publishing Company case, *supra*, should be followed in the instant case in applying section 24(b) of the Code, that is, that the taxpayer's one-half vested community interest in the property invested in the partnership by her husband should be recognized. The result would be the same whether the community investment is in a corporation or in a partnership.

There is no doubt that the taxpayer's husband suffered a loss (although the loss was not allowable to him under sec. 24(b) of the Code) as a result of the partnership transaction for it is well settled that items of partnership income and deduction in the absence of an express provision to the contrary come down without loss of identity to the individual partner. (See *Harry H. Neuberger* v. *Commissioner*, 311 U. S. 83, Ct. D. 1470, C. B. 1940-2, 228; and *Helvering* v. *Estate of John M. Enright*, 312 U. S. 636, Ct. D. 1500, C. B. 1941-1, 353.) Inasmuch as the taxpayer owned a community interest in the property contributed to the partnership which entitled her to part of the profits it would appear that she would also share in the losses.

In view of the foregoing, it is held that where community property is invested by a husband in a partnership the wife, who under the laws of the State of Washington has a vested interest in community property equal to that of her husband, is entitled to the deduction in her separate Federal income tax return of one-half of her husband's share of a partnership loss resulting from the sale of certain depreciable assets by the partnership to a corporation in which her husband owned directly or indirectly more than 50 percent of the stock.

REGULATIONS 111, SECTION 29.182-1: Distributive share of partners.

INTERNAL REVENUE CODE

Limitation on deduction for loss from trade or business carried on by a partnership. (See Rev. Rul. 155, p. 180.)

SECTION 187.—PARTNERSHIP RETURNS

REGULATIONS 111, SECTION 29.187-1: Partnership returns. Rev. Rul. 144

(Also Section 113(a), Sections 29.113(a)(5)-1, 29.113(a)(13)-1.)

INTERNAL REVENUE CODE

A change in the membership of a partnership resulting from the death, withdrawal, substitution, or addition of a partner, or a shift of interests among existing partners does not, in itself, effect a termination of a partnership for Federal income tax purposes. Ordinarily, a partnership will be treated as continuing where the business of the partnership, or a substantial portion thereof, is continued. The returns of a continuing partnership should continue to be filed on the basis of the annual accounting period previously established by the partnership. A partnership's basis in its assets is distinct from the partners' bases in their partnership interests, and is not affected by changes in such partnership interests. The bases of the interests of the partners in the partnership may be increased by the amount paid for a retiring partner's interest, and in the event of the death of a partner the basis of his partnership interest to his estate is the fair market value of such interest at the date of his death.

O. D. 228, C. B. 1, 190 (1919), revoked.

Advice is requested respecting the effect on a partnership, for Federal income tax purposes, of the death, withdrawal, substitution or addition of a partner.

As defined in section 3797(a)(2) of the Internal Revenue Code, the term "partnership" for tax purposes is broader than the term under common law, the Uniform Partnership Act, or individual State laws. Accordingly, the Federal tax consequences of transactions involving partnerships and interests in partnerships will be determined upon the basis of their substance and in accordance with the Federal tax laws without regard to the technical refinements of State laws. (See *Commissioner* v. *Francis E. Tower*, 327 U. S. 280; Ct. D. 1670, C. B. 1946-1, 11, and *Heiner* v. *Mellon*, 304 U. S. 271; Ct. D. 1345, C. B. 1938-1, 349.)

Sections 187 and 188 of the Code, which refers to the "taxable year" of the partnership, recognize a partnership as a unit for the purpose of filing returns. These sections do not contemplate that a partnership may terminate its taxable year and thus change its accounting period by the mere act of admitting or retiring a partner, nor that the Commissioner may force a change of accounting period under such circumstances.

In *Mary D. Walsh et al.* v. *Commissioner*, 7 T. C. 205, the Tax Court held that the death of a partner did not terminate the taxable year of the partnership insofar as the surviving partners were con-

cerned. In *Robert E. Ford et al.* v. *Commissioner*, 6 T. C. 499, and *Estate of Lowenstein, First National Bank of Mobile, Exr.* v. *Commissioner*, 12 T. C. 694, affirmed *First National Bank of Mobile* v. *Commissioner*, 183 Fed. (2d) 172, certiorari denied, 340 U. S. 911, the courts, in holding that a partnership's basis in its assets was not affected by changes in the firm's membership, recognized that a partnership may continue beyond changes in its membership. See also *Heiner* v. *Mellon*, *supra*, and *Ransohoff's, Inc.* v. *Commissioner*, 9 T. C. 376.

G. C. M. 26379, C. B. 1950-1, 58, holds that a sale of a partnership interest under certain circumstances is treated as a sale of a capital asset, distinct from the partner's interest in the partnership assets, and thereby recognizes that for tax purposes a partnership may continue beyond changes in membership.

Accordingly, it is held that a change in the membership of a partnership resulting from the death, withdrawal, substitution, or addition of a partner, or a shift of interests among existing partners does not, in itself, effect a termination of a partnership for Federal income tax purposes. Ordinarily, a partnership will be treated as continuing where the business of the partnership, or a substantial portion thereof, is continued. The returns of a continuing partnership should continue to be filed on the basis of the annual accounting period previously established by the partnership. A partnership's basis in its assets is distinct from the partners' bases in their partnership interests, and is not affected by changes in such partnership interests. The bases of the interests of the partners in the partnership interests are increased by the amount paid for a retiring partner's interest, and in the event of the death of a partner the basis of his partnership interest to his estate is the fair market value of such interest at the date of his death.

In view of the foregoing, O. D. 228, C. B. 1, 190 (1919) is hereby revoked.

It is not intended herein to state that a partnership is invariably to be treated as a unit intervening between a partner and partnership transactions and income for Federal tax purposes. See *Commissioner* v. *Whitney*, 169 F. (2d) 562; Ct. D. 1719, C. B. 1949-1, 70; *Neuberger* v. *Commissioner*, 311 U. S. 83; Ct. D. 1470, C. B. 1940-2, 228.

SECTION 191.—FAMILY PARTNERSHIPS

REGULATIONS 111, SECTION 29.191-1: Family partnerships. T. D. 6037

(Also Section 29.191-2; Section 113(a), Section 29.113(a)(13)-1; Section 181, Section 29.181-1; Section 3797, Section 29.3797-4.)

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 29.—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1941

Regulations 111 amended to conform to section 340 of the Revenue Act of 1951.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

On December 20, 1952, notice of proposed rulemaking with respect to section 340 of the Revenue Act of 1951, approved October 20, 1951, was published in the Federal Register (17 F. R. 11663). After consideration of all such relevant matter as was presented by interested persons regarding the rules proposed, the amendments to Regulations 111 [26 CFR, pt. 29] set forth below are hereby adopted.

PARAGRAPH 1. Section 29.113(a)(13)–1 [26 CFR 29.113(a)(13)–1] and section 29.181–1 [26 CFR 29.181–1] are each amended by adding at the end thereof the following:

For rules as to allocation of partnership income in the case of family partnerships, see section 191 and the regulations thereunder.

PAR. 2. There is inserted immediately after section 29.190–1, as amended by Treasury Decision 5851 [C. B. 1951–2, 63], approved August 10, 1951 [26 CFR 29.190–1], the following:

SEC. 340. FAMILY PARTNERSHIPS [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

(a) DEFINITION OF PARTNER.—Section 3797(a)(2) is hereby amended by adding at the end thereof the following: "A person shall be recognized as a partner for income tax purposes if he owns a capital interest in a partnership in which capital is a material income-producing factor, whether or not such interest was derived by purchase or gift from any other person."

(b) ALLOCATION OF PARTNERSHIP INCOME.—Supplement F of chapter 1 is hereby amended by adding at the end thereof the following new section:

"SEC. 191. FAMILY PARTNERSHIPS.

"In the case of any partnership interest created by gift, the distributive share of the donee under the partnership agreement shall be includible in his gross income, except to the extent that such share is determined without allowance of reasonable compensation for services rendered to the partnership by the donor, and except to the extent that the portion of such share attributable to donated capital is proportionately greater than the share of the donor attributable to the donor's capital. The distributive share of a partner in the earnings of the partnership shall not be diminished because of absence due to military service. For the purpose of this section, an interest purchased by one member of a family from another shall be considered to be created by gift from the seller, and the fair market value of the purchased interest shall be considered to be donated capital. The 'family' of any individual shall include only his spouse, ancestors, and lineal descendants, and any trust for the primary benefit of such persons."

(c) EFFECTIVE DATE.—The amendments made by this section shall be applicable with respect to taxable years beginning after December 31, 1950. The determination as to whether a person shall be recognized as a partner for income tax purposes for any taxable year beginning before January 1, 1951, shall be made as if this section had not been enacted and without inferences drawn from the fact that this section is not expressly made applicable with respect to taxable years beginning before January 1, 1951. In applying this subsection where the taxable year of any family partner is different from the taxable year of the partnership—

(1) if a taxable year of the partnership beginning in 1950 ends within or with, as to all of the family partners, taxable years which

begin in 1951, then the amendments made by this section shall be applicable with respect to all distributive shares of income derived by the family partners from such taxable year of the parnership beginning in 1950, and

(2) if a taxable year of the partnership ending in 1951 ends within or with a taxable year of any family partner which began in 1950, then the amendments made by this section shall not be applicable with respect to any of the distributive shares of income derived by the family partners from such taxable year of the partnership.

SEC. 29.191-1. FAMILY PARTNERSHIPS.—(*a*) *In general.*—(1) *Introduction.*—The production of income by a partnership is attributable to the capital or services, or both, contributed by the partners. The provisions of supplement F, which govern the taxation of the income of individuals carrying on business in partnership, are to be read in the light of their relationship to section 22(a), which requires that income be taxed to the person who earns it through his own labor and skill and the utilization of his own capital.

(2) *Recognition of donee as partner.*—With respect to partnerships in which capital is a material income-producing factor, section 340(a) of the Revenue Act of 1951 amends section 3797(a)(2) (dealing with definition of partnership and partner) to provide that a person shall be recognized as a partner for income tax purposes for taxable years beginning after December 31, 1950, if he owns a capital interest in such a partnership whether or not such interest is derived by purchase or gift from any other person. In the case of any partnership in which capital is a material income-producing factor, if any capital interest in such partnership is created by gift, section 191, as added by section 340(b) of the Revenue Act of 1951, provides for allocation of the partnership income where the distributive share of a donee partner under the partnership agreement is determined without allowance of reasonable compensation for services rendered to the partnership by the donor or is proportionately greater than the share of the donor attributable to the donor's capital. For rules of allocation, see section 29.191-2.

(3) *Requirement of complete transfer to donee.*—A donee or purchaser of a capital interest in a partnership is not recognized as a partner under the principles of section 3797(a)(2) unless the capital interest is acquired in a bona fide transaction, not a mere sham for tax avoidance purposes or otherwise, and the donee or purchaser is the real owner of such interest. To be recognized, a transfer must vest dominion and control of the partnership interest in the transferee. The existence of such dominion and control in the donee is to be determined from all the pertinent facts and circumstances. A transfer is not recognized if the transferor retains such incidents of ownership that the transferee has not acquired full and complete ownership of the partnership interest. Transactions between members of a family will be closely scrutinized, and in the case of such transactions the circumstances at the time of a purported transfer and during the periods preceding and following it will be taken into consideration in determining the bona fides or lack of bona fides of the purported gift or sale. A partnership may be recognized for income tax purposes as to some alleged partners but not as to others.

(4) *Capital as a material income-producing factor.*—The determination as to whether capital is a material income-producing factor, for purposes of section 3797(a)(2), must be made by reference to all the relevant facts of the individual case. Capital is a material income-producing factor if a substantial portion of the gross income of the business is attributable to the employment of capital in the business conducted by the partnership. In general, capital is not a material income-producing factor where the income of the business consists principally of fees, commissions or other compensation for personal services performed by members or employees of the partnership. On the other hand, capital is ordinarily a material income-producing factor if the operation of the business requires substantial inventories or a substantial investment in plant, machinery, or equipment.

(5) *Capital interest in a partnership.*—For purposes of sections 191 and 3797(a)(2), a capital interest in a partnership means an interest in the capital of the partnership, including accretions thereto, which interest is distributable to the owner of the capital interest upon his withdrawal from the partnership or upon dissolution or liquidation of the partnership. The mere right to participate in the earnings and profits of a partnership is not a capital interest in the partnership.

(6) *Taxable years affected.*—Section 340 of the Revenue Act of 1951, which added section 191 and amended section 3797(a)(2), is effective for taxable years beginning after December 31, 1950, and expressly provides that no inferences as to family partnerships with respect to taxable years beginning prior to January 1, 1951, are to be drawn from the enactment of such section. If the taxable year of any family partner is different from that of the partnership, the amendments made by section 340 will apply to all distributive shares of income derived by family partners from a fiscal year of the partnership beginning in 1950 if it ends with or within taxable years of all the family partners which began in 1951, but will not apply in the case of a fiscal year of the partnership ending in 1951 which ends with or within a taxable year of any family partner which began in 1950.

(*b*) *Basic tests as to ownership.*—(1) *In general.*—Whether an alleged partner in a gift capital case is the real owner of the capital interest attributed to him and whether the donee has dominion and control over his or her interest, must be ascertained from all the facts and circumstances of the particular case. Isolated facts should not be considered determinative; the reality of the donee's ownership is to be determined in the light of the transaction as a whole. The execution of legally sufficient and irrevocable deeds or other instruments of gift under State law is a factor to be taken into account but is not determinative of ownership in the donee. The reality of the transfer and of the donee's ownership of the property attributed to him are to be ascertained from the conduct of the parties with respect to the alleged gift and not by any mechanical or formulistic test. Some of the more important factors to be considered in determining whether the donee has acquired ownership of the capital interest in a partnership are indicated below.

(2) *Retained controls.*—The donor may have retained such controls of the interest which he has purported to transfer to the donee that the donor should be treated as remaining the substantial owner of the interest. Controls of particular significance include, for example, the following:

(i) Retention of control of the distribution of income or restrictions on the distribution of income other than amounts retained in the partnership annually with the consent of the partners (including the donee partner) for the reasonable needs of the business. If there is a partnership agreement providing for a managing partner, or partners, then, amounts of income may be retained in the partnership without the acquiescence of all the partners if such amounts are retained for the reasonable needs of the business.

(ii) Limitation of the right of the donee to withdraw or sell his interest in the partnership at his discretion without financial detriment.

(iii) Retention of control of assets essential to the business (for example, through retention of assets leased to the alleged partnership).

(iv) Retention of management powers inconsistent with normal relationships among partners. Retention by the donor of control of business management or of voting control, such as is common in ordinary business relationships, is not by itself to be considered as inconsistent with normal relationships among partners provided the donee is free to withdraw his interest without financial detriment at his discretion. The donee shall not be considered free to withdraw his interest unless, considering all the facts, it is evident that the donee is independent of the donor and has such maturity and understanding of his rights as to be capable of deciding to exercise, and of exercising, his right to withdraw his capital interest from the partnership.

The existence of some of the indicated controls, though amounting to less than substantial ownership retained by the donor, may be considered along with other facts and circumstances as tending to show the lack of reality of the partnership interest of the donee.

(3) *Indirect controls.*—Controls inconsistent with ownership by the donee may be exercised indirectly as well as directly, for example, through a separate business organization, estate, trust, individual, or other partnership. Where such indirect controls exist, the reality of the donee's interest will be determined as if such controls were exercisable directly.

(4) *Participation in management.*—Substantial participation by the donee in the control and management of the business (including participation in the major policy decisions affecting the business) is strong evidence of a donee partner's exercise of the dominion and control over his interest. Such participation

presupposes sufficient maturity and experience on the part of the donee to deal with the business problems of the partnership.

(5) *Income distributions.*—The actual distribution to a donee partner of all or the major portion of his distributive share of the business income for the sole benefit and use of the donee is substantial evidence of the reality of the donee's interest provided the donor has not retained controls inconsistent with real ownership in the donee. Amounts distributed are not considered to be used for the donee's sole benefit if, for example, they are deposited, loaned, or invested in such ways that the donor controls or can control the use or enjoyment of such funds.

(6) *Conduct of partnership business.*—In determining the reality of the donee's ownership of a capital interest in a partnership, consideration shall be given to whether the donee is actually treated as a partner in the operation of the business. It is of principal importance for this purpose whether the donee has been held out publicly as a partner in the conduct of the business, in relations with customers or with creditors or other sources of financing. Other factors of significance in this connection include:

(i) Compliance with local partnership, fictitious name, and business registration statutes.

(ii) Control of business bank accounts.

(iii) Recognition of the donee's interest in appropriate capital and drawing accounts.

(iv) Recognition of the donee's interest in insurance policies, leases, and other business contracts and in litigation affecting business.

(v) The existence of written agreements, records or memoranda, contemporaneous with the taxable year or years concerned, establishing the nature of the partnership agreement and the rights and liabilities of the respective partners.

(vi) Filing of partnership tax returns as required by law.

However, despite formal compliance with the above factors, other circumstances may indicate that the donor has retained substantial ownership of the interest purportedly transferred to the donee.

(7) *Trustees as partners.*—A trustee may be recognized as a partner for income tax purposes under the principles relative to family partnerships generally as applied to the particular facts of the trust-partnership arrangement. A trustee who is unrelated to and independent of the grantor, and who participates as a partner and receives distribution of the income distributable to the trust, will ordinarily be recognized as the owner of the partnership interest which he holds for the trust unless the grantor has retained controls inconsistent with such ownership. However, if the grantor is the trustee, or if the trustee is amenable to the will of the grantor, the provisions of the trust instrument (particularly with relation to whether the trustee is subject to the responsibilities of a fiduciary), the provisions of the partnership agreement, and the conduct of the parties must all be taken into account in determining whether the trustee in a fiduciary capacity has become the real owner of the partnership interest. In a case where the grantor (or person amenable to his will) is the trustee, the trust may be recognized as a partner only if the grantor (or such other person) in his participation in the affairs of the partnership actively represents and protects the interests of the beneficiaries in accordance with the obligations of a fiduciary, and does not subordinate such interests to the interests of the grantor. Furthermore, if the grantor (or person amenable to his will) is the trustee, particular consideration should be given to the following factors:

(i) Whether the trust is recognized as a partner in business dealings with customers and creditors, and

(ii) Whether, if the partnership income is not properly retained for the reasonable needs of the business, the trust's share of the income is distributed to the trust annually and paid to the beneficiaries or reinvested solely in the interest of the beneficiaries.

(8) *Interests of minor children (not held in trust).*—Except where a minor child is shown to be competent to manage his own property and participate in the partnership activities in accordance with his interest in the property, a minor child generally will not be recognized as a member of a partnership unless control of the property and its enjoyment is exercised by another person as fiduciary for the sole benefit of the child and unless there is such judicial supervision of the conduct of the fiduciary, guardian or otherwise, as is required by law. The use of the child's property or income for support for which a parent

is legally responsible will be considered a use for the parent's benefit. "Judicial supervision of the conduct of a fiduciary" includes filing of such accountings and reports as are required by law of the fiduciary who participates in the affairs of the partnership on behalf of the minor. A minor child will be considered as competent to manage his own property if he actually has sufficient maturity and experience to be treated by disinterested persons as competent to enter into business dealings and otherwise to conduct his affairs on a basis of equality with adult persons, notwithstanding legal disabilities of the minor under State law.

(9) *Donees as limited partners.*—The recognition of a donee's interest in a limited partnership will depend, as in the case of other donated interests, on whether the transfer of property is real and the donee has acquired dominion and control over the interests purportedly transferred to him. To be recognized for Federal income tax purposes, a limited partnership must be organized and conducted in accordance with the requirements of the applicable State limited partnership law. The absence of services and participation in management by a donee in a limited partnership is immaterial if the limited partnership meets all the other requirements prescribed in this section. If the limited partner's right to withdraw his interest is subject to substantial restrictions (for example, where the interest of the limited partner is not assignable in a real sense or where it may be required to be left in the business for a long term of years), or if the general partner retains any other control which substantially limits any of the rights which would ordinarily be exercisable by unrelated limited partners in normal business relationships, such restrictions on the right to withdraw or retention of other control will be considered strong evidence of lack of reality of ownership by the donee.

(10) *Motive.*—If the reality of the transfer of interest is satisfactorily established, the motives for the transaction are immaterial. However, the presence or absence of a tax avoidance motive is one of many factors to be considered in determining the reality of a gift capital transaction.

(*c*) *Purchased interest.*—(1) *In general.*—If a purported purchase of a capital interest in a partnership does not meet the requirements of paragraph (2), below, the ownership by the transferee of such capital interest will be recognized only if it qualifies under the requirements applicable to a transfer of a partnership interest by gift. In a case not qualifying under paragraph (2), if payment of any part of the purchase price is made out of the partnership earnings, the transaction may be regarded in the same light as a purported gift subject to deferred enjoyment of the income. Such a transaction may be lacking in reality either as a gift or as a bona fide purchase.

(2) *Tests as to reality of purchased interests.*—A purchase of a capital interest in a partnership either directly or by means of a loan or credit extended by a member of the family will be recognized if it is shown to be bona fide under either of the following tests:

(i) That the purchase has the usual characteristics of an arm's length transaction, considering all relevant factors including the terms of the purchase agreement (as to price, due date of payment, rate of interest, and security, if any) and the terms of any loan or credit arrangement collateral to the purchase agreement; the credit standing of the purchaser, apart from relationship to the seller; and the capacity of the purchaser to incur a legally binding obligation; or

(ii) Assuming the lack of one or more of the usual characteristics of arm's length dealing, that the transaction was genuinely intended to promote the success of the business through securing participation in the business of the purchaser or the addition of his or her credit to that of other participants.

However, if the alleged purchase price or loan has not been paid or the obligation otherwise discharged the factors indicated in (i) and (ii), above, shall be taken into account only as an aid in determining whether a bona fide purchase or loan obligation existed.

SEC. 29.191-2. ALLOCATION OF FAMILY PARTNERSHIP INCOME FOR TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1950.—(*a*) *In general.*—(1) In the case of any partnership in which capital is a material income-producing factor, if any capital interest in such a partnership is created by gift before, on, or after December 31, 1950, the distributive share of the donee under the partnership agreement, for taxable years beginning after December 31, 1950, shall be includible in his gross income, except to the extent that such share is determined without allowance of reasonable compensation for services rendered to the partnership by

the donor, and except to the extent that the portion of such share attributable to donated capital is proportionately greater than the share attributable to the donor's capital. For the purpose of this section, a capital interest in a partnership purchased by one member of a family from another shall be considered to be created by gift from the seller, and the fair market value of the purchased interest shall be considered to be donated capital. For the purpose of the preceding sentence, the "family" of any individual shall include only his spouse, ancestors, and lineal descendants, and any trust for the primary benefit of such persons.

(2) To the extent that the partnership agreement does not so allocate the partnership income, the partnership income of the donor and donee shall be reallocated by making a reasonable allowance for the services of the donor and by attributing the balance of such income (other than a reasonable allowance for the services, if any, rendered by the donee) to the partnership capital of the donor and donee. The portion of income, if any, thus attributable to partnership capital for the taxable year shall be allocated between donor and donee in accordance with their respective interests in the partnership capital.

(3) In determining a reasonable allowance for services rendered by the partners, consideration shall be given to all the circumstances of the business, including the fact that some of the partners may have greater managerial responsibility than others. Among other factors, there shall be considered the amount that would ordinarily be paid in order to obtain comparable services from a person not having a capital interest in the partnership.

(4) In the case of a partner who rendered services to a partnership prior to entering service in the Armed Forces of the United States, his distributive share in the earnings of the partnership, determined under (2), above, shall not be diminished because of absence due to military service. Such distributive share shall be adjusted to reflect increases or decreases in the capital interest of the absent partner. However, the partners may by agreement allocate a smaller share to the absent partner due to his absence.

(*b*) *Special rules.*—(1) The provisions of (*a*), above, relating to allocation, are applicable where the gift interest in the partnership is created indirectly as well as directly. Where the partnership interest is created indirectly, the term "donor" may include persons other than the nominal transferor.

Example (*1*). A father gives property to his son who shortly thereafter conveys the property to a partnership consisting of the father and the son. The partnership interest of the son may be considered created by gift and the father may be considered the donor of the son's partnership interest.

Example (*2*). A father, the owner of a business conducted as a sole proprietorship, transfers the business to a partnership consisting of his wife and himself. The wife subsequently conveys such interest to their son. In such case, the father, as well as the mother, may be considered the donor of the son's partnership interest.

Example (*3*). A father makes a gift to his son of stock in the family corporation. The corporation is subsequently liquidated. The son later contributes the property received in the liquidation of the corporation to a partnership consisting of his father and himself. In such case, the son's partnership interest may be considered created by gift and the father may be considered the donor of his son's partnership interest.

(2) The allocation rules set forth in section 191 and (*a*) of this section apply in any case in which the transfer or creation of the partnership interest has any of the substantial characteristics of a gift. Thus, allocation may be required where transfer of a partnership interest is made between members of a family (including collaterals) under a purported purchase agreement, if the characteristics of a gift are ascertained from the terms of the purchase agreement, the terms of any loan or credit arrangements made to finance the purchase, or from other relevant data.

(3) In the case of limited partnership, for the purpose of the allocation provisions of (*a*) of this section, proper weight shall be given to the fact that a general partner, unlike the limited partner, risks his credit in the partnership business.

PAR. 3. There is inserted immediately preceding section 29.3797-1 [26 CFR 29.3797-1] the following:

SEC. 340. FAMILY PARTNERSHIPS [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

(a) DEFINITION OF PARTNER.—Section 3797(a)(2) is hereby amended by adding at the end thereof the following: "A person shall be recognized as a partner for income tax purposes if he owns a capital interest in a partnership in which capital is a material income-producing factor, whether or not such interest was derived by purchase or gift from any other person."

* * * * * * *

(c) EFFECTIVE DATE.—The amendments made by this section shall be applicable with respect to taxable years beginning after December 31, 1950. The determination as to whether a person shall be recognized as a partner for income tax purposes for any taxable year beginning before January 1, 1951, shall be made as if this section had not been enacted and without inferences drawn from the fact that this section is not expressly made applicable with respect to taxable years beginning before January 1, 1951. In applying this subsection where the taxable year of any family partner is different from the taxable year of the partnership—

(1) if a taxable year of the partnership beginning in 1950 ends within or with, as to all of the family partners, taxable years which begin in 1951, then the amendments made by this section shall be applicable with respect to all distributive shares of income derived by the family partners from such taxable year of the partnership beginning in 1950, and

(2) if a taxable year of the partnership ending in 1951 ends within or with a taxable year of any family partner which began in 1950, then the amendments made by this section shall not be applicable with respect to any of the distributive shares of income derived by the family partners from such taxable year of the partnership.

PAR. 4. Section 29.3797-4 [26 CFR 29.3797-4] is amended by inserting immediately following the fifth sentence thereof the following:

See section 191 and the regulations thereunder, for treatment as a partner, for taxable years beginning after December 31, 1950, of any person who owns a capital interest in a partnership in which capital is a material income producing factor, whether or not such interest was derived by purchase or gift from any other person.

(This Treasury Decision is issued under the authority contained in secs. 62 and 3791 of the Internal Revenue Code (53 Stat. 32, 467; 26 U. S. C. 62, 3791).)

T. COLEMAN ANDREWS,
Commissioner of Internal Revenue.

Approved August 18, 1953.

H. CHAPMAN ROSE,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register August 24, 1953, 8:48 a. m.)

SUPPLEMENT G.—INSURANCE COMPANIES

SECTION 201.—LIFE INSURANCE COMPANIES

REGULATIONS 111, SECTION 29.201-7: Net income and deductions. Rev. Rul. 197

INTERNAL REVENUE CODE

Section 202(b) and section 203A (b) and (d) of the Internal Revenue Code require that interest paid be included as an element

in the computation of the "reserve and other policy liability credit" and the "reserve interest credit," respectively. Section 201(c)(7)(C) provides that certain taxes and other expenses paid during the taxable year exclusively upon or with respect to real estate owned are allowable deductions to a life insurance company in determining net income. The interest paid that is required to be included in the computation of the "reserve and other policy liability credit" and the "reserve interest credit" relates to interest paid on policy obligations. Section 201(f) provides that "Nothing in this section or in sections 202, 203, or 203A shall be construed to permit the same items to be twice deducted." Accordingly, it is held that interest paid on mortgages assumed by insurance companies in connection with the purchase of real estate for rental purposes is deductible under section 201(c)(7)(C) and is not includible in the computation of the "reserve and other policy liability credit" and the "reserve interest credit" referred to in section 202(b) and section 203A (b) and (d) of the Code.

REGULATIONS 111, SECTION 29.201–7: Net income and deductions. Rev. Rul. 198

(Also Section 22(a), Section 29.22(a)–1.)

INTERNAL REVENUE CODE

The entire amount paid by a life insurance company for accrued dividends with respect to stock purchased, is an investment of capital and may not be allowed as an offset against dividends received for Federal income tax purposes.

Advice is requested whether, in the case of life insurance companies, the amount paid for accrued dividends with respect to stock purchased is allowable as an offset against dividends received for Federal income tax purposes.

Section 201 of the Internal Revenue Code provides:

* * * * * * *

(c) OTHER DEFINITIONS.—In the case of a life insurance company—

(1) GROSS INCOME.—The term "gross income" means the gross amount of income received during the taxable year from interest, dividends, and rents.

Life insurance companies are required by the States in which they operate to prepare annual statements on a form that is in general use throughout the United States. In reporting "dividends on stock" on this form for the year in question the life insurance companies were required to exclude amounts "paid for accrued dividends on purchases." It is held that the amount shown as "dividends on stock" on the form in question is not determinative for Federal income tax purposes.

Section 29.22(a)–1 of Regulations 111 provides that an amount paid by a purchaser of stock to the seller in contemplation of the next dividend payment is an investment of capital and may not be claimed by the purchaser as a deduction from gross income. In I. T. 2569, C. B. X–1, 101 (1931), it is stated that although the purchaser of stock may have every reason to expect the full amount of the regular dividend to be paid after the stock is purchased, the price paid for the stock is the cost of the stock to him. I. T. 2569, *supra*, holds that

in cases of stock sold between dividend dates no distinction is made between common and preferred stock, and the entire amount of the dividend received by the vendee is income to him. Accordingly, it is held that the entire amount paid by a life insurance company for accrued dividends with respect to stock purchased, is an investment of capital and may not be allowed as an offset against dividends received for Federal income tax purposes.

REGULATIONS 111, SECTION 29.201-9: Amortization of premium and accrual of discount.

INTERNAL REVENUE CODE

Premiums paid for Federal Housing Administration insured mortgage loans. (See Rev. Rul. 258, p. 143.)

SECTION 204.—INSURANCE COMPANIES OTHER THAN LIFE OR MUTUAL

REGULATIONS 111, SECTION 29.204-1: Tax on insurance companies other than life or mutual and mutual marine insurance companies and mutual fire insurance companies issuing perpetual policies.

INTERNAL REVENUE CODE

Regulations 111 amended. (See T. D. 6024, 91.)

REGULATIONS 111, SECTION 29.204-2: Gross income. Rev. Rul. 151

INTERNAL REVENUE CODE

The Bureau adheres to, and amplifies the reasons for, the holding in I. T. 3798, C. B. 1946-1, 127, that the portions of original premiums established and segregated as a reinsurance reserve by a title insurance company from June 1, 1938, to May 31, 1945, under section 434 1.a. of the New York State Insurance Law may not be treated as unearned premiums under section 204(b)(5) of the Code.

The question has arisen as to the precise meaning of I. T. 3798, C. B. 1946-1, 127, in view of the reference therein to the case of *Early* v. *Lawyers Title Insurance Corporation*, (CA-4, 1942) 132 F. (2d) 42. In that I. T., it was stated in part:

Section 434 1.b. of the New York State Insurance Laws, supra, gives to the portions of the premiums which it requires to be placed in the reserve all the attributes that pertain to unearned premiums, i. e., it withdraws them from the power of the company to use them for its general purposes and impresses them with a trust in favor of the contract holders until the risk shall have been carried for the period that the statute prescribes. In that respect it is similar to the provisions of the Virginia statute involved in *Early* v. *Lawyers Title Insurance Corporation*, supra. However, the provisions of section 434 1.a. of the laws of New York, supra, and its counterpart, section 434 1.a. of chapter 28 of the consolidated laws as enacted by chapter 882 of the laws of 1939, supra, are similar to the Pennsylvania statutory provisions which were involved in *American Title Co.* v. *Commissioner*, supra. They merely provide for a solvency reserve, and, unlike the provisions of the Virginia statute involved in *Early* v. *Lawyers Title Insurance Corporation*, supra, they do not impress the reserve funds with a trust in favor of the contract holders.

In view of the foregoing, it is held that the portions of original premiums established and segregated as a reinsurance reserve by a title insurance company on and after June 1, 1945, under section 434 1.b. of the New York State Insurance Law, supra, may be treated as unearned premiums under section 204(b)(5) of the Internal Revenue Code. The portions of original premiums established and segregated as a reinsurance reserve by a title insurance company from June 1, 1938, to May 31, 1945, under section 434 1.a. of the New York State Insurance Law, supra, may not be treated as unearned premiums under section 204(b)(5) of the Code. (See *City Title Insurance Co.* v. *Commissioner*, 152 Fed. (2d), 859, as to the latter conclusion.)

Actually, the court in *Early* v. *Lawyers Title Insurance Corporation* made no distinction, for Federal income tax purposes, under the Virginia statute there involved between reinsurance reserves set up out of premiums received prior to the enactment of the Virginia statute and reinsurance reserves set up out of premiums received subsequent to that time. Under similar Oregon statutes, the Court of Appeals for the Ninth Circuit held, following *Early* v. *Lawyers Title Insurance Corporation*, that reinsurance reserves composed of and measured by earned premiums received in prior years constituted "unearned premiums". *Pacific Abstract Title Co.* v. *United States* (C. A.-9, 1951) 192 F. (2d) 931; and *Title and Trust Company* v. *Commissioner* (C. A.-9, 1951) 192 F. (2d) 934, decided together with Pacific Abstract.

However, it was not the purpose of the Bureau in I. T. 3798, *supra*, to accept as correct the decision in *Early* v. *Lawyers Title Insurance Corporation* that the reinsurance reserves set up out of premiums previously received should be treated as unearned premiums in the computation of tax liability arising after the passage of the Virginia statute.

Federal income taxes are imposed on the basis of annual periods. See *Security Flour Mills Co.* v. *Commisioner*, Ct. D. 1603, C. B. 1944, 526; (1944) 321 U. S. 281 in which it was stated in part:

The rationale of the system is this: "It is the essence of any system of taxation that it should produce revenue ascertainable, and payable to the government, at regular intervals. Only by such a system is it practicable to produce a regular flow of income and apply methods of accounting, assessment, and collection capable of practicable operation."

This legal principle has often been stated and applied. The uniform result has been denial both to government and to taxpayer of the privilege of allocating income or outgo to a year other than the year of actual receipt or payment, or, applying the accrual basis, the year in which the right to receive, or the obligation to pay, has become final and definite in amount.

Furthermore, Congress intended to provide a system of taxation which would be uniform in all the States and intended that local law should not be controlling except where the Federal taxing act by express language or necessary implication makes its own operation dependent upon State law. *Burk-Waggoner Oil Association* v. *Hopkins* (1925) 269 U. S. 110, and *Burnet* v. *Harwel*, Ct. D. 611, C. B. XI-2, 210; (1932) 287 U. S. 103, in which latter case the Supreme Court stated:

Here we are concerned only with the meaning and application of a statute enacted by Congress, in the exercise of its plenary power under the Constitution, to tax income. The exertion of that power is not subject to State control. It is the will of Congress which controls, and the expression of its will in legislation, in the absence of language evidencing a different purpose, is to be interpreted so as to give a uniform application to a nation-wide scheme of taxation. [citing

cases] State law may control only when the operation of the Federal taxing act, by express language or necessary implication makes its own operation dependent upon State law.

It is the position of the Bureau that there is no implication in the provisions of the Internal Revenue Code dealing with the computation of "unearned premiums" that the annual method of tax reporting should be affected by a State statute retroactively converting, either directly or indirectly, some portion of previously received premiums into a reinsurance reserve.

It is true that payments received by a taxpayer which are subject to a restriction *at the time they are received*, such as a trust, may not be income to the recipient, if the restriction is substantial, at least so long as the restriction continues. See, for example, *Marion H. McArdle* (1948) 11 T. C. 961, involving part of purchase price withheld under agreement guarantee with purchaser, and G. C. M. 8446, C. B. IX-2, 370; *Los Angeles Cemetery Association* (1925) 2 B. T. A. 496, involving portion of the purchase price of cemetery lots received in trust for perpetual care and maintenance. Accordingly, that portion of premiums received *after* the enactment of a State statute (which constitutes such portion a reinsurance reserve) may properly be construed as unearned premiums.

However, a clear cut distinction should be made between reinsurance reserves set up by statute and imposed for a reasonable time upon *future* receipts and the reinsurance reserves which a statute attempts, directly or indirectly, to constitute out of *premiums previously received*, and which were fully earned at the time of receipt.

Title insurance premiums received in years prior to the enactment of a State statute were clearly taxable as income at the time they were received. It is a well established rule of taxation that income received under claim of right without restriction as to its disposition at the time of receipt constitutes taxable income in the year of its receipt even though subject to some future contingency. *Brown* v. *Helvering* (1934) 291 U. S. 193, affirming (C. A.-9th, 1933) 63 F. (2d) 66; *Philadelphia Title Insurance Company* (1951) 17 T. C. 1068, acquiescence C. B. 1953-1, 5; *Wayne Title & Trust Company* (C. A.-3, 1952) 195 F. (2d) 401. Income thus taxed in a prior year must necessarily be construed as premiums earned in such year, and a state statute cannot be considered as changing their character retroactively to "unearned premiums."

In view of the foregoing, the Bureau adheres to the conclusions reached in I. T. 3798, *supra*.

SUPPLEMENT H.—NONRESIDENT ALIEN INDIVIDUALS

SECTION 212.—GROSS INCOME

REGULATIONS 111, SECTION 29.212-2: Exclusion of earnings of foreign ships or aircraft from gross income. (Also Section 231, Section 29.231-3.) — Rev. Rul. 171

INTERNAL REVENUE CODE

The Japanese Ministry of Foreign Affairs has confirmed the validity of Japanese Law No. 6 of 1924, as amended by Law No. 57 of 1940, relating to the exemption from income tax, corporate tax, and business tax of income and net profits derived from the operation of foreign vessels. Accordingly, Japan satisfies the equivalent exemption requirements of sections 212(b)(1) and 231(d)(1) of the Internal Revenue Code.

SUPPLEMENT I.—FOREIGN CORPORATIONS

SECTION 231.—TAX ON FOREIGN CORPORATIONS

REGULATIONS 111, SECTION 29.231-1: Taxation of foreign corporations.

INTERNAL REVENUE CODE

Regulations 111 amended. (See T. D. 6024, p. 91.)

REGULATIONS 111, SECTION 29.231-3: Exclusion of earnings of foreign ships or aircraft from gross income.

INTERNAL REVENUE CODE

Japan-equivalent exemption provisions of section 231(d)(1) of the Internal Revenue Code. (See Rev. Rul. 171, p. 224.)

SUPPLEMENT J.—POSSESSIONS OF THE UNITED STATES

SECTION 251.—INCOME FROM SOURCES WITHIN POSSESSIONS OF UNITED STATES

REGULATIONS 111, SECTION 29.251-4: Definition. (Also Section 116, Section 29.116-1; Section 131, Section 29.131-1.) Rev. Rul. 199

INTERNAL REVENUE CODE

The term "United States" when used in the geographical sense is defined in section 3797(a)(9) of the Internal Revenue Code as including only the States, the Territories of Alaska and Hawaii, and the District of Columbia. In I. T. 4080, C. B. 1952-1, 139, it is held that the Marshall Islands, which are a part of the former Japanese mandated islands now known as the Territory of the Pacific Islands (of which Okinawa in the Ryukyu group also is a part), administered by the United States under a trusteeship agreement between the United States and the Security Council of the United Nations, do not constitute a possession of the United States. Accordingly, it is held that Okinawa is not a possession of the United States within the meaning of section 251 of the Code, but is a foreign country for the purposes of sections 116(a) and 131 of the Code.

SUPPLEMENT L.—ASSESSMENT AND COLLECTION OF DEFICIENCIES

SECTION 271.—DEFINITION OF DEFICIENCY

REGULATIONS 111, SECTION 29.271-1: Deficiency defined.

INTERNAL REVENUE CODE

Penalty based upon a deficiency existing prior to application of carryback loss where tax in original return is equal to or in excess of tax finally determined. (See Rev. Rul. 173, p. 227.)

SUPPLEMENT M.—INTEREST AND ADDITIONS TO THE TAX

SECTION 291.—FAILURE TO FILE RETURN

REGULATIONS 111, SECTION 29.291-1: Addition to the tax in case of failure to file return. (Also Section 500, Section 29.500-1.) Rev. Rul. 172

INTERNAL REVENUE CODE

The delinquency penalty under section 291 of the Internal Revenue Code should not be asserted against a personal holding company in any case in which failure to file a timely Form 1120H is attributable to reliance in good faith upon the advice of a reputable accountant or attorney, experienced in Federal tax matters, and to whom all relevant information has been furnished.

SECTION 292.—INTEREST ON DEFICIENCIES

(Also Section 112(n), Section 29.112(n)-1, Regulations 111.)

INTERNAL REVENUE CODE

Interest must be assessed on a deficiency in Federal income tax which arises when a taxpayer who has sold his "old residence" has not purchased a "new residence" within the period of time prescribed by section 112(n) of the Internal Revenue Code.

Advice is requested whether a taxpayer may be relieved from the assessment of interest on a deficiency in Federal income tax which arises because the taxpayer, who has sold his "old residence," is unable to purchase a "new residence" suitable for his needs within the period of time prescribed by section 112(n) of the Internal Revenue Code.

Section 112(n) of the Code provides in part as follows:

(n) GAIN FROM SALE OR EXCHANGE OF RESIDENCE.—

(1) NONRECOGNITION OF GAIN.—If property (hereinafter in this subsection called "old residence") used by the taxpayer as his principal residence is sold by him and, within a period beginning 1 year prior to the date of such sale and ending 1 year after such date, property (hereinafter in this subsection called "new residence") is purchased and used by the taxpayer as his principal residence, gain (if any) from such sale shall be recognized

only to the extent that the taxpayer's selling price of the old residence exceeds the taxpayer's cost of purchasing the new residence.

Section 29.112(n)-1 of Regulations 111 provides that if an intention not to replace his old residence is formed by a taxpayer, or if the period in which replacement may result in nonrecognition of gain expires, or if the cost of purchasing the new residence is less than the selling price of the old residence, the recognizable gain shall be included in the gross income for the taxable year or years in which such gain was realized.

The gain from the sale of a taxpayer's principal residence is a gain realized by him in the year of the sale of such residence. Whether any part of that gain is not to be recognized depends upon the taxpayer's meeting the conditions of section 112(n) of the Code, *supra*. If the taxpayer does not meet the conditions of section 112(n), the additional income tax resulting therefrom is a "deficiency," within the meaning of sections 271 and 292(a) of the Code, for the taxable year in which the sale occurred.

Section 292(a) of the Code provides in part that interest upon the amount determined as a deficiency shall be assessed at the same time as the deficiency, shall be paid upon notice and demand from the collector, and shall be collected as a part of the tax at the rate of 6 per centum per annum from the date prescribed for the payment of the tax to the date the deficiency is assessed, or, in the case of a waiver under section 272(d), to the 30th day after the filing of such waiver or to the date the deficiency is assessed whichever is the earlier.

The assessment and collection of interest on a deficiency is mandatory and may not be waived by the Bureau regardless of the circumstances which caused the deficiency. Accordingly, it is held that interest must be assessed on a deficiency in Federal income tax which arises when a taxpayer who has sold his "old residence" has not purchased a "new residence" within the period of time prescribed by section 112(n) of the Code, *supra*. Such interest must be assessed from the date the tax on the gain from the sale of a taxpayer's "old residence" would have been due, without regard to the provisions of section 112(n) of the Code, to the date the deficiency is assessed, or, if a waiver has been filed by the taxpayer under section 272(d) of the Code, to the 30th day after the filing of such waiver or to the date the deficiency is assessed whichever is the earlier.

SECTION 293.—ADDITIONS TO THE TAX IN CASE OF DEFICIENCY

(Also Section 271, Section 29.271-1, Regulations 111.) **Rev. Rul. 173**

INTERNAL REVENUE CODE

An ad valorem penalty (negligence, delinquency, or fraud) based upon the amount of a deficiency existing prior to the application of a relief provision such as a net operating loss carryback is to be imposed in connection with a Federal income tax liability, even though the tax as reported in the original return is equal to or in excess of the correct tax as finally determined after the application of such provision.

Advice is requested whether section 293(b) of the Internal Revenue Code requires the imposition of a fraud penalty upon a deficiency existing prior to the application of a carryback of a net operating loss or an unused excess-profits credit, even though the tax as reported in the original return is equal to or in excess of the tax as finally determined after the application of such credit.

In the instant case, the taxpayer filed an income tax return disclosing Federal income tax liability of $40x$ dollars, which was paid. Subsequently, the taxpayer filed an amended return, disclosing fraud in the original return and paid additional tax of $9x$ dollars. As the result of the application of a carryback of an unused excess-profits credit the tax was reduced to $20x$ dollars and the overpayment was refunded. Upon examination of the returns, further adjustments (not related to the fraud items) were made resulting in additional tax due of $3x$ dollars and tax as finally determined of $23x$ dollars. The basic question is whether section 293(b) of the Code requires the imposition of the fraud penalty on a total deficiency of $12x$ dollars even though the correct liability of $23x$ dollars is less than the liability of $40x$ dollars shown in the original return, and the deficiency of $3x$ dollars does not result from an item of fraud. The answer to this question is to be found in the construction of section 293(b), relating to fraud penalties, and section 271, defining "deficiency."

Section 293(b) of the Internal Revenue Code provides as follows:

(b) FRAUD.—If any part of any deficiency is due to fraud with intent to evade tax, then 50 per centum of the total amount of the deficiency (in addition to such deficiency) shall be so assessed, collected, and paid, in lieu of the 50 per centum addition to the tax provided in section 3612(d)(2).

Section 271(a) of the Code provides in part as follows:

(a) IN GENERAL.—As used in this chapter [chapter 1 of the Code] in respect of a tax imposed by this chapter, "deficiency" means the amount by which the tax imposed by this chapter exceeds the excess of—

(1) the sum of (A) the amount shown as the tax by the taxpayer upon his return, if a return was made by the taxpayer and an amount was shown as the tax by the taxpayer thereon, plus (B) the amounts previously assessed (or collected without assessment) as a deficiency, over—

(2) the amount of rebates * * * made.

Section 29.271-1 of Regulations 111, promulgated pursuant to section 271 of the Code, provides in part as follows:

When a case is considered for the first time, the deficiency is the excess of the amount determined to be the correct amount of the tax over the amount shown as the tax by the taxpayer on his return, or, if it is a case where no tax was reported by the taxpayer, the deficiency is the amount determined to be the correct amount of the tax. Subsequent information sometimes discloses that the amount previously determined to be the correct amount of the tax is less than the correct amount, and that a redetermination of the tax is necessary. In such a case the deficiency on redetermination is the excess of the amount determined to be the correct amount of the tax over the sum of the amount of tax reported by the taxpayer and the deficiency assessed in connection with the previous determination. If it is a case where no tax was reported by the taxpayer, the deficiency is the excess of the amount determined to be the correct amount of the tax over the amount of the deficiency disclosed by the previous determination. *If the previous determination resulted in a credit or refund to the taxpayer, the deficiency upon the second determination is the excess of the amount determined to be the correct amount of the tax over the amount of tax reported by the taxpayer decreased by the amount of the credit or refund.* (Italics supplied.)

The case of Daniel J. Leary and Sadie D. Leary, Tax Court Memorandum Opinion entered January 25, 1945, and April 10, 1945, illustrates the interrelation of sections 271 and 293(b) in the computation of the fraud penalty. In that case the Commissioner assessed deficiencies for 2 of the years involved and later discovered fraud, at which time he assessed for each year an additional deficiency and a penalty to the extent of 50 percent of the total of the two deficiencies assessed for each year. For the other year involved, the taxpayer had obtained a refund prior to the discovery of fraud which resulted in the assessment of a deficiency and fraud penalty. In computing the penalty the amount of tax shown on the return was reduced by the amount of the refund. This sum was then deducted from the correct amount of the tax and the deficiency arrived at. The full amount that the correct amount of tax exceeded the amount shown on the return as decreased by the refund was assessed as a deficiency. Fifty percent of this identical figure was asserted as a fraud penalty. The Tax Court of the United States accepted the computation of the Commissioner for the year involving the refund, but at first objected to the computations involving the two deficiencies. After consideration of a motion filed by the Commissioner, in which it was contended that such computations of penalty were determined in accordance with the provisions of section 271(a) of the Code, defining deficiency, the court ordered its former opinion amended. This case is significant in that it involves a refund after which a deficiency due to fraud was discovered. It demonstrates that the amount of tax shown on the return must be adjusted by the amount of the prior refund even for the purpose of asserting the fraud penalty under section 293(b) of the Code. The fact that the court in the same case had before it the proper treatment of a situation where there was a deficiency prior to the deficiency due to fraud adds additional weight to the holding. In this connection also see *Maitland A. Wilson* v. *Commissioner*, 7 T. C. 395.

In *John E. Manning* v. *Seeley Tube & Box Co.*, 338 U. S. 561, Ct. D. 1729, C. B. 1950-1, 113, it was held that while a net operating loss carryback may serve to eliminate a deficiency for a previous year, the interest which had theretofore accrued on such deficiency was not eliminated. In holding that the Government was entitled to interest, the Supreme Court of the United States concluded that there was a real deficiency existing prior to the occurrence of the carryback loss and the right to interest is dependent upon the existence of a deficiency. It follows that for purposes of the penalties imposed under sections 291 and 293 of the Code, a real deficiency must likewise be considered to exist.

In G. C. M. 26455, C. B. 1950-1, 118, it is held that interest and penalties assessed and collected in connection with a Federal income tax liability should not be credited or refunded even though such tax liability is reduced or eliminated by net operating loss carrybacks. The ruling points out that the statutory pattern requiring prompt payment of taxes was the foundation of the decision of the Supreme Court in *Manning* v. *Seeley Tube & Box Co.*, *supra*, and that the rationale of that case applied to penalties. The prompt filing of returns which convey complete and accurate information is equally a statutory duty

of every taxpayer. The carryback provisions of the Code do not modify such duties. (See S. Rept. 1631, C. B. 1942-2, 504, 597.) Although the facts in the instant case differ from those in the Supreme Court case and G. C. M. 26455 cited above, in that the question involved is the assertion of penalty instead of the proper refund of interest or a penalty already asserted, and the carryback is with respect to an unused excess-profits credit rather than a net operating loss, it seems clear that the same reasoning applies.

Section 293(b) of the Code provides a penalty computed not upon "any part of any deficiency" but upon "the total amount of the deficiency". In view of the foregoing it follows that section 293 of the Code and section 271, which define "deficiency," are interdependent and that the sum total of the deficiency referred to in clause (B) of section 271(a)(1) has the same meaning as the total amount of the deficiency in section 293(b). The proper procedure in determining the total amount of deficiency is, therefore, to compute each deficiency pursuant to the provisions of section 271 of the Code and add them together for the purposes of section 293(b). This procedure gives effect to reductions in the correct amount of tax due to carryback losses or elimination of excessive profits, and prior refunds or credits received in renegotiation settlements under section 3806 of the Code, and requires the amounts of such adjustments to be deducted from the original return in computing the total deficiency.

Accordingly, it is held that an ad valorem penalty (negligence, delinquency, or fraud) based upon the amount of a deficiency existing prior to the application of a relief provision such as a net operating loss carryback is to be imposed in connection with a Federal income tax liability, even though the tax as reported in the original return is equal to or in excess of the correct tax as finally determined after the application of such provision. Applying these principles to the instant case, the imposition of the fraud penalty on the total deficiency of 12x dollars is required by statute.

SUPPLEMENT O.—OVERPAYMENTS

SECTION 322.—REFUNDS AND CREDITS

REGULATIONS 111, SECTION 29.322-7: Limitations upon the crediting and refunding of taxes paid.

INTERNAL REVENUE CODE

Limitation upon the amount of refund or credit of taxes paid, based upon a net operating loss carryback to a year in which a net operating loss carryover was not properly taken into account, the time for filing a claim for refund or credit based upon the net operating loss carryover having expired. (See Rev. Rul. 218, p. 176.)

SUBCHAPTER D.—EXCESS-PROFITS TAX

PART I.—RATE AND COMPUTATION OF TAX

SECTION 430.—IMPOSITION OF TAX

REGULATIONS 130, SECTION 40.430–1: Scope of tax. T. D. 6046

(Also Section 40.430–2; Section 431, Section 40.431–1; Section 432, Section 40.432–1; Section 141, Section 24.31(a)(90), Regulations 129.)

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 24 AND PART 40

Regulations 129 and 130 amended to conform to the provisions of Public Law 125, Eighty-third Congress [p. 473, this Bulletin], approved July 16, 1953, relating to the extension until December 31, 1953, of the period with respect to which the excess-profits tax shall be effective.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

In order to conform Regulations 129 [26 CFR, pt. 24] and Regulations 130 [26 CFR, pt. 40] to the provisions of Public Law 125, Eighty-third Congress [p. 473, this Bulletin], approved July 16, 1953, relating to the extension until December 31, 1953, of the period with respect to which the excess-profits tax shall be effective, such regulations are hereby amended as follows:

REGULATIONS 129 [26 CFR, PT. 24]

PARAGRAPH 1. Subdivision (iii) of section 24.31(a)(90) is amended by striking "June 30, 1953" and "July 1, 1953", wherever such dates appear, and inserting in lieu thereof "December 31, 1953" and "January 1, 1954", respectively, so that such subdivision as amended shall read as follows:

(iii) In the case of a taxable year of the group beginning before January 1, 1954, and ending after December 31, 1953, such amount shall be reduced to an amount which is such part thereof as the number of days in such taxable year before January 1, 1954, is of the total number of days in such taxable year; and

REGULATIONS 130 [26 CFR, PT. 40]

PAR. 2. There is inserted immediately preceding section 40.430–1 the following:

PUBLIC LAW 125, EIGHTY-THIRD CONGRESS
APPROVED JULY 16, 1953

* * * sections 430(a), 430(c), * * * of the Internal Revenue Code are amended, effective with respect to taxable years ending after June 30, 1953, by striking "June 30, 1953," and "July 1, 1953," wherever such dates appear, and inserting in lieu thereof "December 31, 1953," and "January 1, 1954," respectively.

PAR. 3. The second sentence of section 40.430–1 is amended by striking "July 1, 1953" and inserting in lieu thereof "January 1, 1954" so that such sentence as amended shall read as follows:

The excess-profits tax is imposed upon the adjusted excess-profits net income of every corporation, both domestic and foreign, for each taxable year ending after June 30, 1950, and beginning before January 1, 1954, except in the case of certain corporations which are exempt from the tax under the provisions of section 454.

PAR. 4. Paragraph (c) of section 40.430–2 is amended by striking "June 30, 1953" and "July 1, 1953", wherever such dates appear, and inserting in lieu thereof "December 31, 1953" and "January 1, 1954", respectively, so that such paragraph as amended shall read as follows:

(c) *Taxable years beginning before January 1, 1954, and ending after December 31, 1953.*—In the case of a taxable year which begins before January 1, 1954, and ends after December 31, 1953, the excess-profits tax will be an amount equal to that portion of a tentative tax determined under section 430(a) and under (a) of this section as the number of days in such year prior to January 1, 1954, bears to the total number of days in such year.

PAR. 5. The last sentence of section 40.431–1, as added by Treasury Decision 6024 [p. 91, this Bulletin], approved June 25, 1953, is amended by striking "June 30, 1953" and "July 1, 1953", and inserting in lieu thereof "December 31, 1953" and "January 1, 1954", respectively, so that such sentence as amended shall read as follows:

For treatment of taxable years beginning before January 1, 1954, and ending after December 31, 1953, see section 40.430–2(c).

PAR. 6. There is inserted immediately preceding section 40.432–1 the following:

PUBLIC LAW 125, EIGHTY-THIRD CONGRESS APPROVED JULY 16, 1953

* * * sections * * * 432(b) of the Internal Revenue Code are amended, effective with respect to taxable years ending after June 30, 1953, by striking "June 30, 1953," and "July 1, 1953," wherever such dates appear, and inserting in lieu thereof "December 31, 1953," and January 1, 1954," respectively.

PAR. 7. The first and fourth sentences of paragraph (a) of section 40.432–1 are amended by striking "June 30, 1953" and "July 1, 1953", wherever such dates appear, and inserting in lieu thereof "December 31, 1953" and "January 1, 1954", respectively, so that such sentences as amended shall read as follows:

Section 432 provides that the unused excess-profits credit for any taxable year ending after June 30, 1950, and beginning before January 1, 1954, is the excess of the corporation's excess-profits credit for such taxable year over its excess-profits net income for such year computed without regard to the net operating loss deduction and computed on the basis of the excess-profits credit applicable to such year. * * * If the taxable year begins before January 1, 1954, and ends after December 31, 1953, the unused excess-profits credit will be an amount which is such portion of the unused excess-profits credit determined under the general rule as the number of days in the taxable year before January 1, 1954, is of the total number of days in such taxable year.

Inasmuch as this Treasury Decision merely provides for the extension, until December 31, 1953, of the period with respect to which the excess-profits tax shall be effective, in conformity with the provisions of Public Law 125, Eighty-third Congress, approved July 16, 1953, it is hereby found that it is unnecessary to issue such Treasury Decision with notice and public procedure thereon under section 4(a) of the Administrative Procedure Act, approved June 11, 1946, or subject to the effective date limitation of section 4(c) of that act.

(This Treasury Decision is issued under authority contained in secs. 62, 141, and 3791 of the Internal Revenue Code (53 Stat. 32, 467; 64 Stat. 1217; 26 U. S. C. 62, 141, 3791).)

T. COLEMAN ANDREWS,
Commissioner of Internal Revenue.

Approved October 28, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register November 2, 1953, 8:51 a. m.)

REGULATIONS 130, SECTION 40.430-2: Rate of tax. Rev. Rul. 200

INTERNAL REVENUE CODE

A new corporation, which succeeded to the business and assets of a predecessor partnership in a tax-free transaction under section 112(b)(5) of the Internal Revenue Code, is deemed to have commenced business, for the purpose of computing its excess-profits tax under section 430(e) of the Code, on the date it acquired the business and assets from the partnership and the organization date of the predecessor partnership is immaterial for such purposes.

REGULATIONS 130, SECTION 40.430-2: Rate of tax. Rev. Rul. 212
(Also Section 445, Section 40.445-1.)

INTERNAL REVENUE CODE

A new corporation does not commence business within the meaning of section 430(e) and section 445(a) of the Internal Revenue Code until it starts the business operations for which it was organized regardless of the fact that it may have incidental income prior to that time. A new corporation organized in 1946 to engage in the banking business will not be considered as having commenced business in 1947 merely because it realized income in that year from the sale of a building site which was unsuitable for its purposes and had filed a Federal income tax return for 1947 (the corporation's first return) reporting such income. Inasmuch as the corporation had, as of the end of 1947 only a comparatively small portion of the assets necessary for the banking business, and since the corporation did not start any of the business operations for which it was organized until 1948 when it was authorized by the State bank commissioner to commence the general business of banking, it is held that the corporation did not commence business within the meaning of section 430(e) and section 445(a) of the Code until 1948.

SECTION 431.—DEFINITION OF ADJUSTED EXCESS-PROFITS NET INCOME

REGULATIONS 130, SECTION 40.431-1: Definition of adjusted excess-profits net income.

INTERNAL REVENUE CODE

Regulations 130 amended. (See T. D. 6024, p. 91.)

REGULATIONS 130, SECTION 40.431-1: Definition of adjusted excess-profits net income.

INTERNAL REVENUE CODE

Regulations 130 amended. (See T. D. 6046, p. 231.)

SECTION 432.—UNUSED EXCESS-PROFITS CREDIT ADJUSTMENT

REGULATIONS 130, SECTION 40.432-1: Unused excess-profits credit adjustment.

INTERNAL REVENUE CODE

Regulations 130 amended. (See T. D. 6046, p. 231.)

SECTION 435.—EXCESS-PROFITS CREDIT—BASED ON INCOME

REGULATIONS 130, SECTION 40.435-6: Capital additions in base period.

INTERNAL REVENUE CODE

Regulations 130 amended. (See T. D. 6054, p. 242.)

REGULATIONS 130, SECTION 40.435-6(a): Capital additions in base period—(a) In general.

INTERNAL REVENUE CODE

Date for determining yearly base period capital for second preceding taxable year of component corporation treated as acquiring corporation in case of part II transaction. (See Rev. Rul. 186, p. 249.)

SECTION 445.—AVERAGE BASE PERIOD NET INCOME—NEW CORPORATION

REGULATIONS 130, SECTION 40.445-1: New corporations.

INTERNAL REVENUE CODE

Application of term "commenced business" to new corporations. (See Rev. Rul. 242, p. 233.)

SECTION 448.—EXCESS-PROFITS CREDIT—REGULATED PUBLIC UTILITIES

REGULATIONS 130, SECTION 40.448-2: Definitions. (Also Section 141, Section 24.31(b)(20), Regulations 129.) — Rev. Rul. 123

INTERNAL REVENUE CODE

The Securities and Exchange Commission, in its capacity as administrator under the Public Utility Holding Company Act of 1935 for the protection of investments of stockholders, does not qualify as "an appropriate regulatory body" under section 448(b)(3) of the Internal Revenue Code in determining whether the books of account of a regulated public utility are properly regulated for the purpose of determining its excess-profits credit. The term "an appropriate regulatory body" as used in section 448(b)(3) of the Code is confined to rate regulating bodies. (See sec. 40.448-2(e)(2)(ii), Regulations 130.) Accordingly, in computing the consolidated section 448 inadmissible asset adjustment of such a public utility, its assets may not be determined by reference solely to the amounts recorded in its books of account which are maintained in accordance with a system of accounts prescribed by the Securities and Exchange Commission. (See Rev. Rul. 63, C. B. 1953-1, 355.)

SECTION 453.—NONTAXABLE INCOME FROM CERTAIN MINING AND TIMBER OPERATIONS, AND FROM NATURAL GAS PROPERTIES

REGULATIONS 130, SECTION 40.453-2: Definitions.

INTERNAL REVENUE CODE

Regulations 130 amended. (See T. D. 6031, p. 120.)

SECTION 456.—ABNORMALITIES IN INCOME IN TAXABLE PERIOD

REGULATIONS 130, SECTION 40.456-2: Classification of income. — T. D. 6026

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 40.—EXCESS-PROFITS TAX; TAXABLE YEARS ENDING AFTER JUNE 30, 1950

Section 40.456-2(b) of Regulations 130 amended

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

On December 4, 1952, a notice of proposed rulemaking was published in the Federal Register (17 F. R. 10973) amending section

40.456-2(b) of Regulations 130 [26 CFR, pt. 40]. After consideration of such relevant suggestions as were presented regarding the proposals, such regulations are hereby amended by adding at the end of section 40.456-2(b) the following:

Income from the sale of tangible property arising out of research and development which extended over a period of more than 12 months is not included in the list of abnormal types of income to which section 456 is applicable, and such income may not constitute a class of income for purposes of that section. However, section 456 is applicable to such income if the income is otherwise properly includible within a class of income to which such section is applicable for example, the class described in section 456(a)(2)(D).

(This Treasury Decision is issued under the authority contained in sec. 62 of the Internal Revenue Code (53 Stat. 32; 26 U. S. C. 62).)

T. COLEMAN ANDREWS,
Commissioner of Internal Revenue.

Approved July 3, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register July 8, 1953, 8:52 a. m.)

REGULATIONS 130, SECTION 40.456-7: Exploration, discovery, prospecting. Rev. Rul. 236

INTERNAL REVENUE CODE

Application of section 456 of the Internal Revenue Code to the oil and gas extractive industry: Abnormal income resulting from exploration, discovery, or prospecting.

1. *Purpose.*—The purpose of this Revenue Ruling is to state the position of the Internal Revenue Service with respect to the application of section 456 of the Internal Revenue Code (relating to the excess-profits tax) to taxpayers engaged in the extraction of petroleum and natural gas.

2. *Exploration, discovery, or prospecting.*—Exploration or prospecting by a taxpayer begins with the first field work designed to determine whether to acquire or retain the acreage in the area in which a discovery is later made. (See I. T. 4006, C. B. 1950-1, 38.) It does not include the general research of published reports to determine where exploration might be profitable. Exploration is ended and discovery occurs for a pool when a well is completed that proves the presence of oil or gas in commercial quantities. Subsequent drilling in the pool, while it may contain a large element of risk, constitutes exploitation to reap the benefits of the discovery. To the extent that "development" is the equivalent of "exploration" or "discovery," it may result in abnormal income under section 456; to the extent that "development" is the equivalent of "exploitation," it will not result in any abnormal income within the meaning of section 456.

3. *Period of exploration, discovery, or prospecting.*—To qualify under section 456(a)(2)(B) income must result from exploration, discovery, or prospecting, or any combination of the foregoing, extending over a period of more than 12 months. This means that the

elapsed time between the commencement of exploration or prospecting and the resulting discovery, as defined in paragraph 2, exclusive of any intervening periods of inactivity, must total more than 12 months. Only the actual time consumed from the initial steps in the exploration or prospecting to the final completion of the discovery well that proved the presence of oil or gas in commercial quantities is to be considered in measuring the time elapsed.

4. *Class of income.*—The entire income of a taxpayer which results from exploration, discovery, or prospecting, or any combination of the foregoing, extending over a period of more than 12 months, constitutes a single class of income.

5. *Determination of abnormal income.*—That part of the gross income from the sale of oil and/or gas from properties of the taxpayer which meets the other requirements of section 456 and which it attributable to the exploration, discovery, or prospecting of such properties constitutes abnormal income within the meaning of section 456(a)(2)(B). That part of the gross income from the sale of oil and/or gas from the taxpayer's properties which is attributable to the exploitation of such properties, however, does not under any circumstances constitute abnormal income within the meaning of section 456(a)(2)(B). Any method of allocation will be acceptable which reasonably determines the portions of income which are attributable to exploration, discovery, or prospecting of the properties and the portions of income which are attributable to the development or exploitation of the properties in view of the respective risks undertaken. For example, an amount equal to the total amount which would be realized over the life of the properties as overriding royalties if the properties had been subleased on the discovery date (or the actual amount so realized if the properties in fact were subleased) qualifies as abnormal income. Such amount will not include any income which would be realized by the sublessee as the result of exploitation of such properties.

The amount which would be equal to the assumed overriding royalties (if the properties were not in fact subleased), or the income otherwise determined as attributable to exploration, discovery, or prospecting of the properties, must be established in the light of the conditions and circumstances known at the discovery date, regardless of later information concerning the properties. The terms of an assumed sublease shall be determined on the basis of a transfer between a willing sublessor and a willing sublessee as of the discovery date. Due weight shall be given to any and all facts and evidence having a bearing on the amount of such overriding royalties, or income attributable to exploration, discovery, or prospecting, such as the actual subleasing of similar properties, or the determination by an analytical method which will reasonably apportion the anticipated, undiscounted net earnings from such properties between the interest of the explorer, discoverer, or prospector, and the interest of a developer or exploiter. In the determination of net earnings, deductions from anticipated gross income shall include not only the estimated direct operating costs attributable to the production of oil and/or

gas but also the estimated costs of drilling subsequent wells, general overhead, and any other deductions attributable to exploitation of the properties.

A method of determining abnormal income may be illustrated as follows: Assume that as of the date of discovery of a new pool, the estimated undiscounted net earnings from the taxpayer's properties are $1,250,000. Assume further that these properties could be subleased on a 40-60 basis (i. e. 40% of the estimated net earnings attributed to the sublessor and 60% to the sublessee). These are all facts with respect to the properties to be determined by expert analysis such as by a petroleum engineer. Under these assumptions, the sublessor's share of the total estimated net earnings is $500,000, and if the total estimated recoverable oil is 1,000,000 barrels, 50 cents of the income realized from each barrel of oil will be the income resulting from exploration, discovery, and prospecting (without regard to the ultimate amount of oil recovered from the property), and such 50 cents per barrel thus will represent abnormal income.

6. *Items of abnormal income.*—An item of abnormal income consists of the abnormal income, as defined above, attributable to a single discovery. Thus, the amount of an item of abnormal income in any taxable year is equal to that portion of the income, attributable to the discovery, realized in such taxable year from a particular oil and/or gas pool which is proved by a single discovery well. For the purposes of this Revenue Ruling, a "pool" means any underground accumulation of crude petroleum or associated hydrocarbon substances including, but not limited to, natural gas, constituting a single and separate reservoir or source of supply within a field. The probable limits of such new pool, as determined by the best evidence available at the date of completion of the discovery well, thus define the area within which all leases or properties owned at the time by the discoverer would be included in the discovery. Later discoveries of new pools in the same area may be made in different sands or horizons, and again the income attributable to the discovery of the new pool would be determined by the facts known as of the date of discovery. No adjustments will be made because of any subsequent information.

The abnormal income of a taxpayer for any year, either the current taxable year or one of the 4 prior taxable years, consists of the sum of the items of abnormal income, as defined above, from all discovery units of the taxpayer yielding such income in the given year.

7. *Net abnormal income attributable to other years.*—Net abnormal income, and items of net abnormal income, are to be determined as provided in Regulations 130, section 40.456–1. With respect, however, to the reduction for costs or deductions relating to the abnormal income called for by sections 40.456–1 (c)(3) and (d)(2), these costs and deductions, other than the depletion allowable, are zero, since it is the expected *net* realization from anticipated production that is reflected in the sublessor's share of anticipated net earnings (50 cents per barrel of oil in the example given in paragraph 5) which is used to measure abnormal income. The amount of the depletion allowance relating to the abnormal income with respect to each item is an amount equal to the depletion deduction multiplied by the ratio of

abnormal income to the net income before depletion. (The depletion allowance relating to the class of abnormal income is the sum of the depletion allowances relating to all of the items constituting the class.)

The amounts of net abnormal income attributable to other years are to be determined as provided in section 40.456-3. Any net abnormal income due to an increase in demand for oil or gas, as shown by appropriate sales or consumption data, is not attributable to other years, but to the current taxable year. Similarly, any net abnormal income due to increased prices is not attributable to other years; but if abnormal income has been determined by the method shown in the illustration in paragraph 5 above, or by any other method not involving fluctuating prices, then no net abnormal income so determined will be attributable to the current taxable year by virtue of such increased prices.

Each item of net abnormal income attributable to other years is attributable to the years of exploration, discovery, or prospecting for such item in proportion to the ratio of expenditures for these activities in each such year to their total for all years.

8. *Example.*—The following example will illustrate some of the principles and methods described above. The example concerns only the petroleum extraction phases of the operations of a company which may also operate a refinery or have other activities. The M Oil Company during the taxable year 1952 and prior years sold oil, or transferred oil to its refineries at market prices, from its various properties as follows:

Item A, discovered by the taxpayer in 1935 after more than 12 months' exploration; sublessor's share of anticipated net earnings $400,000; estimated reserves 1 million barrels (result, 40¢ per bbl.); average annual production 1948–51, 50,000 barrels; reserves exhausted in 1949;

Item B, discovered by the taxpayer in 1948 after more than 12 months' exploration; sublessor's share of anticipated net earnings $500,000; estimated reserves 1 million barrels (result, 50¢ per bbl.); average annual production 1948–51, 50,000 barrels; 1952 production 80,000 barrels;

Item C, discovered by the taxpayer in 1950 after more than 12 months' exploration; exploration and discovery costs $40,000 in 1949 and $80,000 in 1950; sublessor's share of anticipated net earnings $600,000; estimated reserves 1 million barrels (result, 60¢ per bbl.); average annual production 1948–51, 10,000 barrels; 1952 production 90,000 barrels;

Property D, acquired from others in 1940 after discovery; average production 1948–51, 150,000 barrels; 1952 production 200,000 barrels.

Total assumed average annual production 1948–51, 260,000 barrels; 1952 total production 370,000 barrels. Assume the market price of oil in 1952 was $2.50 per barrel. Assume also that countrywide data on oil consumption and exports show that in 1952 the demand was 10 percent higher than the average of the 4 prior years.

Under the assumed facts, the net abnormal income computations as shown herein ensue.

M Oil Company, petroleum operations, taxable year 1952

I. Net income computations	Item A	Item B	Item C	Prop. D		Total
a. Sales of oil (at $2.50 per bbl.)	0	200, 000	225, 000	500, 000	add	925, 000
b. Production costs (including, in case of item C, intangible drilling costs incurred in connection with exploitation in 1952)	0	40, 000	125, 000	100, 000	add	265, 000
c. Net income before depletion allowance	0	160, 000	100, 000	400, 000	add	660, 000
d. Depletion allowance (27½% of gross in items B and D, 50% of net in item C)	0	55, 000	50, 000	137, 500	add	242, 500
e. Net income after depletion allowance	0	105, 000	50, 000	262, 500		417, 500
II. Net abnormal income computation						
f. Abnormal income in 1952 (1952 production of each item times amount of abnormal income per barrel)	0	40, 000	54, 000	None	add	94, 000
g. 115% of abnormal income in 4 prior years (average 1948–51 production of each item times amount per bbl.)	23, 000	28, 750	6, 900	None	add	58, 650
h. Excess of line f over line g	0	11, 250	47, 100	None	(*)	35, 350
i. Percent of depletion allowance relating to abnormal income (f/c)		25%	54%			
j. Depletion allowance relating to abnormal income (i×d)	0	13, 750	27, 000		add	40, 750
k. Percent of depletion allowance allocable to excess over 115% (h/f)		28. 125%	87. 222%	Items B and C	(*)	37. 606%
l. Amount of depletion allowance allocable to excess over 115% (k×j)		3, 867	23, 550		(*)	15, 324
m. Net abnormal income, item and class (h—l)		7, 383	23, 550	add 30,933	(*)	20, 026
n. Percent items are of their total (m/30, 933)		23. 868%	76. 132%	add 100%		
o. Net abnormal income total (class) allocated to items by percents in line n		4, 780	15, 246			20, 026

III. Attribution of net abnormal income to years of exploration and discovery	Item B	Item C	Attributable to taxable year	
			1949 and prior	1950
o. (Repeated) Net abnormal income	4, 780	15, 246		
p. Amount attributable to increased prices (see par. 7)	0	0		
q. Business improvement factor assumed (volume)	1. 10	1. 10		
r. Amount attributable to business improvement (line o times .10/1.10)	434	1, 386		
s. Net abnormal income attributable to years of exploration and discovery (o—r)	4, 346	13, 860		
t. Item B all attributable to 1948 and prior years of exploration and discovery			4, 346	----------
u. Item C attributable to 1949 and 1950 in proportions of $40,000 and $80,000, assumed as 1949 and 1950 expenditures on exploration and discovery			4, 620	9, 240
v. Net abnormal income, by years to which attributable			8, 966	9, 240

*Do not add horizontally.

NOTE.—If any of the Items A, B, or C in the above example is comprised of two or more properties, then the various amounts (such as income, production costs, depletion allowance, etc.) shown with respect to such item are the aggregates of the applicable amounts with respect to each of the several properties comprising the item.

SECTION 459(d).—MISCELLANEOUS PROVISIONS: TELEVISION BROADCASTING COMPANIES

REGULATIONS 130, SECTION 40.459(d)-1: Television broadcasting companies. T. D. 6054

(Also Sections 40.459(d)-2, 40.459(d)-3, 40.459(d)-4, 40.459(d)-5, 40.459(d)-6, 40.459(e)-1; Section 435, Sections 40.435-6, 40.435-7.)

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER A, PART 40.—EXCESS-PROFITS TAX; TAXABLE YEARS ENDING AFTER JUNE 30, 1950

Regulations 130 amended to conform to section 519 of the Revenue Act of 1951, relating to television broadcasting companies.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

On December 13, 1952, a notice of proposed rulemaking was published in the Federal Register [17 F. R. 11347] to conform Regulations 130 [26 CFR, pt. 40] to section 519 of the Revenue Act of 1951, approved October 20, 1951. After consideration of such relevant suggestions as were presented regarding the proposals, the amendments set forth below are hereby adopted.

PARAGRAPH 1. Section 40.435-6(a)(1) is amended by inserting at the end thereof the following new sentence:

In the case of a taxpayer engaged in the television broadcasting business which computes its average base period net income under section 459(d), see section 40.459(d)-5(c).

PAR. 2. Section 40.435-7(a)(2) is amended by inserting at the end thereof the following new sentence:

For rules applicable in the case of a taxpayer engaged in the television broadcasting business which computes its average base period net income under section 459(d), see section 40.459(d)-5(d).

PAR. 3. There is inserted immediately after section 40.459(c)-1(d)(4) the following:

SEC. 519. TELEVISION BROADCASTING COMPANIES [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

Section 459, as added by sections 516 to 518 of this Act, is hereby amended by adding after subsection (c) thereof the following new subsections:

"(d) TELEVISION BROADCASTING COMPANIES.—

"(1) IN GENERAL.—In the case of a taxpayer engaged in the business of television broadcasting throughout a period beginning before January 1, 1951, and ending with the close of the taxable year, the taxpayer's average base period net income determined under this subsection shall be the amount computed under paragraph (2) or (3), whichever is applicable.

"(2) IF ENGAGED IN TELEVISION BROADCASTING AT CLOSE OF BASE PERIOD.—If the taxpayer was engaged in the business of television broadcasting at the close of its base period, the average base period net income computed under this paragraph shall be computed as follows:

"(A) If the taxpayer was engaged during its base period in any business or businesses other than television broadcasting, by computing the average base period net income under section 435(d) for such other business or businesses (determined without regard to income, deductions, losses, or other items attributable to the television broadcasting business).

"(B) By multiplying such part of its total assets (as defined in section 442(f)) for the last day of its base period, as was attributable to the television broadcasting business by—

"(i) the base period rate of return determined under section 447(c) for the industry classification which includes radio broadcasting, or

"(ii) if the taxpayer was engaged during its base period in the business of radio broadcasting, its individual rate of return computed under paragraph (4),

whichever rate of return produces the greater average base period net income under this subsection. If the amount computed under this subparagraph is computed by the use of the rate of return specified in clause (i), the amount so computed shall be reduced by an amount equal to such portion of the total interest paid or incurred by the taxpayer, for the period of 12 months following the close of its base period, as is attributable to its television broadcasting business.

"(C) By adding the amount computed under subparagraph (B) to the amount, if any, computed under subparagraph (A).

"(3) COMMENCING TELEVISION BROADCASTING AFTER BASE PERIOD AND BEFORE 1951.—If the taxpayer acquires its television broadcasting business after the close of its base period and before January 1, 1951, the average base period net income computed under this paragraph shall be computed as provided in paragraph (2), except that—

"(A) the applicable rate of return under paragraph (2)(B) shall be multiplied by such part of its total assets (as defined in section 442(f)), for the last day of the calendar month in which it first engaged in such business, as was attributable to such business, and

"(B) the reduction specified in the last sentence of paragraph (2) (B) shall, if applicable, be equal to such portion of the total interest paid or incurred by the taxpayer, for the period of 12 months following the month in which it first engaged in such business, as is attributable to such business.

"(4) INDIVIDUAL RATE OF RETURN.—The individual rate of return shall be computed as follows:

"(A) By determining the amount of the taxpayer's total assets (as defined in section 442(f) attributable to the business of radio broadcasting for the last day of each month in its base period.

"(B) By computing the aggregate of the amounts ascertained under subparagraph (A) and dividing by 48.

"(C) By computing for each month in the base period the excess profits net income of the radio broadcasting business (determined without regard to income, deductions, losses, or other items attributable to any other business), by adding such amounts for all of the months in the base period, and by dividing by 4.

"(D) By dividing the amount computed under subparagraph (C) by the amount computed under subparagraph (B).

"(5) RULES FOR APPLICATION OF SUBSECTION.—

"(A) For the purpose of section 435(a)(1)(B), an average base period net income determined under this subsection shall be considered an average base period net income determined under section 435(d); but, in computing the base period capital addition under section 435(f), the computations under such section shall be adjusted, under regulations prescribed by the Secretary, so as to exclude therefrom items attributable to the television broadcasting business.

"(B) If any part of the total assets referred to in paragraph (2)(B) or paragraph (3)(A), whichever is applicable, were acquired, directly or indirectly, through the use of assets attributable at any time during the base period to a business of the taxpayer other than television broadcasting, the amount determined under paragraph (2)(A) shall be properly adjusted by eliminating from the excess profits net income (computed for the purpose of paragraph (2)(A)) for each month prior to such acquisition such portion thereof as is attributable to the assets used, directly or indirectly, for such acquisition. For the purpose of this subparagraph, the excess profits net income for any month shall be attributed to such assets on the basis of the ratio, as of the beginning of the day of the acquisition, of such assets to total assets (as defined in section 442(f)) determined without regard to assets attributable to the television broadcasting business.

"(C) The Secretary shall by regulations prescribe rules for the application of this subsection, including rules for the computation of the taxpayer's net capital addition or reduction.

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SEC. 523. EFFECTIVE DATE OF TITLE V [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

Except as otherwise provided in section 506(d), the amendments made by this title [including sec. 519] shall be applicable only with respect to taxable years ending after June 30, 1950.

SEC. 40.459(d)-1. TELEVISION BROADCASTING COMPANIES—IN GENERAL.—(a) A corporation which was engaged in the business of television broadcasting throughout a period beginning before January 1, 1951, and ending with the close of an excess profits tax taxable year may compute its average base period net income for the purpose of determining its excess profits tax for such taxable year under section 459(d) instead of under any other applicable provision of the Code. The average base period net income computed under section 459(d) shall be the amount computed under paragraph (2) of section 459(d) and under section 40.459(d)-2 if the taxpayer was engaged in the business of television broadcasting at the end of its base period, and shall be the amount computed under paragraph (3) of section 459(d) and under section 40.459(d)-3 if the taxpayer did not acquire its television broadcasting business until after the close of its base period. In no event shall the benefit of section 459(d) be available, however, unless the taxpayer was engaged in the television broadcasting business before January 1, 1951. The amount determined as the average base period net income under section 459(d) shall be used as the average base period net income in computing the excess profits tax for any taxable year ending after June 30, 1950, if the taxpayer continued in the business of television broadcasting through the end of such taxable year, and if the use of such amount computed under section 459(d) as the average base period net income would result in a lesser excess profits tax for such taxable year than would result under any other allowable computation of such tax.

(b) A taxpayer which does not actually broadcast television will not be considered to be engaged in the television broadcasting business even though it is engaged in a business which is related to television broadcasting, such as advertising, the manufacturing of television equipment, or the preparation and sale of television programs. A taxpayer which is engaged in the television broadcasting business and also in any other business or businesses, however, may be entitled to the benefit of section 459(d).

SEC. 40.459(d)-2. COMPUTATION OF AVERAGE BASE PERIOD NET INCOME IF TAXPAYER WAS ENGAGED IN TELEVISION BROADCASTING AT CLOSE OF BASE PERIOD.—If the taxpayer was engaged in the business of television broadcasting at the close of its base period, its average base period net income determined under section 459(d) shall be computed as follows:

(a) If the taxpayer was engaged during its base period in any business or businesses other than television broadcasting, its average base period net income for such other business or businesses shall be computed under section 435(d) and section 40.435-1(d), relating to the computation of average base period net income under the general average method. The determination of the average base period net income of such business or businesses other than

television broadcasting shall be made without regard to any income, deductions, losses, or other items which are attributable to the television broadcasting business. See section 40.459(d)-5(a). If the taxpayer was not engaged during its base period in any business other than television broadcasting, the amount determined under this paragraph shall be zero. See section 40.459(d)-5(b) for adjustment of the amount computed under this paragraph where assets attributable to the television broadcasting business were acquired, directly or indirectly, through the use of assets attributable at any time during the base period to a business other than the television broadcasting business.

(b) Such part of the taxpayer's total assets for the last day of its base period as was attributable to the television broadcasting business shall be multiplied—

(1) by the base period rate of return determined under section 447(c) for the industry classification which includes radio broadcasting, and the amount so determined shall then be reduced by an amount equal to such portion of the total interest paid or incurred by the taxpayer for the period of 12 months following the close of its base period as is attributable to its television broadcasting business, or

(2) if the taxpayer was engaged during its base period in the business of radio broadcasting, by its individual rate of return computed under section 459(d)(4) and section 40.459(d)-4,

whichever produces the greater average base period net income under section 459(d) and this section.

(c) The amount, if any, computed under section 459(d)(2)(A) and under (a) of this section shall be added to the amount computed under section 459(d)(2)(B) and under (b) of this section.

The amount determined under (c) of this section—that is, the total of the amounts determined under (a) and (b) of this section—shall be the average base period net income computed under section 459(d) of a taxpayer which was engaged in the television broadcasting business at the close of its base period.

SEC. 40.459(d)-3. COMPUTATION OF AVERAGE BASE PERIOD NET INCOME IF TAXPAYER COMMENCED TELEVISION BROADCASTING AFTER CLOSE OF BASE PERIOD AND BEFORE 1951.—If the taxpayer did not acquire its television broadcasting business until after the close of its base period (but before January 1, 1951), its average base period net income determined under section 459(d) shall be computed in the same manner as provided in section 459(d)(2) and section 40.459(d)-2 as in the case of a taxpayer which was engaged in the television broadcasting business at the close of its base period, except that—

(a) the applicable rate of return specified in section 459(d)(2)(B) and section 40.459(d)-2(b) shall be multiplied by such part of the taxpayer's total assets for the last day of the calendar month in which it first engaged in the television broadcasting business (instead of for the last day of its base period) as was attributable to such television broadcasting business; and

(b) the reduction for interest specified in the last sentence of section 459(d)(2)(B) and in section 40.459(d)-2(b)(1) shall, if applicable, be equal to that portion of the total interest paid or incurred by the taxpayer for the period of 12 months following the month in which it first engaged in the television broadcasting business (instead of for the period of 12 months following the close of its base period) as is attributable to such television broadcasting business.

SEC. 40.459(d)-4. INDIVIDUAL RATE OF RETURN.—The individual rate of return, for the purpose of the computations provided in sections 459(d)(2)(B)(ii) and 40.459(d)-2(b)(2) and in sections 459(d)(3)(A) and 40.459(d)-3(a), in the case of a taxpayer which was engaged in the business of radio broadcasting during its base period, shall be computed as follows:

(a) The taxpayer's total assets attributable to its radio broadcasting business for the last day of each month in its base period shall be determined. See section 40.459(d)-5(a) for rules for the determination of the business to which assets are attributable.

(b) The amounts determined under (a) of this section shall be added together and the aggregate divided by 48.

(c) The excess profits net income for each month in the base period attributable to the radio broadcasting business shall be computed, such excess profits net income being determined without regard to income, deductions, losses, or any other items attributable to any business other than the radio broadcasting business (see section 40.459(d)-5(a)). Such amounts of

excess profits net income attributable to the radio broadcasting business for each month in the base period shall be added together and the total of such amounts then divided by 4. The excess profits net income for any month attributable to the radio broadcasting business, for the purpose of (c) of this section, shall be the excess profits net income or deficit in excess profits net income, as the case may be, attributable to such business for the taxable year in which such month falls divided by the number of calendar months in such year.

(d) The amount computed under (c) of this section shall be divided by the amount computed under (b) of this section. That is, the aggregate, divided by 4, of the excess profits net income attributable to the radio broadcasting business for each month in the base period shall be divided by the aggregate, divided by 48, of the taxpayer's total assets attributable to the radio broadcasting business for the last day of each month in the base period. The resulting figure shall be the taxpayer's individual rate of return.

SEC. 40.459(d)-5. RULES FOR APPLICATION OF SECTION 459(d).—(a) *Determination of business to which items are attributable.*—(1) the determination, for the purpose of section 459(d) and sections 40.459(d)-1 through 40.459(d)-5, whether any income, deductions, losses, interest, assets, or any other items are attributable to the television broadcasting business, to the radio broadcasting business, or to any other business shall be made in such manner as will clearly reflect the income attributable to each such business, and, in the case of assets, will reflect the extent to which assets are used in, or devoted to, the businesses of the taxpayer. Administrative expenses, for example, in the case of a taxpayer which is engaged in the television broadcasting business and also in some other business or businesses may not be attributed to any one business but shall be properly allocated among the various businesses of the taxpayer. If an asset is used in or devoted to the television broadcasting business, or the radio broadcasting business, and also some other business, such asset shall not be included at an amount equal to its full adjusted basis in determining at any time the total assets of the taxpayer which are attributable, as the case may be, to the television broadcasting business or to the radio broadcasting business. In such case, proper adjustment shall be made to reflect the fact that such asset directly or indirectly is used in or devoted to, or is part of, the television broadcasting business, the radio broadcasting business, or some other business. Similarly, proper adjustment shall also be made in the case of any other items (including, for example, interest) as are attributable to more than one business.

(2) (i) For the purpose of the adjustment provided in section 459(d)(5)(B) and in (b) of this section, for the purpose of computing the individual rate of return provided in section 459(d)(4), and for the purpose of computing an average base period net income under section 459(d)(2)(A) for the business or businesses of the taxpayer other than the television broadcasting business, if cash or other liquid assets were in fact set aside pursuant to a resolution of the board of directors of the taxpayer or other corporate action for the purpose of acquiring assets to be used in the television broadcasting business, the setting aside of such assets shall be considered the acquisition, on the date the assets were set aside, of assets attributable to the television broadcasting business.

(ii) The rules provided in (i) shall also apply to cash or other liquid assets not so set aside to the extent that the taxpayer establishes to the satisfaction of the Commissioner that such cash or other liquid assets were held for the purpose of acquiring assets to be used in the television broadcasting business (for example, through designation in the accounting records of the taxpayer) and that such cash or other liquid assets had no material effect upon the excess profits net income during the base period of the business or businesses of the taxpayer other than television broadcasting. Such cash or other liquid assets shall be deemed to have been set aside for the purpose of acquiring assets to be used in the television broadcasting business on the date which the taxpayer so establishes as the date that such cash or other liquid assets were first held for this purpose.

(iii) The rules provided in (i) and (ii) shall not apply to any assets therein described which were used for a purpose other than that for which they were set aside.

(b) *Adjustment of average base period net income of business other than television broadcasting business.*—(1) If any part of the total assets attributable to the television broadcasting business which were held by the taxpayer on the date as of which the applicable rate of return is to be applied to its television broadcasting assets was acquired, directly or indirectly, through the use of assets which were attributable at any time during the base period to a business of the

taxpayer other than the television broadcasting business, an adjustment, as provided in section 459(d)(5)(B), must be made in determining under section 459(d)(2)(A) the average base period net income, if any, of the taxpayer's nontelevision broadcasting business or businesses. See (3) below for rules with respect to the circumstances in which such adjustment is required. The conversion in whole or in part of assets attributable to a business other than the television broadcasting business to use in the television broadcasting business shall be considered for the purpose of section 459(d) and of this section, to the extent of such conversion, to be an acquisition of television broadcasting assets by the use of assets attributable to a business of the taxpayer other than its television broadcasting business. In determining the extent of such conversion, appropriate allowance shall be made for offsetting effects of conversion in whole or in part of assets attributable to the television broadcasting business to use in a business other than the television broadcasting business.

(2) If an adjustment is required under the provisions of section 459(d)(5)(B) and of (b) of this section with respect to any acquisition of assets attributable to the television broadcasting business, then in determining the average base period net income under section 459(d)(2)(A) of such nontelevision broadcasting business or businesses there shall be excluded from the excess profits net income for each month prior to any such acquisition such portion of such excess profits net income as is attributable to the assets used, directly or indirectly, for such acquisition. In determining the amount which is to be excluded from the excess profits net income for any month, under the provisions of section 459(d)(5)(B) and of (b)(2) of this section, the part of the excess profits net income attributable to any assets which were used, directly or indirectly, to acquire assets attributable to the television broadcasting business shall be determined on the basis of the ratio, as of the beginning of the date of acquisition, of such assets which were so used to the total assets of the taxpayer other than its assets attributable to the television broadcasting business. If the acquisition took place on any day other than the first day of a calendar month, the adjustment for the month in which the acquisition took place shall be reduced to an amount determined on the basis of the ratio of the number of days in such month prior to the day on which the acquisition was made to the total number of days in such month.

(3) The adjustment provided in section 459(d)(5)(B) and in (b) of this section is required in any case in which an average base period net income for a business or businesses of the taxpayer other than its television broadcasting business is computed under section 459(d)(2)(A) except to the extent that television broadcasting assets were acquired by the taxpayer through a bona fide long-term increase in its capital structure made in conjunction with and for the purpose of such acquisition. A bona fide long-term increase in the capital structure within the meaning of (b)(3) of this section (whether an increase in equity capital or in borrowed capital as defined in section 439(b)) shall be deemed to have occurred only to the extent that such increase is reflected in the capital structure throughout the period beginning with the time such increase was originally made and ending with the close of the taxable year for which the tax is being computed. For the purpose of determining whether such increase is reflected in the capital structure, proper adjustment shall be made to eliminate the effect of any loss occurring after the original increase is made, and, in the case of such determination as of any time during a taxable year, the determination shall be made without regard to the earnings and profits of such taxable year. If the increase in the capital structure is the result of a part II transaction, (b)(3) of this section and section 40.462-9(b)(1)(ii) shall be applied in the light of the facts applicable both to the taxpayer and to the component corporation in such transaction. For the purpose of (b)(3) of this section, an increase in the capital structure does not result from the conversion of inadmissible assets into admissible assets or from the accumulation of earnings and profits prior to the beginning of the first taxable year which begins after the date of the acquisition. If the assets of the television broadcasting business were acquired partly in the manner described in (b)(3) of this section and partly in another manner the adjustment shall be made to the extent the acquisition was made in such other manner.

(c) *Computation of base period capital addition.*—The average base period net income under section 459(d) shall be considered, for the purpose of section 435(a)(1)(B), to be an average base period net income computed under section 435(d) which provides for the computation of the average base period net income under the general average method. The base period capital addition

provided in section 435(f) accordingly will be allowed in any case in which the average base period net income computed under section 459(d) is used in determining the excess profits tax for any excess profits tax taxable year, but such base period capital addition shall be allowed only with respect to the taxpayer's business or businesses other than its television broadcasting business. The following rules shall be applicable in computing the base period capital addition in the case of a taxpayer which computes its average base period net income under section 459(d):

(1) In computing the yearly base period capital as of any day, there shall be excluded from each item in the computation (such as assets, liabilities, borrowed capital, or the adjustment for interest) any amount attributable or allocable to the assets of the television broadcasting business held on such day.

(2) If an adjustment is required to be made under section 459(d)(5)(B) with respect to assets of the taxpayer used directly or indirectly to acquire television broadcasting assets, the amount of the adjusted basis of assets with respect to which such adjustment is required shall be excluded from assets of the taxpayer in computing equity capital as of any day prior to such acquisition. Such further adjustments shall be made in computing other items (such as liabilities, borrowed capital, or the adjustment for interest) in the determination of yearly base period capital as of such day as are, under generally accepted accounting principles, consistent with the elimination of such amount from total assets.

(3) In making computations necessary for the determination of yearly base period capital for any taxable year, such computations shall be made, under the rules and principles set forth in (a) of this section, in the light of all the facts of the particular case and consistent with the purpose of restricting the base period capital addition to the business or businesses of the taxpayer other than its television broadcasting business and the avoidance of any duplication in the computation of such base period capital addition.

(d) *Computation of net capital addition or reduction.*—(1) In the case of a taxpayer which was engaged in the business of television broadcasting at the close of its base period, the net capital addition or reduction, provided in section 435(g), shall be computed in the same manner as in the case of any taxpayer which computes its average base period net income under the general average method provided in section 435(d). See sections 40.437-6 and 40.437-7.

(2) In the case of a taxpayer which did not acquire its television broadcasting business until after the close of its base period (but before January 1, 1951), the net capital addition or reduction, provided in section 435(g), shall be determined in the same manner as in the case of any taxpayer which computes its average base period net income under the general average method provided in section 435(d) (see sections 40.437-6 and 40.437-7), except that the following adjustment shall be made:

(i) There shall be determined the amount of any proceeds obtained from borrowing, from the issuance of capital stock, as paid-in surplus, as a contribution to capital, or in any other manner, on or after the first day of the taxpayer's first taxable year ending after June 30, 1950, and before the first day of the first calendar month following the calendar month in which the taxpayer first engaged in the television broadcasting business.

(ii) There shall be determined the excess of (*a*) the amount of the taxpayer's assets attributable to the television broadcasting business as of the last day of the calendar month in which the taxpayer first engaged in the television broadcasting business over (*b*) the amount of the taxpayer's assets with respect to which an adjustment is required under the provisions of section 459(d)(5)(B) and of (b) of this section.

(iii) The amount determined under (i), but not more than the amount determined under (ii), shall be considered, for the purpose of any computations necessary for the determination of the net capital addition or reduction, to have been obtained prior to the first day of the taxpayer's first taxable year ending after June 30, 1950.

SEC. 40.459(d)-6. DEFINITIONS.—For the purpose of section 459(d) and sections 40.459(d)-1 through 40.459(d)-5—

(a) The term "total assets" shall have the same meaning as in sections 442(f) and 40.442-3(d)(1).

(b) The "amount of an asset" in the case of property other than money shall be an amount equal to the adjusted basis of such property for determining gain on the sale or exchange thereof, and in the case of money shall be the amount thereof.

SEC. 519. TELEVISION BROADCASTING COMPANIES [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

Section 459, as added by sections 516 to 518 of this Act, is hereby amended by adding after subsection (c) thereof the following new subsections:

* * * * * * *

"(e) BASIS OF ASSETS.—For the purposes of this section, any reference to the adjusted basis of property or to the basis (unadjusted) of property means the adjusted basis or the basis (unadjusted), as the case may be, for determining gain upon sale or exchange."

SEC. 523. EFFECTIVE DATE OF TITLE V [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

Except as otherwise provided in section 506(d), the amendments made by this title [including sec. 519] shall be applicable only with respect to taxable years ending after June 30, 1950.

SEC. 40.459(e)-1. BASIS OF ASSETS.—For the purpose of section 459 (including all subsections thereof) and the regulations thereunder, any reference to the adjusted basis of property or to the basis (unadjusted) of property means the adjusted basis or the basis (unadjusted), as the case may be, of such property for determining gain upon the sale or exchange thereof.

(This Treasury Decision is issued under the authority contained in sec. 62 of the Internal Revenue Code (53 Stat. 32; 26 U. S. C. 62) and in sec. 459(d) of the Internal Revenue Code as added by sec. 519 of the Revenue Act of 1951 (Public Law 183, 82d Cong., approved October 20, 1951).)

T. COLEMAN ANDREWS,
Commissioner of Internal Revenue.

Approved November 27, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register December 2, 1953, 8:52 a. m.)

PART II.—EXCESS-PROFITS CREDIT BASED ON INCOME IN CONNECTION WITH CERTAIN EXCHANGES

SECTION 461.—DEFINITIONS

REGULATIONS 130, SECTION 40.461-2: Acquiring corporations.

INTERNAL REVENUE CODE

Requirements of adequate and separate records. (See Rev. Rul. 201, p. 251.)

REGULATIONS 130, SECTION 40.461-7: Provisions generally applicable under Part II. (Also Section 464, Section 40.464-1; Section 435, Section 40.435-6.) Rev. Rul. 186

The base period capital addition of a component corporation in a transaction described in section 461(a)(1)(E) of the Internal Revenue Code which occurred during the calendar year 1948 (the second preceding taxable year), shall be computed as though the component corporation were an acquiring corporation, and its yearly base period capital for the second preceding taxable year shall be determined as of the day following the transaction.

Advice is requested relative to the proper method of computing the base period capital addition of a component corporation in a transaction described in section 461(a)(1)(E) of the Internal Revenue Code relating to excess-profits credits based on income in connection with tax-free exchanges.

In 1948 the taxpayer corporation transferred cash to another corporation in return for all of its capital stock. In this transaction the corporation to which the cash was transferred became the "acquiring" corporation and the taxpayer became its "component," within the meaning of section 461 of the Code.

In computing the base period capital addition of the acquiring corporation, the yearly base period capital for the second preceding taxable year is to be determined as of the day following the transaction. See sections 435(f) and 464(b)(2) of the Code. The question presented is the proper date for determining the yearly base period capital for the second preceding taxable year of the component corporation in the computation of its base period capital addition under section 435(f) of the Code.

Part II of subchapter D of chapter 1 of the Code applies not only in the determination of that portion of the component corporation's experience which is available to an acquiring corporation after a splitup, but also to that portion of such experience which the component corporation (if it continues in existence) may use after the splitup. The principles applicable in determining the portion of experience retained are the same as the principles applicable in determining the portion of the experience transferred to the acquiring corporation. Section 40.461-7(c) of Regulations 130 provides that the excess-profits credit of a component corporation is a transaction described in section 461(a)(1)(E) of the Code shall be computed as though such component corporation were an acquiring corporation receiving in such transaction the properties which it in fact retained. See T. D. 5865, C. B. 1951-2, 97; and T. D. 6017, C. B. 1953-1, 364. This rule clarifies section 461(c) (3) and (4) of the Code as regards transaction where the average base period net income of the component corporation and base period capital addition is not already determined at the time of the transaction and makes certain the rights of such component corporations under section 435 (e), (f), and (g), and sections 442 through 446 of the Code.

In view of the foregoing, it is held that the base period capital addition of the component corporation is to be computed under section 435(f) of the Internal Revenue Code as though it were an acquiring corporation, and its yearly base period capital for the second preceding taxable year determined, as provided in section 464(b)(2) of the Code, as of the day following the transaction.

SECTION 462.—AVERAGE BASE PERIOD NET INCOME—DETERMINATION

REGULATIONS 130, SECTION 40.462-9: Allocation rules in the case of Part II transactions described in section 461(a)(1)(E).

INTERNAL REVENUE CODE

Requirements of adequate and separate records. (See Rev. Rul. 201, below.)

SECTION 464.—CAPITAL CHANGES DURING THE BASE PERIOD

REGULATIONS 130, SECTION 40.464-1: Base period capital additions under Part II.

INTERNAL REVENUE CODE

Date for determining yearly base period capital for second preceding taxable year of component corporation treated as acquiring corporation in case of part II transaction. (See Rev. Bul. 186, p. 249.)

PART IV.—EXCESS-PROFITS CREDIT BASED ON INCOME IN CONNECTION WITH CERTAIN TAXABLE ACQUISITIONS OCCURRING PRIOR TO DECEMBER 1, 1950

SECTION 474.—EXCESS-PROFITS CREDIT BASED ON INCOME—CERTAIN TAXABLE ACQUISITIONS

REGULATIONS 130, SECTION 40.474-1: Purpose and scope of Part IV. Rev. Rul. 201

(Also Section 461, Section 40.461-2; Section 462, Section 40.462-9.)

INTERNAL REVENUE CODE

Records of the predecessor which are sufficiently separate to permit a reasonable identification of the base period experience attributable to the properties acquired in a part II or part IV transaction will satisfy the requirements for adequate and separate records of sections 40.461-2(a)(4), 40.462-9(b)(1), and 40.474-1(b)(2) of Regulations 130.

Advice is requested whether records from which earnings attributable to a separate business unit can be ascertained, although such business unit records are not separate and independent from the records of other business units, are sufficient to meet the adequate and separate records requirement of sections 40.461-2(a)(4), 40.462-9(b)(1), and 40.474-1(b)(2) of Regulations 130.

For the purposes of each of these sections there is the requirement of the existence of a going business unit for which adequate and separate records were maintained. It is recognized that in many instances the records relating to a business unit may not be maintained completely separate and independent from the records of other business units

operated by the taxpayer, but that nevertheless, the earnings attributable to such business unit can be reasonably ascertained from the records available. The determination of the adequacy of the records available for such purpose must of necessity be a matter of case by case analysis.

It is not intended to require an absolute separation of all records pertaining to each business. In the case of a sole proprietorship no record of a salary for the sole proprietor is likely to be found. In the case of a corporation, administrative expenses and salaries of the president and other principal officers will ordinarily not be allocated to each business. In such cases an allocation and separation would generally be proper. On the other hand, where only the property accounts of the businesses are separately maintained, the test would not ordinarily be met. If the income and expense accounts are maintained separately but the property accounts are intermingled, the separateness of the income figures may be sufficient if the property accounts can be readily separated.

The requirement of sections 40.474–1(b)(2), 40.461–2(a)(4), and 40.462–9(b)(1) of Regulations 130, regarding adequate and separate records, may be met even though completely separate records have not been maintained if the records of the predecessor are adequate to permit a reasonable identification at all pertinent times of the base period experience attributable to the properties acquired in the part II or part IV transaction.

SUBCHAPTER E.—TAX ON SELF-EMPLOYMENT INCOME

SECTION 481.—DEFINITIONS

REGULATIONS 111, SECTION 29.481–1: Net earnings from self-employment.

INTERNAL REVENUE CODE

Regulations 111 amended. (See T. D. 6021, p. 169.)

CHAPTER 2.—ADDITIONAL INCOME TAXES

SUBCHAPTER A.—PERSONAL HOLDING COMPANIES

SECTION 500.—SURTAX ON PERSONAL HOLDING COMPANIES

REGULATIONS 111, SECTION 29.500–1: Surtax on personal holding companies.

INTERNAL REVENUE CODE

Application of delinquency penalty in case of failure to file Form 1120H. (See Rev. Rul. 172, p. 226.)

CHAPTER 3.—ESTATE TAX

SUBCHAPTER A.—BASIC ESTATE TAX

PART II.—ESTATES OF CITIZENS OR RESIDENTS OF THE UNITED STATES

SUBPART I.—COMPUTATION OF TAX

SECTION 811.—GROSS ESTATE

REGULATIONS 105, SECTION 81.10: Valuation of property.
(Also Section 822, Section 81.78.)

Rev. Rul. 156

INTERNAL REVENUE CODE

To the extent that marketable United States Treasury bonds owned by a decedent at death may be applied at par in payment of Federal estate taxes, the par value thereof or their mean quoted selling price at the time of his death (and accrued interest to the date of death), whichever is higher, constitutes the value at which such bonds are includible in his gross estate for Federal estate tax purposes. As to bonds in excess of the amount which may be so applied, their mean quoted price at the time of death (and accrued interest to the date of death) will be the value at which they are includible in the decedent's gross estate for Federal estate tax purposes.

Procedure, for effecting such application of the bonds, indicated.

Advice is requested as to valuation, for Federal estate tax purposes, of marketable United States Treasury bonds owned by a decedent which may be applied at par in payment of Federal estate taxes, and as to procedure for effecting such application of the bonds.

Various Treasury Department circulars provide that certain marketable (transferable and negotiable) and interest-bearing United States Treasury bonds, which upon the death of the owner constitute part of his gross estate, may be redeemed at the option of the duly constituted representatives of the deceased owner's estate at par value (face, principal, amount), plus accrued interest to the date of payment, provided that the bonds were owned by the decedent at the time of his death and that the Secretary of the Treasury be authorized to apply the entire proceeds of redemption to the payment of Federal estate taxes. A recent Treasury statement of the public debt indicates that the following issues of such Treasury bonds so redeemable are outstanding: 2¼ percent 1956–59 dated February 1, 1944; 2¼ percent 1959–62 dated June 1, 1945; 2¼ percent 1959–62 dated November 15, 1945; 2½ percent 1962–67 dated May 5, 1942; 2½ percent 1963–68 dated December 1, 1942; 2½ percent 1964–69 dated April 15, 1943; 2½ percent 1964–69 dated September 15, 1943; 2½ percent 1965–70 dated February 1, 1944; 2½ percent 1966–71 dated December 1, 1944; 2½ percent 1967–72 dated June 1, 1945; 2½ percent 1967–72 dated November 15, 1945; and 3¼ percent 1978–83 dated May 1, 1953.

In this connection it is to be noted that, where a bond is in a denomination too large for application of the entire proceeds in payment of

Federal estate taxes due from the estate of a deceased owner, denominational exchange will be permitted in order that bonds totaling the denominational amount (including accrued interest) next lower than the tax liability may be available for such purpose. For example, if a bond of the par value of $10,000 is to be applied in payment of a Federal estate tax liability of $6,800 and the lowest denomination in which such bonds are issued is $500, the bond will be redeemed to the extent of $6,500 par value for application toward payment of the tax liability. Bonds totaling $3,500 par value will be reissued for the amount of the bond in excess of the portion thereof ($6,500 par value) applied in payment of Federal estate tax.

The bonds should be submitted for redemption and application to payment of Federal estate tax by the decedent's executors or administrators to the Bureau of the Public Debt (Division of Loans and Currency), Treasury Department, Washington 25, D. C., directly or through a Federal Reserve bank (the bonds being not directly acceptable by a district director of internal revenue). Such Bureau has indicated that, in order to secure proper payment and credit, the bonds should reach it at least 3 full weeks before the date upon which credit to the district director's account is desired, although, unless otherwise requested, payment and credit will be made as soon as possible following receipt of the bonds. The Treasury Department circulars offering the bonds generally provide that they should be accompanied for such taxpayment redemption by Form PD 1782 properly completed, signed, and sworn to, and by a certificate of appointment of the representatives of the decedent's estate, under seal of court, dated not more than 6 months prior to the submission of the bonds and showing that at the time thereof the appointment was still in full force. Copies of Form PD 1782 may be obtained from the Bureau of the Public Debt or any Federal Reserve bank.

Section 811 of the Internal Revenue Code provides that "The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property * * *," and the regulations (section 81.10(*a*) of Regulations 105) provide that "The value of every item of property includible in the gross estate is the fair market value thereof at the time of the decedent's death; * * *." In the absence of any express provision to the contrary, it is clear that the includible "value," within the meaning of that term as used in the Code, is that which passes by virtue of the decedent's death and, hence, the words "at the time of his death" mean immediately upon, rather than before, death. For instance, a life estate may have substantial "value" during its owner's lifetime and yet nothing passes or arises in respect thereof by virtue of, or upon, his death. Also see *James E. Tyler, Jr., et al.*, v. *United States* (281 U. S. 497; Ct. D. 190, C. B. IX–1, 383, 385, 386 (1930)). In *Estate of Henry Hauptfuhrer, Deceased*, (Docket No. 17086, Tax Court Memorandum Opinion entered October 24, 1950), the Commissioner was sustained in the inclusion in gross estate, for Federal estate tax purposes, of the par value of United States savings bonds of Series G owned by the decedent at death and which, though not matured, were redeemable immediately upon his death at par (face amount, purchase price), and without refund by the bondholder of a portion of the interest previously realized thereon as would have been required if redeemed prior to

maturity during his lifetime (see I. T. 3504, C. B. 1941-2, 93). With respect to testimony of one of the petitioner's witnesses that, although the bonds were supposed to be worth face value at the time of the decedent's death, they were discounted by the Government because of delay either of a bank or employees of the Government in handling them, the court said: "The fact that a penalty may have been incurred for delay in presenting the bonds after the decedent's death could have no effect on their value at the date of death." Since Treasury bonds passing by the death of the owner are, to the extent that they may be applied at par in payment of Federal estate tax liability, immediately upon his death redeemable at par value for that purpose, it follows that the par value thereof or their mean quoted selling price at that time, whichever is higher, is their "value" or "fair market value" within the meaning of the statute and regulations. Section 81.10(*c*) of Regulations 105.

In view of the foregoing, it is held that to the extent marketable United States Treasury bonds owned by a decedent at death may be applied at par in payment of Federal estate taxes the par value thereof or the mean between their highest and lowest quoted selling price at the time of his death (and accrued interest to the date of death), whichever is higher, constitutes the value at which such bonds are includible in his gross estate for Federal estate tax purposes. As to bonds in excess of the amount which may be so applied, such mean quoted price thereof (and accrued interest to the date of death) will be the value at which they are includible in the decedent's gross estate for Federal estate tax purposes. Applying these rules to the above example, the portion of the $10,000 bond ($6,500) which may be applied at par in payment of Federal estate tax liability will be valued at $6,500 or the aforesaid mean quoted selling price thereof (and accrued interest to the date of death), whichever is higher, and the excess portion thereof ($3,500) will be included in the gross estate only at such mean quoted selling price thereof (and accrued interest to the date of death).

SECTION 811(a).—GROSS ESTATE: DECEDENT'S INTEREST

REGULATIONS 105, SECTION 81.10(*d*): Interest in business. (Also Section 81.10(*c*).) — Rev. Rul. 157

INTERNAL REVENUE CODE

Although the bylaws of a corporation contain a binding agreement, effective only upon a shareholder's death, providing for the sale to the corporation of the shareholder's interest in the business at a price which does not reflect consideration for goodwill, the Commissioner would not be precluded, for Federal estate tax purposes, from evaluating the shareholder's interest in the business to include goodwill.

Advice is requested whether, under the facts presented, in valuing a decedent's interest in a business for Federal estate tax purposes, an amount for goodwill should be added to the book value of the business.

In the instant case the bylaws of a corporation, in which the de-

cedent and another taxpayer each held 50 percent of the outstanding stock, provide that upon the death of a stockholder all of his stock shall, at the option of the board of directors if exercised within 30 days, become the property of the corporation to be paid for at such price as may be agreed upon by and between the corporation and the legal representative of the deceased as the fair value of such stock, or if an agreement cannot be reached then the corporation may purchase the stock at such price as may be determined as such fair value by a board of three appraisers. The bylaws further provide that in ascertaining the price to be paid for the stock, whether by agreement or appraisal, no allowance shall be made for the value of any goodwill possessed or claimed to be possessed by the corporation. These provisions are applicable only to the disposition of the stock after the death of either stockholder; they do not apply to the disposition of the stock by either shareholder during his lifetime.

Section 811(a) of the Internal Revenue Code provides in part that "the value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated, except real property situated outside the United States * * *," to the extent of the interest therein of the decedent at the time of his death.

Section 81.10(*d*) of Regulations 105, provides with respect to the valuation of property as follows:

(*d*) *Interest in business.*—Care should be taken to arrive at an accurate valuation of any business in which the decedent was interested, whether as partner or proprietor. A fair appraisal as of the applicable valuation date should be made of all the assets of the business, tangible and intangible, including good will, and the business should be given a net value equal to the amount which a willing purchaser, whether an individual or a corporation, would pay therefor to a willing seller in view of the net value of the assets and the demonstrated earning capacity. Special attention should be given to fixing an adequate figure for the value of the good will of the business in all cases in which the decedent has not agreed, for an adequate and full consideration in money or money's worth, that his interest therein shall pass at his death to his surviving partner or partners.

The factors hereinbefore stated relative to the valuation of other property, if applicable, will be considered in determining the valuation of an interest in a business held as proprietor or partner. All evidence bearing upon such valuation should be submitted with the return, including copies of reports in any case in which examinations of the business have been made by accountants, engineers, or any technical experts as of or near the applicable valuation date.

In the case under consideration the bylaws of the corporation do not purport to fix the price at which the corporation may purchase the shares of a deceased stockholder. They merely provide that the corporation may purchase the stock at its fair value, as agreed upon by the corporation and the legal representatives of the deceased, and if an agreement cannot be reached then the corporation may purchase at such price as may be determined as such fair value by a board of three appraisers, excluding any allowance for goodwill.

In the *Estate of George Marshall Trammell* v. *Commissioner*, 18 T. C. 662, the decedent was in business as an equal partner with his wife and the partnership agreement contained the following provision:

In the event this agreement is terminated by the death or inability to act of either of said partners, it is expressly agreed that the surviving partner may continue the business as theretofore, and buy out the business of such partner, by

paying therefor the reasonable value of the partner's property as may be determined from the books of the partnership, *paying nothing for good will*, and taking into account depreciation, etc. [Italics supplied.]

The court there held that while the provision in the partnership agreement, that the surviving partner may purchase a deceased partner's share without paying for goodwill, is binding upon the parties to the agreement, such provision is not binding upon the Commissioner in fixing valuations for estate tax purposes. Consequently, in valuing the deceased partner's interest, the court determined that goodwill value should be included in addition to mere book value. In the valuation of such goodwill the court considered several factors, including the earning record of the business for several years, the business location, the reputation for fair dealing, the type of clientele, quality of merchandise, amount and kind of advertising, and public esteem. The Trammell case involved a partnership consisting of two partners whereas the instant case involves a corporation owned equally by two stockholders. That distinction is not deemed material.

In view of the foregoing, it is held that although the bylaws of a corporation contain a binding agreement, effective only upon a shareholder's death, providing for the sale to the corporation of the shareholder's interest in the business at a price which does not reflect consideration for goodwill, the Commissioner would not be precluded, for Federal estate tax purposes, from evaluating the shareholder's interest in the business to include goodwill.

REGULATIONS 105, SECTION 81.13: Property of decedent at time of death. Rev. Rul. 293

INTERNAL REVENUE CODE

In determining the net value of the assets of an inter vivos trust created by the decedent and included in his gross estate, allowance should be made for the amount of attorney's fees incurred in connection with the usual issues involved in a trust accounting made necessary by the decedent's death.

Advice is requested in view of the decision in *Emma P. Abbett et al.* v. *Commissioner* (17 T. C. 1293, acquiescence C. B. 1952-2, 1), whether the value of an inter vivos revocable trust includible in the gross estate for Federal estate tax purposes may be reduced by the amount of an attorney's fee paid in connection with the usual issues involved in a trustee's accounting or whether such fee is properly deductible as an administration expense under section 812(b) of the Internal Revenue Code.

In the instant case, the decedent establishd an inter vivos revocable trust which provided that the income therefrom was to be paid to him for the duration of his life, and that following his death the trustee was to pay to the executor the funds necessary for the administration of the estate and retain the balance in further trust for certain named beneficiaries. The net value of the trust is subject to Federal estate tax under section 811(c)(1)(B) and/or section 811(d) of the Code. The corpus of the trust was included in the estate tax return reduced by an amount representing an attorney's fee incurred in connection with an accounting made by the trustee. The applicable State court allowed such fee as proper in the administration of the decedent's affairs.

In the Abbett case, *supra*, the trust instrument provided, as of the date of the decedent's death, that the trust was irrevocable, that the life income was payable to the decedent with several remainders over, and that on the decedent's death his two sons should become cotrustees with the corporate trustee. The Tax Court of the United States stated that although an accounting was not specifically required by the statutory law of the State, it was necessitated and required by orderly procedure so that the corporate trustee might account before it assumed to function with cotrustees. The court allowed as a deduction from the decedent's gross estate that portion of the expenses incurred by the corporate trustee for attorney's fees and guardian's fees which were attributable to the settlement of the usual issues involved in a trust accounting and allowed by the proper State court.

Although the Tax Court in the Abbett case stated that the attorney's fees paid by the trustee for the trust accounting were deductible as administration expenses under section 812(b) of the Code, that was not the real issue in the case. The Commissioner contended that the net taxable estate should not be reduced by the attorney's fees either as a reduction in the value of the trust property or as a deduction from the gross estate as an administration expense. The taxpayer contended for one or the other. Thus, the issue there involved and the issue raised here are different.

In the case of the *Estate of Elizabeth W. Haggart et al.* v. *Commissioner*, 182 Fed. (2d) 514, the facts were similar to those in the case here under consideration except that the decedent's residuary testamentary estate was to be added to the corpus of the trust and upon the death of the decedent a designated individual was to become a cotrustee. In its decision allowing a deduction for attorney's fees paid in connection with a court accounting, the court stated:

> Whether they [attorney fees and other expenses] are to be allowed as expenses of administration or whether they are to be allowed in diminution of the gross estate does not matter in this case. It comes out the same either way and, therefore, we refrain from committing ourselves to a choice.

It is usually not material whether attorney's fees or expenses paid in connection with an accounting of an inter vivos trust which is included in the grantor's gross estate are treated as a reduction in the value of the trust property or as an administration expense under section 812(b) of the Code. It is material, however, in some cases. For example, if the revocable trust qualifies for the marital deduction, the surviving spouse will receive the net amount after payment of the expenses chargeable against the trust and the deduction should be limited to what passes to the surviving spouse. However, if the expenses chargeable to the inter vivos trust are held deductible as ordinary administration expenses, a marital deduction will be allowable in some cases for an amount in excess of that passing to the surviving spouse. In such cases treatment of the expenses incurred in connection with the inter vivos trust as deductible administration expenses would result in a double deduction to the extent of the trust expenses.

In view of the foregoing it is held that an allowance should be made for the amount of attorney's fees incurred in connection with the usual issues involved in a trust accounting made necessary by the decedent's death in determining the net value of the assets of an inter vivos trust

created by the decedent and included in his gross estate rather than as an administration expense deductible under section 812(b) of the Internal Revenue Code.

REGULATIONS 105, SECTION 81.13: Property of decedent at time of death.

INTERNAL REVENUE CODE

Unexercised nontransferable stock options. (See Rev. Rul. 196, p. 178.)

SECTION 811(c).—GROSS ESTATE: TRANSFERS IN CONTEMPLATION OF, OR TAKING EFFECT AT, DEATH

REGULATIONS 105, SECTION 81.17: Transfers intended to take effect at or after the decedent's death. Rev. Rul. 158

(Also Section 81.18; Section 811(f), Section 81.24; Section 113(a), Section 29.113(a)-(5)-1, Regulations 111.)

INTERNAL REVENUE CODE

The exercise of an option by a decedent under a pension plan to take a reduced annuity for himself and to provide a survivorship annuity for his wife does not constitute a transfer within the meaning of section 811(c)(1)(B) of the Internal Revenue Code which is includible in his gross estate, where the election was made prior to October 8, 1949; however, where such an election was made after October 7, 1949, the value of the surviving annuitant's interest is includible in his gross estate under section 811(c)(3) or section 811(f) of the Code.

The basis of such annuity to the surviving spouse, for Federal income tax purposes, is determined according to the treatment of her annuity interest as a part of the decedent's estate for Federal estate tax purposes.

Advice is requested whether the value of an annuity payable to a survivor annuitant is includible in the gross estate of a decedent, for Federal estate tax purposes under section 811(c) of the Internal Revenue Code, where the decedent elected, under an option provided in a pension plan, to take a reduced annuity on his retirement and to provide a survivorship annuity for his wife.

This question was considered in *Commissioner* v. *Estate of Frederick John Twogood* (15 T. C. 989, acquiescence, C. B. 1953–1, 6, affirmed, 194 Fed. (2d) 627). In the Twogood case, the decedent, Frederick John Twogood, was an employee of the Standard Oil Co. of New York and its successors from May 1912 until his retirement on July 1, 1943. The employer of the decedent took out annuity contracts for the benefit of its employees, including the decedent, with such contract being underwritten and administrated by the Metropolitan Life Insurance Co. under a group annuity contract. By the terms of the contract, the decedent was entitled to retire after 30 years of continuous foreign service and to receive a retirement annuity. Pursuant to the contract, the decedent was entitled, prior to his normal retirement date, to elect to receive a reduced annuity for

his life and to have paid to a designated dependent an annuity for the life of such dependent, should he or she survive the decedent. By the terms of the plan, this election could not be changed by the decedent within 5 years before he reached retirement age which was on June 1, 1942, except with the consent of the insurance company and after that date, it could not be changed at all. Neither could the decedent or the designated dependent sell, assign, or transfer in any way their rights to the annuity payments.

On October 15, 1937, the decedent exercised such option and elected to receive only $955.82 a month if and when he became eligible to retire and designated his then wife as his dependent who was to be entitled to receive an annuity of $416.67, monthly, if he lived to retire and she survived him. This designation was made irrevocable by an agreement incident to his divorce in 1938. If the decedent had died at any time during the period from October 15, 1937, the date of the election and designation, and June 1, 1942, the date on which he became entitled to retire, no annuity would have been payable to any one. The decedent's total contribution to the annuity plan was $8,616 which amount would have been paid to his estate had he died previous to the maturity of his annuity. The decedent did not retire on his normal retirement date, January 1, 1942, but was formally retired on July 1, 1943, and was paid an annuity at the reduced amount which he had previously elected. This reduced annuity was paid to him until his death on April 28, 1944. Thereafter, monthly payments were made to his former wife in accordance with the terms of the plan. The United States Court of Appeals for the Second Circuit held, *inter alia*, that the value of the annuity payable to the decedent's first wife was not includible in his gross estate as a transfer within the meaning of section 811(c)(1)(B) of the Internal Revenue Code.

In *Estate of William J. Higgs* v. *Commissioner* (184 Fed. (2d) 427), this question was considered by the United States Court of Appeals for the Third Circuit, which held that the value of the survivorship annuity was not includible in the decedent's gross estate under section 811(c)(1)(B) of the Internal Revenue Code, as a transfer with a retention of income for the life of the decedent.

The basis of the decisions by the United States Courts of Appeals for the Second and Third Circuits in the Twogood and Higgs cases, is that if an employee is entitled to an annuity for life under an employers' retirement plan and elects to receive a reduced annuity for his life with a survivorship annuity to a designated dependent if he or she survives the decedent, the decedent has not retained an interest in the part of the property upon which the designated surviving dependent's annuity is based, even if it were considered that the decedent had made a transfer of property. The theory was that the purchase price of the entire contract was divisible into two parts—one, the price of the single life annuity and the other the price of the survivorship annuity.

With respect to elections made prior to October 8, 1949, the Internal Revenue Service has decided to follow the decision in the Twogood case. However, the law with respect to such elections made after October 7, 1949, has been changed. Section 811(c)(3) of the Code,

as amended by Public Law 378 (81st Cong., 63 Stat. 891, C. B. 1949–2, 275, 279), provides in part as follows:

> (3) TRANSFERS TAKING EFFECT AT DEATH—TRANSFERS AFTER OCTOBER 7, 1949.—An interest in property transferred by the decedent after October 7, 1949, shall be included in this gross estate under paragraph (1)(C) of this subsection (whether or not the decedent retained any right or interest in the property transferred) if and only if—
>
> (A) possession or enjoyment of the property can, through ownership of such interest, be obtained only by surviving the decedent; or
>
> (B) under alternative contingencies provided by the terms of the transfer, possession or enjoyment of the property can, through ownership of such interest, be obtained only by surviving the earlier to occur of (i) the decedent's death or (ii) some other event; and such other event did not in fact occur during the decedent's life. * * *

Under this amendment the decisive question is whether a transfer is made when the decedent elects to take a reduced annuity, gives another person a survivorship annuity and thereafter retires. If such action is considered as effecting a transfer, then the property will be includible in the decedent's gross estate under section 811(c)(3), *supra*, whether or not the decedent retains an income interest in the part transferred to the surviving annuitant, because that section now requires the property to be included in the decedent's gross estate if possession or enjoyment of the property can, through ownership of such interest, be obtained only by surviving the decedent.

The Tax Court of the United States in the Twogood case, took the position that the decedent's interests in the annuity which he would receive in the future were property rights and that he made a transfer of that part of the annuity upon which the surviving beneficiary's annuity was based. In the Twogood and Higgs cases, the United States Courts of Appeals for the Second and Third Circuits did not decide whether the decedents made transfers of property to the surviving annuitants but held that even if it were assumed that transfers occurred, such transfers were not taxable within the meaning of section 811(c)(1)(B) of the Code.

It is the position of the Revenue Service that a transfer within the meaning of section 811(c)(3), *supra*, is effected in such cases by the decedent to the surviving annuitant, since the exercise of the option by the decedent deprives the decedent of an interest in property which he would otherwise enjoy, or in the alternative, that the value of the survivorship annuity is includible in the decedent's gross estate under section 811(f) of the Code, as amended, as the exercise of a general power of appointment in respect of property "by a disposition which is of such nature that if it were a transfer of property owned by the decedent, such property would be includible in the decedent's gross estate under subsections (c) or (d)", inasmuch as the decedent's right to take the entire annuity or a lesser annuity would constitute a general power of appointment exercisable in his own favor. See Regulations 111, section 22(b)(2)-2, example 5.

The discussion above has no application to survivorship annuities purchased for cash. See *Commissioner* v. *Wilder's Estate* (118 Fed. (2d) 281, certiorari denied, 314 U. S. 634); *Commissioner* v. *Clise* (122 Fed. (2d) 998, certiorari denied, 315 U. S. 821); *Mearkle's Estate* v. *Commissioner* (129 Fed. (2d) 386).

Attention is directed to the provisions of section 303 of the Revenue Act of 1951 which provides as follows:

(a) AMENDMENT OF SECTION 22(b)(2).—Section 22(b)(2) is amended by adding at the end thereof the following new subparagraph:

"(C) Joint and Survivor Annuities.—For purposes of subparagraphs (A) and (B) of this paragraph, where amounts are received by a surviving annuitant under a joint and survivor's annuity contract and the basis of such survivor annuitant's interest is determined under section 113(a)(5) the consideration paid for such survivor's annuity shall be considered to be an amount equal to such basis."

(b) AMENDMENT OF SECTION 113(a)(5).—Section 113(a)(5) is amended by adding at the end thereof the following: "For the purposes of this paragraph, the survivor's interest in a joint and survivor's annuity shall be considered to be property 'acquired by bequests, devise, or inheritance' from the decedent if the death of the decedent was after December 31, 1950, and if the value of any part of such interest was required to be included in determining the value of the decedent's gross estate under section 811."

(c) EFFECTIVE DATES.—The amendments made by this section shall be applicable to taxable years ending after December 31, 1950.

For taxable years prior to 1951, a joint and survivorship annuity was treated for gain purposes as having the same basis as it had in the hands of the donor. (See S. Rept. 781, C. B. 1951-2, 458 at p. 495.) Thus, where the annuity contracts were purchased entirely by the employer, it was held that the entire amounts received each year were includible in the gross income with no part thereof being excluded under section 22(b)(2) of the Code. Under section 113(a)(5), as amended, *supra*, if the joint and survivorship annuity is included in the decedent's gross estate, it is given a "stepped-up" basis equal to the value of such interest included in the gross estate. However, if the annuity is not included in the gross estate it does not get the "stepped-up" basis. Therefore, where the transfer occurs, as in the Twogood and Higgs cases, prior to October 8, 1949, even though the death of the decedent is after December 31, 1950, the surviving annuitant will not be entitled to the treatment provided by section 303 of the Revenue Act of 1951, and the annuity will be fully taxable for income tax purposes.

In view of the foregoing, it is held that the decision in the Twogood case, will be followed in similar cases only where prior to October 8, 1949, the decedent elected to take a reduced annuity with a survivorship interest. The value of a survivorship annuity will be included in the decedent's gross estate under section 811(c)(3) and section 811(f) of the Code, where such an election was made after October 7, 1949.

REGULATIONS 105, SECTION 81.17: Transfers intended to take effect at or after the decedent's death. Rev. Rul. 260

(Also Section 811(d), Section 81.20.)

INTERNAL REVENUE CODE

The commuted value of the right to receive annuity payments pursuant to an agreement entered into between an employee and his employer prior to October 8, 1949, providing for the retirement of the employee and, in the event of his death, for payments to certain named beneficiaries is includible in the decedent's gross estate for

Federal estate tax purposes under section 811(c)(2) of the Internal Revenue Code. The value of the right to receive such payments is also includible in the gross estate under section 811(d) of the Code where the decedent possessed at his death the power to modify the contract.

Advice is requested relative to the status, for Federal estate tax purposes, of the right to receive annuity payments pursuant to an agreement entered into between an employee and his employer prior to October 8, 1949, providing for the retirement of the employee and, in the event of his death, for payments to certain named beneficiaries.

In the instant case the employee had entered into an agreement with his employer providing that the employee could retire at a later date and receive thereafter a stated annual deferred compensation payable in 120 monthly installments during his lifetime. If death occurred after retiring but before receiving the total number of installments the employer would make the remaining payments to certain named beneficiaries; and, if death occurred before the retirement date the payments would be made in equal monthly installments for a period of 10 years to the named beneficiaries. The agreement states that the purpose thereof is to assure the continuance of the employee's services to the employer corporation and his availability for services to certain subsidiary corporations and to the sole stockholder of the corporation. The rights of the employee under the contract could not be cutoff for reasons other than his discharge for dishonesty or the voluntary termination by him of his services. The agreement could not be modified except by an instrument in writing signed by both parties thereto.

Section 811 of the Internal Revenue Code provides in part as follows:

The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated, except real property situated outside of the United States—

* * * * * * *

(c) TRANSFERS IN CONTEMPLATION OF, OR TAKING EFFECT AT, DEATH.—

(1) GENERAL RULE.—To the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise—

* * * * * * *

(C) intended to take effect in possession or enjoyment at or after his death.

(2) TRANSFERS TAKING EFFECT AT DEATH—TRANSFERS PRIOR TO OCTOBER 8, 1949.—An interest in property of which the decedent made a transfer, on or before October 7, 1949, intended to take effect in possession or enjoyment at or after his death shall not be included in his gross estate under paragraph (1)(C) of this subsection unless the decedent has retained a reversionary interest in the property, arising by the express terms of the instrument of transfer and not by operation of law, and the value of such reversionary interest immediately before the death of the decedent exceeds 5 per centum of the value of such property. For the purposes of this paragraph, the term "reversionary interest" includes a possibility that property transferred by the decedent (A) may return to him or his estate, or (B) may be subject to a power of disposition by him, but such term does not include a possibility that the income alone from such property may return to him or become subject to a power of disposition by him. * * *

* * * * * * *

(d) REVOCABLE TRANSFERS.—

(1) TRANSFERS AFTER JUNE 22, 1936.—To the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise, where the enjoyment thereof was subject at the date of his death to any change through the exercise of a power (in whatever capacity exercisable) by the decedent alone or by the decedent in conjunction with any other person (without regard to when or from what source the decedent acquired such power), to alter, amend, revoke, or terminate, or where any such power is relinquished in contemplation of decedent's death;

The payments to the beneficiaries under the instant agreement are not voluntary on the part of the corporation but are made pursuant to a contractual obligation. Cf. *Estate of William L. Nevin* v. *Commissioner*, 11 T. C. 59, acquiescence C. B. 1949-1, 3. The fact that a right was reserved to the corporation to fund such obligation, or that it actually did so by purchasing insurance on the decedent's life, would not be material. In the case of *Estate of Paul G. Leoni* v. *Commissioner*, Tax Court Memorandum Opinion entered October 20, 1948, a contract entered into by the decedent and his employer provided for the payment by the employer to the decedent's widow, if living, of an annuity for a period of 8 years after the decedent's death. The estate contended that since these payments were given solely to the widow, the decedent or his estate had no right, title, or interest to, or in, any part of the payments and, therefore, the decedent made no transfer intended to take effect in possession or enjoyment at or after his death, within the purview of section 811(c) of the Code. In holding that the decedent did make a transfer of property includible under section 811(c) of the Code, the Court said:

The services to be rendered by the decedent furnished the consideration for the employer's promise to make the prescribed payments to this widow after decedent's death. * * * We think there was a transfer of property procured through the performance of services by the decedent, with the intent of having it pass at the time of his death. The death of the decedent was the operative fact which matured the promisor's duty to pay and completed the shifting of the economic benefits of property. Transfers of like purport have been held to come within the purview of section 811(c) of the Code, requiring the value of the property right transferred to be included in the decedent's estate.

It is, therefore, clear that the agreement in question gave rise to transfers of property on the part of the instant decedent. The value of such transfers, however, cannot be reached for Federal estate tax purposes under section 811(a) of the Code as property owned by the decedent at death, and, as the transfers were made prior to October 8, 1949, includibility in the decedent's gross estate cannot be required under section 811(c) of the Code, as amended, unless the decedent retained a reversionary interest in the property, arising by the express terms of the instrument of transfer. It is held that such a reversionary interest was retained by the decedent under the terms of the contract in that all property rights thereunder were to revert to him in the event he should be living on the retirement date and should thereafter live long enough to receive 120 equal monthly installments. As the value at the time of decedent's death of the right to receive the payments if living on the retirement date and during his lifetime thereafter was in excess of 5 percent of the value of interests passing upon his death, the entire value of the right to receive the payments pro-

vided for in the contract is includible in the gross estate for Federal estate tax purposes under section 811(c)(2) of the Internal Revenue Code. Since the contract could have been modified by an instrument in writing signed by both parties thereto (the decedent and the employer), it follows that the enjoyment of the transferred property was, at the time of the decedent's death, subject to change through the exercise by him of such power. It is therefore held that the value of the right to receive the payments provided for could also be included in the decedent's gross estate under section 811(d) of the Code as a transfer under which he possessed, at the time of his death, the power to change the enjoyment of the property transferred.

REGULATIONS 105, SECTION 81.18: Transfers with possession or enjoyment retained. Rev. Rul. 277

INTERNAL REVENUE CODE

Within the meaning of section 7 of the Technical Changes Act of October 25, 1949, as amended, a revocable inter vivos transfer in the form of a trust with income retained is deemed to have been made at the time after March 3, 1931, when the donor relinquished his power to revoke, amend, or terminate the trust rather than in 1926 when the trust was created, and the value thereof is includible in the donor's gross estate for Federal estate tax purposes under the provisions of section 811(c)(1)(B) of the Internal Revenue Code.

Advice is requested whether certain transfers of property in the form of revocable trusts with income retained created by decedent in 1926 are includible in decedent's gross estate for Federal estate tax purposes under the provisions of section 811(c)(1)(B) of the Internal Revenue Code, where the decedent relinquished his power to revoke, amend, or terminate the trusts after March 3, 1931.

In the instant case, the decedent created three trusts on February 5, 1926, one for the ultimate benefit of each of his three daughters, retaining the right to the income from the trusts during his life and the unrestricted power to revoke, amend, or terminate the trusts. On April 27, 1932, he executed an amendment to each trust pursuant to which he relinquished his right to revoke, amend, or terminate the trusts. He died on December 17, 1949.

Section 811 of the Code provides in part as follows:

The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated, except real property situated outside of the United States—

* * * * * * *

(c) TRANSFERS IN CONTEMPLATION OF, OR TAKING EFFECT AT, DEATH.—

(1) GENERAL RULE.—To the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise—

* * * * * * *

(B) under which he has retained for his life or for any period not ascertainable without reference to his death or for any period which does not in fact end before his death (i) the possession or enjoyment of, or the right to the income from, the property, * * *

Section 81.18 of Regulations 105 relating to transfers with possession or enjoyment retained provides in part as follows:

> * * * In the case of a decedent who died before January 1, 1951, property shall not be included in the gross estate under this section unless transferred—
>
> (1) after March 3, 1931, and before June 7, 1932, and the retention or reservation by the decedent was (A) for his life or (B) for such a period as to evidence his intention that it should extend at least for the duration of his life, and his death occurs before the expiration of such period; * * *

The above-quoted regulations are based upon section 7, as amended, of the Technical Changes Act of October 25, 1949 (Public Law 378, 81st Cong., 63 Stat. 891).

In the case presented the primary question, in determining whether the value of the transfers is to be included in the gross estate of the decedent, is whether the transfers were made, within the meaning of section 7 of the Technical Changes Act of October 25, 1949, when the trusts were first created in 1926, or when the transferor relinquished his right to revoke, amend, or terminate the trusts on April 27, 1932.

The rationale in the case of *Burnet, Commissioner of Internal Revenue* v. *Murray Guggenheim*, 288 U. S. 280, Ct. D. 636, C. B. XII-1 (1933), 374, is believed to be controlling in the instant case. That case involved a trust created in 1917 under which the grantor originally reserved a power of revocation and relinquished such power in 1925. In holding that the gift was made in 1925, the Supreme Court of the United States stated that:

> While the powers of revocation stood uncanceled in the deeds, the gifts, from the point of view of substance, were inchoate and imperfect. By concession there would have been no gift in any aspect if the donor had attempted to attain the same result by the mere delivery of the securities into the hands of the donees. A power of revocation accompanying delivery would have made the gift a nullity. * * * By the execution of deeds and the creation of trusts, the settlor did indeed succeed in divesting himself of title and tranferring it to others, * * * but the substance of his dominion was the same as if these forms had been omitted. * * * He was free at any moment, with reason or without, to revest title in himself, except as to any income then collected or accrued. As to the principal of the trusts and as to income to accrue thereafter, the gifts were formal and unreal. They acquired substance and reality for the first time in July 1925, when the deeds became absolute through the cancellation of the power.
>
> * * * * * * *
>
> If a revocable deed of trust is a present transfer by gift, there is not another transfer when the power is extinguished. If there is not a present transfer upon the delivery of the revocable deed, then there is such a transfer upon the extinguishment of the power.

In the instant case, applying the rationale of the Supreme Court in *Burnet, Commissioner of Internal Revenue* v. *Murray Guggenheim*, *supra*, there was not a "present transfer" by the decedent upon the delivery of the revocable deeds of trust on February 5, 1926, but there was such a transfer on April 27, 1932, upon the extinguishment of the power to revoke, amend, or terminate the trusts.

In view of the foregoing, it is held that, within the meaning of section 7 of the Technical Changes Act of October 25, 1949, the instant transfers were made in 1932 when the decedent relinquished his power to revoke, amend, or terminate the trusts, and the value thereof is includible in his gross estate under the provisions of section 811(c)(1)(B) of the Internal Revenue Code.

SECTION 811(d).—GROSS ESTATE: REVOCABLE TRANSFERS

REGULATIONS 105, SECTION 81.20: Transfers with power to change the enjoyment.

INTERNAL REVENUE CODE

Value for estate tax purposes of right to receive payments under a deferred compensation agreement. (See Rev. Rul. 260, p. 262.)

SECTION 811(f).—GROSS ESTATE: POWERS OF APPOINTMENT

REGULATIONS 105, SECTION 81.24: Property subject to power of appointment by decedent. Rev. Rul. 243

INTERNAL REVENUE CODE

A devise in general terms, expressing neither a fee nor a life estate, coupled with the power in the devisee to sell, convey, encumber, and otherwise dispose of the property devised as may to the devisee seem best, without any authority or order of any court whatsoever, and with a further power in the devisee to distribute by will any property remaining undisposed of at his or her death to certain named beneficiaries, under State law generally creates in the devisee such a power of disposal during life as to constitute a general power of appointment within the purview of section 811(f) of the Internal Revenue Code. The Internal Revenue Service will apply the foregoing general rule in all cases except those in which the decisions of the courts in the State wherein the estate is situated hold that a devise in the manner set forth above gives the devisee a life estate with a restricted power such as a power to use the corpus only for purposes of the devisee's health, education, support, or maintenance.

REGULATIONS 105, SECTION 81.24: Property subject to power of appointment by decedent. Rev. Rul. 278

INTERNAL REVENUE CODE

Where an insured retains until his death the right to change the beneficiary and the right to surrender the policies or obtain loans thereon, a power of appointment given in the policies to the beneficiary with respect to the proceeds of such policies is "created" at the time of the death of the insured within the meaning of section 811(f) of the Internal Revenue Code.

Advice is requested whether the amount of the proceeds of certain insurance policies which were payable to the decedent in monthly installments with privilege of surrender and withdrawal are includible in her gross estate under the provisions of section 811(f) (2) of the Internal Revenue Code.

In the instant case the decedent's husband executed settlement options prior to October 22, 1942, providing for the payment of the proceeds of several insurance policies to his wife, the present decedent, in installments with privilege of surrender and withdrawal, and for

the payment of the remainder of the proceeds upon her death to his children. The insured retained until his death, in 1950, the right to change the designation of his wife as primary beneficiary and the right to surrender the policies or to obtain loans thereon. The proceeds of the insurance policies were included in the husband's gross estate in the return filed for his estate and the marital deduction provided for in section 812(e) of the Code was claimed and allowed with respect thereto. The representatives of the estate of the wife, the present decedent, contend that the power given to her to appoint the property to herself was created prior to October 22, 1942, and that since she died in 1951 without exercising the power, the property is not includible in her gross estate under section 811(f) of the Code.

Section 811(f) of the Code, with exceptions not here material, defines a general power of appointment as a power which is exercisable in favor of the decedent, his estate, his creditors, or the creditors of his estate, and provides that property subject to such a power created on or before October 21, 1942, is includible in the gross estate of a decedent only if the power is exercised; property subject to a general power of appointment created after such date is includible in the gross estate for estate tax purposes whether or not the power is exercised.

It is the position of the Internal Revenue Service that a power of appointment conferred in a life insurance policy that does not become effective until the death of the insured is not "created" within the meaning of section 811(f) of the Code so long as the insured retains the right to surrender the policy.

In the instant case it is held that since the insured retained until his death in 1950 the right to surrender the policies, the power of appointment conferred upon his wife, the present decedent, with respect to the proceeds of such policies, was "created" within the meaning of section 811(f) of the Code at the time of the death of the insured in 1950 and not at the date of execution of the settlement options. The amount of the proceeds of the policies are, therefore, includible in the gross estate of the wife for estate tax purposes under the provisions of section 811(f)(2) of the Internal Revenue Code.

Regulations 105, Section 81.24: Property subject to power of appointment by decedent.

INTERNAL REVENUE CODE

Value of an annuity payable to a survivor annuitant. (See Rev. Rul. 158, p. 259.)

SECTION 811(g).—GROSS ESTATE: PROCEEDS OF LIFE INSURANCE

Regulations 105, Sections 81.26 and 81.27: Insurance in favor of the estate, and insurance received by other beneficiaries. (Also Section 812(e), Section 81.47a; Section 812(b), Section 81.36 of Regulations 105; Section 1000, Section 86.2 (Regulations 108.) Rev. Rul. 232

INTERNAL REVENUE CODE

Treatment of life insurance policies and the proceeds therefrom for Federal estate and gift tax purposes under the community property laws of the State of Louisiana in certain factual situations wherein the insured at death possessed incidents of ownership in the policies which had been taken out by him, either before or during the existence of the community, and premium payments thereof were made entirely with separate funds of either spouse with separate funds of both spouses combined, entirely with community funds, or in part with the separate funds of the insured and in part with community funds, and the beneficiary is (1) anyone other than the insured's estate or surviving spouse, (2) the surviving spouse, or (3) the insured's estate.

Advice is requested with respect to the treatment of life insurance policies and the proceeds therefrom for Federal estate and gift tax purposes under the community property laws of the State of Louisiana in certain factual situations not covered in Rev. Rul. 48, C. B. 1953–1, 392. In Rev. Rul. 48 it was held that, where a married man in Louisiana or Texas takes out an insurance policy on his own life in favor of a beneficiary other than his estate, reserving the right to change the beneficiary, and pays the premiums with community funds, upon the death of the husband, one-half of the proceeds of the policy was includible in his gross estate for Federal estate tax purposes under section 811(g)(2) of the Internal Revenue Code, and the remaining one-half of the proceeds, in which he had incidence of ownership as the agent for his wife, became an absolute gift by the wife for Federal gift tax purposes, and that in the event the wife predeceased the husband, one-half of the value of the policy was includible in her gross estate as her interest in a community asset or as a revocable transfer under section 811(d) of the Code.

Inasmuch as each case presented below requires a consideration of the Louisiana law to determine whether the policies of life insurance therein involved constitute community or separate property of the spouses, a brief preliminary statement of the principles of law in the Louisiana community property system will assist in resolving these factual situations.

Article 2334 of the Louisiana Civil Code relating to separate and common property of spouses provides in pertinent part as follows:

> The property of married persons is divided into separate and common property.
> Separate property is that which either party brings into the marriage, or acquires during the marriage with separate funds, or by inheritance, or by donation made to him or her particularly. * * *
> Common property is that which is acquired by the husband and wife during marriage, in any manner different from that declared.

With respect to the purchase of life insurance policies, the Louisiana courts have announced the general rule that the time of issuance of the policies governs the character of the insurance proceeds, that is, a policy acquired by the husband before marriage is his separate property, and a policy taken out during marriage falls into the community. However, the application of the rule in article 2334, *supra*, indicates that a policy taken out by the husband during marriage on his own life would be his separate property if he can prove the premiums were paid with his separate funds.

In Louisiana it is clear that where an insurance policy is acquired before marriage the character of the policy is not affected by the pay-

ment of the premiums after marriage from community funds. The policy remains the insured's separate property, and the community is entitled to reimbursement for the amount of premiums so paid. See *Succession of Lewis*, 189 So. 118; *Succession of Verneuille*, 45 So. 520. The same rule applies with respect to insurance taken out by the husband during marriage on his own life, with premiums paid from community funds, his spouse predeceases him, and the husband uses his separate funds thereafter to pay the premiums. The policy remains a community asset, and the husband's estate, on his death, is entitled to reimbursement from the community for the amount of premiums so paid. *Succession of LeBlanc* (1917) 76 So. 223.

In Louisiana if the husband takes out during marriage a policy on his own life payable at his death to his estate, or to his executor, administrator, or assigns, and pays the premiums with community funds, when the marriage is dissolved by the death of the husband, the proceeds received by the husband's legal representative belong to the community. *Succession of Buddig* (1902) 32 So. 361; *Succession of LeBlanc, supra; Berry* v. *Franklin State Bank & Trust Company* (1937) 173 So. 126. In reaching the above result, the courts have reasoned that the contract right to receive the money was acquired by the husband during marriage with community funds, and, like all other property acquired in that way, belongs to the community.

Also in Louisiana when the wife is named beneficiary in a policy taken out by the husband upon his own life and paid for with community funds, the proceeds received by the wife at the husband's death are her separate property. *Kelly* v. *Kelly* (1913) 60 So. 671; *Nulsen* v. *Herndon* (1933) 147 So. 359. No right of reimbursement exists in favor of the community by reason of the premiums having been paid with community funds. *Succession of Brownlee* (1892) 11 So. 590; *Kelly* v. *Kelly, supra.* By making the policy payable to the wife, the cases usually reason, the husband has manifested an intention of making a gift to her of his share of the proceeds. *Pilcher* v. *New York Life Insurance Company* (1881) 33 La. Ann. 322.

The factual situations with respect to which advice is requested are set forth below. In each instance it is assumed that the insured at death possessed incidents of ownership in the policy.

(A) The insured takes out a policy of life insurance during the existence of the community and all the premiums are paid out of community funds, and the beneficiary is (1) anyone other than the insured's estate or surviving spouse, (2) the surviving spouse, or (3) the insured's estate.

This is in part the factual situation dealt with in Revenue Ruling 48, *supra.* In situations (1), (2), and (3), there is included in the insured's estate one-half of the proceeds of the policy. However, in situation (1), the surviving spouse is considered to have made a gift of the other one-half of the proceeds and incurs a gift tax liability if the amount is in excess of the exclusion. In situations (2) and (3) the surviving spouse is not considered to have made a gift, since the donor and donee would be the same person. In situation (3) the proceeds of the policy are community assets in which the surviving spouse has a one-half interest.

(B) The insured takes out a policy of life insurance during the existence of the community, all of the premiums are paid out of the insured's separate funds, and the beneficiary is (1) anyone other than the insured's estate or surviving spouse, (2) the surviving spouse, or (3) the insured's estate.

Article 2334, *supra*, provides that separate property is that which is "acquired during marriage with separate funds." The fact that the insurance policy here was acquired by the husband's separate funds appears to meet the requirements of the statute. Accordingly, the insurance policy is the separate property of the insured husband. Therefore, in situations (1), (2), and (3), the entire proceeds of the policy are includible in the insured's gross estate, since he possessed incidents of ownership of such policy in his own right. Inasmuch as community property is not here involved, the special rule provided by section 812(e)(2)(B) of the Internal Revenue Code in computing the limitation on the extent of the marital deduction does not apply. The marital deduction as provided in sections 812(e)(1)(A) and 812(e)(1)(H) of the Internal Revenue Code and section 81.47a(b) of Regulations 105 is allowed in situation (2) with respect to these proceeds.

(C) The insured takes out a policy of life insurance on his own life during the existence of the community and dies possessed of incidents of ownership. All premiums were paid out of the *noninsured spouse's separate funds*, and the beneficiary is (1) anyone other than the insured's estate or surviving spouse, (2) the surviving spouse, or (3) the insured's estate.

In view of article 2334, *supra*, it would appear that the insurance policy here constitutes the separate property of the noninsured spouse, rather than of the community, under the law of Louisiana. However, in this situation where the insured has retained the right to change the policy beneficiary without the consent of the premium-paying noninsured spouse, insurance law is to the effect that the interest of the latter is slight; the substantial ownership of the chose represented by the policy is in the insured. Therefore, in situations (1) and (2), where a third party and the noninsured spouse is named beneficiary, respectively, section 81.27 of Regulations 105 requires the full amount to be included in the decedent insured's gross estate under the incidents of ownership rule established by section 811(g)(2)(B) of the Code. In situation (3), where the insured's estate is named beneficiary, section 81.26 of Regulations 105 requires the entire amount of the proceeds to be included in the decedent insured's gross estate under section 811(g)(1) of the Code. The marital deduction provided by section 812(e) of the Code may be allowed with respect to the proceeds which are transferred to the surviving spouse in situation (2).

A claim for reimbursement of the amount of premiums paid by the noninsured spouse to the insured decedent's estate may not be allowed under section 812(b)(3) of the Code in each of the situations presented. Such amount of premiums, in the absence of evidence to the contrary, is considered to be an irrevocable gift between the spouses.

(D) The insured takes out a policy of life insurance during the existence of the community, some of the premiums are paid out of *community funds* and some of the premiums are paid out of the *insured's separate funds*, and the beneficiary is (1) anyone other than the insured's estate or surviving spouse, (2) the surviving spouse, or (3) the insured's estate.

Assuming under these facts, that community funds were used initially to pay the premiums on the policy, such policy takes on the character of a community asset which, under article 2334, *supra*, it retains thereafter, despite the later use of the insured's separate funds to maintain it. Succession of LeBlanc, *supra*. Accordingly, the

solution to this factual situation is identical with (A), *supra.* However, there may be included as an asset in the insured's separate estate, in situations (2) and (3), a claim against the community for premiums paid out of the insured's separate funds.

(E) The insured takes out a policy of life insurance before the existence of the community, one premium is paid out of the insured's separate funds before marriage and the balance of the premiums are paid out of community funds, and the beneficiary is (1) anyone other than the insured's estate or surviving spouse, (2) the surviving spouse, or (3) the insured's estate.

Since the character of the policy is determined at the time it is taken out by the payment of premiums from separate funds, it is believed the policy here constitutes the separate property of the insured. This rule clearly applies in situation (3), and is applicable to situations (1) and (2) since the insured retained the sole power to name the policy beneficiary. Therefore, in each situation all policy proceeds are includible in the insured's gross estate in accord with sections 811(g)(1) and 811(g)(2)(B) of the Code. The marital deduction as provided in section 812(e) may be allowed in situation (2) with respect to these proceeds. Inasmuch as community property is not here involved, section 812(e)(2)(B) is not applicable in computing a limitation on the extent of the marital deduction. A claim by the community for reimbursement for premiums paid with community funds against the insured's gross estate under section 812(b)(3) may be allowed in situations (1) and (3) if such claim is presented and actually paid by the insured's estate representatives. Where in situation (3) the surviving spouse is the sole legatee of the insured's separate estate, the marital deduction may be allowed with respect to all separate property to the extent such property passes from the decedent to his surviving spouse within the meaning of section 812(e) of the Code. In the event of the noninsured's prior decease, such spouse's separate estate may properly include as an asset thereof, the claim against the community for one-half the premiums paid from community funds in each situation presented.

(F) The insured takes out a policy of life insurance before the existence of the community, one premium is paid out of the insured's separate funds before marriage and the balance of the premiums are paid out of the noninsured spouse's separate funds, and the insured dies possessed of incidents of ownership of [the] policy, and the beneficiary is (1) anyone other than the insured's estate or surviving spouse, (2) the surviving spouse, or (3) the insured's estate.

In accord with the discussion of factual situation (E) the policy here is regarded as a separate asset of the insured. Therefore, in each situation all policy proceeds are includible in the insured's gross estate in accord with section 811(g) of the Code. The marital deduction as provided in section 812(e) may be allowed in situation (2) with respect to these proceeds. Inasmuch as community property is not here involved, section 812(e)(2)(B) is not applicable in computing a limitation on the extent of the marital deduction. A claim by the noninsured spouse for reimbursement of premiums paid with separate funds against the insured's gross estate under section 812(b)(3) may not be properly allowed in any of the situations presented for the reasons stated in solution (C), *supra.* This same conclusion would follow if sole legatee of the insured's estate had submitted a claim for reimbursement of the amount of

premiums paid. In situation (3), where the surviving spouse is the sole legatee of the insured's separate estate, the marital deduction may be allowed with respect to all separate property to the extent such property passes from the decedent to the surviving spouse within the meaning of section 812(e) of the Code. In the event of the noninsured's prior decease, such spouse's separate estate may not properly include as an asset thereof, the claim against the separate property of the insured spouse for the amount of the premiums paid in each situation presented.

SECTION 812(b).—NET ESTATE: EXPENSES, LOSSES, INDEBTEDNESS, AND TAXES

REGULATIONS 105, SECTION 81.29: Deduction of administration expenses, claims, etc.

INTERNAL REVENUE CODE

Election with respect to the treatment of certain administrative expenses of an estate for Federal estate tax purposes. (See Rev. Rul. 240, p. 79.)

REGULATIONS 105, SECTION 81.36: Claims against the estate.

INTERNAL REVENUE CODE

Treatment of life insurance policies under community property laws of Louisiana in situations involving marital deduction. (See Rev. Rul. 232, p. 268.)

SECTION 812(d).—NET ESTATE: TRANSFERS FOR PUBLIC, CHARITABLE, AND RELIGIOUS USES

REGULATIONS 105, SECTION 81.44: Transfers for public, charitable, religious, etc., uses. Rev. Rul. 145

INTERNAL REVENUE CODE

Where a charity is legatee under a will and, as such, contests the probate of a later will and such contest is settled by agreement with the parties in interest, the amount deductible for testamentary charitable gifts under section 812(d) of the Internal Revenue Code is calculated on the basis of what the charity actually received.

Advice is requested relative to the deduction, for Federal estate tax purposes, of amounts paid to certain charitable organizations pursuant to a settlement agreement resulting from the contest of a will.

In the instant case the decedent left two wills. One will created a trust of the residuary estate for the benefit of a son for life with remainder interest of two-thirds to charity and one-third to grandchildren. A later will left the bulk of the estate to certain persons other than the legatees in the first will. From an order of the probate court admitting the second will to probate, several appeals were filed by the charities which contested the later will relying on the first will, and by the heirs who contested both wills, claiming the decedent died

intestate. Before judgments were rendered in these suits, a settlement agreement was reached whereby the second will would stand admitted to probate and would be administered as written in all respects, with the exception of the residue. The charities received substantial amounts in settlement of their claims. The question presented is whether: (1) as the later will was the one admitted to probate, the amounts deductible for charitable bequests are only those given in that will, or (2) in view of the fact that the charities actually received substantial amounts in compromise of claims based on the prior will, such amounts are, for Federal estate tax purposes, considered to have been received from the decedent by bequest or devise and deductible from the gross estate under the provisions of section 812(d) of the Internal Revenue Code.

Section 812 of the Internal Revenue Code provides, in part, as follows:

> For the purpose of the tax the value of the net estate shall be determined, in the case of a citizen or resident of the United States by deducting from the value of the gross estate—
>
> * * * * * * *
>
> (d) TRANSFERS FOR PUBLIC, CHARITABLE AND RELIGIOUS USES.—The amount of all bequests, legacies, devices, or transfers, * * * to or for the use of the United States, any State, Territory, any political subdivision thereof, or the District of Columbia, for exclusively public purposes, or to or for the use of any corporation organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes. * * *.

Where charity is designated as the sole legatee and devisee under a will but actually receives something less than the entire estate by reasons of a will contest instituted by the heirs, the amount of the deduction is limited to the actual amount received by charity. This position has been followed since the decision in *Munro L. Lyeth* v. *Hoey*, 305 U. S. 188, Ct. D. 1370, C. B. 1938–2, 208. In that case an heir of the decedent contested the validity of the decedent's will in which only a small legacy had been left to him. The heirs, devisees, legatees, and the executors under the will entered into a compromise providing that the will be probated and that a specific sum be paid to the heir. The court held that the money the heir received pursuant to the compromise should be treated, with respect to his Federal income tax liability, as acquired by inheritance for the reason that it was possible for him to receive it only because of his standing as an heir and of his claim in that capacity. While the issue there presented was the income tax liability of such heir, the rationale has been followed by the Bureau in Federal estate tax cases. (See E. T. 17, C. B. 1940–1, 231.) In *Estate of John Sage* v. *Commissioner*, 122 Fed. (2d), 480, the decedent bequeathed the entire residuary estate to charity. A will contest instituted on behalf of the decedent's widow was abandoned in consideration of her receiving one-fourth of the residuary estate. In determining the amount of the charitable deduction, the court sustained the Bureau's position that the deduction for testamentary charitable gifts was limited to the amount actually received by charity, which was three-fourths of the residuary estate. In *Estate of Frederick F. Dumont* v. *Commissioner*, 150 Fed. (2d), 691, two wills were involved and in the later one the bequest to charity (but not the entire will) was void under the Pennsylvania 30-day statute. Both wills contained charitable bequests. The charity contested the va-

lidity of the later will and claimed under the earlier will. A settlement was made, the later will (under which the charitable bequests would have been void) was admitted to probate, but the charity was paid a substantial amount. It was held that the amount paid to the charity was deductible under the provisions of section 812(d) of the Code. All of these decisions are based on the fact that the person attacking the will is an heir, a widow, or a legatee under a prior will. (Also see *Helvering* v. *Safe Deposit and Trust Co. of Baltimore*, 316 U. S. 56, Ct. D. 1552, C. B. 1942–1, 246, and *Quigley* v. *Commissioner*, 143 Fed. (2d) 27.)

In the instant case the status of the charities contesting the probated will was that of legatees under the prior will which they proffered as the decedent's last will. Such status commanded the settlement agreement and was recognized by it. If the parties to this controversy were reversed so that the probated will bequeathed the residuary estate to charity but the amount was reduced by a settlement agreement by heirs and/or legatees (not charitable organizations) under a prior will, the charitable deduction would not comprise the entire residue but would be limited to the amount actually received after the settlement agreement. Such result was obtained in the Sage case and E. T. 17, cited above. This rule should operate both ways.

In view of the foregoing, it is held that where a charity is legatee under a will and, as such, contests the probate of a later will and such contest is settled by agreement with the parties in interest, the amount deductible for testamentary charitable gifts under section 812(d) of the Internal Revenue Code is calculated on the basis of what the charity actually received.

SECTION 812(e).—NET ESTATE: BEQUESTS, ETC., TO SURVIVING SPOUSE

REGULATIONS 105, SECTION 81.47a(a): Allowance of marital deduction.

INTERNAL REVENUE CODE

Treatment of life insurance policies under community property laws of Louisiana in situations involving marital deduction. (See Rev. Rul. 232, p. 268.)

REGULATIONS 105, SECTION 81.47(b): Nondeductible interests. Rev. Rul. 279

INTERNAL REVENUE CODE

An interest in real property passing to a surviving spouse in the form of a dower interest under the laws of descent and distribution of the State of Alabama constitutes a terminable interest within the meaning of section 812(e)(1)(B) of the Internal Revenue Code, and any amount paid to a surviving spouse as the fair value of such dower interest from the subsequent sale of the property, is not an amount paid in lieu of dower within the meaning of section 812(e)(3) of the Code and is not allowable as a marital deduction for Federal estate tax purposes.

Advice is requested whether an amount paid to a surviving spouse as the fair equivalent of an interest in real property which passed to her in the form of a dower interest under the laws of descent and

distribution of the State of Alabama is allowable as a marital deduction under section 812(e) of the Internal Revenue Code.

In the case presented, the decedent died intestate, survived by his wife and children, owning at the time of his death real properties in the State of Alabama which were subsequently sold by the administrators of the estate. One-third of the amount received from such sale was awarded by the probate court having jurisdiction over the estate to decedent's widow, pursuant to State statutes, as the fair equivalent of her dower interest in the properties, she having consented to the sale of such interest. The estate contends that it is entitled to a marital deduction under section 812(e) of the Code with respect to that portion of the sales price allotted to the widow as the fair value of her dower interest in the lands sold, it being maintained that the amount thus received by her constituted her statutory interest therein in lieu of dower, within the meaning of the definition contained in section 812(e)(3) of the Code, and, that since such amount passed to her as absolute owner, it is a deductible interest under section 812(e)(1) of the Code.

Under the provisions of section 812(e)(1)(B) of the Code, no marital deduction will be allowed with respect to a property interest which passes or has passed from a decedent to his surviving spouse in any case where the surviving spouse has only a life estate or terminable interest, which will terminate or fail upon the lapse of time, upon the occurrence of an event or contingency, or upon the failure of an event or contingency to occur (1) if an interest in such property passes or has passed at any time (for less than an adequate and full consideration in money or money's worth) from the decedent to any person other than such spouse (or the estate of such spouse); and (2) if by reason of such passing such person (or his heirs or assigns) may possess or enjoy any part of such property after such termination or failure of the interest so passing to the surviving spouse. Regulations 105, section 81.47b(d), provides that section 812(e)(1)(B), *supra*, is to be applied with respect to the property interests which actually passed from the decedent to his spouse and any subsequent conversion of the property is immaterial for this purpose. Section 812(e)(3)(C) of the Code provides that an interest in property shall be considered as passing from the decedent to any person if and only if such interest is the dower or courtesy interest (or statutory interest in lieu thereof) of such person as surviving spouse of the decedent.

Section 1, title 16, of the Code of Alabama (1940) provides that:

> The real estate of persons dying intestate, as to such estate descends, subject to the payment of debts, charges against the estate, and the widow's dower, as follows:
>
> (1) To the children of the intestate, or their descendants, in equal parts.

Section 40, title 34, of the Alabama Code defines dower as:

> * * * an estate for the life of the widow in a certain portion of the following real estate of her husband, to which she has not relinquished her right during the marriage * * *.

Section 41, title 34, of the Alabama Code provides that:

> The quantity of the dower interest is as follows:
>
> * * * * * * *
>
> (3) When there are lineal descendants, then to one-third part thereof, whether the estate be solvent or not.

Under title 61 of the Alabama Code, in case of intestacy, lands may be sold by the administrator for the payment of debts when the personal estate is insufficient therefor (sec. 244); and the lands of an estate may be sold by order of the probate court having jurisdiction of the estate, when the same cannot be equitably divided among the heirs or devisees, when an adult heir or devisee files his written consent that the land be sold (sec. 245). In such cases, the application for the sale of lands, either for the payment of debts or for division, must be made by the executor or administrator and such application may be contested by any party interested in the estate (sec. 246). Where, under the provisions of title 61, the lands of a decedent can be ordered to be sold by the probate court, the widow may file in the office of the judge of probate her written consent that her dower interest in the land be sold, so as to vest in the purchaser the complete title; and thereupon the court must order such dower interest to be sold with the residue of the lands (sec. 271). When the sale is confirmed, the court, on application of the widow, must make an order that a fair equivalent for the dower interest be paid to her by the personal representative, when the purchase money is collected, the value of such interest to be ascertained by proof, having regard to the age and health of the widow, but in no case to exceed one-third of the purchase money (sec. 272, as amended July 6, 1945).

Alabama has adopted substantially the common law concept of dower. It is clear that dower in that State, as defined by section 40, title 34, *supra*, is nothing more than a life estate in which the wife is entitled to a part of the lands of her husband at death or upon her dissent from his will. It is also clear that sections 271 and 272, title 61, of the Alabama Code provide no statutory substitute for dower such as is contemplated in the definition set forth in section 812(e)(3) of the Code. Section 271 merely prohibits the court from ordering the sale of the widow's dower interest without her written consent; and section 272 merely makes it mandatory on the court if lands of the estate are sold, the widow consenting thereto in writing, to make an order for the payment to her of the fair equivalent of the dower interest out of the purchase money. Dower in Alabama has not been abolished by statute and, therefore, no statutory substitute for dower is provided. Neither do the sections of Alabama law referred to confer upon the widow any vested right of property such as will qualify for the marital deduction under section 812(e)(1) of the Code. The only interest in the Alabama lands which passed upon the death of the decedent to his widow was the dower interest as defined by the law of the State, or an estate for life in and to a one-third part of such lands. Since fee simple title to the whole of such lands vested in the children at the time of their father's death, subject only to the dower interest therein of the widow, the children or their descendants may possess or enjoy all of such property upon the death of their mother. The interest in such lands which passed to the widow is, therefore, clearly a terminable one. The subsequent sale of the lands and the payment of a portion of the proceeds of the sale as the fair equivalent of the widow's dower interest therein amounted to no more than a conversion of the interest passing to her on the decedent's death.

Under the provisions of section 812(e) of the Code, the marital deduction is allowable with respect to any interest in property which passes from a decedent to his surviving spouse as absolute owner. Such is not the law of Alabama with respect to the interest of a widow in lands of her intestate husband where there are lineal descendants, as here. The widow's death terminates any rights she may have in the lands. It is true that her dower interest in the lands cannot be sold without her consent but it also is true that she cannot compel a sale of her dower interest or the payment to her of the fair value of such interest or its equivalent in cash.

In view of the foregoing, it is held that an interest in real property passing to a surviving spouse in the form of a dower interest under the laws of descent and distribution of the State of Alabama constitutes a terminable interest within the meaning of section 812(e)(1)(B) of the Internal Revenue Code, and any amount paid to a surviving spouse as the fair value of such dower interest from the subsequent sale of the property is not an amount paid in lieu of dower within the meaning of section 812(e)(3) of the Code and is not allowable as a marital deduction for Federal estate tax purposes.

SECTION 813(b).—CREDITS AGAINST TAX: ESTATE, SUCCESSION, LEGACY, AND INHERITANCE TAXES

REGULATIONS 105, SECTION 81.9: Credit for death taxes. T. D. 6034

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER B, PART 81.—ESTATE TAX UNDER CHAPTER 3 OF THE INTERNAL REVENUE CODE, AS AMENDED

Regulations 105 amended to conform to section 603 of the Revenue Act of 1951, relating to foreign estate tax credit.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

On March 11, 1953, notice of proposed rulemaking with respect to amendments conforming the estate tax regulations to section 603 of the Revenue Act of 1951, approved October 20, 1951, was published in the Federal Register (18 F. R. 1389). After consideration of such relevant suggestions as were presented by interested persons regarding the proposals, the following amendments to Regulations 105 [26 CFR, pt. 81] are hereby adopted:

PARAGRAPH 1. Section 81.2, as amended by Treasury Decision 5941 [C. B. 1952-2, 234], approved October 24, 1952 [26 CFR 81.2], relating to description of tax, is further amended by inserting immediately after the fifth paragraph of (*a*) thereof (which par. commences "Credits for Federal gift taxes") the following new paragraph:

Credits for death taxes paid foreign countries by estates of certain decedents dying after October 20, 1951, are authorized against both the basic and additional taxes. See section 81.9(*b*) as to conditions and limitations.

PAR. 2. Section 81.7, as amended by Treasury Decision 5239, [C. B. 1943, 1081], approved March 10, 1943 [26 CFR 81.7], relating to rates and computation of tax, is further amended as follows:

(A) By inserting in the second sentence of the third paragraph thereof, immediately after "for gift tax" the following: "or for death taxes"; and

(B) By striking the last sentence in example (2) thereof and inserting in lieu thereof the following sentence:

It will be noted that credit for estate or inheritance taxes paid to any State is not allowable against the additional tax imposed by section 935.

PAR. 3. There is inserted immediately preceding section 81.8 [26 CFR 81.8] the following:

SEC. 603. FOREIGN ESTATE TAX CREDIT [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

(a) CREDIT AGAINST BASIC ESTATE TAX.—Section 813 (relating to credits against estate tax) is hereby amended by adding at the end thereof the following new subsection:

"(c) SAME—PAID TO FOREIGN COUNTRIES.—

"(1) IN GENERAL.—The tax imposed by section 810 shall be credited with the amount of any estate, inheritance, legacy, or succession taxes actually paid to any foreign country in respect of any property situated within such foreign country and included in the gross estate (not including any such taxes paid with respect to the estate of a person other than the decedent). If the decedent at the time of his death was not a citizen of the United States, credit shall not be allowed under this subsection unless the foreign country of which such decedent was a citizen or subject, in imposing such taxes, allows a similar credit in the case of a citizen of the United States resident in such country. The determination of the country within which property is situated shall be made in accordance with the rules applicable under Part III of this subchapter in determining whether property is situated within or without the United States.

"(2) LIMITATIONS ON CREDIT.—The credit provided in this subsection with respect to such taxes paid to any foreign country—

"(A) shall not, with respect to any such tax, exceed an amount which bears the same ratio to the amount of such tax actually paid to such foreign country as the value of property which is—

"(i) situated within such foreign country,

"(ii) subjected to such tax, and

"(iii) included in the gross estate bears to the value of all property subjected to such tax; and

"(B) shall not, with respect to all such taxes, exceed an amount which bears the same ratio to the tax imposed by section 810 (after deducting from such tax the credits provided by subsections (a) and (b) of this section) as the value of property which is—

"(i) situated within such foreign country,

"(ii) subjected to the taxes of such foreign country, and

"(iii) included in the gross estate bears to the value of the entire gross estate reduced by the aggregate amount of the deductions allowed under subsections (c), (d), and (e) of section 812.

"(3) VALUATION OF PROPERTY.—

"(A) The values referred to in the ratio stated in paragraph (2)(A) are the values determined for the purposes of the tax imposed by such foreign country.

"(B) The values referred to in the ratio stated in paragraph (2)(B) are the values determined under this chapter; but, in applying such ratio, the value of any property described

in clauses (i), (ii), and (iii) thereof shall be reduced by such amount as will properly reflect, in accordance with regulations prescribed by the Secretary, the deductions allowed in respect of such property under subsections (c), (d), and (e) of section 812.

"(4) PROOF OF CREDIT.—The credits provided in this subsection and in section 936(c) shall be allowed only if the taxpayer establishes to the satisfaction of the Secretary (A) the amount of taxes actually paid to the foreign country, (B) the amount and date of each payment thereof, (C) the description and value of the property in respect of which such taxes are imposed, and (D) all other information necessary for the verification and computation of the credits.

"(5) PERIOD OF LIMITATION.—The credits provided in this subsection and in section 936(c) shall be allowed only for such taxes as were actually paid and credit therefor claimed within four years after the filing of the return required by section 821, except that—

"(A) If a petition for redetermination of a deficiency has been filed with the Tax Court of the United States within the time prescribed in section 871, then within such four-year period or before the expiration of 60 days after the decision of the Tax Court becomes final.

"(B) If, under section 822(a)(2) or section 871(h), an extension of time has been granted for payment of the tax shown on the return, or of a deficiency, then within such four-year period or before the date of the expiration of the period of the extension.

Refund based on such credits may (despite the provisions of sections 910 to 912, inclusive) be made if claim therefor is filed within the period above provided. Any such refund shall be made without interest."

(b) CREDIT AGAINST ADDITIONAL ESTATE TAX.—Section 936 (relating to credits against estate tax) is hereby amended by adding at the end thereof the following new subsection:

"(c) ESTATE, ETC., TAXES PAID TO FOREIGN COUNTRIES.—

"(1) IN GENERAL.—In the case of the estate of a citizen or resident of the United States, the tax imposed by section 935 shall be credited with the amount of any estate, inheritance, legacy, or succession taxes actually paid to any foreign country in respect of any property situated within such foreign country and included in the gross estate (not including any such taxes paid with respect to the estate of a person other than the decedent). If the decedent at the time of his death was not a citizen of the United States, credit shall not be allowed under this subsection unless the foreign country of which such decedent was a citizen or subject, in imposing such taxes, allows a similar credit in the case of a citizen of the United States resident in such country. The determination of the country within which property is situated shall be made in accordance with the rules applicable under Part III of subchapter A in determining whether property is situated within or without the United States.

"(2) LIMITATION ON CREDIT.—The credit provided in this subsection with respect to such taxes paid to any foreign country—

"(A) shall not exceed the amount by which such taxes paid to the foreign country exceed the amount of the credit allowed therefor under section 813(c); and

"(B) shall not exceed an amount which bears the same ratio to the tax imposed by section 935 (after deducting from such tax the credit provided by subsection (b) of this section) as the value of property which is—

"(i) situated within such foreign country,

"(ii) subjected to the taxes of such foreign country, and

"(iii) included in the gross estate bears to the value of the entire gross estate reduced by the aggregate amount of the deductions allowed under subsections (c), (d), and (e) of section 812.

"(3) SAME—SPECIAL RULES.—

"(A) For the purposes of paragraph (2)(A), 'such taxes paid to the foreign country' shall, with respect to any tax paid to the foreign country, be the amount computed under section 813(c)(2)(A).

"(B) The values referred to in the ratio stated in paragraph (2)(B) are the values determined under this chapter; but, in applying such ratio, the value of any property described in clauses (i), (ii), and (iii) thereof shall be reduced by such amount as will properly reflect, in accordance with regulations prescribed by the Secretary, the deductions allowed in respect of such property under subsections (c), (d), and (e) of section 812.

"(4) PROOF OF CREDIT.—

"For provisions relating to proof of credit, see section 813(c)(4).

"(5) PERIOD OF LIMITATION.—

"For provisions relating to period of limitation on claiming of credit or refund based thereon and nonpayment of interest on refund, see section 813(c)(5)."

* * * * * * *

(e) EFFECTIVE DATE.—The amendments made by this section shall be applicable with respect to estates of decedents dying after the date of the enactment of this Act.

SEC. 615. TREATY OBLIGATIONS [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

No amendment made by this Act shall apply in any case where its application would be contrary to any treaty obligation of the United States.

PAR. 4. Section 81.8, as amended by Treasury Decision 5699 [C. B. 1949–1, 181], approved May 13, 1949 [26 CFR 81.8], is further amended as follows:

(A) By striking the word "and" from the first sentence of (*a*) thereof;

(B) By striking the period at the end of the first sentence of (*a*) thereof and inserting in lieu thereof the following: ", and, fourth, if the decedent died after October 20, 1951, the credit under section 81.9(*b*) for death taxes paid to a foreign country."; and

(C) By substituting "81.9(*a*)" for "81.9" wherever "81.9" appears in such section.

PAR. 5. Section 81.9, as amended by Treasury Decision 5820 [C. B. 1950–2, 74], approved December 7, 1950 [26 CFR 81.9], is further amended as follows:

(A) By amending the heading thereof to read as follows: "CREDIT FOR DEATH TAXES.—(*a*) *Taxes paid a State, Territory, the District of Columbia or a possession of the United States*";

(B) By deleting the second and third paragraphs thereof; and

(C) By inserting at the end thereof the following:

(*b*) *Foreign death taxes.*—(1) *In general.*—(i) Subject to certain limitations indicated hereinafter, sections 813(c) and 936(c) of the Internal Revenue Code, as added by section 603 of the Revenue Act of 1951, approved October 20, 1951, authorize additional credits against the basic and additional estate taxes for any estate, inheritance, legacy, or succession taxes actually paid to any foreign country in respect of property situated in such foreign country and included in the gross estate. Such taxes are herein referred to as "foreign death taxes." The credit is available to estates of decedents dying after October 20, 1951, who were citizens of the United States at death. Credit is also allowable in the case of a decedent dying after October 20, 1951, who was a resident but not a citizen of the United States if the country, of which the decedent was a national, in

imposing death taxes allows a similar credit to estates of citizens of the United States resident in such country. For definition of resident see section 81.5.

(ii) The credit is allowable not only as to death taxes paid foreign countries which are states in the international sense, but also as to estate, inheritance, legacy, or succession taxes paid to possessions or political subdivisions of foreign states. However, the credit is limited to estate, inheritance, legacy, or succession taxes imposed with respect to the death of such a decedent and does not apply to any such taxes paid with respect to the estate of a person other than the decedent. No credit is allowable as to property situated outside of the foreign country in which is imposed the tax in respect of which credit is claimed. Whether particular property of the decedent is situated in the foreign country imposing the tax is determined in accordance with the same principles that would be applied in determining whether similar property of a nonresident decedent not a citizen of the United States is situated within the United States for Federal estate tax purposes. See section 81.50. For example, under that section, a bond for the payment of money is not within the United States unless the certificate is physically located in the United States; accordingly, a bond is deemed situated in the foreign country imposing the tax only if the certificate therefor is physically located in such foreign country. Similarly, under section 81.50, stock of a domestic (United States) corporation, irrespective of location of the certificate, and stock of a foreign corporation, if the certificate therefor is located in the United States, is deemed to be situated in the United States; therefore, a share of corporate stock is regarded as situated in the foreign country imposing the tax if the issuing corporation is incorporated in that country, or if the certificate of stock (regardless of country of incorporation) is physically located in such country. Further, under the provisions of section 863(b) and section 81.50, moneys deposited with any person carrying on the banking business by or for a nonresident not a citizen of the United States who was not engaged in business in the United States at time of death is not deemed to be situated in the United States. Consequently, such an account with a foreign bank in the country imposing the tax is not considered to be situated in such country.

(iii) The credit is limited to the foreign estate, inheritance, legacy, or succession tax attributable to property situated in a foreign country and included in the gross estate. Further, the credit cannot exceed the Federal estate tax attributable to such property, determined in the manner hereinafter prescribed. No credit is allowable for any interest or penalty paid in connection with the foreign estate, inheritance, legacy, or succession tax. Where credit for a particular foreign death tax is authorized by convention, there shall be allowed either the credit provided by the convention or the credit computed under this section, whichever is the greater. Where a foreign death tax is imposed by both a foreign country with which the United States has entered into a death duty convention and one of its possessions or political subdivisions, the credit authorized by such convention or by this section, whichever is the greater, shall be allowed. For example, if a portion of the estate of a citizen of the United States is situated in Canada and is subjected to death taxes imposed by both the Dominion of Canada and the Province of Quebec, credit is allowable for the Dominion duty computed under the estate tax convention with Canada or for the combined Dominion duty and the provincial duties under this section, whichever is greater. Where foreign death taxes are imposed in respect of the same property by more than one foreign country, credit shall be allowed for all such taxes, whether such credit is allowed under a convention or under this section, subject to the limitations prescribed in this section. These rules may be illustrated by the following examples:

Example (1). The decedent was a citizen of and domiciled in the United States at death. His estate consisted of bonds of United States corporations, the certificates for which were physically located in Quebec, $750,000; stocks of Canadian corporations, the certificates for which were located in the United States, $200,000; and bonds of Canadian corporations, the certificates being located in the United States at death, $50,000. Debts and charges amounted to $40,000. The Federal estate tax prior to allowance of credit for foreign death taxes amounted to $257,740. Assume that the net succession duty imposed by the Dominion of Canada on the Canadian stock and bonds amounted to $28,320. Under the Death Duty Convention between the United States and Canada, the Federal estate tax attributable to such property is: $\frac{250,000}{1,000,000} \times \$257,740 = \$64,435$. On the basis of these facts alone, credit would be allowable under the Canadian

Convention for the tax paid to the Dominion of Canada in the amount of $28,320, since this amount is less than the Federal estate tax attributable to the property. No credit is allowable under the convention for the tax imposed by the Province of Quebec.

Assume further that a succession duty was imposed by the Province of Quebec on the bonds of United States corporations in the amount of $48,096. Under the situs rules in subdivision (*b*)(1)(ii), the bonds of United States corporations and stocks of Canadian corporations are deemed to be situated in the foreign country. Under the rules in subdivision (*b*)(2)(ii) below for determining the amount of the first limitation the total Quebec duty attributable to the United States bonds situated in Canada amounted to $48,096, and the Dominion succession duty attributable to the Canadian stocks amounted to $22,656. The total foreign death tax attributable to the property situated in a foreign country and included in the gross estate amounted to $70,752. The credit cannot exceed the Federal estate tax attributable to such property which is computed as follows: $\frac{950,000}{1,000,000} \times \$257,740 = \$244,853$. Since this limitation exceeds the foreign tax attributable to the property, the credit under this section for both the taxes imposed by the Dominion of Canada and the Province of Quebec is limited to $70,752. Credit may not be claimed separately under the convention for the Dominion succession duty and under this section for the Quebec succession duty.

Example (2). The decedent was a citizen of the United States, domiciled in France at death. It is assumed that death occurred after November 21, 1951, the effective date of the supplementary convention between the United States and Canada. The estate of the decedent consisted of stock of United States corporations valued at $750,000, the certificates for which were physically located in the United States; stock of French corporations endorsed in blank, the certificates for which were located in Canada, $50,000; and bearer bonds of French corporations, the certificates for which were in Canada, $200,000. Under the convention between the United States and France, the French stocks and bonds are deemed to be situated in France, and credit for the tax imposed by France in respect of such property is allowable under such convention. If not claimed under such convention, credit for the tax imposed by France is available under this section with respect to the stock of French corporations for the reason that under section 81.50 stocks of corporations are deemed situated in the country where the issuing company is incorporated or at the physical location of the certificates. No credit is allowable, under this section for tax imposed by France on the bonds of French corporations since, in accordance with section 81.50, bonds are considered as being situated at the physical location of the bonds. No credit is available under the convention between the United States and Canada with respect to the tax imposed by Canada on the French stocks and bonds for the reason that under such convention, the property is deemed to be situated in France. Credit, however, is allowable under this section for the Canadian tax attributable to the French stocks and bonds, the certificates for which were located in Canada.

(iv) If at the time the Federal estate tax return, Form 706, is filed, the foreign death tax has not been determined and paid, credit therefor may be entered on the return in an estimated amount. The computation of the credit should be set forth on a schedule attached to Form 706. However, before credit for foreign death tax is finally allowed satisfactory evidence such as a statement by an authorized official of each country, possession, or political subdivision thereof, imposing such tax must be submitted certifying (A) the full amount of such tax (exclusive of any interest or penalties), as computed before allowance of any credit, remission, or relief; (B) the amount of any credit, allowance, remission, or relief, and other pertinent information, including the nature of such allowance and a description of the property to which it pertains; (C) the net foreign death tax payable after such allowance; (D) the date on which such death tax was paid, or if not all paid at one time, the amount of each partial payment; and (E) a list of the property situated in such foreign country and subjected to its tax, showing a description and the value thereof. Satisfactory evidence must also be submitted showing that no refund of such death tax is pending and none authorized or, if any such refund is pending or has been authorized, the amount thereof and other pertinent information. The following information should also be submitted whenever applicable:

(A) If any of the property subjected to such death tax was situated outside of the country imposing the tax, the description of each item of such property and the value thereof.

(B) If more than one inheritance or succession is involved with respect to which credit is claimed, or where the foreign country, possession or political subdivision thereof imposes more than one kind of death tax, or where the foreign country, possession or political subdivision thereof each imposes a death tax, separate computation with respect to each inheritance, succession tax.

(v) In addition to the foregoing, the Commissioner may require the submission of any further proof deemed necessary to establish the right to credit.

(2) *Limitation on amount of credit allowable.*—(i) *General.*—The credit allowable under this section is limited to the smaller of the following amounts:

(A) The foreign death tax attributable to property situated in a foreign country, subject to foreign death tax, and included in the gross estate; or

(B) The Federal estate tax attributable to such property, as prescribed hereinafter.

(ii) *First limitation.*—The amount of the foreign death tax attributable to the property described in (i)(A) above, is an amount A, which bears the same ratio to B (the amount of the foreign death tax imposed upon the particular inheritance or succession, without allowance of credit, if any, for Federal estate tax) that C (the value of the inheritance or succession situated in the foreign country which was included in the gross estate for Federal estate tax) bears to D (the value of the entire inheritance or succession subjected to the foreign death tax). Where the foreign country imposes more than one kind of death tax or imposes taxes at different rates upon the several shares of an estate, or where the foreign country and a political subdivision or possession thereof each impose a death tax, the first limitation is to be computed separately for each such tax or rate. The values used in this proportion are the values determined for the foreign death tax. The amount of the foreign death tax for which credit is allowable must be converted into United States money.

As an example of the determination of the foreign death tax attributable to specific property, assume that the decedent was a citizen of the United States and his widow and son are beneficiaries under his will. The decedent owned real estate in Country X valued at $90,000 and stock of Y Corporation (a corporation organized under the laws of Country X) valued at $75,000. There is no death duty convention between the United States and Country X. $60,000 of the real estate and $15,000 of the stock of Y Corporation passed to the surviving spouse. Assume that under the laws of the Country X the inheritance tax is computed as follows:

Properties included in the widow's inheritance for tax of Country X

1. Value of real estate in X	$60,000
2. Value of stock of Corporation Y	15,000
Total value	75,000
Tax of Country X	12,000

Property included in the son's inheritance for tax of Country X

1. Value of real estate in X	$30,000
2. Value of stock of Corporation Y	60,000
Total value	90,000
Tax of Country X	14,400

The amount of the foreign inheritance tax attributable to personal property in the widow's inheritance is $\frac{\$15,000}{\$75,000} \times \$12,000 = \$2,400$. The amount of the foreign inheritance tax attributable to personal property in the son's inheritance is $\frac{\$60,000}{\$90,000} \times \$14,400 = \$9,600$.

1. Country X tax on personalty on widow's inheritance	$2,400
2. Country X tax on personalty on son's inheritance	9,600
Total Country X inheritance tax attributable to included property	12,000

(iii) *Second limitation.*—For the purpose of (i)(B) above, the amount of the Federal estate tax attributable to property for which the credit is allowable is to be computed as follows:

(*1*) The first step is to determine the value of the foreign property which enters into the computation. In case no deduction is allowed under section 812(c) (relating to the deduction for property previously taxed), section 812(d) (relating to the so-called charitable deduction), or section 812(e) (relating to the so-called marital deduction), such value shall be the value of property situated in the foreign country, subject to the foreign death tax, and included in the gross estate. However, if any deduction is allowable under section 812 (c), (d), or (e) such value shall be the value of property situated in the foreign country, subject to the foreign death tax, and included in the gross estate, reduced in accordance with the following rules: (*a*) Where any such property is specifically bequeathed, devised, or transferred to an organization described in section 812(d), or passes to the surviving spouse within the meaning of section 812(e), such value is to be reduced by the amount of the deduction under section 812(d) or (e) attributable to such bequest, devise, or transfer, or to the passing of such property. (*b*) Where any such property is property with respect to which a deduction may be allowed under section 812(c), such value shall be reduced by that part of the aggregate deduction allowed under section 812(c) which the value of such property with respect to which a deduction may be allowed under the first three paragraphs of section 812(c) bears to the value of all property with respect to which a deduction may be allowed under the first three paragraphs of section 812(c). (*c*) Where an interest in a group of assets which consists in part of such property is bequeathed, devised, or transferred to an organization described in section 812(d), or passes to the surviving spouse within the meaning of section 812(e), such value is to be reduced by an amount A which bears the same ratio to B (the amount of such bequests to charity or such property passing to the surviving spouse) which C (such property less the amount of reductions computed under paragraphs (*a*) and (*b*)) bears to D (the value of all property less (i) the amount of all property specifically bequeathed, devised, or transferred to an organization described in section 812(d), or specifically passing to the surviving spouse within the meaning of section 812(e), and (ii) the aggregate deductions allowed under section 812(c)). (*d*) For the purpose of determining the deduction under section 812(e) under rules (*a*) and (*c*) if the aggregate marital deduction allowed under section 812(e) is less than the amount of such deduction computed without regard to the limitation stated in section 81.47d, then the portion of such deduction attributable to particular property is an amount which bears the same ratio to the deduction which would be attributable to such property without regard to the limitation stated in section 81.47d as the aggregate marital deduction allowed bears to the aggregate marital deduction computed without regard to the limitation stated in section 81.47d.

(*2*) The second step is to compute the amount of the Federal estate tax attributable to property for which the credit is allowable, which is an Amount A, which bears the same ratio to B (the Federal estate tax, after allowance of credits for State inheritance, etc., taxes under section 813(b) and for gift taxes under sections 813(a) and 936(b)) as C (the value of the foreign property which enters into the computation, as determined under the first step) bears to D (the value of the gross estate, reduced by the aggregate amount of the deductions allowed under sections 812 (c), (d), and (e)).

The following examples indicate the application of the above rules of this subdivision. These examples are solely for the purpose of illustrating the determination of the amount of credit under this section and are without regard to the amount of credit which may be allowable under the convention between the United States and France.

Example (1). The decedent was a citizen of and domiciled in, the United States at time of death; a son and daughter were beneficiaries, each taking one-half of the residue of the estate, and cash in the amount of $400,000 was bequeathed to a charitable organization in the United States. The estate consists of shares of stock of United States corporations, the certificates for which were physically located in the United States, $750,000; bonds issued by the French Government physically located in the United States, $50,000; shares of stock of French corporations, the certificates for which were physically located in France, $200,000; and debts and administration expenses total $40,000. Under the situs rules prescribed in subdivision (*b*) (1) (ii), the French stock comprises the only property deemed to be situated in France. The amount of the French inheritance

tax in United States money imposed in respect of such property is $48,000. The amount of Federal estate tax is $133,300 after the allowance of State inheritance tax. The credit cannot exceed the amount of the Federal estate tax attributable to the included property which is

$$\frac{120{,}000\ \text{(French stocks adjusted)}}{600{,}000\ \text{(gross estate adjusted)}} \times \$133{,}300 = \$26{,}660.$$

Since the cash bequest to charity is not specifically identifiable with any particular property, each amount used in the above proportion is adjusted to reflect its prorated share of the charitable deduction allowed. The credit is allowable in the lesser of the two amounts, $26,660.

Example (2). The facts are the same as in example (1) except that, in lieu of the cash bequest to charity, $40,000 of the French stocks are specifically bequeathed to a public charitable establishment in France. The total amount of French inheritance tax attributable to property included in the gross estate is $42,800 ($4,800 allocable to the bequest to charity and $38,000 to the shares passing to the son and daughter). The amount of the Federal estate tax is $245,180. The credit cannot exceed the amount of the Federal estate tax attributable to the French stocks which is

$$\frac{160{,}000\ \text{(value of French stocks adjusted)}}{960{,}000\ \text{(gross estate adjusted)}} \times \$245{,}180 = \$40{,}863.33.$$

Since a charitable deduction is involved in this case, the value of the French stocks and the value of the gross estate are adjusted in computing the Federal estate tax attributable to the included property. As the amount of the Federal estate tax attributable to the property included in the gross estate (as adjusted) is less than the amount of the French tax attributable to the included property, the credit is allowable in the former amount, $40,863.33.

Example (3). The decedent was domiciled in the United States at death; his wife, son, daughter, and a charitable organization being the beneficiaries of his estate. The estate consists of shares of stocks of United States corporations, the certificates for which were physically located in the United States, $440,000; United States real estate, $100,000; shares of stocks of French corporations, the certificates for which were in France, $300,000; and debts and administration expenses total $40,000. He bequeathed $40,000 in real estate to a charity in the United States and $300,000 of French stocks and $200,000 of United States stocks to his wife. The residue of the estate passed to his children. Under the situs rules of subdivision (*b*) (1) (ii), the only property considered to be situated in France comprises the shares of stocks of the French corporations. The amount of French inheritance taxes in United States money is $71,250.

The adjusted gross estate is $840,000 less $40,000 debts and charges, or $800,000. The marital deduction is therefore limited to one-half of $800,000 or $400,000. The amount of the Federal estate tax, after the allowance of the 80 percent State inheritance tax credit, is $76,180. The French property comprised in the marital deduction is

$$\frac{400{,}000}{500{,}000} \times \$300{,}000 \text{ or } \$240{,}000.$$

The French inheritance tax attributable to the property included in the gross estate is $71,250. The credit, however, cannot exceed

$$\frac{60{,}000\ \text{(French property adjusted)}}{400{,}000\ \text{(gross estate adjusted)}} \times \$76{,}180 \text{ or } \$11{,}427.$$

The value of the French stock is adjusted for its prorated share of the marital deduction allowed and the value of the gross estate is adjusted for the marital deduction and the bequest to charity. As the amount of the Federal estate tax attributable to the included property is less than the amount of the French inheritance tax imposed on the property included in the gross estate, the credit is allowable in the amount of the former, $11,427.

(*3*) For the purposes of this limitation, where a particular foreign country imposes more than one kind of death tax or imposes taxes at different rates upon the several shares of an estate or a particular country and its possession or political subdivision each impose a death tax, the foreign property entering into the computation (as determined under step (1) above) which is subjected to each such tax or different rate shall be combined. The combined value shall not exceed the value at which such property was included in the gross

estate for Federal estate tax purposes. For example, if the Dominion of Canada imposes a succession duty with respect to property A at 10 percent and with respect to property B at 20 percent, or property A is subjected to tax by the Dominion of Canada and property B by the Province of Quebec, the total value of properties A and B shall be combined in computing this limitation. Further, in such a case, the foreign death taxes attributable to such property separately computed with respect to each tax or rate under the first limitation shall be combined when determining whether the foreign death tax is greater or smaller than the Federal estate tax attributable to such property. See part 1 of example (1) below.

(4) In case credits against the Federal estate tax are allowable under this section or under this section and one or more death duty conventions in respect of death taxes paid to more than one country, such credits shall be combined and the aggregate amount thereof credited against the Federal estate tax. If a particular item of property included in the gross estate is subjected to tax by more than one foreign country, the total amount of the credits is limited to the amount of the Federal estate tax attributable to such property, adjusted to give effect to the principles stated in (3) above. See part 2 of example (1) below. The amount of the Federal estate tax attributable to such property shall be determined in accordance with the rules prescribed for computing the second limitation in subdivision (*b*) (2) (iii).

Example (1). The decedent's estate consisted of properties A, B, and C, each valued at $100,000 for Federal estate tax purposes, and the total Federal estate tax with respect to all such property amounted to $72,000. Assume that properties A and B qualify for the credit and that such properties were fully subjected to foreign death tax as follows:

Property A by the Dominion of Canada	$20,000
Property B by the Province of Quebec	26,000
Property A by Country X	10,000

Since properties A and B were fully subjected to foreign death tax, the amount of the foreign death tax attributable to such property (computed separately under the first limitation for each separate foreign death tax) is the full amount of the foreign death taxes. The foreign death tax attributable to such property, thus computed separately under the first limitation with respect to each separate foreign death tax, is to be compared with the Federal estate tax attributable to such property computed under the second limitation.

Part (1). In the case of the property subjected to tax by the Dominion of Canada and the Province of Quebec, the amount of the Federal estate tax attributable to such property is not to be computed separately, under the second limitation with respect to each separate foreign tax, but properties A and B are combined as follows:

$$\frac{200{,}000\text{ (property subject to tax by Canada and Quebec)}}{300{,}000\text{ (gross estate)}} \times \$72{,}000\text{ (Federal tax)} = \$48{,}000$$

Further, the amounts of the Canadian and Quebec taxes attributable to properties A and B computed under the first limitation are combined ($46,000) for purposes of comparison with the Federal estate tax attributable to such property ($48,000) in determining the allowable credit with respect to the foreign death taxes imposed by Canada and Quebec. Credit is, therefore, allowable in the amount of $46,000 with respect to the taxes imposed by Canada and Quebec since this amount is less than the amount computed under the second limitation. Note: That if the second limitation were computed separately for properties A and B, the total credit allowable with respect to property B would be only $24,000 rather than $26,000.

Part (2). In the case of property A subjected to tax by Country X, the second limitation is computed as follows:

$$\frac{100{,}000\text{ (property subject to tax by X)}}{300{,}000\text{ (gross estate)}} \times \$72{,}000\text{ (Federal tax)} = \$24{,}000$$

The foreign tax imposed by Country X attributable to such property under the first limitation is $10,000. This amount is less than the Federal estate tax attributable to such property ($24,000), and on the basis of these facts alone, credit would be allowable for the tax imposed by Country X in the amount of $10,000. However, the Federal estate tax attributable to property A is $24,000 and, of this amount, $22,000 has been taken into account in part 1 of this example

in determining the credit allowable with respect to the death taxes imposed by the Dominion of Canada and the Province of Quebec as follows:

$20,000 credit allowed with respect to property A for the tax imposed by the Dominion of Canada;

$2,000 credit allowed with respect to property B in excess of the Federal estate tax attributable to such property ($24,000) for the tax imposed by the Province of Quebec.

Accordingly, additional credit allowable for the tax imposed by Country X is limited to $2,000. If, under the facts in this example, property B had also been subjected to death tax by Country X no additional credit would be allowable for such tax for the reason that the Federal estate tax attributable to such property amounted to only $24,000. Nevertheless, the credit of $26,000 otherwise allowable with respect to property B shall not be reduced. The combined credits allowable with respect to all foreign death taxes is limited to $48,000.

Example (2). If it be assumed under the facts otherwise indicated in example (1) above that only property A was subjected to foreign death tax, the total credit allowable with respect to such property would be $24,000. While the total death taxes imposed with respect to property A amounted to $30,000, the Federal estate tax attributable to such property amounted to only $24,000 and the credit is, accordingly, limited to the smaller amount.

(iv) *Allocation of credit.*—The amount computed under the lower of the two limitations is the total credit authorized with respect to both the basic and additional taxes. The amount of credit authorized against the basic estate tax is the lower of (A) the amount computed under the "first limitation" and (B) the amount of the basic estate tax attributable to the property computed in the manner described under the "second limitation." For this purpose, the basic estate tax is the net basic tax after allowance of credits for State inheritance, etc., taxes under section 813(b) and gift taxes under section 813(a). The amount of credit authorized against the additional estate tax is the lower of (C) the amount computed under the "first limitation" less the credit allowed against the basic estate tax and (D) the amount of the additional estate tax attributable to the property computed in the manner described in the "second limitation." For this purpose, the additional estate tax is the net additional tax after allowance of credit for gift tax under section 936(b).

(*c*) *Claim for credit or refund and interest on refund.*—The credit is also limited to such taxes as were actually paid and credit therefor claimed within 4 years after the filing of the return, except as otherwise provided in this paragraph. If a petition is filed with the Tax Court for the redetermination of a deficiency within the time prescribed by section 871(a) (see section 81.73), the credit is limited to such taxes as were actually paid and credit therefor claimed within 4 years after the filing of the return or before the expiration of 60 days after the decision of the Tax Court becomes final, whichever period is the longer. If an extension of time has been granted for payment of the tax shown on the return or of a deficiency under section 822(a)(2) or section 871(h), the credit is limited to such taxes as were actually paid and credit therefor claimed within 4 years after the filing of the return or before the date of the expiration of the extension, whichever period is the longer. Should the executor, in accordance with the provisions of sections 925 and 926, elect to postpone the payment of the Federal estate tax attributable to a reversionary or remainder interest, the credit allowable against the tax attributable to such interest is limited to estate, inheritance, legacy, or succession taxes attributable to such interest as are actually paid and credit therefor claimed prior to the expiration of 60 days after the termination of the precedent interest. (See section 927 of the Internal Revenue Code and section 81.79(*b*) of these regulations.)

Refund based on the credit, despite the provisions of sections 910, 911, and 912, will be made if claim therefor is filed within the period provided for filing claim for credit. Such refunds will be made without interest.

(*d*) *Recovery of death tax claimed as credit.*—If subsequent to the allowance of credit for death taxes under section 813 (b) or (c) or section 936(c), recovery is made of any overpayment of such taxes, then the executor or other person recovering such overpayment is required at once to notify the Commissioner thereof. The Commissioner will thereupon redetermine the additional amount of estate tax due resulting from the incorrect credit allowed and such amount will be paid by the executor upon receipt of notice and demand therefor. Assessment of such additional tax may be made at any time.

PAR. 6. Section 81.56 [26 CFR 81.56] is amended by changing the first sentence thereof to read as follows:

The provisions relating to credits under sections 81.8 and 81.9(*a*) and to rates and payment of the tax are the same in estates of nonresidents not citizens and of residents or citizens.

PAR. 7. There is inserted immediately after section 874 and preceding section 875 of the Internal Revenue Code which precede section 81.74 the following:

SEC. 603. FOREIGN ESTATE TAX CREDIT [REVENUE ACT OF 1951, ENACTED OCTOBER 20, 1951].

* * * * * * *

(d) EXTENSION OF PERIOD OF LIMITATIONS, ETC., IN CASE OF RECOVERY OF TAXES CLAIMED AS CREDIT.—Section 874(b) (relating to exceptions to general rule as to period of limitation upon assessment and collection of estate tax) is hereby amended by inserting at the end thereof the following new paragraph:

"(3) RECOVERY OF TAXES CLAIMED AS CREDIT.—If any tax claimed as a credit under section 813 (b) or (c) or section 936(c) is recovered from any foreign country, any State, any Territory or possession of the United States, or the District of Columbia, the executor, or any other person or persons recovering such amount, shall give notice of such recovery to the Secretary at such time and in such manner as may be required by regulations prescribed by him, and the Secretary shall redetermine the amount of the tax under this chapter and the amount, if any, of the tax due upon such redetermination, shall be paid by the executor or such person or persons, as the case may be, upon notice and demand."

(e) EFFECTIVE DATE.—The amendments made by this section shall be applicable with respect to estates of decedents dying after the date of the enactment of this Act.

PAR. 8. Section 81.74 [26 CFR 81.74] is amended by striking the first sentence of the fourth paragraph and inserting in lieu thereof the following:

All assessments against executors (as to assessments against transferees and fiduciaries, see section 81.102), except in the case of a false or fraudulent return, or of a failure to file a return, or in the case of the recovery of tax claimed as a credit under section 813 (b) or (c) or section 936(c), must be made within 3 years after the return was filed.

PAR. 9. There is inserted immediately preceding section 81.79 [26 CFR 81.79] the following:

SEC. 603. FOREIGN ESTATE TAX CREDIT [REVENUE ACT OF 1951, ENACTED OCTOBER 20, 1951].

* * * * * * *

(c) REVERSIONARY OR REMAINDER INTEREST.—Section 927 (relating to credit for State death taxes) is hereby amended to read as follows:

"SEC. 927. CREDIT FOR DEATH TAXES.

"Such part of any estate, inheritance, legacy, or succession taxes allowable as a credit under section 813 (b) or (c) against the tax imposed by this subchapter, or under section 936(c) against the tax imposed by subchapter B, as is attributable to such reversionary or remainder interest may be allowed as a credit against the tax attributable to such interest, subject to the limitations on the amount of credit contained in such sections, if such part is paid, and credit therefor claimed, at any time prior to the expiration of 60 days after the termination of the precedent interest or interests in the property."

* * * * * * *

(e) EFFECTIVE DATE.—The amendments made by this section shall be applicable with respect to estates of decedents dying after the date of the enactment of this Act.

PAR. 10. Section 81.79, as amended by Treasury Decision 5699 [26 CFR 81.79] is further amended as follows:

(A) By striking therefrom the sentence in the last paragraph of (*a*) beginning "An extension of time to pay the tax", and inserting in lieu thereof the following:

An extension of time to pay the tax may extend the period within which taxes allowed as a credit by section 813 (b) or (c) or section 936(c) are required to be paid and the credit therefore claimed. (See section 81.9);

(B) By amending the fifth paragraph of (*b*) thereof to read as follows:

If the time for payment of Federal estate tax attributable to a reversionary or remainder interest in property is postponed, all estate, inheritance, legacy, or succession taxes allowable as a credit under the provisions of sections 813 (b) or (c), or 936(c), which are paid and for which credit is claimed within the period provided in such sections will be allowed (not to exceed the limitations in such sections) and the allowance will be applied first to the respective portions of the Federal tax attributable to the same interests in property to which the estate, inheritance, legacy, or succession taxes are attributable. Estate, inheritance, legacy, or succession taxes, as described in section 813 (b) or (c), or under section 936(c), which are attributable to the reversionary or remainder interest and which are paid and for which credit is claimed after the expiration of the period provided in those sections will also be allowed as a credit against the Federal tax attributable to such interest (not to exceed the limitations in such sections) if such taxes are paid and credit therefor is claimed prior to the expiration of 60 days after the termination of the preceding interest or interests in the property;

(C) By inserting the following example immediately following the example in the fifth paragraph of (*b*):

Example. The facts are the same as in the preceding example except that, in addition, the estate is entitled to a credit for foreign death tax paid in the amount of $4,000. The additional Federal estate tax before allowance of such credit is $142,500, of which $47,500 is attributable to the reversionary or remainder interest and $95,000 is attributable to other property. Of the total credit of $4,000 for foreign death tax, $1,000 is attributable to the reversionary or remainder interest and $3,000 to other property. $500 of the credit is allowable against the Federal basic tax and $3,500 against the additional tax. Assume that the foreign death tax paid within the 4-year period amounts to $3,500 none of which is attributable to the reversionary or remainder interest. Of this payment, $500 will be credited against the Federal basic tax and $3,000 against the additional tax. Accordingly, under these added facts, the estate will be required to pay at once $1,500 (Federal basic tax attributable to property other than the reversionary or remainder interest minus the credits of $8,000 and $500) and the additional Federal tax of $92,000 (the additional Federal estate tax of $95,000 attributable to property other than the reversionary or remainder interest minus the credit of $3,000). An extension will be allowed for payment of $4,000 (Federal basic tax of $5,000 minus credit for State inheritance tax of $1,000) and $47,500 (the portion of the additional Federal tax attributable to the reversionary or remainder interest). After expiration of the 4-year period, but before expiration of 60 days after termination of the precedent interest, the estate pays additional State estate, inheritance, legacy, or succession taxes of $5,000 and foreign death tax of $1,000 attributable to the reversionary or remainder interest. As the maximum credit for both taxes is $16,000, and $12,500 has already been allowed, there will be an additional allowance of $3,500 and the estate will be required to pay $48,000 at the end of the extension period. ; and

(D) By inserting in the first sentence of the last paragraph thereof immediately after "District of Columbia" the following: ", or by any foreign country".

PAR. 11. The second sentence of the last paragraph of section 81.80 [26 CFR 81.80] is amended to read as follows:

An extension of time to pay the deficiency may extend the period within which taxes allowed as a credit by section 813 (b) or (c) or section 936(c) are required to be paid and the credit therefor claimed. (See sec. 81.9.)

PAR. 12. Section 81.97 [26 CFR 81.97] is amended by striking therefrom the last sentence and inserting in lieu thereof the following:

If a refund is based upon the credit for payment of estate, inheritance, legacy, or succession taxes allowed by section 813 (b) or (c) or section 936(c) (see sec. 81.9), the refund will be made without interest.

(This Treasury Decision is issued under the authority contained in sec. 3791 of the Internal Revenue Code (53 Stat. 467; 26 U. S. C. 3791).)

T. COLEMAN ANDREWS,
Commissioner of Internal Revenue.

Approved July 29, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register August 3, 1953 at 8:51 a. m.)

SUBPART II.—RETURNS AND PAYMENT OF TAX

SECTION 822.—PAYMENT OF TAX

REGULATIONS 105, SECTION 81.78: Payment with bonds or notes of the United States.

INTERNAL REVENUE CODE

Application of United States Treasury bonds in payment of Federal estate taxes. (See Rev. Rul. 156, p. 253.)

PART III.—ESTATES OF NONRESIDENTS NOT CITIZENS OF THE UNITED STATES

SECTION 861.—NET ESTATE

REGULATIONS 105, SECTION 81.13: Property of decedent at time of death. Rev. Rul. 187

INTERNAL REVENUE CODE

Upon the death of a foreign envoy duly accredited to the United States who at the time of death is neither domiciled in nor a national of the United States, the estate tax is not applied to personal property used by him in the conduct of his official mission and reasonably required for such purpose. The estate tax is applied to personal property not so used (such as bonds or shares of corporate stock or other investment property) and to all real property situated in the United

States, owned by the envoy. The agreement, effective November 21, 1947, between the United States of America and the United Nations respecting the headquarters of the United Nations (61 Stat. 3416, 3427) provides that certain representatives of member nations and their staffs and certain representatives of specialized agencies and their staffs shall be entitled to the same privileges and immunities accorded to diplomatic envoys accredited to the United States. In the event of the death of any such representatives or such staff members their estates are accorded the same estate tax treatment as is applied to estates of deceased envoys accredited to the United States.

CHAPTER 4.—GIFT TAX

SECTION 1000.—IMPOSITION OF TAX

REGULATIONS 108, SECTION 86.2: Transfers reached.

INTERNAL REVENUE CODE

A gift by the wife of one-half the proceeds of an insurance policy on life of the husband becomes absolute in Louisiana upon death of the husband. (See Rev. Rul. 232, p. 268.)

REGULATIONS 108, SECTION 86.3a: Gift of husband or wife to third party after April 2, 1948. Rev. Rul. 146

INTERNAL REVENUE CODE

Where a husband and his wife elect to treat any gifts of property made by one of the spouses to third persons during the year as having been made one-half by each spouse, the consent which is executed for that year under section 1000(f) of the Internal Revenue Code will apply to all of the gifts made by the spouses during the year, including every gift of separate property made by the husband or the wife even though a consent is executed only on one of the separate gift tax returns which are filed.

REGULATIONS 108, SECTION 86.3a: Gift of husband or wife to third party after April 2, 1948. Rev. Rul. 188

INTERNAL REVENUE CODE

A husband and wife, each having failed to execute the "consent of spouse" paragraph on the Federal gift tax return, Form 709, filed by the other, will not be denied the gift-splitting privilege provided by section 1000(f) of the Internal Revenue Code if on each of their separate gift tax returns they signified their consents to treat all gifts made by them to third parties as having been made one-half by each spouse.

Advice is requested whether the gift-splitting privilege provided by section 1000(f) of the Internal Revenue Code should be denied to

a husband and wife where on each of their separate Federal gift tax returns, Form 709, they signified consents to treat all gifts made by them to third parties as having been made one-half by each spouse but failed to execute the "consent of spouse" paragraphs on each other's returns.

In the instant case the donor filed a Federal gift tax return for the year involved and elected to split the gifts made between himself and his wife. The wife filed a separate gift tax return. On each of the separate returns the parties indicated in answering question "B" that each consented to have the gifts made by them to third parties considered as having been made one-half by each spouse. However, on neither of the returns of the husband or the wife was the "consent of spouse" paragraph executed. The question presented is whether the filing of the separate returns and the affirmative answers thereon relating to consents satisfy the requirements of section 1000(f) of the Code and the regulations promulgated pursuant thereto so as to permit the gift-splitting privileges to each spouse.

Section 1000(f) of the Code, insofar as it is pertinent to the question in issue, provides that a gift made after the date of the enactment of the Revenue Act of 1948 (April 2, 1948) by one spouse to a person other than his spouse shall, for the purpose of the Federal gift tax, be treated as having been made one-half by each spouse. This provision of the gift tax law is applicable only if both parties consent (in accordance with the regulations) to treat all such gifts made during the year by either while married to the other as having been made one-half by each spouse. Subparagraph (b) of section 86.3a reads in pertinent part as follows:

> Consent to the application of the provisions of section 1000(f) with respect to a calendar year shall, in order to be effective, be signified by both spouses. If both spouses file gift tax returns, Form 709, within the time for signifying consent it is sufficient if (1) the consent of both spouses is signified on one of such returns or (2) the consent of one spouse is signified on one such return and the consent of the other spouse is signified on the other return. If only one spouse files a gift tax return within the time provided for signifying consent, the consent of both spouses shall be signified on such return. However, wherever possible notice of the consent is to be shown on both returns. * * *.

In view of the foregoing it is held that if it is necessary for only one spouse to file a Federal gift tax return the "consent of spouse" paragraph must be executed on such return by the other spouse; or, if either spouse should on his or her return neglect to answer question "B" on the return relating to consents, execution of said paragraph would likewise be essential. However, where each party has on his and her separate return by an affirmative answer to question "B" signified consent to treat all gifts made by them to third parties as having been made one-half by each spouse (and if such gifts otherwise qualify), the parties will not be denied the gift-splitting privilege because of the failure to execute the "consent of spouse" paragraphs on each other's returns. The affirmative answers by each to question "B" relating to consents constitutes a sufficient compliance with the requirements of section 1000(f) of the Code and the regulations promulgated pursuant thereto. As to the effect of a consent executed by only one of the spouses, see Rev. Rul. 146, page 292, this Bulletin.

SECTION 1005.—GIFTS MADE IN PROPERTY

REGULATIONS 108, SECTION 86.19: Valuation of property. **Rev. Rul. 189**

INTERNAL REVENUE CODE

Restrictions attaching to shares of corporate stock, providing that the owner may not sell, transfer, or otherwise dispose of the shares without first offering them for sale to certain interested persons at a fixed price, or at a price determined by the application of a particular formula, while a factor to be considered with all other pertinent factors of valuation, are not binding upon the Commissioner in determining fair market values for Federal gift tax purposes. See *Estate of Halsted James* v. *Commissioner*, 148 Fed. (2d) 236; *Charles T. Kline* v. *Commissioner*, 130 Fed. (2d) 742; *Frederick Kraus et al.* v. *United States*, 140 Fed. (2d) 510; *Commissioner* v. *Harrison K. McCann*, 146 Fed. (2d) 385; *Harry H. Spitzer* v. *Commissioner*, 153 Fed. (2d) 967. Also see Rev. Rul. 157, page 255, this Bulletin.

CHAPTER 9.—EMPLOYMENT TAXES

SUBCHAPTER A.—EMPLOYMENT BY OTHERS THAN CARRIERS

PART I.—TAX ON EMPLOYEES

SECTION 1401.—DEDUCTION OF TAX FROM WAGES

REGULATIONS 128, SECTION 408.304: Collection of, and liability for, employee tax.

INTERNAL REVENUE CODE

Withholding table combining employee tax under the Federal Insurance Contributions Act and Federal income tax to be withheld from weekly wages paid on and after January 1, 1954. (See Rev. Rul. 294, p. 317.)

PART III.—GENERAL PROVISIONS

SECTION 1426.—DEFINITIONS

REGULATIONS 128, SECTION 408.204: Who are employees. **Rev. Rul. 233**

(Also Section 1607, Section 403.204, Regulations 107; Section 1621, Section 405.101, Regulations 116.)

INTERNAL REVENUE CODE

Babysitters performing services for the customers of an establishment engaged in a babysitter service which furnishes rules in-

structing them in their conduct while on assignment and the nature of services to be performed as well as the manner of performance of such services are employees of that establishment for purposes of Federal employment taxes and wages for such services are subject to withholding of income tax under section 1622 of the Internal Revenue Code.

Advice is requested whether individuals performing services as babysitters for the customers of a babysitter service are employees of that establishment for Federal employment tax purposes.

An establishment which is engaged in the operation of a complete babysitter service furnishes its customers with babysitters and assumes full responsibility with respect thereto. The establishment advertises in the classified section of the telephone directory and by distribution of business cards through personal contact. Parents applying for babysitters (from the establishment) sign an agreement whereby a certain charge is fixed by the establishment for the services of the babysitters plus an additional amount to the firm.

The individuals engaged as babysitters are personally interviewed by the establishment and their qualifications checked with respect to personal habits and character, as well as for their ability to care for children. A card record is maintained by the establishment on each babysitter showing all pertinent information with respect to qualifications such as the individual's name, address, former address, date on health card, date on police identification card, personal references, business references, availability, job preference, etc. An availability list is made up each day in order that each babysitter may be given her turn for assignment. The establishment furnishes each babysitter a set of rules or instructions covering the services required. Those rules or instructions provide, among other things, that babysitters are not to take over as permanent any assignment made to them; that they are not to give the parents their personal telephone numbers; that if parents insist on having such numbers, they may be given, but the establishment must be notified of any future appointments; that a 4-hour minimum engagement, plus transportation fee, is obtained by the establishment for the babysitters; and that any suggestion by the parents to bargain differently is to be ignored. The rules further provide that the babysitters must not entertain on an assignment; that they must not ask how late the assignment will be; that they may feel free to rest after 1 a. m.; that if they become ill on an assignment or accept an assignment which they cannot fulfill, they must call the establishment; and that the child must not be left alone for any reason. A weekly report and accounting is made by the babysitter to the establishment.

The establishment retains the right to exercise direction and control over the services performed by the babysitters to an extent sufficient to constitute an employer-employee relationship. Accordingly, it is held that the babysitters are employees of the establishment for the purposes of the Federal Insurance Contributions Act and the Federal Unemployment Tax Act, and the withholding of income tax at the source on wages under section 1622 of the Internal Revenue Code.

REGULATIONS 128, SECTION 408.204: Who are employees. (Also Section 1607, Section 408.204, Regulations 107.) Rev. Rul. 261

INTERNAL REVENUE CODE

A pathologist engaged to devote his time and ability to the management of a pathological laboratory for a hospital under an agreement whereby he may not assume outside duties to the detriment of his primary services to the hospital, may not contract to provide pathology service to other hospitals without the written consent of the administrator of the hospital, and is required to comply with all rules and regulations of the hospital, is an employee of the hospital for purposes of the Federal Insurance Contributions Act and the Federal Unemployment Tax Act.

Advice is requested whether a pathologist who conducts a laboratory in a hospital under the conditions hereinafter set forth is an employee of the hospital for the purposes of the Federal employment taxes.

Under a contract between the pathologist and the hospital the hospital agrees to furnish space, equipment, utilities, and related services, including maintenance and repairs for the laboratory. The pathologist agrees to conduct and operate the hospital's laboratory as its director and administrative head, and is the sole judge of the scientific procedures used therein. He is required to devote his time and ability to the proper management of the laboratory, and thereby foster the respective interest of the hospital and its medical staff. He is required to comply with the policies, rules, and regulations of the hospital, subject to State and Federal laws applicable to his professional practice. In addition, he is required to assume certain teaching and other duties. He may not assume outside duties to the detriment of his primary services to the hospital, nor shall he contract to provide pathology service to other hospitals without written consent of the administrator of the hospital.

The pathologist receives a monthly compensation equal to a stated percentage of all charges appearing on the books and records of the hospital for services rendered by the pathologist and the laboratory. However, in the event his monthly compensation does not total a guaranteed amount of $6x$ dollars per year, proper adjustment will be made at the end of the year.

All laboratory services performed by the pathologist and other laboratory personnel are considered by the parties concerned to be services rendered by the hospital, and it is the responsibility of the hospital to prepare bills, keep books and records, and collect for all such services. The pathologist and other laboratory personnel are required to prepare such daily or periodic records and reports as may be necessary to expedite the maintenance by the hospital of proper records of the work and services performed in the laboratory. Such daily records and reports are considered hospital records. The policies of the laboratory are established by the hospital and the pathologist. Laboratory charges are determined by the pathologist after consultation with the administrator of the hospital, and with the approval of the board of trustees. Such charges must be in accord with the prevailing charges in the area.

The selection of personnel deemed necessary to the operation of the laboratory, their tenure of employment, assignment of duties, place of

work, hours of work, and all other employment factors are determined by the pathologist only after consultation with, and subject to the approval of, the hospital's administrator and its board of trustees. All such personnel are considered by the hospital to be its employees, and are required to observe rules and regulations prescribed by the hospital for its other employees.

Section 408.204(c) of Regulations 128 provides in part that every individual is an employee if under the usual common law rules the relationship between him and the person for whom he performs services is the legal relationship of employer and employee. Such section further provides that generally such relationship exists when the person for whom services are performed has the right to control and direct the individual who performs the services, not only as to the result to be acomplished by the work but also as to the details and means by which that result is accomplished. That is, an employee is subject to the will and control of the employer not only as to what shall be done but how it shall be done. In this connection, it is not necessary that the employer actually direct or control the manner in which the services are performed; it is sufficient if he has the right to do so. The right to discharge is also an important factor indicating that the person possessing that right is an employer. Other factors characteristic of an employer, but not necessarily present in every case, are the furnishing of tools and the furnishing of a place to work, to the individual who performs the services.

From the facts presented, it is apparent that the hospital either exercises or has the right to exercise such control and direction over the pathologist as to establish the relationship of employer and employee. Accordingly, it is held that the pathologist is an employee of the hospital for the purposes of the Federal Insurance Contributions Act and the Federal Unemployment Tax Act. (*Cf.* S. S. T. 363, C. B. 1939-1 (Part 1), 291.)

REGULATIONS 128, SECTION 408.208: Agricultural labor. Rev. Rul. 159

INTERNAL REVENUE CODE

A full-time employee of a greenhouse, who devotes at least 80 percent of his time in the performance of agricultural labor within the meaning of section 1426(h) of the Federal Insurance Contributions Act and the remaining 20 percent of his time in the performance of other services of an incidental nature is considered as being engaged to perform agricultural labor on a full-time basis for the purposes of such act. Where such an individual has qualified as a regular employee of his employer for a calendar quarter of a year, the wages received by him in each succeeding quarter are taxable under the provisions of the Federal Insurance Contributions Act so long as he earns $50 or more in cash wages and works for the same employer on 60 or more days on a full-time basis.

Advice is requested whether an employee of the operator of a greenhouse, who devotes approximately 80 percent of his working time to the growing and cultivating of horticultural products and the remaining portion of his time in the performance of other services of an incidental nature is considered to be engaged to perform agricultural services on a full-time basis within the meaning of section 1426(b)(1)(A) of the Federal Insurance Contributions Act.

In the instant case, the operator of a greenhouse raises flowers and other horticultural commodities and sells them at retail. All of his business operations are conducted from one unit, which includes a greenhouse, display and salesroom, and garage, and in which are produced one-half or less of the horticultural commodities marketed. On October 1, 1952, he engaged an employee to perform services on a full-time basis. The employee generally worked 48 hours per week, the working hours varying with the number of daylight hours each day. He performed services on 6 days of each week during the first quarter of 1953, devoting at least 80 percent of his working time to the actual growing and cultivating of horticultural products, which constituted agricultural labor, and the remaining portion of his time to preparing bouquets and making deliveries during rush periods. Such latter services could not qualify as agricultural labor under paragraph 4(A) of section 1426(h) of the act since the operator did not produce more than one-half of the commodities marketed. He was paid more than $50 for his services during such quarter.

The term "employment," as defined in the Federal Insurance Contributions Act in effect on and after January 1, 1951, does not include "agricultural labor" performed in any calendar quarter by an employee for his employer unless the cash remuneration paid for such labor (with certain specified exceptions) is $50 or more and such labor is performed by an individual who is regularly employed to perform such "agricultural labor." In order for an employee to be "regularly employed" within the meaning of section 1426(b)(1)(A) of the act he must first be continuously employed (not necessarily in farm labor) by the same employer during all of a calendar quarter, which is known as the "qualifying quarter," and in the next following quarter he must perform "agricultural labor" for the same employer on a full-time basis on 60 or more days.

In order to satisfy the requirement of the performance of agricultural labor on a full-time basis on at least 60 days during a calendar quarter, the arrangement under which an employee performs agricultural labor for an employer must contemplate the performance of such labor on a full-time basis, and the employee must perform agricultural labor for the employer on at least 60 days during the calendar quarter. Thus, the requirement of the performance of agricultural labor on a full-time basis relates to the arrangement under which the employee is engaged to perform agricultural labor, whereas the requirement of the performance of agricultural labor on at least 60 days during a calendar quarter relates to the performance of agricultural labor by an employee on the required number of days during such calendar quarter. An arrangement for the performance of agricultural labor on a full-time basis means an arrangement under which an employee is engaged to perform agricultural labor for a single employer on the basis of a full workday. The term "full workday" as used in the preceding sentence has reference to the full workday prevailing in the particular locality for the type of agricultural occupation in which the employee is engaged. The fact that an employee who performs agricultural labor primarily for one employer also performs other services of an incidental character for such employer or any incidental services for some other person does not prevent such employee from being engaged on a full-time basis in the performance

of agricultural labor for such employer. In determining whether an employee has performed agricultural labor on at least 60 days during a calendar quarter, there shall be counted as 1 day—

(A) any day or portion thereof on which the employee actually performs such labor; and

(B) any day or portion thereof on which the employee does not perform agricultural labor but with respect to which cash remuneration is paid or payable to the employee for such labor, such as a day on which the employee is sick or on vacation.

An employee who reports for work on a particular day and, at the direction of his employer, holds himself in readiness to perform agricultural labor will be considered to be engaged in the actual performance of such labor on that day.

In the instant case a continuing employer-employee relationship of the type necessary to constitute a "qualifying quarter" within the meaning of section 1426(b)(1)(A)(ii)(I) of the Federal Insurance Contributions Act, as amended, existed between the operator of the greenhouse and his employee during the calendar quarter ended December 31, 1952. Moreover, pursuant to the principles set forth above, the employment agreement with the operator of the greenhouse contemplated the performance of agricultural labor on a full-time basis. The fact that during the calendar quarter ended March 31, 1953, the employee devoted not more than 20 percent of his time to the performance of services which do not constitute "agricultural labor," as defined in section 1426(h) of the Federal Insurance Contributions Act, does not operate to prevent his classification as being engaged to perform agricultural services on a full-time basis since such services are of an incidental character. Accordingly, inasmuch as the employee performed "agricultural labor" for the operator of the greenhouse on a full-time basis on 60 or more days during the calendar quarter ended March 31, 1953, and earned cash remuneration of $50 or more for such services, liability for the taxes imposed under the Federal Insurance Contributions Act was incurred with respect to the wages for such services.

REGULATIONS 128, SECTION 408.208: Agricultural labor. Rev. Rul. 174

INTERNAL REVENUE CODE

(1) A partnership which entered into crop purchase agreements with various growers of grapes and peaches on an acreage basis does not qualify as the operator of a farm within the meaning of section 1426(h)(4)(A) of the Federal Insurance Contributions Act, as amended, even though it conducts some, if not all, of the operations necessary for the production and harvesting of such crops; (2) the services performed by the partnership's employees after 1950 in hauling such crops to its packing plant as well as services performed at the plant do not constitute "agricultural labor" for the purposes of such act; however, (3) the services performed by the partnership's employees on the farms of the sellers, prior to and on or after January 1, 1951, in connection with the cultivation, harvesting, and other related services of such crops constitute "agricultural labor" within the meaning of such act.

Advice is requested whether a partnership qualifies as the operator of a farm within the meaning of section 1426(h)(4)(A) of the Federal Insurance Contributions Act, as amended, through its ac-

tivity in connection with certain crop purchase agreements on an acreage basis with various growers of grapes and peaches, and as to the status of the partnership's employees for the purposes of such act.

At the beginning of the growing season the partnership in the instant case entered into crop purchase agreements with the growers of grapes and peaches of a certain variety, grown on specified acreages owned by the sellers, for which the partnership pays the sellers a fixed sum at the times and in the amounts specified. The agreements stipulate whether the necessary crop production operations such as cultivating, irrigating, etc., are to be conducted by the partnership or by the sellers. In all cases the partnership pays for the fertilizer and sulphur used, and its employees do the necessary girdling, thinning, leaf stripping, packing, loading, hauling, and packaging and sometimes the cultivating, irrigating, fertilizing, and pruning. The partnership owns and furnishes all the equipment used in its operations. From about June 1 until the end of the harvest season the taxpayer hires a regular field crew of 25 or 30 members and during the rush season an additional crew.

Section 1426(h) of the Federal Insurance Contributions Act, as amended by the Social Security Act Amendments of 1950, provides in part as follows:

> AGRICULTURAL LABOR.—The term "agricultural labor" includes all service performed—
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> * * * * * * *
>
> (4) (A) In the employ of the operator of a farm in handling, planting, drying, packing, packaging, processing, freezing, grading, storing, or delivering to storage or to market or to a carrier for transportation to market, in its unmanufactured state, any agricultural or horticultural commodity; but only if such operator produced more than one-half of the commodity with respect to which such service is performed.

Section 408.208(d) (5) of Regulations 128 provides that the "operator of a farm" as used in section 1426(h) (4) (A) of the act means an owner, tenant, or other person, in possession of a farm and engaged in the operation of such farm. If the partnership in the instant case is held to be the operator of a farm, the services of its employees performed in handling, planting, etc., as specified in section 1426(h) (4) (A), *supra*, would constitute "agricultural labor" and would be considered taxable employment only if the conditions specified in section 1426(b) (1) (A) of the act are met; otherwise, those services will constitute taxable employment without regard to the provisions of section 1426(b) (1) (A) of the act (see Rev. Rul. 159, p. 297, this Bulletin), unless excluded by the operation of section 1426(c) of the act.

Under the terms of the crop purchase agreements the "seller" does not surrender, nor is there vested in the partnership a right of possession to the land covered by the agreement. The partnership's right of possession extends only to possession of the specific crop grown on the land and the payment made to the seller is for crop produced. While the partnership conducts or pays for certain operations necessary for the production of the crop, the number of specific operations to be conducted by each party is a matter of bargaining or agreement related to the production and ultimate disposition of a crop and not

the discharge by the partnership of duties devolving upon it as the operator of a farm.

Under such circumstances the partnership does not qualify as the "operator of a farm" within the meaning of section 1426(h)(4)(A) of the act, as amended, and the services performed after 1950 by its employees in hauling to its packing plant any agricultural or horticultural commodities obtained under its crop purchase agreements, as well as services performed in its plant in the handling, grading, packing, etc., of such commodities and delivering them to market or to a carrier for transportation to market, do not constitute "agricultural labor" within the meaning of the act.

However, the services performed by the partnership's employees on the farms of the sellers covered by the crop purchase agreements, prior to and on and after January 1, 1951, which relate to the cultivation of the soil and raising of grapes and peaches, such as the application of fertilizer, sulfur, etc., irrigation services, girdling, thinning, pruning, leaf stripping, and other related services, as well as services performed in the harvesting and field loading of grapes and peaches, constitute "agricultural labor" within the meaning of section 1426(h)(1) of the act.

If one-half or more of an employee's time in the employ of the partnership in a particular pay period is spent in performing services which constitute employment under section 1426(b) of the act, then all of the services of that employee for the partnership in that pay period shall be deemed to be employment; however, if less than one-half of the employee's time is spent in performing services which constitute employment, then none of his services shall be deemed to be employment. For this purpose, a pay period is construed as a period (of not more than 31 days) for which a payment of remuneration is ordinarily made to the employee by the employer.

REGULATIONS 128, SECTION 408.213: United States and instrumentalities thereof. Rev. Rul. 147

(Also Section 1621, Section 405.101, Regulations 116.)

INTERNAL REVENUE CODE

Remuneration paid by the Department of the Army to civilian instructors at army education centers located in the Panama Canal Zone for services performed on a contract or fee basis, does not constitute "wages" with respect to "employment" for the purposes of the Federal Insurance Contributions Act, as amended. However, such remuneration paid to civilian instructors who are citizens or residents of the United States, constitute "wages" subject to withholding of income tax at the source under section 1622 of the Internal Revenue Code.

Advice is requested whether the remuneration for services performed on a contract or fee basis by civilian instructors at army education centers located in the Panama Canal Zone constitutes "wages" for the purposes of the Federal Insurance Contributions Act, as amended, and withholding of income tax at the source under section 1622 of the Internal Revenue Code.

Civilian instructors performing services in the army education centers located in the Panama Canal Zone are engaged under

authority of section 2(c) of the Armed Services Procurement Act of 1947, 62 Stat. 21, and paragraph 18b(1) of Department of the Army Special Regulations 355–30–1, dated August 8, 1950, as amended. Paragraph 18b(1) of Special Regulations 355–30–1, as amended, relating to instructors engaged on a fee basis, provides that such instructors will not be appointed to positions in the competitive service as employees of the Department of the Army, but will have the status of independent contractors engaged on a fee basis for services separate and complete in themselves, and not computed on a per diem or other time basis. Instructors will be paid on the basis of a specific fee for each individual teaching session, purely on a performance basis without any bulk, annual, or periodic method of computation.

Department of the Army Special Regulations 355–30–1, as amended, further provide that army education centers include facilities, personnel, and equipment provided and designated by the commanding officer for army education program activities. Tests designed to place individual students at various educational levels are available from the United States Armed Forces Institute, hereinafter referred to as USAFI. Instructions for administration accompany the tests, and the educational placement levels based upon individual test scores are prescribed by the USAFI. Group-study courses offered under the army education program may be based upon either USAFI materials and tests or upon those of civilian institutions, but the two types may not be intermingled in any one course. When an army education program group study class which utilizes non-USAFI materials is completed, a descriptive outline of the course, a duplicate individual class record card for each student and the test answer sheet must be forwarded to the appropriate USAFI. The outline of the course must include the following:

"(1) Title, author, and copyright date of each text used.

"(2) Length of course in hours, and number and frequency of class meetings.

"(3) Outline of qualifications of instructors. (Experience qualifications or number of hours of pertinent training.)

"(4) A copy of the end-of-course test used, with certificate attached stating that it was administered and used under the conditions and the manner required for administration and use of USAFI end-of-course tests."

Standards of progress have been established which students are expected to achieve, and the work of the instructors is observed and inspected to insure that the students achieve such standards.

Section 1426(b) of the Federal Insurance Contributions Act, as amended, provides in part as follows:

> The term "employment" means * * * any service, of whatever nature, performed after 1950 * * *; except that * * * such term shall not include—
>
> (C) Service performed in the employ of the United States or in the employ of any instrumentality of the United States, if such service is performed—
>
> * * * * * * *
>
> (v) by any individual as an employee who is excluded by Executive order from the operation of the Civil Service Retirement Act of 1930 because he is paid on a contract or fee basis * * *

Section 1622 of the Internal Revenue Code provides in part as follows:

(a) REQUIREMENT OF WITHHOLDING.—Every employer making payment of wages shall deduct and withhold upon such wages a tax equal to 18 per centum of the amount by which the wages exceed the number of withholding exemptions claimed, multiplied by the amount of one such exemption as shown in subsection (b) (1), except that in the case of wages paid on or after November 1, 1951, and before January 1, 1954, the tax shall be equal to 20 per centum of such excess in lieu of 18 per centum.

It is the opinion of this Bureau that the Department of the Army exercises or has the right to exercise control over the services of the instructors at army education centers to an extent sufficient to establish the relationship of employer and employee. If the relationship of employer and employee exists, the description of the relationship by the parties as anything other than that of employer and employee is immaterial. Thus, it is of no consequence that the employee is designated as a partner, coadventurer, agent, or independent contractor. (See, however, sec. 1420(e) of the Act.)

It is presumed that the services of the instructor-employees at army education centers, paid on a contract or fee basis, are excluded from operation of the Civil Service Retirement Act by Executive Order 9154 of May 1, 1942, and amendments thereto, unless their services are covered under such Act by reason of continuity of service, reinstatement, or otherwise. Accordingly, it is further the opinion of this Bureau that remuneration paid to civilian instructors for services performed on a contract or fee basis at army education centers located in the Panama Canal Zone is not subject to the taxes imposed by the Federal Insurance Contributions Act, as amended, but that remuneration paid to civilian instructors who are citizens or residents of the United States for such services constitutes "wages" for the purpose of withholding of income tax at the source under section 1622 of the Code.

REGULATIONS 128, SECTION 408.226: Wages. (Also Section 1607, Section 403.227, Regulations 107; Section 1621, Section 405.101, Regulations 116; Section 22(n), Section 29.22(n)-1; Section 23(a), Section 29.23 (a)-1; Section 147, Section 29.147-2, Regulations 111.) Rev. Rul. 190

INTERNAL REVENUE CODE

Reasonable transportation allowances paid by a company to its employees while working for a strictly temporary period on a construction project located at a distance from their principal or regular place of employment do not constitute "wages" for employment tax purposes under subchapters A, C, and D of chapter 9 of the Internal Revenue Code.

Treatment for Federal income tax purposes of allowances received and actual expenses incurred, by construction workers for daily transportation between their prinicpal or regular place of employment and a distant construction project where they are employed for a strictly temporary period.

S. S. T. 413, C. B. 1941-1, 408, revoked.

Reconsideration has been given to S. S. T. 413, C. B. 1941-1, 408, in which it is held that transportation allowances paid to employees

of a company constitute "wages" for purposes of subchapters A and C, chapter 9, of the Internal Revenue Code.

It is stated in S. S. T. 413, *supra*, that the company paid its employees allowances to cover their daily transportation expenses to and from a Federal project, where sufficient skilled labor was not available in the immediate vicinity, pursuant to the following authorization contained in an agreement between representatives of the Government and certain labor unions:

> The transportation reimbursement to the contractor shall be in a flat amount for all trades concerned at 75 cents per day per man, and the workman shall be reimbursed for this transportation in checks entirely separate from the payroll.

It has now been established by additional facts, not appearing in S. S. T. 413, *supra*, that the employees in question lived, and ordinarily worked at their trades on local construction jobs, within the metropolitan area of a certain city, and further that they received such allowances only for a period of from 2 to 4 months while they were constructing military facilities on a site located 18 miles from the limits of that city and some distance beyond the suburbs generally regarded as constituting part of such metropolitan area.

Subject to limitations not here applicable, the term "wages" is defined in sections 1426(a) and 1607(b) of subchapters A and C of chapter 9 of the Internal Revenue Code to mean "all remuneration for employment, including the cash value of all remuneration paid in any medium other than cash * * *."

Section 408.226(a) of Regulations 128 (which supersedes section 402.227(b)(2) of Regulations 106), issued pursuant to subchapter A, chapter 9, of the Code, provides in part as follows:

> Amounts paid specifically—either as advances or reimbursements—for traveling or other bona fide ordinary and necessary expenses incurred or reasonably expected to be incurred in the business of the employer are not wages. Traveling and other reimbursed expenses must be identified either by making a separate payment or by specifically indicating the separate amounts where both wages and expense allowances are combined in a single payment.

Section 403.227(a) of Regulations 107, as amended by T. D. 5805, C. B. 1950-2, 112, issued pursuant to subchapter C, chapter 9, of the Code contains identical provisions. Furthermore, the corresponding provisions relating to the withholding of income tax at the source on wages under section 1621(a) of subchapter D, chapter 9, of the Code, and section 405.101(c) of Regulations 116, are substantially the same as the above-cited provisions pertaining to subchapters A and C.

Relying on S. M. 1048, C. B. 1, 101 (1919), and *Appeal of Frank H. Sullivan*, 1 B. T. A. 93, it was concluded in S. S. T. 413, *supra*, that any amounts expended by the instant employees for transportation to and from this construction project did not represent expenses incurred in the business of the employer, but constituted personal expenses incurred by the employees.

However, it is now recognized, in view of the decision in *Harry F. Schurer* v. *Commissioner*, 3 T. C. 544, acquiescence, C. B. 1944, 24, that S. M. 1048 and the *Sullivan* case must be distinguished from the

situation presented herein. Each of the taxpayers considered in those cases merely commuted between his abode and his principal or regular place of business. In the instant situation, however, the construction workers did not commute between their abodes and their principal or regular place of employment, but incurred daily transportation expenses between the metropolitan area in which they ordinarily worked and a distant construction project where they were employed for a strictly temporary period. Since it has now been established that these construction workers lived and customarily carried on their trades during the taxable year in such metropolitan area, and were not regularly employed at any specific location or by any single contractor, their principal or regular place of employment would be considered as that metropolitan area. Thus, their expenses for daily transportation between that metropolitan area and the project in question were necessarily incurred for business reasons, rather than for personal reasons as in the case of a commuter who fixes his residence as a matter of personal convenience and preference at a distance from his regular place of business.

From the point of view of the employee considered herein, all such transportation allowances received are, of course, includible in his gross income. *Cf.* section 29.23(a)–2 of Regulations 111. However, when such a worker is employed for a strictly temporary (as distinguished from an indefinite) period on a construction project situated at a distance from the metropolitan area in which he is regularly employed, he may deduct, in computing adjusted gross income under section 22(n)(3) of the Code, his actual expenses incurred for daily transportation between his principal or regular place of employment and such job up to, but not exceeding, his reimbursement therefor. If his actual expenses for such daily transportation exceed his reimbursement, the excess thereof may be deducted as an ordinary and necessary business expense incurred in carrying on the *employee's* trade, but only in computing net income and on condition that the employee elects to itemize his actual deductions, in lieu of computing his tax by using the tax table or the optional standard deduction. Since the employee returns to the metropolitan area at the end of each day's work, he is not considered to be traveling "away from home" within the meaning of section 23(a)(1)(A) of the Code. See *Louis Drill* v. *Commissioner*, 8 T. C. 902, and *Fred Marion Osteen* v. *Commissioner*, 14 T. C. 1261. Thus, any expenses incurred for meals while at, or en route to and from, such project constitute personal and nondeductible expenses.

From the employer's point of view, reasonable transportation allowances paid to such employees while working for a strictly temporary period on a construction project located at a distance from their principal or regular place of employment represent payments made for business purposes directly connected with the conduct of the *employer's* business. Thus, such payments should be treated as reimbursements of expenses incurred by the employee in the buisness of the employer, rather than of the employee's personal expenses. It follows that such allowances for transportation expenses (as distinguished from payments made for travel time) represent amounts

paid specifically as reimbursements for bona fide ordinary and necessary expenses incurred or reasonably expected to be incurred in the business of the employer within the meaning of the above-cited regulations for employment tax purposes. In view of the foregoing, it is held that such allowances (when reasonably segregated from the payment of remuneration for employment) do not constitute "wages" for purposes of, and hence are not subject to tax under, subchapters A, C, and D of chapter 9 of the Internal Revenue Code. Accordingly, S. S. T. 413, *supra*, is hereby revoked.

Although such transportation allowances are not subject to income tax withholding under section 1622 of subchapter D of chapter 9 of the Code, it is important to note that section 29.147–2 of Regulations 111 provides that every employer paying an employee an aggregate (in wages plus such allowances) of $600 or more in a calendar year must report the employee's allowances not subject to income tax withholding on Form 1099, in addition to the usual reporting of wages subject to withholding on Form W–2.

REGULATIONS 128, SECTION 408.227: Exclusions from wages. Rev. Rul. 135

INTERNAL REVENUE CODE

In determining whether a bona fide employment relationship exists in those cases where a member of one's family performs domestic services in his home, for purposes of the taxes imposed by the Federal Insurance Contributions Act, as amended, the existence of a contract of employment, the dependency status of the alleged employee, the work history of the alleged employee, and the details of remuneration paid are major factors to be considered.

Advice is requested relative to the factors to be considered in determining whether a bona fide employer-employee relationship exists, for purposes of the taxes imposed by the Federal Insurance Contributions Act (subch. A of ch. 9 of the Internal Revenue Code), as amended, in those cases where it is alleged that a member of one's family is performing domestic services in his home under an employer-employee relationship. Advice is also requested relative to the extent of consideration given by the Bureau to data secured and presented by the Social Security Administration, as well as rulings issued by it in connection with the social security benefits program, for the purpose of determining the liability of individuals for payment of the taxes imposed by the Federal Insurance Contributions Act.

The Bureau of Internal Revenue is responsible for determining the status of an individual for Federal tax purposes; however, in reaching its conclusion information from all sources, including that made available to the Bureau by the Social Security Administration, will be carefully considered.

Section 1400 of the act imposes upon the income of every individual a tax equal to a certain percentage of the "wages" received by him after December 31, 1936, with respect to "employment." Section 1410 of the act imposes upon every employer an excise tax equal to the

same percentage of the "wages" paid by him after December 31, 1936, with respect to "employment."

The terms "wages" and "employment" are defined in section 1426 of the act. Under the terms of that section, in order for the remuneration paid by an employer to an employee for domestic service in a private home to constitute "wages" with respect to "employment," the following tests must be met:

(1) A bona fide employer-employee relationship must exist;

(2) the service must not be performed by the individual in the employ of his son, daughter, or spouse, and if the employee is under the age of 21 years the service must not be performed in the employ of his father or mother;

(3) the employee must be paid cash remuneration in the calendar quarter for such service of $50 or more by the employer (remuneration paid for domestic service in a private home in other than cash does not constitute "wages" as that term is defined in section 1426 of the act); and

(4) the employee must have performed domestic service in a private home of such employer for some portion of a day on at least 24 days during the calendar quarter (not necessarily consecutive days), or for some portion of a day on at least 24 days during the preceding calendar quarter.

As a general rule, little difficulty is experienced in determining whether cash remuneration of $50 or more was paid in a calendar quarter, whether the service was performed in the employ of a relative as set forth in test (2), above, and whether domestic service was performed in a private home of the employer for the required number of days. Considerable difficulty has been encountered, however, in determining whether an "in-law" or other close relative not mentioned in (2), above, is an employee. While the basic principles are the same in such cases as in those cases where no family relationship exists, the information necessary to apply the principles is sometimes difficult to obtain since the working arrangement in domestic employment is usually very informal and the statements of the parties to the arrangement may be self-serving inasmuch as there may be a community of interests in the benefits which later may be derived under the Social Security Act, as amended.

The following guides may be used in determining whether a true employer-employee relationship exists, or whether the domestic services are performed under a family or dependency arrangement:

Contract of employment.—Ordinarily, a formal written contract will not exist. If there is an oral or written contract its terms should be examined for the purpose of ascertaining when the agreement was made, when rendition of the services and the pay therefor began, what supervision or control was exercised and by whom, whether there were any special conditions, and the time and nature of any changes that occurred.

Claim of dependency for income tax purposes.—If the alleged employer claims the alleged employee as a dependent for Federal or State income tax purposes, that fact is strong but not conclusive evidence

that the arrangement is based on a family relationship rather than an employment relationship. Where the alleged employer's income is in a tax bracket in which an additional dependency exemption would be of little or no benefit to him, the fact that the alleged employee is not claimed as a dependent should not be considered as a material factor. Discontinuing the claiming of an alleged employee as a dependent during the period of the alleged employment, likewise, should not be considered as a material factor.

Work history.—The employment record of the alleged employee is significant. Previous employment, particularly as a domestic, would favor the existence of an employment relationship. On the other hand, a record of no previous employment tends to indicate that the individual performs services as a member of the family group. The alleged employer's record of hiring of domestics is also important. For instance, if the alleged employer had regularly employed a domestic whose services were terminated when the relative assumed the duties, that fact would tend to support an employer-employee relationship.

Remuneration.—There are certain factors in connection with the source and purpose of payments made to an alleged employee that may be helpful in determining whether an employment relationship actually exists. Remuneration, including payments in kind, which varies substantially from the prevailing wage rates for the same or similar services shows family consideration rather than an employment relationship. For Federal tax purposes the same payment is not regarded as both remuneration for services and a contribution for support. The source of the funds from which an individual is paid does not necessarily identify the employer, if any, but it may be indicative. The alleged employer's financial ability to hire domestics and pay the wages is important. The amounts paid to the alleged employee must, of course, be paid for services rendered, and not for expenses of running a household.

As indicated above, the existence of a contract of employment, the dependency status of the alleged employee, the work history, and the details of remuneration are major factors in determining whether a relationship of employer and employee exists. However, they are not the sole factors. Many others may have a bearing on the determination. For instance, if the alleged employee is owner or joint owner of the premises where the services were performed, the arrangement may be a rental agreement or a cooperative arrangement. In order to establish the existence or nonexistence of an employment relationship, it is necessary to consider all the facts and circumstances in a particular case.

Where the tests set forth in numbers (2), (3), and (4) above have been met and there is doubt as to whether a bona fide employment relationship exists in a particular case, it is suggested that the field offices develop the facts in the case by procuring the following information:

(1) A certified or photostatic copy of any written agreement under which the services were performed. If the agreement was

made orally, a statement of the terms and conditions of the agreement.

(2) A statement showing (*a*) where the alleged employee resided during the period that the services in question were performed, (*b*) whether the individual was a member of the household in which the services were performed, (*c*) who owned or leased the house or apartment in which the services were performed, (*d*) the number of days per week and the number of hours per day the alleged employee was required to perform the services, and (*e*) who prescribed the days and hours of employment.

(3) Whether any instructions were given to the alleged employee as to how, when, and where the services were to be performed. If so, instructions by whom.

(4) Whether the alleged employer or anyone in his immediate family previously claimed, or now claims, the alleged employee as a dependent for income tax purposes, if so, the year or years in which so claimed.

(5) The nature of the services performed by the alleged employee.

(6) Whether the alleged employee was paid for the services. If so, whether paid in cash or by check.

(7) Whether the remuneration received by the alleged employee varies substantially from the prevailing wage rates for the same or similar services.

(8) Whether payments or contributions were made to the alleged employee prior to the date of the alleged employment. If so, the amounts paid or contributed each week or month and the reasons therefor.

(9) If any service was performed before January 1, 1951, or before the alleged employment relationship started, the manner in which the alleged employee was paid for such service and at what intervals the payments were made.

(10) Whether the alleged employee filed an income tax return reporting the wages alleged to have been received for the services in question.

(11) If the alleged employee lived in the home of the alleged employer, the length of time resided there and the length of time wages were received.

(12) Whether other domestics are or have been employed in the household, if so, determine who was considered to be the employer of such individuals and how the work was divided among all the domestics.

It is believed that the guides set forth above will enable the field offices of the Bureau to determine the status, under the Federal Insurance Contributions Act, as amended, of individuals who perform domestic services in the private homes of relatives. However, in those cases where doubt exists as to the status of such individuals, the case should be transmitted to this office for consideration. Correspondence relating to this Revenue Ruling should refer to its number and the symbols T:R:E.

REGULATIONS 128, SECTION 408.227: Exclusions from wages. Rev. Rul. 244

INTERNAL REVENUE CODE

Amounts of $50 or more paid for each calendar quarter during 1952 to an individual who is regularly employed to perform domestic service in a private home constitute "wages" with respect to employment, for purposes of the Federal Insurance Contributions Act, even though such individual was temporarily unable to perform services due to sickness. Such amounts are, however, excluded from the term "wages" if they are paid after the expiration of 6 calendar months following the last calendar month in which the employee actually performed services for such employer.

Advice is requested whether amounts paid to an individual engaged to perform domestic service in a private home constitute wages for the year 1952, for purposes of the Federal Insurance Contributions Act, even though such individual was temporarily unable to perform services due to sickness.

An individual has been employed to perform domestic service in the private home of a taxpayer for approximately 25 years. Due to sickness she was unable to perform services during the first two quarters of 1952 and performed services intermittently as her health permitted during the remainder of the year; however, she was paid her regular wages during the entire year. Such individual has now recovered sufficiently to perform services at intervals.

Section 408.227(h) of Regulations 128 provides that the term "wages" does not include cash remuneration paid in any calendar quarter by an employer to an employee for domestic service in a private home of the employer unless the cash remuneration paid in a calendar quarter for such service is $50 or more, and the employee is *regularly employed* by the employer in the calendar quarter in which the payment is made.

An individual is deemed to be regularly employed by an employer during a calendar quarter only if such individual performs domestic service in a private home of such employer for some portion of the day on at least 24 days, whether or not consecutive, during such calendar quarter, or such individual was regularly employed in the performance of domestic service in a private home of such employer during the preceding calendar quarter (including the last calendar quarter of 1950).

In determining whether an employee has performed service on at least 24 days during a calendar quarter, any day or portion thereof on which the employee actually performs services is counted as a day. Also counted as a day is any day, or portion thereof, on which the employee does not perform services, but with respect to which cash remuneration is paid or payable to the employee for such services, such as a day on which the employee is sick or on vacation.

In the instant case cash remuneration of $50 or more was paid by the employer in each of the calendar quarters during which the domestic was sick. Also, as the employee has performed services for the taxpayer for the past 25 years and is continuing to work for the taxpayer when she is physically able, she is considered to be regularly

employed by such employer. It is accordingly held that the amounts paid to such individual during the time she was temporarily unable to perform services due to sickness constitute "wages" with respect to employment for purposes of the act.

However, the term "wages" does not include any payment made by an employer to an employee on account of the employee's sickness, if such payment is made after the expiration of 6 calendar months following the last calendar month in which such employee actually performed services for such employer. See section 403.227(d) of Regulations 128.

REGULATIONS 128, SECTION 408.227: Exclusions from wages.

INTERNAL REVENUE CODE

Premium paid on "Employees' Annuities" by an employer exempt from Federal income tax under section 101(6) of the Internal Revenue Code. (See Rev. Rul. 181, p. 111.)

SUBCHAPTER C.—TAX ON EMPLOYERS OF EIGHT OR MORE

SECTION 1607.—DEFINITIONS

REGULATIONS 107, SECTION 403.204: Who are employees.

INTERNAL REVENUE CODE

Pathologist engaged to conduct a laboratory in a hospital. (See Rev. Rul. 261, p. 296.)

REGULATIONS 107, SECTION 403.204: Who are employees.

INTERNAL REVENUE CODE

Babysitters engaged by an establishment which furnishes babysitter services to its customers. (See Rev. Rul. 233, p. 294.)

REGULATIONS 107, SECTION 403.227: Wages.

INTERNAL REVENUE CODE

Transportation allowances paid to employees working on a temporary construction project located at a distance from their regular place of employment. (See Rev. Rul. 190, p. 303.)

SUBCHAPTER D.—COLLECTION OF INCOME TAX AT SOURCE ON WAGES

SECTION 1621.—DEFINITIONS

REGULATIONS 116, SECTION 405.101: Wages.

INTERNAL REVENUE CODE

Contributions required of employees under article 9 of the New York workmen's compensation law, assumed and paid by employers. (See Rev. Rul. 130, p. 99.)

REGULATIONS 116, SECTION 405.101: Wages.

INTERNAL REVENUE CODE

Remuneration paid to civilian instructors, for services performed on a contract or fee basis at army education centers located in the Panama Canal Zone. (See Rev. Rul. 147, p. 301.)

REGULATIONS 116, SECTION 405.101: Wages.

INTERNAL REVENUE CODE

Premium paid on "Employees' Annuities" by an employer exempt from Federal income tax under section 101(6) of the Internal Revenue Code. (See Rev. Rul. 181, p. 111.

REGULATIONS 116, SECTION 405.101: Wages.

INTERNAL REVENUE CODE

Transportation allowances paid to employees working on a temporary construction project located at a distance from their regular place of employment. (See Rev. Rul. 190, p. 303.)

REGULATIONS 116, SECTION 405.101: Wages.

INTERNAL REVENUE CODE

Compensation paid to babysitters by an establishment engaged in furnishing babysitter services. (See Rev. Rul. 233, p. 294.)

REGULATIONS 116, SECTION 405.102: Exclusions from wages. T. D. 6040

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER D, PART 405.—COLLECTION OF INCOME TAX AT SOURCE ON WAGES

Regulations 116 amended to conform to section 321 of the Revenue Act of 1951 and to section 204 of the Technical Changes Act of 1953 [p. 508, this Bulletin].

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

On December 13, 1952, there was published in the Federal Register (17 F. R. 11350) a notice of proposed rulemaking to conform Regulations 116 [26 CFR, pt. 405] to section 321 of the Revenue Act of 1951, relating to earned income from sources without the United States, approved October 20, 1951. After consideration of such relevant matter as was presented by interested persons relating to the rules proposed, the amendments to such regulations set forth below, including such supplemental amendments as are necessary to conform Regulations 116 to section 204 of the Technical Changes Act of 1953 [p. 508, this Bulletin], approved August 15, 1953, are hereby adopted:

PARAGRAPH 1. There is inserted immediately preceding section 405.101 the following:

SEC. 321. EARNED INCOME FROM SOURCES WITHOUT THE UNITED STATES [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

* * * * * * *

(b) WITHHOLDING OF TAX ON WAGES.—Section 1621(a)(8)(A) (relating to definition of wages) is hereby amended to read as follows:

"(A) for services for an employer (other than the United States or any agency thereof) performed in a foreign country by a citizen of the United States, if at the time of the payment of such remuneration the employer is required by the law of any foreign country to withhold income tax upon such remuneration, or it is reasonable to believe that such remuneration will be excluded from gross income under the provisions of section 116(a) (1) or (2), or".

(c) EFFECTIVE DATES.—* * * The amendment made by subsection (b) shall be applicable with respect to wages paid on or after January 1, 1952.

SEC. 204. EARNED INCOME FROM SOURCES WITHOUT THE UNITED STATES [TECHNICAL CHANGES ACT OF 1953, APPROVED AUGUST 15, 1953].

* * * * * * *

(b) WITHHOLDING OF TAX ON WAGES OF CITIZENS OUTSIDE THE UNITED STATES.—So much of section 1621(a)(8) (relating to the definition of wages) as precedes subparagraph (B) thereof is hereby amended to read as follows:

"(8) (A) for services for an employer (other than the United States or any agency thereof) (i) performed by a citizen of the United States if, at the time of the payment of such remuneration, it is reasonable to believe that such remuneration will be excluded from gross income under section 116(a), or (ii) performed in a foreign country by such a citizen if, at the time of the payment of such remuneration, the employer is required by the law of any foreign country to withhold income tax upon such remuneration, or".

(c) EFFECTIVE DATE.—* * * The amendments made by subsections * * * (b) shall not affect the liability of any employer to deduct and withhold the tax imposed by section 1622 in the case of any remuneration paid before the first day of the first month beginning more than ten days after the date of the enactment of this Act.

PAR. 2. Section 405.102, as amended by Treasury Decision 5891 [C. B. 1952-1, 196], approved April 4, 1952, is further amended as follows:

(A) By inserting immediately after "January 1, 1948," in the heading of (h)(2) thereof "and before January 1, 1952," so that such heading will read as follows:

(2) *Remuneration paid on or after January 1, 1948, and before January 1, 1952, to citizens resident in foreign countries.*

(B) By inserting immediately after "January 1, 1948," in the first sentence of the first paragraph of (h)(2) thereof "and before January 1, 1952,".

(C) By redesignating (h)(3) thereof as (h)(4).

(D) By inserting immediately after the last paragraph of (h)(2) thereof the following new subparagraph:

(3) *Remuneration paid on or after January 1, 1952, to citizens in foreign countries.*—(i) *Elimination of double withholding.*—The remuneration paid on or after January 1, 1952, for services performed in a foreign country for an employer (other than the United States or any agency or instrumentality thereof) by a citizen of the United States does not constitute wages under section 1621(a)(8)(A) and hence is not subject to withholding, if at the time of the payment of such remuneration the employer is required by the law of any foreign country to withhold income tax upon such remuneration.

The remuneration is not exempt from withholding under this subdivision if the employer is not required by the law of a foreign country to withhold income tax upon such remuneration. Mere agreements between the employer and the employee whereby the estimated income tax of a foreign country is withheld from the remuneration in anticipation of actual liability under the law of such country will not suffice.

The exemption from withholding provided by this subdivision does not apply by reason of withholding of income tax pursuant to the law of a possession or Territory of the United States or of a political subdivision of a foreign state.

(ii) *Resident of a foreign country.*—The remuneration paid on or after January 1, 1952, and before September 1, 1953, for services performed in a foreign country, and the remuneration paid on or after September 1, 1953, for services performed outside the United States, for an employer (other than the United States or any agency or instrumentality thereof) by a citizen of the United States does not constitute wages under section 1621(a)(8)(A) and hence is not subject to withholding, if at the time of payment it is reasonable to believe that such remuneration will be excluded from gross income under the provisions of section 116(a)(1).

Section 116(a)(1) provides that, in the case of an individual citizen of the United States who establishes to the satisfaction of the Commissioner that he has been a bona fide resident of a foreign country or countries for an uninterrupted period which includes an entire taxable year, all amounts received from sources without the United States (except amounts paid by the United States or any agency or instrumentality thereof) shall be excluded from gross income if such amounts constitute earned income, as defined in section 116(a)(3), which is attributable to such uninterrupted period. See section 116(a) and the regulations thereunder.

The employer may, in the absence of cause for a reasonable belief to the contrary, presume that remuneration for services performed outside the United States during the taxable year, or applicable portion thereof, will be excluded from gross income under the provisions of section 116(a)(1) for each taxable year in respect of which the employee properly executes and files in duplicate with the employer a statement in the form set forth below. However, in the case of payments made on or after January 1, 1952, and before September 1, 1953, the presumption shall apply only to remuneration for services performed in a foreign country or countries.

STATEMENT FOR CLAIMING BENEFIT OF SECTION 116(a)(1) FOR CALENDAR YEAR _____ OR FISCAL YEAR BEGINNING _____ AND ENDING _____

(A) My name is _____. My present address is _____ _____. I am employed by _____.

(B) My last address in the United States was _____. The internal revenue district in which I filed my last income tax return is _____.

(C) I _____ file my income tax return on the calendar (Do or do not)
year basis.

(D) I file my income tax return on the basis of the fiscal year beginning _____ ____, 19____, and ending _____ ____, 19____.

(E) I am a citizen of the United States.

(F) I have been a bona fide resident of the following foreign country or countries, namely, _____, for an uninterrupted period which began on _____ ____, 19____.

(G) I expect to remain a bona fide resident of a foreign country or countries from the date of this statement until the end of the taxable year in respect of which this statement is filed.

(H) On the basis of the facts in my case I have good reason to believe that, with respect to the above period of foreign residence falling within the taxable year, I will satisfy the bona fide foreign-residence requirement prescribed by section 116(a)(1) of the Internal Revenue Code.

(I) I understand that any exemption from withholding of tax permitted by reason of the filing of this statement is not a determination by the Commissioner of Internal Revenue that any remuneration paid to me for any services performed during the taxable year is excludable from gross income under the provisions of section 116(a)(1) of the Internal Revenue Code.

I declare under the penalties of perjury that this statement has been examined by me and to the best of my knowledge and belief is true and correct.

_____
(Signature of taxpayer)

Date _____ ____, 19____.

If with respect to any employee the employer was entitled to presume for the 2 consecutive taxable years immediately preceding the employee's current taxable year that the employee's remuneration for services performed in a foreign country or countries during such preceding taxable years would be excluded from gross income under the provisions of section 116(a)(1), he may, if such employee is residing in a foreign country on the first day of such current taxable year, presume that, in the absence of cause for a reasonable belief to the contrary, the remuneration for services performed in a foreign country or countries during such current taxable year and, in the case of payments made on and after September 1, 1953, any other remuneration for services performed outside the United States during such year will be excluded from gross income under the provisions of section 116(a)(1).

(iii) *Physical presence in a foreign country.*—The remuneration paid on or after January 1, 1952, and before September 1, 1953, for services performed in a foreign country, and the remuneration paid on or after September 1, 1953, for services performed outside the United States, for an employer (other than the United States or any agency or instrumentality thereof) by a citizen of the United States does not constitute wages under section 1621(a)(8)(A) and hence is not subject to withholding, if at the time of payment it is reasonable to believe that such remuneration will be excluded from gross income under the provisions of section 116(a)(2).

Section 116(a)(2) provides that, in the case of an individual citizen of the United States who during any period of 18 consecutive months is present in a foreign country or countries during at least 510 full days in such period, all amounts received from sources without the United States (except amounts paid by the United States or any agency or instrumentality thereof) shall be excluded from gross income if such amounts constitute earned income, as defined in section 116(a)(3), which is attributable to such period. For taxable years ending before

January 1, 1953, there is no limitation upon the amount which may be excluded from gross income under section 116(a)(2). For taxable years ending after December 31, 1952, but only with respect to amounts received after such date, the amount excluded from gross income under the provisions of such section shall not exceed $20,000 if the 18-month period includes the entire taxable year. If the 18-month period does not include the entire taxable year, the amount excluded from gross income under such section for such taxable year shall not exceed an amount which bears the same ratio to $20,000 as the number of days in the part of the taxable year within the 18-month period bears to the total number of days in such year. A special rule is applicable to a fiscal year beginning in 1952 and ending in 1953. See section 116(a) and the regulations thereunder.

The employer may, in the absence of cause for a reasonable belief to the contrary, presume that remuneration for services performed outside the United States during the taxable year, or applicable portion thereof, will be excluded from gross income under the provisions of section 116(a)(2) for each taxable year in respect of which the employee properly executes and files in duplicate with the employer a statement in the form set forth below. However, in the case of payments made on or after January 1, 1952, and before September 1, 1953, the presumption shall apply only to remuneration for services performed in a foreign country or countries. In the case of payments made on or after September 1, 1953, the presumption shall not apply after the total payments made during the taxable year of the employee equal $20.000 or such lesser amount as may be allowable under section 116(a)(2) on the basis of the facts shown in the statement described below.

STATEMENT OF CLAIMING BENEFIT OF SECTION 116(a)(2) FOR CALENDAR YEAR _____ OR FISCAL YEAR BEGINNING _____ AND ENDING _____

(A) My name is _____. My present address is _____ _____. I am employed by _____.

(B) My last address in the United States was _____. The internal revenue district in which I filed my last income tax return is _____.

(C) I _____ file my income tax return on the calendar year
(Do or do not)
basis.

(D) I file my income tax return on the basis of the fiscal year beginning _____ ____, 19____, and ending _____ ____, 19____.

(E) I am a citizen of the United States.

(F) Except for occasional absences which have not disqualified me for the benefit of section 116(a)(2) of the Internal Revenue Code, I have been present in the following foreign country or countries, namely, _____, during the period of time which began on _____ ____, 19____.

(G) I expect to be present in a foreign country or countries, except for occasional absences not disqualifying me for the benefit of section 116(a)(2), from the date of this statement until the end of the taxable year in respect of which this statement is filed; or, if not for such period, from the date of this statement until the following date within such taxable year, namely, _____ ____, 19____.

(H) On the basis of the facts in my case I have good reason to believe that, with respect to the above period of presence in a foreign country or countries falling within the taxable year, I will satisfy the 510 full day requirement prescribed by section 116(a)(2) of the Internal Revenue Code.

(I) In the event I become disqualified for the exclusion provided by section 116(a)(2) in respect of all or part of the above period of presence in a foreign country or countries falling within the taxable year, I will immediately notify my employer, giving sufficient facts to indicate the part, if any, of such period falling within such year in respect of which I am qualified for such exclusion.

(J) I understand that any exemption from withholding of tax permitted by reason of the filing of this statement is not a determination by the Commissioner of Internal Revenue that any remuneration paid to me for any services performed during the taxable year is excludable from gross income under the provisions of section 116(a)(2) of the Internal Revenue Code.

I declare under the penalties of perjury that this statement has been examined by me and to the best of my knowledge and belief is true and correct.

(Signature of taxpayer)

Date -------- ------, 19-----.

(iv) *General.*—Remuneration paid on or after January 1, 1952, and before September 1, 1953, in respect of services performed in an area other than a foreign country, for example, the United States, a possession of the United States, or the high seas, shall not be excluded from wages under section 1621(a)(8)(A).

The reasonable belief referred to in section 1621(a)(8)(A) may be based upon any evidence reasonably sufficient to induce such belief, even though such evidence may be insufficient upon closer examination by the Commissioner or the courts finally to establish the exclusion from gross income, and exemption from tax, allowed by section 116(a) (1) or (2).

The original of each statement filed with the employer pursuant to subdivisions (ii) and (iii) shall be transmitted to the district director of internal revenue with the employer's return on Form 941 required by section 405.601 for the quarter of the calendar year within which such statement is filed. The duplicate copy shall be retained by the employer.

(This Treasury Decision is issued under the authority contained in secs. 1429 and 3791 (53 Stat. 178, 467; 26 U. S. C. 1429, 3791), and sec. 1627 (57 Stat. 138; 26 U. S. C. 1627), of the Internal Revenue Code.)

O. GORDON DELK,
Acting Commissioner of Internal Revenue.

Approved August 27, 1953.

H. CHAPMAN ROSE,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register August 31, 1953, 8:54 a. m.)

SECTION 1622.—INCOME TAX COLLECTED AT SOURCE

REGULATIONS 116, SECTION 405.201: Requirement of withholding. Rev. Rul. 294

(Also Section 1401, Section 408.304, Regulations 128.)

INTERNAL REVENUE CODE

Table which may be used by employers in withholding Federal income tax and employee tax under the Federal Insurance Contributions Act from weekly wages paid on and after January 1, 1954.

The following table has been constructed for the convenience of those employers who wish to use a table which combines amounts to be withheld as Federal income tax and employee tax under the Federal Insurance Contributions Act from weekly wages paid on and after January 1, 1954.

The table reflects the lower income tax withholding rate prescribed by section 1622 of the Internal Revenue Code and the higher employee tax rate prescribed by section 1400 of the Federal Insurance Contributions Act with respect to wages paid on and after January 1,

1954. Such table supersedes the table set forth in Mim. 6703, C. B. 1951-2, 178.

Since the Internal Revenue Code provides no table method for determining the amount of employee tax under the Federal Insurance Contributions Act, the wage brackets shown in the table are functions of the 2 percent Federal Insurance Contributions Act employee tax rate, and the amounts of employee tax determined for the table are computed to the nearest cent. The table is designed to cover weekly wages under $135.25 but can be extended to weekly wages of $135.25 and over by utilizing the same wage bracket increments and adding the Federal Insurance Contributions Act employee tax at 2 percent to the income tax to be withheld. The amount of income tax to be withheld is determined by reference to the weekly income tax withholding table provided by the Internal Revenue Code (see p. 20 of Circular E, Rev. January 1954, Employer's Tax Guide) in all cases except those where the wage brackets used in the combined table fall within more than one bracket of the weekly income tax withholding table (for example, $13.75 to $14.25). In such cases, the income tax to be withheld is determined in accordance with the percentage method of withholding (see p. 19 of Circular E, Rev. January 1954), which permits the rounding of wages to the nearest dollar for purposes of computing the amount to be withheld.

The use of the combined table results in the correct aggregate withholding only if wages for purposes of the income tax withholding and for purposes of the Federal Insurance Contributions Act are identical. The table should not be used with respect to the excess over $3,600 of wages paid to an employee in a calendar year or in other instances where the wages differ.

For purposes of employer's quarterly Federal tax returns (Form 941), there will be no objection, in the case of employers using the combined withholding table, to (1) determining the amount of Federal Insurance Contributions Act employee tax withheld by applying the 2 percent Federal Insurance Contributions Act employee tax rate to total wages taxable for purposes of such Act, and (2) determining the amount of income tax withheld by subtracting such amount of Federal Insurance Contributions Act employee tax from the total tax withheld.

With respect to employees' annual receipts on Form W-2 for 1954, and thereafter, on which employers are required to show (1) total Federal Insurance Contributions Act wages paid, (2) employee tax deducted under the Federal Insurance Contributions Act, (3) total wages subject to the income tax withholding, and (4) income tax withheld therefrom, no objection will be interposed, in the case of employers using the combined withholding table, to determining the Federal Insurance Contributions Act employee tax deducted from each employee's wages in the year by applying the 2 percent rate to wages, not in excess of $3,600, under such Act, and determining the amount of income tax withheld by subtracting the employee tax so determined from the total tax withheld from the employee's wages in the year.

Weekly withholding table combining income tax and employees' Federal Insurance Contributions Act tax (2 percent)

This table to be used only if wages for income tax withholding and wages for employees' F. I. C. A. tax are identical

If wages are—		And the number of withholding exemptions claimed is—										
At least	But less than	0	1	2	3	4	5	6	7	8	9	10
		The amount of income tax and F. I. C. A. tax to be withheld shall be—										
$0.00	$13.25	20% of wages	2% of wages	2% of wages	2% of wages	2% of wages	2% of wages	2% of wages	2% of wages	2% of wages	2% of wages	2% of wages
$13.25	$13.75	$2.67	$0.37	$0.27	$0.27	$0.27	$0.27	$0.27	$0.27	$0.27	$0.27	$0.27
$13.75	$14.25	2.80	.46	.28	.28	.28	.28	.28	.28	.28	.28	.28
$14.25	$14.75	2.89	.59	.29	.29	.29	.29	.29	.29	.29	.29	.29
$14.75	$15.25	3.00	.66	.30	.30	.30	.30	.30	.30	.30	.30	.30
$15.25	$15.75	3.11	.81	.31	.31	.31	.31	.31	.31	.31	.31	.31
$15.75	$16.25	3.20	.86	.32	.32	.32	.32	.32	.32	.32	.32	.32
$16.25	$16.75	3.33	1.03	.33	.33	.33	.33	.33	.33	.33	.33	.33
$16.75	$17.25	3.40	1.06	.34	.34	.34	.34	.34	.34	.34	.34	.34
$17.25	$17.75	3.55	1.15	.35	.35	.35	.35	.35	.35	.35	.35	.35
$17.75	$18.25	3.60	1.26	.36	.36	.36	.36	.36	.36	.36	.36	.36
$18.25	$18.75	3.67	1.37	.37	.37	.37	.37	.37	.37	.37	.37	.37
$18.75	$19.25	3.80	1.46	.38	.38	.38	.38	.38	.38	.38	.38	.38
$19.25	$19.75	3.89	1.59	.39	.39	.39	.39	.39	.39	.39	.39	.39
$19.75	$20.25	4.00	1.66	.40	.40	.40	.40	.40	.40	.40	.40	.40
$20.25	$20.75	4.11	1.81	.41	.41	.41	.41	.41	.41	.41	.41	.41
$20.75	$21.25	4.20	1.86	.42	.42	.42	.42	.42	.42	.42	.42	.42
$21.25	$21.75	4.33	2.03	.43	.43	.43	.43	.43	.43	.43	.43	.43
$21.75	$22.25	4.40	2.06	.44	.44	.44	.44	.44	.44	.44	.44	.44
$22.25	$22.75	4.55	2.15	.45	.45	.45	.45	.45	.45	.45	.45	.45
$22.75	$23.25	4.60	2.26	.46	.46	.46	.46	.46	.46	.46	.46	.46
$23.25	$23.75	4.67	2.37	.47	.47	.47	.47	.47	.47	.47	.47	.47
$23.75	$24.25	4.80	2.46	.48	.48	.48	.48	.48	.48	.48	.48	.48
$24.25	$24.75	4.89	2.59	.49	.49	.49	.49	.49	.49	.49	.49	.49
$24.75	$25.25	5.00	2.66	.50	.50	.50	.50	.50	.50	.50	.50	.50
$25.25	$25.75	5.11	2.81	.51	.51	.51	.51	.51	.51	.51	.51	.51
$25.75	$26.25	5.20	2.86	.52	.52	.52	.52	.52	.52	.52	.52	.52
$26.25	$26.75	5.33	3.03	.73	.53	.53	.53	.53	.53	.53	.53	.53
$26.75	$27.25	5.40	3.06	.72	.54	.54	.54	.54	.54	.54	.54	.54
$27.25	$27.75	5.55	3.15	.85	.55	.55	.55	.55	.55	.55	.55	.55
$27.75	$28.25	5.60	3.26	.92	.56	.56	.56	.56	.56	.56	.56	.56
$28.25	$28.75	5.67	3.37	1.07	.57	.57	.57	.57	.57	.57	.57	.57
$28.75	$29.25	5.80	3.46	1.12	.58	.58	.58	.58	.58	.58	.58	.58
$29.25	$29.75	5.89	3.59	1.29	.59	.59	.59	.59	.59	.59	.59	.59
$29.75	$30.25	6.00	3.66	1.32	.60	.60	.60	.60	.60	.60	.60	.60
$30.25	$30.75	6.11	3.81	1.51	.61	.61	.61	.61	.61	.61	.61	.61
$30.75	$31.25	6.20	3.86	1.52	.62	.62	.62	.62	.62	.62	.62	.62
$31.25	$31.75	6.33	4.03	1.73	.63	.63	.63	.63	.63	.63	.63	.63
$31.75	$32.25	6.40	4.06	1.72	.64	.64	.64	.64	.64	.64	.64	.64
$32.25	$32.75	6.55	4.15	1.85	.65	.65	.65	.65	.65	.65	.65	.65
$32.75	$33.25	6.60	4.26	1.92	.66	.66	.66	.66	.66	.66	.66	.66
$33.25	$33.75	6.67	4.37	2.07	.67	.67	.67	.67	.67	.67	.67	.67
$33.75	$34.25	6.80	4.46	2.12	.68	.68	.68	.68	.68	.68	.68	.68
$34.25	$34.75	6.89	4.59	2.29	.69	.69	.69	.69	.69	.69	.69	.69
$34.75	$35.25	7.00	4.66	2.32	.70	.70	.70	.70	.70	.70	.70	.70
$35.25	$35.75	7.11	4.81	2.51	.71	.71	.71	.71	.71	.71	.71	.71
$35.75	$36.25	7.20	4.86	2.52	.72	.72	.72	.72	.72	.72	.72	.72
$36.25	$36.75	7.33	5.03	2.73	.73	.73	.73	.73	.73	.73	.73	.73
$36.75	$37.25	7.40	5.06	2.72	.74	.74	.74	.74	.74	.74	.74	.74
$37.25	$37.75	7.55	5.15	2.85	.75	.75	.75	.75	.75	.75	.75	.75
$37.75	$38.25	7.60	5.26	2.92	.76	.76	.76	.76	.76	.76	.76	.76
$38.25	$38.75	7.67	5.37	3.07	.77	.77	.77	.77	.77	.77	.77	.77
$38.75	$39.25	7.80	5.46	3.12	.78	.78	.78	.78	.78	.78	.78	.78
$39.25	$39.75	7.89	5.59	3.29	.99	.79	.79	.79	.79	.79	.79	.79
$39.75	$40.25	8.00	5.66	3.32	.98	.80	.80	.80	.80	.80	.80	.80
$40.25	$40.75	8.11	5.81	3.51	1.21	.81	.81	.81	.81	.81	.81	.81
$40.75	$41.25	8.20	5.86	3.52	1.18	.82	.82	.82	.82	.82	.82	.82
$41.25	$41.75	8.33	6.03	3.73	1.33	.83	.83	.83	.83	.83	.83	.83
$41.75	$42.25	8.40	6.06	3.72	1.38	.84	.84	.84	.84	.84	.84	.84
$42.25	$42.75	8.55	6.15	3.85	1.55	.85	.85	.85	.85	.85	.85	.85
$42.75	$43.25	8.60	6.26	3.92	1.58	.86	.86	.86	.86	.86	.86	.86
$43.25	$43.75	8.67	6.37	4.07	1.77	.87	.87	.87	.87	.87	.87	.87
$43.75	$44.25	8.80	6.46	4.12	1.78	.88	.88	.88	.88	.88	.88	.88
$44.25	$44.75	8.89	6.59	4.29	1.99	.89	.89	.89	.89	.89	.89	.89
$44.75	$45.25	9.00	6.66	4.32	1.98	.90	.90	.90	.90	.90	.90	.90
$45.25	$45.75	9.11	6.81	4.51	2.21	.91	.91	.91	.91	.91	.91	.91
$45.75	$46.25	9.20	6.86	4.52	2.18	.92	.92	.92	.92	.92	.92	.92
$46.25	$46.75	9.33	7.03	4.73	2.33	.93	.93	.93	.93	.93	.93	.93
$46.75	$47.25	9.40	7.06	4.72	2.38	.94	.94	.94	.94	.94	.94	.94
$47.25	$47.75	9.55	7.15	4.85	2.55	.95	.95	.95	.95	.95	.95	.95
$47.75	$48.25	9.60	7.26	4.92	2.58	.96	.96	.96	.96	.96	.96	.96

Weekly withholding table combining income tax and employees' Federal Insurance Contributions Act tax (2 percent)—Continued

This table to be used only if wages for income tax withholding and wages for employees' F. I. C. A. tax are identical

If wages are—		And the number of withholding exemptions claimed is—										
At least	But less than	0	1	2	3	4	5	6	7	8	9	10
		The amount of income tax and F. I. C. A. tax to be withheld shall be—										
$48.25	$48.75	$9.67	$7.37	$5.07	$2.77	$0.97	$0.97	$0.97	$0.97	$0.97	$0.97	$0.97
$48.75	$49.25	9.80	7.46	5.12	2.78	.98	.98	.98	.98	.98	.98	.98
$49.25	$49.75	9.89	7.59	5.29	2.99	.99	.99	.99	.99	.99	.99	.99
$49.75	$50.25	10.00	7.66	5.32	2.98	1.00	1.00	1.00	1.00	1.00	1.00	1.00
$50.25	$50.75	10.11	7.81	5.61	3.21	1.01	1.01	1.01	1.01	1.01	1.01	1.01
$50.75	$51.25	10.20	7.86	5.52	3.18	1.02	1.02	1.02	1.02	1.02	1.02	1.02
$51.25	$51.75	10.33	8.03	5.73	3.33	1.03	1.03	1.03	1.03	1.03	1.03	1.03
$51.75	$52.25	10.40	8.06	5.72	3.38	1.04	1.04	1.04	1.04	1.04	1.04	1.04
$52.25	$52.75	10.55	8.15	5.85	3.55	1.25	1.05	1.05	1.05	1.05	1.05	1.05
$52.75	$53.25	10.60	8.26	5.92	3.58	1.24	1.06	1.06	1.06	1.06	1.06	1.06
$53.25	$53.75	10.67	8.37	6.07	3.77	1.47	1.07	1.07	1.07	1.07	1.07	1.07
$53.75	$54.25	10.80	8.46	6.12	3.78	1.44	1.08	1.08	1.08	1.08	1.08	1.08
$54.25	$54.75	10.89	8.59	6.29	3.99	1.69	1.09	1.09	1.09	1.09	1.09	1.09
$54.75	$55.25	11.00	8.66	6.32	3.98	1.64	1.10	1.10	1.10	1.10	1.10	1.10
$55.25	$55.75	11.11	8.81	6.61	4.21	1.91	1.11	1.11	1.11	1.11	1.11	1.11
$55.75	$56.25	11.20	8.86	6.52	4.18	1.84	1.12	1.12	1.12	1.12	1.12	1.12
$56.25	$56.75	11.33	9.03	6.73	4.33	2.03	1.13	1.13	1.13	1.13	1.13	1.13
$56.75	$57.25	11.40	9.06	6.72	4.38	2.04	1.14	1.14	1.14	1.14	1.14	1.14
$57.25	$57.75	11.55	9.15	6.85	4.55	2.25	1.15	1.15	1.15	1.15	1.15	1.15
$57.75	$58.25	11.60	9.26	6.92	4.58	2.24	1.16	1.16	1.16	1.16	1.16	1.16
$58.25	$58.75	11.67	9.37	7.07	4.77	2.47	1.17	1.17	1.17	1.17	1.17	1.17
$58.75	$59.25	11.80	9.46	7.12	4.78	2.44	1.18	1.18	1.18	1.18	1.18	1.18
$59.25	$59.75	11.89	9.59	7.29	4.99	2.69	1.19	1.19	1.19	1.19	1.19	1.19
$59.75	$60.25	12.00	9.66	7.32	4.98	2.64	1.20	1.20	1.20	1.20	1.20	1.20
$60.25	$60.75	12.21	9.91	7.61	5.31	2.91	1.21	1.21	1.21	1.21	1.21	1.21
$60.75	$61.25	12.22	9.92	7.62	5.32	2.92	1.22	1.22	1.22	1.22	1.22	1.22
$61.25	$61.75	12.23	9.93	7.63	5.33	2.93	1.23	1.23	1.23	1.23	1.23	1.23
$61.75	$62.25	12.40	10.06	7.72	5.38	3.04	1.24	1.24	1.24	1.24	1.24	1.24
$62.25	$62.75	12.55	10.25	7.95	5.65	3.35	1.25	1.25	1.25	1.25	1.25	1.25
$62.75	$63.25	12.56	10.26	7.96	5.66	3.36	1.26	1.26	1.26	1.26	1.26	1.26
$63.25	$63.75	12.57	10.27	7.97	5.67	3.37	1.27	1.27	1.27	1.27	1.27	1.27
$63.75	$64.25	12.80	10.46	8.12	5.78	3.44	1.28	1.28	1.28	1.28	1.28	1.28
$64.25	$64.75	12.99	10.69	8.39	6.09	3.79	1.49	1.29	1.29	1.29	1.29	1.29
$64.75	$65.25	13.00	10.70	8.40	6.10	3.80	1.50	1.30	1.30	1.30	1.30	1.30
$65.25	$65.75	13.01	10.71	8.41	6.11	3.81	1.51	1.31	1.31	1.31	1.31	1.31
$65.75	$66.25	13.20	10.86	8.52	6.18	3.84	1.50	1.32	1.32	1.32	1.32	1.32
$66.25	$66.75	13.43	11.13	8.73	6.43	4.13	1.83	1.33	1.33	1.33	1.33	1.33
$66.75	$67.25	13.44	11.14	8.74	6.44	4.14	1.84	1.34	1.34	1.34	1.34	1.34
$67.25	$67.75	13.45	11.15	8.75	6.45	4.15	1.85	1.35	1.35	1.35	1.35	1.35
$67.75	$68.25	13.60	11.26	8.92	6.58	4.24	1.90	1.36	1.36	1.36	1.36	1.36
$68.25	$68.75	13.77	11.47	9.17	6.87	4.57	2.27	1.37	1.37	1.37	1.37	1.37
$68.75	$69.25	13.78	11.48	9.18	6.88	4.58	2.28	1.38	1.38	1.38	1.38	1.38
$69.25	$69.75	13.79	11.49	9.19	6.89	4.59	2.29	1.39	1.39	1.39	1.39	1.39
$69.75	$70.25	14.00	11.66	9.32	6.98	4.64	2.30	1.40	1.40	1.40	1.40	1.40
$70.25	$70.75	14.21	11.91	9.61	7.31	4.91	2.61	1.41	1.41	1.41	1.41	1.41
$70.75	$71.25	14.22	11.92	9.62	7.32	4.92	2.62	1.42	1.42	1.42	1.42	1.42
$71.25	$71.75	14.23	11.93	9.63	7.33	4.93	2.63	1.43	1.43	1.43	1.43	1.43
$71.75	$72.25	14.40	12.06	9.72	7.38	5.04	2.70	1.44	1.44	1.44	1.44	1.44
$72.25	$72.75	14.55	12.25	9.95	7.65	5.35	3.05	1.45	1.45	1.45	1.45	1.45
$72.75	$73.25	14.56	12.26	9.96	7.66	5.36	3.06	1.46	1.46	1.46	1.46	1.46
$73.25	$73.75	14.57	12.27	9.97	7.67	5.37	3.07	1.47	1.47	1.47	1.47	1.47
$73.75	$74.25	14.80	12.46	10.12	7.78	5.44	3.10	1.48	1.48	1.48	1.48	1.48
$74.25	$74.75	14.99	12.69	10.39	8.09	5.79	3.49	1.49	1.49	1.49	1.49	1.49
$74.75	$75.25	15.00	12.70	10.40	8.10	5.80	3.50	1.50	1.50	1.50	1.50	1.50
$75.25	$75.75	15.01	12.71	10.41	8.11	5.81	3.51	1.51	1.51	1.51	1.51	1.51
$75.75	$76.25	15.20	12.86	10.52	8.18	5.84	3.50	1.52	1.52	1.52	1.52	1.52
$76.25	$76.75	15.43	13.13	10.73	8.43	6.13	3.83	1.53	1.53	1.53	1.53	1.53
$76.75	$77.25	15.44	13.14	10.74	8.44	6.14	3.84	1.54	1.54	1.54	1.54	1.54
$77.25	$77.75	15.45	13.15	10.75	8.45	6.15	3.85	1.55	1.55	1.55	1.55	1.55
$77.75	$78.25	15.60	13.26	10.92	8.58	6.24	3.90	1.56	1.56	1.56	1.56	1.56
$78.25	$78.75	15.77	13.47	11.17	8.87	6.57	4.27	1.97	1.57	1.57	1.57	1.57
$78.75	$79.25	15.78	13.48	11.18	8.88	6.58	4.28	1.98	1.58	1.58	1.58	1.58
$79.25	$79.75	15.79	13.49	11.19	8.89	6.59	4.29	1.99	1.59	1.59	1.59	1.59
$79.75	$80.25	16.00	13.66	11.32	8.98	6.64	4.30	1.96	1.60	1.60	1.60	1.60
$80.25	$80.75	16.21	13.91	11.61	9.31	6.91	4.61	2.31	1.61	1.61	1.61	1.61
$80.75	$81.25	16.22	13.92	11.62	9.32	6.92	4.62	2.32	1.62	1.62	1.62	1.62
$81.25	$81.75	16.23	13.93	11.63	9.33	6.93	4.63	2.33	1.63	1.63	1.63	1.63
$81.75	$82.25	16.40	14.06	11.72	9.38	7.04	4.70	2.36	1.64	1.64	1.64	1.64
$82.25	$82.75	16.55	14.25	11.95	9.65	7.35	5.05	2.75	1.65	1.65	1.65	1.65
$82.75	$83.25	16.56	14.26	11.96	9.66	7.36	5.06	2.76	1.66	1.66	1.66	1.66

Weekly withholding table combining income tax and employees' Federal Insurance Contributions Act tax (2 percent)—Continued

This table to be used only if wages for income tax withholding and wages for employees' F. I. C. A. tax are identical

If wages are—		And the number of withholding exemptions claimed is—										
At least	But less than	0	1	2	3	4	5	6	7	8	9	10
		The amount of income tax and F. I. C. A. tax to be withheld shall be—										
$83.25	$83.75	16.57	$14.27	$11.97	$9.67	$7.37	$5.07	$2.77	$1.67	$1.67	$1.67	$1.67
$83.75	$84.25	16.80	14.46	12.12	9.78	7.44	5.10	2.76	1.68	1.68	1.68	1.68
$84.25	$84.75	16.99	14.69	12.39	10.09	7.79	5.49	3.19	1.69	1.69	1.69	1.69
$84.75	$85.25	17.00	14.70	12.40	10.10	7.80	5.50	3.20	1.70	1.70	1.70	1.70
$85.25	$85.75	17.01	14.71	12.41	10.11	7.81	5.51	3.21	1.71	1.71	1.71	1.71
$85.75	$86.25	17.20	14.86	12.52	10.18	7.84	5.50	3.16	1.72	1.72	1.72	1.72
$86.25	$86.75	17.43	15.13	12.73	10.43	8.13	5.83	3.53	1.73	1.73	1.73	1.73
$86.75	$87.25	17.44	15.14	12.74	10.44	8.14	5.84	3.54	1.74	1.74	1.74	1.74
$87.25	$87.75	17.45	15.15	12.75	10.45	8.15	5.85	3.55	1.75	1.75	1.75	1.75
$87.75	$88.25	17.60	15.26	12.92	10.58	8.24	5.90	3.56	1.76	1.76	1.76	1.76
$88.25	$88.75	17.77	15.47	13.17	10.87	8.57	6.27	3.97	1.77	1.77	1.77	1.77
$88.75	$89.25	17.78	15.48	13.18	10.88	8.58	6.28	3.98	1.78	1.78	1.78	1.78
$89.25	$89.75	17.79	15.49	13.19	10.89	8.59	6.29	3.99	1.79	1.79	1.79	1.79
$89.75	$90.25	18.00	15.66	13.32	10.98	8.64	6.30	3.96	1.80	1.80	1.80	1.80
$90.25	$90.75	18.21	15.91	13.61	11.31	8.91	6.61	4.31	2.01	1.81	1.81	1.81
$90.75	$91.25	18.22	15.92	13.62	11.32	8.92	6.62	4.32	2.02	1.82	1.82	1.82
$91.25	$91.75	18.23	15.93	13.63	11.33	8.93	6.63	4.33	2.03	1.83	1.83	1.83
$91.75	$92.25	18.40	16.06	13.72	11.38	9.04	6.70	4.36	2.02	1.84	1.84	1.84
$92.25	$92.75	18.55	16.25	13.95	11.65	9.35	7.05	4.75	2.45	1.85	1.85	1.85
$92.75	$93.25	18.56	16.26	13.96	11.66	9.36	7.06	4.76	2.46	1.86	1.86	1.86
$93.25	$93.75	18.57	16.27	13.97	11.67	9.37	7.07	4.77	2.47	1.87	1.87	1.87
$93.75	$94.25	18.80	16.46	14.12	11.78	9.44	7.10	4.76	2.42	1.88	1.88	1.88
$94.25	$94.75	18.99	16.69	14.39	12.09	9.79	7.49	5.19	2.79	1.89	1.89	1.89
$94.75	$95.25	19.00	16.70	14.40	12.10	9.80	7.50	5.20	2.80	1.90	1.90	1.90
$95.25	$95.75	19.01	16.71	14.41	12.11	9.81	7.51	5.21	2.81	1.91	1.91	1.91
$95.75	$96.25	19.20	16.86	14.52	12.18	9.84	7.50	5.16	2.82	1.92	1.92	1.92
$96.25	$96.75	19.43	17.13	14.73	12.43	10.13	7.83	5.53	3.23	1.93	1.93	1.93
$96.75	$97.25	19.44	17.14	14.74	12.44	10.14	7.84	5.54	3.24	1.94	1.94	1.94
$97.25	$97.75	19.45	17.15	14.75	12.45	10.15	7.85	5.55	3.25	1.95	1.95	1.95
$97.75	$98.25	19.60	17.26	14.92	12.58	10.24	7.90	5.56	3.22	1.96	1.96	1.96
$98.25	$98.75	19.77	17.47	15.17	12.87	10.57	8.27	5.97	3.67	1.97	1.97	1.97
$98.75	$99.25	19.78	17.48	15.18	12.88	10.58	8.28	5.98	3.68	1.98	1.98	1.98
$99.25	$99.75	19.79	17.49	15.19	12.89	10.59	8.29	5.99	3.69	1.99	1.99	1.99
$99.75	$100.25	20.00	17.66	15.32	12.98	10.64	8.30	5.96	3.62	2.00	2.00	2.00
$100.25	$100.75	20.51	18.11	15.81	13.51	11.21	8.91	6.61	4.31	2.01	2.01	2.01
$100.75	$101.25	20.52	18.12	15.82	13.52	11.22	8.92	6.62	4.32	2.02	2.02	2.02
$101.25	$101.75	20.53	18.13	15.83	13.53	11.23	8.93	6.63	4.33	2.03	2.03	2.03
$101.75	$102.25	20.54	18.14	15.84	13.54	11.24	8.94	6.64	4.34	2.04	2.04	2.04
$102.25	$102.75	20.55	18.15	15.85	13.55	11.25	8.95	6.65	4.35	2.05	2.05	2.05
$102.75	$103.25	20.56	18.16	15.86	13.56	11.26	8.96	6.66	4.36	2.06	2.06	2.06
$103.25	$103.75	20.57	18.17	15.87	13.57	11.27	8.97	6.67	4.37	2.07	2.07	2.07
$103.75	$104.25	20.58	18.18	15.88	13.58	11.28	8.98	6.68	4.38	2.08	2.08	2.08
$104.25	$104.75	20.59	18.19	15.89	13.59	11.29	8.99	6.69	4.39	2.09	2.09	2.09
$104.75	$105.25	21.00	18.66	16.32	13.98	11.64	9.30	6.96	4.62	2.28	2.10	2.10
$105.25	$105.75	21.51	19.11	16.81	14.51	12.21	9.91	7.61	5.31	3.01	2.11	2.11
$105.75	$106.25	21.52	19.12	16.82	14.52	12.22	9.92	7.62	5.32	3.02	2.12	2.12
$106.25	$106.75	21.53	19.13	16.83	14.53	12.23	9.93	7.63	5.33	3.03	2.13	2.13
$106.75	$107.25	21.54	19.14	16.84	14.54	12.24	9.94	7.64	5.34	3.04	2.14	2.14
$107.25	$107.75	21.55	19.15	16.85	14.55	12.25	9.95	7.65	5.35	3.05	2.15	2.15
$107.75	$108.25	21.56	19.16	16.86	14.56	12.26	9.96	7.66	5.36	3.06	2.16	2.16
$108.25	$108.75	21.57	19.17	16.87	14.57	12.27	9.97	7.67	5.37	3.07	2.17	2.17
$108.75	$109.25	21.58	19.18	16.88	14.58	12.28	9.98	7.68	5.38	3.08	2.18	2.18
$109.25	$109.75	21.59	19.19	16.89	14.59	12.29	9.99	7.69	5.39	3.09	2.19	2.19
$109.75	$110.25	22.00	19.66	17.32	14.98	12.64	10.30	7.96	5.62	3.28	2.20	2.20
$110.25	$110.75	22.51	20.11	17.81	15.51	13.21	10.91	8.61	6.31	4.01	2.21	2.21
$110.75	$111.25	22.52	20.12	17.82	15.52	13.22	10.92	8.62	6.32	4.02	2.22	2.22
$111.25	$111.75	22.53	20.13	17.83	15.53	13.23	10.93	8.63	6.33	4.03	2.23	2.23
$111.75	$112.25	22.54	20.14	17.84	15.54	13.24	10.94	8.64	6.34	4.04	2.24	2.24
$112.25	$112.75	22.55	20.15	17.85	15.55	13.25	10.95	8.65	6.35	4.05	2.25	2.25
$112.75	$113.25	22.56	20.16	17.86	15.56	13.26	10.96	8.66	6.36	4.06	2.26	2.26
$113.25	$113.75	22.57	20.17	17.87	15.57	13.27	10.97	8.67	6.37	4.07	2.27	2.27
$113.75	$114.25	22.58	20.18	17.88	15.58	13.28	10.98	8.68	6.38	4.08	2.28	2.28
$114.25	$114.75	22.59	20.19	17.89	15.59	13.29	10.99	8.69	6.39	4.09	2.29	2.29
$114.75	$115.25	23.00	20.66	18.32	15.98	13.64	11.30	8.96	6.62	4.28	2.30	2.30
$115.25	$115.75	23.51	21.11	18.81	16.51	14.21	11.91	9.61	7.31	5.01	2.71	2.31
$115.75	$116.25	23.52	21.12	18.82	16.52	14.22	11.92	9.62	7.32	5.02	2.72	2.32
$116.25	$116.75	23.53	21.13	18.83	16.53	14.23	11.93	9.63	7.33	5.03	2.73	2.33
$116.75	$117.25	23.54	21.14	18.84	16.54	14.24	11.94	9.64	7.34	5.04	2.74	2.34
$117.25	$117.75	23.55	21.15	18.85	16.55	14.25	11.95	9.65	7.35	5.05	2.75	2.35
$117.75	$118.25	23.56	21.16	18.86	16.56	14.26	11.96	9.66	7.36	5.06	2.76	2.36

Weekly withholding table combining income tax and employees' Federal Insurance Contributions Act tax (2 percent)—Continued

This table to be used only if wages for income tax withholding and wages for employees' F. I. C. A. tax are identical

If wages are—		And the number of withholding exemptions claimed is—										
At least	But less than	0	1	2	3	4	5	6	7	8	9	10
		The amount of income tax and F. I. C. A. tax to be withheld shall be—										
$118.25	$118.75	$23.57	$21.17	$18.87	$16.57	$14.27	$11.97	$9.67	$7.37	$5.07	$2.77	$2.37
$118.75	$119.25	23.58	21.18	18.88	16.58	14.28	11.98	9.68	7.38	5.08	2.78	2.38
$119.25	$119.75	23.59	21.19	18.89	16.59	14.29	11.99	9.69	7.39	5.09	2.79	2.39
$119.75	$120.25	24.00	21.66	19.32	16.98	14.64	12.30	9.96	7.62	5.28	2.94	2.40
$120.25	$120.75	24.51	22.11	19.81	17.51	15.21	12.91	10.61	8.31	6.01	3.71	2.41
$120.75	$121.25	24.52	22.12	19.82	17.52	15.22	12.92	10.62	8.32	6.02	3.72	2.42
$121.25	$121.75	24.53	22.13	19.83	17.53	15.23	12.93	10.63	8.33	6.03	3.73	2.43
$121.75	$122.25	24.54	22.14	19.84	17.54	15.24	12.94	10.64	8.34	6.04	3.74	2.44
$122.25	$122.75	24.55	22.15	19.85	17.55	15.25	12.95	10.65	8.35	6.05	3.75	2.45
$122.75	$123.25	24.56	22.16	19.86	17.56	15.26	12.96	10.66	8.36	6.06	3.76	2.46
$123.25	$123.75	24.57	22.17	19.87	17.57	15.27	12.97	10.67	8.37	6.07	3.77	2.47
$123.75	$124.25	24.58	22.18	19.88	17.58	15.28	12.98	10.68	8.38	6.08	3.78	2.48
$124.25	$124.75	24.59	22.19	19.89	17.59	15.29	12.99	10.69	8.39	6.09	3.79	2.49
$124.75	$125.25	25.00	22.66	20.32	17.98	15.64	13.30	10.96	8.62	6.28	3.94	2.50
$125.25	$125.75	25.51	23.11	20.81	18.51	16.21	13.91	11.61	9.31	7.01	4.71	2.51
$125.75	$126.25	25.52	23.12	20.82	18.52	16.22	13.92	11.62	9.32	7.02	4.72	2.52
$126.25	$126.75	25.53	23.13	20.83	18.53	16.23	13.93	11.63	9.33	7.03	4.73	2.53
$126.75	$127.25	25.54	23.14	20.84	18.54	16.24	13.94	11.64	9.34	7.04	4.74	2.54
$127.25	$127.75	25.55	23.15	20.85	18.55	16.25	13.95	11.65	9.35	7.05	4.75	2.55
$127.75	$128.25	25.56	23.16	20.86	18.56	16.26	13.96	11.66	9.36	7.06	4.76	2.56
$128.25	$128.75	25.57	23.17	20.87	18.57	16.27	13.97	11.67	9.37	7.07	4.77	2.57
$128.75	$129.25	25.58	23.18	20.88	18.58	16.28	13.98	11.68	9.38	7.08	4.78	2.58
$129.25	$129.75	25.59	23.19	20.89	18.59	16.29	13.99	11.69	9.39	7.09	4.79	2.59
$129.75	$130.25	26.00	23.66	21.32	18.98	16.64	14.30	11.96	9.62	7.28	4.94	2.60
$130.25	$130.75	26.51	24.11	21.81	19.51	17.21	14.91	12.61	10.31	8.01	5.71	3.41
$130.75	$131.25	26.52	24.12	21.82	19.52	17.22	14.92	12.62	10.32	8.02	5.72	3.42
$131.25	$131.75	26.53	24.13	21.83	19.53	17.23	14.93	12.63	10.33	8.03	5.73	3.43
$131.75	$132.25	26.54	24.14	21.84	19.54	17.24	14.94	12.64	10.34	8.04	5.74	3.44
$132.25	$132.75	26.55	24.15	21.85	19.55	17.25	14.95	12.65	10.35	8.05	5.75	3.45
$132.75	$133.25	26.56	24.16	21.86	19.56	17.26	14.96	12.66	10.36	8.06	5.76	3.46
$133.25	$133.75	26.57	24.17	21.87	19.57	17.27	14.97	12.67	10.37	8.07	5.77	3.47
$133.75	$134.25	26.58	24.18	21.88	19.58	17.28	14.98	12.68	10.38	8.08	5.78	3.48
$134.25	$134.75	26.59	24.19	21.89	19.59	17.29	14.99	12.69	10.39	8.09	5.79	3.49
$134.75	$135.25	27.00	24.66	22.32	19.98	17.64	15.30	12.96	10.62	8.28	5.94	3.60
		20 percent of the excess over $135.25 plus—										
$135.25 and	over	27.05	24.71	22.37	20.03	17.69	15.35	13.01	10.67	8.33	5.99	3.65

REGULATIONS 116, SECTION 405.201: Requirement of withholding. Rev. Rul. 295

INTERNAL REVENUE CODE

Tables which may be used by employers in withholding Federal income tax from wages paid for payroll periods of 10 days and 28 days.

The following withholding tables covering payroll periods of 10 days and 28 days have been constructed on the basis of the lower withholding rate prescribed by section 1622 of the Internal Revenue Code with respect to wages paid on and after January 1, 1954.

The 10-day and 28-day payroll period withholding tables may be obtained by employers from the district directors of internal revenue.

The percentage method of withholding and the regular tables covering weekly, biweekly, semimonthly, monthly, and daily or miscellaneous payroll periods are found in Circular E, Rev. January 1954, Employer's Tax Guide.

If the payroll period with respect to an employee is a 10-day period

And the wages are—		And the number of withholding exemptions claimed is—										
At least	But less than	0	1	2	3	4	5	6	7	8	9	10 or more
		The amount of tax to be withheld shall be—										
$0	$20.00	18% of wages	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
$20.00	$22.50	$4.00	.50	0	0	0	0	0	0	0	0	0
$22.50	$25.00	4.50	1.00	0	0	0	0	0	0	0	0	0
$25.00	$27.50	4.50	1.50	0	0	0	0	0	0	0	0	0
$27.50	$30.00	5.00	2.00	0	0	0	0	0	0	0	0	0
$30.00	$32.50	5.50	2.50	0	0	0	0	0	0	0	0	0
$32.50	$35.00	6.00	3.00	0	0	0	0	0	0	0	0	0
$35.00	$37.50	6.50	3.00	0	0	0	0	0	0	0	0	0
$37.50	$40.00	7.00	3.50	.50	0	0	0	0	0	0	0	0
$40.00	$42.50	7.50	4.00	1.00	0	0	0	0	0	0	0	0
$42.50	$45.00	8.00	4.50	1.50	0	0	0	0	0	0	0	0
$45.00	$47.50	8.50	5.00	1.50	0	0	0	0	0	0	0	0
$47.50	$50.00	9.00	5.50	2.00	0	0	0	0	0	0	0	0
$50.00	$52.50	9.00	6.00	2.50	0	0	0	0	0	0	0	0
$52.50	$55.00	9.50	6.50	3.00	0	0	0	0	0	0	0	0
$55.00	$57.50	10.00	7.00	3.50	.50	0	0	0	0	0	0	0
$57.50	$60.00	10.50	7.50	4.00	.50	0	0	0	0	0	0	0
$60.00	$62.50	11.00	7.50	4.50	1.00	0	0	0	0	0	0	0
$62.50	$65.00	11.50	8.00	5.00	1.50	0	0	0	0	0	0	0
$65.00	$67.50	12.00	8.50	5.50	2.00	0	0	0	0	0	0	0
$67.50	$70.00	12.50	9.00	6.00	2.50	0	0	0	0	0	0	0
$70.00	$72.50	13.00	9.50	6.00	3.00	0	0	0	0	0	0	0
$72.50	$75.00	13.50	10.00	6.50	3.50	0	0	0	0	0	0	0
$75.00	$77.50	13.50	10.50	7.00	4.00	.50	0	0	0	0	0	0
$77.50	$80.00	14.00	11.00	7.50	4.50	1.00	0	0	0	0	0	0
$80.00	$82.50	14.50	11.50	8.00	5.00	1.50	0	0	0	0	0	0
$82.50	$85.00	15.00	12.00	8.50	5.00	2.00	0	0	0	0	0	0
$85.00	$87.50	15.50	12.00	9.00	5.50	2.50	0	0	0	0	0	0
$87.50	$90.00	16.00	12.50	9.50	6.00	3.00	0	0	0	0	0	0
$90.00	$92.50	16.50	13.00	10.00	6.50	3.50	0	0	0	0	0	0
$92.50	$95.00	17.00	13.50	10.50	7.00	3.50	.50	0	0	0	0	0
$95.00	$97.50	17.50	14.00	10.50	7.50	4.00	1.00	0	0	0	0	0
$97.50	$100.00	18.00	14.50	11.00	8.00	4.50	1.50	0	0	0	0	0
$100.00	$105.00	18.50	15.00	12.00	8.50	5.50	2.00	0	0	0	0	0
$105.00	$110.00	19.50	16.00	13.00	9.50	6.00	3.00	0	0	0	0	0
$110.00	$115.00	20.50	17.00	13.50	10.50	7.00	4.00	.50	0	0	0	0
$115.00	$120.00	21.00	18.00	14.50	11.50	8.00	4.50	1.50	0	0	0	0
$120.00	$125.00	22.00	19.00	15.50	12.00	9.00	5.50	2.50	0	0	0	0
$125.00	$130.00	23.00	19.50	16.50	13.00	10.00	6.50	3.00	0	0	0	0
$130.00	$135.00	24.00	20.50	17.50	14.00	10.50	7.50	4.00	1.00	0	0	0
$135.00	$140.00	25.00	21.50	18.00	15.00	11.50	8.50	5.00	1.50	0	0	0
$140.00	$145.00	25.50	22.50	19.00	16.00	12.50	9.00	6.00	2.50	0	0	0
$145.00	$150.00	26.50	23.50	20.00	16.50	13.50	10.00	7.00	3.50	0	0	0
$150.00	$155.00	27.50	24.00	21.00	17.50	14.50	11.00	7.50	4.50	1.00	0	0
$155.00	$160.00	28.50	25.00	22.00	18.50	15.00	12.00	8.50	5.50	2.00	0	0
$160.00	$165.00	29.50	26.00	22.50	19.50	16.00	13.00	9.50	6.00	3.00	0	0
$165.00	$170.00	30.00	27.00	23.50	20.50	17.00	13.50	10.50	7.00	4.00	.50	0
$170.00	$175.00	31.00	28.00	24.50	21.00	18.00	14.50	11.50	8.00	4.50	1.50	0
$175.00	$180.00	32.00	28.50	25.50	22.00	19.00	15.50	12.00	9.00	5.50	2.50	0
$180.00	$185.00	33.00	29.50	26.50	23.00	19.50	16.50	13.00	10.00	6.50	3.50	0
$185.00	$190.00	34.00	30.50	27.00	24.00	20.50	17.50	14.00	10.50	7.50	4.00	1.00
$190.00	$195.00	34.50	31.50	28.00	25.00	21.50	18.00	15.00	11.50	8.50	5.00	2.00
$195.00	$200.00	35.50	32.50	29.00	25.50	22.50	19.00	16.00	12.50	9.00	6.00	2.50
$200.00	$210.00	37.00	33.50	30.50	27.00	23.50	20.50	17.00	14.00	10.50	7.50	4.00
$210.00	$220.00	38.50	35.50	32.00	29.00	25.50	22.50	19.00	15.50	12.50	9.00	6.00
$220.00	$230.00	40.50	37.00	34.00	30.50	27.50	24.00	21.00	17.50	14.00	11.00	7.50
$230.00	$240.00	42.50	39.00	35.50	32.50	29.00	26.00	22.50	19.50	16.00	12.50	9.50
$240.00	$250.00	44.00	41.00	37.50	34.00	31.00	27.50	24.50	21.00	18.00	14.50	11.00
$250.00	$260.00	46.00	42.50	39.50	36.00	32.50	29.50	26.00	23.00	19.50	16.50	13.00
$260.00	$270.00	47.50	44.50	41.00	38.00	34.50	31.50	28.00	24.50	21.50	18.00	15.00
$270.00	$280.00	49.50	46.00	43.00	39.50	36.50	33.00	30.00	26.50	23.00	20.00	16.50
$280.00	$290.00	51.50	48.00	44.50	41.50	38.00	35.00	31.50	28.50	25.00	21.50	18.50
$290.00	$300.00	53.00	50.00	46.50	43.00	40.00	36.50	33.50	30.00	27.00	23.50	20.00
		18 percent of the excess over $300 plus—										
$300.00 and over		54.00	50.50	47.50	44.00	41.00	37.50	34.50	31.00	27.50	24.50	21.00

If the payroll period with respect to an employee is a 28-day period

And the wages are—		And the number of withholding exemptions claimed is—										
At least	But less than	0	1	2	3	4	5	6	7	8	9	10 or more
		The amount of tax to be withheld shall be—										
$0	$56.00	18% of wages	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0
$56.00	$63.00	$11.20	1.40	0	0	0	0	0	0	0	0	0
$63.00	$70.00	12.60	2.80	0	0	0	0	0	0	0	0	0
$70.00	$77.00	12.60	4.20	0	0	0	0	0	0	0	0	0
$77.00	$84.00	14.00	5.60	0	0	0	0	0	0	0	0	0
$84.00	$91.00	15.40	7.00	0	0	0	0	0	0	0	0	0
$91.00	$98.00	16.80	8.40	0	0	0	0	0	0	0	0	0
$98.00	$105.00	18.20	8.40	0	0	0	0	0	0	0	0	0
$105.00	$112.00	19.60	9.80	1.40	0	0	0	0	0	0	0	0
$112.00	$119.00	21.00	11.20	2.80	0	0	0	0	0	0	0	0
$119.00	$126.00	22.40	12.60	4.20	0	0	0	0	0	0	0	0
$126.00	$133.00	23.80	14.00	4.20	0	0	0	0	0	0	0	0
$133.00	$140.00	25.20	15.40	5.60	0	0	0	0	0	0	0	0
$140.00	$147.00	25.20	16.80	7.00	0	0	0	0	0	0	0	0
$147.00	$154.00	26.60	18.20	8.40	0	0	0	0	0	0	0	0
$154.00	$161.00	28.00	19.60	9.80	1.40	0	0	0	0	0	0	0
$161.00	$168.00	29.40	21.00	11.20	1.40	0	0	0	0	0	0	0
$168.00	$175.00	30.80	21.00	12.60	2.80	0	0	0	0	0	0	0
$175.00	$182.00	32.20	22.40	14.00	4.20	0	0	0	0	0	0	0
$182.00	$189.00	33.60	23.80	15.40	5.60	0	0	0	0	0	0	0
$189.00	$196.00	35.00	25.20	16.80	7.00	0	0	0	0	0	0	0
$196.00	$203.00	36.40	26.60	16.80	8.40	0	0	0	0	0	0	0
$203.00	$210.00	37.80	28.00	18.20	9.80	0	0	0	0	0	0	0
$210.00	$217.00	37.80	29.40	19.60	11.20	1.40	0	0	0	0	0	0
$217.00	$224.00	39.20	30.80	21.00	12.60	2.80	0	0	0	0	0	0
$224.00	$231.00	40.60	32.20	22.40	14.00	4.20	0	0	0	0	0	0
$231.00	$238.00	42.00	33.60	23.80	14.00	5.60	0	0	0	0	0	0
$238.00	$245.00	43.40	33.60	25.20	15.40	7.00	0	0	0	0	0	0
$245.00	$252.00	44.80	35.00	26.60	16.80	8.40	0	0	0	0	0	0
$252.00	$259.00	46.20	36.40	28.00	18.20	9.80	0	0	0	0	0	0
$259.00	$266.00	47.60	37.80	29.40	19.60	9.80	1.40	0	0	0	0	0
$266.00	$273.00	49.00	39.20	29.40	21.00	11.20	2.80	0	0	0	0	0
$273.00	$280.00	50.40	40.60	30.80	22.40	12.60	4.20	0	0	0	0	0
$280.00	$294.00	51.80	42.00	33.60	23.80	15.40	5.60	0	0	0	0	0
$294.00	$308.00	54.60	44.80	36.40	26.60	16.80	8.40	0	0	0	0	0
$308.00	$322.00	57.40	47.60	37.80	29.40	19.60	11.20	1.40	0	0	0	0
$322.00	$336.00	58.80	50.40	40.60	32.20	22.40	12.60	4.20	0	0	0	0
$336.00	$350.00	61.60	53.20	43.40	33.60	25.20	15.40	7.00	0	0	0	0
$350.00	$364.00	64.40	54.60	46.20	36.40	28.00	18.20	8.40	0	0	0	0
$364.00	$378.00	67.20	57.40	49.00	39.20	29.40	21.00	11.20	2.80	0	0	0
$378.00	$392.00	70.00	60.20	50.40	42.00	32.20	23.80	14.00	4.20	0	0	0
$392.00	$406.00	71.40	63.00	53.20	44.80	35.00	25.20	16.80	7.00	0	0	0
$406.00	$420.00	74.20	65.80	56.00	46.20	37.80	28.00	19.60	9.80	0	0	0
$420.00	$434.00	77.00	67.20	58.80	49.00	40.60	30.80	21.00	12.60	2.80	0	0
$434.00	$448.00	79.80	70.00	61.60	51.80	42.00	33.60	23.80	15.40	5.60	0	0
$448.00	$462.00	82.60	72.80	63.00	54.60	44.80	36.40	26.60	16.80	8.40	0	0
$462.00	$476.00	84.00	75.60	65.80	57.40	47.60	37.80	29.40	19.60	11.20	1.40	0
$476.00	$490.00	86.80	78.40	68.60	58.80	50.40	40.60	32.20	22.40	12.60	4.20	0
$490.00	$504.00	89.60	79.80	71.40	61.60	53.20	43.40	33.60	25.20	15.40	7.00	0
$504.00	$518.00	92.40	82.60	74.20	64.40	54.60	46.20	36.40	28.00	18.20	9.80	0
$518.00	$532.00	95.20	85.40	75.60	67.20	57.40	48.00	39.20	29.40	21.00	11.20	2.80
$532.00	$546.00	96.60	88.20	78.40	70.00	60.20	50.40	42.00	32.20	23.80	14.00	5.60
$546.00	$560.00	99.40	91.00	81.20	71.40	63.00	53.20	44.80	35.00	25.20	16.80	7.00
$560.00	$588.00	103.60	93.80	85.40	75.60	65.80	57.40	47.60	39.20	29.40	21.00	11.20
$588.00	$616.00	107.80	99.40	89.60	81.20	71.40	63.00	53.20	43.40	35.00	25.20	16.80
$616.00	$644.00	113.40	103.60	95.20	85.40	77.00	67.20	58.80	49.00	39.20	30.80	21.00
$644.00	$672.00	119.00	109.20	99.40	91.00	81.20	72.80	63.00	54.60	44.80	35.00	26.60
$672.00	$700.00	120.20	114.80	105.00	95.20	86.80	77.00	68.60	58.80	50.40	40.60	30.80
$700.00	$728.00	128.80	119.00	110.60	100.80	91.00	82.60	72.80	64.40	54.60	46.20	36.40
$728.00	$756.00	133.00	124.60	114.80	106.40	96.60	88.20	78.40	68.60	60.20	50.40	42.00
$756.00	$784.00	138.60	128.80	120.40	110.60	102.20	92.40	84.00	74.20	64.40	56.00	46.20
$784.00	$812.00	144.20	134.40	124.60	116.20	106.40	98.00	88.20	79.80	70.00	60.20	51.80
$812.00	$840.00	148.40	140.00	130.20	120.40	112.00	102.20	93.80	84.00	75.60	65.80	56.00
		18 percent of the excess over $840 plus—										
$840 and over		151.20	141.40	133.00	123.20	114.80	105.00	96.60	86.80	77.00	68.60	58.80

CHAPTER 10.—ADMISSIONS AND DUES

SUBCHAPTER A.—ADMISSIONS

SECTION 1700.—TAX

REGULATIONS 43, ETC. Rev. Rul. 296

INTERNAL REVENUE CODE

Exemption from Federal excise taxes extends to foreign diplomatic, consular, and other officers, and agencies of foreign governments. M. T. 7, C. B. 1943, 1151, and M. T. 19, C. B. 1944, 588, revoked.

Advice is requested as to the exemption from Federal excise taxes extended to foreign diplomatic, consular, and other officers, and agencies of foreign governments.

Ambassadors, ministers, and other duly accredited diplomatic representatives of foreign governments, together with the members of their families living with them, and members of their households, including attaches, secretaries, and clerks (but not servants), who are not citizens of the United States, nor permanent residents of the United States in an immigrant status, and who are nationals of the country of the diplomatic mission where employed, (1) are not required to pay Federal excise taxes, the legal incidence of which would otherwise fall upon them, and (2) if any such person purchases from the manufacturer thereof an article otherwise subject to a Federal excise tax on sales by manufacturers, or purchases from a retailer an article otherwise subject to a Federal excise tax on sales by retailers, the transaction will not be taxed.

The first classification, that is, Federal excise taxes the legal incidence of which would otherwise fall upon the diplomatic representatives, includes: The taxes on admissions and dues imposed under chapter 10 of the Internal Revenue Code; the tax with respect to safe deposit boxes under chapter 12 of the Code; the taxes with respect to telegraph, telephone, radio and cable facilities under subchapter B of chapter 30 of the Code; the tax on the transportation of persons under subchapter C of chapter 30 of the Code; the tax on the transportation of property under subchapter E of chapter 30 of the Code; and the documentary stamp taxes relating to the issuance and transfer of shares of stock and corporate securities, and relating also to certain foreign insurance policies, and conveyances of realty sold, imposed under chapters 11 and 31 of the Code.

The second classification includes the manufacturers' excise taxes imposed under chapter 29 of the Code; the retailers' excise taxes imposed under chapters 9A and 19 of the Code, and the tax on the sale or use of diesel fuel imposed under chapter 20 of the Code.

Consular officers of foreign governments, and other officers (other than diplomatic representatives), as well as agencies and commissions, of foreign governments are not required to pay Federal excise taxes, the legal incidence of which would otherwise fall upon them (the first classification above), in respect of transactions arising in the

performance of their official functions for which payment is made by the foreign government. However, it is to be noted that the privileges of this group do not extend to the manufacturers' and retailers' excise taxes (the second classification above).

The foregoing privileges are not dependent upon treaty provisions and apply irrespective of whether there is a treaty in force between the United States and the foreign government relative to its consular officers or other officers, agencies, or commissions.

There are in force a number of treaties between the United States and foreign governments which confer tax exemptions upon consular officers. In general, consular officers are exempted by those treaties from Federal excise taxes, the legal incidence of which would otherwise fall upon them (the first classification above), without regard to whether the transaction is official or personal, but subject to the conditions that the consular officers are not citizens of the United States and are not engaged in professional business, trade, manufacture, or commerce within the United States. It is to be noted, therefore, that under the privileges specified in the preceding paragraphs, consular officers are not required to pay the excise taxes included in the first classification above in respect of official transactions regardless of their citizenship or their professional or business activities, whereas, by virtue of the treaty exemptions, certain consular officers who comply with the conditions as to citizenship and as to professional or business activities are, unless otherwise hereinafter noted, also exempt in respect of personal transactions from the excise taxes included in the first classification above. Treaties with the nations listed below have this effect with respect to the classes of consular representatives named:

Argentina—Consuls general and consuls.
Austria—Consular officers and employees in consulates.
Belgium—Consuls general, consuls, vice consuls, and consular agents.
Bolivia—Consuls general, consuls, and officers and persons attached to the consulate.
Brazil—Consular agents and employees of consulates.
Colombia—Consuls general, consuls, and their chancellors or secretaries.
Costa Rica—Consular officers or employees.
Cuba—Consular agents and employees of consulates.
Denmark—Consuls general, consuls, and persons attached to their necessary service and vice consuls.
Ecuador—Consular agents and employees of consulates.
El Salvador—Consular officers.
Estonia—Consular officers.
Finland—Consular officers.
France—Consuls general, consuls, vice consuls, or consular agents, as well as their consular pupils, chancellors, and secretaries.
Germany—Consular officers and employees in consulates.
Greece—Consuls general, consuls, vice consuls, and consular agents.
Honduras—Consular officers.
Italy—Consular officers.
Latvia—Consular officers.
Liberia—Consular officers including employees in a consulate.
Mexico—Consular officers and employees in consulates.
Nicaragua—Consular agents and employees of consulates.
Norway—Consular officers.
Panama—Consular agents and employees of consulates.
Paraguay—Consuls general and consuls.
Peru—Consular agents and employees of consulates.
Philippines—Consular officers and employees in consulates.
Rumania—Consuls general, consuls, vice consuls, and consular agents.

Spain—Consuls general, consuls, vice consuls, consular agents, consular chancellors, secretaries, and clerks.
Sweden—Consuls general, consuls, vice consuls, deputy consuls general, deputy consuls, and consular agents.
Switzerland—Consuls general, consuls, and vice consuls.
Thailand—Consuls general, consuls, vice consuls, and other consular officers or agents.
United Kingdom—Consular officers of employees. (Except documentary stamp taxes imposed under chapters 11 and 31 of the Code, relating to the issuance and transfer of shares of stock and corporate securities, foreign insurance policies, and conveyances of realty sold.)
Uruguay—Consular agents and employees of consulates.
Yugoslavia—Consuls general, consuls, vice consuls, and consular agents.
Zanzibar—Consuls general, consuls, and consular agents.

M. T. 7, C. B. 1943, 1151, and M. T. 19, C. B. 1944, 588, are hereby revoked.

REGULATIONS 43, SECTION 101.2: Meaning of "admission." Rev. Rul. 124

INTERNAL REVENUE CODE

Payments covering admission charges to athletic and other events of educational institutions made by the Veterans' Administration on behalf of veterans attending such institutions are not subject to the tax on admissions imposed under section 1700(a) of the Internal Revenue Code.

Advice is requested whether charges for admission to athletic and other events imposed with respect to veterans attending educational institutions, payment of which is made by the Veterans' Administration, are exempt from the tax on admissions imposed by section 1700(a) of the Internal Revenue Code.

Section 3 of the act of August 12, 1935, 49 Stat. 607, relating to benefit payments to veterans, provides in part that "* * * Payments made to or on account of a beneficiary under any of the laws relating to veterans shall be exempt from taxation * * *." (See Mim. 4411, C. B. XV-1, 497.) The act of March 24, 1943, 57 Stat. 43, providing for the vocational rehabilitation of veterans, and the Servicemen's Readjustment Act of 1944, 58 Stat. 284, providing for aid for the readjustment in civilian life of returning World War II veterans, provide for certain benefit payments by the Veterans' Administration on behalf of veterans. These payments are subject to the provisions of section 3 of the act of August 12, 1935. Also, the Servicemen's Readjustment Act of 1944 specifically provides, except as otherwise provided therein, that the provisions of the act of August 12, 1935, shall be applicable under that act.

In view of the foregoing, it is held that payments covering admission charges to athletic and other events of educational institutions made by the Veterans' Administration on behalf of veterans attending such institutions under the above-mentioned acts are not subject to the tax on admissions imposed by section 1700(a) of the Code.

REGULATIONS 43, SECTION 101.2: Meaning of "admission." Rev. Rul. 175

INTERNAL REVENUE CODE

The tax on admissions imposed by section 1700(a) of the Internal Revenue Code applies to charges made by a beach club for the sea-

sonal use of cabins and cabanas, and to daily charges for guests, where admission to the premises is gained by the payment of such charges.

Advice is requested whether the tax on admissions imposed by section 1700(a) of the Internal Revenue Code applies to charges made for the seasonal use of cabins and cabanas and to daily charges for guests under the following circumstances.

A beach club operated by a private enterprise for profit maintains cabins, cabanas, swimming pools, wading pools for children, and a dancing area. The property is not open to the public. The cabins and cabanas are leased on a seasonal basis. The lease of a cabin or cabana entitles the lessee and his family to the right of admission to the grounds and to the use of all facilities for the season. It also entitles him to have day guests at a stated charge per person. The beach club does not qualify as a social, athletic, or sporting club or organization within the meaning of section 1710(a)(1) of the Code, since the lessees have no voice in the management of the enterprise nor any of the other usual privileges granted to members of such social, athletic, or sporting clubs.

Section 1700(a) imposes a tax on admissions to any place, including admission by season ticket. Section 101.2 of Regulations 43 provides that the tax applies to the amount which must be paid in order to gain admission to a place.

It has been the policy of the Internal Revenue Service not to regard seasonal charges of the nature described as charges for admission. Therefore, such charges have not been subjected to the tax imposed by section 1700(a) of the Code, although the daily charges for guests have been regarded as taxable admission charges. Upon reconsideration, it is now held that, since the seasonal lease of a cabin or cabana from the club entitles the lessee and his family (in each case specifically limited to the number of persons) to admission to the ground and to the use of the facilities maintained by the club, the charge made for the lease of the cabin or cabana, as well as the daily charges for guests, constitute charges for the right of admission, and as such are subject to the tax on admissions imposed by section 1700(a) of the Code. *Cf.* Rev. Rul. 177, page 341.

Because of the policy heretofore maintained regarding the nonapplication of the tax on admissions to such seasonal charges, under the authority contained in section 3791(b) of the Code, the instant ruling will not be applied retroactively with respect to any seasonal charges made and paid prior to October 1, 1953, for the current season.

REGULATIONS 43, SECTION 101.2: Meaning of "admission."

INTERNAL REVENUE CODE

Application of tax to daily ground fees paid to a private club the purposes of which include the promotion of nudism. (See Rev. Rul. 253, p. 342.)

REGULATIONS 43, SECTION 101.3: Meaning of the term "place." (Also Section 3469, Regulations 42, Section 130.51.) Rev. Rul. 223

INTERNAL REVENUE CODE

An amount paid for a ride on a miniature or subgauge railway furnishing point to point transportation service for the accommodation and convenience of the public is not considered an amount paid for admission to a "place" within the meaning of section 1700(a) of the Internal Revenue Code, but rather a charge for transportation and is not subject to the tax on admissions imposed by that section. Where the amount paid for transportation on such a railway exceeds 35 cents, the amount so paid is subject to tax on the transportation of persons imposed by section 3469 of the Code. Amounts paid for rides on a miniature railway which is operated as an amusement device and not for the purpose of furnishing point to point transportation for the accommodation and convenience of the public constitute amounts paid for admission to a "place" or definite location within the meaning of section 1700(a) of the Code and are subject to the tax imposed thereunder. See M. T. 30, C. B. 1948-2, 167.

REGULATIONS 43, SECTION 101.13: Basis, rate, and computation of tax. Rev. Rul. 176

INTERNAL REVENUE CODE

The cabaret tax imposed by section 1700(e) of the Internal Revenue Code does not apply to amounts for food, refreshment, or merchandise paid by entertainers, waitresses, or other employees of a cabaret during the time they are engaged in the performance of their respective duties, since the tax imposed by that section applies only to amounts paid by or for patrons or guests of a cabaret.

SECTION 1701.—EXEMPTIONS FROM TAX

REGULATIONS 43, SECTION 101.15: Exemptions from tax. Rev. Rul. 125

INTERNAL REVENUE CODE

The rental of an athletic field, on a variable basis, by a high school for the purpose of holding its athletic events would not defeat its exemption from the admissions tax under section 1701(a)(1)(A)(ii) of the Internal Revenue Code.

Advice is requested whether a high school's exemption from admissions tax under section 1701(a)(1)(A)(ii) of the Internal Revenue Code would be affected if the high school paid rent on a variable basis for the use of an athletic field on which to hold its athletic events.

In the instant case, an athletic field is available to a high school for the purpose of holding its athletic events on such field. An agreement has been reached between school authorities and the owners of the athletic field whereby the school will pay for the direct expenses of

each game, such as the costs of lights, ground upkeep, supplies, and insurance. In addition, the first $100 of net proceeds are to be retained by the school for its purposes, the second $100 shall be paid to the owners of the field as a rental fee for the school's use of the field, and the balance remaining shall be retained by the school. Where the gate receipts from any event are not sufficient for the payment of the direct expenses, the first $100 credit and the rental fee, the owners will waive the requirement of that fee.

Section 1701 of the Internal Revenue Code provides in part as follows:

SEC. 1701. EXEMPTIONS FROM TAX.

No tax shall be levied * * * in respect of—

(a) CERTAIN RELIGIOUS, EDUCATIONAL, OR CHARITABLE ENTERTAINMENTS, ETC.—

(1) IN GENERAL.— * * * any admissions all the proceeds of which inure—

(A) exclusively to the benefit of—

* * * * * * *

(ii) an educational institution which is exempt under section 101(6) or which is an educational institution of a government or political subdivision thereof, if such organization normally maintains a regular faculty and curriculum and normally has a regularly organized body of pupils or students in attendance at the place where its educational activities are regularly carried on; * * *

* * * * * * *

if no part of the net earnings thereof inures to the benefit of any private stockholder or individual; * * *

* * * * * * *

(2) NONEXEMPT ADMISSIONS.—The exemption provided under paragraph (1) shall not apply in the case of admissions to (A) any athletic game or exhibition unless the proceeds inure exclusively to the benefit of an elementary or secondary school or unless in the case of an athletic game between two elementary or secondary schools, the entire gross proceeds from such game inure to the benefit of a hospital for crippled children, (B) wrestling matches, prize fights, or boxing, sparring, or other pugilistic matches or exhibitions, (C) carnivals, rodeos, or circuses in which any professional performer or operator participates for compensation, or (D) any motion picture exhibition.

Admissions, or charges in excess of the regular or established price of admissions, are not exempt merely because the proceeds are to be used for educational purposes. The primary conditions are that (1) all the proceeds of the admissions or excess charges, as the case may be, inure to the benefit of a qualified educational institution, and (2) the event is not of a type described in section 1701(a)(2) of the Code. The term "all the proceeds" means all the proceeds of the regular admission charges or excess charges, as the case may be, after payment of actual and reasonable expenses incurred in presenting the event. If the expenses are in excess of what is reasonable and necessary under the circumstances, all the proceeds would not be deemed to inure exclusively to the benefit of the exempt organization. (Sec. 101.15 of Regulations 43.)

It is held that the payment of direct expenses, plus a rental fee for the use of an athletic field by a high school on the foregoing basis, constitutes a reasonable and necessary expense and would not defeat the school's exemption under section 1701(a)(1)(A)(ii) of the Internal Revenue Code.

REGULATIONS 43, SECTION 101.15: Exemptions from tax. Rev. Rul. 126

INTERNAL REVENUE CODE

The exemption from the tax on admissions provided for educational institutions by section 1701(a)(1)(A)(ii) of the Internal Revenue Code does not apply to admissions to plays conducted by a "little theater" organization, the proceeds of which inure to the benefit of such organization.

Advice is requested whether the exemption from the tax on admissions provided by section 1701(a)(1)(A)(ii) of the Internal Revenue Code is applicable to admissions to plays conducted by a "little theater" organization, the proceeds of which inure to the benefit of such organization.

In the instant case, the purpose of the "little theater" is to provide for the people of the community the opportunity of self expression in the drama and kindred fields. The organization has been held exempt from Federal income tax under section 101(6) of the Internal Revenue Code, as being organized and operated exclusively for educational purposes.

Section 1701 of the Code provides in part as follows:

SEC. 1701. EXEMPTIONS FROM TAX.

No tax shall be levied * * * in respect of—

(a) CERTAIN RELIGIOUS, EDUCATIONAL, OR CHARITABLE ENTERTAINMENTS, ETC.—

(1) IN GENERAL.—* * * any admissions all the proceeds of which inure—

(A) exclusively to the benefit of—

* * * * * * *

(ii) an educational institution which is exempt under section 101(6) or which is an educational institution of a government or political subdivision thereof, if such organization normally maintains a regular faculty and curriculum and normally has a regularly organized body of pupils or students in attendance at the place where its educational activities are regularly carried on; * * *

Section 101.15(b)(3) of Regulations 43 provides that admissions, or excess charges, all the proceeds of which inure exclusively to the benefit of an educational institution are exempt from the tax provided (i) the educational institution is exempt from Federal income tax under section 101(6) of the Code, or is an educational institution of a government or political subdivision thereof, (ii) the institution normally maintains a regular faculty and curriculum and normally has a regularly organized body of pupils or students in attendance at the place where its educational activities are regularly carried on, and (iii) no part of the net earnings thereof inures to the benefit of any private stockholder or individual. Generally, this exemption applies in the case of institutions engaged in the presentation of formal instruction, such as elementary and high schools, colleges and universities, through the medium of a regular faculty and curriculum with a regularly organized body of pupils or students in attendance.

The fact that an organization may be exempt from Federal income tax under section 101(6) of the Code does not of itself qualify the organization for exemption from the admissions tax. It is the position of the Bureau that a "little theater" organization is not an educa-

tional institution of the kind contemplated by section 1701(a)(1)-(A)(ii) of the Code so as to entitle it to exemption from the collection of the admissions tax, since it does not meet the statutory requirements regarding a regular faculty and curriculum and a regularly organized body of pupils or students. Accordingly, it is held that the tax on admissions imposed by section 1700(a) of the Code, applies to charges for admission to performances by a "little theater" organization, the proceeds of which inure to its benefit.

REGULATIONS 43, SECTION 101.15: Exemptions from tax. Rev. Rul. 127

INTERNAL REVENUE CODE

Organizations of the type commonly supported by community chests which are engaged in character building, citizenship training, combating juvenile delinquency, and like programs, are performing a charitable function within the meaning of paragraph (iii) of sections 1701(a)(1)(A) of the Internal Revenue Code. Such organizations, exempt under section 101(6) of the Code, which are primarily supported by contributions from the general public, are entitled to exemption from admissions tax under section 1701(a)(1)(A)(iii) of the Code with respect to any admissions the proceeds of which inure to their benefit.

Advice is requested whether organizations of the type commonly supported by community chests which are engaged in character building and citizenship training of young people as a service to the community are exempt under section 1701(a)(1)(A) of the Internal Revenue Code from the tax on admissions.

Section 1701 of the Code provides in part as follows:

SEC. 1701. EXEMPTIONS FROM TAX.

No tax shall be levied * * * in respect of—

(a) CERTAIN RELIGIOUS, EDUCATIONAL, OR CHARITABLE ENTERTAINMENTS, ETC.—

(1) IN GENERAL.—* * * any admissions all the proceeds of which inure—

(A) exclusively to the benefit of—

* * * * * * *

(ii) an educational institution which is exempt under section 101(6) or which is an educational institution of a government or political subdivision thereof, if such organization normally maintains a regular faculty and curriculum and normally has a regularly organized body of pupils or students in attendance at the place where its educational activities are regularly carried on;

(iii) a corporation or any community chest, fund, or foundation organized and operated exclusively for charitable purposes, exempt under section 101(6), if such corporation or organization is supported, in whole or in part, by funds contributed by the United States or any State or political subdivision thereof, or is primarily supported by contributions from the general public; * * *

(2) NONEXEMPT ADMISSIONS.—The exemption provided under paragraph (1) shall not apply in the case of admissions to (A) any athletic game or exhibition unless the proceeds inure exclusively to the benefit of an elementary or secondary school or unless in the case of an athletic game between two elementary or secondary schools, the entire gross proceeds from such game inure to the benefit of a hospital for crippled children, (B) wrestling matches, prize fights, or boxing, sparring, or other pugilistic matches or exhibitions, (C) carnivals, rodeos, or circuses in which any professional performer or operator participates for compensation, or (D) any motion picture exhibition.

Section 101.15(b)(4) of Regulations 43, as amended by Treasury Decision 6007, C. B. 1953–1, 412, at page 418, provides that admissions, or excess charges all the proceeds of which inure exclusively to the benefit of a corporation or any community chest, fund or foundation organized and operated exclusively for charitable purposes are exempt from admissions tax where such corporation or organization is (1) exempt from Federal income tax under section 101(6) of the Code, and (2) supported, in whole or in part, by funds contributed by the United States or any State or political subdivision thereof, or (3) primarily supported by contributions from the general public. Such exemption applies only if no part of the net earnings of the organization inures to the benefit of any private stockholder or individual. Charitable organizations supported by contributions received from the general public, in order to show that they are primarily supported in such manner, must establish that more than 50 percent of all the income received by the organization, is derived from that source. Amounts paid for admissions are not regarded as "contributions" for purposes of this exemption.

It is held that organizations of the type commonly supported by community chests which are engaged in character building, citizenship training, combating juvenile delinquency, and like programs, are performing a charitable function within the meaning of paragraph (iii) of section 1701(a)(1)(A) of the Internal Revenue Code. Such organizations, exempt under section 101(6) of the Code, which are primarily supported by contributions from the general public, are entitled to exemption under section 1701(a)(1)(A)(iii) of the Code from the admissions tax with respect to any admissions the proceeds of which inure to their benefit. However, the fact that an organization may qualify as charitable will not preclude it from recourse to paragraph (ii) of section 1701(a)(1)(A) of the Code if it qualifies under the latter paragraph.

REGULATIONS 43, SECTION 101.15: Exemptions from tax. Rev. Rul. 136

INTERNAL REVENUE CODE

Nonprofit hospitals which admit and treat patients on a charity basis are considered to be organized and operated exclusively for charitable purposes within the meaning of section 1701(a)(1)(A)(iii) of the Internal Revenue Code. Such hospitals must receive more than 50 percent of their revenue from contributions from the general public in order to qualify for the exemption from the tax on admissions.

Hospitals operated and maintained by the United States, a State, or a political subdivision thereof, being public welfare institutions, are charitable institutions within the meaning of section 1701(a)(1)(A)(iii) of the Code. Private hospitals, otherwise qualified, which are supported to any degree by contributions from the United States, a State, or a political subdivision thereof, are likewise entitled to the exemption.

Advice is requested relative to the means of determining whether a hospital qualifies as a charitable organization for purposes of the exemption from the tax on admissions provided by section 1701(a)(1)(A)(iii) of the Internal Revenue Code.

Section 1701 of the Code provides in part as follows:

SEC. 1701. EXEMPTIONS FROM TAX.

No tax shall be levied * * * in respect of—

(a) CERTAIN RELIGIOUS, EDUCATIONAL, OR CHARITABLE ENTERTAINMENTS, ETC.—

(1) IN GENERAL.—* * * any admissions all the proceeds of which inure—

(A) exclusively to the benefit of—

* * * * * * *

(iii) a corporation or any community chest, fund, or foundation organized and operated exclusively for charitable purposes, exempt under section 101(6), if such corporation or organization is supported, in whole or in part, by funds contributed by the United States or any State or political subdivision thereof, or is primarily supported by contributions from the general public; * * *

It is held that in order for a nonprofit hospital, not operated or supported by the United States, a State, or political subdivision thereof, to qualify as an organization operated exclusively for charitable purposes within the meaning of section 1701(a)(1)(A)(iii) of the Code, it is necessary only to establish that patients who cannot pay for hospital care are admitted and treated on a charity basis. However, in order to qualify for the exemption with respect to the tax on admissions, such hospital must be primarily supported by contributions from the general public, that is, it must receive more than 50 percent of its revenue from such source. In making such determination, direct gifts from individuals or corporations, legacies, bequests, endowments, etc., and any income therefrom, and allocations from community chests, or similar funds arising from solicited public contributions, are considered to be contributions from the general public. Legacies, bequests, endowments, etc., which are added to the permanent fund of a hospital, are considered contributions from the general public for the year in which received. After that time, only the income from such legacies, bequests, and endowments may be considered as contributions from the general public. Revenue received from pay patients is considered as earned income in determining the amount of support from contributions from the general public.

It is also held that hospitals operated and maintained by the United States, a State, or political subdivision thereof, as public welfare institutions, are, *per se*, charitable institutions and are entitled to the benefits of the exemption, even though patients who can afford to pay are required to reimburse such institutions for the cost of treatment. In this connection, a privately operated nonprofit hospital, which qualifies as a charitable institution and which is supported to any degree by contributions from the United States, a State, or political subdivision thereof, is likewise entitled to the benefit of the exemption.

REGULATIONS 43, SECTION 101.15: Exemptions from tax. Rev. Rul. 161

INTERNAL REVENUE CODE

The exemption provided by section 1701(b) of the Internal Revenue Code with respect to admissions to agricultural fairs applies to a separate charge, made in addition to the general admission charge, for admission to grandstand events which qualify in their own right as agricultural fairs, such as exhibitions of cattle or other farm animals.

Advice is requested whether the exemption provided by section 1701(b) of the Internal Revenue Code with respect to admissions to agricultural fairs applies to a charge, made in addition to the general admission charge, for admission to a grandstand.

Section 1701(b) of the Code provides in part as follows:

SEC. 1701. EXEMPTIONS FROM TAX.

No tax shall be levied * * * in respect of—

* * * * * * *

(b) AGRICULTURAL FAIRS.—Any admissions to agricultural fairs if no part of the net earnings thereof inures to the benefit of any stockholders or members of the association conducting the same—if the proceeds therefrom are used exclusively for the improvement, maintenance, and operation of such agricultural fairs; * * *

Section 101.15(d) of Regulations 43, as amended by Treasury Decision 6007, C. B. 1953-1, 412, at page 420, provides that the exemption afforded with respect to agricultural fairs is limited to the general admission charge to the fair grounds or to any additional payment for seating accommodations offered in connection with any free event held in connection with the fair. The term "agricultural fairs" includes, in general, all exhibitions of farm produce, livestock, poultry, flowers, or the like held for the promotion or advancement of agriculture, including horticulture.

It is held that the exemption provided by section 1701(b) of the Code with respect to admissions to agricultural fairs applies to a separate charge, made in addition to the general admission charge, for admission to grandstand events which qualify in their own right as agricultural fairs, such as exhibitions of cattle or other farm animals.

Where, in addition to the general admission charge a separate charge is made for grandstand events which do not qualify in their own right as agricultural fairs, such as rodeos or races, and only those persons who have paid the separate charge are permitted to view the entertainment from the grandstand, the separate charge and any other charge made for a grandstand seat under similar conditions are subject to admissions tax under section 1700(a) of the Code. However, if all persons who have paid the general admission charge are entitled to view such events without payment of an additional charge, any additional payments for seating accommodations (e. g. grandstand seats) provided in connection with the free events is considered an extension of the general admission charge to the fair and is exempt from tax under section 1701(b) of the Code.

REGULATIONS 43, SECTION 101.15: Exemptions from tax. Rev. Rul. 163

INTERNAL REVENUE CODE

Charges for admissions to a play presented by an association, the proceeds of which inure to the benefit of a university which qualifies for exemption under section 1701(a)(1)(A)(ii) of the Internal Revenue Code for use in providing a scholarship for an individual to be designated by the association, are exempt from the tax on admissions.

Advice is requested whether exemption from the admissions tax may be granted under section 1701(a)(1)(A)(ii) of the Internal

Revenue Code where the proceeds from a play inure to the benefit of a university and are specifically designated for use as a scholarship for an individual.

In the instant case, an association presents plays each year and turns over the proceeds to a university which qualifies for exemption from the tax on admissions under section 1701(a)(1)(A)(ii) of the Code. The proceeds inure to the university under an agreement that the funds will be used in providing a scholarship for an individual to be specifically designated by the association. The scholar is selected from the high school graduates of the same community.

Section 1701 of the Code provides in part as follows:

SEC. 1701. EXEMPTIONS FROM TAX.

No tax shall be levied * * * in respect of—

(a) CERTAIN RELIGIOUS, EDUCATIONAL, OR CHARITABLE ENTERTAINMENTS, ETC.

(1) IN GENERAL—* * * any admissions all the proceeds of which inure—

(A) exclusively to the benefit of—

* * * * * * *

(ii) an educational institution which is exempt under section 101(6) or which is an educational institution of a government or political subdivision thereof, if such organization normally maintains a regular faculty and curriculum and normally has a regularly organized body of pupils or students in attendance at the place where its educational activities are regularly carried on:

* * * * * * *

if no part of the net earnings thereof inures to the benefit of any private stockholder or individual; * * *

It is held that charges for admissions to a play presented by an association, the proceeds of which inure directly to a university which qualifies for exemption under section 1701(a)(1)(A)(ii) of the Code, are exempt from the tax on admissions imposed by section 1700(a) of the Code, even though the funds are used by the university in providing a scholarship for an individual to be designated by the association.

REGULATIONS 43, SECTION 101.15: Exemptions from tax. Rev. Rul. 164

INTERNAL REVENUE CODE

A historic museum which is not maintained in connection with a historic site, house, or shrine, does not qualify for exemption under section 1701(e)(2) of the Internal Revenue Code.

Advice is requested whether a nonprofit society is entitled to exemption from the tax on admissions under section 1701(e)(2) of the Internal Revenue Code with respect to charges for admission to a museum which it maintains.

In the instant case, the society was organized for the purpose of creating and fostering an interest in the history of the territory surrounding it; to maintain a marine museum which also contains household arts and crafts; to collect and provide for the proper custody of marine and historical documents and relics; and to take and hold historic sites and to provide proper care thereof.

Section 101.15(d)(5) of Regulations 43, as amended by Treasury Decision 6007, C. B. 1953-1, 412, at page 421, provides that admissions to historic sites, houses, and shrines, and museums conducted in con-

nection therewith, maintained and operated by a society or organization devoted to the preservation and maintenance of such historic sites, houses, shrines, and museums are exempt from tax, if no part of the net earnings thereof inures to the benefit of any private stockholder or individual. This exemption applies regardless of the disposition made of the proceeds from the admissions. Historic museums not maintained in connection with historic sites, houses, or shrines are not entitled to exemption with respect to admissions thereto.

Whether or not an organization conducts a museum in connection with a historic site, house, or shrine is a question of fact to be established by substantiating evidence. In the instant case, the evidence submitted fails to establish the existence of that fact. Accordingly, it is held that such museum is not entitled to exemption under section 1701(e)(2) of the Code, and charges for admission thereto are subject to the tax on admissions imposed by section 1700(a) of the Code.

REGULATIONS 43, SECTION 101.15: Exemptions from tax. Rev. Rul. 245

INTERNAL REVENUE CODE

A ballet company operated as a nonprofit organization for the purpose of educating talented persons of the area in the art of dancing is considered to be a civic or community membership association within the meaning of section 1701(c) of the Internal Revenue Code, and the ballet performances conducted by such an organization are included within the term "concerts" as used in that section.

Advice is requested whether a ballet company under the following circumstances constitutes a civic or community membership association within the meaning of section 1701(c) of the Internal Revenue Code, and whether it is entitled to the exemption from tax on admissions to performances which it conducts.

The ballet company, a nonprofit organization, was designed for the purpose of furthering the artistic standards and education of talented youth in the area in the art of dancing. It was incorporated under the laws of the State in which it operates and is directed by its officers and executive committee. Membership in the ballet is awarded to those passing a written examination and a live test of dancing ability. At the end of the season a performance is given by the members of the ballet for the public of the area. The dancers, dancing directors, and the supporting organization give their services without compensation. Financial support is derived from gifts from patrons and from membership dues.

Section 1701(c) of the Code provides that no tax is due with respect to payments for admission to concerts conducted by a civic or community association operating under a constitution, bylaws, or other rules or regulations providing for a definite class of membership, if no part of the net earnings inures to the benefit of any member or stockholder.

It is held that the instant organization is a type of civic or community association contemplated by section 1701(c) of the Code. It is further held that ballet performances presented by civic or community membership associations may be included within the term "concerts" as used in that section. Accordingly, if no part of the net

earnings inures to the benefit of any member the proceeds from ballet performances conducted by the ballet company are exempt from the tax on admissions imposed by section 1700(a)(1) of the Code.

REGULATIONS 43, SECTION 101.15: Exemptions from tax. Rev. Rul. 246

INTERNAL REVENUE CODE

The exemption from tax on admissions to concerts conducted by a civic or community membership association provided by section 1701(c) of the Internal Revenue Code applies with respect to concerts given by such an association even though it is not engaged solely in musical pursuits. However, where a single charge covers admission to a series of concerts and to a number of other performances not qualifying as concerts the exemption provided by that section applies only with respect to that part of the admission allocable to the concerts. The term "concerts" includes ballet and dance performances presented by a civic or community membership association. (See Rev. Rul. 245, p. 337, this Bulletin.)

REGULATIONS 43, SECTION 101.15: Exemptions from tax. Rev. Rul. 262

INTERNAL REVENUE CODE

A contribution from the United States for the purpose of aiding in the construction of a privately operated nonprofit hospital constitutes funds for the support of the hospital within the meaning of section 1701(a)(1)(A)(iii) of the Internal Revenue Code for the year in which the contribution is made. Amounts paid by a State or political subdivision thereof for the care of indigent patients in a privately operated nonprofit hospital likewise constitute contributions toward the support of the hospital within the meaning of section 1701(a)(1)(A)(iii) of the Code.

Advice is requested whether a contribution from the United States for the purpose of aiding in the construction of a privately operated nonprofit hospital or amounts paid by a State or political subdivision thereof for the care of indigent patients in such a hospital constitute contributions toward the support of the hospital within the meaning of section 1701(a)(1)(A)(iii) of the Code.

Section 1701 of the Code provides in part as follows:

SEC. 1701. EXEMPTIONS FROM TAX.

No tax shall be levied * * * in respect of—

(a) CERTAIN RELIGIOUS, EDUCATIONAL, OR CHARITABLE ENTERTAINMENTS, ETC.—

(1) IN GENERAL.—* * * any admissions all the proceeds of which inure—

(A) exclusively to the benefit of—

* * * * * * *

(iii) a corporation or any community chest, fund, or foundation organized and operated exclusively for charitable purposes, exempt under section 101(6), if such corporation or organization is supported, in whole or in part, by funds contributed by the United States or any State or political subdivision thereof, or is primarily supported by contributions from the general public; * * *

A privately operated nonprofit hospital exempt under section 101(6) of the Code qualifies as a corporation, fund, or foundation organized

and operated "exclusively for charitable purposes" within the meaning of section 1701(a)(1)(A)(iii) of the Code if it establishes that patients who cannot pay for hospital care are admitted and treated on a charity basis. However, in order to qualify for the exemption with respect to the tax on admissions, such hospital must further establish that it is supported in part by contributions from the United States, a State, or political subdivision thereof, or that it is primarily supported by contributions from the general public. *Cf.* Rev. Rul. 136, page 333, this Bulletin.

It is held that a contribution made by the United States for the purpose of aiding in the construction of a privately operated nonprofit hospital, which qualifies as a charitable institution, constitutes funds for the support of the hospital within the meaning of section 1701(a)(1)(A)(iii) of the Code and the hospital is entitled to the exemption provided by that section for the year in which the contribution is made.

It is further held that amounts paid by a State or political subdivision thereof for the care of indigent patients in a privately operated nonprofit hospital, which qualifies as a charitable institution, constitute contributions toward the support of the hospital and entitle it to the exemption provided by section 1701(a)(1)(A)(iii) of the Code.

REGULATIONS 43, SECTION 101.15: Exemptions from tax. Rev. Rul. 263

INTERNAL REVENUE CODE

Charges for admission to a performance consisting of a motion picture and a lecture, the proceeds of which inure to an educational institution, are not exempt from the admissions tax imposed by section 1700(a) of the Internal Revenue Code.

Advice is requested whether charges for admission to a performance consisting of a motion picture and a lecture, the proceeds of which inure to an educational institution, are exempt from the admissions tax imposed under section 1700(a) of the Internal Revenue Code.

In the instant case, a lecture was given which was illustrated by motion pictures. The proceeds from the lecture inured to a scholarship fund of an educational institution which qualifies for exemption under section 1701(a)(1)(A)(ii) of the Code. The pictures, illustrating the experiences of the lecturer on a world cruise, were taken by amateur photographers. An amateur operated and donated the use of the projector for showing the pictures.

Section 1701 of the Code provides in part as follows:

SEC. 1701. EXEMPTIONS FROM TAX.

No tax shall be levied * * * in respect of—

(a) CERTAIN RELIGIOUS, EDUCATIONAL, OR CHARITABLE ENTERTAINMENTS, ETC.—

(1) IN GENERAL.—

(A) exclusively to the benefit of—

* * * * * * *

(ii) an educational institution which is exempt under section 101(6) or which is an educational institution of a government or political subdivision thereof, if such organization normally maintains a regular

faculty and curriculum and normally has a regularly organized body of pupils or students in attendance at the place where its educational activities are regularly carried on;

* * * * * * *

if no part of the net earnings thereof inures to the benefit of any private stockholder or individual;

* * * * * * *

(2) NONEXEMPT ADMISSIONS.—The exemption provided under paragraph (1) shall not apply in the case of admissions to * * * (D) any motion picture exhibition.

The provision of section 1701(a)(2)(D) of the Code is mandatory and unqualified, and applies without regard to the character of the organization to which the proceeds of the admission charges inure. Since the law makes no distinction in the classification or purpose of the motion picture exhibition, educational institutions are liable for the collection and payment of the admissions tax with respect to all motion picture exhibitions sponsored by them. Accordingly, it is held that a performance consisting of a motion picture and a lecture constitutes a motion picture exhibition for the purposes of the statute and the charges for admission thereto, the proceeds of which inure to an educational institution, are subject to the admissions tax imposed by section 1700(a) of the Internal Revenue Code.

In a case where a lecture is illustrated only by the use of slides, the performance does not constitute a motion picture exhibition and the charges for admission thereto, the proceeds of which inure to an organization exempt under section 1701 of the Code, are not subject to the admissions tax.

REGULATIONS 43, SECTION 101.15: Exemptions from tax. Rev. Rul. 297

INTERNAL REVENUE CODE

Organizations of the type commonly supported by community chests which are engaged in furthering the standards of health and hygiene in a community by providing health services and instruction are performing a charitable function within the meaning of paragraph (iii) of section 1701(a)(1)(A) of the Internal Revenue Code. Such organizations, exempt under section 101(6) of the Code, which are primarily supported by contributions from the general public, are entitled to exemption from admissions tax under section 1701(a)(1)(A)(iii) of the Code with respect to any admissions the proceeds of which inure to their benefit, except as otherwise provided by section 1701(a)(2) of the Code. *Cf.* Rev. Rul. 127, page 332, this Bulletin.

REGULATIONS 43, SECTION 101.15: Exemptions from tax. Rev. Rul. 298

INTERNAL REVENUE CODE

The Civil Air Patrol is exempt from income tax under section 101(6) of the Internal Revenue Code and maintains, as a substantial part of its activities, a regular faculty and curriculum to provide aviation education and normally has a regularly organized body of students. *Held*, the Civil Air Patrol meets the requirements of section 1701(a)(1)(A)(ii) of the Code and charges for admission to an air show conducted by a squadron of the Civil Air Patrol, the pro-

ceeds of which inure to such squadron's benefit, are not subject to the tax imposed by section 1700(a) of the Code.

SUBCHAPTER B.—DUES

SECTION 1710.—TAX

REGULATIONS 43, SECTION 101.22: Meaning of dues or membership fees. Rev. Rul. 177

INTERNAL REVENUE CODE

The tax on dues and initiation fees imposed by section 1710(a) of the Internal Revenue Code applies to charges made by a beach club to its members for the use of cabins and cabanas for the summer season, where bathing and swimming privileges are obtained only by payment of such charges.

Advice is requested whether the tax on dues and initiation fees imposed by section 1710(a) of the Internal Revenue Code applies to charges made to members of a beach club for the use of cabins and cabanas for the summer season under the following circumstances.

A beach club maintains, among its facilities, cabins and cabanas for the use of its members. Dues of $25 per year are paid for family membership and $12.50 per year for single membership. The members are entitled to vote in the management of the affairs of the club, and to share pro rata in any distribution of the proceeds of the club property in the event of the sale or dissolution of the club. To obtain bathing and swimming privileges for the season, members are required to pay, in addition to dues, charges for the use of the cabins and cabanas for the summer season.

Section 1710(a)(1) of the Code imposes a tax equivalent to 20 percent of any amount paid as dues or membership fees to any social, athletic, or sporting club or organization, if the dues or fees of an active resident annual member are in excess of $10 per year. Section 1712(a) defines the term "dues" to include any charge for social privileges or facilities, or for golf, tennis, polo, swimming, or other athletic or sporting privileges or facilities for a period of more than 6 days.

It has been the policy of the Internal Revenue Service to regard a beach club, organized and operated in the manner described, as a social, athletic, or sporting club or organization within the meaning of section 1710(a)(1) of the Code. Therefore, dues and fees paid by members of such a club were subjected to the tax on dues and initiation fees imposed by section 1710(a) of the Code.

It is now held that since members obtain bathing and swimming privileges only by payment of the charges for the cabins and cabanas, such charges constitute charges for bathing and swimming privileges within the meaning of section 1712(a) of the Code, and are likewise subject to the tax on dues under section 1710(a)(1) of the Code. *Cf.* Rev. Rul. 175, page 327, in this Bulletin.

Because of the policy heretofore maintained regarding the nonapplication of the tax to charges for cabins and cabanas, under the authority of section 3791(b) of the Code the instant ruling will not be applied retroactively with respect to such charges made and paid prior to October 1, 1953, for the current season.

REGULATIONS 43, SECTION 101.24: Determination of character of club.
(Also Section 1700, Section 101.2.)

Rev. Rul. 253

INTERNAL REVENUE CODE

A private club the purposes of which include the promotion of nudism and which maintains quarters and facilities for social and recreational activities of its members, constitutes a social, athletic, or sporting club within the meaning of section 1710 of the Internal Revenue Code.

Application of the tax on dues and initiation fees imposed by section 1710 of the Code, and of the tax on admissions imposed by section 1700 of the Code, to amounts paid to the club as dues, for subleases of parcels of ground, registration fees, and daily ground fees.

Advice is requested concerning the application of the tax imposed by section 1710 of the Internal Revenue Code to dues and other charges paid by members of a private club the purposes of which include the promotion of nudism. Advice is also requested concerning the application of the tax on admissions imposed by section 1700 of the Code to amounts paid as daily ground fees.

In the instant case, an organization maintains land and facilities for a private club, the purpose of which is to provide seclusion for the exposure of the members to air and sunlight without molestation by or offense to others, and to acquaint and educate others of like mind with the benefits, both psychologically and physically, of this mode of recreation and living. The club maintains for its members outdoor facilities, which include a swimming pool, volleyball court, tennis court, and other such recreational facilities. The club also maintains on the premises a clubhouse, dining hall, and private and rental cabins. The clubhouse is used in the evening for dancing, reading, and other forms of indoor recreation.

The club has three classes of membership, designated as A, B, and C. All members are required to pay dues of $10 per year. Class A members are required to maintain a sublease on a parcel of ground within the organization's premises for which they pay an annual charge of $80. Those accepted as class A members after a specified date must pay an additional registration fee of $50. Class B members are also required to maintain a sublease on a parcel of ground. Class C members are only required to pay daily ground fees at $1.50 per family in addition to the yearly dues. Guests of any of the members are required to pay daily ground fees of $1.50 per family. The class A and B members have voting privileges and, in the event of the sale of the assets of the club, they will receive their proportionate shares of the proceeds from the sale.

Section 1710(a)(1) of the Code imposes a tax equivalent to 20 percent of any amount paid as dues or membership fees to any social, athletic, or sporting club or organization, if the dues or fees of an active resident annual member are in excess of $10 per year. Section 1710(a)(2) of the Code imposes a tax equivalent to 20 percent of any amount paid as initiation fees to such a club or organization, if such fees amount to more than $10, or if the dues or membership fees, not including initiation fees, of an active resident annual member are in excess of $10 per year. The purposes and activities of a club or organization determine its character for the purposes of the tax.

It has been the policy for the Internal Revenue Service not to regard a club, the purposes of which include the promotion of nudism, as a social, athletic, or sporting club within the meaning of section 1710 of the Code. Upon reconsideration it is now held that a club operated in the manner and for the purpose described above constitutes a social, athletic, or sporting club or organization within the meaning of section 1710 of the Code.

Section 1712(a) of the Code provides that the term "dues" includes any assessment, irrespective of the purpose for which made, and any charge for social privileges or facilities, for any period of more than 6 days. It is held that since the annual payment for a sublease on a parcel of ground within the organization's premises is a condition necessary for continuance of membership within the club for class A and B members, such payment constitutes an additional payment of dues within the meaning of that section of the Code. Accordingly, since the total of the annual dues and the amounts paid under the sublease agreement by such members is in excess of $10 per year, the amounts paid as dues by all members of the club, including the amounts paid for sublease agreements, are subject to the tax.

Section 1712(b) of the Code provides that the term "initiation fees" includes any payment, contribution, or loan, required as a condition precedent to membership. Since class A members accepted for membership after a specified date are required to pay an additional registration fee of $50, it is held that such payment constitutes an initiation fee within the meaning of that section of the Code and as such is subject to the tax.

Where daily ground fees are paid for a period of more than 6 consecutive days by class C members, such fees constitute dues within the meaning of section 1712(b) of the Code and are subject to the tax. However, where such daily ground fees are paid for a period of six or less consecutive days they do not constitute amounts paid as dues, but are taxable as amounts paid for admission within the meaning of section 1700(a)(1) of the Code. The tax on admissions also applies to daily ground fees paid by guests of the club.

Because of the policy heretofore maintained, the instant ruling, under the authority of section 3791(b) of the Code, will not be applied retroactively; however, it will become effective as of December 1, 1953.

REGULATIONS 43, SECTION 101.28: Initiation fees. Rev. Rul. 137

INTERNAL REVENUE CODE

A transfer fee required by a country club with respect to the sale of stock by a member withdrawing from the club is not a condition precedent to membership and the amount of such transfer fee is not subject to the tax on initiation fees imposed by section 1710(a)(2) of the Internal Revenue Code.

Advice is requested whether the tax on initiation fees imposed by section 1710(a)(2) of the Internal Revenue Code is applicable to a transfer fee paid by a withdrawing member of a country club.

Section 1710 of the Code imposes a tax on any amount paid as initiation fees to any social, athletic, or sporting club or organization, if such fees amount to more than $10, or if the dues or membership

fees, not including initiation fees, of an active resident annual member are in excess of $10 per year.

Under the Internal Revenue Code, the term "initiation fees" includes any payment, contribution, or loan, required as a condition precedent to membership, whether or not such payment, contribution or loan is evidenced by a certificate of interest or indebtedness, or share of stock, and irrespective of the person or organization to whom paid, contributed, or loaned. (Sec. 101.28 of Regulations 43.)

In view of the foregoing. it is held that a transfer fee required by a country club with respect to the sale of stock by a member withdrawing from the club is not a condition precedent to membership in the club and the amount of such transfer fee is not subject to the tax on initiation fees imposed by section 1710(a)(2) of the Internal Revenue Code.

Regulations 43, Section 101.28: Initiation fees. Rev. Rul. 281

INTERNAL REVENUE CODE

A country club which qualifies as a social, athletic, or sporting club within the meaning of section 1710 of the Internal Revenue Code has four classes of memberships. The members may enjoy the facilities of the club according to the particular class of membership held. Only those members who have purchased a share of stock or a certificate of interest may vote in the management and control of the club and share in its assets. *Held*, those members who are entitled to vote in the management and control of the club and share in its assets comprise an additional or separate class of membership, regardless of whether specified as such, and any amount paid for a share of stock or a certificate of interest constitutes an amount paid as a condition precedent to membership of that class and is subject to the tax on initiation fees imposed by section 1710(a)(2) of the Code. See S. T. 387, C. B. I-2(1922), 291.

SUBCHAPTER C.—PROVISIONS COMMON TO ADMISSIONS AND DUES

SECTION 1715.—PAYMENT OF TAX

Regulations 43, Section 101.31: Duty to collect, return, and pay tax. Rev. Rul. 202

INTERNAL REVENUE CODE

A certificate of exemption from admissions tax was issued to an organization which qualified therefor under section 1701(a)(1)(A) of the Internal Revenue Code. However, prior to the issuance of the certificate, tickets to an affair conducted by the organization were printed which showed the charge for admission and an additional amount identified as admissions tax. Such tickets were sold for the total charges shown thereon, and the amounts charged as tax were retained by the organization. *Held*, the Government has no right to the amount collected by the organization as admissions tax, and has no authority to authorize the organization to retain the money which it collected as tax against proper claims of the persons who paid it.

Where an amount has been improperly collected as admissions tax and is turned over to the Government, such tax may be refunded only to the persons who actually paid it, or to their duly authorized agents.

CHAPTER 11.—DOCUMENTS, OTHER INSTRUMENTS, AND PLAYING CARDS [INCLUDING STAMP TAXES]

SUBCHAPTER A.—RATE AND PAYMENT OF TAX

SECTION 1801.—CORPORATE SECURITIES

REGULATIONS 71, SECTION 113.50: Scope of tax. Rev. Rul. 203

INTERNAL REVENUE CODE

Applicability of the tax imposed by sections 1800 and 1801 of the Internal Revenue Code on the issuance of corporate securities to the issuance of short-term notes.

Advice is requested whether the following described short-term notes are debentures within the meaning of sections 1800 and 1801 of the Internal Revenue Code.

M Corporation, which is engaged in the finance and loan business, obtains a substantial portion of its working capital by the issuance of short-term notes. The notes are issued at a discount and contain a simple promise to pay a certain sum of money at maturity, which ranges from 30 days to 9 months from date of issue. They do not contain, and are not issued pursuant to, any collateral agreement with the lender that places restrictions upon, or imposes duties upon the M Corporation, other than the obligation to pay at maturity. The corporation uses two forms of notes which are both in the usual form of ordinary promissory notes, except that their appearance is formalized by printing them on tinted paper with engraved borders. On one form the principal amount and the name of the payee are left blank and are filled in upon issuance. The other form is made payable to bearer and the principal amount is printed thereon in denominations ranging from $1,000 to $1,000,000. Under the regulations of the Board of Governors of the Federal Reserve System, short-term notes of finance companies, which category includes the M Corporation, are eligible for rediscount where the maturity at the time of rediscount is not more than 90 days away.

Sections 1800 and 1801 of the Code impose a tax on all bonds, debentures, or certificates of indebtedness issued by any corporation, and all instruments, however termed, issued by any corporation, with interest coupons or in registered form, known generally as corporate securities. From the history of sections 1800 and 1801, which derive from the Revenue Act of 1898, it is evident that these sections do not apply to ordinary promissory notes.

Both debentures and promissory notes are evidences of indebtedness, and therefore have certain common characteristics with respect to terms and provisions. Each contains a promise to pay a certain sum of money at a future date. Usually in each there is a statement of a

fixed amount of interest to be paid periodically, although promissory notes are frequently issued at a discount with no interest. On the other hand, there are certain characteristics which are common to debentures as a class, which are not common to promissory notes, and which serve to distinguish the one from the other. In the application of sections 1800 and 1801 of the Code it is the position of the Service that the two most important distinguishing characteristics are: (1) debentures are issued for relatively long-terms, whereas promissory notes are issued for relatively short-terms; and (2) debentures usually contain provisions designed to afford the lender security for his loan, and frequently give the lender some element of control over the borrower's business activities while the debentures are outstanding, whereas such provisions are unusual in promissory notes.

In *General Motors Acceptance Corporation* v. *Higgins*, 161 Fed. (2d) 593, Ct. D. 1708, C. B. 1948-2, 157, certiorari denied, 332 U. S. 810, it was held that certain instruments termed "notes" issued for a term of 4½ to 5 years were "debentures" within the meaning of sections 1800 and 1801. Such notes were subject to provisions which restricted the financial activities of the borrower in such a way as to afford the lender security for his loan. (Also see *Commercial Credit Co.* v. *Hofferbert*, 93 Fed. Supp. 562, affirmed, 188 Fed. (2d) 574.) The instant notes, on the other hand, are short-term notes which contain a simple promise to pay and the issuer is subject to no further duties or restrictions.

It is held that the short-term notes issued by M Corporation under the circumstances outlined above do not constitute debentures within the meaning of section 1801 of the Code. Accordingly, the issuance of such notes is not subject to tax under section 1800 of the Code.

CHAPTER 15.—TOBACCO, SNUFF, CIGARS, AND CIGARETTES

SECTIONS 2000-2199.—TOBACCO, SNUFF, CIGARS, AND CIGARETTES

REGULATIONS 8, SECTION 140.212: Shipments restricted. T. D. 6052

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER C, PART 140.—TAXES ON TOBACCO, SNUFF, CIGARS, AND CIGARETTES, AND PURCHASE AND SALE OF LEAF TOBACCO

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER E, PART 450.—WITHDRAWAL OF FILLED CHEESE, PLAYING CARDS, TOBACCO, SNUFF, CIGARS, AND CIGARETTES, FROM FACTORIES, FREE OF TAX, FOR USE OF THE UNITED STATES

Shipments of tax-free tobacco products, also cigarette papers and tubes, for use of the United States.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

On July 1, 1953, notice of proposed rulemaking, relating to the removal tax-free of manufactured tobacco, snuff, cigars, cigarettes,

and cigarette papers and tubes, from domestic factories for use of the United States, was published in the Federal Register (18 F. R. 3758). No comments having been received in regard to the rules proposed, the regulations set forth below are hereby adopted.

PARAGRAPH 1. Regulations 8 [26 CFR, pt. 140], but only as prescribed and made applicable to the Internal Revenue Code by Treasury Decision 4885 [C. B. 1939–1 (Part 1), 396], approved February 11, 1939, are amended by renumbering section 140.215 (art. 215), as last renumbered by Treasury Decision 5868 (16 F. R. 11998) [C. B. 1951–2, 275], as section 140.225 (art. 225).

PAR. 2. Regulations 8 [26 CFR, pt. 140] are further amended by adding, immediately following section 140.211, a new subpart P, Tax-Free Shipment of Tobacco, Snuff, Cigars, Cigarettes, and Cigarette Papers and Tubes For Use of United States, as follows:

SUBPART P—TAX-FREE SHIPMENT OF TOBACCO, SNUFF, CIGARS, CIGARETTES, AND CIGARETTE PAPERS AND TUBES, FOR USE OF UNITED STATES.

SEC. 3331, INTERNAL REVENUE CODE, EXEMPTION FROM TAX OF DOMESTIC GOODS PURCHASED FOR THE UNITED STATES.

The privilege existing by provision of law on December 1, 1873 or thereafter of purchasing supplies of goods imported from foreign countries for use of the United States, duty free, shall be extended, under such regulations as the Secretary may prescribe, to all articles of domestic production which are subject to tax by the provisions of this subtitle.

SEC. 140.212. SHIPMENTS RESTRICTED.—Manufacturers of tobacco, snuff, cigars, cigarettes, and cigarette papers and tubes, may ship such articles tax-free from their factories, in accordance with this subpart, to Federal agencies and institutions for gratuitous distribution. Shipments of such articles for sale by Federal agencies or institutions are not within the meaning of the law authorizing the purchase of articles tax-free for use of the United States. Institutions owned or controlled by the Governments of the several States, Territories, or the District of Columbia, are not entitled to receive such articles tax-free.

SEC. 140.213. FEDERAL REQUISITION.—Whenever manufactured tobacco, snuff, cigars, cigarettes, and cigarette papers or tubes, are purchased by a Federal agency or institution for the use of the United States, and it is proposed to ship such articles from the place of manufacture, tax-free, the agency or institution desiring the product shall prepare a requisition on Form 7996, in quadruplicate. All of the information called for by the headings of the various columns and lines on the form and the instructions printed thereon or issued in respect thereto, and as required by this subpart, shall be furnished. Each of the four copies of the form must agree in every respect, and shall be signed and approved by the head of the agency or institution or by a person duly authorized to sign and approve for such officer. The agency or institution shall retain one copy of the form and transmit the remaining three copies to the manufacturer concerned at the time of placing its order for the merchandise. Immediately after removal of the shipment from the factory, the manufacturer shall forward two copies of the requisition, Form 7996, with two copies of the notice of shipment, Form 7997, as required in this subpart, to the assistant regional commissioner for the region in which the factory is located. The remaining copy of the Form 7996 shall be retained by the manufacturer at the factory from which the shipment is made, with a copy of the Form 7997, for his records and for inspection, upon demand, by any internal revenue officer.

BOND

SEC. 140.214. MANUFACTURER OF TOBACCO PRODUCTS.—A shipment of tax-free tobacco, snuff, cigars, or cigarettes, made by a manufacturer of such articles under this subpart, shall be charged against the bond, Form 40 or Form 71, furnished by the manufacturer to cover the operation of his factory from which the shipment is removed.

SEC. 140.215. MANUFACTURER OF CIGARETTE PAPERS AND TUBES.—A manufacturer of cigarette papers and tubes desiring to remove cigarette papers in packages, books, or sets, of more than 25 papers each, and any cigarette tubes, from his factory, tax-free, under this subpart, shall furnish to the assistant regional commissioner for the region in which his factory is located, a bond on Form 7999, with acceptable corporate surety, or at least two individual sureties, or collateral, as required by this part. Bond, Form 7999, shall be prepared and executed, in triplicate, in accordance with this subpart, as supplemented by the instructions printed on the form, or issued in respect thereto. If given with individual sureties, the manufacturer shall furnish from each such individual surety an affidavit on Form 33, in triplicate, to show his qualification to act as such surety, a copy of which affidavit shall be attached to each copy of the related bond when filed by the manufacturer. A separate bond shall be furnished for each such factory from which tax-free removals under this subpart are to be made.

(a) *Penal sum.*—The bond must be in a penal sum sufficient to cover the estimated amount of tax which may at any time constitute a charge against the bond: *Provided*, That the penal sum of the bond furnished under this section shall not exceed $25,000 nor be less than $500. The bond shall be a continuing one, and the liability thereof subject to increase as successive withdrawals are made thereunder, and to decrease as evidence of delivery, as required by this subpart, is received by the assistant regional commissioner. When the limit of liability under a bond given in less than the maximum penal sum has been reached, no further shipments may be made under such bond, until an additional or strengthening bond, with the same surety as that on the original bond, or a new or superseding bond, has been filed to cover further shipments of such articles from the factory.

(b) *Action on the bond.*—The assistant regional commissioner shall, if the bond meets with his approval, make endorsement to that effect on all three copies. He shall retain one copy, forward one copy promptly to the Commissioner of Internal Revenue, and transmit the remaining copy to the manufacturer as notice of approval of the bond and authority to make tax-free shipments of the articles covered by the bond. The copy of the bond, together with copies of any Forms 33 or any other documents returned to him in connection therewith, shall be retained by the manufacturer at the factory from which such tax-free shipments are to be made, for his records and for inspection, upon demand, by any internal revenue officer.

NOTICE OF SHIPMENT FROM FACTORY

SEC. 140.216. NOTICE OF SHIPMENT.—For each shipment of tax-free tobacco products or cigarette papers or tubes removed from his factory under this subpart, the manufacturer shall prepare a notice of shipment on Form 7997, in triplicate. All of the information called for by the headings of the various columns and lines on the form and the instructions printed thereon or issued in respect thereto, and as required by this subpart, shall be furnished. The manufacturer shall assign to each notice of shipment a serial number, which shall begin with No. 1 with respect to the first shipment made under this subpart and begin again with No. 1 with respect to the first shipment made on January 1 of each year thereafter, which serial number shall be the same on all three copies of the notice. Immediately after removal of the shipment from the factory, the manufacturer shall forward two copies of the notice of shipment, Form 7997, with two copies of the requisition, Form 7996, as required in this subpart, to the assistant regional commissioner for the region in which the factory is located. The remaining copy of the Form 7997 shall be retained by the manufacturer at the factory from which the shipment is made, with a copy of the Form 7996, for his records and for inspection, upon demand, by any internal revenue officer.

PACKING AND LABELING

SEC. 140.217. TOBACCO PRODUCTS.—Manufactured tobacco, snuff, cigars, and cigarettes shipped from a factory under this subpart, must be put up in packages of the same sizes prescribed by law for such articles removed taxpaid for domestic sale or consumption. Each package must show either the name of the manufacturer or the identity of his factory by number and State, which may appear in the form of the caution notice and/or factory brand required to be

affixed to each package removed from the factory for taxable purposes. There shall be affixed to each package a label or sticker, clearly distinguishable from an internal revenue stamp, on which shall be printed in legible letters the words "Free of Tax—Use of U. S. NOT to be Sold". Printing of any additional words, inscription, or legend on such label may be permitted, when approved by the assistant regional commissioner for the region in which the factory is located.

SEC. 140.218. CIGARETTE PAPERS AND TUBES.—When cigarette papers and tubes are shipped by a manufacturer under this subpart, such articles may be put up in packages, books, or sets of any sizes desired. Packages, books, or sets containing more than 25 cigarette papers each, and all packages of cigarette paper tubes, must bear the name and address of the manufacturer and a label or sticker, clearly distinguishable from an internal revenue stamp, on which shall be printed in legible letters the words "Free of Tax—Use of U. S. NOT to be Sold". Printing of any additional words, inscription, or legend on such label may be permitted, when approved by the assistant regional commissioner for the region in which the factory is located.

ENTRIES IN MANUFACTURER'S RECORDS

SEC. 140.219. MANUFACTURER OF TOBACCO PRODUCTS.—Entry of each shipment of tax-free tobacco, snuff, cigars, or cigarettes, actually removed from his factory under this subpart shall be made by the manufacturer in the proper column in the prescribed revenue book, Form 73, Part 1 or 2, or Form 74, as the case may be. Such shipment shall also be included in the revenue book in the recapitulation or account of manufactured tobacco and snuff, or cigars or cigarettes, for the month in which the shipment was removed.

SEC. 140.220. MANUFACTURER OF CIGARETTE PAPERS AND TUBES.—Appropriate entry of each shipment of cigarette papers and tubes actually removed from his factory under this subpart shall be made by the manufacturer in the revenue book required to be kept by him. Such entry shall carry a notation "For use of U. S.". With respect to the manufacturer's return, Form 734, cigarette papers so shipped shall be reported in the appropriate column, under cigarette papers removed, with the notation "For use of U. S.", while cigarette tubes so shipped shall be reported on the return in the column covering tubes delivered tax-free, with a similar notation to appear through or across the columns headed "Factory No." and "District".

EVIDENCE OF DELIVERY REQUIRED

SEC. 140.221. CERTIFICATE OF RECEIPT.—The officer responsible for receiving a shipment of tax-free tobacco products, or cigarette papers and tubes, delivered to a Federal agency or institution, for use of the United States, shall, upon receipt of the shipment, inspect it in order that he may certify as to the quantity and class of product actually received and date of receipt. Such certificate shall be executed on Form 7998, to be prepared in triplicate. All of the information called for by the headings of the various columns and lines on the form and the instructions printed thereon or issued in respect thereto, and as required by this subpart, shall be furnished. The receiving officer shall retain one copy of such certificate and transmit the other two copies promptly to the manufacturer who made the shipment. The manufacturer shall keep one copy of the certificate, Form 7998, at the factory from which the shipment was removed, for his records and for inspection, upon demand, by any internal revenue officer. The other copy of the Form 7998 shall be forwarded by the manufacturer to the assistant regional commissioner for the region in which the factory is located, in order that the manufacturer may be relieved of liability to tax on the product actually received by the agency or institution. Where there is a loss of goods in transit, or there is any difference between the quantity of product withdrawn from the factory as described on the notice of shipment and that certified by the receiving officer as having been delivered to the Federal agency or institution, the manufacturer making the shipment shall be liable for the tax on such shortage or difference.

PAR. 3. Regulations 34 [26 CFR, pt. 450], but only as prescribed and made applicable to the Internal Revenue Code by Treasury De-

cision 4884 [C. B. 1939-1 (Part 1), 395], approved February 11, 1939, are amended to remove therefrom all references to tobacco, snuff, cigars, and cigarettes, as follows:

(A) The headnote of "REGULATIONS No. 34, REVISED" is amended to read as follows:

PART 450—WITHDRAWAL OF FILLED CHEESE AND PLAYING CARDS, FROM FACTORIES, FREE OF TAX, FOR USE OF THE UNITED STATES

(B) The first sentence of the preamble (26 CFR 450.0), as last amended by Treasury Decision 5818 (15 F. R. 8819) [C. B. 1950-2, 132], is further amended by striking out ", tobacco, snuff, cigars, and cigarettes" and by inserting the word "and" between the words "filled cheese" and "playing cards".

(C) The first sentence of article 2 (26 CFR 450.2), as last amended by Treasury Decision 5818 (15 F. R. 8819), is further amended by striking out "tobacco, snuff, cigars, and cigarettes,".

(D) Article 5 (26 CFR 450.5), as last amended by Treasury Decision 5818 (15 F. R. 8819), is further amended by striking out subsection (*b*) and by relettering subsection (*c*) as (*b*).

(E) The second sentence of the second paragraph of article 8(*a*) (26 CFR 450.8(a)), as last amended by Treasury Decision 5818 (15 F. R. 8819), is further amended by striking out "and tobacco manufactures".

This Treasury Decision shall be effective on the 31st day after publication in the Federal Register.

(This Treasury Decision is issued under the authority contained in sec. 3791 of the Internal Revenue Code (53 Stat. 467; 26 U. S. C. 3791).)

JUSTIN F. WINKLE,
Acting Commissioner of Internal Revenue.

Approved November 10, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Published in the Federal Register, November 17, 1953)

CHAPTER 19.—RETAILERS' EXCISE TAXES

SECTION 2400.—TAX ON JEWELRY, ETC.

REGULATIONS 51, SECTION 320.6: Charges for coverings, containers, etc., generally. (Also Section 2403, Section 320.5.) — Rev. Rul. 204

INTERNAL REVENUE CODE

A chest designed for use in holding sterling flatware, when sold in connection with the sale of the flatware, is considered a container for such articles within the meaning of section 2403(c) of the Internal Revenue Code and the 20 percent tax imposed by section 2400 of the Code attaches to the price for which the flatware is sold at

retail including the price charged for the chest. Where a chest is furnished to a purchaser in connection with the sale of the flatware and no separate charge is made for the chest, the tax applies to the total amount charged. However, no tax attaches where a chest is sold separately, at a different time, and not in connection with the sale of such flatware.

Where a retailer in connection with the sale of taxable flatware gives to the purchaser a nontaxable article, the transaction, for tax computation purposes, constitutes a sale of the taxable and nontaxable articles at a combined or lump-sum price.

Advice is requested concerning the application of the tax on jewelry, etc., imposed by section 2400 of the Internal Revenue Code to a charge made for a chest sold as a container for sterling flatware. Advice is also requested as to the basis for computing the tax where a retailer in connection with the sale of such flatware gives to the purchaser an article not subject to retailers' excise tax.

Under the provisions of section 2400 of the Code a tax of 20 percent attaches to the price for which gold, gold plated, silver, or sterling flatware are sold at retail. Section 2403(c) of the Code provides that in determining the price for which a taxable article is sold there shall be included any charge for coverings and containers of whatever nature.

It is held that a chest designed for use in holding sterling flatware, when sold in connection with the sale of the flatware, is considered a container for such taxable articles within the meaning of section 2403(c) of the Code and the tax imposed by section 2400 of the Code attaches to the price for which the sterling flatware is sold at retail including the price charged for the chest. Where a chest is furnished to a purchaser in connection with the sale of the flatware and no separate charge is made for the chest, the tax applies to the total amount charged. However, no tax attaches where a chest is sold separately, at a different time, and not in connection with the sale of such flatware.

It is further held that where a retailer in connection with the sale of taxable flatware gives to the purchaser a nontaxable article, the transaction, for tax computation purposes, constitutes a sale of the taxable and nontaxable articles at a combined or lump-sum price. In such a transaction the tax applies to the portion of the price charged for the combination which is attributable to the taxable articles. Such portion may be determined by applying to the combined price, the ratio which the established retail selling price of the taxable articles bears to the sum of the established selling prices of the taxable and nontaxable articles when sold separately at retail. If the retailer does not have established separate selling prices for the taxable and nontaxable articles the portion of the combined selling price attributable to the taxable articles may be determined by applying to the retail selling price of the combination, the ratio which the cost of the taxable articles bears to the sum of the costs of the taxable and nontaxable articles. For example, if the cost of the sterling flatware and the chest sold in connection therewith represents ¾ of the sum of the costs of the flatware, chest, and the nontaxable article, the tax should be computed on ¾ of the amount charged the purchaser for the combined articles.

REGULATIONS 51, SECTION 320.31: Jewelry. Rev. Rul. 178

INTERNAL REVENUE CODE

Barrettes or combs designed to be worn in the hair, which are ornamented with pearls, precious or semiprecious stones, or imitations thereof including rhinestones, are articles of jewelry within the meaning of section 2400 of the Internal Revenue Code and are subject to the 20 percent tax imposed by that section when sold at retail.

REGULATIONS 51, SECTION 320.32: Pearls, precious and semiprecious stones, and imitations thereof. Rev. Rul. 149

INTERNAL REVENUE CODE

Petrified wood as such is not a semiprecious stone under section 2400 of the Internal Revenue Code. However, petrified wood known as wood agate or wood opal from which gems are ordinarily cut are semiprecious stones which are subject to the tax imposed by that section of the Code, when sold at retail, regardless of whether such semiprecious stones are in the rough, cut, or polished as gems. Likewise, articles made of wood agate or wood opal from which gems are ordinarily cut are subject to the tax when sold at retail.

SECTION 2403.—RETURN AND PAYMENT OF RETAILERS' EXCISE TAXES

REGULATIONS 51, SECTION 320.5: Basis of tax on sales generally.

INTERNAL REVENUE CODE

Application of the tax where a retailer gives to a purchaser a nontaxable article in connection with the sale of a taxable article. (See Rev. Rul. 204, p. 350.)

CHAPTER 21.—COCONUT AND OTHER VEGETABLE OILS

SECTION 2474.—EXPORTATION

REGULATIONS 48, SECTION 306.14: Refund on articles exported. Rev. Rul. 191

INTERNAL REVENUE CODE

A refund of tax allowed pursuant to section 2474 of the Internal Revenue Code to an exporter of articles, consisting wholly or in chief value of coconut and other vegetable oils, is not a refund of tax erroneously, illegally, or otherwise wrongfully collected, but is considered a rebate dependent on the performance of certain acts after the liability for the tax was legally incurred and paid by the processor of

such oils. There is no authority in the law or regulations for the payment of interest on a refund made under section 2474 of the Code, to the exporter of such articles.

CHAPTER 25.—FIREARMS

SUBCHAPTER A.—PISTOLS AND REVOLVERS

SECTION 2705.—EXPORTATION

REGULATIONS 46, SECTION 316.25: Sales for exportation. Rev. Rul. 247

INTERNAL REVENUE CODE

> Claim for refund or credit may be filed by the manufacturer, or claim for refund may be filed by the exporter or shipper, with respect to manufacturers' excise tax paid on articles sold by the manufacturer for export and exported in due course. A statement furnished by a purchaser to a manufacturer setting forth the estimated number or percentage of articles purchased during a calendar month for export, based upon export orders on hand or on previous export requirements, is acceptable as evidence that such articles are sold by the manufacturer for export. No exemption from tax, nor credit or refund of tax paid, is allowable with respect to those articles exported in excess of the number or percentage purchased for export as shown by such statement for the month involved.

Advice is requested whether a claim for refund of manufacturers' excise tax paid with respect to articles sold by the manufacturer for export and exported in due course may be filed by either the manufacturer or the exporter. Advice is further requested whether a statement furnished by a purchaser to the manufacturer estimating the percentage of the articles purchased for export is acceptable as evidence that such articles were sold by the manufacturer for export.

Under the provisions of section 2705 of the Internal Revenue Code, manufacturers' excise tax does not apply with respect to articles sold or leased for export or for shipment to a possession of the United States and in due course so exported or shipped. That section also provides that the amount of any internal revenue tax erroneously or illegally collected with respect to such articles so exported or shipped may be refunded to the exporter or shipper of the articles, instead of to the manufacturer, if the manufacturer waives his right to any claim for the amount to be refunded.

Section 316.25 of Regulations 46 provides, in part, that in order for a sale for export to be exempt from tax it is necessary that two conditions be met, namely, (1) that the article be identified as having been sold by the manufacturer for export and (2) that it be exported in due course. Section 316.26 of the regulations outlines the evidence required to establish that an article is exported in due course.

A manufacturer may file a claim for refund or credit of the amount of tax paid with respect to articles sold by him for export and exported in due course. As an alternative the exporter or shipper may

file the claim for refund of the tax paid with respect to articles purchased for export and exported in due course, provided he obtains a signed statement from the manufacturer waiving any claim for the amount to be refunded and showing (1) that the manufacturer had in his possession at the time of the sale of the articles evidence that the articles were to be exported, (2) the amount of tax paid, and (3) the district directors office to which the tax was paid as well as date of payment.

It is held that where a purchaser in placing an order with a manufacturer furnishes the manufacturer a statement that an estimated number or percentage of a particular article or class of articles purchased during a calendar month is for export, such a statement, when based on export orders on hand or on previous export requirements, is acceptable as evidence that the articles covered thereby are sold by the manufacturer for export. No exemption from tax, nor credit or refund of tax paid, is allowable with respect to those articles exported in excess of the number or percentage purchased for export as shown by such statement for the month involved.

CHAPTER 26.—LIQUOR

SECTIONS 2800-3195.—LIQUOR

REGULATIONS 3, SECTION 182.64: Weighing tanks for alcohol. T. D. 6049

(Also Section 183.92, Regulations 4; Section 184.121, Regulations 5; Section 185.110, Regulations 10; Section 190.116, Regulations 15.)

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER C, PARTS 182, 183, 184, 185, AND 190

Amendment of regulations governing the quantities of spirits to be weighed in scale tanks.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

In order to authorize the use of tank scales having a capacity of more than 2,000 pounds for gauging, for the purpose of taxpayment, spirits in quantities less than 20 per centum of the total capacity of the scales, the following amendments to regulations are hereby adopted:

PARAGRAPH 1. Section 182.64 of Regulations 3 [26 CFR, pt. 182], as amended by Treasury Decision 5801 [C. B. 1950-2, 154], approved August 11, 1950, is further amended by inserting immediately after the word "*Provided*," in the last sentence, the following: "That the weighing of lesser quantities for determination of tax may be authorized by the assistant regional commissioner where the beam of the

scale is calibrated in ½ or 1 pound graduations and it is found by actual test that the scales break accurately at such graduations: *Provided further*,".

PAR. 2. Section 183.92 of Regulations 4 [26 CFR, pt. 183] is amended by inserting immediately after the word "*Provided*," in the fourth sentence, the following: "That the weighing of lesser quantities for determination of tax may be authorized by the assistant regional commissioner where the beam of the scale is calibrated in ½ or 1 pound graduations and it is found by actual test that the scales break accurately at such graduations: *Provided further*,".

PAR. 3. Section 184.121 of Regulations 5 [26 CFR, pt. 184] is amended by inserting immediately after the word "*Provided*," in the fourth sentence, the following: "That the weighing of lesser quantities for determination of tax may be authorized by the assistant regional commissioner where the beam of the scale is calibrated in ½ or 1 pound graduations and it is found by actual test that the scales break accurately at such graduations: *Provided further*,".

PAR. 4. Section 185.110 of Regulations 10 [26 CFR, pt. 185] is amended as follows:

(A) By inserting immediately after the word "*Provided*," in the last sentence, the following: "That the weighing of lesser quantities for determination of tax may be authorized by the assistant regional commissioner where the beam of the scale is calibrated in ½ or 1 pound graduations and it is found by actual test that the scales break accurately at such graduations: *Provided further*,".

(B) By amending the citation to read as follows: (53 Stat. 307, 332; 26 U. S. C. 2808, 2873.)

PAR. 5. Section 190.116 of Regulations 15 [26 CFR, pt. 190] is amended as follows:

(A) By striking the colon and the proviso following the phrase "capacity over 50,000 pounds" in the last sentence and inserting in lieu thereof a period.

(B) By adding at the end of the section a new sentence as follows: "Except in the case of scales having a capacity of 2,000 pounds or less, where spirits are to be gauged for taxpayment, not less than 20 percent of the total capacity of the gauging tank scale may be entered into the tank for gauging for determination of the tax: *Provided*, That the weighing of lesser quantities for determination of tax may be authorized by the assistant regional commissioner where the beam of the scale is calibrated in ½ or 1 pound graduations and it is found by actual test that the scales break accurately at such graduations."

(C) By amending the citation to read as follows: (53 Stat. 307, 318; 26 U. S. C. 2808, 2829.)

Because the changes made are of a liberalizing character, it is found that it is unnecessary to issue this Treasury Decision with notice and public procedure thereon under section 4(a) of the Administrative Procedure Act, approved June 11, 1946, or subject to the effective date limitations of section 4(c) of said act.

This Treasury Decision shall be effective upon the date of publication in the Federal Register.

(This Treasury Decision is issued under the authority contained in sec. 161 of the Revised Statutes and sections 2808, 3105, 3124, and 3176

of the Internal Revenue Code. (Sec. 161 R. S.; 5 U. S. C. 22; 53 Stat. 307, 358, 364, 375; 26 U. S. C. 2808, 3105, 3124, 3176).)

T. Coleman Andrews,
Commissioner of Internal Revenue.

Approved November 5, 1953.

M. B. Folsom,
Acting Secretary of the Treasury.

(Published in the Federal Register November 11, 1953)

Regulations 3, Section 182.279a: Where no bonded warehouse or denaturing plant on premises. (Also Sections 182.279b, 182.279c, 182.279d, 182.279e, 182.423.) T. D. 6048

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER C, PART 182.—INDUSTRIAL ALCOHOL

Amendment of requirements for alternate operation of industrial alcohol plant as registered distillery or fruit distillery.

Treasury Department,
Office of Commissioner of Internal Revenue,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

In order to conform Regulations 3 [26 CFR, pt. 182] with the provisions of Regulations 4 [26 CFR, pt. 183] and 5 [26 CFR, pt. 184] regarding the procedure for the alternate operation of a registered distillery or fruit distillery as an industrial alcohol plant, Regulations 3 are hereby amended as follows:

Paragraph 1. Wherever the term "supervisor" or "district supervisor" appears in the sections of the regulations revised by this Treasury Decision, such term is hereby amended to read "assistant regional commissioner."

Par. 2. Sections 182.276, 182.277, 182.278, and 182.279 are revoked.

Par. 3. There is inserted immediately following Article XV the following new subtitles, sections, and citations:

Qualifications for Initial Alternating Operations

Sec. 182.279a. Where no Bonded Warehouse or Denaturing Plant on Premises.—An industrial alcohol plant may be operated alternately for the production of alcohol under this part, the production of distilled spirits under Regulations 4 [26 CFR, pt. 183], or the production of brandy under Regulations 5 [26 CFR, pt. 184]. Where it is desired to conduct alternating operations at an industrial alcohol plant and there is no industrial alcohol bonded warehouse or denaturing plant located on the industrial alcohol plant premises, the successor (incoming) proprietor must first qualify as proprietor of the premises. At the time of the first suspension for the purpose of conducting alternate operations, the outgoing proprietor must discontinue operations and comply with the following requirements:

(*a*) *Amended application, Form 1431.*—File with the assistant regional commissioner an amended application on Form 1431, in triplicate, stating thereon

the purpose of the application to be "Temporary discontinuance in order that the industrial alcohol plant may be operated as a registered distillery" (or fruit distillery, as the case may be), and give the date of discontinuance.

(*b*) *Consent of surety.*—File with the assistant regional commissioner a blanket consent of surety, Form 1533, in triplicate, to continue in effect bond Form 1432-A (and Form 1604, if required). Such blanket consent of surety may be filed to cover all such alternate operations and may be executed in the following form:

To continue in effect the said bond (or bonds), whenever operation of the industrial alcohol plant is resumed from time to time, pursuant to application on Form 1696, filed by the principal following suspension of operations as a registered distillery or fruit distillery.

(*c*) *Materials and unfinished alcohol.*—If distilling materials are transferred to the successor, or if unfinished alcohol is to be retained in the industrial alcohol plant pending the resumption of operations as an industrial alcohol plant, comply with the requirements of sections 182.439 to 182.441. Whenever alternate operations are to be conducted after the first suspension, the procedure prescribed by sections 182.279c and 182.279d will be followed.

SEC. 182.279b. WHEN BONDED WAREHOUSE OR DENATURING PLANT ON PREMISES.—Where an industrial alcohol bonded warehouse or denaturing plant is located on the industrial alcohol plant premises, the industrial alcohol plant may be operated alternately as an industrial alcohol plant, registered distillery or a fruit distillery upon compliance with the requirements of section 182.279a. The permittee shall designate the plat on file which depicts the entire industrial alcohol plant premises, including the bonded warehouse or denaturing plant, as "plat A," and file a new plat which will be designated as "plat B," depicting the bonded warehouse or denaturing plant and any other portion of the industrial alcohol premises not to be operated by the incoming alternate proprietor. The permittee shall also describe in the amended application, Form 1431, the bonded warehouse or denaturing plant and any portion of the industrial alcohol plant premises not to be operated by the incoming proprietor. The description thereof must correspond with the depiction of the premises on plat B. Whenever alternate operations are to be conducted after the first suspension, the procedure prescribed by sections 182.279c and 182.279d will be followed.

SUSPENSION FOR SUBSEQUENT ALTERNATE OPERATIONS

SEC. 182.279c. REQUIREMENTS.—Where a permittee desires to suspend operations of the industrial alcohol plant preparatory to resumption of operations as a registered distillery or fruit distillery, he must comply with the following requirements:

(*a*) *Notice of alternate operations.*—File Form 1696, through the storekeeper-gauger in charge, with the assistant regional commissioner, giving notice of intention to suspend operations. The form shall be executed and filed in accordance with the various lines on the form and the instructions printed thereon, or issued in respect thereto. Form 1696 shall contain or be verified by a written declaration that it is executed under the penalties of perjury. Operations will be suspended upon approval of the notice by the assistant regional commissioner in accordance with section 172.279e.

(*b*) *Materials and unfinished alcohol.*—If distilling materials are transferred to the successor or if unfinished alcohol is to be retained on the premises pending the resumption of operations as an industrial alcohol plant, comply with the requirements of sections 182.439 to 182.441. (63 Stat. 667; 26 U. S. C. 3809.)

RESUMPTION FOR SUBSEQUENT ALTERNATE OPERATIONS

SEC. 182.279d. REQUIREMENTS.—When a permittee desires to resume operation of the industrial alcohol plant following suspension of operations as a registered distillery or fruit distillery, he must comply with the following requirements:

(*a*) *Notice of alternate operations.*—File Form 1696, through the storekeeper-gauger in charge, with the assistant regional commissioner for authority to resume operations. The notice shall be executed in accordance with the instruc-

tions printed on the form, or issued in respect thereto, and otherwise completed as provided in section 182.279c.

(*b*) *Materials.*—If distilling materials are received by transfer from the predecessor, comply with the requirements of sections 182.440 and 182.441. (63 Stat. 667; 26 U. S. C. 3809.)

ACTION BY ASSISTANT REGIONAL COMMISSIONER

SEC. 182.279e. APPROVAL AND DISPOSITION OF FORM 1696.—Upon receipt of Form 1696, the assistant regional commissioner will, if he finds that the notice may be property approved, execute the certificate of approval on all copies and dispose of the copies in accordance with the instructions printed on the form, or issued in respect thereto.

PAR. 4. Section 182.423 is amended by adding at the end of the second sentence the following new sentence:

Form 124 will not be required when operations are suspended pursuant to the requirements of Article XV.

Because the changes made are of a liberalizing character, it is found that it is unnecessary to issue this Treasury Decision with notice and public procedure thereon under section 4(a) of the Administrative Procedure Act, approved June 11, 1946.

This Treasury Decision shall be effective upon the date of publication in the Federal Register.

(This Treasury Decision is issued under the authority contained in secs. 3105, 3124(a)(6) and 3176 of the Internal Revenue Code (53 Stat. 358, 364, 375; 26 U. S. C. 3105, 3124(a)(6), 3176).)

JUSTIN F. WINKLE,
Acting Commissioner of Internal Revenue.

Approved November 5, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Published in the Federal Register November 11, 1953)

REGULATIONS 3, (Appendix). T. D. 6051

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER C, PART 182.—INDUSTRIAL ALCOHOL

Specially denatured alcohol formula No. 29

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

The purpose of these amendments is to provide more flexibility in the selection of denaturants which may be authorized for use in Specially Denatured Alcohol Formula No. 29, by eliminating the restrictive requirement that any alternate denaturant must be a chemical produced from ethyl alcohol. The proposed amendments will permit the use as denaturants of chemicals other than those pro-

duced from ethyl alcohol. These amendments are considered necessary since present authorized denaturants have been found unsatisfactory for modern chemical manufacturing processes. Accordingly, the Appendix to Regulations 3, "Industrial Alcohol" (26 CFR, pt. 182; 7 F. R. 1858), as amended, is hereby amended as follows:

PARAGRAPH 1. The composition of Specially Denatured Alcohol Formula No. 29 is amended to read as follows:

To every 100 gallons of ethyl alcohol add: One gallon of 100 percent acetaldehyde or 5 gallons of an alcoholic solution of acetaldehyde containing not less than 20 percent acetaldehyde, or not less than 1 part by weight if solid, or volume if liquid, of any chemical that meets with the approval of the Commissioner.

This formula is restricted to processes where the alcohol loses its identity as alcohol by being converted into other chemicals. Where it is desired to use any chemicals other than acetaldehyde or an alcoholic solution of acetaldehyde for Formula No. 29, the use of such chemicals shall be subject to approval by the Commissioner as to kind and amount required.

PAR. 2. The specifications for denaturant ethylamines, listed immediately following the specifications for ethyl acetate in the "Specifications for Denaturants in Specially Denatured Alcohol," are revoked.

PAR. 3. The specifications for denaturant ethyl propionate, listed immediately following the specifications for ethyl ether in the "Specifications for Denaturants in Specially Denatured Alcohol," are revoked.

PAR. 4. The list "Denaturants Authorized for Completely and Specially Denatured Alcohol," is amended by striking therefrom the following:

Ethyl propionate	S. D. 29
Ethylamines	S. D. 29

The provisions of these amendments are not to be construed as restricting the use of alternate denaturants such as "GC–78," and "GC–79," which have been previously authorized.

Because the amendments made by this Treasury Decision are of a liberalizing character, it is unnecessary to issue this Treasury Decision with notice and public procedure thereon under section 4(a) of the Administrative Procedure Act, approved June 11, 1946, or subject to the effective date limitations of section 4(c) of said act.

This Treasury Decision shall be effective upon its publication in the Federal Register.

(This Treasury Decision is issued under the authority contained in secs. 3070, 3105, 3170, and 3176 of the Internal Revenue Code (53 Stat. 355, 358, 373 as amended, 375; 26 U. S. C. 3070, 3105, 3170, 3176).)

T. COLEMAN ANDREWS,
Commissioner of Internal Revenue.

Approved November 6, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Published in the Federal Register November 13, 1953)

REGULATIONS 7, SECTION 178.223a: Tankships, barges, and deep tanks of vessels. (Also Sections 178.216, 178.251a, 178.251b.) T. D. 6045

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER C, PART 178.—PRODUCTION, FORTIFICATION, TAXPAYMENT, ETC., OF WINES

Removal of wine in tankships, barges, and deep tanks of vessels

TREASURY DEPARTMENT.
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

In order to permit the shipment of wine from bonded premises, in bulk, by means of tankships, barges, or deep tanks of vessels, Regulations 7 [26 CFR, pt. 178] are hereby amended as follows:

PARAGRAPH 1. The second sentence of section 178.216 is amended to read as follows:

Wines may also be removed in uncased bottles, by pipeline or by hose, and in tankships, barges, or deep tanks of vessels, as hereinafter provided.

PAR. 2. There is inserted immediately following section 178.223 the following new section:

SEC. 178.223a. TANKSHIPS, BARGES, AND DEEP TANKS OF VESSELS.—Tankships, barges, and deep tanks of vessels used for the transportation of wine, whether in bond, tax-free, or taxpaid, must be equipped with route boards, similar in construction to those prescribed in section 178.223 for tank trucks and tank cars. Such route boards must be affixed to each compartment (if any) of such tankship, barge, or deep tank or tanks of a vessel. The compartments of tankships, barges, or deep tanks of vessels shall be marked and stamped in the manner provided in sections 178.219 and 178.242, insofar as applicable and, in addition, bear the marks prescribed in section 178.251 where the wine is transferred in bond. The required marks and stamps must be destroyed or otherwise obliterated immediately the compartment is empty. Wine to be transferred in bond may be shipped in bulk by means of tankships, barges, or deep tanks of vessels only pursuant to special permission first obtained from the assistant regional commissioner, as set forth in section 178.251a, and subject to such limitations and conditions as may be imposed by him. Such in-bond shipments may be made only where the premises of both the consignee and consignor are equipped with suitable facilities and where the wine is run directly from storage tanks on the consignor's premises into the tankship, barge, or deep tank or tanks of a vessel and directly from the tankship, barge, or deep tank or tanks of a vessel into storage tanks on the consignee's premises. The tanks of tankships, barges, and vessels, used to transfer wine in bond must be equipped for sealing, and be sealed, as required in section 178.251b. The provisions of section 178.223 concerning the consigning of wine by compartments of tank trucks or tank cars to more than one consignee will govern the consigning in bond of wine in tankships, barges, and deep tanks of vessels. (53 Stat. 354; 26 U. S. C. 3040.)

PAR. 3. There are inserted immediately following section 178.251 the following new sections:

SEC. 178.251a. APPLICATION FOR AUTHORITY TO USE TANKSHIPS, BARGES, AND DEEP TANKS OF VESSELS.—A proprietor desiring permission to transfer wines in tank-

ships, barges, and deep tanks of vessels shall make application therefor, in duplicate, to the assistant regional commissioner. The application may cover a specific lot of wine or be for continuing authority. Where shipment is to be made to more than one consignees' premises, separate application must be submitted for each such premises. The application must state:

(*a*) The name and address of the consignee,

(*b*) the name, serial number, registry number, or other identifying symbol or mark of each tankship, barge, or vessel to be used.

(*c*) the name and address of the carrier,

(*d*) the course or route to be followed from consignor to consignee premises, and

(*e*) whether the premises of both the consignor and consignee are equipped with suitable dock facilities and the wine is to be run directly from storage tanks on the consignor's premises into the tankship, barge, or deep tank or tanks of a vessel, and directly from the tankship, barge, or deep tank or tanks of a vessel into storage tanks on the consignee's premises. If the application is in order, the assistant regional commissioner will conduct such inquiries and investigations as may be necessary to verify the application, and the suitability of the tankship, barge, or deep tank or tanks of the vessel, and the dock and storage facilities at the shipping and receiving premises. In the case of interregion shipments, the suitability of the dock and storage facilities of the consignee will be verified by inquiry addressed to the assistant regional commissioner for the consignee's region. Upon approval by the assistant regional commissioner the original will be returned to the applicant and the copy retained for the assistant regional commissioner's files.

(53 Stat. 353; 26 U. S. C. 3037.)

SEC. 178.251b. SEALING OF TANKS.—Where wine is transferred in bond in tankships, barges, and deep tanks of vessels, the manhole covers, outlet valves, and all other openings of the tanks containing the wine shall be equipped with facilities for sealing so that the contents cannot be removed without showing evidence of tampering. Serially numbered seals, dissimilar in marking from cap seals used by the Internal Revenue Service shall be furnished and affixed by the carrier or proprietor. The serial numbers of the seals used on each shipment shall be reported by the consignor on the Form 703 prepared in accordance with section 178.252. (53 Stat. 353; 26 U. S. C. 3037.)

Because the amendments made by this Treasury Decision are of a liberalizing character, it is unnecessary to issue this Treasury Decision with notice and public procedure thereon under section 4(a) of the Administrative Procedure Act, approved June 11, 1946, or subject to the effective date limitations of section 4(c) of said act.

This Treasury Decision shall be effective on the date of its publication in the Federal Register.

(This Treasury Decision is issued under the authority contained in secs. 3037, 3040, 3176, and 3901 of the Internal Revenue Code (53 Stat. 353, 354, 375, 477; 26 U. S. C. 3037, 3040, 3176, 3901).)

JUSTIN F. WINKLE,
Acting Commissioner of Internal Revenue.

Approved October 19, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Published in the Federal Register, October 23, 1953)

REGULATIONS 7, SECTION 178.367: Inventories. T. D. 6032
(Also Regulations 3, 5, 11, 15, and 16.)

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER C, PARTS 178, 182, 184, 187, 189, AND 190

Discontinuance of Commissioner's copy of monthly reports concerning liquors.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

Regional Commissioners of Internal Revenue, Assistant Regional Commissioners of Internal Revenue, Alcohol and Tobacco Tax, and Others Concerned:

1. The purpose of these amendments is to discontinue the Commissioner's copy of the following monthly reports concerning liquors:

Premises	CFR part	IR Reg. No.	Form No.	Title
Bonded wineries and storerooms.	178	7	261	Winemaker's Monthly Report of Materials for Fortification and Amelioration (or Sweetening) of Wines
			276	Fortification of Wine
			701	Winemaker's Production Record
			702	Winemaker's Report of Production, Receipt, Treatment, and Disposition of Still Wines
			702-A	Winemaker's Report of Production, Receipt, and Disposition of Champagne and Other Sparkling Wines, and Artificially Carbonated Wines
			702-B	Winemaker's Vermouth Report (modified for aperitif wines)
			702-C	Winemaker's Inventory of Still Wines
Industrial alcohol plants	182	3	1442	Proprietor's Report of Operations at Industrial Alcohol Plants
Industrial alcohol bonded warehouses.	182	3	1443-A	Report of Uncoopered Alcohol at Bonded Warehouse
			1443-B	Report of Alcohol in Packages at Bonded Warehouse
Industrial alcohol denaturing plants.	182	3	129	Report of Denaturants
			1468-A	Ethyl Alcohol Received and Disposed of at Denaturing Plant
			1468-B	Denaturants Used at Denaturing Plant
			1468-C	Summary of Denaturants Used at Denaturing Plant
			1468-D	Denatured Alcohol Produced and Disposed of at Denaturing Plant
			1468-E	Summary of Denatured Alcohol
			1468-F	Recovered Alcohol Received and Disposed of at Denaturing Plant
Dealers in denatured alcohol.	182	3	1478	Bonded Dealer's Report of Specially Denatured Alcohol Received and Disposed of
Manufacturers using denatured alcohol.	182	3	1482	User's Report of Denatured Alcohol
Fruit distilleries	184	5	1493	Monthly Statement of Brandy Distillery Producing Wine Containing Less Than One-Half of One Percent of Alcohol by Volume
Distillery denaturing bonded warehouses.	187	16	129	Report of Denaturants
			575	Report for Denaturing Bonded Warehouse
Taxpaid bottling houses	189	11	52-D	Monthly Record and Report of Tax-Paid Bottling House Operations
Rectifying plants	190	15	702-A	Winemaker's Report of Production, Receipt, and Disposition of Champagne and Other Sparkling Wines, and Artificially Carbonated Wines

The amendments will also discontinue the preparation and submission of the Commissioner's copy of the power of attorney (Form 1534) where the proprietor's reports are signed by an agent.

2. Sections 178.367, 178.379, 178.381, 178.382, 178.384, 178.387, 178.390, 178.393, 178.401, 178.479, 178.502, and 178.507 of Regulations 7 (26 CFR, pt. 178; 10 F. R. 12307), "Production, Fortification, Taxpayment, Etc., of Wines," as amended, are amended as follows:

LOSSES

SEC. 178.367. INVENTORIES.—Each proprietor of a bonded winery or bonded storeroom shall take a physical inventory of all wines on hand on June 30 and December 31 of each year, and enter on his winery or storeroom accounts, Forms 702, 702-A, and 702-B, for those months any losses disclosed by such inventories. A detailed report of the inventory shall be made on Form 702-C, in duplicate, giving all the information called for by the form. One copy of Form 702-C shall be attached to each copy of Form 702, 702-A, or 702-B, to which it pertains, for the month in which the inventory was taken. Additional inventories may be taken at such other times as the proprietor may desire and any losses disclosed thereby shall be entered on the winery or storeroom accounts. Other losses ascertained to have been actually sustained may be entered on Forms 702, 702-A, and 702-B, but estimated losses may not be entered on the forms. When an inventory is taken, such fact should be noted on Forms 702, 702-A, and 702-B.

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(53 Stat. 353, 354, 373, 375, 477; 26 U. S. C. 3039, 3040, 3171, 3176, 3901.)

MONTHLY RECORDS

SEC. 178.379. FORM 702.—The proprietor of every bonded winery or bonded storeroom shall keep a monthly record on Form 702, in duplicate, of all still wine produced, received, and disposed of at his winery or storeroom. (53 Stat. 373, 375, 477; 26 U. S. C. 3171, 3176, 3901.)

SEC. 178.381. FORM 702-A.—The proprietor of every bonded winery manufacturing champagne, sparkling wine, or artificially carbonated wine, and the proprietor of every bonded winery or storeroom receiving, storing, or disposing of champagne, sparkling wine, or artificially carbonated wine, shall also keep a monthly record on Form 702-A, in duplicate, of all champagne, sparkling wine, and artificially carbonated wine produced, received, and disposed of at his winery or storeroom. (53 Stat. 373, 375, 477; 26 U. S. C. 3171, 3176, 3901.)

SEC. 178.382. FORM 702-B.—The proprietor of every bonded winery manufacturing vermouth, or other aperitif wine, and the proprietor of every bonded winery or storeroom receiving, storing, or disposing of vermouth, or other aperitif wine, shall also keep a monthly record on Form 702-B, in duplicate, of all vermouth, or other aperitif wine, produced, received, or disposed of at his winery or storeroom. (53 Stat. 373, 375, 477; 26 U. S. C. 3171, 3176, 3901.)

SEC. 178.384. INVENTORY RECORD, FORM 702-C.—The proprietor of every bonded winery or storeroom shall make a detailed record on Form 702-C, in duplicate, of each inventory taken by him of all wines on storage at his winery or storeroom on June 30 and December 31 of each year, and at any other time an inventory is taken. One copy of Form 702-C shall be attached to each copy of Form 702, 702-A, or 702-B, to which it pertains, for the same month. (53 Stat. 354, 373, 375, 477; 26 U. S. C. 3040, 3171, 3176, 3901.)

SEC. 178.387. MATERIAL RECORD, FORM 701.—The proprietor of every bonded winery shall keep a monthly record on Form 701, in duplicate, of all materials received and used for the manufacture of wine. The total of each kind of such materials received each day must be entered on the form on the day on which the materials are received. Form 701 should not be kept when there are no materials on hand or wine in the process of manufacture.

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(53 Stat. 373, 375, 477; 26 U. S. C. 3171, 3176, 3901.)

SEC. 178.390. COMPLETE RECORDS REQUIRED.—All the information called for in Forms 701, 702, 702-A, 702-B, and 702-C, as indicated by the headings of the columns and lines of the forms and the instructions printed thereon or issued in respect thereto, and as required by these regulations, must be reported. All operations and transactions must be entered on the forms before the close of the business day next succeeding the day on which the transactions occur. Where the making of the entries is deferred to the next business day, as herein

authorized, appropriate memoranda shall be maintained for the purpose of making the entries correctly. The entries must be made by the proprietor, or by his agent from personal knowledge or from data furnished by the proprietor. The entries must be made from day to day during the month (*a*) on both copies of each form, or (*b*) on one copy of each form, from which one additional copy must be prepared at the close of the month, or (*c*) on a rough copy of each form, from which two copies must be prepared at the close of the month. When a rough copy is kept, the entries shall be made thereon with indelible pencil, ink, or typewriter, and the rough copy shall be filed with the copy (prepared therefrom) retained at the winery or storeroom. When the entries are made from memoranda furnished by the proprietor, such memoranda shall be filed at the winery or storeroom. Care must be used to insure the keeping of accurate and complete records. Each report should be carefully checked before being forwarded to the Assistant Regional Commissioner.[1] Reports prepared by persons who have no knowledge of the winery or storeroom operations and who are not furnished with the necessary data by the proprietor will not be accepted. Where forms are rendered in blank they should bear the notation "No transactions." Upon discontinuance of a bonded winery or bonded storeroom, the last reports should be marked "Final." (53 Stat. 373, 375, 477; 26 U. S. C. 3171, 3176, 3901.)

SEC. 178.393. DISPOSITION OF FORMS.—One copy each of Forms 701, 702, 702-A, 702-B, and 702-C will be retained at the winery or storeroom by the proprietor as a permanent record, subject to inspection by Government officers at any reasonable hour. On or before the 10th day of the month succeeding that for which rendered, the proprietor will forward the original of each form to the Assistant Regional Commissioner for audit and retention. (53 Stat. 373, 375, 477; 26 U. S. C. 3171, 3176, 3901.)

ASSISTANT REGIONAL COMMISSIONER'S ACCOUNTS

SEC. 178.401. ACCOUNTS IN DUPLICATE.—Assistant Regional Commissioner's monthly accounts will be prepared in duplicate and by States within the region. One copy of each account will be retained by the Assistant Regional Commissioner and one copy of each forwarded on or before the last day of the month, succeeding that for which rendered, to the Commissioner. (53 Stat. 375, 477; 26 U. S. C. 3176, 3901.)

FORTIFICATION OF WINE

SEC. 178.479. MONTHLY REPORT, FORM 276.—Each day wines are fortified the officer will enter on Form 276 the information called for on that form, as required by this part and as indicated by the headings of the various columns and lines and the instructions printed on the form. Losses of brandy will be entered on Form 276 in accordance with section 178.477. At the close of the month, or upon completion of fortification for the month, the officer will complete Form 276, retain one copy at the winery as a permanent record, and forward the original to the Assistant Regional Commissioner for audit and retention. (53 Stat. 351, 375, 477; 26 U. S. C. 3034, 3176, 3901.)

WINEMAKER'S BRANDY AND SWEETENING—AGENTS REPORT

SEC. 178.502. FILING OF REPORT.—One copy of Form 261 shall be retained at the winery by the winemaker as a permanent record, subject to inspection by Government officers at any reasonable hour. On or before the 10th day of the succeeding month, the winemaker will forward the original of the form to the Assistant Regional Commissioner for audit and retention. (53 Stat. 348 as amended, 350 as amended, 351, 373, 375, 477; 26 U. S. C. 3031, 3032, 3033, 3171, 3176, 3901.)

ASSISTANT REGIONAL COMMISSIONER'S ACCOUNT

SEC. 178.507. FILING OF ACCOUNTS.—The accounts will be prepared, in duplicate, by States within the region. One copy will be retained by the Assistant Regional Commissioner, and the original will be forwarded to the Commissioner not later than the last day of the month succeeding that for which the account is rendered. (53 Stat. 375, 477; 26 U. S. C. 3176, 3901.)

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[1] Denotes the Assistant Regional Commissioner of Internal Revenue, Alcohol and Tobacco Tax.

3. Regulations 3 (26 CFR, part 182; 7 F. R. 1864), "Industrial Alcohol," as amended, are amended as follows:

(*a*) Sections 182.355, 182.456, 182.459, 182.642, 182.645, 182.646, 182.647, 182.668, 182.781, 182.787, 182.819, 182.822, 182.867, 182.868, 182.873, 182.874, and 182.876 are amended; and

(*b*) Sections 182.649, 182.789, and 182.823 are revoked.

OPERATION OF INDUSTRIAL ALCOHOL PLANTS

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DISTILLATION

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SEC. 182.355. REDISTILLATION OF ALCOHOL.—(a) AUTHORIZATION AND PROCEDURE.—The Assistant Regional Commissioner may, in his discretion, provided he deems it proper so to do and subject to such conditions and restrictions as he may impose, authorize the transfer of alcohol from an industrial alcohol plant or a bonded warehouse to an industrial alcohol plant for redistillation. In making the request for such special authorization the proprietor of the industrial alcohol plant desiring to redistill alcohol will submit to the Assistant Regional Commissioner of his region a statement in duplicate showing the source and quantity of the alcohol and the necessity for redistillation. The Assistant Regional Commissioner will note his approval or disapproval on all copies of the application. He will return the original to the proprietor and retain one copy for file. Where the alcohol for redistillation is to be received from an industrial alcohol bonded warehouse on the industrial alcohol plant premises, the procedure prescribed by the regulations in this part governing the transfer of alcohol from an industrial alcohol plant to a bonded warehouse will be followed insofar as applicable. See particularly section 182.408b. Where the alcohol for redistillation is to be received from an industrial alcohol bonded warehouse not on the same premises or from another industrial alcohol plant, the procedure prescribed by the regulations in this part will be followed insofar as applicable. See particularly sections 182.408c and 182.408d. The transfer application and permit Form 1436 will be appropriately modified.

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(53 Stat. 357, 358, 364, 375; 26 U. S. C. 3103, 3105, 3124, 3176.)

PROPRIETOR'S RECORDS AND REPORTS

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SEC. 182.456. FORM 1442.—The proprietor of every industrial alcohol plant shall keep a daily record of industrial alcohol plant operations on Form 1442, "Proprietor's Report of Operations at Industrial Alcohol Plant." Entries shall be made as indicated by the headings of the various columns and lines on the form and the instructions printed thereon or issued in respect thereto, and as required by the regulations in this part. Entries shall be made on the form before the close of the business day next succeeding the day on which the transactions occur, except that summary entries will be made at the close of the month. Where the making of entries is deferred to the next business day, as authorized herein, appropriate memoranda shall be maintained for the purpose of making the entries correctly. Where an industrial alcohol plant, in connection with the production of ethyl alcohol by any method, produces other chemicals as byproducts, or where an industrial alcohol plant, in connection with the production of substances other than ethyl alcohol, such as butyl alcohol, produces ethyl alcohol as a byproduct, a separate record on Form 1442 will be maintained for each process. The quantity of materials used in the production of ethyl alcohol will be determined separately from the quantity used in the production of other substances. Such determination may be made at the close of the month for reporting on Form 1442. Form 1442 must be verified under oath (or affirmation) by the proprietor or his authorized agent at the plant: *Provided*, That if the form officially prescribed for such report contains therein a provision for verification by a written declaration that such report is made under penalties of perjury, such report shall be verified by the execution of such declaration, and such declaration so executed shall be in lieu of the oath required herein for verification. The proprietor will deliver Form 1442, in duplicate, to the storekeeper-gauger on or before the 5th day of the month succeeding

that for which the report is rendered. The storekeeper-gauger will examine the report, execute the certificate of the government officer on both copies of the form, return one copy to the proprietor, and forward the original to the Assistant Regional Commissioner for audit and retention. (53 Stat. 357, 358, 364, 373, 375, 63 Stat. 667; 26 U. S. C. 3103, 3105, 3124, 3171, 3176, 3809.)

SEC. 182.459. SIGNING OF REPORTS.—Forms 1442 and 52-E must be signed in the same manner as the application, Form 1431, except that in the case of a corporation, the affixing of the corporate seal will not be required. Where the reports are signed by an agent, proper power of attorney authorizing the agent to execute the reports for the proprietor must be filed on Form 1534, in duplicate, with the Assistant Regional Commissioner who will, after entering the date of receipt and his signature on both copies, retain the original and return the copy to the principal. (53 Stat. 358, 364, 375, 63 Stat. 667; 26 U. S. C. 3105, 3124, 3176, 3809.)

OPERATION OF INDUSTRIAL ALCOHOL BONDED WAREHOUSES

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RECORDS AND REPORTS OF PROPRIETOR

SEC. 182.642. GENERAL.—The proprietor of every industrial alcohol bonded warehouse shall keep monthly records and render daily reports as hereinafter provided. Entries shall be made as indicated by the headings of the various columns and lines of the form and the instructions printed thereon or issued in respect thereto and as required by the regulations in this part. The provisions of section 182.455 concerning the time of making entries; of section 182.455a concerning the failure to keep records or allow inspection and of section 182.461 concerning the filing of reports by proprietors of industrial alcohol plants are hereby made applicable to records and reports rendered by proprietors of industrial alcohol bonded warehouses. The reports must be signed in the same manner as the application, Form 1431, except that in the case of a corporation the affixing of the corporate seal will not be required. Where the reports are signed by an agent, proper power of attorney authorizing the agent to execute the reports for the proprietor must be filed on Form 1534, in duplicate, with the Assistant Regional Commissioner who will, after entering the date of receipt and his signature on both copies, retain the original and return the copy to the principal. (53 Stat. 357, 358, 364, 371, 375; 26 U. S. C. 3101, 3105, 3124, 3171, 3176.)

SEC. 182.645. FORM 1443-A.—The proprietor of every bonded warehouse shall keep a monthly record, Form 1443-A, "Report of Uncoopered Alcohol," and render monthly reports thereon, in duplicate, of all uncoopered alcohol received and disposed of. Before the close of the business day next succeeding the day on which the transactions occur entries shall be made in the respective columns of the quantity of alcohol deposited in the warehouse, or received in bond at the bonded warehouse, or packages filled, and the quantities withdrawn for shipment uncoopered. Where the making of the entries is deferred to the next business day, as authorized herein, appropriate memoranda shall be maintained for the purpose of making the entries correctly.

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(53 Stat. 357, 358, 359, 364, 373, 375; 26 U. S. C. 3101, 3105, 3107, 3124, 3171, 3176.)

SEC. 182.646. FORM 1443-B.—The proprietor shall keep a monthly record on Form 1443-B, "Report of Alcohol in Packages," in duplicate. There shall be entered daily the quantity of alcohol transferred at the warehouse to packages or received in packages from industrial alcohol plants and from other bonded warehouses and the quantities withdrawn for shipment in packages from the warehouse. Entries of withdrawals of alcohol for taxpayment and deposit in the taxpaid storeroom (if any) should show the disposition of such alcohol to the proprietor of the warehouse for such purpose. The required entries shall be made in the form before the close of the business day next succeeding the day on which the transactions occur. Where the making of the entries is deferred to the next business day, as authorized herein, appropriate memoranda shall be maintained for the purpose of making the entries correctly. (53 Stat. 357, 358, 364, 375; 26 U. S. C. 3101, 3105, 3124, 3176.)

SEC. 182.647. DISPOSITION OF FORMS 1443-A AND 1443-B.—On or before the 5th day of the month succeeding that for which Forms 1443-A and 1443-B are rendered, the proprietor shall deliver two copies of each form to the storekeeper-

gauger in charge. Each form shall be duly subscribed and sworn to: *Provided*, That if the form officially prescribed for such report contains therein a provision for verification by a written declaration that such report is made under penalties of perjury, such report shall be verified by the execution of such declaration, and such declaration so executed shall be in lieu of the oath required herein for verification. The storekeeper-gauger shall examine the forms carefully, and, if they are complete in all respects, and the quantities shown on hand at the end of the month are correct, he will initial all copies of the forms, forward the original of each form to the Assistant Regional Commissioner for audit and retention and return the copy of each form to the proprietor who shall file the same in bound form as a permanent record available for inspection by Government officers. (53 Stat. 358, 364, 375, 63 Stat. 667; 26 U. S. C. 3105, 3124, 3176, 3809.)

OPERATIONS BY USERS OF TAX-FREE ALCOHOL

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RECORDS AND REPORTS OF PERMITTEE

SEC. 182.668. GENERAL.—Every person holding basic permit, Form 1447, shall keep records and render reports as hereinafter provided. Entries shall be made as indicated by the headings of the various columns and lines of the form and the instructions printed thereon or issued in respect thereto and as required by this part. The provisions of section 182.455 concerning the time of making entries, of section 182.455a concerning the failure to keep records or allow inspection and of section 182.461 concerning the filing of forms by proprietors of industrial alcohol plants are hereby made applicable to reports by persons holding basic permit, Form 1447. The reports must be signed in the same manner as the application, Form 1447, except that in the case of a corporation the affixing of the corporate seal will not be required. Where the reports are signed by an agent, proper power of attorney authorizing the agent to execute the reports for the proprietor must be filed on Form 1534 in duplicate, with the Assistant Regional Commissioner who will, after entering the date of receipt and his signature on both copies, retain the original and return the copy to the principal. (53 Stat. 357, 358, 359, 364, 373, 375; 26 U. S. C. 3101, 3105, 3108, 3124, 3171, 3176.)

OPERATION OF INDUSTRIAL ALCOHOL DENATURING PLANTS

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RECORDS AND REPORTS OF PROPRIETOR

SEC. 182.781. GENERAL.—The proprietor of every denaturing plant shall render daily reports on Forms 1466, 1467, 1453–A, and 1473 and shall keep monthly records on Forms 129 and 1468–A, B, C, D, E, and F. All of the information called for in each form, as indicated by the headings of the various columns and lines of the form and the instructions printed thereon or issued in respect thereto and as required by the regulations in this part will be given. The requirements of section 182.455 concerning the time of making entries, of section 182.455a concerning the failure to keep records or allow inspection, and of section 182.461 concerning the filing of forms by proprietors of industrial alcohol plants, are hereby made applicable to reports rendered by proprietors of denaturing plants. The reports must be signed in the same manner as the application, Form 1431, except that in the case of a corporation the affixing of the corporate seal will not be required. Forms 129, 1468–A, 1468–E, and 1468–F must be verified under oath (or affirmation) by the proprietor or his authorized agent at the plant: *Provided*, That if the form officially prescribed for such report contains therein a provision for verification by a written declaration that such report is made under penalties of perjury, such report shall be verified by the execution of such declaration, and such declaration so executed shall be in lieu of the oath required herein for verification. Where the reports are signed by an agent, proper power of attorney authorizing the agent to execute the reports for the proprietor must be filed on Form 1534, in duplicate, with the Assistant Regional Commissioner who will, after entering the date of receipt and his signature on both copies, retain the original and return the copy to the principal. (53 Stat. 355, 358, 364, 375; 63 Stat. 667; 26 U. S. C. 3070, 3105, 3124, 3176, 3809.)

SEC. 182.787. FORMS 129 AND 1468–A, B, C, D, E, AND F.—The proprietor shall keep a monthly record on Forms 129 and 1468–A, B, C, D, E, and F, in duplicate,

of all alcohol and denaturants used for denaturation, and removed (either before or after denaturation) during the month, and on hand the first and last of the month. Entries shall be made on the forms before the close of the business day next succeeding the day on which the transactions occur, except that summary entries will be made at the close of the month. Where the making of the entries is deferred to the next business day, as authorized herein, appropriate memoranda shall be maintained for the purpose of making the entries correctly.

* * * * * * *

(e) DISPOSITION OF FORMS.—The proprietor will deliver both copies of Forms 129 and 1468-A, B, C, D, E, and F to the storekeeper-gauger on or before the 10th day of the month succeeding that for which the forms are rendered. The storekeeper-gauger will examine the forms, and if they are complete in every respect, and if the quantities of denaturants received and shipped out, the shipment of completely denatured alcohol, the quantities of recovered alcohol restored and the losses in restoration, and the quantities on hand last of month are all correctly reported, he will initial all copies of the forms, return the copy of each form to the proprietor and forward the original of each form to the Assistant Regional Commissioner for audit and retention. The Assistant Regional Commissioner, in his discretion, may extend (to the 10th day of the month) the time for delivering the monthly report. Form 1442, for the industrial alcohol plant on the denaturing plant premises and Forms 1443-A and 1443-B for the bonded warehouse on the denaturing plant premises, in order that all of the monthly reports for the same premises may be submitted together.

* * * * * * *

(53 Stat. 355, 358, 363, 364, 375; 26 U. S. C. 3070, 3105, 3121, 3124, 3176.)

OPERATIONS BY DEALERS IN SPECIALLY DENATURED ALCOHOL

RECORDS AND REPORTS OF BONDED DEALERS

SEC. 182.819. GENERAL.—Every person holding basic permit, Form 1476, shall keep records and render reports as hereinafter provided. Entries shall be made as indicated by the headings of the various columns and lines of the forms and the instructions printed thereon or issued in respect thereto and as required by this part. The provisions of section 182.455a concerning the failure to keep records or allow inspection and of section 182.461 concerning the filing of forms by proprietors of industrial alcohol plants are hereby made applicable to reports rendered by bonded dealers holding basic permit, Form 1476. The reports must be signed in the same manner as the application, Form 1474, except that in the case of a corporation the affixing of the corporate seal will not be required. Where the reports are signed by an agent proper power of attorney authorizing the agent to execute the reports for the proprietor must be filed on Form 1534, in duplicate, with the Assistant Regional Commissioner who will, after entering the date of receipt and his signature on both copies, retain the original and return the copy to the principal. (53 Stat. 355, 357, 358, 364, 373, 375; 26 U. S. C. 3070, 3101, 3105, 3124, 3171, 3176.)

SEC. 182.822. RECORD, FORM 1478.—Every bonded dealer holding permit to deal in specially denatured alcohol must keep Form 1478, covering his transactions for each month and prepare monthly reports therein, in duplicate. Form 1478 must be verified under oath (or affirmation) by the bonded dealer or his authorized agent: *Provided*, That if the form officially prescribed for such report contains therein a provision for verification by a written declaration that such report is made under penalties of perjury, such report shall be verified by the execution of such declaration, and such declaration so executed shall be in lieu of the oath required herein for verification. One copy of the form shall be retained by the bonded dealer and the original must be forwarded by the bonded dealer on or before the 5th day of the succeeding month to the Assistant Regional Commissioner for audit and retention. There will be entered daily the details of all specially denatured alcohol received, and when received from a denaturing plant the number of such plant shall be entered in the column provided therefor. The amount of specially denatured alcohol lost from each lot in transit to the bonded dealer's storeroom will be entered in the proper column on the same line with the quantity reported received in such lot. The quantities reported

lost in transit will not be included in the losses in the storeroom reported in the summary. Details will be entered daily of all specially denatured alcohol disposed of to manufacturers or other bonded dealers or any other disposition of such specially denatured alcohol. The number of the basic permit of the manufacturer or bonded dealer to whom specially denatured alcohol is shipped shall also be appropriately entered. Where several packages are shipped or delivered on the same day to the same person, the aggregate quantity so shipped or delivered may be stated on one line. The required entries shall be made in the form before the close of the business day next succeeding the day on which the transactions occur. Where the making of the entries is deferred to the next business day, as authorized herein, appropriate memoranda shall be maintained for the purpose of making the entries correctly.

* * * * * * *

(53 Stat. 358, 364, 375, 63 Stat. 667; 26 U. S. C. 3105, 3124, 3176, 3809.)

OPERATIONS BY USERS OF SPECIALLY DENATURED ALCOHOL

* * * * * * *

DESTRUCTION AND DISPOSITION OF SPECIALLY DENATURED ALCOHOL

SEC. 182.867. DESTRUCTION.—Specially denatured alcohol in the possession of a permittee may, upon approval of the Assistant Regional Commissioner, be destroyed by the permittee. The permittee shall file application so to do with the Assistant Regional Commissioner, in duplicate, stating fully the reason therefor. The specially denatured alcohol shall be destroyed in the presence of a Government officer, unless the quantity involved is small and insufficient in the opinion of the Assistant Regional Commissioner to warrant such supervision. Upon approval of the application, the Assistant Regional Commissioner shall instruct the permittee whether or not such destruction shall be witnessed by a Government officer. If a Government officer is assigned to witness the destruction of the specially denatured alcohol, the officer shall certify to the destruction on each copy of the approved application specifying the date and manner of destruction. If the permittee is authorized to destroy the specially denatured alcohol without Government supervision, he shall likewise certify to the destruction of the specially denatured alcohol on each copy of the approved application. One copy of the approved application will be filed by the permittee and one copy returned to the Assistant Regional Commissioner. (53 Stat. 358, 364, 375; 26 U. S. C. 3105, 3124, 3176.)

SEC. 182.868. RETURN TO INDUSTRIAL ALCOHOL PLANT, DENATURING PLANT OR BONDED DEALER.—Where specially denatured alcohol, lawfully in the possession of a manufacturer, is found to be unsuitable for use, or where any such manufacturer discontinues the use thereof, or where for any other legitimate reason such manufacturer desires so to do, such denatured alcohol may be returned to any industrial alcohol plant, denaturing plant, or bonded dealer for lawful disposition: *Provided*, That (*a*) consent of surety is filed on the bond (if any) of the manufacturer, extending terms thereof to cover the transportation of the specially denatured alcohol to the industrial alcohol plant, denaturer, or bonded dealer, (*b*) the industrial alcohol plant, denaturer, or bonded dealer consents to the return, and (*c*) permission for such transfer is, in each instance, first obtained from the Assistant Regional Commissioner of the region from which the specially denatured alcohol is to be returned. The application shall be filed in duplicate with the Assistant Regional Commissioner. If the application is approved, the Assistant Regional Commissioner will forward one copy of the approved application to the permittee, and retain the remaining copy for his files. If the industrial alcohol plant, denaturer, or bonded dealer is situated in another region, the Assistant Regional Commissioner authorizing the return will forward a letter of authorization to the Assistant Regional Commissioner of such other region. (53 Stat. 358, 364, 375; 26 U. S. C. 3105, 3124, 3176.)

RECORDS AND REPORTS OF MANUFACTURERS

SEC. 182.873. GENERAL.—Every person holding basic permit, Form 1481, shall keep records and render reports as hereinafter provided. Entries shall be made

as indicated by the headings of the various columns and lines of the form and the instructions printed thereon or issued in respect thereto and as required by the regulations in this part. The provisions of section 182.455a concerning the failure to keep records or allow inspection and of section 182.461 concerning the filing of forms by proprietors of industrial alcohol plants are hereby made applicable to reports rendered by manufacturers holding basic permit, Form 1481, to use specially denatured alcohol. The reports must be signed in the same manner as the application, Form 1479, except that in the case of a corporation the affixing of the corporate seal will not be required. Where the reports are signed by an agent, proper power of attorney authorizing the agent to execute the reports for the proprietor must be filed on Form 1534, in duplicate, with the Assistant Regional Commissioner who will, after entering the date of receipt and his signature on both copies, retain the original and return the copy to the principal. (53 Stat. 355, 358, 364, 375; 26 U. S. C. 3070, 3105, 3124, 3176.)

SEC. 182.874. FORM 1482.—Every manufacturer holding permit to use specially denatured alcohol or to recover completely denatured alcohol or articles for reuse must make a report on Form 1482, covering his transactions for each month and prepare monthly reports thereon, in duplicate. The report must show all of the information as indicated by the various columns and lines, including all denatured alcohol on hand, received, used, and recovered during the month, and as indicated by the instructions on the form or issued in respect thereto and as required by the regulations in this part. Form 1482 must be verified under oath (or affirmation) by the manufacturer or his authorized agent: *Provided*, That if the form officially prescribed for such report contains therein a provision for verification by a written declaration that such report is made under penalties of perjury, such report shall be verified by the execution of such declaration, and such declaration so executed shall be in lieu of the oath required herein for verification. One copy of the form shall be retained by the manufacturer and the original must be forwarded by the manufacturer on or before the 10th day of the succeeding month to the Assistant Regional Commissioner for audit and retention in accordance with section 182.876. Failure to keep or file this report as herein required will constitute grounds for the issuance of citation for the revocation of the manufacturer's basic permit.

* * * * * * *

(53 Stat. 355, 358, 364, 375, 63 Stat. 667; 26 U. S. C. 3070, 3105, 3124, 3176, 3809.)

SEC. 182.876. AUDIT OF REPORTS.—Upon receipt of Form 1482 from the manufacturer, the Assistant Regional Commissioner will carefully examine the same, and shall see that all specially denatured alcohol shown shipped to the manufacturer on shippers' memorandum slips, Form 1473, has been accounted for by the manufacturer. Upon completion of the examination and audit, the Assistant Regional Commissioner will file the Form 1482 in his office. (53 Stat. 358, 364, 375; 26 U. S. C. 3105, 3124, 3176.)

4. Section 184.842 of Regulations 5 (26 CFR, part 184; 15 F. R. 5552), "Production of Brandy," is amended as follows:

SUBPART NN—MANUFACTURE OF DEALCOHOLIZED WINES

* * * * * * *

SEC. 184.842. RECORD AND REPORT, FORM 1493.—Every fruit distiller manufacturing dealcoholized wine shall keep a record on Form 1493 for each month that dealcoholized wine is produced, or dealcoholized wine or wine containing one-half of 1 percent or more of alcohol by volume procured for the manufacture of dealcoholized wine, remains on the premises. Entries shall be made on the form as indicated by the headings of the various columns and lines thereof. The form will be retained at the distillery as a permanent record, subject to inspection by Government officers. The distiller shall prepare and forward an original of Form 1493 to the Assistant Regional Commissioner not later than the 10th day of the month succeeding that for which the report is rendered. Form 1493 must be sworn to before an officer authorized to administer oaths: *Provided*, That if the form officially prescribed for such report contains therein a provision for verification by a written declaration that the report is made under penalties of perjury, such report shall be verified by the execution of such declaration, and

such declaration so executed shall be in lieu of the oath required herein for verification. The Assistant Regional Commissioner will, after audit, retain the report in his office. (53 Stat. 347 as amended, 348 as amended, 375; 63 Stat. 667; 26 U. S. C. 3030, 3031, 3176, 3809.)

5. Sections 187.316 and 187.326 of Regulations 16 (26 CFR, part 187; 15 F. R. 5009), "Denaturation of Rum," are amended as follows:

SUBPART X—PROPRIETOR'S RECORD AND REPORT

* * * * * * *

SEC. 187.316. MONTHLY REPORT.—The proprietor shall render a monthly report on Record 129, to the Assistant Regional Commissioner on or before the 5th day of the succeeding month. Record 129 must be sworn to before an officer authorized to administer oaths: *Provided*, That if the form officially prescribed for such report contains therein a provision for verification by a written declaration that such report is made under penalties of perjury, such report shall be verified by the execution of such declaration, and such declaration so executed shall be in lieu of the oath required herein for verification. The Assistant Regional Commissioner will, after audit, retain the report in his office. (53 Stat. 373, 375, 63 Stat. 667; 26 U. S. C. 3171, 3176, 3809.)

SUBPART Y—STOREKEEPER-GAUGER'S RECORD AND REPORT

* * * * * * *

SEC. 187.326. MONTHLY REPORT.—The storekeeper-gauger shall render a monthly report on Form 575, to the Assistant Regional Commissioner on or before the 5th day of the succeeding month. The Assistant Regional Commissioner will, after audit, retain the report in his office. (53 Stat. 375; 26 U. S. C. 3176.)

6. Sections 189.295 and 189.301 of Regulations 11 (26 CFR, part 189; 15 F. R. 4581), "Bottling of Taxpaid Distilled Spirits," are amended as follows:

SUBPART Y—PROPRIETOR'S RECORDS AND REPORTS

SEC. 189.295. Form 52-D.—Every proprietor of a taxpaid bottling house shall keep a record and render a monthly report, on Form 52-D, of all spirits received, dumped for bottling, bottled, and disposed of at his bottling house. (53 Stat. 327 as amended, 375, 495; 26 U. S. C. 2857, 3176, 4041.)

SEC. 189.301. REPORTS.—Except as otherwise provided in this section, the proprietor shall file, daily, full and complete transcripts, of Form 52-D (part 3) on Form 52-D (part 3) and full and complete transcripts of Record 52 on Forms 52-A and 52-B (one copy of each) with the Assistant Regional Commissioner, by delivering or mailing them to such officer on the date the transactions entered therein occurred: *Provided*, That in any case in which the Assistant Regional Commissioner shall direct, the transcripts shall be so filed with the supervisor in charge instead of with the Assistant Regional Commissioner. The transcripts shall bear the following certification signed by the person or officer authorized to execute Form 338 or 52-D:

> I hereby certify that these transcripts, consisting of —— pages disclose all the transactions which occurred during the period covered thereby, and that each entry is correct.

If in any case the Assistant Regional Commissioner shall so authorize, the transcripts, in lieu of being filed daily, may be filed with him on or before the 10th day of the month succeeding the month in which the transactions occurred. In such event, transactions will be entered on Form 52-D and Record 52 in accordance with the provisions of section 189.299. A full and complete transcript of Form 52-D (except part 3 where such part is filed daily) shall be prepared and forwarded to the Assistant Regional Commissioner on or before the 10th day of the month succeeding the month in which the transactions occurred. Form 52-D must be sworn to before an officer authorized to administer oaths: *Provided*, That if the form officially prescribed for such report contains therein a

provision for verification by a written declaration that such report is made under penalties of perjury, such report shall be verified by the execution of such declaration, and such declaration so executed shall be in lieu of the oath required herein for verification. When Record 52 is kept, a monthly summary report on Form 338 shall be prepared in duplicate, one copy of which will be retained on file and the original forwarded to the Assistant Regional Commissioner on or before the 10th day of the month succeeding the month in which the transactions occurred. Form 338 must be sworn to before an officer authorized to administer oaths: *Provided*, That if the form officially prescribed for such report contains therein a provision for verification by a written declaration that such report is made under penalties of perjury, such report shall be verified by the execution of such declaration, and such declaration so executed shall be in lieu of the oath required herein for verification. Records kept on Form 52–D and Record 52 shall be preserved for a period of four years, and during such period shall be available during business hours for inspection and the taking of abstracts by the Commissioner or any internal revenue officer. (53 Stat. 327 as amended, 373 as amended, 375, 495, 63 Stat. 667; 26 U. S. C. 2857, 3170, 3176, 4041, 3809.)

7. Section 190.510 of Regulations 15 (26 CFR, pt. 190; 15 F. R. 4790), "Rectification of Spirits and Wines," is amended as follows:

SUBPART Y—RECTIFICATION

* * * * * * *

MANUFACTURE OF SPARKLING WINES

* * * * * * *

SEC. 190.510. RECORDS AND REPORTS.—Where the sparkling wine is to be manufactured by secondary fermentation within the bottle, the rectifier will, upon bottling the still wine, prepare a special report on Form 702–A, in duplicate, properly modified as to the heading, and showing in Statement II the date, quantity, and alcoholic content of the still wines used and the number of bottles of each size filled. Form 702–A must be sworn to before an officer authorized to administer oaths: *Provided*, That if the form officially prescribed for such report contains therein a provision for verification by a written declaration that such report is made under the penalties of perjury, such report shall be verified by the execution of such declaration, and such declaration so executed shall be in lieu of the oath required herein for verification. The rectifier will retain the copy of Form 702–A and forward the original copy to the Assistant Regional Commissioner for audit and retention. Thereafter, as long as sparkling wines are in the process of manufacture the rectifier will prepare a report thereof each month on Form 702–A, in duplicate, the copy of which will be retained at the rectifying plant and the original forwarded to the Assistant Regional Commissioner enclosed with the rectifier's monthly report, Form 45. The rectifier will also make appropriate entries on Form 45 of the manufacture and disposition of all sparkling wines produced. (53 Stat. 327, 373 as amended, 375; 63 Stat. 667; 26 U. S. C. 2855, 3170, 3176, 3809.)

8. It is found that compliance with the notice and public rule-making procedure and effective date requirements of the Administrative Procedure Act (5 U. S. C. 1001, et seq.) is unnecessary in connection with the issuance of these amendments for the reason that the changes are of a liberalizing and administrative character.

9. These regulations shall be effective on July 1, 1953.

T. COLEMAN ANDREWS,
Commissioner of Internal Revenue.

Approved July 23, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register July 27, 1953, 8:50 a. m.)

REGULATIONS 10, SECTION 185.270: Basic qualifications required. T. D. 6050
(Also Sections 185.271, 185.272, 185.273.)

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER C, PART 185.—WAREHOUSING OF DISTILLED SPIRITS

Approval of alternate operations of a bottling-in-bond department as a taxpaid bottling house.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

In order that the storekeeper-gauger in charge at an internal revenue bonded warehouse, in lieu of the assistant regional commissioner, may approve the alternate operation of the bottling-in-bond department of such warehouse as a taxpaid bottling house, Regulations 10 [26 CFR, pt. 185] are amended as follows:

PARAGRAPH 1. Section 185.270 is amended as follows:

(A) By inserting immediately after the words "taxpaid bottling house" in the proviso of the first sentence, the following: "is for a period of 24 hours, or multiples thereof, concurrent with the calendar day, or days, as the case may be, and".

(B) By striking the words "district supervisor" in the two places they appear in the last sentence and inserting in lieu thereof in the first instance "assistant regional commissioner" and in the second instance "storekeeper-gauger in charge of the warehouse".

PAR. 2. Section 185.271 is amended by striking the words "district supervisor" and inserting in lieu thereof "storekeeper-gauger in charge of the warehouse".

PAR. 3. Section 185.272 is amended as follows:

(A) By striking the words "district supervisor" in the first sentence of paragraph (a) and inserting in lieu thereof "storekeeper-gauger in charge of the warehouse".

(B) By amending the second sentence of paragraph (a) which begins "The form shall" to read as follows: "The form shall be executed in accordance with the instructions printed thereon or issued in respect thereto, and as required by this part."

(C) By inserting after the second sentence of paragraph (a) the following new sentence: "Upon approval of Form 404, the storekeeper-gauger in charge will forward the original copy to the assistant regional commissioner, deliver one copy to the proprietor and retain the remaining copy for his files."

PAR. 4. Section 185.273 is amended as follows:

(A) By striking the words "district supervisor" in the first sentence of paragraph (a) and inserting in lieu thereof "storekeeper-gauger in charge of the warehouse".

(B) By amending the second sentence of paragraph (a) which begins "The form shall" to read as follows: "The form shall be executed in accordance with the instructions printed thereon or issued in respect thereto, and as required by this part."

(C) By inserting after the second sentence of paragraph (a) the following new sentence: "Upon approval of Form 404, the storekeeper-gauger in charge will forward the original copy to the assistant regional commissioner, deliver one copy to the proprietor and retain the remaining copy for his files."

Because the changes made are of an administrative character, it is found that it is unnecessary to issue this Treasury Decision with notice and public procedure thereon under section 4(a) of the Administrative Procedure Act, approved June 11, 1946, or subject to the effective date limitations of section 4(c) of said act.

This Treasury Decision shall be effective upon the date of publication in the Federal Register.

(This Treasury Decision is issued under the authority contained in sec. 3176 of the Internal Revenue Code (53 Stat. 375; 26 U. S. C. 3176).)

JUSTIN F. WINKLE,
Acting Commissioner of Internal Revenue.

Approved November 6, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Published in the Federal Register November 13, 1953)

REGULATIONS 10, SECTION 185.943: Marks and brands on cases for domestic spirits. T. D. 6018

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER C, PART 185.—WAREHOUSING OF DISTILLED SPIRITS

Amending section 185.943 of Regulations 10 to permit identification of bottle labels and State stamps to be shown on Government side of cases of bottled-in-bond spirits.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To District Commissioners, Assistant District Commissioners, Alcohol and Tobacco Tax, and Others Concerned:

1. Section 185.943 of Regulations 10, "Warehousing of Distilled Spirits" (26 CFR, pt. 185; 15 F. R. 5233), is hereby amended as follows:

SUBPART PP—MARKS AND BRANDS AND CONSTRUCTION OF CASES

* * * * * * *

SEC. 185.943. MARKS AND BRANDS ON CASES FOR DOMESTIC SPIRITS.—Each case of distilled spirits bottled in bond for domestic consumption shall have plainly burned, embossed, printed, or stenciled on the Government side thereof, in letters and figures not less than one-half of an inch in height, in addition to the serial number, the registry number and State in which the warehouse at which the spirits are bottled is located, and the quantity and proof of the spirits. There shall also be plainly burned, embossed, printed, or stenciled on the Government side of each case, in letters not less than one-half of an inch in height, the kind of spirits, such as "Rye Whisky," "Rum," "Gin," etc., the real name of the actual bona fide distiller or of the individual, firm, partnership, corporation, or association in whose name the spirits were produced and warehoused, the registry number and location (city or town and State) of the

distillery at which the spirits were produced, and the season and year of production and bottling. The word "Inspected," followed by the date of inspection, shall also be marked on each case in letters and figures not less than one-fourth of an inch in height. Where the spirits are taxpaid and removed directly from the bottling-in-bond department, the word "Taxpaid," in letters not less than one-half inch in height, and the date the stamps were canceled and surrendered, and the name of the storekeeper-gauger supervising the removal of the spirits from the bottling-in-bond department, and his title, in letters and figures not less than one-fourth inch in height, shall be marked on the Government side of the case. All marks on cases, which are embossed, printed, or stenciled, must be made with a permanent ink in a color distinctly in contrast to the color used as a background. No marks, brands, labels, caution notices, or other devices whatever, other than those required by law and this part will be permitted on the Government side of the case: *Provided*, That the Assistant District Commissioner,[1] upon written application from the proprietor, may authorize for commercial identification purposes, the affixing of bottle labels or other concise data descriptive of the contents of the case, including indications of payment of State taxes thereon or symbols, in lieu thereof, so describing the contents: *Provided further*, Such additional information is set apart from and does not in any way detract from, conflict with, or obscure any of the markings required to be placed thereon by this part. (53 Stat. 342 as amended, 343, 375; 26 U. S. C. 2903, 2904, 3176.)

2. The purpose of the amendment is to permit the warehouseman to affix bottle labels or concise data descriptive of the contents of the case, including indications of payment of State taxes, or symbols in lieu thereof, on the Government side of cases, provided such additional information does not conflict with, or detract from, the prescribed marks on such side of the case.

3. It is found that compliance with the notice, public rulemaking procedure, and effective date requirements of the Administrative Procedure Act (5 U. S. C. 1001, et seq.) is unnecessary in connection with the issuance of these regulations for the reason that the change made is of a liberalizing character.

4. This Treasury Decision shall be effective upon the date of publication in the Federal Register.

(This Treasury Decision is issued under the authority contained in 53 Stat. 342 as amended, 343, 375; 26 U. S. C. 2903, 2904, 3176).

O. Gordon Delk,
Acting Commissioner of Internal Revenue.

Approved June 11, 1953.

M. B. Folsom,
Acting Secretary of the Treasury.

(Published in the Federal Register June 16, 1953)

Regulations 13, Section 175.34: Indicia for domestic liquor bottles. (Also Sections 175.33, 175.43, 175.55, 175.56, 175.56a, 175.57, 175.57a, 175.59a, 175.89, 175.90, 175.94, 175.94a, 175.95, 175.115.) T. D. 6053

[1] Pursuant to Reorganization Plan No. 1 of 1952 (17 F. R. 2243) the office of district supervisor has been abolished and the office of Assistant District Commissioner, Alcohol and Tobacco Tax, created in place thereof.

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER C, PART 175.—TRAFFIC IN CONTAINERS OF DISTILLED SPIRITS

Amendment of requirements for marking liquor bottles and earthenware containers, labeling distilled spirits, and disposing of marked containers.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

On August 6, 1953, notice of proposed rulemaking, regarding amendments to Regulations 13 [26 CFR, pt. 175], relating to the requirements for marking liquor bottles and earthenware containers, labeling spirits and disposing of marked containers was published in the Federal Register (18 F. R. 4626). After consideration of all such relevant matter as was presented by interested persons relating to the rules proposed, the amendments to Regulations 13 set forth below are hereby adopted:

PARAGRAPH 1. Section 175.33 is amended by striking the word "Commissioner" and inserting in lieu thereof "assistant regional commissioner, or the Commissioner in the case of States,".

PAR. 2. Section 175.34 is amended as follows:

(A) By striking the word "Commissioner" in item (*c*) and inserting in lieu thereof "assistant regional commissioner, or by the Commissioner in the case of symbols and numbers assigned to States,".

(B) By striking the proviso and substituting in lieu thereof the following proviso:

Provided, That (*a*) liquor bottles which are ascertained by the Commissioner to be of distinctive shape or design for the packaging of liqueurs, cordials, bitters, cocktails, gin fizzes, and such other specialties as may be specified from time to time by the Commissioner, and (*b*) liquor bottles for the packaging of other distilled spirits authorized by the Commissioner under section 175.56a, may be manufactured and shipped, consigned, or delivered not marked as required by this section.

PAR. 3. Section 175.43 is amended to read as follows:

On labels of domestic distilled spirits, there shall be stated the phrase "Bottled by", immediately followed by the name of the bottler or the trade name under which the spirits are bottled, and the place where such spirits are bottled. If the bottler is the actual bona fide operator of more than one bottling plant engaged in bottling the same brand of distilled spirits, there may be stated immediately following the name (or trade name) of such bottler the addresses of the plants at which such product is bottled: *Provided*, That on labels of whisky and straight whisky there shall be stated the State of distillation of such whisky, if such whisky is not distilled in the State given in the address of the brand label: *Provided further*,

(*a*) That, where distilled spirits are bottled by or for the distiller thereof, there may be stated, in lieu of the phrase "Bottled by", followed by the bottler's name (or trade name) and address, the phrase "Distilled by", followed by the name (or trade name) under which the particular spirits were distilled, and the address (or addresses) of the distiller;

(*b*) That, where distilled spirits are bottled by or for the rectifier thereof, there may be stated, in lieu of the phrase "Bottled by", followed by the bottler's name (or trade name) and address, the phrase "Blended by", "Made by", "Prepared by", "Manufactured by", or "Produced by" (whichever may be appropriate to the act of rectification involved), followed by the name (or trade name) under which the distilled spirits were rectified, and the address (or addresses) of the rectifier;

(c) That, on labels of distilled spirits bottled for a retailer or other person who is not the actual distiller or rectifier of such distilled spirits there may also be stated the name and address of such retailer or other person, immediately preceded by the words "Bottled for" or "Distributed by", or other similar statement.

PAR. 4. The headnote to subpart E is amended to read as follows:

SUBPART E. USE OF CONTAINERS FOR PACKAGING DISTILLED SPIRITS

PAR. 5. Section 175.55 is amended to read as follows:

The use for packaging distilled spirits for sale at retail of containers of one-half pint capacity or greater, not marked as prescribed by this part, is prohibited except as provided in sections 175.56–175.58.

PAR. 6. Section 175.56 and headnote are amended to read as follows:

SEC. 175.56. DISTINCTIVE LIQUOR BOTTLES FOR LIQUEURS AND CORDIALS.—Upon application (Form 98) by any bottler, the assistant regional commissioner of the region in which the plant of such bottler is situated may, by the issuance of an appropriate permit, authorize the procurement and use by such bottler of liquor bottles which are ascertained by the Commissioner to be of distinctive shape or design for the packaging of liqueurs, cordials, bitters, cocktails, gin fizzes, and such other specialties as may be specified from time to time by the Commissioner, not marked as required by section 175.34.

PAR. 7. There is inserted immediately following section 175.56 the following new section:

SEC. 175.56a. UNMARKED LIQUOR BOTTLES FOR OTHER DISTILLED SPIRITS.—Upon application (Form 98) by any bottler, the assistant regional commissioner of the region in which the plant is situated may, by the issuance of an appropriate permit, authorize the procurement and use by such bottler, for the packaging of distilled spirits such as whisky, brandy, rum, gin, vodka, etc., of liquor bottles, not marked as required by section 175.34, which the Commissioner finds will not afford a jeopardy to the revenue because of their unique or distinctive shape or design and cost of manufacture.

PAR. 8. Section 175.57 is amended to read as follows:

Upon application (Form 98) by any bottler, the assistant regional commissioner of the region in which the plant of such bottler is situated may, by the issuance of an appropriate permit, authorize the procurement and use, for packaging distilled spirits, of earthenware containers marked legibly, by underglaze coloring, (*a*) either on the bottom or on the body with a symbol and number assigned by the assistant regional commissioner, or by the Commissioner in the case of symbols and numbers assigned to States, to represent the name of the bottler procuring the same; and (*b*) on the shoulder with the words, "Federal Law Forbids Sale or Reuse of This Bottle:" *Provided*, That upon application (Form 98) by any bottler, the assistant regional commissioner of the region in which the plant is situated may, by the issuance of an appropriate permit, authorize the procurement and use by such bottler for the packaging of distilled spirits such as whisky, brandy, rum, gin, vodka, etc., of earthenware containers, not marked as required by this section, which the Commissioner finds will not afford a jeopardy to the revenue because of their unique or distinctive shape or design and cost of manufacture.

PAR. 9. There is inserted immediately following section 175.57 the following new section:

SEC. 175.57a. APPROVAL OF DISTINCTIVE UNMARKED CONTAINERS.—Application in letter form for the approval of any distinctive container, accompanied by a specimen, photograph or drawing of the container, and in the case of any such container for the packaging of distilled spirits such as whisky, brandy, rum, gin, vodka, etc., a statement of the cost of manufacture shall be submitted to the Commissioner and approval procured, prior to submission of an application (Form 98) to the assistant regional commissioner. Such application (Form 98) shall specify the number of the container assigned by the Commissioner.

PAR. 10. There is inserted immediately following section 175.59 the following new section:

SEC. 175.59a. USE OF EARTHENWARE CONTAINERS BEARING THE SAME INDICIA, BY PARENT COMPANY AND WHOLLY-OWNED SUBSIDIARIES.—Any bottler authorized to bottle distilled spirits at more than one location may select, for marking on earthenware containers, any one permit symbol and number assigned to him, or to any of his wholly-owned subsidiaries, for use by him and at any or all of the premises of his wholly-owned subsidiaries at which distilled spirits are bottled. The bottler shall notify the Commissioner of such selection. Application (Form 98) filed by the bottler pursuant to section 175.57 for the procurement and use of earthenware containers shall give the location or locations to which such containers are to be shipped. Stocks of earthenware containers bearing such selected indicia held by the parent company or any of its wholly-owned subsidiaries may be transferred between such premises without obtaining a permit authorizing such transfer; however, earthenware containers bearing any symbol and number other than the selected indicia, may not be so transferred without first obtaining a permit from the assistant regional commissioner.

PAR. 11. There is inserted immediately preceding section 175.89 the following new undesignated center head: "Importation of Filled Containers."

PAR. 12. Section 175.89 and headnote are amended to read as follows:

SEC. 175.89. IMPORTATION OF DISTILLED SPIRITS IN UNMARKED CONTAINERS.—No distilled spirits for sale at retail may be imported into the United States in containers of one-half pint capacity or greater, not marked as prescribed by this part: *Provided*, That upon application (Form 98) by the importer, the assistant regional commissioner of the region in which the port of entry is situated may, by the issuance of an appropriate permit, authorize the importation of liquor bottles or earthenware containers containing distilled spirits such as whisky, brandy, rum, gin, vodka, etc., not marked as prescribed by this part, which the Commissioner finds will not afford a jeopardy to the revenue because of their unique or distinctive shape or design and cost of manufacture. The provisions of this section shall not apply to the importation of distilled spirits in bulk containers of a capacity of 5 wine gallons or greater.

PAR. 13. The undesignated center head immediately preceding section 175.90 which reads "Indicia for Imported Filled Containers" is revoked.

PAR. 14. Section 175.90 is amended by striking the words "sections 175.91–175.94" and inserting in lieu thereof "sections 175.89, 175.91–175.94, and 175.95."

PAR. 15. Section 175.94 is amended to read as follows:

Upon application (Form 98) the assistant regional commissioner of the region in which the port of entry is situated may issue a permit authorizing the importation of distilled spirits in earthenware containers marked legibly in underglaze coloring (*a*) either on the bottom or on the body with the name, and the name of the city or country of address, of the manufacturer of the spirits, or of the exporter abroad, or the name, and the name of the city of address, of the importer in the United States, and (*b*) on the shoulder with the words "Federal Law Forbids Sale or Reuse of This Bottle," except as provided in sections 175.89 and 175.95.

PAR. 16. There is inserted immediately following section 175.94 the following new section:

SEC. 175.94a. APPROVAL OF DISTINCTIVE UNMARKED CONTAINERS.—Approval of distinctive unmarked containers shall be prepared in accordance with the procedure prescribed by section 175.57a.

PAR. 17. Section 175.95 is amended by changing the period at the end of the first sentence to a colon and adding the following:

Provided, That upon application (Form 98) the assistant regional commissioner of the region in which the port of entry is situated may, in nonrecurring cases, authorize the release from customs custody of distilled spirits in containers which, through unintentional error, are not marked completely in accordance with the provisions of this part, if the Commissioner finds that such release will not afford a jeopardy to the revenue.

PAR. 18. Section 175.115 is amended to read as follows:

When the permit of a bottle manufacturer or bottler is suspended, revoked, or surrendered, stocks of liquor bottles and other authorized marked containers on hand or in process may be disposed of under permit to a person authorized to receive liquor bottles, in accordance with the directions of the Commissioner. Application shall be made on Form 98 by such person for permission to acquire the entire stock, regardless of place of storage or persons or concerns holding title thereto, and submitted to the assistant regional commissioner of the region in which the applicant is located: *Provided*, That, where it is found that the entire stock cannot be disposed of to one authorized bottler, the Commissioner may authorize the disposal of such containers, in lots, by size or type, to more than one bottler if he finds that such authorization will not afford a jeopardy to the revenue. The application on Form 98 shall be supported by a statement filed by the vendor setting forth whether the Form 98 covers his entire stock, or his entire stock of a particular size or type of bottle. A sample of each size or type of container represented in the stock which the applicant or applicants desire to purchase shall be submitted to the assistant regional commissioner with the application Form 98 and the supporting statement of the vendor. If such stocks are not disposed of in accordance with the directions of the Commissioner, they shall be seized and forfeited, as provided in section 2871 of the Internal Revenue Code.

PAR. 19. The footnote to the source of sections 175.1 to 175.131, which reads "Sections 175.60, 175.62, 175.63, 175.74, 175.75, 175.76, 175.77, 175.78, 175.96 and 175.122 appearing herein are amendments effective only during the period of the unlimited national emergency proclaimed by the President on May 27, 1941 (Proc. 2519; 3 CFR 1943 Cum. Supp.). Upon termination of the unlimited national emergency these amendments will be automatically revoked and the regulations, as they existed prior to the issuance of Treasury Decision 5292, shall be reissued.", is revoked.

These regulations shall be effective upon the date of publication in the Federal Register.

(This Treasury Decision is issued under the authority contained in secs. 2871 and 3170 of the Internal Revenue Code (53 Stat. 331, 373 as amended; 26 U. S. C. 2871, 3170).)

M. B. FOLSOM,
Acting Secretary of the Treasury.

November 23, 1953.

(Published in the Federal Register, November 28, 1953)

(Also Section 3285, Section 325.21; Section 3290, Section 325.42, Regulations 132.) Rev. Rul. 264

INTERNAL REVENUE CODE

Automobiles containing property that is used or intended for use in connection with operations which are in violation of the wagering tax law (ch. 27A of the Internal Revenue Code) are subject to seizure and forfeiture by the Federal Government under section 3116 of the Code.

Advice is requested whether automobiles containing lottery paraphernalia which are owned and operated by lottery operators who have not paid the required wagering tax are subject to seizure and forfeiture by the Federal Government.

The provisions of the Internal Revenue Code imposing the taxes on wagering do not contain any specific reference to seizures or forfeitures. However, authority for seizure by the Federal Government of property intended for use in violation of the internal revenue laws is contained in section 3116 of the Code which provides as follows:

> It shall be unlawful to have or possess any liquor or property intended for use in violating the provisions of this part, or the internal-revenue laws, or regulations prescribed under such part of laws, or which has been so used, and no property rights shall exist in any such liquor or property. A search warrant may issue as provided in title XI of the Act of June 15, 1917, 40 Stat. 228 (U. S. C., title 18, §§ 611–633), for the seizure of such liquor or property. Nothing in this section shall in any manner limit or affect any criminal or forfeiture provision of the internal-revenue laws, or of any other law. The seizure and forfeiture of any liquor or property under the provisions of this part, and the disposition of such liquor or property subsequent to seizure and forfeiture, or the disposition of the proceeds from the sale of such liquor or property, shall be in accordance with existing laws or those hereafter in existence relating to seizures, forfeitures, and disposition of property or proceeds, for violation of the internal-revenue laws.

Although section 3116 of the Code appears in the subchapter of the Code relating to industrial alcohol, its authorization for forfeitures and seizures of liquor or property intended for use in violation of internal revenue laws is not limited only to violations of internal revenue laws governing industrial alcohol. The leading case setting forth this principle is *United States* v. *3935 Cases of Distilled Spirits*, 55 Fed. Supp. 84, which involved property that was seized under section 3116 of the Code for violation of the wholesale liquor tax law. The claimant contended that section 3116 was not intended to include all violations of the internal revenue laws, but was limited to violations involving industrial alcohol. This contention was rejected by the court and after quoting from the legislative history of section 3116 of the Code, it concluded with respect thereto that "These reports plainly and unequivocally refer to the internal revenue laws generally and are not confined to those which have to do with industrial alcohol. * * * The phrase 'internal revenue laws' and 'regulations prescribed under such * * * laws' of course refer to internal revenue laws, and since no qualification is made to the effect that only *some* internal revenue laws are meant, the plain and literal meaning of the section is that the violation or the intended violation of *any* valid internal revenue law or regulation gives rise to operation of section 3116."

The principle set forth in the above case has been consistently followed in other cases involving this issue. See *Anderson* v. *United States*, 185 Fed. (2d) 343; *One Ford Tudor Automobile, 1946 Model, Motor No. 99A1229317* v. *United States*, 164 Fed. (2d) 1020 (imposition of penalties by other sections of the Code does not prevent forfeitures under section 3116 of the Code); *United States* v. *Windle*, 158 Fed. (2d) 196; and *United States* v. *One 1942 Pontiac Sedan Automobile et al.*, 56 Fed. Supp. 929.

In view of the foregoing, it is held that automobiles containing property that is used or intended for use in connection with operations which are in violation of the wagering tax law (ch. 27A of the Internal

Revenue Code) are subject to seizure and forfeiture by the Federal Government under section 3116 of the Code.

MISCELLANEOUS REGULATIONS RELATING TO LIQUOR, SECTION 171.2: Basic permit procedure under Federal Alcohol Administration Act. Rev. Rul. 148*

INTERNAL REVENUE CODE

Cancellation of requirement to file applications for new basic permits under the Federal Alcohol Administration Act to cover changes in location.

Rev. Rul. 37, C. B. 1953–1, 444, revoked.

1. *Purpose.*—The purpose of this Revenue Ruling is to rescind Rev. Rul. 37, C. B. 1953–1, 444, which required the filing of applications for new basic permits under the Federal Alcohol Administration Act to cover changes in location.

2. *Procedure Now Applicable.*—Form 1643, "Application for Amended Basic Permit Under the Federal Alcohol Administration Act," will again be used to report changes of location of holders of permits under the Federal Alcohol Administration Act, as it was prior to the issuance of Revenue Ruling No. 37. This change in procedure is being made because of administrative and enforcement difficulties encountered as a result of Revenue Ruling No. 37.

3. *Correspondence.*—Any correspondence relative to this Revenue Ruling should refer to the number and date thereof and to the symbols O:AT:BP.

* Originally issued as IR Mimeograph No. 181, dated May 8, 1953.

MISCELLANEOUS REGULATIONS RELATING TO LIQUOR, SECTION 171.176: Distilled spirits. Rev. Rul. 205*

INTERNAL REVENUE CODE

National emergency transfers of distilled spirits

1. This Revenue Ruling prescribes detailed reporting procedure for transactions authorized by Treasury Decision 5864, C. B. 1951–2, 248, as amended by Treasury Decision 6005, C. B. 1953–1, 445, concerning national emergency transfers of distilled spirits. The term "Treasury Decision" when used without a number in this Revenue Ruling shall mean Treasury Decision 5864, as amended by Treasury Decision 6005.

2. The Treasury Decision authorizes:

(*a*) Additional types of transfers in bond and removable from bonded premises as:

(1) Transfers in bond from registered and fruit distilleries and internal revenue bonded warehouses to industrial alcohol plants and bonded warehouses,

(2) Transfers in bond from industrial alcohol plants and bonded warehouses to registered and fruit distilleries and internal revenue bonded warehouses, and

*Originally issued at IR-Mimeograph 198, dated June 5, 1953.

(3) Removals of distilled spirits produced at registered and fruit distilleries, if of a proof of 160° or more, from an industrial alcohol plant or bonded warehouse for any tax-free purpose, or upon payment of tax for any purpose, authorized by part II of subchapter C, or from any distillery or internal revenue bonded warehouse for any purpose authorized by part II of subchapter C or for any purpose authorized in the case of like spirits produced at a distillery; and

(*b*) Temporary storage of distilled spirits and alcohol at registered and fruit distilleries and industrial alcohol plants.

In order that details of reporting such transactions may be uniform and that necessary statistics may be made available, the following reporting procedure is prescribed, supplementing that prescribed by the Treasury Decision and Regulations 3, 4, 5, and 10.

3. The term "distilled spirits" is defined in section 171.176 of the Treasury Decision as follows: "'Distilled spirits' or 'spirits' shall include alcohol, but not those beverage spirits commonly known as whisky, brandy, rum, gin, etc., or other beverage spirits of less than 160° of proof, except when removed for redistillation or for storage pending redistillation." However, for the purpose of clarity in reporting such distilled spirits, the term "distilled spirits," as used herein, represents only the production of registered and fruit distilleries, and the term "alcohol," as used herein, represents the production of an industrial alcohol plant.

REGISTERED DISTILLERIES

4. *Removals.*—(*a*) *Distiller's report.*—Distilled spirits produced at a registered distillery and removed therefrom for any purpose authorized by the Treasury Decision but not covered by Form 1598, will be reported on such form in part 2, "Statement of Withdrawals." The purpose of removal, as, for example, "Transferred to industrial alcohol plant," "Removed for use of United States," etc., will be reported in column 15 or 16. Such transactions summarized for the month will be entered in part 3, section 4, "Summary of Withdrawals," using blank lines and interlining as may be necessary.

(*b*) *Statistical report.*—The assistant district commissioner will include in his monthly statistical report, Form 1554–A, additional items reported on Form 1598, using blank lines and interlining as may be necessary.

5. *Temporary storage.*—Transactions concerning distilled spirits and alcohol received at a registered distillery for temporary storage pursuant to section 171.231, must be reported separately from distilled spirits produced at the distillery and therefore will not be reported by the distiller on Form 1598 or by the storekeeper-gauger on Form 1686. Such transactions will be reported as follows:

(*a*) *Distiller's report.*—The receipts, removals, and stocks of distilled spirits and alcohol will be reported by the distiller on Form 1443–A revised to read "Report of Distilled Spirits and Alcohol Stored Temporarily at Registered Distillery." Receipts will be reported on part 1 and removals on part 2. Such transactions will be summarized for the month in part 2, section 2, "Summary," using blank lines and interlining as may be neces-

sary. The distiller will prepare Form 1443–A in triplicate. He will submit them with Form 1598 to the storekeeper-gauger.

(*b*) *Storekeeper-gauger's record.*—The storekeeper-gauger will maintain a record on Form 1621 of distilled spirits and alcohol stored temporarily at the distillery in order that he may insure the distiller's proper marking of such distilled spirits and alcohol removed therefrom and verify the total receipts and removals during the month and the quantity on hand at the end of the month as reported by the proprietor on Form 1443–A. After verification of Form 1443–A he will initial all three copies, submit the original and one copy with Form 1598 to the assistant district commissioner, and return the remaining copy to the proprietor.

(*c*) *Statistical report.*—The assistant district commissioner will prepare a special statistical report on Form 1554–A. The title will be revised to read "Statistical Report of Distilled Spirits and Alcohol Stored Temporarily at Registered Distilleries." All of the transactions reported in part 2, section 2, of Form 1443–A will be reported on Form 1554–A, using blank lines and interlining as may be necessary.

FRUIT DISTILLERIES

6. *Removals.*—(*a*) *Distiller's report.*—Distilled spirits produced at a fruit distillery and removed therefrom for any purpose authorized by the Treasury Decision but not covered by Form 15, will be reported on such form in part 2, "Statement of Withdrawals." The purpose of removal, as, for example, "Transferred to industrial alcohol plant," "Removed for use of United States," etc., will be reported in column 15 or any other available column. Such transactions summarized for the month will be entered in part 3, section 7, "Statement of Production and Withdrawals," using blank lines and interlining as may be necessary.

(*b*) *Statistical report.*—The assistant district commissioner will include in his monthly statistical report, Form 1554, additional items reported on Form 15, using blank lines and interlining as may be necessary.

7. *Temporary storage.*—Transactions concerning distilled spirits and alcohol received at a fruit distillery for temporary storage pursuant to section 171.231, must be reported separately from distilled spirits produced at the distillery and therefore will not be reported by the distiller on Form 15. Such transactions will be reported as follows:

(*a*) *Distiller's report.*—The receipts, removals, and stocks of distilled spirits and alcohol will be reported by the distiller on Form 1443–A revised to read "Report of Distilled Spirits and Alcohol Stored Temporarily at Fruit Distillery." Receipts will be reported on part 1 and removals on part 2. Such transactions will be summarized for the month in part 2, section 2, "Summary," using blank lines and interlining as may be necessary. The distiller will prepare Form 1443–A in triplicate. He will submit them to the storekeeper-gauger at the adjoining internal revenue bonded warehouse. After verification by the storekeeper-gauger as provided in paragraph (*b*), he will submit the original and one copy with Form 15 to the assistant district commissioner.

(*b*) *Storekeeper-gauger's record.*—The storekeeper-gauger at the adjoining internal revenue bonded warehouse will maintain a record on Form 1621 of distilled spirits and alcohol stored temporarily at the distillery in order that he may insure the distiller's proper marking of such distilled spirits and alcohol removed therefrom and verify the total receipts and removals during the month and the quantity on hand at the end of the month as reported by the distiller on Form 1443–A. After verification of Form 1443–A, he will initial all three copies and return them to the distiller.

(*c*) *Statistical report.*—The assistant district commissioner will prepare a special statistical report on Form 1554. The title will be revised to read "Statistical Report of Distilled Spirits and Alcohol Stored Temporarily at Fruit Distilleries." All of the transactions reported in part 2, section 2, of Form 1443–A will be reported on Form 1554, using blank lines and interlining as may be necessary.

INTERNAL REVENUE BONDED WAREHOUSES

8. (*a*) *Storekeeper-gauger's report.*—Distilled spirits and alcohol received at and removed from internal revenue bonded warehouses will be reported by the storekeeper-gauger on Forms 1621 and 1699, using blank lines and interlining as may be necessary.

(*b*) *Statistical report.*—The audit clerk in the office of the assistant district commissioner will report transactions covering distilled spirits and alcohol received at and removed from internal revenue bonded warehouses on Form 1700, in the manner prescribed by such form.

INDUSTRIAL ALCOHOL PLANTS

9. *Removals.*—(*a*) *Proprietor's report.*—Alcohol produced at an industrial alcohol plant and removed therefrom for any purpose authorized by the Treasury Decision but not covered by Form 1442, will be reported on such form in part 2, "Statement of Withdrawals." The purpose of removal, as, for example, "Transferred to registered distillery," will be reported in column 18. Such transactions summarized for the month will be entered in part 3, section 4, "Summary of Withdrawals," using blank lines and interlining as may be necessary.

(*b*) *Statistical report.*—The assistant district commissioner will include in his monthly statistical report, Form 1555, additional items reported on Form 1442, using blank lines and interlining as may be necessary.

10. *Temporary storage.*—Transactions concerning distilled spirits and alcohol received at an industrial alcohol plant for temporary storage pursuant to section 171.248, must be reported separately from alcohol produced at the plant and therefore will not be reported by the proprietor on Form 1442 or by the storekeeper-gauger on Form 1686. Such transactions will be reported as follows:

(*a*) *Proprietor's report.*—The receipts, removals, and stocks of distilled spirits and alcohol will be reported by the proprietor on Form 1443–A revised to read "Report of Alcohol Stored Temporarily at Industrial Alcohol Plant." Receipts will be reported on part 1 and removals on part 2. Such transactions will be summarized for the month in part 2, section 2, "Summary," using

blank lines and interlining as may be necessary. The proprietor will prepare Form 1443–A in triplicate. He will submit them with Form 1442 to the storekeeper-gauger.

(*b*) *Storekeeper-gauger's record.*—The storekeeper-gauger will keep such memoranda records of the distilled spirits and alcohol received for temporary storage as will enable him to verify the total receipts and removals during the month and the quantity on hand at the end of the month as reported by the proprietor of the industrial alcohol plant on Form 1443–A. After verification of Form 1443–A, he will initial all three copies, submit the original and one copy with Form 1442 to the assistant district commissioner, and return the remaining copy to the proprietor.

(*c*) *Statistical report.*—The assistant district commissioner will prepare a special statistical report on Form 1555. The title will be revised to read "Statistical Report of Alcohol Stored Temporarily at Industrial Alcohol Plants." All of the transactions reported in part 2, section 2, of Form 1443–A will be reported on Form 1555, using blank lines and interlining as may be necessary.

INDUSTRIAL ALCOHOL BONDED WAREHOUSES

11. (*a*) *Proprietor's report.*—Distilled spirits and alcohol received at and removed from industrial alcohol bonded warehouses will be reported by the proprietor on his regular monthly reports, Forms 1443–A and 1443–B. Receipts and removals authorized by the Treasury Decision but not covered by such forms will be reported in parts 1 and 2, respectively. The purpose of removal, as, for example, "Transferred to Internal Revenue Bonded Warehouses," will be reported in available columns. Such transactions will be summarized for the month in part 2, section 2, "Summary," of the forms, using blank lines and interlining as may be necessary.

(*b*) *Storekeeper-gauger's record.*—Distilled spirits and alcohol received at and removed from industrial alcohol bonded warehouses will be reported by storekeeper-gaugers on their memoranda records prescribed by Regulations 3 for alcohol received at and removed from such premises.

(*c*) *Statistical report.*—The assistant district commissioner will include in his monthly statistical report, Form 1555–A, additional items reported on Forms 1443–A and 1443–B, in the manner prescribed by Form 1555–A.

COPIES OF REPORTS FOR GOVERNMENTAL AGENCIES

12. *General.*—Section 171.279 of the Treasury Decision authorizes the Commissioner to require such additional copies of forms prescribed therein, or such other records, as he may deem necessary to meet the requirements of the national defense. Pursuant to such authorization, additional copies of forms and reports relating to removals of denatured or undenatured distilled spirits and alcohol made by, or for the account of the Reconstruction Finance Corporation, Office of Synthetic Rubber, Materials Procurement, Washington 25, D. C. (hereinafter referred to as the Reconstruction Finance Corporation), will be prepared and disposed of in accordance with the following instructions.

REPORTS FOR RECONSTRUCTION FINANCE CORPORATION

13. *Removals from distilleries and internal revenue bonded warehouses.*—In addition to the forms prescribed by the Treasury Decision covering removals of distilled spirits and alcohol from distilleries and internal revenue bonded warehouses, the storekeeper-gauger will prepare two extra copies of Form 1520 and the proprietor will prepare two extra copies of Form 236, 1704, or 1453, as the case may be. All copies of the forms reporting shipments from each type of premises for the Reconstruction Finance Corporation will be serially numbered in the upper right hand corner beginning with "1" for the first report of each calendar year, except that, where forms are required by regulations or the instructions on the form to be serially numbered, a separate series of numbers for the Reconstruction Finance Corporation will be placed above other required serial numbers. The serial numbers used for the Reconstruction Finance Corporation will be identified by preceding them with the symbol "RFC." Each extra copy of the forms will be marked "Copy for Reconstruction Finance Corporation." The storekeeper-gauger will give one of the extra copies of Form 236, 1704, or 1453, with one of the extra copies of Form 1520 attached, to the proprietor to send to the Reconstruction Finance Corporation. The storekeeper-gauger will send the remaining extra copy of Form 236 or 1704, with Form 1520 attached thereto, to the storekeeper-gauger at the consignee's premises. The remaining extra copy of Form 1453, with attached Form 1520, will be sent to the consignee. Upon receipt of the distilled spirits or alcohol transferred pursuant to Form 236, the storekeeper-gauger at the consignee's premises will execute his certificate of receipt on the extra copy of Form 236 marked for the Reconstruction Finance Corporation and deliver it, with the attached marked extra copy of Form 1520, to the proprietor, who will forward them to the Reconstruction Finance Corporation. Upon receipt of distilled spirits transferred pursuant to Form 1704, the consignee proprietor will execute his certificate of receipt on the extra copy of Form 1704 marked for the Reconstruction Finance Corporation and will give it, with the attached marked extra copy of Form 1520, to the storekeeper-gauger who will note his verification, followed by his signature and title in the lower left hand portion of Form 1704. The storekeeper-gauger will then return the extra copy of Form 1704, with Form 1520 attached, to the proprietor who will forward them to the Reconstruction Finance Corporation. Upon receipt of distilled spirits or alcohol described on Form 1453, the consignee will execute his certificate of receipt on the extra copy of the form marked for the Reconstruction Finance Corporation and send it, with the attached marked extra copy of Form 1520, to the Reconstruction Finance Corporation.

14. *Removals from industrial alcohol plants, bonded warehouses, and denaturing plants.*—In addition to the forms prescribed by the Treasury Decision covering transfers in bond and other removals from industrial alcohol plants, bonded warehouses, and denaturing plants, the proprietor will prepare two extra copies of Form 1440, 1453, 1453–A, 1467, or 1473, as the case may be. All copies of the forms reporting shipments from each type of premises for the Reconstruction Finance Corporation will be serially numbered beginning with "1" for the

first report for each calendar year. The serial numbers will be placed on the forms in the upper right hand corner preceded by the symbol "RFC." Each extra copy of the forms will be marked "Copy for Reconstruction Finance Corporation."

(*a*) *Removals from industrial alcohol plants and bonded warehouses.*—The proprietor will submit to the storekeeper-gauger all copies of Form 1440 covering transfers in bond of alcohol to other bonded premises and removals of alcohol to denaturing plants. He will submit to the storekeeper-gauger all copies of Forms 1440 and 1453 covering removals tax-free for the use of the United States. The storekeeper-gauger will endorse on the front of the extra copies of the forms the word "verified" followed by his name and title. He will return one each of the extra copies to the proprietor to transmit to the Reconstruction Finance Corporation. He will send the remaining extra copy of Form 1440, or Forms 1440 and 1453, to the storekeeper-gauger at the receiving premises or to the consignee, as the case may be. Upon receipt of alcohol covered by Form 1440, the consignee proprietor will execute his record of receipt on the extra copy of Form 1440 marked for the Reconstruction Finance Corporation and will submit the form to the storekeeper-gauger who will note thereon the word "verified" followed by his name and title. The storekeeper-gauger will return such extra copy of Form 1440 to the proprietor who will forward it to the Reconstruction Finance Corporation. Upon receipt of alcohol covered by Form 1453, the consignee will execute his certificate of receipt on the extra copy of the form marked for the Reconstruction Finance Corporation and send it with the attached marked extra copy of Form 1440 to the Reconstruction Finance Corporation.

(*b*) *Removals from denaturing plants.*—The disposition of copies of Form 1440 covering transfers of alcohol between denaturing plants, and copies of Forms 1440 and 1453 covering removals from denaturing plants of alcohol, tax-free, for use of the United States, will be in accordance with the provisions of paragraph (*a*) above. In the case of transfers of denatured alcohol to another denaturing plant, the proprietor will submit to the storekeeper-gauger all copies of Forms 1467 and 1473. The storekeeper-gauger will endorse on the front of the extra copies of the forms the word "verified" followed by his name and title. He will return one each of the extra copies to the proprietor to transmit to the Reconstruction Finance Corporation. The storekeeper-gauger will send the remaining extra copies of such forms to the storekeeper-gauger in charge of the receiving denaturing plant. Upon receipt of the denatured alcohol covered by Forms 1467 and 1473, the consignee proprietor will execute his certificate of receipt on the extra copy of the Form 1473 marked for the Reconstruction Finance Corporation and will submit the form to the storekeeper-gauger, who will note thereon the word "verified" followed by his name and title. The storekeeper-gauger will return the extra copy of Form 1473 to the proprietor who will forward it with the marked extra copy of Form 1467 to the Reconstruction Finance Corporation. In the case of tax-free re-

movals of denatured alcohol for use of the United States covered by Form 1453–A, or removals of denatured alcohol to manufacturers or users thereof covered by Form 1473, as the case may be, the proprietor will submit to the storekeeper-gauger all copies of such forms. The storekeeper-gauger will endorse on the front of the extra copies of the forms the word "verified" followed by his name and title. He will return one each of the extra copies to the proprietor to transmit to the Reconstruction Finance Corporation. The storekeeper-gauger will send the remaining extra copies of such forms to the consignee. Upon receipt of the denatured alcohol covered by Form 1453–A or 1473, as the case may be, the consignee will execute his certificate of receipt on the extra copy of the form marked for the Reconstruction Finance Corporation and forward it to the Reconstruction Finance Corporation.

15. *Withdrawals from customs custody of imported alcohol.*—In addition to the forms prescribed by Regulations 3 covering withdrawals of alcohol from customs custody, two extra copies of Form 1440 will be prepared and marked "Copy for Reconstruction Finance Corporation." The customs officer will forward the extra copies of Form 1440 to the storekeeper-gauger at the consignee's premises, who will note thereon his verification of the quantity of alcohol received, followed by his signature and title. The storekeeper-gauger will deliver the marked extra copies to the proprietor of the consignee premises who will forward them to the Reconstruction Finance Corporation. All copies of Form 1440 reporting receipt from customs custody for the Reconstruction Finance Corporation will be serially numbered by the proprietor in the upper right hand corner of the form beginning with "1" for the first report for each calendar year. The serial numbers will be preceded by the symbol "RFC." In addition, the name of the vessel from which the spirits were unladen will be shown on Form 1440.

16. *Proprietor's monthly report.*—Proprietors of industrial alcohol plants, industrial alcohol bonded warehouses, distilleries, and internal revenue bonded warehouses storing distilled spirits and alcohol, under contract, exclusively for the Reconstruction Finance Corporation, will prepare one extra copy each of the monthly report, Form 1443–A, 1443–B, or 52–C, as the case may be, marked "Copy for Reconstruction Finance Corporation." Proprietors of denaturing plants storing or denaturing alcohol, under contract, exclusively for the Reconstruction Finance Corporation, will prepare one extra copy each of Forms 1468–A, 1468–B, 1468–C, 1468–D, and 1468–E marked "Copy for Reconstruction Finance Corporation." The extra copies of the reports will be submitted to the storekeeper-gauger who will note his verification thereon, followed by his name and title. The extra copies will then be forwarded by the proprietor to the Reconstruction Finance Corporation.

OTHER GOVERNMENTAL AGENCIES

17. *General.*—Upon request submitted to the Revenue Service by any governmental agency, the Commissioner will issue instructions relative to the preparation and disposition of additional copies of forms and records relating to transactions in distilled spirits and alcohol.

ADDITIONAL INSTRUCTIONS CONCERNING REMOVALS FOR RECONSTRUCTION FINANCE CORPORATION

PIPELINES

18. *Flexible hose.*—Pipelines conforming to the requirements of Regulations 3 (26 CFR, pt. 182) or 10 (26 CFR, pt. 185), as the case may be, shall be used for the filing of approved conveyances of unpackaged denatured or undenatured distilled spirits and alcohol, except the spirits may be transferred to such conveyances by means of flexible hose where the entire length thereof is in full view of the storekeeper-gauger.

INSPECTION PRIOR TO FILLING OF TANK CARS, TANK TRUCKS, TANK BARGES, ETC.

19. *Procedure.*—Approved conveyances which are to be used for shipping unpackaged denatured or undenatured distilled spirits or alcohol, and approved pipelines and flexible hoses used in connection with the transfer of denatured or undenatured distilled spirits and alcohol to and from storage tanks, weighing tanks, and approved conveyances, shall be clean and free of any foreign substance which would contaminate the spirits to be deposited or conveyed therein. Storekeeper-gaugers will make inspections for cleanliness in the case of tank cars, tank trucks, tank barges, pipelines, and hoselines which are to be used for the conveyance of denatured or undenatured distilled spirits and alcohol. In addition, the Reconstruction Finance Corporation will, at its option, assign licensed petroleum or other inspectors to make inspections for cleanliness in the case of barges to be used for the conveyance of denatured or undenatured distilled spirits and alcohol. If inspection by the storekeeper-gauger discloses that the vessels are not clean and free from foreign substance likely to contaminate the spirits to be deposited or conveyed therein, the use of such vessels will be prohibited until they are properly cleaned and put in suitable condition: *Provided*, That where the proprietor reports to the Reconstruction Finance Corporation the uncleanliness of a conveyance, it may be used, upon the acceptance of the conveyance in its unclean condition by the Reconstruction Finance Corporation. Such acceptance of an unclean conveyance shall be given, in duplicate, to the storekpeeper-gauger, one copy of which shall be retained by him. The remaining copy of the acceptance will be attached by the storekeeper-gauger to the Form 1520, 1440, or 1467 which is furnished to the assistant district commissioner of the district in which the shipping plant is located. The storekeeper-gauger will also note such information on all copies of Form 1520, 1440, or 1467.

SAMPLES

20. *Samples at point of shipment.*—A representative one-pint sample of unpackaged denatured or undenatured distilled spirits or alcohol will be taken for each conveyance, except that a sample will not be taken when such spirits are transferred by pipeline between plants as provided in section 171.201 of the Treasury Decision. Samples will be taken from the pipeline or hose by the proprietor of the shipping premises in the immediate presence of the storekeeper-gauger at the time the distilled spirits or alcohol are being pumped

into, and prior to their deposit in, the tank car, tank truck, tank barge, or other approved conveyance. An additional representative one-pint sample will also be permitted to be taken from each conveyance in the presence of the storekeeper-gauger by a licensed petroleum or other inspector, where such inspectors are assigned by the Reconstruction Finance Corporation, immediately after the conveyance has been loaded for shipment and prior to its sealing. The samples will be placed in screw top pint glass bottles which will be provided by the shipping proprietor. In no case will cork stoppers be used. Each bottle will be labeled to show the date the sample was taken, the kind of spirits (denatured or undenatured alcohol, neutral spirits, etc.), whether the sample was taken during or after loading, the name and address of the shipper, the kind and registry number of the shipper's plant, the name and address of the consignee, the kind and registry number of the consignee's plant, the name or number of the tank car or barge or the tank truck State license number (trailer license in the case of a tank trailer), as the case may be, the number of wine gallons in the shipment, the proof of the distilled spirits or alcohol, the serial number of Form 1440, 1520, 1467, 236, 1704, 1453, 1453–A, or 1473, as the case may be, and such other information as may be necessary to fully identify the shipment. All samples, after being taken and labeled, shall be placed in the custody of the storekeeper-gauger who shall place his name or initials and title upon the labels and keep the samples under Government lock. Requests to forward the samples taken by the proprietor to a laboratory for analysis will be made by the Reconstruction Finance Corporation. Requests to forward samples taken by an inspector assigned by the Reconstruction Finance Corporation to laboratories for analysis will be made by such inspector with the assent of the Reconstruction Finance Corporation. If no request is received to send such samples to the Alcohol and Tobacco Tax Division Branch Laboratory, or to another laboratory designated by the Reconstruction Finance Corporation, within 60 days, the storekeeper-gauger will dump them into tanks containing similar spirits at the shipping premises. The bottles will be returned to the proprietor for cleaning and reuse when taking other samples.

21. *Samples at point of receipt.*—A representative one-pint sample will be taken from each shipment of unpackaged denatured or undenatured distilled spirits or alcohol received in tank barges. Such samples will be taken by the consignee proprietor in the immediate presence of the storekeeper-gauger, prior to removal of the spirits from the tank barge. The samples will be placed in screw top pint glass bottles which will be provided by the consignee proprietor. In no case will cork stoppers be used. Each bottle will be labeled to show the date the sample was taken, the kind of spirits (denatured or undenatured alcohol, neutral spirits, etc.), the name and address of the consignee, the kind and registry number of the consignee's plant, the name and address of the shipper, the kind and registry number of the shipper's plant, the name of the barge, the number of wine gallons in the shipment, the proof of the distilled spirits or alcohol, the serial number of Form 1440, 1520, 1467, 236, 1704, 1453, 1453–A, or 1473, as the case may be, and such other information as may be necessary to fully identify the shipment. All such samples, after being taken and labeled, shall be placed in the custody of the storekeeper-gauger who shall place his

name or initials and title upon the labels and keep the samples under Government lock. Requests to forward the samples to a laboratory for analysis will be made by the Reconstruction Finance Corporation. If no request is received to send such samples to the Alcohol and Tobacco Tax Division Branch Laboratory, or to another laboratory designated by the Reconstruction Finance Corporation, within 60 days, the storekeeper-gauger will dump them into tanks containing similar spirits at the receiving premises. The bottles will be returned to the proprietor for cleaning and reuse when taking other samples. Additional samples desired by the proprietor for his organoleptic or laboratory examination will be taken in accordance with the provisions of Regulations 3 and 10.

22. *Reports of analysis of samples.*—The Alcohol and Tobacco Tax Division Branch Laboratory analyzing samples of distilled spirits or alcohol will prepare a report of the results of analysis. Each report will be prepared in triplicate and will identify the sample analyzed by showing therein the information appearing on the label affixed to the sample. The original report will be sent immediately to the Reconstruction Finance Corporation, and one copy will be retained by the laboratory. In the case of samples taken at the point of shipment, the remaining copy of the report will be sent to the shipper, and in the case of samples taken at the point of receipt, the copy will be sent to the consignee.

GENERAL INSTRUCTIONS CONCERNING NATIONAL EMERGENCY TRANSFERS OF DISTILLED SPIRITS AND ALCOHOL

REMOVALS TO DISTILLERIES FROM INDUSTRIAL ALCOHOL PLANTS AND BONDED WAREHOUSES

23. *Amended notice, Form 27-A or Form 27½.*—Distillers who desire to withdraw alcohol from industrial alcohol plants and industrial alcohol bonded warehouses as provided in section 171.231 of the Treasury Decision shall file amended notice on Form 27-A or Form 27½, as the case may be, as provided in section 171.258 in accordance with the applicable provisions of Regulations 4 or 5, respectively. The purpose for which notice is filed shall be stated, "To withdraw alcohol from industrial alcohol plants and industrial alcohol bonded warehouses under section 3183 of the Internal Revenue Code." If such alcohol is to be withdrawn for redistillation, the distiller shall list on the notice under kind of material to be used, "Alcohol under section 3183, IRC."

REMOVALS TO INTERNAL REVENUE BONDED WAREHOUSES FROM INDUSTRIAL ALCOHOL PLANTS AND BONDED WAREHOUSES

24. *Amended application, Form 27-D.*—Proprietors of internal revenue bonded warehouses who desire to withdraw alcohol from industrial alcohol plants or industrial alcohol bonded warehouses as provided in section 171.240 of the Treasury Decision shall file amended application on Form 27-D, as provided in section 171.258 in accordance with the applicable provisions of Regulations 10. The purpose for which application is filed shall be stated, "To withdraw alcohol from industrial alcohol plants and industrial alcohol bonded warehouses under section 3183 of the Internal Revenue Code." Proprietors shall also amend their applications by adding the indicated underscored

phrasing thereto, as follows: "Notice is hereby given, that * * * to carry on or engage in the business of warehousing distilled spirits (including alcohol withdrawn under sec. 3183, IRC) * * *."

REMOVALS TO INDUSTRIAL ALCOHOL PLANTS, BONDED WAREHOUSES, AND DENATURING PLANTS FROM DISTILLERIES AND INTERNAL REVENUE BONDED WAREHOUSES

25. *Amended application, Form 1431.*—Proprietors of industrial alcohol plants, industrial alcohol bonded warehouses, or denaturing plants who desire to withdraw distilled spirits from distilleries or internal revenue bonded warehouses as provided in sections 171.248 and 171.260 of the Treasury Decision, shall file application on Form 1431 for amendment of basic permit, Form 1433, as provided in sections 171.251 and 171.261 in accordance with the applicable provisions of Regulations 3. The purpose for which application is filed shall be stated, "For amendment of permit to authorize withdrawals of distilled spirits from distilleries and internal revenue bonded warehouses under section 3183 of the Internal Revenue Code." At line 11, indicated underscoring shall be added as follows: "in accordance with the provisions of sections 3070 to 3125, and 3183, Internal Revenue Code, as amended and supplemented, and regulations promulgated thereunder, etc." If distilled spirits are to be withdrawn for redistillation, the proprietor shall list in the application under kind of material to be used "Distilled spirits under section 3183, IRC."

26. *Amended permit, Form 1433.*—Upon approval of application on Form 1431, the assistant district commissioner shall amend the proprietor's basic permit, Form 1433, as provided in sections 171.251 and 171.261 of the Treasury Decision. At line 8, indicated underscoring shall be added as follows: "in accordance with the terms hereof, and the provisions of sections 3070–3124 and 3183, Internal Revenue Code, as amended and supplemented, and all regulations issued pursuant thereto." In the space following Stipulation 11, and above his signature, the assistant district commissioner shall insert "This permit authorizes the withdrawal of distilled spirits from distilleries and internal revenue bonded warehouses pursuant to section 3183, Internal Revenue Code."

GAUGING OF DISTILLED SPIRITS AND ALCOHOL

27. *Determination of proof.*—The proof of distilled spirits and alcohol shall be determined in accordance with section 171.217 of Treasury Decision 5864 as amended by Treasury Decision 6005.

28. *Gauge by volume.*—In instances where the distilled spirits or alcohol are gauged by volume in tanks, the report of gauge shall show the proof gallon content computed by multiplying the total wine gallons by the proof, extended to tenths of degrees. For example, 4,000 wine gallons at 190.3° of proof would be reported as 7,612.0 proof gallons. When distilled spirits are withdrawn or received on volumetric gauge, the number of wine gallons shall be included in the report of gauge on Form 1520.

29. *Gauge by weight.*—In instances where the distilled spirits or alcohol are gauged in weighing tanks mounted on scales, or by weighing railroad cars on railroad car scales, or by weighing tank trucks on tank truck scales, the proof gallon content shall be computed from Table No. 4 (Revised 1953) of the Gauging Manual. When distilled

spirits are to be received on volumetric gauge, or are withdrawn for tax-free purposes under Treasury Decision 5864, the number of wine gallons shall be included in the shipping report of gauge on Form 1520.

30. Correspondence relative to this Revenue Ruling should refer to the number thereof and the symbols O:AT:PPt.

CHAPTER 27.—OCCUPATIONAL TAXES

SUBCHAPTER A.—SPECIAL PROVISIONS

PART VII.—LIQUOR

SECTION 3250.—TAX

REGULATIONS 29, SECTION 197.21: Claims. T. D. 6044
(Also Sections 197.21a, 197.22, 197.24, 197.25, 197.25a, 197.35, 197.36, 197.37, 197.38, 197.39, 197.40, 197.41, 197.42, 197.43, 197.44, 197.45, 197.46, 197.47, 197.48, 197.49, 197.50, 197.51, 197.52, 197.53, 197.54, 197.55, 197.56, 197.57.)

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER C, PART 197.—DRAWBACK OF TAX ON DISTILLED SPIRITS USED IN THE MANUFACTURE OF NONBEVERAGE PRODUCTS

Amendment of Regulations 29 to permit the filing of claims for drawback on a monthly basis and to make changes of administrative nature.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

Section 3250(1)(5) of the Internal Revenue Code was amended by Public Law 283 (83d Cong.) [p. 484, this Bulletin], to read as follows:

SEC. 3250. TAX. * * *

(1) MANUFACTURERS OR PRODUCERS OF DESIGNATED NONBEVERAGE PRODUCTS.—* * *

* * * * * * *

(5) DRAWBACK.—In the case of distilled spirits taxpaid and used as provided in this subsection, a drawback shall be allowed—

(A) at the rate of $6 on each proof gallon upon which tax is paid at a rate of $9 per proof gallon prior to the effective date of section 462 of the Revenue Act of 1951,

(B) at the rate of $9.50 on each proof gallon upon which tax is paid at a rate of $10.50 per proof gallon on and after the effective date of section 462 of the Revenue Act of 1951, and

(C) at the rate of $8 on each proof gallon upon which tax is paid at a rate of $9 per proof gallon after March 31, 1954.

Such drawback shall be due and payable quarterly upon filing of a proper claim with the Secretary; except that, where any person entitled to such drawback shall elect in writing to file monthly claims therefor, such drawback

shall be due and payable monthly upon filing of a proper claim with the Secretary: *Provided, however,* That the Secretary may require persons electing to file monthly drawback claims to file with him a bond or other security in such amount and with such conditions as he shall by regulations prescribe. Any such election may be revoked upon filing of notice thereof with the Secretary. No claim under this subsection shall be allowed unless filed with the Secretary within the 3 months next succeeding the quarter in which the distilled spirits covered by the claim were used as provided in this subsection.

* * * * * * *

In order to conform Regulations 29 [26 CFR, pt. 197], to such amendment, and to conform the regulations to the delegation to assistant regional commissioners, Alcohol and Tobacco Tax, of final authority for allowance or disallowance of drawback claims, such regulations are amended as follows:

PARAGRAPH 1. Section 197.21 is amended to read as follows:

The claim for drawback shall be filed on Form 843, (original only) with the assistant regional commissioner, for the region in which the place of manufacture is located, and shall pertain only to distilled spirits used in the manufacture or production of nonbeverage products during any one quarter of the year, and only one claim may be filed for each quarter: *Provided,* That where the manufacturer has notified the assistant regional commissioner, in writing, of his intention to file claims on a monthly basis, in lieu of a quarterly basis, and has filed a bond in compliance with the provisions of section 197.21a, claims may be filed monthly in lieu of quarterly: *Provided further,* That any such election for the filing of monthly claims may be revoked upon filing of notice thereof, in writing, with the assistant regional commissioner.

PAR. 2. There is inserted immediately following section 197.21 the following new section:

SEC. 197.21a. BOND, FORM 1730.—Every person desiring to file claims for drawback on a monthly basis shall, upon filing his notice of such intention as provided in section 197.21, execute a bond on Form 1730, in triplicate, in conformity with the provisions of sections 197.35 through 197.50, and file the same with the assistant regional commissioner. The penal sum of the bond must be sufficient to cover the amount of drawback which will, during any quarterly period, constitute a charge against the bond: *Provided,* That the penal sum of any bond shall not exceed $200,000 nor be less than $1,000. The bond shall be a continuing one, and the liability thereof subject to increase as successive monthly claims are allowed thereunder and to decrease as the verifications of such monthly claims are made. When the limit of liability under a bond given in less than the maximum penal sum has been reached, no further drawback on monthly claims will be allowed unless prior charges against the bond have been decreased, or a new, or additional, bond in sufficient penal sum is furnished.

PAR. 3. Section 197.22 is amended to read as follows:

Quarterly claims for drawback must be filed with the assistant regional commissioner within the 3 months next succeeding the quarter in which the distilled spirits covered by the claim were used in the manufacture of nonbeverage products. Monthly claims for drawback may be filed at any time after the end of the month in which the distilled spirits covered by the claim were used in the manufacture of nonbeverage products, but must be filed not later than the close of the third month succeeding the quarter in which such spirits were used.

PAR. 4. Section 197.24 is amended as follows:

(A) By striking the phrase "which shall be prepared in duplicate" in the first sentence.

(B) By striking the second sentence, which begins "One copy shall be".

(C) By striking the word "collection" in item (5) of paragraph (*a*) and inserting in lieu thereof the following: "internal revenue".

(D) By striking the words "Deputy Commissioner" wherever they appear in subparagraphs (3) and (4) of paragraph (*c*) and inserting in lieu thereof the following: "Director".

(E) By striking the phrase "American Institute of Homeopathy" in subparagraph (3) of paragraph (*c*) and inserting in lieu thereof the following: "Homeopathic Pharmacopoeia of the United States".

(F) By striking the phrase "A. I. H.," in subparagraph (3) of paragraph (*c*) and inserting in lieu thereof the following: "H. P. U. S.,".

(G) By striking the word "quarter" wherever it appears in subparagraphs (1), (2), (3), and (4) of paragraph (*d*) and inserting in lieu thereof the word "period".

(H) By striking the word "quarter" wherever it appears in paragraph (*e*) and inserting in lieu thereof the word "period".

PAR. 5. Section 197.25 and headnote are amended to read as follows:

SEC. 197.25. ACTION ON QUARTERLY CLAIMS.—The assistant regional commissioner will date stamp the claim and, after recording, will examine the claim for the purpose of determining whether it is properly executed and that all supporting data have been submitted and will conduct such inquiries and investigations as may be necessary to verify that drawback is allowable on the distilled spirits covered by the claim. After completion of such verification he will allow or disallow the claim in accordance with his findings and existing law and regulations.

PAR. 6. There is inserted immediately following section 197.25 the following new section:

SEC. 197.25a. ACTION ON MONTHLY CLAIMS.—The assistant regional commissioner will date stamp the claim and, after recording, will examine the claim for the purpose of determining whether it is properly executed and that all required supporting data have been submitted. Where a bond in the maximum penal sum or, if less than such maximum, in a sufficient penal sum, is on file, the assistant regional commissioner will verify that the amount of drawback claimed is correctly calculated, based on the quantity of distilled spirits stated to have been used by the manufacturer, and, without investigation, allow or disallow the claim (including the final claim for any quarter) in accordance with existing law and regulations. Where the bond on file is not in a sufficient penal sum, action on the claim will be withheld pending completion of an investigation subsequent to the end of the quarterly period. When the final claim for a quarter is received, the assistant regional commissioner will conduct such investigation as may be necessary to verify, as to each claim filed for the quarter, that the drawback allowed, or claimed where bond was insufficient, was proper: *Provided*, That where the total charges outstanding against the manufacturer's bond are less than the penal sum of such bond, the assistant regional commissioner may, at his discretion, conduct such investigation at less frequent intervals. Upon completion of verification the assistant regional commissioner will credit the manufacturer's bond in an amount equal to the drawback on the spirits found to have been lawfully used.

PAR. 7. There is inserted at the end of article VII the following new article:

ARTICLE VIII.—BONDS AND CONSENTS OF SURETIES

SEC. 197.35. GENERAL.—Every person required to file a bond or consent of surety under the provisions of this part shall prepare and execute it on the prescribed form, in triplicate, in accordance with the provisions in this part and the instructions printed on the form, and shall submit it to the assistant regional commissioner. The bonds required by the provisions in this part shall be given with surety or collateral security. The surety may be individual or corporate. The surety may not have any interest, either direct or indirect, in the business of the principal on the bond.

SEC. 197.36. CORPORATE SURETY.—Bonds may be given with corporate surety authorized by the Secretary of the Treasury to become surety on Federal bonds, subject to the limitations prescribed by the Secretary in Treasury Department Form 356, Commissioner of Accounts, Surety Bonds Branch, which is issued annually, and subject to such amendatory circulars as may be issued from time to time. A bond executed by two or more corporate sureties shall be the joint and several liability of the principal and the sureties: *Provided*, That each corporate surety may limit its liability in terms upon the face of the bond in a definite, specified amount, which amount shall not exceed the limitations prescribed for such corporate surety by the Secretary, as set forth in Treasury Department Form 356. When the sureties so limit their liability, the aggregate of such limited liabilities must equal the required penal sum of the bond.

SEC. 197.37. POWERS OF ATTORNEY.—Powers of attorney and other evidence of appointment of agents and officers to execute bonds on behalf of corporate sureties are required to be filed with, and passed upon by, the Commissioner of Accounts, Surety Bonds Branch, Treasury Department. Such powers and other evidence of appointment need not be filed with, or submitted to, assistant regional commissioners. Powers of attorney or other evidence of appointment of agents and officers to execute bonds on behalf of the principal, must be filed on Form 1534, in triplicate, with the assistant regional commissioner with whom the bond is filed.

SEC. 197.38. INDIVIDUAL SURETIES.—Bonds may be given with individual sureties of which there must be not less than two, each of whom must qualify by executing Form 33(AT), in triplicate. Individual sureties must be citizens of the United States and reside in the State in which the business of the principal is to be conducted. No person will be accepted as an individual surety in a State in which he is not authorized to become a surety.

SEC. 197.39. OWNERSHIP OF REAL PROPERTY.—Each individual surety must own unencumbered real property, in fee simple, the appraised value of which, over and above any exemptions from execution allowed by the laws of the State, is equal to the penal sum of the bond. Such real property must be located within the State where the business of the principal is to be conducted. The real property must be described in the surety's affidavit, Form 33(AT), with all of the formalities required in conveyances of real estate by the laws of the State in which it is situated.

SEC. 197.40. EXECUTION OF FORM 33(AT).—The surety's affidavit on Form 33(AT) shall contain all of the information required by this part and the instructions printed on the form. The form shall be subscribed and sworn to before an officer duly authorized to administer oaths, and one copy thereof shall be attached to each copy of the bond to which it relates.

SEC. 197.41. CERTIFICATE OF TITLE.—There must be submitted with the surety's affidavit, Form 33(AT), a certificate of title, in triplicate, showing that the surety has a fee simple title free of encumbrances to the realty described in the form: *Provided*, That where recognized by the laws of the State in which the realty is located, there may be submitted, in lieu of a certificate of title, a document of comparable validity, such as a certified copy of a title insurance policy or a certificate of search and finding executed by an authorized attorney.

SEC. 197.42. APPRAISAL.—There will also be submitted with Form 33(AT) an appraisal, in triplicate, by two or more competent persons, designated by the assistant regional commissioner for the purpose, showing separately the value of the land and buildings, and a full and clear statement of the method employed by them in determining their valuation. The appraisal shall be at the expense of the principal on the bond, unless it is made by Government officers.

SEC. 197.43. INVESTIGATION.—The assistant regional commissioner must cause an investigation to be made of all the facts stated in the surety's affidavit on Form 33(AT) and supporting documents, and shall forward one copy of the report of such investigation to the Commissioner with the bond and accompanying Form 33(AT).

SEC. 197.44. REQUALIFICATION.—The Commissioner or assistant regional commissioner may at any time require the requalification of individual sureties on Form 33(AT).

SEC. 197.45. DEPOSIT OF COLLATERAL.—Except as provided in this section, bonds or notes of the United States, or other obligations which are unconditionally guaranteed as to both interest and principal by the United States, may be pledged and deposited by principals as collateral security in lieu of individual or corporate sureties. Assistant regional commissioners on receiving such bonds or notes,

or other obligations, pledged and deposited by principals as collateral security in lieu of surety, shall deposit such securities as required by Department Circular No. 154, revised (31 CFR, pt. 225). United States savings, defense savings, and war savings bonds issued under the authority of section 22 of the Second Liberty Bond Act, as amended, and other bonds and notes of the United States, which are nontransferable or the hypothecation of which will not be recognized by the Treasury Department, may not be pledged and deposited as security in lieu of corporate or individual sureties. (Sec. 1126, 44 Stat. 122 as amended, sec. 7, 49 Stat. 22; 6 U. S. C. 15.)

SEC. 197.46. CONSENTS OF SURETY.—Consents of surety to a change in the terms of a bond must be executed on Form 1533, in as many copies as are required of the bond which they affect, by the principal and all sureties with the same formality and proof of authority to execute as are required for the execution of bonds. Form 1533 will be used by obligors on collateral bonds as well as those on surety bonds. The Form 1533 must properly identify the bond affected thereby and state specifically and precisely what is covered by the extended terms thereof. If the surety is a corporation, the consent may be executed by an agent or attorney in fact duly authorized so to do by power of attorney filed by the surety with the appropriate assistant regional commissioner, or the consent may be executed by the home office officials of such corporate surety; except that, in cases where the saving of time is an element, the consent may be executed by an agent or attorney in fact where the home office officials, by specific direction, order its execution. A copy of such specific direction should be attached to each copy of such consent.

SEC. 197.47. APPROVAL REQUIRED.—No person using distilled spirits in the manufacture of nonbeverage products may file monthly claim for drawback under the provisions of this part until bond on Form 1730 has been approved by the assistant regional commissioner.

SEC. 197.48. AUTHORITY TO APPROVE.—Assistant regional commissioners are authorized to approve all bonds and consents of surety required by this part.

SEC. 197.49. ADDITIONAL OR STRENGTHENING BONDS.—In all cases where the penal sum of a bond on file and in effect is not sufficient, computed as prescribed by this part, the principal may give an additional or strengthening bond in a sufficient penal sum, provided the surety thereon is the same as on the bond already on file and in effect: otherwise a new bond covering the entire liability will be required. Such additional or strengthening bonds, being filed to increase the bond liability of the principal and the surety, shall not be construed in any sense to be substitute bonds, and the assistant regional commissioner will refuse to approve an additional or strengthening bond where any notation is made thereon which may be construed as a release of any former bond or as limiting the amount of either bond to less than its full penal sum. Additional or strengthening bonds must show the current date of execution and the effective date in the blank spaces provided therefor. Such bonds must have marked thereon, by the obligors at the time of execution, "Additional Bond," or "Strengthening Bond," as the case may be.

SEC. 197.50. NEW OR SUPERSEDING BONDS.—The principal on any bond filed pursuant to this part may, at any time, substitute a new bond therefor. Executors, administrators, assignees, receivers, trustees, or other persons acting in a fiduciary capacity, continuing or liquidating the business of the principal, must execute and file a new bond or obtain the consent of the surety or sureties on the existing bond or bonds. When, in the opinion of the Commissioner or the assistant regional commissioner, the interests of the Government demand it or in any case where the security of the bond becomes impaired in whole or in part for any reason whatever, the principal will be required to give a new bond. A new bond shall be required immediately in case of death, removal from the State, or insolvency of an individual surety, or the insolvency of a corporate surety. Where a bond is found to be not acceptable or for any reason becomes invalid or of no effect, the principal shall be required to file immediately a new and satisfactory bond. Superseding bonds must show the current date of execution and the date they are to be effective, and each such bond shall have marked thereon, by the obligors at the time of execution, "Superseding Bond." Where a new bond is submitted by the principal to supersede a bond or bonds then in effect, and such superseding bond has been approved, the superseded bond shall be released as to transactions occurring wholly subsequent to the effective date of the superseding bond and notice of termination of the superseded bond may be issued as provided in section 197.55.

SEC. 197.51. ACCOUNT WITH DRAWBACK BOND.—The assistant regional commissioner will keep an account with each bond governing the allowance of drawback on a monthly basis. The principal will be charged with the amount of drawback allowed on each monthly claim. Credit will be given on the account with the bond in the amount equal to the drawback found by audit and investigation to be allowable, under the provisions of this part.

TERMINATION OF BONDS

SEC. 197.52. GENERAL.—Continuing bonds on Form 1730 will be terminated by the assistant regional commissioner as to liability on drawback allowed after a specified future date (*a*) pursuant to a notice by the surety as provided in section 197.53, (*b*) following approval of a superseding bond, as provided in section 197.50, or (*c*) following notification by the principal of his intent to discontinue the filing of claims on a monthly basis: *Provided*, That the bond will not be terminated until all outstanding liability thereunder has been discharged. Upon termination, the assistant regional commissioner will mark the bond "canceled" followed by the date of cancellation, and will issue a notice of termination, Form 1490, or a notice of release, Form 1491, as provided in section 197.56.

SEC. 197.53. APPLICATION OF SURETY FOR RELEASE FROM BOND.—A surety on any bond required by this part may at any time, in writing, notify the assistant regional commissioner in whose office the bond is on file, and the principal, that he desires to be relieved of liability under the bond at a date not less than 60 days after the date of the notification. One copy of the notice must be delivered to the principal and two copies shall be delivered to the assistant regional commissioner. If the notice is given by an agent of the surety it must be accompanied by a power of attorney authorizing the agent to give such notice, or by a verified statement that such power of attorney is on file with the Treasury Department. The surety must also file with the assistant regional commissioner an acknowledgment or other proof of service of such notice on the principal.

SEC. 197.54. EXTENT OF RELEASE OF SURETY FROM LIABILITY UNDER BOND.—If the notice required by section 197.53 is not withdrawn thereafter in writing, the rights of the principal as supported by the said bond shall be terminated on the date named in the notice, and the surety will be relieved from liability for drawback allowed subsequent to the date named. Liability for drawback allowed prior to the date named in the surety's notice will continue until the claims for such drawback have been properly verified by the assistant regional commissioner according to law and this part. Where the principal files a valid superseding bond, the surety on the bond superseded will be relieved from liability for drawback allowed wholly subsequent to the effective date of the superseding bond.

SEC. 197.55. ACTION BY ASSISTANT REGIONAL COMMISSIONER.—When an application by the surety for release from bond is filed with the assistant regional commissioner, or when a superseding bond has been approved, or when the principal has discontinued filing claims on a monthly basis, the assistant regional commissioner will make a complete examination of records to determine whether there is any liability then due and payable, or chargeable, outstanding against the bond. If it is found that liabilities chargeable against the bond have not been paid or credited or otherwise settled, no further action will be taken until all such liabilities have been settled. If the assistant regional commissioner finds that the bond may be properly terminated, he will issue notice of termination in accordance with the provisions of section 197.56.

SEC. 197.56. NOTICE OF TERMINATION.—Upon determining that the bond on Form 1730 may be terminated, the assistant regional commissioner will execute a notice of termination, Form 1490, where a superseding bond has been approved, or a notice of release, Form 1491, where the principal has discontinued filing monthly claims, or where the surety has made application for release from bond as provided in section 197.53. The notice of termination or the notice of release shall be prepared in quadruplicate where there is but one surety, and in quintuplicate where there are two sureties, The assistant regional commissioner will forward the original of the notice to the Commissioner, together with a copy of the surety's application, if any, furnish one copy to each obligor, and retain one copy of the notice and the surety's application, if any, on file with the bond to which it relates.

SEC. 197.57. RELEASE OF COLLATERAL.—The release of collateral pledged and deposited to support bonds required by this part will be in accordance with the provisions of Department Circular No. 154, revised (31 CFR, pt. 225), subject to the conditions governing issuance of notices on Forms 1490 and 1491 of the termination of such bonds. When the assistant regional commissioner determines that there is no outstanding liability against the bond, and has satisfied himself that the interests of the Government will not be jeopardized, the security may be released and returned to the principal. (44 Stat. 122 as amended; 6 U. S. C. 15.)

Compliance with the notice, public procedure thereon, and effective date requirements of the Administrative Procedure Act, approved June 11, 1946, has been found impracticable and contrary to the public interest in connection with the issuance of these amendments, for the reason that the provisions of section 3250(l)(5) as amended by Public Law 283 (83d Cong.) are effective October 1, 1953.

These amendments will become effective October 1, 1953, except the amendment to section 197.25 which is hereby made effective July 1, 1953.

(This Treasury Decision is issued under the authority contained in sections 3250(l) as amended and 4041 of the Internal Revenue Code (53 Stat. 338 as amended, 495; 26 U. S. C. 3250(l) as amended, 4041).)

T. COLEMAN ANDREWS,
Commissioner of Internal Revenue.

Approved October 6, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register October 9, 1953, 8:49 a. m.)

PART IX.—COIN-OPERATED AMUSEMENT AND GAMING DEVICES

SECTION 3267.—TAX ON COIN-OPERATED AMUSEMENT AND GAMING DEVICES

REGULATIONS 59, SECTION 323.22: Rates and computation of tax. Rev. Rul. 179

INTERNAL REVENUE CODE

A recording machine which, upon the insertion of a coin, records a person's voice, plays the recording back, and then delivers the record to the purchaser is not considered to be a coin-operated amusement or music device within the meaning of section 3267 of the Internal Revenue Code, and no liability for the special tax imposed by that section is incurred with respect to its maintenance for use.

CHAPTER 27A.—WAGERING TAXES

SUBCHAPTER A.—TAX ON WAGERS

SECTION 3285.—TAX

REGULATIONS 132, SECTION 325.21: Scope of tax.

INTERNAL REVENUE CODE

Seizure of automobiles used in violation of wagering tax law. (See Rev. Rul. 264, p. 379.)

SUBCHAPTER B.—OCCUPATIONAL TAX

SECTION 3290.—TAX

REGULATIONS 132, SECTION 325.42: Rate and computation of tax.

INTERNAL REVENUE CODE

Seizure of automobiles used in violation of wagering tax law. (See Rev. Rul. 264, p. 379.)

CHAPTER 28.—PROVISIONS COMMON TO MISCELLANEOUS TAXES

SUBCHAPTER A.—GENERAL PROVISIONS

PART II.—ASSESSMENT, COLLECTION, AND REFUND

SECTION 3310.—RETURNS AND PAYMENT OF TAX

T. D. 6025

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER E, PART 477.—RETURN AND PAYMENT OF CERTAIN EXCISE TAXES

Filing of returns and payment of certain excise taxes required on a quarterly basis in lieu of a monthly basis; such quarterly returns to be accompanied with prescribed depositary receipts.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

On May 15, 1953, notice of proposed rulemaking, relating to the filing of returns and payment of certain excise taxes, was published in the Federal Register (18 F. R. 2827). After consideration of all such relevant matter as was presented by interested persons regarding the rules proposed, the regulations set forth below are hereby adopted.

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SECTION 477.1. STATUTORY PROVISIONS.

SECTION 3310. RETURNS AND PAYMENT OF TAX [INTERNAL REVENUE CODE, AS AMENDED BY SEC. 471(b), REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

* * * * * * *

(f) DISCRETION ALLOWED COMMISSIONER.—

(1) RETURNS AND PAYMENT OF TAX.—Notwithstanding any other provision of law relating to the filing of returns or payment of any tax imposed by chapter 9, 9A, 10, 12, 19, 21, 30, 32, subchapter A of chapter 25, subchapter A of chapter 27A, or subchapter A of chapter 29, the Commissioner may by regulations approved by the Secretary prescribe the period for which the return for such tax shall be filed, the time for the filing of such return, the time for the payment of such tax, and the number of copies of the return required to be filed.

(2) USE OF GOVERNMENT DEPOSITARIES.—The Secretary may authorize Federal Reserve banks, and incorporated banks or trust companies which are despositaries or financial agents of the United States, to receive any tax imposed by this title, in such manner, at such times, and under such conditions as he may prescribe; and he shall prescribe the manner, times, and conditions under which the receipt of such tax by such banks and trust companies is to be treated as payment of such tax to the collector.

SEC. 477.2. QUARTERLY TAX RETURNS.—(a) *General rules.*—In rules and regulations applicable to the Bureau of Internal Revenue and in returns, notices, mimeographs, instructions, circulars, and any other forms or publications of whatever nature prescribed, furnished, or used in or by the Bureau of Internal Revenue with respect to the excise taxes and regulations listed in paragraph (b) of this section, the following rules shall, except as otherwise provided in section 477.3(b), apply:

(1) Reference to a month as the period for which a return must be filed shall, with respect to the return required for any period beginning on or after July 1, 1953, be deemed to refer to one quarter of a calendar year.

(2) Reference to a monthly return shall, with respect to the return required for any period beginning on or after July 1, 1953, be deemed to refer to a quarterly return.

(3) The term "quarter of a calendar year," as used herein, means a period of 3 calendar months ending on March 31, June 30, September 30, or December 31. The term "quarterly return" means a return for a quarter of a calendar year.

(b) *Excise taxes and regulations subject to general rules.*—The excise taxes and regulations referred to in paragraph (a) of this section are as follows:

Regulations	*Relating to tax on*
42 (1942 Edition)	Safe deposit boxes; transportation of oil by pipeline; telephone, telegraph, radio and cable messages, and services; transportation of persons.
43 (1941 Edition)	Admissions, dues, and initiation fees.
44 (1944 Edition)	Gasoline, lubricating oil, and matches.
46 (1940 Edition)	Sales by the manufacturer.
47 (Rev. 1928)[1]	Sales by the manufacturer of pistols and revolvers.
48[1]	Processing of certain oils.
51 (1941 Edition)	Sales by the retailer.
99[1]	Manufacture of manufactured sugar.
113 (1943 Edition)	Transportation of property.
119	Diesel fuel.

[1] These regulations made applicable to the Internal Revenue Code by Treasury Decision 4885 [C. B. 1939–1 (Part 1), 396], approved February 11, 1939.

SEC. 477.3. FILING OF EXCISE TAX RETURNS.—(a) *Quarterly returns.*—Except as otherwise provided in paragraph (b) of this section, every person required by any of the regulations listed in section 477.2(b) to file a return and pay any of the excise taxes covered by such regulations shall make a tax return on Form 720 for the first calendar quarter beginning on or after July 1, 1953, in which falls a month for which such person would be required to file a return under such regulations were it not for the provisions of this part, and for each subsequent calendar quarter until he files a final return. A final return is not to be filed so long as the taxpayer continues the operation of any business or activity in which he may incur liability for any of the taxes reportable on Form 720. Form 720 shall be used in lieu of the form specified in the applicable regulations listed in section 477.2(b). Each quarterly return shall be filed on or before the last day of the first month following the period for which it is made. However, if, and only if, the return is accompanied by depositary receipts (Form 537, Depositary Receipt for Federal Excise Taxes), showing timely deposits, in full payment of the taxes due for the entire calendar quarter, the return may be filed on or before the 10th day of the second month following the period for which it is made. For the purpose of the preceding sentence, the timeliness of the deposit will be determined by the date of the endorsement by a designated commercial bank or by a Federal Reserve bank made on the reverse side of Form 537. Deposit of the taxes for the last month of the calendar quarter with a designated commercial bank or a Federal Reserve bank, as the case may be, may be made on or before the last day of the first month following the close of such quarter. If the last day for filing any return falls on Sunday or a legal holiday, the return may be filed on the next following business day. If placed in the mails, the return shall be posted in ample time to reach the district director of internal revenue for the taxpayer's district, under ordinary handling of the mails, on or before the due date.

(b) *Monthly returns.*—If the district director of internal revenue determines that any taxpayer who is required to make deposit of taxes under the provisions of section 477.4(c) has failed to make deposit of such taxes for the first or second month of any calendar quarter, such taxpayer shall be required, if so notified in writing by the district director, to file a monthly return on Form 720 of the excise taxes listed in section 477.2 for the calendar month in which such notice is received from the district director and for each subsequent calendar month until he files a final return or is again authorized to file quarterly returns. If the notice is received in the second or third month of a calendar quarter, the tax due for the prior month or months of the quarter shall be included in the first return filed pursuant to the notice. Each monthly return shall be filed not later than the last day of the month following the period for which it is made and shall be prepared in accordance with the instructions and regulations applicable to such return. If the district director is satisfied that the taxpayer will comply with the depositary receipt requirements of section 477.4(c), if again permitted to file quarterly returns, the taxpayer may file returns as provided in paragraph (a) of this section upon notification to that effect by the district director.

SEC. 477.4. PAYMENT OF TAX.—(a) *In general.*—The excise taxes listed in section 477.2 required to be reported on a return on Form 720 are due and payable to the district director of internal revenue, without assessment by the Commissioner or notice by the district director, at the time fixed for filing such return. Each quarterly return filed after June 30, 1953, pursuant to this part shall clearly show the identification number, if any, assigned to such taxpayer for depositary receipt purposes.

(b) *Direct remittance to district director.*—Every person required to file a return and pay any of the excise taxes listed in section 477.2 shall include with his return direct remittance to the district director of internal revenue for the total amount of such taxes, except that the provisions of paragraph (c) of this section shall apply if such person is required to file a quarterly return of such excise taxes and the total amount of all such taxes reportable by him exceeds $100 for a calendar month.

(c) *Use of Federal Reserve banks and authorized commercial banks required in connection with payment of taxes.*—(1) *Payments for first 2 months of the calendar quarter.*—If any person required to file a quarterly return and pay any of the excise taxes listed in section 477.2 has a total liability of more than $100 for all such excise taxes reportable by him for a calendar month, the amount of

tax reportable with respect to such calendar month shall be deposited by him with a Federal Reserve bank on or before the last day of the next succeeding calendar month. The remittance of such amount shall be accompanied with a Depositary Receipt for Federal Excise Taxes (Form 537). Such depositary receipt shall be prepared in accordance with the instructions and regulations applicable thereto. The taxpayer, at his election, may forward such remittance, together with such depositary receipt, to a commercial bank authorized in accordance with Treasury Department Circular No. 848 to accept remittances of the aforementioned taxes for transmission to a Federal Reserve bank. After the Federal Reserve bank has validated the depositary receipt, such depositary receipt will be returned to the taxpayer. Every taxpayer making deposits pursuant to this section shall attach to his return for the calendar quarter with respect to which such deposits are made, in part or full payment of the taxes shown thereon, depositary receipts so validated, and shall pay to the district director of internal revenue the balance, if any, of the taxes due for such quarter.

(2) *Payments for last month of the calendar quarter.*—With respect to payment of tax for the last month of the calendar quarter, the taxpayer may either include with his return direct remittance to the district director of internal revenue for the amount of such taxes or attach to such return a depositary receipt validated by a Federal Reserve bank as provided in subparagraph (1) of this paragraph. Payment of the taxes required to be reported on the return, in the form of validated depositary receipts or direct remittances, shall be made to the district director at the time fixed for filing such return. If a deposit is made for the last month of the quarter, the taxpayer shall make it in ample time to enable the Federal Reserve bank to return the validated receipt to the taxpayer so that it can be attached to and filed with the taxpayer's return at the time fixed for filing the return.

(3) *Procurement of depositary receipt form.*—Initially, Form 537, Depositary Receipt for Federal Excise Taxes, will so far as possible be furnished the taxpayer by the district director of internal revenue. A taxpayer not supplied with the proper form should make application therefor to the district director in ample time to have such form available for use in making his initial deposit within the time prescribed in subparagraph (1) of this paragraph. Thereafter, a blank form will be sent to the taxpayer by the Federal Reserve bank when returning the validated depositary receipt. A taxpayer may secure additional forms from a Federal Reserve bank by applying therefor and advising the bank of his identification number. The taxpayer's identification number and name, on each depositary receipt, should be the same as they are required to be shown on the return to be filed with the district director. The address of the taxpayer as shown on each depositary receipt, should be the address to which the receipt should be returned following validation by the Federal Reserve bank.

(4) *Taxpayer's identification number.*—The taxpayer's identification number for the Depositary Receipt for Federal Excise Taxes, Form 537, shall be the same as the identification number, if any, assigned to the taxpayer for use in connection with depositary receipts required for other internal revenue taxes. If a taxpayer does not have an identification number, he should request the assignment of such a number by the district director of internal revenue for his district.

SEC. 477.5. EFFECTIVE DATE.—These regulations shall be effective on and after July 1, 1953.

(This Treasury Decision is issued pursuant to the authority contained in secs. 3310(f) and 3791 of the Internal Revenue Code (63 Stat. 668; 53 Stat. 467; 26 U. S. C. 3310(f), 3791).)

T. COLEMAN ANDREWS,
Commissioner of Internal Revenue.

Approved July 3, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register July 8, 1953, 8:52 a. m.)

CHAPTER 29.—MANUFACTURERS' EXCISE AND IMPORT TAXES

SUBCHAPTER A.—MANUFACTURERS' EXCISE TAXES

SECTIONS 3400–3415.—MANUFACTURERS' EXCISE TAXES

REGULATIONS 46, SECTION 316.0, ETC. T. D. 6029
(Also Section 3443, Section 316.204;
Section 3444, Section 316.7.)

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER C, PART 316.—EXCISE TAXES ON SALES BY THE MANUFACTURER

Regulations 46 (1940 edition) amended to conform to the Revenue Act of 1951, and for other purposes.

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

On December 2, 1952, notice of proposed rulemaking was published in the Federal Register (17 F. R. 10870) in order to conform Regulations 46 (1940 edition) [26 CFR, pt. 316], relating to excise taxes on sales by the manufacturer under chapter 29 of the Internal Revenue Code, to sections 481–488, inclusive, and section 490 of the Revenue Act of 1951 (Public Law 183, 82d Cong., 1st sess.), approved October 20, 1951; to Public Law 251 (82d Cong., 1st sess.), [C. B. 1951–2, 353], approved October 31, 1951; and to Public Law 352 (82d Cong., 2d sess.) [C. B. 1952–1, 259], approved May 21, 1952, and for other purposes. After consideration of all such relevant matter as was presented by interested persons regarding the proposal, the amendments to Regulations 46 (1940 edition) set forth below are hereby adopted.

PARAGRAPH 1. Section 316.0, as amended by Treasury Decision 5854 [C. B. 1951–2, 205], approved September 13, 1951 [26 CFR 316.0], is further amended by renumbering (b) (16) as (b) (17) and inserting the following after item (a) (15):

(16) Mechanical pencils, fountain and ballpoint pens, and mechanical lighters for cigarettes, cigars, and pipes; and

PAR. 2. There is inserted immediately preceding section 316.2 [26 CFR 316.2] the following:

SEC. 481. AUTOMOBILES, TRUCKS, AND PARTS OR ACCESSORIES [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

* * * * * * *

(g) EFFECTIVE DATE OF SUBSECTION (f).—The amendment made by subsection (f) shall be effective with respect to articles purchased (by the user thereof) on or after the first day of the first month which begins more than 10 days after the date of the enactment of this Act.

* * * * * * *

SEC. 482. NAVIGATION RECEIVERS SOLD TO THE UNITED STATES [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

* * * * * * *

(f) EFFECTIVE DATES.—The amendments made by subsections (a) and (b) shall take effect as provided in section 490. The amendments made by subsections (c) and (e) shall be applicable with respect to articles used in receivers sold to the United States on or after the first day of the first month which begins more than 10 days after the date of the enactment of this Act, and the amendment made by subsection (d) shall be applicable with respect to articles resold to the United States on or after such first day.

SEC. 488. REPEAL OF TAX ON ELECTRICAL ENERGY [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

* * * * * * *

(b) EFFECTIVE DATE.—

(1) Except as provided in paragraph (2), the provisions of subsection (a) shall apply to electrical energy sold on or after the first day of the first month which begins more than 10 days after the date of the enactment of this Act.

(2) In the case of electrical energy sold which is billed to the customer for a period beginning before the effective date specified in paragraph (1) and ending on or after such date, the provisions of subsection (a) shall apply to that portion of the amount billed for the electrical energy sold during such period which the number of days in such period on and after such effective date bears to the total number of days in such period. This section shall not apply to electrical energy sold before such effective date for which a bill was rendered prior to such date.

SEC. 490. EFFECTIVE DATE OF PART VIII [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

Except as otherwise expressly provided in this part, the amendments made by this part [secs. 481–489, inc.] shall take effect on the first day of the first month which begins more than 10 days after the date of the enactment of this Act.

PUBLIC LAW 251 (82d CONG., 1st SESS.), APPROVED OCTOBER 31, 1951

* * * * * * *

SEC. 4. Notwithstanding the provisions of section 490 of the Revenue Act of 1951, the effective date of so much of the amendment made by section 485 of such Act to section 3406(a)(3) of the Internal Revenue Code as relates to electric heating pads shall be April 1, 1952.

PUBLIC LAW 352 (82d CONG., 2d SESS.), APPROVED MAY 21, 1952

* * * * * * *

(b) The provisions of subsection (a) shall be effective as of November 1, 1951.

PAR. 3. Section 316.2, as amended by Treasury Decision 5854 [26 CFR 316.2], is further amended by adding at the end thereof the following new paragraphs:

Part VIII of Title IV of the Revenue Act of 1951, effective November 1, 1951, provides for an increase in the rates of tax on chassis and bodies for trucks and other automobiles and parts or accessories therefor, except that beginning April 1, 1954, the rates revert to the rates in effect prior to November 1, 1951; the removal of the tax on certain sporting goods, the increase of the rate of tax on those sporting goods which remain subject to tax (other than certain fishing tackle), excpet that beginning April 1, 1954, the rate reverts to the rate in effect

prior to November 1 1951; an increase in the rate of tax on photographic film, the limiting of the tax to certain cameras, lenses, and film, and the reduction of the rate of tax on cameras and lenses; a change in the method of computing tax liability on sales of rebuilt automobile parts or accessories sold on an exchange basis; a refund or credit to manufacturers of automobile parts or accessories used or sold as repair or replacement parts for farm equipment; an exemption of certain types of communication, detection, or navigation receivers sold to the United States for its exclusive use, and components taxable under section 3404(b) used or sold for use by the vendee as material in the manufacture or production of, or as a component part of, such receivers, together with complementary credit or refund provisions; tax-free sales of refrigerator components to vendees for resale to manufacturers of refrigeration equipment; the imposition of tax on mechanical pencils, fountain and ballpoint pens, and mechanical lighters for cigarettes, cigars, and pipes; the revision of section 3406(a)(3), relating to electric, gas, and oil appliances, by applying the tax imposed thereunder to electric direct motor-driven fans and air circulators of the nonindustrial type and to an increased number of other appliances of the household type only; the removal of the tax on tires for toys, etc.; and the repeal of the tax on electrical energy.

The provisions of Public Law 251, 82d Congress, approved October 31, 1951, postpone the repeal of the tax on electric heating pads, as provided for by the Revenue Act of 1951, from November 1, 1951, to April 1, 1952.

The provisions of Public Law 352, 82d Congress, approved May 21, 1952, discontinue the tax on unperforated microfilm effective November 1, 1951.

PAR. 4. Immediately preceding section 316.7 [26 CFR 316.7], there is inserted the following:

SEC. 482. NAVIGATION RECEIVERS SOLD TO THE UNITED STATES [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

* * * * * * *

(e) USE BY MANUFACTURER OF TAXABLE PARTS.—Section 3444(b) (relating to tax on use by manufacturer of taxable articles) is hereby amended to read as follows:

"(b) This section shall not apply with respect to the use by the manufacturer, producer, or importer of articles described in section 3404(b) if such articles are used by him as material in the manufacture or production of, or as a component part of, communication, detection, or navigation receivers of the type used in commercial, military, or marine installations if such receivers are to be sold to the United States for its exclusive use."

* * * * * * *

PAR. 5. Section 316.7, as amended by Treasury Decision 5854 [26 CFR 316.7], is further amended as follows:

(A) By amending the first sentence thereof to read as follows:

If a person manufactures, produces, or imports an article covered by these regulations, with the exceptions noted in the next two succeeding paragraphs, and uses it for any purpose (other than as material in the manufacture or production of, or as a component part of, another article manufactured or produced by him which will be taxable or sold free of tax under the provisions of section 316.21, 316.22, or 316.61A), he shall be liable for tax with respect to the use of such article in the same manner as if it were sold by him.

(B) By inserting immediately after the second paragraph a new paragraph to read as follows:

If a person manufactures, produces, or imports an article taxable under section 3404(b) and uses it as material in the manufacture or production of, or as a component part of, a communication, detection, or navigation receiver of the type used in commercial, military, or marine installations, he incurs no liability for tax with respect to such use of the article, provided he has a copy of a contract, purchase order, or other written evidence establishing that the receiver is to be sold to the United States on or after November 1, 1951, for its exclusive use. (See sec. 316.61A.)

PAR. 6. Immediately preceding section 316.30 [26 CFR 316.30], there is inserted the following:

SEC. 481. AUTOMOBILES, TRUCKS, AND PARTS OR ACCESSORIES [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

* * * * * * *

(h) REMOVAL OF TAX ON TIRES FOR TOYS, ETC.—Paragraph (1) of section 3400(a) (relating to tax on tires) is hereby amended by adding at the end thereof the following: "The tax imposed by this paragraph shall not apply to (A) tires which are not more than 20 inches in diameter and not more than one and three-fourths inches in cross-section, if such tires are of all-rubber construction (whether hollow center or solid) without fabric or metal reinforcement, or (B) tires of extruded tiring with internal wire fastening agent."

PAR. 7. Section 316.30, as amended by Treasury Decision 5348 [C. B. 1944, 613], approved March 15, 1944 [26 CFR 316.30], is further amended as follows:

(A) By changing the heading to read as follows:

SEC. 316.30. SCOPE OF TAX.—(*a*) *In general.*—

(B) By adding a new paragraph at the end thereof to read as follows:

(*b*) *Certain Tires Not Subject to Tax.*—On and after November 1, 1951, the tax does not apply to sales of (1) tires of all rubber construction (whether hollow center or solid) having no fabric or metal reinforcement if such tires are not more than 20 inches in diameter measured to the outside circumference and not more than one and three-fourth inches in cross section measured on a horizontal plane, or (2) tires of any size or dimensions manufactured or produced from extruded tiring the ends of which are fastened or held together by means of a wire or other metallic material inserted into the extruded tiring.

PAR. 8. Immediately preceding section 316.50 [26 CFR 316.50], there is inserted the following:

SEC. 481. AUTOMOBILES, TRUCKS, AND PARTS OR ACCESSORIES [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

(a) INCREASE IN TAX ON TRUCKS.—Section 3403(a) (tax on trucks, busses, etc.) is hereby amended by striking out "5 per centum" and inserting in lieu thereof "8 per centum, except that on and after April 1, 1954, the rate shall be 5 per centum".

(b) INCREASE IN TAX ON PASSENGER AUTOMOBILES AND MOTORCYCLES.—Section 3403(b) (tax on automobile chassis and bodies, etc.) is hereby amended to read as follows:

"(b) OTHER CHASSIS AND BODIES, ETC.—Other automobile chassis and bodies, chassis and bodies for trailers and semitrailers (other than house trailers) suitable for use in connection with passenger automobiles, and motorcycles (including in each case parts or accessories therefor sold on or in connection therewith or with the sale thereof), except tractors, 10 per centum, except that on and after April 1, 1954, the rate shall be 7 per centum. A sale of an automobile, trailer, or semitrailer shall, for the purposes of this subsection, be considered to be a sale of the chassis and of the body."

* * * * * * *

PAR. 9. Section 316.50, as amended by Treasury Decision 5099 [C. B. 1941–2, 267], approved November 28, 1941 [26 CFR 316.50], is further amended by adding at the end thereof the following new paragraph:

The tax does not apply to house trailers sold on and after November 1, 1951.

PAR. 10. Paragraph (b) of section 316.50A, as added by Treasury Decision 5099 [26 CFR 316.50A], is amended by adding at the end thereof the following sentence:

On and after November 1, 1951, the term shall not include house trailers.

PAR. 11. Section 316.51, as amended by Treasury Decision 5099 [26 CFR 316.51], is further amended to read as follows:

SEC. 316.51. RATES OF TAX.—The tax is payable by the manufacturer on the sale price of the articles listed at the rates specified below:

(a) Automobile truck chassis and bodies; highway tractors; automobile bus chassis and bodies; automobile truck and bus trailer and semitrailer chassis and bodies:	
October 1, 1941 to October 31, 1951, inclusive	5 percent
November 1, 1951 to March 31, 1954, inclusive	8 percent
On and after April 1, 1954	5 percent
(b) Other automobile chassis and bodies; other automobile trailer and semitrailer chassis and bodies; motorcycles:	
October 1, 1941 to October 31, 1951, inclusive	7 percent
November 1, 1951 to March 31, 1954, inclusive	10 percent
On and after April 1, 1954	7 percent
(c) House trailers:	
October 1, 1941 to October 31, 1951, inclusive	7 percent
On and after November 1, 1951	None

In each case the taxable sale price shall be determined in accordance with the provisions of sections 316.8 to 316.15, inclusive.

PAR. 12. The first two sentences of section 316.52, as amended by Treasury Decision 5099 [26 CFR 316.52], are further amended to read as follows:

If the manufacturer of a truck body installs it on an "other automobile chassis" manufactured by him, he must record and bill the sale of the body and chassis separately, and pay tax on the separate sale price of the body and chassis at the rate applicable to each such article. In case a passenger body is installed by the manufacturer thereof on an "automobile truck chassis" manufactured by him, the transaction must be handled in a similar manner, and the tax paid at the rate applicable to each separate article.

PAR. 13. Immediately preceding section 316.54 [26 CFR 316.54], there is inserted the following:

SEC. 481. AUTOMOBILES, TRUCKS, AND PARTS OR ACCESSORIES [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

* * * * * * *

(e) TECHNICAL AMENDMENT.—Section 3403(e) (relating to certain credits against the tax imposed by section 3403) is hereby amended by striking out "in the case of an article taxable under subsection (a), 5 per centum, and in the case of an article taxable under subsection (b), 7 per centum" and inserting in lieu thereof "in the case of an article taxable under subsection (a) or subsection (b), the applicable percentage rate of tax provided in such subsections".

* * * * * * *

PAR. 14. Section 316.54, as amended by Treasury Decision 5854 [26 CFR 316.54], is further amended as follows:

(A) The second sentence of the second paragraph is amended to read as follows:

For example, if the sale price of an automobile is $2,000, the tax payable thereon $200, and the cost to the automobile manufacturer of the tires, inner tubes or automobile radio or television receiving set, sold on or in connection therewith is $80, the manufacturer will be permitted to take a credit against the tax payable on the selling price of the automobile in an amount equal to 10 percent of $80, or $8.

(B) The third paragraph is amended by striking out "rate of 7 percent" and inserting in lieu thereof "applicable rate".

PAR. 15. Immediately preceding section 316.55 [26 CFR 316.55], there is inserted the following:

SEC. 481. AUTOMOBILES, TRUCKS, AND PARTS OR ACCESSORIES [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

* * * * * * *

(c) INCREASE IN TAX ON PARTS OR ACCESSORIES.—Section 3403(c) (tax on parts or accessories for automobiles, etc.) is hereby amended by striking out "5 per centum" and inserting in lieu thereof "8 per centum, except that on and after April 1, 1954, the rate shall be 5 per centum".

(d) REBUILT PARTS OR ACCESSORIES.—Section 3403(c) (tax on parts or accessories) is hereby amended by adding at the end thereof the following: "In determining the sale price of a rebuilt automobile part or accessory there shall be excluded from the price, in accordance with regulations prescribed by the Secretary, the value of a like part or accessory accepted in exchange."

* * * * * * *

PAR. 16. Immediately following section 316.55 [26 CFR 316.55], there is inserted the following new section:

SEC. 316.55A. REBUILT PARTS OR ACCESSORIES SOLD ON AN EXCHANGE BASIS.—On and after November 1, 1951, the tax on the sale of rebuilt automobile parts or accessories will be determined without taking into consideration the value of a like part or accessory accepted in exchange. The total amount charged in terms of cash in an exchange will be the basis for tax. For example, if a rebuilt automobile engine is sold for $100 on an exchange basis, the tax on the rebuilt engine will be computed on the basis of $100.

PAR. 17. Section 316.56, as amended by Treasury Decision 5099 [26 CFR 316.56], is further amended to read as follows:

SEC. 316.56. RATES OF TAX.—The tax is payable by the manufacturer on the sale price of the articles listed at the rates specified below:

Automobile parts and accessories:	
October 1, 1941 to October 31, 1951, inclusive	5 percent
November 1, 1951 to March 31, 1954, inclusive	8 percent
On and after April 1, 1954	5 percent

In each case the taxable sale price shall be determined in accordance with the provisions of sections 316.8 to 316.15, inclusive.

PAR. 18. Immediately preceding section 316.60 [26 CFR 316.60], there is inserted the following:

SEC. 482. NAVIGATION RECEIVERS SOLD TO THE UNITED STATES [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

(a) EXEMPTION ON SALES TO UNITED STATES OF CERTAIN RADIO SETS.—Section 3404(a) (relating to manufacturers' excise tax on radio receiving sets, etc.) is hereby amended by adding at the end thereof the following new sentence: "No tax shall be imposed under this subsection with respect to the sale to the United States for its exclusive use of a communication, detection, or navigation receiver of the type used in commercial, military, or marine installaitons."

(b) TAX-FREE SALES OF RADIO PARTS.—Section 3404(b) (relating to manufacturers' excise tax on component parts of radio receiving sets, etc.) is hereby amended by adding at the end thereof the following new sentence: "Under regulations prescribed by the Secretary, no tax shall be imposed under this subsection with respect to the sale of any article for use by the vendee as material in the manufacture or production of, or as a component part of, communication, detection, or navigational receivers of the type used in commercial, military, or marine installations if such receivers are to be sold by the vendee to the United States for

its exclusive use. If any article sold tax-free to such vendee is not so used by him, or being so used the receiver is not so sold, the vendee shall be considered as the manufacturer or producer of such article."

* * * * * * *

PAR. 19. Immediately following section 316.61 [26 CFR 316.61], there is inserted the following new section:

SEC. 316.61A. SPECIFIC EXEMPTION OF CERTAIN COMMUNICATION RECEIVERS, ETC., AND COMPONENT PARTS.—(*a*) *Receivers.*—On and after November 1, 1951, the tax imposed under section 3404(a) does not apply with respect to the sale to the United States for its exclusive use of a communication, detection, or navigation receiver of the type used in commercial, military, or marine installations. To establish the right to exemption from the tax with respect to such sale, it is necessary that the manufacturer (1) have in his possession a copy of the prime contract, subcontract, or Government purchase order, under which the sale to the United States is made by him directly or through the prime contractor, or (2), in the absence of such contract or purchase order, obtain from an authorized officer of the United States and retain in his possession a properly executed exemption certificate in the form prescribed by this paragraph.

The certificate required by this paragraph shall be in substantially the following form:

EXEMPTION CERTIFICATE

(To support tax-free sales to the United States of communication, detection, or navigation receivers under section 3404(a) of the Internal Revenue Code, as amended by section 482 of the Revenue Act of 1951.)

_____, 19____.
(Date)

The undersigned hereby certifies that he is_____ of
(Title of officer)
_____;
(United States Governmental Unit)
that he is authorized to execute this certificate; and that the article or articles specified in the accompanying order, or on the reverse side hereof, are purchased from _____for the exclusive use of the United States.
(Name of company)

It is understood that the exemption from tax in the case of sales of articles under this exemption certificate to the United States is limited to the sale of articles purchased for its *exclusive use.* It is also understood that the fraudulent use of this certificate to secure exemption will subject the undersigned and all guilty parties to a fine of not more than $10,000, or to imprisonment for not more than five years, or both, together with costs of prosecution.

_____
(Signature)

_____
(Title of officer)

The articles covered by the exemption certificate must be fully identified as to type, quantity, and date of sale. If it is impracticable to furnish a separate exemption certificate for each order or contract, a certificate covering all orders between given dates (such period not to exceed 6 months) will be acceptable.

Such certificates and proper records of invoices, orders, etc., relative to tax-free sales must be retained as provided in section 316.202.

Where the evidence required to support a tax-free sale is obtained subsequent to the sale but prior to the time the manufacturer is required to file a return covering taxes due for the month during which the sale was made he shall include the tax on such sale in his return for that month, in the item "Total tax due", but may deduct an amount equivalent to the tax applicable to such sale and pay the net tax resulting, making appropriate explanation either on the face of the return or on a rider attached thereto. If such evidence is not so obtained, the manufacturer must include the tax on such sale in his return for the month in which the sale was made. However, if such evidence is later obtained a claim for refund of tax paid may be filed on Form 843, or a credit taken upon a subsequent return, but such action must be taken within the 4-year period of limitation prescribed by section 3313.

No sale of a receiver may be made free of tax by the manufacturer to a dealer for resale to the United States. However, where a taxpaid receiver is sold by a dealer on or after November 1, 1951, to the United States for its exclusive use, the manufacturer may be allowed a credit or refund in the amount of tax paid on the article in accordance with the provisions of section 316.204.

(*b*) *Components for receivers.*—On and after November 1, 1951, no tax attaches under section 3404(b) with respect to the sale by the manufacturer of any component named in such section for use by his vendee as material in the manufacture or production of, or as a component part of, a communication, detection, or navigation receiver of the type used in commercial, military, or marine installations if such receiver is to be sold by such vendee to the United States for its exclusive use.

Where the United States contracts for the manufacture and purchase of receivers of the prescribed character under a prime-subcontract arrangement whereby the receivers or subassemblies for such receivers are manufactured or produced by a subcontractor, the entire arrangement is considered as a single transaction so that a sale of a component taxable under section 3404(b) to the subcontractor is considered a sale to the vendee manufacturing the receiver for sale by him, directly or through the prime contractor, to the United States.

To establish the right to exemption with respect to any component taxable under section 3404(b), the manufacturer must obtain prior to or at the time of the sale, and retain in his possession, a certificate substantially in the form prescribed below showing that the article is to be used by his vendee for the purpose mentioned above.

If any person purchases a component free of tax under an exemption certificate for use in the manufacture of a receiver of the prescribed character to be sold to the United States for its exclusive use or for use in the manufacture of a subassembly of such a receiver, and if the component is not so used or, being so used, the receiver is not so sold, such person shall be considered the manufacturer of such component and shall be liable for tax on his use or resale of the component.

The following form of exemption certificate will be acceptable for the purpose of this paragraph:

EXEMPTION CERTIFICATE

(To support tax-free sales of components under section 3404(b) of the Internal Revenue Code, as amended by section 482 of the Revenue Act of 1951, to be used in the manufacture of communication, detection, or navigation receivers to be sold to the United States.)

---------- 19----.
(Date)

The undersigned hereby certifies that he is engaged in the manufacture of ---------- receivers of the type used in ----------
(Communication, detection, or navigation) (Commercial,
---------- installations or subassemblies for such receivers; that the com-
military, or marine)
ponents taxable under section 3404(b) of the Internal Revenue Code which are specified in the accompanying order or contract will be used by him as material in the manufacture or production of, or as a component part of, such receivers or subassemblies to be incorporated therein; and that the receivers will be sold to the United States for its exclusive use, either directly by him or under a prime-subcontract arrangement with the United States to which he is a party.

It is understood that if any of the components purchased under this certificate are resold separately by the undersigned, or are used for any purpose other than that stated above, the undersigned will be considered as the manufacturer of the components so purchased and shall pay to the Government the tax on such resale or use unless his resale or use of the articles is exempt from tax under another provision of law.

It is further understood that the fraudulent use of this certificate to secure exemption will subject the undersigned and all guilty parties to a fine of not more than $10,000, or to imprisonment for not more than 5 years, or both, together with costs of prosecution.

(Name)

(Address)

If it is impracticable to furnish a separate exemption certificate with each order or contract, a certificate covering all orders between given dates (such period not to exceed 6 months) will be acceptable.

The certificates and proper records of orders, invoices, etc., shall be retained by the manufacturer of the components as provided in section 316.202.

Where a certificate is not in the possession of the manufacturer at the time he sells the components, he is liable for the tax and is not entitled to a credit or refund on the ground that the receiver is to be sold by his vendee to the United States. The manufacturer of the receiver may, however, be allowed a credit or refund in the amount of the tax paid on the components in accordance with the provisions of section 316.204 after he sells the receiver to the United States.

The exemption provided for under this paragraph applies to the sale of a taxable component for use by the vendee as material in the manufacture or production of, or as a component part of, a communication, detection, or navigation receiver to be sold by such vendee to the United States for its exclusive use. The exemption also applies to the sale of a taxable component to the manufacturer of a nontaxable subassembly provided the subassembly is to be sold to a manufacturer for use as material in the manufacture or production of, or as a component part of, a communication, detection, or navigation receiver to be sold by such manufacturer to the United States for its exclusive use. This exemption is illustrated by the following example: A holds a prime contract with the United States for the manufacture of a commercial type of nontaxable detection receiver; A subcontracts with B for a nontaxable chassis to be used in the manufacture of such receiver; and B subcontracts with C for certain taxable tubes to be used in the manufacture of the chassis. Neither A nor B is required to pay tax on his sale inasmuch as the article sold by him is nontaxable. C is exempt from tax on his sale of tubes to B, since the tubes are to become components of the detection receiver to be sold to the United States by A.

For provisions with respect to tax-free sales for further manufacture of taxable articles under section 3442, see sections 316.20 to 316.23, inclusive.

PAR. 20. Immediately preceding section 316.70 [26 CFR 316.70], there is inserted the following:

SEC. 483. TAX-FREE SALES OF REFRIGERATOR COMPONENTS TO WHOLESALERS FOR RESALE TO MANUFACTURERS [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

Section 3405(b) is hereby amended by inserting "(hereinafter referred to as 'refrigerating equipment')" before the period at the end of the first sentence and by striking out the second and third sentences and inserting in lieu thereof the following: "Under regulations prescribed by the Secretary, the tax under this subsection shall not apply in the case of sales of any such refrigerator components by the manufacturer, producer, or importer to (1) a manufacturer or producer of refrigerating equipment, or (2) a vendee for resale to a manufacturer or producer of refrigerating equipment if such components are in due course so resold. If any such refrigerator components are resold by the manufacturer or producer to whom sold or resold otherwise than on or in connection with, or with the sale of, complete refrigerating equipment manufactured or produced by him, then for the purposes of this section such manufacturer or producer shall be considered the manufacturer or producer of the refrigerator components so resold by him."

PAR. 21. Section 316.70, as amended by Treasury Decision 5854 [26 CFR 316.70], is further amended by striking out the first sentence of the fourth paragraph of (c) and inserting in lieu thereof a new sentence to read as follows:

A manufacturer of household type refrigerators, other type refrigerators, household type units for the quick freezing or frozen storage of foods, other quick-freeze units, or refrigerating or cooling apparatus may purchase tax free for use as components in the manufacture of such articles any of the refrigerating and freezing apparatus specified in section 3405(b).

PAR. 22. Section 316.71, as amended by Treasury Decision 5854 [26 CFR 316.71], is further amended by striking out the last sentence and inserting in lieu thereof a new sentence to read as follows:

Sales of such refrigerating apparatus as component parts of complete refrigerators, refrigerating or cooling apparatus, or quick-freeze units are not subject to tax.

PAR. 23. Section 316.72, as added by Treasury Decision 5854 [26 CFR 316.72], is amended as follows:

(A) By striking the fourth paragraph and inserting in lieu thereof the following:

Prior to November 1, 1951, this exemption from tax does not apply in the case of a sale of refrigerator components by the manufacturer thereof to a wholesaler, jobber, dealer, etc., where such wholesaler, jobber, dealer, etc., does not qualify as a manufacturer of complete refrigerators, refrigerating or cooling apparatus, or quick-freeze units.

On and after November 1, 1951, a manufacturer of taxable refrigerator components, as specified in section 3405(b), may sell such refrigerator components tax free to a wholesaler, jobber, dealer, or any other person buying for resale to a manufacturer of complete refrigerators, refrigerating or cooling apparatus, or quick-freeze units. Tax-free sales of such refrigerator components may not be made to repairmen or servicemen for repair or service work.

In order to make a tax-free sale it is necessary that the manufacturer of the components (a) obtain from the wholesaler, etc., prior to or at the time of the sale and retain in his possession, a statement showing that the component is being purchased for resale to a manufacturer of complete refrigerators, refrigerating or cooling apparatus, or quick-freeze units, and (b) obtain proof that the component has been so resold. Such proof shall be either an exemption certificate in the form set forth below properly executed by the manufacturer purchasing the component for further manufacture, or a statement by the wholesaler, etc., that he has obtained from his vendee, and has in his possession, available for inspection by internal revenue officers, such a certificate. The statement referred to in (a) above suspends the liability of the manufacturer of the component for payment of the tax for a period of two months from the date of his sale. If within such period the manufacturer of the component has not obtained proof of the tax-free character of the resale by the wholesaler, etc., then the temporary suspension of liability for the payment of the tax ceases, and the manufacturer of the component shall include the tax on the sale of such component in his return for the month in which such 2-month period expires. If such proof subsequently becomes available, a credit for the tax paid may be taken upon a subsequent return or a claim for refund may be filed at any time within the 4-year period of limitation prescribed by section 3313. Where the manufacturer of the taxable component has in his possession the evidence required by (a) above but elects to pay the tax instead of making a tax-free sale, he may take a credit or file a refund claim for the tax so paid when he has in his possession the proof required by (b) above.

The foregoing exemption and credit or refund provisions apply only where there is not more than one intervening sale between the manufacturer of the component and the manufacturer of the complete refrigerator, refrigerating or cooling apparatus, or quick-freeze unit.

(B) By striking out the words "refrigerators, refrigerating and cooling apparatus, or quick-freeze units" in the first paragraph of the "EXEMPTION CERTIFICATE" and inserting in lieu thereof the words "complete refrigerators, refrigerating or cooling apparatus, or quick-freeze units".

PAR. 24. Immediately preceding section 316.90 [26 CFR 316.90], there is inserted the following:

SEC. 484. SPORTING GOODS [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

Section 3406(a)(1) (relating to manufacturers' excise tax on sporting goods) is hereby amended to read as follows:

"(1) SPORTING GOODS.—Badminton nets; badminton rackets (measuring 22 inches overall or more in length); badminton racket frames (measuring 22 inches overall or more in length); badminton racket string; badminton shuttlecocks; badminton standards;

billiard and pool tables (measuring 45 inches overall or more in length); billiard and pool balls and cues for such tables; bowling balls and pins; clay pigeons and traps for throwing clay pigeons; cricket balls; cricket bats; croquet balls and mallets; curling stones; deck tennis rings, nets, and posts; golf bags (measuring 26 inches or more in length); golf balls; golf clubs (measuring 30 inches or more in length); lacrosse balls; lacrosse sticks; polo balls; polo mallets; skis, ski poles; snowshoes; snow toboggans and sleds (measuring more than 60 inches overall in length); squash balls; squash rackets (measuring 22 inches overall or more in length); squash racket frames (measuring 22 inches overall or more in length); squash racket string; table tennis tables, balls, nets, and paddles; tennis balls; tennis nets; tennis rackets (measuring 22 inches overall or more in length); tennis racket frames (measuring 22 inches overall or more in length); tennis racket string; 15 per centum, except that on and after April 1, 1954, the rate shall be 10 per centum; fishing rods, creels, reels, and artificial lures, baits, and flies; 10 per centum."

PAR. 25. Section 316.90, as added by Treasury Decision 5099 [26 CFR 316.90], is amended as follows:

(A) By changing the heading to read as follows:

SEC. 316.90. SCOPE OF TAX.—(*a*) *For the period October 1, 1941, to October 31, 1951, inclusive.*—

(B) By adding at the end thereof the following:

(*b*) *For the period beginning November 1, 1951.*—On and after November 1, 1951, the tax does not apply with respect to sales of the following:

Baseball paraphernalia and equipment
Basketball paraphernalia and equipment
Football paraphernalia and equipment
Hockey paraphernalia and equipment
Indoor baseball paraphernalia and equipment
Soccer paraphernalia and equipment
Softball paraphernalia and equipment
Volley ball paraphernalia and equipment
Water polo paraphernalia and equipment
Wrestling paraphernalia and equipment
Boxing apparatus and equipment
Fencing apparatus and equipment
Track apparatus and equipment
Gymnasium apparatus and equipment
Push balls apparatus and equipment
Mass balls apparatus and equipment
Skates apparatus and equipment
Snow toboggans and sleds (measuring sixty inches or less overall in length)

All articles subject to tax during the period October 1, 1941 to October 31, 1951, inclusive, and not listed above continue to be subject to tax.

PAR. 26. Section 316.91, as added by Treasury Decision 5099 [26 CFR 316.91], is amended to read as follows:

SEC. 316.91. RATES OF TAX.—The tax is payable by the manufacturer on the sale price of the articles listed at the rates specified below:

(a) All articles, except fishing tackle:	
October 1, 1941 to October 31, 1951, inclusive	10 percent
November 1, 1951 to March 31, 1954, inclusive	15 percent
On and after April 1, 1954	10 percent
(b) Fishing tackle:	
All periods	10 percent

In each case the taxable price shall be determined in accordance with the provisions of sections 316.8 to 316.15, inclusive.

PAR. 27. Immediately preceding section 316.110 [26 CFR 316.110], there is inserted the following:

SEC. 485. ELECTRIC, GAS, AND OIL APPLIANCES [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

Section 3406(a)(3) (relating to manufacturers' excise tax on electric, gas, and oil appliances) is hereby amended (1) by striking out "Electric direct motor-driven fans and air circulators;" and inserting in lieu thereof "Electric direct motor-driven fans and air circulators (not of the industrial type); and the following appliances of the household type:", (2) by striking out "electric heating pads and blankets" and inserting in lieu thereof "electric blankets, sheets, and spreads", and (3) by inserting after "juicers;" the following: "electric belt-driven fans; electric exhaust blowers; electric or gas clothes driers; electric door chimes; electric dehumidifiers; electric dishwashers; electric floor polishers and waxers; electric food choppers and grinders; electric hedge trimmers; electric ice cream freezers; electric mangles; electric motion or still picture projectors; electric pants pressers; electric garbage disposal units; and power lawn mowers;".

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* * * * * * *

SEC. 4. Notwithstanding the provisions of section 490 of the Revenue Act of 1951, the effective date of so much of the amendment made by section 485 of such Act to section 3406(a)(3) of the Internal Revenue Code as relates to electric heating pads shall be April 1, 1952.

PAR. 28. Section 316.110, as amended by Treasury Decision 5348 [26 CFR 316.110], is further amended as follows:

(A) By changing the heading to read as follows:

SEC. 316.110. SCOPE OF TAX.—(*a*) *For the period October 1, 1941, to October 31, 1951, inclusive.*—

(B) By adding the following new paragraphs at the end thereof:

(*b*) *For the period beginning November 1, 1951.*—(1) *Electric direct motor-driven fans and air circulators.*—On and after November 1, 1951, section 3406(a)(3) imposes a tax on sales by the manufacturer of all electric direct motor-driven fans and air circulators except those of the industrial type. The following list is illustrative of the direct motor-driven fans and air circulators which are of the nonindustrial type and therefore subject to tax:

Ceiling fans of the wood blade type (regardless of whether the blades are made of wood or other material)
Hassock type radial discharge fans and air circulators and modifications thereof, regardless of blade diameter
Exhaust or intake ventilating fans of the household type for use in window or attic
Exhaust or intake ventilating fans of the household kitchen type (built-in wall and built-in ceiling types)
Desk, bracket, and pedestal type fans and air circulators with blade diameter of 16 inches and less

(2) *Household type electric, gas, or oil appliances.*—On and after November 1, 1951, section 3406(a)(3) imposes a tax on sales by the manufacturer of the appliances listed below if they are of the household type. The term "household type" is general in application so that any article falling within the category of those named in the following list is considered of the "household type" and subject to tax if it has an actual practical commercial fitness for household use or if it is specifically designed and constructed for use in the household:

Electric, gas, or oil water heaters
Electric flat irons
Electric air heaters (not including furnaces)
Electric immersion heaters
Electric blankets, sheets, and spreads
Electric heating pads (only if sold prior to April 1, 1952)
Electric, gas, or oil appliances of the type used for cooking, warming, or keeping warm food or beverages for consumption on the premises
Electric mixers, whippers, and juicers
Electric belt-driven fans

Electric exhaust blowers
Electric or gas clothes driers
Electric door chimes
Electric dehumidifiers
Electric dishwashers
Electric floor polishers and waxers
Electric food choppers and grinders
Electric hedge trimmers
Electric ice cream freezers
Electric mangles
Electric motion or still picture projectors
Electric pants pressers
Electric garbage disposal units
Power lawn mowers

(3) *Parts or accessories.*—The tax also attaches to any parts or accessories sold on or in connection with, or with the sale of, any taxable direct motor-driven fan or air circulator or any household type appliance.

PAR. 29. Immediately preceding section 316.120 [26 CFR 316.120], there is inserted the following:

SEC. 486. ADJUSTMENTS OF TAX RATES ON PHOTOGRAPHIC APPARATUS AND FILM; REPEAL OF TAX ON CERTAIN ITEMS [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

(a) ITEMS SUBJECT TO TAX.—Section 3406(a)(4) (relating to the manufacturers' excise tax on photographic apparatus) is hereby amended to read as follows:

"(4) PHOTOGRAPHIC APPARATUS.—Cameras and camera lenses, and unexposed photographic film in rolls (including motion picture film), 20 per centum. The tax imposed under this paragraph shall not apply to X-ray cameras, to cameras weighing more than four pounds exclusive of lens and accessories, to still camera lenses having a focal length of more than one hundred and twenty millimeters, to motion picture camera lenses having a focal length of more than thirty millimeters, to X-ray film, to film more than one hundred and fifty feet in length, or to film more than twenty-five feet in length and more than thirty millimeters in width. Any person who acquires unexposed photographic film not subject to tax under this paragraph and sells such unexposed film in form and dimensions subject to tax hereunder (or in connection with a sale cuts such film to form and dimensions subject to tax hereunder) shall for the purpose of this subsection be considered the manufacturer of the film so sold by him."

(b) FLOOR STOCKS REFUNDS ON BULBS.—

(1) With respect to any photo-flash or other bulb upon which the tax imposed under section 3406(a)(4) of the Internal Revenue Code has been paid, and which on the effective date specified in section 489 of this Act is held by any person and intended for sale, or for use in the manufacture or production of any article intended for sale, there shall be credited or refunded to the manufacturer or producer of such bulb (without interest), subject to such regulations as may be prescribed by the Secretary, an amount equal to so much of the tax so paid as has been paid by such manufacturer or producer to such person as reimbursement for the elimination on such effective date of the tax on such bulb, if claim for such credit or refund is filed with the Secretary prior to the expiration of three months after such effective date. No credit or refund shall be allowable under this paragraph for any bulb held by any person for sale which was purchased by such person as a component part of any other article.

(2) No person shall be entitled to credit or refund under paragraph (1) unless he has in his possession such evidence of the inventories with respect to which he has made the reimbursements described in paragraph (1) as the regulations under paragraph (1) shall prescribe.

(3) All provisions of law, including penalties, applicable with respect to the tax imposed under section 3406(a)(4) of the Internal Revenue Code shall, insofar as applicable and not inconsistent with this subsection, be applicable in respect of the credits and refunds provided for in this subsection to the same extent as if such credits or refunds constituted credits or refunds of such taxes.

PUBLIC LAW 352 (82d CONG. 2d SESS.), APPROVED MAY 21, 1952.

* * * * * * *

That (a) the second sentence of section 3406(a)(4) of the Internal Revenue Code as amended by section 486(a) of the Revenue Act of 1951 is further amended by adding after the comma following the words "to X-ray film" the following: "to unperforated microfilm,".

* * * * * * *

PAR. 30. Section 316.120, as amended by Treasury Decision 5189 [C. B. 1942–2, 226], approved November 30, 1942 [26 CFR 316.120], is further amended as follows:

(A) By changing the heading to read as follows:

SEC. 316.120. SCOPE OF TAX.—(*a*) *For the period October 1, 1941, to October 31, 1951, inclusive.*—

(B) By adding at the end thereof the following:

(*b*) *For the period beginning November 1, 1951.*—On and after November 1, 1951, section 3406(a)(4) imposes a tax on sales by the manufacturer of the following articles:

Cameras (other than X-ray cameras) weighing 4 pounds or less exclusive of lens and accessories

Still camera lenses having a focal length of one hundred and twenty millimeters or less

Motion picture camera lenses having a focal length of thirty millimeters or less

Unexposed photographic film (other than X-ray film and unperforated microfilm) in rolls (1) one hundred and fifty feet or less in length and thirty millimeters or less in width and (2) twenty-five feet or less in length and more than thirty millimeters in width

Parts or accessories of any of the above articles sold on or in connection therewith, or with the sale thereof

Beginning November 1, 1951, any person who acquires unexposed photographic film in dimensions not subject to tax and cuts such film to dimensions which are subject to tax shall be considered the manufacturer of such film and shall be liable for tax on his sales of such cut film.

PAR. 31. Section 316.122, as amended by Treasury Decision 5189 [26 CFR 316.122], is further amended to read as follows:

SEC. 316.122. RATES OF TAX.—The tax is payable by the manufacturer on the sale price of the articles listed at the rates specified below:

(a) Cameras and lenses:	
October 1, 1941 to October 31, 1942, inclusive	10 percent
November 1, 1942 to October 31, 1951, inclusive	25 percent
On and after November 1, 1951	20 percent
(b) Unexposed photographic film in rolls (except X-ray film):	
October 1, 1941 to October 31, 1942, inclusive	10 percent
November 1, 1942 to October 31, 1951, inclusive	15 percent
On and after November 1, 1951	20 percent
(c) Unperforated microfilm:	
October 1, 1941 to October 31, 1942, inclusive	10 percent
November 1, 1942 to October 31, 1951, inclusive	15 percent
On and after November 1, 1951	None
(d) Unexposed photographic plates and sensitized paper:	
October 1, 1941 to October 31, 1942, inclusive	10 percent
November 1, 1942 to October 31, 1951, inclusive	15 percent
On and after November 1, 1951	None

(e) Photographic apparatus and equipment:
October 1, 1941 to October 31, 1942, inclusive ..... 10 percent
November 1, 1942 to October 31, 1951, inclusive ..... 25 percent
On and after November 1, 1951 ..... None
(f) Apparatus and equipment designed for use in taking, developing, etc., pictures:
October 1, 1941 to October 31, 1942, inclusive ..... 10 percent
November 1, 1942 to October 31, 1951, inclusive ..... 25 percent
On and after November 1, 1951 ..... None

In each case the taxable sale price shall be determined in accordance with the provisions of sections 316.8 to 316.15, inclusive.

PAR. 32. Immediately following section 316.194 [26 CFR 316.194], there is inserted the following:

SEC. 488. REPEAL OF TAX ON ELECTRICAL ENERGY [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

(a) REPEAL OF TAX.—Section 3411 (relating to tax on electrical energy for domestic or commercial consumption), and sections 3441(d) and 3447(c) (related provisions), are hereby repealed.

(b) EFFECTIVE DATE.—

(1) Except as provided in paragraph (2), the provisions of subsection (a) shall apply to electrical energy sold on or after the first day of the first month which begins more than 10 days after the date of the enactment of this Act.

(2) In the case of electrical energy sold which is billed to the customer for a period beginning before the effective date specified in paragraph (1) and ending on or after such date, the provisions of subsection (a) shall apply to that portion of the amount billed for the electrical energy sold during such period which the number of days in such period on and after such effective date bears to the total number of days in such period. This section shall not apply to electrical energy sold before such effective date for which a bill was rendered prior to such date.

SEC. 316.195. TERMINATION OF TAX.—Effective November 1, 1951, no tax shall apply to electrical energy sold for domestic or commercial consumption on or after that date. Whether or not the tax is applicable is dependent upon the period during which the electrical energy was sold and not upon the date the bill for such electrical energy was rendered to the purchaser. Therefore, the tax will apply to electrical energy sold before November 1, 1951, regardless of whether the bill was rendered to the purchaser before or after that date. Where electrical energy is sold and billed to the customer for a period beginning prior to November 1, 1951, and ending on or after such date, the tax will not apply to that portion of the total amount billed which the number of days in such period on and after November 1, 1951, bears to the total number of days in the entire period. For example, if a bill is rendered for the period Octotber 15, 1951, to November 14, 1951, (both dates inclusive), a total of 31 days, no tax will apply to fourteen thirty-firsts of the total amount billed.

PAR. 33. The heading "SUBPART U. MISCELLANEOUS PROVISIONS", as designated by Treasury Decision 5099, is redesignated as "SUBPART V. MISCELLANEOUS PROVISIONS", and immediately following Subpart T a new Subpart U is added to read as follows:

SUBPART U. MECHANICAL PENCILS, FOUNTAIN AND BALL-POINT PENS, AND MECHANICAL LIGHTERS FOR CIGARETTES, CIGARS, AND PIPES

SEC. 487. IMPOSITION OF TAX ON MECHANICAL PENCILS, FOUNTAIN AND BALLPOINT PENS, AND MECHANICAL LIGHTERS FOR CIGARETTES, CIGARS, AND PIPES [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

Chapter 29 (relating to manufacturers' excise and import taxes) is hereby amended by adding after section 3407 the following new section:

"SEC. 3408. TAX ON MECHANICAL PENCILS, FOUNTAIN AND BALLPOINT PENS, AND MECHANICAL LIGHTERS FOR CIGARETTES, CIGARS, AND PIPES.

"(a) IMPOSITION OF TAX.—There shall be imposed on the following articles, sold by the manufacturer, producer, or importer, a tax equal to 15 per centum of the price for which so sold: Mechanical pencils, fountain pens, and ballpoint pens; mechanical lighters for cigarettes, cigars, and pipes.

"(b) EXEMPTION IF ARTICLE TAXABLE AS JEWELRY.—No tax shall be imposed under this section on any article taxable under section 2400 (relating to jewelry tax). If any article, on the sale of which tax has been paid under this section, is further manufactured or processed resulting in an article taxable under section 2400, the person who sells such article at retail shall, in the computation of the retailers' excise tax due on such sale, be entitled to a credit or refund in an amount equal to the tax paid under this section."

SEC. 316.196. SCOPE OF TAX.—The tax imposed by section 3408 attaches to the sale by the manufacturer on and after November 1, 1951, of mechanical pencils, fountain pens, ballpoint pens, and mechanical lighters for cigarettes, cigars, and pipes.

SEC. 316.197. USE OF TERMS.—The term "mechanical pencil" includes any writing instrument containing a moveable marking or writing instrument containing a moveable marking or writing substance in which the desired length of the marking or writing substance is controlled by a propelling or repelling device.

The term "fountain pen" includes a writing instrument of the type equipped with a reservoir for holding ink or other writing fluid which feeds the point when the instrument is in use.

The term "ballpoint pen" includes a writing instrument of the type having an inking reservoir or magazine which feeds a ball writing part when the instrument is in use.

The term "mechanical lighters for cigarettes, cigars, and pipes" includes any articles designed to produce by means of any type of mechanical action a flame or other heat generating source for the lighting of cigarettes, cigars, and pipes.

SEC. 316.198. EXEMPTION IF ARTICLES TAXABLE AS JEWELRY.—The tax imposed by section 3408 does not apply to the sale by the manufacturer of any article named therein if such article is, when sold, subject to the tax imposed by section 2400 (relating to jewelry, etc.). For further details, see section 320.33 of Regulations 51 [26 CFR 320.33].

Where subsequent to the sale by the manufacturer and prior to the sale at retail, any article named in section 3408 is further manufactured or processed in any manner so that it becomes subject to the tax imposed under section 2400, the person who sells such article at retail shall, in computing the retailers' excise tax due on such sale, be entitled to a credit or refund in an amount equal to the tax paid under section 3408. However, such credit or refund is not allowable to the manufacturer who originally paid tax under section 3408, but is allowable only to the person who sells the article at retail.

SEC. 316.199. RATE OF TAX.—The tax is payable by the manufacturer at the rate of 15 percent of the sale price as determined under sections 316.8 to 316.15, inclusive.

PAR. 34. Immediately preceding section 316.204 [26 CFR 316.204], there is inserted the following:

SEC. 481. AUTOMOBILES, TRUCKS, AND PARTS OR ACCESSORIES [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

* * * * * * *

(f) PARTS OR ACCESSORIES FOR FARM EQUIPMENT.—Section 3443(a)(3)(A) is hereby amended by striking out the period at the end of clause (v) and inserting in lieu thereof a semicolon, and by inserting after clause (v) the following:

"(vi) in the case of articles taxable under section 3403(c) (other than spark plugs, storage batteries, leaf springs, coils, timers, and tire chains), used or resold for use as repair or replacement parts or accessories for farm

equipment (other than equipment taxable under sub-section (a) or (b) of section 3403);".

* * * * * * *

SEC. 482. NAVIGATION RECEIVERS SOLD TO THE UNITED STATES [REVENUE ACT OF 1951, APPROVED OCTOBER 20, 1951].

* * * * * * *

(c) REFUND IN CASE OF USE OF PARTS.—Section 3443(a)(1) (relating to credits and refunds) is hereby amended to read as follows:

"(1) to a manufacturer or producer, in the amount of any tax under this chapter which has been paid with respect to the sale of—

"(A) any article (other than a tire, inner tube, or automobile radio or television receiving set taxable under section 3404) purchased by him and used by him as material in the manufacture or production of, or as a component part of, an article with respect to which tax under this chapter has been paid, or which has been sold free of tax by virtue of section 3442, relating to tax-free sales;

"(B) any article described in section 3404(b) purchased by him and used by him as material in the manufacture or production of, or as a component part of, communication, detection, or navigation receivers of the type used in commercial, military, or marine installations if such receivers have been sold by him to the United States for its exclusive use."

(d) REFUND IN CASE OF RESALE TO UNITED STATES.—Section 3443(a)(3)(A) is hereby amended by adding at the end thereof the following:

"(vii) in the case of a communication, detection, or navigation receiver of the type used in commercial, military, or marine installations, resold to the United States for its exclusive use."

* * * * * * *

PAR. 35. Section 316.204, as amended by Treasury Decision 5880 [C. B. 1952–1, 217], approved February 11, 1952 [26 CFR 316.204], is further amended as follows:

(A) By inserting "(1)" immediately after the words "with respect to the sale of" in the first sentence of the first paragraph and by changing the period at the end thereof to a comma and adding the following:

or (2) any article described in section 316.61 purchased and used by such manufacturer as material in the manufacture or production of, or as a component part of, a receiver of the type described in section 316.61A(a) which is sold on or after November 1, 1951, to the United States for its exclusive use directly by him or under a prime-subcontractor arrangement to which he is a party.

(B) By adding at the end thereof the following new paragraphs:

By virtue of the provisions of section 3443(a)(3)(A)(vii) of the Code, as added by section 482(d) of the Revenue Act of 1951, a manufacturer of a communication, detection, or navigation receiver of the type used in commercial, military, or marine installations may be allowed a refund or may take credit on a subsequent return in the amount of any tax paid by him on the sale of such a receiver, if on or after November 1, 1951, such receiver is sold by any person to the United States for its exclusive use. Refund or credit will be allowed in such cases only upon the submission of the evidence required by the preceding paragraphs relating to transactions within the scope of section 3443(a)(3)(A).

Under the provisions of section 3443(a)(3)(A), prior to November 1, 1951, no credit or refund was allowable with respect to tax paid on automobile parts or accessories used or resold for use as repair or replacement parts or accessories for farm equipment even though it was known at the time of the sale that the articles would be so used. On and after November 1, 1951, a manufacturer may be allowed a refund or may take credit against the tax shown to be due upon

any subsequent monthly return, in the amount of tax paid by him with respect to the sale of any article taxable under section 3403(c) (other than spark plugs, storage batteries, leaf springs, coils, timers, and tire chains) used by the ultimate vendor thereof (retailer, repairman, etc.) on or after November 1, 1951, or resold by such ultimate vendor on or after such date for use by his purchaser, as a repair or replacement part or as an accessory for farm equipment (other than equipment taxable under subsection (a) or (b) of section 3403), provided the manufacturer can establish the date the tax on his sale of such article was paid to the United States and the amount of such tax, and he has in his possession a certificate from the ultimate vendor in the form prescribed in the following paragraph. Where the certificate is obtained prior to the time the manufacturer is required to file a return covering taxes due for the month in which the sale was made, he should include the tax on such sale in his return for that month, in the item "Total tax due", but he may deduct an amount equivalent to the tax applicable to such sale and pay the net tax resulting, making appropriate explanation on a rider attached to the return. If the certificate is not so obtained, the manufacturer must include the tax on such sale in his return for the month in which the sale was made, and when the certificate is later obtained he may file a claim for refund on Form 843, or take a credit upon any subsequent return, but such action must be taken within the four-year period of limitation prescribed by section 3313.

The following is the form of certificate which will be acceptable for the purposes of the preceding paragraph:

CREDIT OR REFUND CERTIFICATE

(For use by ultimate vendors (retailers, repairmen, etc.) to support a credit or claim for refund under section 3443(a)(3)(A)(vi) of the Internal Revenue Code.)

The undersigned vendor hereby certifies that the automobile parts or accessories (other than spark plugs, storage batteries, leaf springs, coils, timers, and tire chains) specified below or on the reverse side hereof were purchased tax paid and, on or after November 1, 1951, were used by him or were resold for use by the purchaser thereof as repair or replacement parts or accessories for farm equipment (other than automobile truck chassis and bodies, etc., taxable under section 3403 (a) or (b) of the Internal Revenue Code); that the purpose for which such parts or accessories were used or resold comes within the credit or refund provision of section 3443(a)(3)(A)(vi) of the Internal Revenue Code, as added by section 481(f) of the Revenue Act of 1951; that he consents to the allowance of a credit or refund to

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(Name and address of manufacturer)

in the amount of the tax paid by such manufacturer on the sale of the articles; and that he has not heretofore given his consent to the allowance of this credit or refund to any other manufacturer and has not made application for a credit or refund of this Federal tax from any other source.

It is understood by the undersigned that the fraudulent use of this certificate will subject him to a fine of not more than $10,000, or to imprisonment of not more than 5 years, or both, together with the cost of prosecution.

(Name)

(Address)

(Date)

Suppliers' invoice No.	Article and quantity	Date of use or resale	Name and address of customer

If it is impracticable to furnish a separate certificate for each use or resale, a certificate covering each use or resale between given dates (such period not to exceed 6 months) will be acceptable. Such certificate and supporting records shall be retained by the manufacturer as provided by section 316.202.

(This Treasury Decision is issued pursuant to the authority contained in secs. 3450 and 3791 of the Internal Revenue Code (53 Stat. 419, 467; 26 U. S. C. 3450, 3791).)

T. COLEMAN ANDREWS,
Commissioner of Internal Revenue.

Approved July 8, 1953.

H. CHAPMAN ROSE,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register July 14, 1953, 8:48 a. m.)

SECTION 3403.—TAX ON AUTOMOBILES, ETC.

REGULATIONS 46, SECTION 316.50: Scope of tax. Rev. Rul. 165

(Also Section 316.55, Regulations 46.)

INTERNAL REVENUE CODE

Hoppers or beds which are primarily designed or adapted to be mounted on or pulled behind trucks or tractors and equipped with power driven devices, used solely in spreading fertilizers or other materials on farms, or in the construction, maintenance of, or spreading ice control materials on highways, streets, sidewalks, etc., are not taxable automobile truck bodies or automobile parts or accessories within the purview of section 3403 of the Internal Revenue Code.

REGULATIONS 46, SECTION 316.55: Definition of parts or accessories. Rev. Rul. 166

INTERNAL REVENUE CODE

A grease seal kit, consisting of a steel flange, a grease seal, gaskets, and cork seals, with or without an axle nut, which is primarily designed or adapted for use on a rear axle of an automobile truck of the type used on highways, is considered a part or accessory for an automobile truck chassis and taxable under section 3403(c) of the Internal Revenue Code when sold by the manufacturer, producer, or importer, even though it is sold for heavy duty use on trucks operating on forest trails as well as on the highways and is used either as a replacement of or an additional unit to be attached to the grease seals installed on such trucks by the manufacturer of the trucks. The grease seal, gaskets, cork seals, and axle nut, when sold separately, are not considered to be parts or accessories of a truck chassis but articles susceptible of general use; accordingly, the separate sales of such parts are not subject to tax. However, the steel flange normally made a part of the kit is considered to be a part or accessory for an automobile truck chassis and is subject to tax whether sold separately or as a part of the kit.

SECTION 3403.—TAX ON AUTOMOBILES, ETC.

REGULATIONS 46, SECTION 316.55: Definition of parts or accessories. Rev. Rul. 180

INTERNAL REVENUE CODE

Rear assemblies for milk tank trucks constitute parts or accessories of automobile truck bodies within the meaning of section 3403(c) of the Internal Revenue Code and are subject to the tax imposed by that section upon the sale thereof by the manufacturer.

Advice is requested concerning the application of the tax on automobile parts or accessories, imposed by section 3403(c) of the Internal Revenue Code, to the sale by the manufacturer of rear assemblies for milk tank trucks used by the dairy industry. In the instant case, some of the parts for the assemblies are purchased by the manufacturer on the open market and some are constructed by the manufacturer of the assemblies. Sales of the complete assemblies are made by the manufacturer both at wholesale and retail.

Section 3403(c) of the Code imposes a tax of 8 percent on the sale by the manufacturer of parts or accessories for automobile truck bodies and other articles taxable under subsections (a) and (b) of section 3403 of the Code. The term "parts or accessories" for an automobile truck or other automobile chassis or body includes (*a*) any article the primary use of which is to improve, repair, replace, or serve as a component part of such vehicle or article, (*b*) any article designed to be attached to or used in connection with such vehicle or article to add to its utility or ornamentation, or (*c*) any article the primary use of which is in connection with such vehicle or article whether or not essential to its operation or use. (Sec. 316.55, Regulations 46.)

It is held that the rear assemblies in question are parts or accessories of automobile truck bodies within the meaning of section 3403(c) of the Code. Accordingly, sales of the rear assemblies by the manufacturer are subject to the tax regardless of whether they are installed by the manufacturer or by other persons. However, the manufacturer may take credit for the tax paid on any new parts purchased and used in the manufacture of the assemblies against tax due on the sale of the completed assemblies.

With respect to sales of assemblies by the manufacturer at wholesale, the tax is based on the wholesale (i. e. invoice) price subject to the following adjustments provided by section 3441(a) of the Code. To the invoice price there should be added any charge made for coverings and containers of whatever nature and any other charge incident to placing the assemblies in condition packed ready for shipment and any charge for transportation or delivery. From such adjusted price may be excluded any transportation or delivery expense actually incurred by the manufacturer in effecting delivery of the articles to the purchasers; charges for installation of the articles; any expense for insuring the shipments to the purchasers, and the tax, if not included on the invoice as a separate charge.

Where the manufacturer sells the complete assemblies to a dealer or jobber for resale or to a truck owner, and installation is made by the purchaser no adjustment of the sale price is required for an installation expense since no such expense is incurred by the manu-

facturer. Where the assembly is installed by the manufacturer and a bona fide installation charge is made separately in addition to the sale price of the assembly, such charge is not to be included in the sale price of the assembly for the purpose of computing the tax. If the manufacturer's sale price of the assembly includes the expense of installation, the sale price should be reduced by deducting the installation expense before computing the tax. In such case the manufacturer's records must show the amount actually allocable to the expense of installation.

Under the authority of section 3441(b) of the Code, the tax on sales of assemblies by the manufacturer at retail is to be based upon the established highest wholesale price to independent dealers after adjustment for the additions and exclusions stated in connection with the sales at wholesale, including adjustment for any installation expense incurred by the manufacturer.

REGULATIONS 46, SECTION 316.55: Definition of parts or accessories. Rev. Rul. 193

INTERNAL REVENUE CODE

Shielded spark plugs, which are suitable for use on chassis or vehicles taxable under subsections (a) and (b) of section 3403 of the Internal Revenue Code, constitute parts or accessories for such articles within the meaning of section 3403(c) of the Code and are subject to tax even though sold by the manufacturer for use on tanks, aircraft, or other nontaxable articles.

Advice is requested whether the tax on automobile parts or accessories imposed by section 3403(c) of the Internal Revenue Code applies to the sale by a manufacturer of shielded spark plugs designed primarily for use on military jeeps, trucks, tanks, aircraft, and motor generator sets for setting jet engines.

Section 3403(c) of the Code imposes a tax of 8 percent on the sale by the manufacturer of parts or accessories for automobile chassis or vehicles taxable under subsections (a) and (b) of section 3403 of the Code. That section also provides that spark plugs, storage batteries, leaf springs, coils, timers, and tire chains which are suitable for use on any of the articles enumerated in subsections (a) and (b) of the section shall be considered parts or accessories for such articles, whether or not primarily adapted for such use.

It is held that since the shielded spark plugs described above are suitable for use on jeeps and trucks which are taxable under section 3403(a) of the Code, they constitute automobile parts or accessories within the meaning of section 3403(c) of the Code and are subject to the tax of 8 percent imposed by that section even though sold by the manufacturer for use on tanks, aircraft, or other nontaxable articles.

REGULATIONS 46, SECTION 316.55: Definition of parts or accessories. Rev. Rul. 248

INTERNAL REVENUE CODE

Payment received by a manufacturer pursuant to a contract with a customer for producing an experimental model brake assembly is not taxable under section 3403(c) of the Internal Revenue Code,

where the circumstances are such that the amount received constitutes compensation for research and development rather than the sale price of the article.

Advice is requested concerning the application of the tax on automobile parts or accessories, imposed by section 3403(c) of the Internal Revenue Code, as amended, where a manufacturer pursuant to a contract with a customer produces an experimental model automobile brake assembly. The manufacturer received payment of considerably more for the experimental model, which was especially made for the customer, than the sale price of a comparable brake assembly in ordinary production.

Where a manufacturer, operating under a contract of research and development, produces a specimen or sample article for testing and experimental purposes, which comes within any of the classifications of articles subject to the manufacturers' excise taxes, and the circumstances are such that the payment to the manufacturer constitutes compensation for research and development rather than the sale price of the article as such, the performance of the contract does not result in a taxable sale. However, the fact that an article is intended to be used for experimental and testing purposes does not in itself render the sale thereof nontaxable. A specific sale by the manufacturer of a taxable article as such is subject to tax even though the article is procured by the purchaser strictly for experimental or testing purposes.

In the instant case, it is held that the amount received by the manufacturer under the contract with its customer for producing the experimental model is considered compensation for research and development rather than the sale price of the article as such. Accordingly, the performance of the contract did not result in a taxable sale and the manufacturer incurred no tax liability under section 3403(c) of the Code with respect thereto.

REGULATIONS 46, SECTION 316.55: Definition of parts or accessories. Rev. Rul. 282

INTERNAL REVENUE CODE

Spark plug terminal protectors are not considered to be automobile parts or accessories within the meaning of section 3403(c) of the Internal Revenue Code but articles susceptible of general use. Accordingly, sales of such articles by the manufacturer are not subject to the tax imposed by that section of the Code.

REGULATIONS 46, SECTION 316.55: Definition of parts or accessories. Rev. Rul. 283

INTERNAL REVENUE CODE

Fitted truck top covers made according to individual design and measurement from material furnished by the manufacturer for fleet operators and other consumers thereof are subject to the tax imposed by section 3403(c) of the Internal Revenue Code. Where a fleet owner or other truck operator makes such covers for use in the operation of his business he is liable for the tax under section 3444 of the Code with respect to the use of the covers.

Advice is requested concerning the application of the tax on automobile parts or accessories imposed by section 3403(c) of the Internal Revenue Code to fitted truck top covers made according to individual design and measurement from material furnished by the manufacturer for fleet operators and other consumers thereof.

Section 3403(c) of the Code imposes a tax of 8 percent on the sale by the manufacturer of parts or accessories for automobile truck bodies and other articles taxable under subsections (a) and (b) of section 3403 of the Code. The term "parts or accessories" for an automobile truck or other automobile chassis or body includes (*a*) any article the primary use of which is to improve, repair, replace, or serve as a component part of such vehicle or article, (*b*) any article designed to be attached to or used in connection with such vehicle or article to add to its utility or ornamentation, or (*c*) any article the primary use of which is in connection with such vehicle or article whether or not essential to its operation or use. Section 316.55, Regulations 46.

Fitted truck top covers are considered to be automobile parts or accessories within the meaning of section 3403(c) of the Code and sales thereof by the manufacturer are subject to tax whether made at wholesale or retail. In accordance with section 3444 of the Code any person who manufactures such covers for his own use is likewise liable for the tax imposed by section 3403(c) of the Code. However, a flat rectangular piece of canvas which may be used as a truck top cover but which is not primarily designed or adapted for such use is not a taxable part or accessory within the purview of section 3403(c) of the Code.

It has been the position of the Internal Revenue Service that the only circumstances under which the tax does not apply to sales by the manufacturer of fitted top covers for trucks is where the top covers are individually designed, cut and fitted to trucks belonging to the person who contracts for the performance of such operation and such person is the consumer of the top covers. Upon reconsideration it is now held that where a manufacturer furnishes the material and produces fitted truck top covers for the consumers thereof, including fleet operators, according to individual design and measurement, the sales by the manufacturer of such covers constitute sales at retail and are taxable under section 3403(c) of the Code regardless of whether they are installed by the manufacturer or by other persons.

It has been the policy of the Service not to regard sales by a manufacturer of fitted truck top covers similarly produced, to a dealer of new or used trucks as sales to the consumer of the covers, but as sales at wholesale. This policy is not affected by the ruling herein and such sales remain subject to the tax.

The following sets forth the method of computing the tax with respect to sales by manufacturers of fitted truck top covers at wholesale, wholesale and retail, and retail only, or upon the use of such covers by the manufacturer thereof.

With respect to sales of fitted truck top covers at wholesale, the tax imposed by section 3403(c) of the Code should be based on the wholesale price subject to the following adjustments provided by section 3441(a) of the Code. To the wholesale price there should be added any charge for containers of whatever nature incident to placing the covers in condition packed ready for shipping and any charge

for transportation or delivery. From such adjusted price should be excluded any expenses actually incurred by the manufacturer (1) in effecting delivery of the covers to the purchasers, (2) for installation of the finished covers, and (3) for insuring shipments to the purchasers. The amount of tax is to be excluded if not entered on the invoice as a separate charge.

Under the authority of section 3441(b)(1) of the Code the tax on retail sales of fitted truck top covers by a manufacturer who also sells such articles at wholesale, is to be based upon his highest established wholesale price to independent dealers, subject to the same adjustments hereinbefore stated in connection with sales at wholesale.

The tax on sales of fitted truck top covers by a manufacturer who sells only at retail is to be computed, under the authority of section 3441(b)(1) of the Code, on the price for which such articles are sold by manufacturers or producers in the ordinary course of trade as determined by the Commissioner. Such determination has been made with respect to fitted truck top covers and it has been found to represent 75 percent of the established retail price subject to adjustment with respect to the above-mentioned additions and exclusions provided by section 3441(a) of the Code. No further adjustment of the established retail price should be made with respect to any trade or quantity discount or reduction in price because of anticipated further sales to a customer. In any case where the actual sales price as adjusted in accordance with section 3441(a) of the Code is less than 75 percent of the established retail price as adjusted the tax may be computed on the adjusted actual sales price. If the tax is to be charged as a separate item on the invoice it should be computed at 8 percent of the adjusted retail price. If the tax is included in the adjusted retail price it may be computed at 2/27 (8/108) of such price.

Where a fleet owner or other truck operator makes fitted truck top covers for use in the operation of his business, the owner or operator is liable for tax under the provisions of section 3444 of the Code at the time the covers are used by him. In accordance with the provisions of that section the tax should be computed on the price for which such covers are sold by manufacturers or producers in the ordinary course of trade as determined by the Commissioner. Such determination has been made and has been found to represent the actual cost of producing the covers plus 10 percent of such cost.

Because of the position heretofore maintained regarding the nonapplication of the tax to fitted truck top covers made according to individual design and measurement for the consumer thereof, it is concluded that under the authority contained in section 3791(b) of the Code the instant ruling will not be applied retroactively with respect to fitted truck top covers sold by manufacturers to the consumers thereof or used by the manufacturers thereof prior to January 1, 1954. However, any tax that has been paid on the sale or use of such covers will not be refunded unless in a particular case it is established to the satisfaction of the Commissioner, as required by section 3443(d) of the Code, that the manufacturer by reason of relying on an existing ruling that the sale of such top covers so produced was not taxable, did not include in his price any part of the manufacturers' excise tax which may have subsequently been paid on the sale.

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SECTION 3404.—TAX ON RADIO RECEIVING SETS, TELEVISION RECEIVING SETS, PHONOGRAPHS, PHONOGRAPH RECORDS, AND MUSICAL INSTRUMENTS

REGULATIONS 46, SECTION 316.60: Scope of tax. Rev. Rul. 167

INTERNAL REVENUE CODE

Radio receiving set kits which contain components for use in the assembly of radio receiving sets are taxable under section 3404(a) of the Internal Revenue Code when sold by the manufacturer.

Advice is requested whether the tax on radio receiving sets imposed by section 3404(a) of the Internal Revenue Code is applicable to the sale by a manufacturer of radio kits which contain all of the necessary components for the assembly of a crystal radio receiving set, except aerial and ground wire, or for the assembly of a one tube radio receiving set, except A and B batteries and aerial and ground wires.

Section 316.4 of Regulations 46 provides that the term "manufacturer" includes a person who produces a taxable article by combining or assembling two or more articles, and further provides that a manufacturer who sells a taxable article in a knockdown condition, but complete as to all component parts, is liable for the tax.

It is held that the above-described radio kits constitute radio receiving sets within the meaning of section 3404(a) of the Code, even though the sets are not assembled. Accordingly, sales of such kits by the manufacturer are subject to tax imposed by that section of the Code.

Under the provisions of section 3443(a) of the Code, credit against tax due on the sale of the kits may be taken by the manufacturer of the kits for tax paid by the manufacturer of the tubes or other taxable components purchased and used in assembling the kits.

REGULATIONS 46, SECTION 316.60: Scope of tax. Rev. Rul. 224

INTERNAL REVENUE CODE

A phonograph record player attachment which is not capable of reproducing sound unless connected to an amplifying system with a speaker attachment is not subject to the tax imposed under section 3404 of the Internal Revenue Code. Pursuant to section 3444 the tax on "phonograph mechanisms" under section 3404(b) attaches to the use of such mechanisms in the manufacture of nontaxable record players.

Advice is requested whether a phonograph record player attachment which is not capable of reproducing sound unless connected to an amplifying system with a speaker attachment, is subject to the tax imposed under section 3404(a) of the Internal Revenue Code.

In the instant case, the manufacturer produces and sells a player attachment which consists of a turntable, pickup arm, switch, and a wood base containing a motor. The player attachment is not capable of reproducing records or sounds unless attached to an amplifying system. The attachment is not sold in connection with radio or television receiving sets or any other such amplifying devices.

Section 3404(a) of the Code imposes a tax equivalent to 10 percent of the sale price of radio receiving sets, television receiving sets,

phonographs, and combinations of any of the foregoing sold by the manufacturer or producer thereof. Section 3404(b) of the Code imposes upon phonograph mechanisms which are suitable for use on or in connection with or as component parts of any of the articles enumerated in section 3404(a) a tax equivalent to 10 percent of the price for which sold.

The term "phonograph mechanisms" includes devices which are suitable for use in combination radio and phonograph sets, or phonographs for the purpose of playing records. (Sec. 316.61 of Regulations 46.) Automatic devices for playing or repeating records, phonograph pickups, and similar devices are subject to the tax if sold on or in connection with or with the sale of radio receiving sets, television receiving sets, phonographs, and combinations thereof. (Sec. 316.60 of Regulations 46.)

It is held that phonograph record player attachment which is not capable of reproducing sound unless connected to an amplifying system with a speaker attachment is not subject to the tax imposed under section 3404 of the Internal Revenue Code.

Where the manufacturer of the player attachment is also the manufacturer of the phonograph mechanism, consisting of the turntable, pickup arm, and motor, which becomes a component of the nontaxable player attachment, or if he purchases it free of tax, he is liable for the tax on the use of such mechanism under section 3444 of the Code. The manufacturer of such players incurs no tax liability if the mechanisms are purchased by him on a taxpaid basis.

If the manufacturer of the players is the actual or statutory manufacturer of the phonograph mechanisms used in the players, the tax attaches to that portion of the sale price of the players which is attributable to the phonograph mechanisms. The tax may be based on the lowest established price for which he sells the phonograph mechanisms separately. If they are not sold separately the tax may be based on that portion of the sale price of the player which is allocable to the phonograph mechanisms determined on the basis of the cost of the phonograph mechanisms as compared to the cost of the nontaxable components. Thus, if the cost of the phonograph mechanism represents three-fifths of the total cost of the entire player attachment, the tax determined on the comparative cost basis attaches to three-fifths of the price charged by the manufacturer for the complete unit.

Where the tax is not included in the sale price of the player it should be computed at the rate of 10 percent of that portion of the manufacturer's sale price which is determined to be attributable to the phonograph mechanisms. If the tax is included in the sale price of the player it should be computed at one-eleventh of the portion of such price determined to be attributable to the phonograph mechanisms.

REGULATIONS 46, SECTION 316.63: Musical instruments. Rev. Rul. 206

INTERNAL REVENUE CODE

Method of computing the tax imposed by section 3404(d) of the Internal Revenue Code, with respect to pianos sold by importers at wholesale, wholesale and retail, or only at retail.

Advice is requested concerning the method of computing the tax imposed by section 3404(d) of the Internal Revenue Code, with respect to pianos sold by importers at wholesale, wholesale and retail, or only at retail.

With respect to sales of pianos by an importer at wholesale, the tax imposed by section 3404(d) of the Code shall be based on the wholesale (i. e., invoice) price subject to the following adjustments provided by section 3441(a) of the Code. To the wholesale price there should be added any charge made for coverings and containers of whatever nature incident to placing the pianos in condition packed ready for shipping, and any charge for transportation or delivery. From such adjusted price should be excluded the transportation or delivery expense actually incurred by the importer in effecting delivery of the pianos to the purchasers; any expense for insuring the shipments to the purchasers, and the tax, if not entered on the invoice as a separate charge.

Under the authority of section 3441(b)(1) of the Code, the tax on retail sales of pianos by an importer who also sells such instruments at wholesale, is to be based upon his highest established wholesale price to independent dealers after adjustment for the additions and exclusions hereinbefore stated in connection with sales at wholesale.

The tax on sales of pianos by an importer who sells only at retail shall be computed, under the authority of section 3441(b)(1) of the Code, on the price for which such articles are sold by manufacturers or producers in the ordinary course of trade as determined by the Commissioner. Such determination has been made with respect to pianos and has been found to represent 55 percent of the retail price subject to adjustment with respect to the above-mentioned additions and exclusions. If the tax is not included in the retail price the tax is to be computed at 10 percent of the discounted retail price as adjusted. Where the tax is included in the retail price the tax may be computed at one-eleventh (10/110) of the discounted retail price as adjusted, in order to provide for exclusion of the tax from the price on which it is based.

In the event the tax base determined in the above-described manner with respect to sales by an importer only at retail results in a price which is less than the importer's cost including duty, shipping, and other charges incident to delivery of the pianos to the importer, the tax must be computed upon such cost.

SECTION 3405.—TAX ON MECHANICAL REFRIGERATORS, QUICK-FREEZE UNITS, AND SELF-CONTAINED AIR-CONDITIONING UNITS

REGULATIONS 46, SECTION 316.70: Refrigerators, etc. Rev. Rul. 128

INTERNAL REVENUE CODE

> In determining the cubical content of net storage space of the normal temperature refrigerator portion of combinations of household type units for the quick freezing or frozen storage of foods and household type refrigerators, the space occupied by equipment such as evaporators, and the freezer storage or nonrefrigerated space is excluded.

Advice is requested with respect to the determination of the net storage space of the normal temperature refrigerator portion of combinations of household type units for the quick freezing or frozen storage of foods and household type refrigerators under section 316.70 of Regulations 46.

Section 3405 of the Internal Revenue Code provides in part as follows:

> There shall be imposed on the following articles * * * sold by the manufacturer, producer, or importer a tax equivalent to 10 per centum of the price for which so sold:
>
> (a) REFRIGERATORS AND QUICK-FREEZE UNITS.—Household type refrigerators * * * having, or being primarily designed for use with, a mechanical refrigerating unit operated by electricity, gas, kerosene, or gasoline; household type units for the quick freezing or frozen storage of foods, operated by electricity, gas, kerosene, or gasoline; combinations of such household type refrigerators and units.

Section 316.70 of Regulations 46 provides in part as follows:

> The term "household type refrigerator" includes refrigerators for single or multiple cabinet installations, which (1) are designed for domestic use, (2) are arranged to provide refrigerated storage space for the preservation of food products or low temperature space for making ice cubes and frozen desserts, (3) have a net storage space not exceeding 14 cubic feet, and (4) have, or are primarily designed for use with, a mechanical refrigerator unit operated by electricity, gas, kerosene, or gasoline.
>
> The term "household type units for the quick freezing or frozen storage of foods" includes units solely for the quick freezing of foods or solely for the storage of frozen foods and combination freezer and storage units for rural or urban home use. Units designed and constructed solely for commercial, industrial, or scientific purposes are not taxable.
>
> * * * * * * *
>
> Combinations of household type units for the quick freezing or frozen storage of foods and household type refrigerators are taxable only if the normal temperature refrigerator portion has a net storage space not exceeding 14 cubic feet.

It is held that in determining the cubical content of net storage space of the normal temperature refrigerator portion of combinations of household type units for the quick freezing or frozen storage of foods and household type refrigerators, the space occupied by equipment such as evaporators, and the freezer storage or nonrefrigerated space is excluded.

REGULATIONS 46, SECTION 316.71: Refrigerating apparatus. Rev. Rul. 300

INTERNAL REVENUE CODE

> Types of compressors and condensing units designed for, or suitable for use as parts of or with, household type refrigerators or quick-freeze units and accordingly subject to tax under section 3405(b) of the Internal Revenue Code.

Advice is requested concerning the types of compressors and condensing units which are subject to tax under section 3405(b) of the Internal Revenue Code.

Under the provisions of section 3405(a) of the Code a tax of 10 percent is imposed on sales by the manufacturer, producer, or importer of household type refrigerators (for single or multiple cabinet installations) having, or being primarily designed for use with, a mechanical refrigerating unit operated by electricity, gas, kerosene, or gasoline;

household type units for the quick freezing or frozen storage of foods, operated by electricity, gas, kerosene, or gasoline; combinations of such household type refrigerators and units. Pursuant to the provisions of section 3405(b) of the Code the tax also applies to sales by the manufacturer, producer, or importer of cabinets, compressors, condensers, condensing units, evaporators, expansion units, absorbers, and controls for, or suitable for use as parts of or with, household type refrigerators or quick-freeze units of the kind described in section 3405(a) of the Code, except when sold as component parts of complete refrigerators, refrigerating or cooling apparatus, or quick-freeze units.

It is the general position of the Internal Revenue Service that the types of compressors and condensing units subject to tax under section 3405(b) of the Code, are hermetic motor-compressors and self-contained type hermetic condensing units under three-fourths horsepower nominal rating, suitable for use at the evaporator temperatures used in household type refrigerators and household type quick-freeze units, and incorporating motors with low starting torque characteristics. These standards governing taxability of the units involved shall apply except where a unit is specifically designed for use other than in connection with household type refrigerators or household type quick-freeze units.

For purposes of this Ruling "evaporator temperatures" shall be defined as under 15° F., and "low torque" shall be defined as motors having locked-rotor torque conforming substantially to type I, section MG1-7.7B of "Standards for Fractional Horsepower Motors," published by The National Electrical Manufacturers Association, publication No. MG2-1951 or subsequent revisions thereof.

Where a compressor or condensing unit is within the taxable specifications, but may be specifically designed for a nontaxable use, the manufacturer thereof may secure a Ruling from the Service concerning the taxability of the individual unit.

SUBCHAPTER C.—GENERAL ADMINISTRATIVE PROVISIONS

SECTION 3442.—TAX-FREE SALES

REGULATIONS 44, SECTION 314.24: Exempt sales for governmental use. — Rev. Rul. 138

INTERNAL REVENUE CODE

The sale of gasoline by the manufacturer or producer thereof to employees and officers of a State, or political subdivision thereof, who receive reimbursement from such State or political subdivision for the actual cost of the gasoline purchased for use in their own vehicles used in the performance of their official duties, is a sale for the exclusive use of a State or political subdivision thereof within the meaning of section 3442(3) of the Internal Revenue Code. Such sales are exempt from the tax on gasoline imposed by section 3412 of the Code provided they are supported by a properly executed exemption certificate as required by section 314.24 of Regulations 44.

However, if the employees and officers are paid on a per diem or per mile basis, the sale of gasoline to them is not considered to be a sale for the exclusive use of a State, or political subdivision thereof, within the meaning of section 3442(3) of the Code.

SECTION 3443.—CREDITS AND REFUNDS

REGULATIONS 46, SECTION 316.204: Credits and refunds. Rev. Rul. 265

INTERNAL REVENUE CODE

Rebuilders of taxable Ford automobile parts or accessories may take as a credit for tax paid on new Ford parts used in the rebuilding of such parts or accessories an amount equal to 3.888 percent of the selling price of such parts by the Ford Motor Company.

Advice is requested concerning the method of computing the credit allowable under section 3443(a) of the Internal Revenue Code for tax paid on new parts purchased from the Ford Motor Company and used in the rebuilding of Ford automobile parts or accessories taxable under section 3403(c) of the Code.

Pursuant to the provisions of section 3443(a) of the Code a credit may be allowed to a rebuilder in the amount of tax which has been paid on new automobile parts purchased and used by him in the rebuilding of automobile parts or accessories with respect to which tax has been reported or paid, or which have been sold free of tax by virtue of the provisions of section 3442 of the Code relating to tax-free sales. Section 316.204 of Regulations 46 requires a rebuilder to substantiate such a credit by a statement showing (1) the name and address of the person who paid to the United States the tax of which credit is claimed, (2) the date of payment, (3) the amount of such tax, and (4) that the article was used as prescribed by law. He is also required to state that he has in his possession evidence to support the statement.

It has been determined that the amount of tax paid with respect to new parts sold by the Ford Motor Company to rebuilders represents an amount equal to 3.888 percent of the price for which the articles are sold by such company. Because of the difficulties involved in obtaining the information required by the above mentioned items (1), (2), and (3) of section 316.204 of Regulations 46 to support credits for tax paid on new Ford parts used in the rebuilding of taxable Ford automobile parts or accessories it is held that, in lieu of establishing the amount of tax paid on new parts used in rebuilding Ford automobile parts or accessories in the manner prescribed by the regulations, rebuilders may take as a credit 3.888 percent of the selling price of such new parts sold to them by the Ford Motor Company.

Where a rebuilder of Ford parts or accessories does not use the percentage factor set forth above he must comply with the requirements of section 316.204 of Regulations 46 with respect to any credit claimed on new Ford tax-paid parts used in the rebuilding of taxable Ford automobile parts or accessories.

REGULATIONS 46, SECTION 316.204: Credits and refunds.

INTERNAL REVENUE CODE

Regulations 46 amended. (See T. D. 6029, p. 404.

SECTION 3444.—USE BY MANUFACTURER, PRODUCER, OR IMPORTER

REGULATIONS 46, SECTION 316.7: Tax on use by manufacturer, producer, or importer.

INTERNAL REVENUE CODE

Regulations 46 amended. (See T. D. 6029, p. 404.

CHAPTER 30.—TRANSPORTATION AND COMMUNICATION

SUBCHAPTER C.—TRANSPORTATION OF PERSONS

SECTION 3469.—TAX ON TRANSPORTATION OF PERSONS, ETC.

REGULATIONS 42, SECTION 130.51: Scope of tax.

INTERNAL REVENUE CODE

Taxability of amount paid for ride on a miniature or subgauge railway. (See Rev. Rul. 223, p. 329.)

REGULATIONS 42, SECTION 130.61: Transportation and facilities furnished to the United States, to States, or political subdivisions thereof. Rev. Rul. 299

INTERNAL REVENUE CODE

Payments for transportation of students of a school operated by a State, Territory of the United States, or political subdivision thereof, or the District of Columbia, which are made by the school from funds collected only from the participating students for the purpose of defraying their individual expenses, constitute payments for transportation furnished to the individual students and not for transportation furnished to the State, etc., within the meaning of the exemption provided by section 3469(f)(1) of the Internal Revenue Code, since such payments are not made from funds belonging to the school. Accordingly, such payments are subject to the tax on the transportation of persons. Clarification of M. T. 28, C. B. 1948-2, 176.

SUBCHAPTER E.—TRANSPORTATION OF PROPERTY

SECTION 3475.—TRANSPORTATION OF PROPERTY

REGULATIONS 113, SECTION 143.1: Meaning of terms. Rev. Rul. 285

INTERNAL REVENUE CODE

The tax on the transportation of property imposed by section 3475 of the Internal Revenue Code applies to amounts paid by a shipper to a transfer and storage company for unloading, segregating, reloading and other accessorial services furnished in connection with portions of pool car shipments which the company delivers to consignees in its cartage area. The tax does not apply to amounts paid by the shipper to the transfer and storage company for accessorial services furnished by the company in connection with portions of pool car shipments which are delivered by other carriers, provided the charges for such services are shown as separate items on bills rendered to the shipper by the transfer and storage company.

Advice is requested concerning the application of the tax on the transportation of property imposed by section 3475 of the Internal Revenue Code to amounts paid by a shipper to a transfer and storage company for unloading, segregating, and other accessorial services furnished in connection with the distribution of pool car shipments.

In the instant case, merchandise is shipped by rail in mixed pool cars to a transfer and storage company for distribution. The transfer and storage company removes the merchandise from the cars to a loading dock, segregates it according to the ultimate consignees, and makes store-door deliveries of merchandise specified for consignees located in its cartage area. The transfer and storage company stencils the names of the consignees on the merchandise which is specified by the shipper to be delivered by other carriers, and loads it on the trucks of other carriers. A flat charge per hundredweight is made by the transfer and storage company for handling the pool car shipments, and an additional charge is made for deliveries which it makes to consignees in its cartage area.

Section 3475(a) of the Code imposes a tax, with certain exceptions not here applicable, upon amounts paid within or without the United States to a person engaged in the business of the transportation, for hire, of property by rail, motor vehicle, water, or air from one point in the United States to another.

Section 143.1(d) of Regulations 113 provides that the term "transportation" means the movement of property by a person engaged in the business of transporting property for hire, including interstate, intrastate, and intracity or other local movements. In general, it includes accessorial services furnished in connection with a transportation movement such as loading, unloading, handling, and similar services.

It is held that amounts paid to a carrier for accessorial services furnished in connection with taxable transportation are subject to the tax on the transportation of property. However, where such services are performed for a shipper or consignee by a person who does not transport the property, the amounts paid to such person by the shipper or consignee are not taxable, even though the person who performs such services may be a carrier.

Accordingly, amounts paid by a shipper to a transfer and storage company for unloading, segregating, reloading, and other accessorial services furnished in connection with portions of pool car shipments which the company delivers to consignees in its cartage area are subject to the tax. However, amounts paid by a shipper to the transfer and storage company for such services furnished by the company in connection with portions of pool car shipments delivered by other carriers are not subject to the tax, provided the charges for such services are shown as a separate item on bills rendered to the shipper by the company. If the charges are billed in a lump sum, the total amount so billed is subject to the tax.

REGULATIONS 113, SECTION 143.13: Application of tax. Rev. Rul. 284

INTERNAL REVENUE CODE

Amounts paid or allowed to a person engaged in the business of transporting property for hire for transporting property purchased for his own use are subject to tax under section 3475 of the Internal Revenue Code.

Advice is requested concerning the application of the tax on the transportation of property imposed by section 3475 of the Internal Revenue Code to the transportation by a carrier of property purchased by it for its own use.

In the instant case M Company, which is engaged in the business of transporting property for hire, transports to its warehouse certain supplies which it purchases for use in the conduct of its business. The person from whom the supplies are purchased pays M Company for the transportation thereof or allows the company a credit against the purchase price of the supplies.

Section 3475 of the Internal Revenue Code provides in part as follows:

(a) TAX.—There shall be imposed upon the amount paid within or without the United States for the transportation of property by rail, motor vehicle, water, or air from one point in the United States to another, a tax equal to 3 per centum of the amount so paid * * * Such tax shall apply only to amounts paid to a person engaged in the business of transporting property for hire, including amounts paid to a freight forwarder, express company, or similar person, but not including amounts paid by a freight forwarder, express company, or similar person for transportation with respect to which a tax has previously been paid under this section * * *.

Section 143.13 of Regulations 113 provides in part as follows:

The tax applies to any payment, not specifically exempted, for the transportation of property, made to a person engaged in the business of transporting property for hire, including a payment made by one such person to another but not including an amount paid by a carrier, a freight forwarder, express company, or similar person for transportation with respect to which a tax is payable to such person.

It has been the position of the Internal Revenue Service that the tax on the transportation of property does not apply to amounts paid or allowed to a person engaged in the business of transporting property for hire for transporting property purchased for his own use. Upon reconsideration it is now held that since amounts paid or allowed to a carrier for such transportation are not specifically exempted from the

tax and in view of the above-quoted provisions of law and regulations the amounts so paid or allowed are properly subject to tax.

Accordingly, in the instant case M Company, a carrier, should collect the tax with respect to any amount paid or allowed to it for the transportation by it of property purchased for use in the conduct of its business.

Because of the position heretofore maintained, the instant ruling, under the authority of section 3791(b) of the Code, will not be applied retroactively but will be effective as of January 1, 1954.

REGULATIONS 113, SECTION 143.16: Excavated material. Rev. Rul. 249

INTERNAL REVENUE CODE

The tax on the transportation of property imposed by section 3475 of the Internal Revenue Code applies to amounts paid for the transportation of material excavated within the boundaries of the taxpayer's premises and transported to a plant located on the premises for processing into sand and gravel.

Advice is requested whether the tax on transportation of property imposed by section 3475 of the Internal Revenue Code applies to the amounts paid for the transportation of material excavated within the boundaries of the taxpayer's premises and transported to a plant located on the premises for processing into sand and gravel.

In this case, the taxpayer is engaged in the business of producing sand and gravel from material excavated from land owned by him. To produce the sand and gravel, it is necessary to process the excavated material. This is done at a cleaning and separating plant located on the taxpayer's premises. The material is transported from the point of excavation to the processing plant by independent truckers who are hired on an hourly basis.

Section 3475 of the Code provides that the tax imposed by that section shall not apply to the transportation of earth, rock, or other material excavated within the boundaries of, and in the course of, a construction project and transported to any place within, or adjacent to, the boundaries of such project. To come within the exemption it is necessary that two conditions be met, namely, (1) that the property be earth, rock, or other material excavated within the boundaries of, and in the course of, *a construction project*, and (2) that the transportation of the excavated material be within the boundaries of the construction project or to a place adjacent thereto. See section 143.16 of Regulations 113.

The taxpayer here involved would meet the above enumerated conditions if the material was excavated in the course of a construction project. However, the facts disclose that the material is excavated in connection with the taxpayer's business of producing sand and gravel and not in the course of a construction project.

Accordingly, it is held that the processing of the excavated material is not a construction project within the meaning of section 3475 of the Code. Therefore, amounts paid to independent truckers for the transportation of the material to the processing plant are subject to the tax imposed by that section.

REGULATIONS 113, SECTION 143.24: States, Territories, etc. Rev. Rul. 250

INTERNAL REVENUE CODE

Application of the tax on the transportation of property imposed by section 3475 of the Internal Revenue Code to charges for transportation of a carload shipment (1) where it is consigned to a commercial firm and a portion of the shipment is unloaded enroute for the government of a State, or political subdivision thereof, and (2) where it is consigned to the government of a State, or political subdivision thereof, and a portion is unloaded enroute for a commercial firm.

Advice is requested whether the tax on the transportation of property imposed by section 3475 of the Internal Revenue Code applies to the total charges paid for transportation of a carload shipment consigned to a commercial firm where a portion of the shipment is unloaded at a stopoff point in transit for a State, or political subdivision thereof. Advice is also requested with respect to the tax consequences where a portion of a carload shipment consigned to a State, or political subdivision thereof, is unloaded at a stopoff in transit for a commercial firm.

Section 3475(a) of the Code imposes a tax equal to 3 per centum of the amount paid for the transportation of property from one point in the United States to another. Section 3475(b) provides an exemption from tax of amounts paid for transportation of property to or from a State, Territory, or political subdivision thereof, or the District of Columbia.

It is held that where a carload shipment is consigned to a commercial firm on a through carload rate with stopoff instructions on the bill of lading for a partial unloading for the government of a State, or political subdivision thereof, the exemption applies to the amount paid for the transportation of that portion of the shipment which is delivered to the State or political subdivision, including any additional amount paid for the stopoff privilege.

It is also held that where a carload shipment is consigned to a State, or political subdivision thereof, on a through carload rate with stopoff instructions on the bill of lading calling for partial unloading to a commercial firm the exemption similarly applies to the amount paid for the transportation of that portion of the shipment which is delivered to the State or political subdivision. However, the exemption does not apply to the amount paid for the transportation of that portion of the shipment which is delivered to the commercial firm, including any additional amount paid for the stopoff privilege.

With respect to the above-mentioned shipments it is understood that the charges for the transportation of those portions of the shipments which are delivered to a State, or political subdivision thereof, as a rule are not shown separately on the shipping papers. Where the charges are not shown separately the tax is collectible by the carrier on the total transportation charges. However, where the shipping papers indicate the portion of the carload that is being delivered to the State, or political subdivision thereof, the carrier may allocate the charges on the basis of the weights of the respective portions and collect the tax on the nonexempt portion only.

If the carrier in either case collects the tax on the total transportation charges, the payor may file a claim for refund on Form 843 with the proper district director of internal revenue and attach thereto the original receipt issued by the carrier showing payment of the tax on the carload shipment involved and documentary evidence establishing the charges allocable to the shipment delivered to the State or political subdivision thereof.

CHAPTER 38.—MISCELLANEOUS PROVISIONS

SECTION 3797.—DEFINITIONS

REGULATIONS 111, SECTION 29.3797-4: Partnerships.

INTERNAL REVENUE CODE

Regulations 111 amended. (See T. D. 6037, p. 213.)

SECTION 3801(a).—MITIGATION OF EFFECT OF LIMITATION AND OTHER PROVISIONS IN INCOME TAX CASES: DEFINITIONS

REGULATIONS 111, SECTION 29.3801(a)(1)-1: Purpose and scope of section 3801. (Also Section 23(d), Section 29.23 (d)(1).) Ct. D. 1762

INCOME TAX—INTERNAL REVENUE CODE—DECISION OF COURT

1. INCOME TAX—MITIGATION OF EFFECT OF LIMITATION AND OTHER PROVISIONS—DOUBLE ALLOWANCE OF DEDUCTION OR CREDIT.

For the years 1941 through 1945 petitioner, a banking corporation organized under Federal law, utilized the accrual method of accounting for income tax purposes and deducted taxes levied by the Commonwealth of Pennsylvania on the value of its shares for the year for which the tax was computed, not for the following year when the tax was actually paid. Pursuant to Treasury ruling, adopting a decision of the Pennsylvania Supreme Court to the effect that such State taxes were deductible, regardless of the method of accounting, only when paid, respondent in 1944 and 1945 disallowed the claimed accrued levies but allowed as a deduction the tax actually paid in those years. The effect was to create small deficiencies for 1944 and 1945, which petitioner paid. Thereafter, petitioner filed a refund claim for 1943 based upon allowance of such taxes accrued in 1942, but paid in 1943, which claim was allowed and paid. Respondent made another adjustment to the 1942 return and determined a deficiency for that year resulting from a disallowance of the tax accrued for 1942, but paid in and later allowed for 1943 as a consequence of taxpayer's refund claim. *Held:* Respondent may make an adjustment pursuant to section 3801 by disallowing the Pennsylvania tax on shares deducted on petitioner's return for 1942 (and also allowed as a deduction for 1943) without allowing a deduction for such tax paid in 1942 but accrued in 1941 and deducted on petitioner's return for 1941.

2. DECISION AFFIRMED.

Decision of the United States Tax Court, 18 T. C. 899 (1952) affirmed.

UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

The First National Bank of Philadelphia, petitioner, v. *Commissioner of Internal Revenue, respondent*

[205 Fed. (2d) 82]

Petition for review of decision of The Tax Court of the United States

Before GOODRICH, MCLAUGHLIN, and KALODNER, Circuit Judges

[May 28, 1953]

OPINION

By MCLAUGHLIN, Circuit Judge. This is an appeal from a decision of the Tax Court, 18 T. C. No. 115 (August 29, 1952), upholding respondent's determination of a deficiency for the year 1942 in the amount of $13,292.76.

The facts are not in dispute and are as follows: Petitioner is a banking association organized under Federal law. At all times here material it has utilized the accrual method of accounting in reporting its Federal income tax returns. For the tax years 1941 through 1945 petitioner deducted taxes levied by the Commonwealth of Pennsylvania on the value of its shares.[1] The deductions, authorized by section 23(d) of the Internal Revenue Code, were, ostensibly because of petitioner's use of the accrual method, claimed for the year for which the tax was computed, not for the following year when the tax was actually paid.

Pursuant to a Treasury ruling [2] respondent, in auditing petitioner's returns for 1944 and 1945, recomputed the deductions arising from the Pennsylvania tax payments, disallowing the claimed accrued levies but allowing as a deduction the tax actually paid in those years. The effect was to create small deficiencies for 1944 and 1945, which petitioner paid. Thereafter, and within the 3-year statute of limitations of section 275(a) of the Code, petitioner filed a refund claim for the year 1943 based on a deduction in the amount of $87,452 42 representing the 1942 State tax which had been claimed as a deduction for 1942 (because accrued then), but which had not been paid until 1943. This claim was allowed and paid.

The events which led to the present litigation followed those above outlined. The Commissioner, acting under section 3801 of the Code, made another adjustment, this time to the 1942 return, and determined a deficiency for that year in the amount of $13,292.76 resulting from a disallowance as a deduction of the $87,452.42 accrued for 1942, but paid in and later allowed for 1943 as a consequence of taxpayers refund claim. Section 3801 permits adjustments to be made, both by the taxpayer and by the Commissioner, in certain cases where the statute of limitations would normally be a bar, as it would be insofar as the 1942 return is concerned. One such situation detailed in section 3801(b) is "When a determination under the income tax laws [3] * * * [a]llows a deduction or credit which was erroneously allowed to the taxpayer for another taxable year * * *." It is further provided that "[s]uch adjustment shall be made only if there is adopted in the determination a position * * * by the taxpayer with respect to whom the determination is made * * * which position is inconsistent with the erroneous * * * allowance * * *", a condition which has been met.

Petitioner's chief arguments, both in the Tax Court and on this appeal, are that (1) section 3801 does not permit the adjustment and (2) if section 3801 is applicable, taxpayer is entitled to a deduction of $84,847.46, the State tax accrued in 1941 and paid in 1942 (and which petitioner used as a deduction in 1941). It is clear that because of the running of the statute of limitations the only permissible adjustments to the 1942 return are those which come within section 3801.

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[1] Until 1945 this tax was levied on the shareholders, although the bank was directed to collect it on their behalf and pay it to the State Treasurer. The act of May 23, 1945, Public Law 908, gave the bank the option of proceeding under this method or of paying the tax directly. The change was applicable to the calendar year 1944.

[2] G. C. M. 21329, 1939-2 C. B. 179, which, following a decision of the Pennsylvania Supreme Court, *Commonwealth* v. *Schuylkill Trust Co.,* 315 Pa. 429, 173 A. 309 (1934), reversed on other grounds, 296 U. S. 113, stated that since this Pennsylvania tax is a tax on the shareholder, although paid by the bank, it is deductible by the latter only in the year it is actually paid regardless of the bank's method of accounting.

[3] Determination under the income tax laws is defined in sec. 3801(a)(1) as including "[a] final disposition by the Commissioner of a claim for refund. A claim for refund is there deemed final when the Commissioner allows refund or credit as to the items with respect to which the claim was allowed.

Preliminarily, we must dispose of an argument which pervades petitioner's entire case, that it is being inequitably treated because no deduction on account of a State tax payment is allowed it for the year 1942. This circumstance, of course, arises from the fact that the 1941 State tax was accrued and allowed as a deduction for 1941, while the 1942 State tax has been allowed as a deduction for 1943 as a result of petitioner's own claim. The State tax for 1943 as well as for succeeding years has been allowed as a deduction in the year in which paid. So, while it is true that petitioner is allowed no such deduction for 1942, every tax payment made to the State for all the years in question has been allowed as a deduction.

Respondent makes the point that were the petitioner to be allowed a deduction for 1942 based on its actual payment in that year of the 1941 Pennsylvania tax it would be receiving a double deduction, the 1941 tax payment having been allowed as a deduction for 1941. Petitioner's answer, in effect, is that in 1921 when the predecessor of section 23(d) was first enacted [4] the Pennsylvania taxing statute with which we are concerned had been in effect many years and that had it known that it would later be required to deduct such tax payments in the year when actually paid rather than in the year they were accrued it would have deducted the 1920 Pennsylvania tax in 1921, the year of payment, rather than the 1921 tax which had accrued on December 31, 1921. Thus, it is intimated, it should now be given the opportunity of regaining the 1 year's deduction which but for its use of the accrual method it would never have lost. This suggestion is without merit. In the first place, because of the many variables too obvious to warrant discussion, allowing a double deduction for the 1941 Pennsylvania tax would not be the equivalent of allowing a deduction for the 1920 tax. Second, the statute of limitations has long ago barred adjustments to petitioner's 1921 tax return. Moreover, an adjustment of petitioner's 1921 return would necessarily require recomputations of all its returns from that year through 1942. If the statute of limitations has any purpose it is to prevent such practices. *Rothensies* v. *Electric Storage Battery Co.*, 329 U. S. 296.

It is urged by petitioner that section 3801 is inapplicable to the present state of facts because merely correcting the method of accounting for 1943 does not mean that a deduction was allowed in that year which was also allowed for 1942 and that it is "pure coincidence" that the amount paid in 1943 is identical to the amount accrued for 1942. Petitioner miscomprehends the nature of the Treasury ruling, *supra*, note 2. This ruling does not purport to change taxpayers' method of accounting—it states that *regardless* of such method these Pennsylvania tax payments may be claimed as a deduction by a bank in the year of actual payment only. The reason, of course, is that prior to the 1945 amendment the bank could act only as a collection agent for its shareholders, i. e., there was nothing to accrue so far as income tax deductions were concerned. The assertion that it is only a coincidence that the amount of the 1942 accrual and the 1943 payment is identical has no sound foundation. It is apparently made in support of the argument that since the 1943 payment *might have been* a different figure from the 1942 accrual [5] it cannot be said that the latter, being merely a similar item was erroneously allowed. Neither section 3801 nor the case of *MacDonald* v. *Commissioner*, 17 T. C. 934 (1951), relied on by petitioner, requires that the *amount* erroneously claimed as a deduction by 1 year must be identical with the amount determined for another year—it is the *item of deduction or credit* which must be the same. Whether the 1942 Pennsylvania tax is claimed as an accrued or cash item of deduction does not change its identity. It was properly made the basis of an adjustment under section 3801.

Finally, it is urged that if section 3801 is found applicable petitioner must, in the recomputation of its 1942 return, be allowed a deduction for the 1941 Pennsylvania tax which it paid in 1942. This theory is premised on reading certain words of section 3801(d) out of context. That subsection deals with the ascertainment of the amount of adjustment and relates to adjustments made in favor of the taxpayer as well as the Commissioner. The pertinent part thereof states:

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[4] Sec. 234(a)(3), Revenue Act of 1921; 42 Stat. 254.

[5] It would seem that such differences as exist are caused by the variance between taxpayer's calculations at the time the accrual entry is made and the time the tax is paid, or between taxpayer's calculations and those of the State Treasurer. If petitioner's argument were sound a taxpayer could defeat the application of sec. 3801 by miscalculating the accrual figure but later making the proper payment. For the years 1941 and 1942 the accrual figure and the payment figure were identical. In 1943 there was a difference of 1 cent, while in 1944 and 1945 the variances were $311.82 and $63.47, respectively. In the years 1941–45 the tax paid varied from $49,236.55 to $87,452.42.

"There shall then be ascertained the increase or decrease in the tax previously determined which results solely from the correct exclusion, inclusion, allowance, disallowance, recognition, or nonrecognition, of the item, inclusion, deduction, credit, gain or loss, which was the subject of the error. The amount so ascertained (together with any amounts wrongfully collected, as additions to the tax or interest, as a result of such error) shall be the amount of the adjustment under this section."

Petitioner reads it thus:

"* * * the increase * * * in the tax previously determined which results solely from the correct * * * *allowance* * * * of the * * * deduction * * * which was the subject of the error." (Emphasis supplied.)

As stated earlier, this case comes within that part of section 3801(b) which permits an adjustment to be made when there is a determination which "[a]llows a deduction or credit which was erroneously allowed to the taxpayer for another year * * *", i. e., the 1942 Pennsylvania tax. The remedy is an "increase * * * in the tax previously determined which results solely from the *correct* * * * *disallowance* * * * *of the item* * * * *which was the subject of the error* * * *"—again the 1942 Pennsylvania tax, paid in 1943 and allowed as a deduction in that year, but erroneously claimed as a deduction for 1942. (Emphasis supplied.) When section 3801 is so applied there is no room for petitioner's contention that it should be allowed the 1941 Pennsylvania tax levy as a deduction for 1942.

To state this case another way, it was not the allowance as a deduction of the 1941 tax in petitioner's 1941 return but the allowance of the 1942 tax in 1942 which was the subject of the error [6] in respect of which petitioner's position, because of its allowed refund claim for the year 1943, is inconsistent. This error has been set right by the correct disallowance of that item (the 1942 tax as a deduction in that year's return) and has resulted in an increase in the tax previously determined for 1942. The Tax Court correctly held that, section 3801 being inapplicable to the 1941 Pennsylvania tax, petitioner is precluded by the statute of limitations from having that item considered in recomputing its 1942 return.

Petitioner's remaining points have been examined and found to be without merit.

The judgment will be affirmed.

SECTION 3804.—TIME FOR PERFORMING CERTAIN ACTS POSTPONED BY REASON OF WAR

Rev. Rul. 207

INTERNAL REVENUE CODE

The personnel of United Nations Korean Reconstruction Agency (UNKRA) who are in the combat zone, as defined in Executive Order 10195, C. B. 1951–1, 6, during the period designated by the President by Executive order as the period of combatant activities and who are serving under the United Nations Command pursuant to certain agreements between the United Nations Command and UNKRA, are individuals serving in support of the Armed Forces of the United States within the meaning of section 3804(f) of the Internal Revenue Code.

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[6] Sec. 3801(e) specifically prohibits an adjustment to be made as to any item which was not the subject of the error.

PART II.—ADMINISTRATIVE MATTERS

T. D. 6038

TITLE 26—INTERNAL REVENUE.—CHAPTER I
TITLE 27—INTOXICATING LIQUORS.—CHAPTER I

Change of nomenclature

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

In rules and regulations heretofore prescribed by the Bureau of Internal Revenue and currently applicable in the administration of the internal revenue laws, and in returns, notices, mimeographs, instructions, circulars, or other forms or publications of whatever nature heretofore prescribed, furnished, or used in or by the Bureau of Internal Revenue and currently in use,

(*a*) reference to the Bureau of Internal Revenue shall be deemed to refer to the Internal Revenue Service,

(*b*) reference to a district commissioner or an assistant district commissioner shall be deemed to refer to a regional commissioner or an assistant regional commissioner, respectively,

(*c*) reference to a collector of internal revenue or a director of internal revenue shall be deemed to refer to a district director of internal revenue,

(*d*) reference to a district supervisor or an assistant district commissioner, Alcohol and Tobacco Tax, shall be deemed to refer to an assistant regional commissioner, Alcohol and Tobacco Tax,

(*e*) reference to investigator in charge, or head, Alcohol and Tobacco Tax Division in the office of the director, shall be deemed to refer to supervisor in charge, Alcohol and Tobacco Tax,

(*f*) reference to a deputy commissioner for the Bureau of Internal Revenue, as the office existed prior to August 11, 1952, or to a head of a division in the Washington Headquarters Office, shall be deemed to refer to a director at the National Office, and

(*g*) reference to a collection district shall be deemed to refer to an internal revenue district.

Because the sole purpose of this Treasury Decision is to conform the documents specified herein to various orders, including Treasury Department Order No. 150-26, it is hereby found that it is unnecessary to issue this Treasury Decision with notice and public procedure under section 4(a) of the Administrative Procedure Act, approved June 11, 1946, or subject to the effective date limitations of section 4(c) of said act.

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This Treasury Decision shall be effective upon its filing for publication in the Federal Register.

(This Treasury Decision is issued under the authority contained in secs. 3176 and 3791 of the Internal Revenue Code (53 Stat. 375, 476; 26 U. S. C. 3176, 3791).)

O. GORDON DELK,
Acting Commissioner of Internal Revenue.

Approved August 21, 1953.

H. CHAPMAN ROSE,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register August 26, 1953, 8:49 a. m.)

T. D. 6043

TITLE 26—INTERNAL REVENUE.—CHAPTER I
TITLE 27—INTOXICATING LIQUORS.—CHAPTER I

Amendments of Treasury Decisions 5900 and 5901

TREASURY DEPARTMENT,
OFFICE OF THE COMMISSONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

Treasury Decision 5900 [C. B. 1952–1, 237], approved May 13, 1952 [17 F. R. 4464], and Treasury Decision 5901 [C. B. 1952–1, 238], approved May 15, 1952 [17 F. R. 4561], are hereby amended by striking "reference to a deputy collector shall be deemed to refer to an internal revenue agent" from subdivision (*b*) of the first paragraph of each and inserting in lieu thereof the following: "reference to a deputy collector shall be deemed to refer to an internal revenue agent, except that after September 30, 1953, reference to a deputy collector shall be deemed to refer to a collection officer".

Because the sole purpose of this Treasury Decision is to conform Treasury Decisions 5900 and 5901, and the documents amended by such Treasury Decisions, to the revision of the titles of certain employees of the Internal Revenue Service, it is hereby found that it is unnecessary to issue this Treasury Decision with notice and public procedure under section 4(a) of the Administrative Procedure Act, approved June 11, 1946, or subject to the effective date limitations of section 4(c) of that act.

This Treasury Decision shall be effective upon its filing for publication in the Federal Register.

(This Treasury Decision is issued under authority of sections 3176 and 3791, Internal Revenue Code (53 Stat. 375, 467; 26 U. S. C. 3176, 3791).)

JUSTIN F. WINKLE,
Acting Commissioner of Internal Revenue.

Approved October 6, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register October 9, 1953, 8:50 a. m.)

Rev. Rul. 150*

Enforcement of Federal statutes relating to firearms, illicit liquor traffic, etc.

The accompanying notice (Form 1712) to all state, county, and city prosecutors and law enforcement officers is for the purpose of bringing to their attention the Federal laws pertaining to firearms and the illicit liquor traffic which the Alcohol and Tobacco Tax Division is charged with enforcing.

It is the desire of this office that every effort be made to afford assistance to law enforcement officers, upon request, as promptly as circumstances permit. Supervisors in Charge, Alcohol and Tobacco Tax, should arrange for their Group Leaders and Investigators to advise them each time there is a change in local prosecutive and enforcement officials in the area under their supervision in order that the new officials may be furnished with copies of the notice on Form 1712.

Any unusual developments resulting from this cooperative enforcement program should be referred to in the Weekly Report of Enforcement Activities under the heading, "General Enforcement."

Correspondence relative to this Revenue Ruling should refer to the number thereof and to the symbols O:AT:EF.

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Form 1712
U. S. TREAS'Y DEPT.
INT. REV. SERVICE
(Revised April 1953)

U. S. TREASURY DEPARTMENT

Office of

COMMISSIONER OF INTERNAL REVENUE

Washington 25, D. C.

April 28, 1953

To All State, County, and City Prosecutors and Law Enforcement Officers:

The purpose of this notice is to bring to your attention certain Federal laws which can be utilized effectively as an aid to law enforcement in the suppression of crime. These laws are:

1. THE FEDERAL FIREARMS ACT (U. S. CODE, TITLE 15, SECTIONS 901 ET SEQ.)

This law deals exclusively with the transportation, shipment, or receipt of firearms or ammunition in interstate or foreign commerce. The statute prohibits, among other acts:

a. A person from shipping, transporting, or receiving a firearm or ammunition in interstate or foreign commerce if he has been convicted of a crime of violence, such as murder, manslaughter, rape, mayhem, kidnapping, robbery, burglary, housebreaking; assault with intent to kill, commit rape, or rob; assault with a dangerous weapon; or assault with intent to commit any offense punishable by imprisonment for more than one year, or if he has been indicted for such a crime or is a fugitive from justice.

b. A person or concern from shipping or transporting knowingly in interstate or foreign commerce firearms or ammunition to the type of individual referred to above.

*Originally issued as IR-Mimeograph No. 173, dated April 28, 1953.

c. Any person from transporting or shipping, or causing to be transported or shipped in interstate or foreign commerce any stolen firearm or ammunition, knowing, or having reasonable cause to believe, same to have been stolen.

d. Any person from receiving, concealing, storing, bartering, selling, or disposing of any firearm or ammunition or pledging or accepting as security for a loan any firearm or ammunition moving in or which is a part of interstate or foreign commerce, and which while so moving or constituting such part has been stolen, knowing, or having reasonable cause to believe the same to have been stolen.

e. Any person from shipping, transporting, or knowingly receiving in interstate or foreign commerce any firearm from which the manufacturer's serial number has been removed, obliterated, or altered.

The purpose of this law is to prevent criminals from obtaining firearms and ammunition.

The term "firearm" means any weapon, by whatever name known, which is designed to expel a projectile or projectiles by the action of an explosive and a firearm muffler or firearm silencer, or any part or parts of such weapon.

The term "ammunition" shall include only pistol or revolver ammunition. It shall not include shotgun shells, metallic ammunition suitable for use only in rifles, or any .22 caliber rimfire ammunition.

The term "interstate or foreign commerce" means commerce between any State, Territory, or possession (but not including the Canal Zone), or the District of Columbia, and any place outside thereof; or between points within the same State, Territory, or possession (but not including the Canal Zone), or the District of Columbia, but through any place outside thereof; or within any Territory or possession or the District of Columbia.

The law provides a criminal penalty, upon conviction, of a fine of not more than $2,000 or imprisonment for not more than five years or both.

The Act provides for the seizure and forfeiture of any firearm or ammunition in respect of which any violation of the Act has been committed.

Every firearm found in possession of the persons referred to represents a potential violation of the Federal Firearms Act, and the legality of the possession of such weapon should be thoroughly investigated.

2. The National Firearms Act of June 26, 1934 (U. S. Code, Title 26, Sections 2720–2734; 3260–3266)

The purpose of the National Firearms Act is to prevent strictly gangster weapons, such as machine guns and sawed-off shotguns, from getting into the hands of the criminal element by the imposition of a prohibitive transfer tax. The Act provides for registration of such firearms and imposes a tax upon the making or transfer of firearms of the following types:

a. A shotgun or rifle having a barrel of less than 18 inches in length; provided, however, that any such rifle is excepted from

the law if its caliber is *.22 or smaller* and if its barrel is *16 inches or more* in length;

b. Any other weapon, *except a pistol or revolver*, from which a shot is discharged by an explosive if such weapon is capable of being concealed on the person; provided, however, that a pistol or revolver attached to, or with, accompanying shoulder stock has been held to come within purview of the statute;

c. A machine gun.—The term "machine gun" means any weapon which shoots, or is designed to shoot, automatically or semiautomatically, more than one shot, without manual reloading, by a single function of the trigger.

d. A muffler or silencer for *any* firearm whether or not the firearm itself is covered by the Act.

Any firearm of a type included by the Act which has been made or transferred without payment of the appropriate tax by the maker or transferor, or which has not been registered in accordance with the provisions of the Act, subjects the violator, upon conviction, to a fine of not more than $2,000 or imprisonment for not more than five years or both.

Any firearm as defined heretofore which has at any time been made or transferred illegally is subject to seizure and forfeiture under the internal revenue laws.

The law does not apply to the transfer of such firearms to the United States Government, any State, Territory, or possession of the United States, or to any political subdivision thereof, or to the District of Columbia, or to sheriffs, chiefs of police, commissioners of police, superintendents, or other chief officers of state police units, including state highway patrols, and directors of public safety, or to Federal law enforcement agencies, or to the transfer of an unserviceable firearm transferred as a curio or ornament, except that the person transferring such fire arm must file an application for exemption from payment of the transfer tax.

3. Act of August 9, 1939 (U. S. Code, Title 49, Sections 781–788)

This Act makes it illegal to use any vessel, vehicle, or aircraft to transport, carry, conceal, convey, possess, or transfer any weapon defined as a firearm under the National Firearms Act, which has not been registered or on which the making or transfer tax due has not been paid as required by the National Firearms Act or with respect to which there has been committed any other violation of said Act, and subjects the vessel, vehicle, or aircraft to seizure and forfeiture under the customs laws.

4. Liquor Tax Administration Act (Approved June 26, 1936) (U. S. Code, Title 26, Section 3173(c))

Section 3173(c) (Possession of Devices for Emitting Gas, Smoke, etc.; Explosives and Firearms) provides as follows:

(1) Whoever, when violating any law of the United States, or of any Territory or possession of the United States, or of the District of Columbia, in regard to the manufacture, taxation, or transportation of or traffic in distilled spirits, wines, or fermented malt liquors, or when aiding in any such violation, has in his possession or in his control any device capable of causing emission of smoke, gas, or fumes, and which may be used for the purpose

of hindering, delaying, or preventing pursuit or capture, any explosive, or any firearm (as defined in sec. 2733), except a machine gun, or a shotgun or rifle having a barrel of less than eighteen inches in length, shall be fined not more than $5,000 or be imprisoned for not more than 10 years, or both, and all persons engaged in any such violation or in aiding in any such violation shall be held to be in possession or control of such device, firearm, or explosive.

(2) Whoever, when violating any such law, has in his possession or in his control a machine gun, or any shotgun or rifle having a barrel of less than eighteen inches in length, shall be punished by imprisonment for not more than twenty years; and all persons engaged in any such violation or in aiding in any such violation shall be held to be in possession and control of such machine gun, shotgun, or rifle.

(3) Every such firearm or device for emitting gas, smoke, or fumes, and every such explosive, machine gun, shotgun, or rifle, in the possession or control of any person when violating any such law, shall be seized and shall be forfeited and disposed of in the manner provided by section 2730.

(4) As used in this subsection the term "machine gun" means any weapon which shoots, or is designed to shoot, automatically or semiautomatically, more than one shot, without manual reloading, by a single function of the trigger.

5. Sections of the Internal Revenue Code Relating to the Illicit Traffic in Liquors

Various sections of the Internal Revenue Code prohibit the manufacture, possession, transportation, and sale of nontaxpaid liquors. Every gallon of 100 proof nontaxpaid liquor manufactured defrauds the Government of $10.50 tax under the present rate.

As an effective aid to law enforcement in general and for the protection of the country's revenue the cooperation of all prosecutive and law enforcement officers is solicited.

In many instances citizens of good repute possess firearms as defined in the National Firearms Act, principally war trophies, such as machine guns and machine pistols, and have failed to register them with the Commissioner of Internal Revenue, being unaware of this requirement by law. In instances of this kind, as well as in all others where there is an apparent violation of one or more of the laws referred to, it will be greatly appreciated if contact is made with the local alcohol and tobacco tax office of the Internal Revenue Service in order that an Investigator may be assigned for the purpose of determining the proper action to be taken.

Mutual cooperation in this regard will result in better law enforcement.

Rev. Rul. 153*

Procedure relating to tobacco invoices, Form 774

1. Beginning with the filing of their July 1953 returns or reports, Forms 62, 62-A, 72-Parts 1 and 2, and 775, manufacturers of tobacco,

*Originally issued as IR Mimeograph 248 dated July 24, 1953.

snuff, cigars, and cigarettes, and dealers in leaf tobacco will no longer submit, with such monthly returns and reports, tobacco invoices, Form 774, covering tobacco materials received and shipped.

2. Form 774 will be prepared in the usual manner in connection with each shipment or removal of tobacco materials, and the original (white) invoice forwarded to the consignee, in the case of a domestic shipment, or to the customs officers at the port, in the case of an export shipment. Except the duplicate (yellow) invoice retained by customs officers in the case of tobacco imported, and the original invoice retained by customs officers in the case of tobacco exported, manufacturers and dealers shall retain the original invoice covering each lot of tobacco received and the duplicate invoice covering each lot of tobacco shipped. In the case of receipt of tobacco from farmers, the duplicate invoices in such cases shall be submitted, on or before the 10th day of each month, to: Bureau of Agricultural Economics, Department of Agriculture, Washington 25, D. C., Attention: Field Crops Division.

3. The original and duplicate invoices retained by manufacturers and dealers shall be kept separately by months, in the order of dates of receipt and shipment of the tobacco, to agree with the entries in their revenue records. The tobacco invoices so retained by manufacturers and dealers shall be kept for a period of 2 calendar years after the close of the year in which the tobacco covered by the invoices was received or shipped, and such invoices shall be available at all times for inspection by any internal revenue officer upon request of such officer.

4. Correspondence relating to this Revenue Ruling should refer to the number and date thereof and to the symbols O:AT:T.

Rev. Rul. 212

Expansion of the program of publishing Revenue Rulings announced in Rev. Rul. 2, C. B. 1953-1, 484, to include rulings addressed to taxpayers or their representatives.

SECTION 1. PURPOSE.

Revenue Ruling 2, C. B. 1953-1, 484, established a system for increased publication in the Internal Revenue Bulletin of communications to field offices involving substantive tax law, procedures affecting taxpayers' rights or duties, or industry regulation. The purpose of this Revenue Ruling is to expand the publication of rulings program to include rulings addressed to taxpayers or their representatives. Accordingly, effective immediately, all such rulings, instructions, and other communications will be considered from the standpoint of publication, whether addressed to field officers, taxpayers, taxpayers' representatives, trade associations, or others.

SEC. 2. PUBLICATION APPROACH.

Under this expanded program, it is the policy to publish in the Internal Revenue Bulletin all rulings, as well as procedures directly affecting taxpayers' basic rights or duties, which may serve as precedents or guides to examining officers and other personnel of the Internal Revenue Service, as well as to the general public.

SEC. 3. PUBLICATION STANDARDS AND PROCEDURES.

Generally, the standards, procedures and form of publication announced in Rev. Rul. 2, *supra*, for controlling the consideration of communications to field offices for purposes of publication will be applicable under the terms of this Revenue Ruling. Thus, every communication dealing with substantive tax law, procedures affecting taxpayers' rights or duties, or industry regulation, will be deemed to be of a character potentially publishable and will be fully considered for publication purposes, unless it clearly falls within any of the exceptions enumerated in paragraph 4 of such Revenue Ruling. However, every communication which has been referred to the Office of the Chief Counsel for review, or is based on a memorandum from the Chief Counsel in the same case, will automatically be considered to be of a potentially publishable character and will be channelled into proper publication procedures for consideration, even though it may fall within one of such exceptions. Communications relating solely to matters of internal management are excepted.

SEC. 4. EFFECT ON OTHER DOCUMENTS.

This Revenue Ruling does not revoke Rev. Rul. 2, *supra*, but merely modifies and supplements it as indicated above and extends the existing publication standards and procedures to all rulings and like communications.

Rev. Rul. 266*

Policy respecting reopening of agreed issues, and raising of new issues, in income and profits tax cases on appeal from examining officers' findings.

1. We are confronted with a seriously congested situation in the Appellate Division and in the Tax Court. We have given considerable thought to this problem and the purpose of this Revenue Ruling is to outline some of the means by which this congestion may be relieved and the number of unagreed cases and issues may be reduced in the future.

2. The obvious beginning point is to increase the number of agreements obtained by the examining officers and the group supervisors. Steps to achieve this already have been taken by increasing the degree of finality accorded such agreements, thereby making them more attractive to taxpayers and their representatives. Further progress can be made by impressing upon group supervisors and upon reviewers in the Audit Division that an agreed issue should not be reopened—and neither should a new issue be raised—unless the ground for such action is a substantial one and the potential effect upon the tax liability is material. The foregoing applies also to the reopening of agreed issues and the raising of new issues by the Appellate Division. At all levels, there should be a clear understanding of the policy against raising issues for trading purposes only, as well as the prohibition against nuisance-value settlements.

3. A field in which effort should be expended is that of obtaining partial agreements. In any case in which no agreement can be se-

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* Originally issued as IR-Mimeograph 298, dated October 9, 1953.

cured with respect to one or more issues or years, we should encourage agreement with respect to the other issues or years. These partial agreements may be reached with the examining officer or the group supervisor in the Audit Division, or in the Appellate Division. In each instance where it is appropriate, an opportunity to waive the restrictions on assessment and collection should be provided so as to avoid accumulation of interest cost to the taxpayer. However, the execution of such a waiver should not be considered a prerequisite to a partial agreement of the type discussed in this Revenue Ruling.

4. In each case in which a partial agreement is reached in the Audit Division, the revenue agent's report should clearly and completely set forth the agreement so that the Appellate Division need not reconsider properly determined issues. The difficulties encountered in this regard prior to the reorganization may be avoided by incorporating in the agent's report the decisions reached at the conclusion of the Audit Division's consideration of the case. Also, in any instance in which the taxpayer's protest indicates that a partial agreement is not set forth correctly in the agent's report, this difference should be considered by the Audit Division and appropriate action taken prior to transmittal of the case to the Appellate Division.

5. The provisions of this Revenue Ruling relating to partial agreements shall not apply in any case in which criminal prosecution is under consideration or is pending, or in any other instance (for example, if assessment or collection of the tax is in jeopardy) where in the opinion of the director or of the Assistant Regional Commissioner, Appellate, the interests of the Government will be prejudiced.

6. In the application of the policies discussed in the foregoing paragraphs, the broad objective should be to achieve a greater degree of finality in a larger number of cases at the earliest possible administrative stage.

SECTION 3310.—RETURNS AND PAYMENT OF TAX

Rev. Rul. 254*

INTERNAL REVENUE CODE

Form 720, Quarterly Federal Excise Tax Return-Statement to be furnished by taxpayer whose records do not supply a portion of the information called for on the return.

SECTION 1. PURPOSE.

The purpose of this Revenue Ruling is to provide rules to be followed in connection with the preparation of Form 720, Quarterly Federal Excise Tax Return.

SEC. 2. DESCRIPTION OF FORM 720.

Form 720 replaces a number of monthly returns formerly prescribed for reporting many excise taxes. It will be filed by taxpayers for the quarter ending September 30, 1953, and subsequent quarters. One of the important features of this new form is the request (in columns 2, 3, and 4) for certain information on taxable sales, services,

*Originally issued as IR-Mimeograph 289, dated September 30, 1953.

or charges, and on exemptions or adjustments, which was not required on previous return forms, but which is designed to aid in the examination of tax returns.

SEC. 3. PREPARATION OF RETURNS.

.01 Treasury Department regulations require taxpayers to maintain records adequate to permit a determination of the tax due. However, notwithstanding the requirements of the regulations, many taxpayers never have geared their accounting to these requirements. Accordingly, the instructions accompanying Form 720 relating to the requirements for completing columns 2, 3, or 4 on the form are modified to the extent provided in the following paragraphs.

.02 The Internal Revenue Service will accept returns on Form 720 in which the taxpayer completes the information called for in items 1 through 5 and shows the amount of tax in column 6 of the appropriate schedule on the form. Taxpayers should, however, complete such other portions of the form as may be feasible, and should supply such additional data as they can based upon existing records of purchases, sales, production, and inventories.

.03 Taxpayers who do not supply the data called for on Form 720 should attach to the form as filed for either the quarter ending September 30, 1953, or for the quarter ending December 31, 1953, a brief statement explaining the failure to supply the necessary data and describing the system employed by the taxpayer to assure the proper determination of excise tax liability. Where the taxpayer is a member of an organization which submits to the Internal Revenue Service a statement of the accounting procedures used by their members, the taxpayer may attach a copy of such statement or refer to such statement, in lieu of submitting a separate statement, if the taxpayer's procedures are in accordance with that described by the organization.

.04 The taxpayer need furnish the foregoing statement only once, unless a further explanation is requested or unless a change in his record-keeping procedures affects his ability to fill in the return or determine the tax. Such statements will be used in connection with audit considerations to be given to such returns and for such reports as may be requested by the National Office as to compliance.

SEC. 4. PERIOD TO WHICH THIS POLICY IS APPLICABLE.

It is intended that this policy will apply to returns covering all quarters through June 30, 1954. Instructions relating to returns for quarters ending after June 30, 1954, will be issued prior to July 1, 1954.

SEC. 5. INQUIRIES.

Taxpayers are invited to consult with district directors of internal revenue about any problem relating to the requirements for filling in Form 720.

SECTION 3657.—PAYMENT BY UNITED STATES NOTES AND CERTIFICATES OF INDEBTEDNESS

D. C. 922

INTERNAL REVENUE CODE

UNITED STATES OF AMERICA.—TREASURY SAVINGS NOTES.—SERIES B

[1953. Department Circular No. 922. Fiscal Service. Bureau of the Public Debt]

TREASURY DEPARTMENT,
OFFICE OF THE SECRETARY,
Washington, May 11, 1953.

Subpart
A. Offering of Notes.
B. Description of Notes.
C. Purchase of Notes.
D. Presentation in Payment of Taxes.
E. Cash Redemption at or Before Maturity.
F. Payment or Reissue to Other Than Inscribed Owner.
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SUBPART A: OFFERING OF NOTES

SECTION 334.1. The Secretary of the Treasury, pursuant to the authority of the Second Liberty Bond Act, as amended, offers for sale to the people of the United States, at par and accrued interest as provided in section 334.12 hereof, an issue of notes of the United States designated Treasury Savings Notes, Series B, which notes, if inscribed in the name of a Federal taxpayer, will be receivable as hereinafter provided at par and accrued interest in payment of income, estate, and gift taxes imposed by the Internal Revenue Code, or laws amendatory or supplementary thereto. The notes may also be redeemed for cash at par and accrued interest, with certain exceptions applicable to banking institutions, as provided in section 334.16 hereof.

SEC. 334.2. WITHDRAWAL OF SERIES A NOTES.—The sale of Treasury Savings Notes, Series A, offered under Department Circular No. 889 [C. B. 1951-2, 221], dated May 10, 1951, is hereby terminated at the close of business May 14, 1953.

SEC. 334.3. DURATION OF OFFER.—The sale of notes of Series B offered by this circular will begin on May 15, 1953, and will continue until terminated by the Secretary of the Treasury.

SEC. 334.4. DEFINITIONS.—(*a*) The word "month" as used herein means the period from and including the 15th day of any 1 calendar month to but not including the 15th day of the next succeeding month.

(*b*) The words "issue date" mean the date as of which a note is issued and will always be the 15th day of a calendar month.

(*c*) The words "interest accrual date" or "accrual date" mean the date upon which a month's interest accrues on a note, the first accrual date being the 15th day of the calendar month next following the issue date.

SUBPART B: DESCRIPTION OF NOTES

SEC. 334.5. GENERAL.—Treasury Savings Notes, Series B, will in each instance be dated as of the 15th day of a calendar month. The issue date will be determined by the day of the month on which payment at par and accrued interest, if any, is received and credited by an agency authorized to issue the notes. For example, payment received

and credited on any day during the period from and including May 15, 1953, to and including June 14, 1953, would result in the issue of notes dated May 15, 1953. They will mature 2 years from that date and may not be called by the Secretary of the Treasury for redemption before maturity. All notes bearing issue dates within any 1 calendar year shall constitute a separate series indicated by the letter "B" followed by the year of maturity. At the time of issue the issuing agency will inscribe on the face of each note the name and address of the owner, will enter the issue date, and will imprint its dating stamp (with current date). The notes will be issued in denominations of $100, $500, $1,000, $5,000, $10,000, $100,000, $500,000, and $1,000,000. Exchange of authorized denominations from higher to lower, but not from lower to higher, may be arranged at any agency that issues Treasury Savings Notes, Series B.

SEC. 334.6. ACCEPTANCE FOR TAXES OR CASH REDEMPTION.—If inscribed in the name of an individual, corporation, or other entity paying income, estate, or gift taxes imposed under the Internal Revenue Code, or laws amendatory or supplementary thereto, the notes will be receivable, subject to the provisions of section 334.15 of this circular, at par and accrued interest, in payment of such income, estate, or gift taxes assessed against the owner or his estate. If not presented in payment of taxes, or if not inscribed in the name of a taxpayer liable to the above-described taxes, and subject to the provisions of section 334.16 of this circular, the notes will be payable at maturity, or at the owner's option and request they will be redeemable before maturity at par and accrued interest.

SEC. 334.7. INTEREST.—Interest on each $1,000 principal amount of Treasury Savings Notes, Series B, will accrue monthly on the 15th calendar day of each month after the issue date on a graduated scale, as follows:

	Each month
First to sixth months, inclusive	$1.80
Seventh to twelfth months, inclusive	2.10
Thirteenth to eighteenth months, inclusive	2.20
Nineteenth to twenty-fourth months, inclusive	2.30

The table [1] appended to this circular shows for notes of each denomination, for each consecutive month after issue date to maturity, (*a*) the amount of interest accrual, (*b*) the principal amount of the note with accrued interest (cumulative) added, and (*c*) the approximate investment yields. Subject to the provisions of sections 334.15 and 334.16 hereof, when Treasury Savings Notes, Series B, are to be paid on an interest accrual date, the payment will include interest accruing on that date; otherwise, interest will be paid only to the interest accrual date next preceding the date of payment. Interest will be paid only with the principal amount, and will not accrue beyond the maturity date of the note.

SEC. 334.8. FORMS OF INSCRIPTION.—Treasury Savings Notes, Series B, may be inscribed in the name of an individual, corporation, unincorporated association or society, or a fiduciary (including trustees under a duly established trust where the notes would not be held as security for the performance of a duty or obligation), whether or not the inscribed owner is subject to taxation under the Internal Revenue Code, or laws amendatory or supplementary thereto. They may also be inscribed in the name of a town, city, county, or State or other governmental body, and in the name of a partnership, but notes in the

[1] The table is omitted from this publication of the Circular.

name of a partnership are not acceptable in payment of taxes, since the partnership is not a taxpaying entity under the Internal Revenue Code. The notes will not be inscribed in the names of two or more persons as joint owners or coowners; or in the name of a public officer, whether or not named as trustee, where the notes would in effect be held as security for the performance of a duty or obligation.

SEC. 334.9. RESTRICTIONS ON TRANSFER.—Except as otherwise specifically provided herein, the notes may not be transferred, reissued, hypothecated, or pledged as security, may not be paid to any person other than the owner, and may not be accepted in payment of Federal income, estate, or gift taxes assessed against any person other than the owner. The notes will not be acceptable to secure deposits of public moneys.

SEC. 334.10. TAXATION.—Income derived from the notes shall be subject to all taxes now or hereafter imposed under the Internal Revenue Code or laws amendatory or supplementary thereto. The notes shall be subject to estate, inheritance, gift, or other excise taxes, whether Federal or State, but shall be exempt from all taxation now or hereafter imposed on the principal or interest thereof by any State, or any of the possessions of the United States, or by any local taxing authority.

SUBPART C: PURCHASE OF NOTES

SEC. 334.11. OFFICIAL AGENCIES.—In addition to the Treasury Department, the Federal Reserve banks and their branches are hereby designated agencies for the issue and redemption of Treasury Savings Notes, Series B. The Secretary of the Treasury, from time to time, in his discretion, may designate other agencies for the issue of the notes, or for accepting applications therefor, or for making payments on account of the redemption thereof.

SEC. 334.12. APPLICATIONS AND PAYMENT.—Applications will be received by the Federal Reserve banks and branches and by the Treasurer of the United States, Washington, D. C. Banking institutions generally may submit applications for the account of customers but only the Federal Reserve banks, their branches, and the Treasury Department are authorized to act as official agencies. The use of an official application form is desirable but not necessary. Such forms may be obtained upon request from any Federal Reserve bank or branch or the Treasurer of the United States. Every application must be accompanied by payment in full, at par and accrued interest, if any. The amount of accrued interest payable by the purchaser will be computed at the rate at which interest accrues on the notes ($1.80 per month per $1,000 par amount) for the actual number of days from but not including the issue date to and including the date funds are credited to the account of the Treasurer of the United States. For example, if funds are credited on the 20th day of January the issue date will be January 15, and 5 days' accrued interest must be paid by the purchaser. If collection is delayed so that credit is not given until February 15, the issue date will be February 15, and no accrued interest will be collectible. One day's accrued interest for a 31-day period is $0.05806 per $1,000, for a 30-day period $0.06 per $1,000, for a 29-day period $0.06207 per $1,000, and for a 28-day period $0.06429 per $1,000. Any form of exchange, including personal checks, will be accepted, subject to collection, and should be drawn to

the order of the Federal Reserve bank or the Treasurer of the United States, as payee, as the case may be. Any depositary qualified pursuant to the provisions of Treasury Department Circular No. 92, Revised, as amended, will be permitted to make payment by credit for notes applied for on behalf of itself or its customers up to any amount for which it shall be qualified in excess of existing deposits.

SEC. 334.13. RESERVATIONS.—The Secretary of the Treasury reserves the right to reject any application in whole or in part, and to refuse to issue or permit to be issued hereunder any notes in any case or in any class or classes of cases if he deems such action to be in the public interest, and his action in any such respect shall be final. If an application is rejected, in whole or in part, any payment received therefor will be refunded.

SEC. 334.14. DELIVERY OF NOTES.—Upon acceptance of a full-paid application, notes will be duly inscribed and, unless delivered in person, will be delivered, at the risk and expense of the United States at the address given by the purchaser, by mail, but only within the United States, its Territories and Island Possessions, and the Canal Zone. No deliveries elsewhere will be made.

SUBPART D: PRESENTATION IN PAYMENT OF TAXES

SEC. 334.15. At any time after 2 months from the issue date, during such time and under such rules and regulations as the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, may prescribe, notes issued hereunder in the name of a Federal taxpayer, may be presented by such taxpayer, his agent, or his estate for credit against any income (current and back, personal and corporation taxes, and excess-profits taxes) or any estate or gift taxes (current and back) imposed by the Internal Revenue Code, or laws amendatory or supplementary thereto, assessed against the inscribed owner or his estate. For example, a note dated January 15 may be presented for credit against taxes due March 15. The notes will be receivable by the director of internal revenue at par and accrued interest to the day (but no accrual beyond maturity) when the taxes are due, if such day falls on the 15th day of a calendar month, whether the notes are received on or before that day. If the taxes are due on any other day of the month than the 15th, accrued interest will be credited to the accrual date next preceding the day when the taxes are due. Notes are receivable only in payment of taxes equal to or exceeding the entire value of the notes, including accrued interest. The notes must be forwarded to the director at the risk and expense of the owner and, for his protection, should be forwarded by registered mail, if not presented in person.

SUBPART E: CASH REDEMPTION AT OR BEFORE MATURITY

SEC. 334.16. GENERAL.—Any Treasury Savings Note, Series B, not presented in payment of taxes will be paid at maturity, or, at the option and request of the owner, and without advance notice, will be redeemed before maturity, at any time after 4 months from the issue date. For example, a note dated January 15 may be redeemed for cash on or after May 15. If redemption prior to maturity is requested on an interest accrual date the redemption will include interest accruing on that date, otherwise redemption will be at par and accrued

interest to the interest accrual date next preceding the redemption date, except in the case of a note inscribed in the name of a bank that accepts demand deposits, in which case payment, whether at or before maturity, will be made only at par, with a refund of any accrued interest which may have been paid at the time of purchase of the note. If a note is acquired by a banking institution through forfeiture of a loan, payment will be made at par and the accrued interest payable as of the date of acquisition.

SEC. 334.17. EXECUTION OF REQUEST FOR PAYMENT.—The owner in whose name the note is inscribed must appear before one of the officers authorized by the Secretary of the Treasury to witness and certify requests for payment, establish his identity, and in the presence of such officer sign and complete the request for payment appearing on the back of the note. After the request for payment has been executed, the witnessing officer should execute the certificate provided for his use.

SEC. 334.18. OFFICERS AUTHORIZED TO CERTIFY REQUESTS FOR PAYMENT.—All officers authorized to certify request for payment of United States Savings Bonds, as set forth in Treasury Department Circular No. 530, Seventh Revision, as amended, are hereby authorized to certify requests for cash redemption of Treasury savings notes issued under this circular. Such officers include, among others, United States postmasters, certain other post office officials, officers of all banks and trust companies incorporated in the United States or its territories, including officers at branches thereof, and commissioned and warrant officers of the Armed Forces of the United States.

SEC. 334.19. PRESENTATION AND SURRENDER.—Notes bearing properly executed requests for payment must be presented and surrendered to any Federal Reserve bank or branch or to the Treasurer of the United States, Washington 25, D. C., at the expense and risk of the owner. For the owner's protection, notes should be forwarded by registered mail, if not presented in person.

SEC. 334.20. PARTIAL REDEMPTION.—Partial cash redemption of a note, corresponding to an authorized denomination, may be made in the same manner as full cash redemption, appropriate changes being made in the request for payment. In case of partial redemption of a note, the remainder will be reissued in the same name and with the same issue date as the note surrendered.

SEC. 334.21. PAYMENT.—Payment of any note, either at maturity or on redemption before maturity, will be made by any Federal Reserve bank or branch or the Treasurer of the United States, following clearance with the agency of issue, which will be obtained by the agency to which the note is surrendered. Payment will be made by check drawn to the order of the owner, and mailed to the address given in his request for payment, or by credit in any account maintained by a banking institution with the Federal Reserve bank of its district.

SUBPART F: PAYMENT OR REISSUE TO OTHER THAN INSCRIBED OWNER

SEC. 334.22. PRESENTATION AND SURRENDER.—A note may be paid or reissued in accordance with any of the provisions of this subpart only upon the presentation and surrender of the note at the risk and expense of the owner to the issuing agency, accompanied by an appropriate request for the particular transaction.

SEC. 334.23. AUTHORIZED TRANSFERS.—(*a*) *Between husband and wife.*—A note inscribed in the name of a married man may be reissued in the name of his wife, and a note inscribed in the name of a married woman may be reissued in the name of her husband.

(*b*) *Between affiliated corporations.*—A note inscribed in the name of a parent corporation, which is hereby defined as a corporation owning more than 50 percent of the stock, with voting power, of another corporation, may be reissued in the name of a subsidiary, and a note registered in the name of a subsidiary may be reissued in the name of the parent corporation.

SEC. 334.24. AUTHORIZED PLEDGE.—A note may be pledged as collateral for a loan from a banking institution, and if title thereto is acquired by the institution because of default in the payment of the loan, the notes will be redeemed at par and accrued interest to the interest accrual date next preceding the date of such acquisition, unless acquired on an interest accrual date, in which case redemption will be made at par and accrued interest to that date. Proof of the date of acquisition must be furnished, and payment must be requested by the pledgee under a power of attorney given by the pledgor in whose name the note is inscribed. The note will not be transferred to the pledgee.

SEC. 334.25. PAYMENT TO REPRESENTATIVES OF DECEASED OR INCOMPETENT OWNERS AND PAYMENT OR REISSUE TO HEIRS OR LEGATEES OF DECEASED OWNERS.—In case of the death or disability of an individual owner, if the notes are not to be presented in payment of taxes, payment will be made to the duly constituted representative of his estate, or they may be reissued to one or more of his heirs or legatees upon satisfactory proof of their right; but no reissue will be made in the names of two or more persons jointly or as coowners.

SEC. 334.26. PAYMENT OR REISSUE TO SUCCESSORS OF CORPORATIONS, UNINCORPORATED ASSOCIATIONS OR PARTNERSHIPS.—If a corporation or unincorporated body in whose name notes are inscribed is dissolved, consolidated, merged or otherwise changes its organization, the notes may be paid to, or reissued in the name of, those persons or organizations lawfully entitled to the assets of such corporation or body by reason of such changes in organization.

SEC. 334.27. PAYMENT TO REPRESENTATIVES OF BANKRUPT OR INSOLVENT OWNERS.—If an owner of notes is declared bankrupt or insolvent, payment, but not reissue, will be made to the duly qualified trustee, receiver, or similar representative if the notes are submitted with satisfactory proof of his appointment and qualification.

SEC. 334.28. PAYMENT AS A RESULT OF JUDICIAL PROCEEDINGS.—Payment, but not reissue, will be made as a result of judicial proceedings in a court of competent jurisdiction, if the notes are submitted with proper proof of such proceedings and their finality.

SEC. 334.29. INSTRUCTIONS AND INFORMATION.—Before executing the request for payment or submitting the notes under the provisions of this subpart, instructions should be obtained from a Federal Reserve bank or branch or from the Treasury Department, Division of Loans and Currency, Washington 25, D. C.

SUBPART G: GENERAL PROVISIONS

SEC. 334.30. REGULATIONS.—Except as provided in this circular, the notes issued hereunder will be subject to the general regulations of the

Treasury Department, now or hereafter prescribed, governing bonds and notes of the United States; the regulations currently in force are contained in Department Circular No. 300, as amended.

SEC. 334.31. LOSS, THEFT OR DESTRUCTION.—In case of the loss, theft or destruction of a savings note immediate notice (which should include a full description of the note) should be given the agency which issued the note and instructions should be requested as to the procedure necessary to secure a duplicate.

SEC. 334.32. FISCAL AGENTS.—Federal Reserve banks and their branches, as fiscal agents of the United States, are authorized to perform such services or acts as may be appropriate and necessary under the provisions of this circular and under any instructions given by the Secretary of the Treasury, and they may issue interim receipts pending delivery of the definitive notes.

SEC. 334.33. AMENDMENTS.—The Secretary of the Treasury may at any time or from time to time supplement or amend the terms of this circular, or of any amendments or supplements thereto, and may at any time or from time to time prescribe amendatory rules and regulations governing the offering of the notes, information as to which will promptly be furnished to the Federal Reserve banks.

G. M. HUMPHREY,
Secretary of the Treasury.

D. C. 931

INTERNAL REVENUE CODE

UNITED STATES OF AMERICA.—TREASURY SAVINGS NOTES.—SERIES C

[1953. Department Circular No. 931. Fiscal Service. Bureau of the Public Debt]

TREASURY DEPARTMENT,
OFFICE OF THE SECRETARY,
Washington, October 1, 1953.

Subpart:
A. Offering of Notes.
B. Description of Notes.
C. Purchase of Notes.
D. Presentation in Payment of Taxes.
E. Cash Redemption at or Before Maturity.
F. Payment or Reissue to Other Than Inscribed Owner.
G. General Provisions.

SUBPART A: OFFERING OF NOTES

SECTION 335.1. The Secretary of the Treasury, pursuant to the authority of the Second Liberty Bond Act, as amended, offers for sale to the people of the United States, at par and accrued interest as provided in section 335.11 hereof, an issue of notes of the United States designated Treasury Savings Notes, Series C, which notes, if inscribed in the name of a Federal taxpayer, will be receivable as hereinafter provided at par and accrued interest in payment of income, estate, and gift taxes imposed by the Internal Revenue Code, or laws amendatory or supplementary thereto. The notes may also be redeemed for cash at par and accrued interest, with certain exceptions applicable to banking institutions, as provided in section 335.15 hereof.

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SEC. 335.2. DURATION OF OFFER.—The sale of notes of Series C offered by this circular will begin on October 1, 1953, and will continue until terminated by the Secretary of the Treasury.

SEC. 335.3. DEFINITIONS.—(*a*) The word "month" as used herein means the period from and including the 15th day of any 1 calendar month to but not including the 15th day of the next succeeding month.

(*b*) The words "issue date" mean the date as of which a note is issued and will always be the 15th day of a calendar month.

(*c*) The words "interest accrual date" or "accrual date" mean the date upon which a month's interest accrues on a note, the first accrual date being the 15th day of the calendar month next following the issue date.

SUBPART B: DESCRIPTION OF NOTES

SEC. 335.4. GENERAL.—Treasury Savings Notes, Series C, will in each instance be dated as of the 15th day of a calendar month. The issue date will be determined by the day of the month on which payment at par and accrued interest, if any, is received and credited by an agency authorized to issue the notes. For example, payment received and credited on any day during the period from and including October 1, 1953, to and including October 14, 1953, would result in the issue of notes dated September 15, 1953. They will mature 2 years from that date and may not be called by the Secretary of the Treasury for redemption before maturity. All notes bearing issue dates within any 1 calendar year shall constitute a separate series indicated by the letter "C" followed by the year of maturity. At the time of issue the issuing agency will inscribe on the face of each note the name and address of the owner, will enter the issue date and will imprint its dating stamp (with current date). The notes will be issued in denominations of $100, $500, $1,000, $5,000, $10,000, $100,000, $500,000, and $1,000,000. Exchange of authorized denominations from higher to lower, but not from lower to higher, may be arranged at any agency that issues Treasury Savings Notes, Series C.

SEC. 335.5. ACCEPTANCE FOR TAXES OR CASH REDEMPTION.—If inscribed in the name of an individual, corporation, or other entity paying income, estate, or gift taxes imposed under the Internal Revenue Code, or laws amendatory or supplementary thereto, the notes will be receivable, subject to the provisions of section 335.14 of this circular, at par and accrued interest, in payment of such income, estate, or gift taxes assessed against the owner or his estate. If not presented in payment of taxes, or if not inscribed in the name of a taxpayer liable to the above-described taxes, and subject to the provisions of section 335.15 of this circular, the notes will be payable at maturity, or at the owner's option and request they will be redeemable before maturity at par and accrued interest.

SEC. 335.6. INTEREST.—Interest on each $1,000 principal amount of Treasury Savings Notes, Series C, will accrue monthly on the 15th calendar day of each month after the issue date on a graduated scale. Interest accruals on the notes first issued hereunder shall be as follows:

	Each month
First to sixth months, inclusive	$1.30
Seventh to twelfth months, inclusive	1.90
Thirteenth to eighteenth months, inclusive	2.10
Nineteenth to twenty-fourth months, inclusive	2.20

The Secretary of the Treasury may at any time terminate the issuance of notes hereunder with interest accruals as provided above, and may at any time, or from time to time, authorize the issuance of additional notes hereunder with such other interest accruals as he may prescribe. The table appended to this circular shows for notes of each denomination, for each consecutive month after issue date to maturity, (*a*) the amount of interest accrual, (*b*) the principal amount of the note with accrued interest (cumulative) added, and (*c*) the approximate investment yields. Subject to the provisions of sections 335.14 and 335.15 hereof, when Treasury Savings Notes, Series C, are to be paid on an interest accrual date, the payment will include interest accruing on that date; otherwise, interest will be paid only to the interest accrual date next preceding the date of payment. Interest will be paid only with the principal amount, and will not accrue beyond the maturity date of the note.

SEC. 335.7. FORMS OF INSCRIPTION.—Treasury Savings Notes, Series C, may be inscribed in the name of an individual, corporation, unincorporated association or society, or a fiduciary (including trustees under a duly established trust where the notes would not be held as security for the performance of a duty or obligation), whether or not the inscribed owner is subject to taxation under the Internal Revenue Code, or laws amendatory or supplementary thereto. They may also be inscribed in the name of a town, city, county, or State or other governmental body, and in the name of a partnership, but notes in the name of a partnership are not acceptable in payment of taxes, since a partnership is not a taxpaying entity under the Internal Revenue Code. The notes will not be inscribed in the names of two or more persons as joint owners or coowners; or in the name of a public officer, whether or not named as trustee, where the notes would in effect be held as security for the performance of a duty or obligation.

SEC. 335.8. RESTRICTIONS ON TRANSFER.—Except as otherwise specifically provided herein, the notes may not be transferred, reissued, hypothecated, or pledged as security, may not be paid to any person other than the owner, and may not be accepted in payment of Federal income, estate, or gift taxes assessed against any person other than the owner. The notes will not be acceptable to secure deposits of public moneys.

SEC. 335.9. TAXATION.—Income derived from the notes shall be subject to all taxes now or hereafter imposed under the Internal Revenue Code or laws amendatory or supplementary thereto. The notes shall be subject to estate, inheritance, gift, or other excise taxes, whether Federal or State, but shall be exempt from all taxation now or hereafter imposed on the principal or interest thereof by any State, or any of the possessions of the United States, or by any local taxing authority.

SUBPART C: PURCHASE OF NOTES

SEC. 335.10. OFFICIAL AGENCIES.—In addition to the Treasury Department, the Federal Reserve banks and their branches, are hereby designated agencies for the issue and redemption of Treasury Savings Notes, Series C. The Secretary of the Treasury, from time to time, in his discretion, may designate other agencies for the issue of the

notes, or for accepting applications therefor, or for making payments on account of the redemption thereof.

SEC. 335.11. APPLICATIONS AND PAYMENT.—Applications will be received by the Federal Reserve banks and branches and by the Treasurer of the United States, Washington, D. C. Banking institutions generally may submit applications for the account of customers but only the Federal Reserve banks, their branches and the Treasury Department are authorized to act as official agencies. The use of an official application form is desirable but not necessary. Such forms may be obtained upon request from any Federal Reserve bank or branch or the Treasurer of the United States. Every application must be accompanied by payment in full, at par and accrued interest, if any. The amount of accrued interest payable by the purchaser will be computed at the rate at which interest accrues on the notes ($1.30 per month per $1,000 par amount) for the actual number of days from but not including the issue date to and including the date funds are credited to the account of the Treasurer of the United States. For example, if funds are credited on the 20th day of January the issue date will be January 15, and 5 days' accrued interest must be paid by the purchaser. If collection is delayed so that credit is not given until February 15, the issue date will be February 15, and no accrued interest will be collectible. One day's accrued interest for a 31-day period is $0.04194 per $1,000, for a 30-day period $0.04333 per $1,000, for a 29-day period $0.04483 per $1,000, and for a 28-day period $0.04643 per $1,000. Any form of exchange, including personal checks, will be accepted, subject to collection, and should be drawn to the order of the Federal Reserve bank or the Treasurer of the United States, as payee, as the case may be. Any depositary qualified pursuant to the provisions of Treasury Department Circular No. 92, Revised, as amended, will be permitted to make payment by credit for notes applied for on behalf of itself or its customers up to any amount for which it shall be qualified in excess of existing deposits.

SEC. 335.12. RESERVATIONS.—The Secretary of the Treasury reserves the right to reject any application in whole or in part, and to refuse to issue or permit to be issued hereunder any notes in any case or in any class or classes of cases if he deems such action to be in the public interest, and his action in any such respect shall be final. If an application is rejected, in whole or in part, any payment received therefor will be refunded.

SEC. 335.13. DELIVERY OF NOTES.—Upon acceptance of a full-paid application, notes will be duly inscribed and, unless delivered in person, will be delivered, at the risk and expense of the United States at the address given by the purchaser, by mail, but only within the United States, its Territories and Island Possessions, and the Canal Zone. No deliveries elsewhere will be made.

SUBPART D: PRESENTATION IN PAYMENT OF TAXES

SEC. 335.14. At any time after 2 months from the issue date, during such time and under such rules and regulations as the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, may prescribe, notes issued hereunder in the name of a Federal taxpayer, may be presented by such taxpayer, his agent or his

estate for credit against any income (current and back, personal and corporation taxes, and excess-profits taxes) or any estate or gift taxes (current and back) imposed by the Internal Revenue Code, or laws amendatory or supplementary thereto, assessed against the inscribed owner or his estate. For example, a note dated January 15 may be presented for credit against taxes due March 15. The notes will be receivable by the district director of internal revenue at par and accrued interest to the day (but no accrual beyond maturity) when the taxes are due, if such day falls on the 15th day of a calendar month, whether the notes are received on or before that day. If the taxes are due on any other day of the month than the 15th, accrued interest will be credited to the accrual date next preceding the day when the taxes are due. Notes are receivable only in payment of taxes equal to or exceeding the entire value of the notes, including accrued interest. The notes may be forwarded to the district director at the risk and expense of the owner and, for his protection, should be forwarded by registered mail, if not presented in person. The notes may also be deposited with a Federal Reserve bank or branch and a receipt obtained therefor which may be forwarded to the district director in lieu of the notes.

SUBPART E: CASH REDEMPTION AT OR BEFORE MATURITY

SEC. 335.15. GENERAL.—Any Treasury Savings Note, Series C, not presented in payment of taxes will be paid at maturity, or, at the option and request of the owner, and without advance notice, will be redeemed before maturity at any time after 4 months from the issue date. For example, a note dated January 15 may be redeemed for cash on or after May 15. If redemption prior to maturity is requested on an interest accrual date the redemption will include interest accruing on that date, otherwise redemption will be at par and accrued interest to the interest accrual date next preceding the redemption date, except in the case of a note inscribed in the name of a bank that accepts demand deposits, in which case payment, whether at or before maturity, will be made only at par, with a refund of any accrued interest which may have been paid at the time of purchase of the note. If a note is acquired by a banking institution through forfeiture of a loan, payment will be made at par and the accrued interest payable as of the date of acquisition.

SEC. 335.16. EXECUTION OF REQUEST FOR PAYMENT.—The owner in whose name the note is inscribed must appear before one of the officers authorized by the Secretary of the Treasury to witness and certify requests for payment, establish his identity, and in the presence of such officer sign and complete the request for payment appearing on the back of the note. After the request for payment has been executed, the witnessing officer should execute the certificate provided for his use.

SEC. 335.17. OFFICERS AUTHORIZED TO CERTIFY REQUESTS FOR PAYMENT.—All officers authorized to certify requests for payment of United States Savings Bonds, as set forth in Treasury Department Circular No. 530, Seventh Revision, as amended, are hereby authorized to certify requests for cash redemption of Treasury savings notes issued under this circular. Such officers include, among others, United States postmasters, certain other post office officials, officers of all banks

and trust companies incorporated in the United States or its Territories, including officers at branches thereof, and commissioned and warrant officers of the Armed Forces of the United States.

SEC. 335.18. PRESENTATION AND SURRENDER.—Notes bearing properly executed requests for payment must be presented and surrendered to any Federal Reserve bank or branch or to the Treasurer of the United States, Washington 25, D. C., at the expense and risk of the owner. For the owner's protection, notes should be forwarded by registered mail, if not presented in person.

SEC. 335.19. PARTIAL REDEMPTION.—Partial cash redemption of a note, corresponding to an authorized denomination, may be made in the same manner as full cash redemption, appropriate changes being made in the request for payment. In case of partial redemption of a note, the remainder will be reissued in the same name and with the same issue date as the note surrendered.

SEC. 335.20. PAYMENT.—Payment of any note, either at maturity or on redemption before maturity, will be made by any Federal Reserve bank or branch or the Treasurer of the United States, following clearance with the agency of issue, which will be obtained by the agency to which the note is surrendered. Payment will be made by check drawn to the order of the owner, and mailed to the address given in his request for payment, or by credit in any account maintained by a banking institution with the Federal Reserve bank of its district.

SUBPART F: PAYMENT OR REISSUE TO OTHER THAN INSCRIBED OWNER

SEC. 335.21. PRESENTATION AND SURRENDER.—A note may be paid or reissued in accordance with any of the provisions of this subpart only upon the presentation and surrender of the note at the risk and expense of the owner to the issuing agency, accompanied by an appropriate request for the particular transaction.

SEC. 335.22. AUTHORIZED TRANSFERS.—(*a*) *Between husband and wife.*—A note inscribed in the name of a married man may be reissued in the name of his wife, and a note inscribed in the name of a married woman may be reissued in the name of her husband.

(*b*) *Between affiliated corporations.*—A note inscribed in the name of a parent corporation, which is hereby defined as a corporation owning more than 50 percent of the stock, with voting power, of another corporation, may be reissued in the name of a subsidiary, and a note registered in the name of a subsidiary may be reissued in the name of the parent corporation.

SEC. 335.23. AUTHORIZED PLEDGE.—A note may be pledged as collateral for a loan from a banking institution, and if title thereto is acquired by the institution because of default in the payment of the loan, the notes will be redeemed at par and accrued interest to the interest accrual date next preceding the date of such acquisition, unless acquired on an interest accrual date, in which case redemption will be made at par and accrued interest to that date. Proof of the date of acquisition must be furnished, and payment must be requested by the pledgee under a power of attorney given by the pledgor in whose name the note is inscribed. The note will not be transferred to the pledgee.

SEC. 335.24. PAYMENT TO REPRESENTATIVES OF DECEASED OR INCOMPETENT OWNERS AND PAYMENT OR REISSUE TO HEIRS OR LEGATEES OF DECEASED OWNERS.—In case of the death or disability of an in-

dividual owner, if the notes are not to be presented in payment of taxes, payment will be made to the duly constituted representative of his estate, or they may be paid or reissued to one or more of his heirs or legatees upon satisfactory proof of their right; but no reissue will be made in the names of two or more persons jointly or as coowners.

SEC. 335.25. PAYMENT OR REISSUE TO SUCCESSORS OF CORPORATIONS, UNINCORPORATED ASSOCIATIONS OR PARTNERSHIPS.—If a corporation or unincorporated body in whose name notes are inscribed is dissolved, consolidated, merged or otherwise changes its organization, the notes may be paid to, or reissued in the name of, those persons or organizations lawfully entitled to the assets of such corporation or body by reason of such change in organization.

SEC. 335.26. PAYMENT TO REPRESENTATIVES OF BANKRUPT OR INSOLVENT OWNERS.—If an owner of notes is declared bankrupt or insolvent, payment, but not reissue, will be made to the duly qualified trustee, receiver or similar representative if the notes are submitted with satisfactory proof of his appointment and qualification.

SEC. 335.27. PAYMENT AS A RESULT OF JUDICIAL PROCEEDINGS.—Payment, but not reissue, will be made as a result of judicial proceedings in a court of competent jurisdiction, if the notes are submitted with proper proof of such proceedings and their finality.

SEC. 335.28. INSTRUCTIONS AND INFORMATION.—Before executing the request for payment or submitting the notes under the provisions of this subpart, instructions should be obtained from a Federal Reserve bank or branch or from the Treasury Department, Division of Loans and Currency, Washington 25, D. C.

SUBPART G: GENERAL PROVISIONS

SEC. 335.29. REGULATIONS.—Except as provided in this circular, the notes issued hereunder will be subject to the general regulations of the Treasury Department, now or hereafter prescribed, governing bonds and notes of the United States; the regulations currently in force are contained in Department Circular No. 300, as amended.

SEC. 335.30. LOSS, THEFT, OR DESTRUCTION.—In case of the loss, theft, or destruction of a savings note immediate notice (which should include a full description of the note) should be given the agency which issued the note and instructions should be requested as to the procedure necessary to secure a duplicate.

SEC. 335.31. FISCAL AGENTS.—Federal Reserve banks and their branches, as fiscal agents of the United States, are authorized to perform such services or acts as may be appropriate and necessary under the provisions of this circular and under any instructions given by the Secretary of the Treasury, and they may issue interim receipts pending delivery of the definitive notes.

SEC. 335.32. AMENDMENTS.—The Secretary of the Treasury may at any time or from time to time supplement or amend the terms of this circular, or of any amendments or supplements thereto, and may at any time or from time to time prescribe amendatory rules and regulations governing the offering of the notes, information as to which will promptly be furnished to the Federal Reserve banks.

G. M. HUMPHREY,
Secretary of the Treasury.

T. D. 6027

TITLE 26—INTERNAL REVENUE.—CHAPTER I, SUBCHAPTER E, PART 471.—ACCEPTANCE OF TREASURY OBLIGATIONS IN PAYMENT OF TAXES

Treasury Decision 4703 [C. B. XV-2, 288 (1936)] amended

TREASURY DEPARTMENT,
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington 25, D. C.

To Officers and Employees of the Internal Revenue Service and Others Concerned:

In order to provide for the acceptance before maturity of Treasury certificates of indebtedness or Treasury notes in payment of income and profits taxes, and to provide for the acceptance of Treasury certificates of indebtedness, Treasury notes, or Treasury bills in payment of such taxes before maturity at other than maturity value, article 1 of Treasury Decision 4703 [C. B. XV-2, 288 (1936)], approved November 3, 1936, as made applicable by Treasury Decision 4885 [C. B. 1939-1 (Part 1), 396], approved February 11, 1939 (26 CFR, Cum. Supp., p. 4876), codified in 26 CFR, part 3 (1938 ed.), as section 3.56-5, and amended by Treasury Decision 5934 [C. B. 1952-2, 217], approved September 25, 1952 (17 F. R. 8680), (*a*) is inserted in title 26, part 471, Code of Federal Regulations, as section 471.3 thereof, the title of which part is amended to read as shown above, and (*b*) as so inserted is amended to read as follows:

SEC. 471.3. TREASURY CERTIFICATES OF INDEBTEDNESS, TREASURY NOTES, AND TREASURY BILLS IN PAYMENT OF INCOME AND PROFITS TAXES.—(a) Treasury certificates of indebtedness, Treasury notes, or Treasury bills of any series (not including interim receipts issued by Federal Reserve banks in lieu of definitive certificates, notes, or bills) may be tendered at or before maturity in payment of income or profits taxes payable under the provisions of the Internal Revenue Code, due on the date on which the certificates, notes, or bills mature or a specified prior date, but only if such certificates, notes, or bills, according to the express terms of their issue, are made acceptable in payment of such income or profits taxes. If the taxes for which the certificates, notes, or bills are tendered in payment become due on the same date as that on which such certificates, notes, or bills mature, they will be accepted at par plus accrued interest, if any, payable with the principal (not represented by coupons attached) in payment of such taxes. If the taxes for which the certificates, notes, or bills are tendered in payment become due on a date prior to that on which the certificates, notes, or bills mature, they will be accepted at the value specified in the terms under which such certificates, notes, or bills were issued. All interest coupons attached to Treasury certificates of indebtedness or Treasury notes shall be detached by the taxpayer before such certificates or notes are tendered in payment of taxes.

(b) Receipts given by a collector, director, or district director of internal revenue for Treasury certificates of indebtedness, Treasury notes, or Treasury bills received in payment of income or profits taxes as provided in this section shall contain an adequate description of such certificates, notes, or bills, and a statement of the value, including accrued interest, if any, payable with the principal (not represented by coupons attached), at which accepted, and shall show that the certificates, notes, or bills are tendered by the taxpayer and received by the collector, director, or district director, subject to no condition, qualification, or reservation whatsoever, in payment of an amount of taxes no greater than such value. Any certificate, note, or bill offered in payment of income or profits taxes under the provisions of the Internal Revenue Code subject to any condition, qualification, or reservation, or for any greater amount than the value at which acceptable in payment of taxes, as specified in the terms under which such certificate, note, or bill was issued, shall not be deemed to be duly tendered and shall be returned to the taxpayer.

(c) For the purpose of saving taxpayers the expense of transmitting such Treasury certificates of indebtedness, Treasury notes, or Treasury bills to the office of the collector, director, or district director of internal revenue in whose district the taxes are payable, taxpayers desiring to pay income or profits taxes with such certificates, notes, or bills acceptable in payment of taxes may deposit such certificates, notes, or bills with a Federal Reserve bank or branch, subject to the condition that the Federal Reserve bank or branch shall issue a receipt in the name of the collector, director, or district director of internal revenue, describing the certificates, notes, or bills by par or dollar face amount and stating on the face of the receipt that the certificates, notes, or bills represented thereby are held by the bank or branch for redemption at the value specified in the terms under which the certificates, notes, or bills were issued, and application of the proceeds in payment of income or profits taxes due on a specified date by the taxpayer named therein.

Because this Treasury Decision extends to taxpayers the privilege of applying specified Treasury certificates of indebtedness or Treasury notes in payment of income or profits taxes due prior to the maturity date of such certificates or notes and enlarges the privilege of applying specified Treasury bills in payment of such taxes, it is hereby found that it is unnecessary to issue this Treasury Decision with notice and public procedure thereon under section 4(a) of the Administrative Procedure Act, approved June 11, 1946, or subject to the effective date limitation of section 4(c) of said act.

This Treasury Decision shall be effective upon its filing for publication in the Federal Register.

(This Treasury Decision is issued under the authority contained in secs. 3657 and 3791 of the Internal Revenue Code (53 Stat. 447, 467; 26 U. S. C. 3657, 3791).)

JUSTIN F. WINKLE,
Acting Commissioner of Internal Revenue.

Approved July 6, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

(Filed with the Division of the Federal Register July 8, 1953, 8:57 a. m.)

SECTION 3672.—VALIDITY AGAINST MORTGAGEES, PLEDGEES, PURCHASERS, AND JUDGMENT CREDITORS

Rev. Rul. 225

INTERNAL REVENUE CODE

In the State of New York a judgment creditor acquires a lien against the personal property of a judgment debtor as of the time of the delivery of a writ of execution to the proper officer. Consequently, under section 3672 of the Internal Revenue Code a notice of Federal tax lien filed subsequent to the delivery of the writ of execution is invalid as against the judgment creditor with respect to personal property levied upon and sold under the execution, even though the sale was made after the filing of such notice.

Advice is requested regarding the priority of a Federal tax lien on personal property as against a judgment creditor.

In the instant case a creditor of the taxpayer obtained a judgment on February 4, 1953, and on February 6, 1953, delivered a writ of execution to the Marshal of the city of New York. On February 9, 1953, a notice of tax lien was filed by the collector of internal revenue

and on February 14, 1953, the Marshal levied upon and subsequently sold certain personal property of the taxpayer. The above-stated facts disclose that the notice of the Federal tax lien was filed after the issuance of the writ of execution by the judgment creditor but before the levy was actually made on the execution.

Since the lien for Federal taxes is statutory in origin, its existence and validity must necessarily depend upon the provisions of the Internal Revenue Code. Section 3670 of the Code provides that if a person liable to pay any tax neglects or refuses to pay such tax after demand, the amount of tax constitutes a lien in favor of the United States on all the personal and real property of the tax delinquent. Under section 3671 of the Code the lien arises at the time the assessment list is received by the local collector (now the district director) and continues until the liability for the tax either is satisfied or becomes unenforceable because of lapse of time.

However, a certain qualification is contained in section 3672 of the Internal Revenue Code which provides in part as follows:

(a) INVALIDITY OF LIEN WITHOUT NOTICE.—Such lien shall not be valid as against any mortgagee, pledgee, purchaser, or judgment creditor until notice thereof has been filed by the collector—

To be entitled to the protection afforded by this section, the one who claims rights prior to those of the United States must fall within one of the enumerated classes, i. e., he must be a mortgagee, pledgee, purchaser, or judgment creditor. *Alexander MacKenzie* v. *United States*, 109 Fed. (2d) 540. Applicable State law will determine his status. *United States* v. *Record Publishing Company et al.*, 60 Fed. Supp. 194.

A "judgment creditor" within the contemplation of section 3672(a) of the Code is a creditor who has obtained not only a judgment against his debtor but also (under applicable State law) a lien against the judgment debtor's property prior to the filing of notice of the Federal lien. See *Edward Miller* v. *Bank of America, N. T. & S. A., et al.*, 166 Fed. (2d) 415.

Section 679 of the Civil Practice Act of the State of New York provides:

PERSONAL PROPERTY BOUND BY EXECUTION.—The goods and chattels of a judgment debtor, not exempt, by express provision of law, from levy and sale by virtue of an execution, and his other personal property which is expressly declared by law to be subject to levy by virtue of an execution, are bound by the execution, when situated within the jurisdiction of the officer to whom an execution against property is delivered, from the time of the delivery thereof to the proper officer to be executed, but not before.

New York cases which interpret section 679 hold that delivery of execution under the conditions prescribed creates a statutory lien in favor of the judgment creditor. See *In re New Lots Sash and Door Corporation*, 3 Fed. Supp. 570; *Rosevele Frocks, Inc.* v. *Sommers et al.*, 78 N. Y. Supp. (2d) 41; *In re Vanity Fair Shoe Corporation*, 84 Fed. Supp. 533; *Heights Promenade, Inc.*, v. *Volper*, 101 N. Y. Supp. (2d) 65.

Sections 680 and 683, respectively, of the Civil Practice Act, *supra*, provide as follows:

ORDER OF PREFERENCE AMONG EXECUTIONS.—Where two or more executions against property are issued out of the same or different courts against the same judgment debtor, the one first delivered to an officer to be executed has preference, notwithstanding that a levy is first made by virtue of an execution sub-

sequently delivered; but if a levy upon and sale of personal property has been made by virtue of the junior execution, before an actual levy by virtue of the senior execution, the same property shall not be levied upon or sold by virtue of the latter.

* * * * * * *

TITLE OF BONA FIDE PURCHASERS BEFORE LEVY.—The title to personal property, acquired before the actual levy of an execution, by a purchaser in good faith, and without notice that the execution has been issued, is not affected by an execution delivered, before the purchase was made, to an officer to be executed.

Accordingly, it is held that in the State of New York a judgment creditor acquires a lien against the personal property of a judgment debtor as of the time of the delivery of a writ of execution to the proper officer. Consequently, under section 3672 of the Internal Revenue Code a notice of Federal tax lien filed subsequent to the delivery of the writ of execution is invalid as against the judgment creditor with respect to personal property levied upon and sold under the execution, even though the sale was made after the filing of such notice.

SECTION 3761.—COMPROMISES

Rev. Rul. 251

INTERNAL REVENUE CODE

Transfer of functions pertaining to offers in compromise to Audit Division.

1. All functions relating to offers in compromise presently vested in the Appellate Division of the National Office are transferred to the Audit Division of the National Office, a branch of which is to be known as the Compromise Branch, Audit Division.

2. All correspondence addressed to the National Office, relating to offers in compromise, except communications pertaining to those cases under the jurisdiction of the Chief Counsel and the Alcohol and Tobacco Tax Division, should be addressed to the Audit Division for the attention of O:A:C. Also, where the symbols O:A appear in Rev. Rul. 117, C. B. 1953-1, 498, and the exhibits attached thereto, there should be substituted the symbols O:A:C.

Rev. Rul. 252

INTERNAL REVENUE CODE

Certain accepted offers in compromise may be inspected in the district directors' offices.

1. The authority to permit public inspection of certain accepted offers in compromise, pursuant to the provisions and authority of Executive Order No. 10386 and Treasury Decision 5927, both dated August 20, 1952, C. B. 1952-2. 298 and 299, and IR-Mim. 26 dated August 27, 1952, C. B. 1952-2, 299, has been delegated to the district directors of internal revenue. Public inspection of accepted offers in compromise coming within the scope of this ruling will no longer be authorized in the National Office.

2. District directors will permit public inspection in the manner indicated below in income, excess-profits, declared value excess-profits,

capital stock, estate and gift tax cases involving offers in compromise which are accepted by the district director pursuant to the provisions of Rev. Rul. 117, C. B. 1953-1, 498.

3. The public inspection in the district director's office of accepted offers shall conform to the provisions of Executive Order 10386, Treasury Decision 5927, and paragraphs 1 and 2 of IR-Mim. 26, *supra*. The inspection may be accomplished by making available for public inspection in the district director's office, or in an office designated by him, a copy of the abstract and statement in each compromise case coming within the scope of paragraph 2 above. Offers will be considered "accepted" as of the date of the letter notifying the proponent of the acceptance.

4. IR-Mim. 26, *supra*, and Rev. Rul. 117, *supra*, and all other instructions which are inconsistent with the provisions of this ruling, are hereby modified or superseded accordingly.

SECTION 3772.—SUITS FOR REFUND

Rev. Rul. 139

INTERNAL REVENUE CODE

A director of internal revenue appointed to succeed a collector of internal revenue pursuant to Reorganization Plan No. 1 of 1952, C. B. 1952-1, 227, which plan placed directors in positions comparable to those previously occupied by collectors, cannot be substituted as a party defendant in a suit brought against a collector for recovery of taxes alleged to have been erroneously assessed or collected. (See *Julius I. Smietanka* v. *Indiana Steel Co.*, 257 U. S. 1, Ct. D. 17, C. B. 5, 251.)

SECTION 3792.—EXPENSES OF DETECTION AND PUNISHMENT OF FRAUDS

Rev. Rul. 140*

INTERNAL REVENUE CODE

New Form 211 prescribed for use by informants in applying for reward under section 3792 of the Internal Revenue Code.

1. Attention is invited to the existence of a new Form 211, Public Voucher for Reward for Original Information, approved March 10, 1952, for use by informants in applying for reward. The use of Form 211 applies to original information furnished to internal revenue officers leading to detection of violation of the internal revenue laws and to the recovery of internal revenue taxes, penalties, fines, and forfeitures. This form, which is designed for direct scheduling by the Budget and Finance Division of the Bureau in Washington to the Chief Disbursing Officer for payment, supersedes the old Form 211 which had been designed for submission to the Claims Division of the General Accounting Office for settlement prior to payment.

*Originally issued as IR Circular No. 127, dated April 7, 1953.

2. The new Form 211 should not be confused with Forms 164 and 164–A which are designed for use in contracting with informers, the first for temporary employment on a per diem basis, and the second for the purchase of information and payment of a lump sum therefor, both types of contracts concerning violations of the internal revenue liquor laws.

3. Any correspondence regarding the provisions of this Revenue Ruling should refer to its number and to the symbols C : A : BF.

PART III.—MISCELLANEOUS

H. R. 5898. PUBLIC LAW 125, EIGHTY-THIRD CONGRESS
[CHAPTER 202, FIRST SESSION]

An Act To extend until December 31, 1953, the period with respect to which the excess-profits tax shall be effective.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That sections 430(a), 430(c), and 432(b) of the Internal Revenue Code are amended, effective with respect to taxable years ending after June 30, 1953, by striking "June 30, 1953," and "July 1, 1953," wherever such dates appear, and inserting in lieu thereof "December 31, 1953," and "January 1, 1954," respectively.

Approved July 16, 1953.

H. R. 5805. PUBLIC LAW 178, EIGHTY-THIRD CONGRESS
[CHAPTER 304, FIRST SESSION]

An Act Making appropriations for the legislative branch and the judiciary branch for the fiscal year ending June 30, 1954, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the following sums are appropriated, out of any money in the Treasury not otherwise appropriated, for the legislative branch and the judiciary branch for the fiscal year ending June 30, 1954, namely:

* * * * * * *

HOUSE OF REPRESENTATIVES

SALARIES, MILEAGE, AND EXPENSES OF MEMBERS

For compensation of Members of the House of Representatives, Delegates from Territories, and the Resident Commissioner from Puerto Rico, $5,492,500.

For mileage and expense allowance of Members of the House of Representatives, Delegates from Territories, and the Resident Commissioner from Puerto Rico, as authorized by law, $1,273,500. The proviso under this head in Public Law 471, Eighty-second Congress, is amended to read as follows: "*Provided*, That in the case of taxable years beginning after December 31, 1953, the place of residence of a Member of Congress (including any Delegate and Resident Commissioner) within the State, Congressional District, Territory, or possession which he represents in Congress shall be considered his home for the purposes of section 23(a)(1)(A) of the Internal Revenue Code, but amounts expended by such Member within each taxable year for living expenses shall not be deductible for income tax purposes in excess of $3,000."

* * * * * * *

SEC. 302. This Act may be cited as the "Legislative-Judiciary Appropriation Act, 1954".

Approved August 1, 1953.

H. R. 5303. PUBLIC LAW 196, EIGHTY-THIRD CONGRESS
[CHAPTER 329, FIRST SESSION]

An Act To amend sections 1606 and 1607 of the Internal Revenue Code in order to permit unemployment insurance coverage under State unemployment compensation laws for seamen employed on certain vessels operated by the United States.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 1606 of the Internal Revenue Code is hereby amended by adding at the end thereof the following new subsections:

(g) The permission granted by subsection (f) of this section shall apply in the same manner and under the same conditions (including the obligation to comply with all requirements of State unemployment compensation laws) to general agents of the Secretary of Commerce with respect to service performed on or after July 1, 1953, by officers and members of the crew on or in connection with American vessels (1) owned by or bareboat chartered to the United States, and (2) whose business is conducted by such general agents. As to any such vessel, the State permitted to require contributions on account of such service shall be the State to which the general agent would make contributions if the vessel were operated for his own account. Such general agents are designated, for this purpose, instrumentalities of the United States not wholly owned by it and shall not be exempt from the tax imposed by section 1600. The permission granted by this subsection is subject to the same conditions and limitations as are imposed in subsection (f) of this section, except that clause (2) of the second sentence of subsection (b) of this section shall apply.

(h) Any State may, as to service performed on or after July 1, 1953, and on account of which contributions are made pursuant to subsection (g) of this section, (1) require contributions from persons performing such service under its unemployment compensation law or temporary disability insurance law administered in connection therewith, and (2) require general agents of the Secretary of Commerce to make contributions under such temporary disability insurance law and to make such deductions from wages or remuneration as are required by such unemployment compensation or temporary disability insurance law.

(i) Each general agent of the Secretary of Commerce making contributions pursuant to subsection (g) or (h) of this section shall, for the purposes of such subsections, be considered a legal entity in his capacity as an instrumentality of the United States, separate and distinct from his identity as a person employing individuals on his own account.

SEC. 2. Section 1607 of the Internal Revenue Code is hereby amended by adding at the end thereof the following new subsection:

(o) Notwithstanding the provisions of subsection (c)(6) of this section, service performed on or after July 1, 1953, by officers and members of the crew of a vessel which would otherwise be included as employment under subsection (c) of this section shall not be excluded by reason of the fact that it is performed on or in connection with an American vessel (1) owned by or bareboat chartered to the United States and (2) whose business is conducted by a general agent of the Secretary of Commerce. For the purposes of this subchapter, each such general agent shall be considered a legal entity in his capacity as such general agent, separate and distinct from his identity as a person employing individuals on his own account, and the officers and members of the crew of such an American vessel whose business is conducted by a general agent of the Secretary of Commerce shall be deemed to be performing services for such general agent rather than the United States. Each such general agent who in his capacity as such is an employer within the meaning of subsection (a) of this section shall be subject to all the requirements imposed upon an employer under this subchapter with respect to service which constitutes employment by reason of this subsection.

SEC. 3. Nothing in the amendments made by this act shall be construed as constituting officers and members of the crew of American

vessels (1) owned by or bareboat chartered to the United States and (2) whose business is conducted by general agents of the Secretary of Commerce employees of such general agents except for the purposes of State unemployment compensation and temporary disability insurance laws and the Federal Unemployment Tax Act.

SEC. 4. This act shall take effect as of July 1, 1953.

Approved August 5, 1953.

H. R. 5134. PUBLIC LAW 212, EIGHTY-THIRD CONGRESS
[CHAPTER 345, FIRST SESSION]

An Act To provide for the jurisdiction of the United States over the submerged lands of the outer Continental Shelf, and to authorize the Secretary of the Interior to lease such lands for certain purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Outer Continental Shelf Lands Act".

* * * * * * *

SEC. 4. LAWS APPLICABLE TO OUTER CONTINENTAL SHELF.—(a) (1) The Constitution and laws and civil and political jurisdiction of the United States are hereby extended to the subsoil and seabed of the outer Continental Shelf and to all artificial islands and fixed structures which may be erected thereon for the purpose of exploring for, developing, removing, and transporting resources therefrom, to the same extent as if the outer Continental shelf were an area of exclusive Federal jurisdiction located within a State: *Provided, however*, That mineral leases on the outer Continental Shelf shall be maintained or issued only under the provisions of this Act.

* * * * * * *

Approved August 7, 1953.

H. R. 4152. PUBLIC LAW 213, EIGHTY-THIRD CONGRESS
[CHAPTER 346, FIRST SESSION]

An Act To extend the time for exemption from income taxes for certain members of the Armed Forces, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 22(b)(13) of the Internal Revenue Code (relating to exclusion from gross income of compensation of certain members of the Armed Forces) is hereby amended by striking out "January 1, 1954" wherever it appears therein and inserting in lieu thereof "January 1, 1955".

SEC. 2. Section 1621(a)(1) of the Internal Revenue Code (relating to definition of the term "wages") is hereby amended by striking out "January 1, 1954" and inserting in lieu thereof "January 1, 1955".

SEC. 3. (a) That the third sentence of section 25(b)(3) of the Internal Revenue Code, relating to the definition of dependent, is amended to read as follows: "For the purposes of determining whether any of the foregoing relationships exist (1) a legally adopted child of a person or (2) a child for which petition for adoption was filed by a

person in the appropriate court and denied because of mental incapacity of surviving natural parent to agree to such adoption, shall be considered a child of such person by blood."

(b) The provisions of subsection (a) shall be applicable to taxable years beginning after December 31, 1945.

Approved August 7, 1953.

H. R. 5256. PUBLIC LAW 219, EIGHTY-THIRD CONGRESS
[CHAPTER 352, FIRST SESSION]

AN ACT To amend the Internal Revenue Code with respect to the retirement of judges of The Tax Court of the United States.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That part I of subchapter A of chapter 5 of the Internal Revenue Code (relating to organization and jurisdiction of The Tax Court of the United States) is hereby amended by inserting after section 1105 the following new section:

SEC. 1106. RETIREMENT.

(a) DEFINITIONS.—For the purposes of this section—

(1) The term "Tax Court" means The Tax Court of the United States.

(2) The term "Civil Service Commission" means the United States Civil Service Commission.

(3) The term "judge" means the chief judge or a judge of The Tax Court; but such term does not include any individual performing judicial duties pursuant to subsection (c).

(4) The term "Civil Service Retirement Act" means the Civil Service Retirement Act of May 29, 1930, as amended.

(5) In any determination of length of service as judge there shall be included all periods (whether or not consecutive) during which an individual served as judge or as a member of the Board.

(b) RETIREMENT.—

(1) Any judge who has served as judge for eighteen years or more may retire at any time.

(2) Any judge who has served as judge for ten years or more and has attained the age of seventy shall retire not later than the close of the third month beginning after whichever of the following months is the latest:

(A) The month in which he attained age seventy;

(B) The month in which he completed ten years of service as judge; or

(C) The month in which this section is enacted.

Section 2(a) of the Civil Service Retirement Act (relating to automatic separation from the service) shall not apply in respect to judges.

(c) RECALLING OF RETIRED JUDGES.—Any individual who is receiving retired pay under subsection (d) may be called upon by the chief judge of The Tax Court to perform such judicial duties with The Tax Court as may be requested of him for any period or periods specified by the chief judge; except that in the case of any such individual—

(1) the aggregate of such periods in any one calendar year shall not (without his consent) exceed ninety calendar days; and

(2) he shall be relieved of performing such duties during any period in which illness or disability precludes the performance of such duties.

Any act, or failure to act, by an individual performing judicial duties pursuant to this subsection shall have the same force and effect as if it were the act (or failure to act) of a judge of The Tax Court; but any such individual shall not be counted as a judge of The Tax Court for the purposes of section 1102(a). Any individual who is performing judicial duties pursuant to this subsection shall be paid the same allowances for travel and other expenses as a judge.

(d) RETIRED PAY.—Any individual who after the date of the enactment of this section—

(1) ceases to be a judge by reason of paragraph (2) of subsection (b), or ceases to be a judge after having served as judge for eighteen years or more; and

(2) elects under subsection (e) to receive retired pay under this subsection,

shall receive retired pay at a rate which bears the same ratio to the rate of the salary payable to him as judge at the time he ceases to be a judge as the number of years he has served as judge bears to twenty-four; except that the rate of such retired pay shall be not less than one-half of the rate of such salary and not more than the rate of such salary. Such retired pay shall begin to accrue on the day following the day on which his salary as judge ceases to accrue, and shall continue to accrue during the remainder of his life. Retired pay under this subsection shall be paid in the same manner as the salary of a judge. In computing the rate of the retired pay under this subsection for any individual who is entitled thereto, that portion of the aggregate number of years he has served as a judge which is a fractional part of one year shall be eliminated if it is less than six months, or shall be counted as a full year if it is six months or more.

(e) ELECTION TO RECEIVE RETIRED PAY.—Any judge may elect to receive retired pay under subsection (d). Such an election—

(1) may be made only while an individual is a judge (except that in the case of an individual who fails to be reappointed as judge at the expiration of a term of office, it may be made at any time before the day after the day on which his successor takes office);

(2) once made, shall be irrevocable;

(3) in the case of any judge other than the chief judge, shall be made by filing notice thereof in writing with the chief judge; and

(4) in the case of the chief judge, shall be made by filing notice thereof in writing with the Civil Service Commission.

The chief judge shall transmit to the Civil Service Commission a copy of each notice filed with him under this subsection.

(f) INDIVIDUALS RECEIVING RETIRED PAY TO BE AVAILABLE FOR RECALL.—Any individual who has elected to receive retired pay under subsection (d) who thereafter—

(1) accepts civil office or employment under the Government of the United States (other than the performance of judicial duties pursuant to subsection (c)); or

(2) performs (or supervises or directs the performance of) legal or accounting services in the field of Federal taxation or in the field of the renegotiation of Federal contracts for his client, his employer, or any of his employer's clients,

shall forfeit all rights to retired pay under subsection (d) for all periods beginning on or after the first day on which he accepts such office or employment or engages in any activity described in paragraph (2). Any individual who has elected to receive retired pay under subsection (d) who thereafter during any calendar year fails to perform judicial duties required of him by subsection (c) shall forfeit all rights to retired pay under subsection (d) for the one-year period which begins on the first day on which he so fails to perform such duties.

(g) COORDINATION WITH CIVIL SERVICE RETIREMENT.—

(1) GENERAL RULE.—Except as otherwise provided in this subsection, the provisions of the Civil Service Retirement Act (including the provisions relating to the deduction and withholding of amounts from basic pay, salary, and compensation) shall apply in respect of service as a judge (together with other service as an officer or employee to whom such Act applies) as if this section had not been enacted.

(2) EFFECT OF ELECTING RETIRED PAY.—In the case of any individual who has filed an election to receive retired pay under subsection (d) and who has not filed a waiver under paragraph (3) of this subsection—

(A) he shall not be entitled to any annuity under section 1, 2, 3A, 6, or 7 of the Civil Service Retirement Act for any period beginning on or after the day on which he files such election;

(B) no amount shall be returned to him under section 7(a) of such Act;

(C) subsections (b) and (c) of section 4 of such Act, and subsection (c) of section 12 of such Act, shall apply in respect of such individual as if he were retiring or had retired under section 1 of such Act on

the date on which his retired pay under subsection (d) of this section began to accrue; except that (i) the amount of any annuity payable to a survivor of such individual under subsection (b) or (c) of such section 4 or under subsection (c) of such section 12 shall be based on a life annuity for such individual computed as provided in subsection (a) of such section 4, and (ii) if such individual makes the election provided by subsection (b) or (c) of such section 4, his retired pay under subsection (d) of this section shall be reduced by the amount by which a life annuity computed as provided in subsection (a) of such section 4 would be reduced;

(D) in computing the "aggregate amount of the annuity paid" for purposes of section 12(g) of such Act, any retired pay which has accrued under subsection (d) of this section (including any such retired pay forfeited under subsection (f)) shall be included as if it were an annuity payable to him under such Act; and

(E) no deduction for the purposes of the civil-service retirement and disability fund shall be made from the retired pay payable to him under subsection (d) of this section, or from any other salary, pay, or compensation payable to him, for any period after the date on which such retired pay began to accrue.

(3) WAIVER OF CIVIL SERVICE BENEFITS.—

(A) Any individual who has elected to receive retired pay under subsection (d) of this section may (at any time thereafter during the period prescribed by subsection (e) (1)) waive all benefits under the Civil Service Retirement Act. Such a waiver (i) once made, shall be irrevocable, and (ii) shall be made in the same manner as is provided for an election by such individual under subsection (e). The chief judge shall transmit to the Civil Service Commission a copy of each notice of waiver filed with him under this paragraph.

(B) In the case of any individual who has made a waiver under this paragraph—

(i) no annuity shall be payable to any person under the Civil Service Retirement Act with respect to any service performed by such individual (whether performed before or after such waiver is filed and whether performed as judge or otherwise);

(ii) no deduction shall be made from any salary, pay, or compensation of such individual for the purposes of the civil-service retirement and disability fund for any period beginning after the day on which such waiver is filed;

(iii) except as provided in clause (iv), no refund shall be made under the Civil Service Retirement Act of any amount credited to the account of such individual or of any interest on any amount so credited;

(iv) additional sums voluntarily deposited by such individual under the second paragraph of section 10 of the Civil Service Retirement Act shall be promptly refunded, together with interest on such additional sums at 3 per centum per annum (compounded on December 31 of each year) to the day of such filing; and

(v) subsections (e) and (g) of section 12 of the Civil Service Retirement Act shall not apply.

(4) EMPLOYEES' COMPENSATION.—The fourth and sixth paragraphs of section 6 of the Civil Service Retirement Act shall apply in respect of retired pay accruing under subsection (d) of this section as if such retired pay were an annuity payable under such Act.

Approved August 7, 1953.

H. R. 5148. PUBLIC LAW 221, EIGHTY-THIRD CONGRESS
[CHAPTER 354, FIRST SESSION]

An Act To continue until the close of June 30, 1954, the suspension of duties and import taxes on metal scrap, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the first sen-

tence of section 2 of the Act of September 30, 1950 (Public Law 869, Eighty-first Congress) [C. B. 1950–2, 253], is hereby amended by striking out "June 30, 1953" and inserting in lieu thereof "June 30, 1954": *Provided*, That this Act shall not apply to lead scrap or zinc scrap (other than zinc scrap purchased under a written contract entered into before July 1, 1953).

SEC. 2. The amendments made by this Act shall not be construed to affect in any way the application of Public Law 38, Eighty-second Congress [C. B. 1951–1, 184], to copper scrap.

Approved August 7, 1953.

H. R. 5257. PUBLIC LAW 238, EIGHTY-THIRD CONGRESS
[CHAPTER 392, FIRST SESSION]

An Act To extend to the Trust Territory of the Pacific Islands certain provisions of the Internal Revenue Code relating to narcotics.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 2563 of the Internal Revenue Code (relating to Territorial extent of law) is amended by inserting "the Territory of the Pacific Islands," immediately after "the insular possessions of the United States,".

SEC. 2. (a) The heading of section 2564 of the Internal Revenue Code is amended to read as follows:

SEC. 2564. ADMINISTRATION IN PUERTO RICO, THE TRUST TERRITORY OF THE PACIFIC ISLANDS, THE CANAL ZONE, AND THE VIRGIN ISLANDS.

(b) Section 2564(a) of the Internal Revenue Code is amended to read as follows:

(a) PUERTO RICO AND THE TRUST TERRITORY OF THE PACIFIC ISLANDS.—In Puerto Rico and the Trust Territory of the Pacific Islands, the administration of this subchapter and part V of subchapter A of chapter 27, the collection of the special tax imposed by section 3220 of chapter 27, and the issuance of the order forms specified in section 2554 shall be performed by the appropriate internal revenue officers of those governments, and all revenues collected thereunder in Puerto Rico and the Trust Territory of the Pacific Islands shall accrue intact to the general governments thereof, respectively. The highest court of original jurisdiction of the Trust Territory of the Pacific Islands shall possess and exercise jurisdiction in all cases arising in such Territory under this subchapter and part V of subchapter A of chapter 27.

SEC. 3. Section 2554(h)(1) of the Internal Revenue Code is amended by striking out "PHILIPPINE ISLANDS" and "Philippine Islands" and inserting in lieu thereof, respectively, "TRUST TERRITORY OF THE PACIFIC ISLANDS" and "Trust Territory of the Pacific Islands".

SEC. 4. Section 2565 of the Internal Revenue Code is amended by adding at the end thereof the following:

TERRITORY.—
Subsection (g).

SEC. 5. Section 3228 of the Internal Revenue Code (relating to definitions) is amended by adding at the end thereof the following new subsection:

(g) TERRITORY.—As used in this part and subchapter A of chapter 23, (1) the word "Territory" shall include the Trust Territory of the Pacific Islands, and (2) the word "Territorial" shall reflect such inclusion.

SEC. 6. The amendments made by this Act shall take effect on the first day of the third month which begins more than ten days after the date of enactment of this Act.

Approved August 8, 1953.

H. R. 5561. PUBLIC LAW 240, EIGHTY-THIRD CONGRESS
[CHAPTER 394, FIRST SESSION]

An Act To amend the Internal Revenue Code and the Narcotic Drugs Import and Export Act so as to provide that certain drugs which are or may be chemically synthesized shall be included within the classification of narcotic drugs.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

DEFINITION OF "NARCOTIC DRUGS"

SECTION 1. Section 3228 of the Internal Revenue Code is amended by adding at the end thereof the following new subsection:

(g) NARCOTIC DRUGS.—The words "narcotic drugs" as used in this part and subchapter A of chapter 23, shall mean any of the following, whether produced directly or indirectly by extraction from substances of vegetable origin, or independently by means of chemical synthesis, or by a combination of extraction and chemical synthesis:

(1) Opium, isonipecaine, coca leaves, and opiate;

(2) Any compound, manufacture, salt, derivative, or preparation of opium, isonipecaine, coca leaves, or opiate;

(3) Any substance (and any compound, manufacture, salt, derivative, or preparation thereof) which is chemically identical with any of the substances referred to in clauses (1) and (2).

TECHNICAL AMENDMENTS

SEC. 2. Section 2550(a) of the Internal Revenue Code (relating to tax on opium and coca leaves) is amended by striking out "opium, isonipecaine, coca leaves, opiate, any compound, salt, derivative, or preparation thereof," and by inserting in lieu thereof "narcotic drugs".

SEC. 3. (a) Section 2558(b) of the Internal Revenue Code is amended (1) by striking out "opium, coca leaves, isonipecaine, opiates, and all salts, derivatives, and preparations of opium, coca leaves, isonipecaine, and opiates," and by inserting in lieu thereof "narcotic drugs", and (2) by striking out "None of the aforesaid drugs" and inserting in lieu thereof "No narcotic drugs".

(b) Sections 2564(b), 3220(g), and 3222(c)(1) of the Internal Revenue Code are each amended by striking out "opium or coca leaves, their sales, derivatives, or preparations" and by inserting in lieu thereof "narcotic drugs".

SEC. 4. Section 2565 of the Internal Revenue Code is amended by striking out all that follows "Subsection (d)." and by inserting in lieu thereof the following:

NARCOTIC DRUGS.—
Subsection (g).

SEC. 5. Section 3220 of the Internal Revenue Code (relating to tax on narcotics) is amended by striking out "opium, coca leaves, isonipe-

caine, or opiate, or any compound, manufacture, salt, derivative, or preparation thereof," and by inserting in lieu thereof "narcotic drugs".

SEC. 6. Subchapter A of chapter 23 of the Internal Revenue Code and part V of subchapter A of chapter 27 of the Internal Revenue Code are amended by striking out "the drugs mentioned in section 2550(a)", "any of the drugs mentioned in section 2550(a)", "any of the drugs mentioned in section 3220", "any of the aforesaid drugs", and "the aforesaid drugs", wherever those words appear, and by inserting in lieu thereof "narcotic drugs".

SEC. 7. Sections 3228(e) and 3228(f) of the Internal Revenue Code are each amended by striking out "and subchapter A of chapter 23".

SEC. 8. Paragraph (a) of the first section of the Narcotic Drugs Import and Export Act (21 U. S. C., sec. 171(a)) is amended to read as follows:

(a) The term "narcotic drug" shall have the meaning ascribed to the term "narcotic drugs" by section 3228(g) of the Internal Revenue Code; the term "isonipecaine" shall have the meaning ascribed to that term by section 3228(e) of such Code; and the term "opiate" shall have the meaning ascribed to that term by section 3228(f) of such Code.

Approved August 8, 1953.

H. R. 5877. PUBLIC LAW 243, EIGHTY-THIRD CONGRESS
[CHAPTER 397, FIRST SESSION]

An Act To amend certain administrative provisions of the Tariff Act of 1930 and related laws, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SHORT TITLE AND EFFECTIVE DATE

SECTION 1. This Act may be cited as the "Customs Simplification Act of 1953" and shall be effective, except as otherwise specially provided for, on and after the thirtieth day following the date of its enactment.

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FREE ENTRY PROVISIONS FOR TRAVELERS

SEC. 8. Paragraph 1798 of the Tariff Act of 1930, as amended (U. S. C., 1946 edition, title 19, sec. 1201, par. 1798), is further amended to read as follows:

"PAR. 1798. (a) Professional books, implements, instruments, and tools of trade, occupation, or employment, when imported by or for the account of any person arriving in the United States by whom or for whose account they were taken abroad.

"(b) In the case of any person arriving in the United States who is not a returning resident thereof—

"(1) wearing apparel, articles of personal adornment, toilet articles, and similar personal effects; all the foregoing, if actually owned by and in the possession of such person abroad at the time of or prior to his departure for the United States, and if appropriate for his own personal use and intended only for such use and not for any other person nor for sale;

"(2) automobiles, trailers, aircraft, motorcycles, bicycles, baby carriages, boats, horse-drawn conveyances, horses, and similar means of transportation, and the usual equipment accompanying the foregoing; any of the foregoing imported in connection with the arrival of such person and to be used in the United States only for the transportation of such person, his family and guests, and such incidental carriage of articles as may be appropriate to his personal use of the conveyance; and

"(3) not exceeding $200 in value of articles accompanying such a person who is in transit to a place outside United States customs territory and who will take the articles with him to such place.

"(c) In the case of any person arriving in the United States who is a returning resident thereof—

"(1) all personal and household effects taken abroad by him or for his account and brought back by him or for his account; and

"(2) articles (including not more than one wine gallon of alcoholic beverages and not more than one hundred cigars) acquired abroad as an incident of the journey from which he is returning, for his personal or household use, but not imported for the account of any other person nor intended for sale, if declared in accordance with regulations of the Secretary of the Treasury, up to but not exceeding in aggregate value—

"(A) $200, if such person arrives from a contiguous country which maintains a free zone or free port (see subparagraph (d)), or arrives from any other country after having remained beyond the territorial limits of the United States for a period of not less than forty-eight hours, and in either case has not claimed an exemption under this subdivision (A) within the thirty days immediately preceding his arrival; and

"(B) $300 in addition, if such person has remained beyond the territorial limits of the United States for a period of not less than twelve days and has not claimed an exemption under this subdivision (B) within the six months immediately preceding his arrival.

"(d) In the case of persons arriving from a contiguous country which maintains a free zone or free port, if the Secretary of the Treasury deems it necessary in the public interest and to facilitate enforcement of the requirement that the exemption shall apply only to articles acquired as an incident of the foreign journey, he shall prescribe by regulation or instruction, the application of which may be restricted to one or more ports of entry, that the exemption authorized by subdivision (2)(A) of subparagraph (c) shall be allowed only to residents who have remained beyond the territorial limits of the United States for not less than a specified period, not to exceed twenty-four hours, and after the expiration of ninety days after the date of such regulation or instruction allowance of the said exemption shall be subject to the limitations so prescribed.

"(e) Any article imported to replace a like article of comparable value previously exempted from duty under subdivision (c) of this paragraph shall be allowed free entry if the article previously exempted shall have been exported, under such supervision as the Secretary may prescribe, within sixty days after its importation because it was found by the importer to be unsatisfactory.

"(f) All articles exempted by this paragraph from the payment of duty shall be exempt also from the payment of any internal-revenue tax imposed upon or by reason of importation.

"(g) If any jewelry or similar articles of personal adornment having a value of $300 or more which have been exempted from duty under subdivision (1) of subparagraph (b) or any article which has been exempted from duty under subdivision (2)(B) of subparagraph (c) is sold within three years after the date of importation, or if any article which has been exempted from duty under subdivision (2) of subparagraph (b) is sold within one year after the date of importation, without prior payment to the United States of the duty which would have been payable at the time of entry if the article had been entered without the benefit of this paragraph, such article, or its value (to be recovered from the importer), shall be subject to forfeiture. A sale pursuant to a judicial order or in liquidation of the estate of a decedent shall not be subject to the provisions of this subparagraph.

"(h) The Secretary of the Treasury shall prescribe methods and regulations for carrying out the provisions of this paragraph. No exemption provided for in this paragraph shall be applied to any article which is not declared in accordance with such regulations."

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SUPPLIES AND EQUIPMENT FOR VESSELS AND AIRCRAFT

SEC. 11. (a) Subsections (a) and (b) of section 309 of the Tariff Act of 1930, as amended (U. S. C., 1946 edition, title 19, sec. 1309 (a) and (b)), relating to articles for certain vessels and aircraft, are further amended to read as follows:

"(a) EXEMPTION FROM DUTIES AND TAXES.—Articles of foreign or domestic origin may be withdrawn, under such regulations as the Secretary of the Treasury may prescribe, from any customs bonded warehouse, from continuous customs custody elsewhere than in a bonded warehouse, or from a foreign-trade zone free of duty and internal-revenue tax, or from any internal-revenue bonded warehouse, from any brewery, or from any winery premises or bonded premises for the storage of wine, free of internal-revenue tax—

"(1) for supplies (not including equipment) of (A) vessels or aircraft operated by the United States, (B) vessels of the United States employed in the fisheries or in the whaling business, or actually engaged in foreign trade or trade between the Atlantic and Pacific ports of the United States or between the United States and any of its possessions, or (C) aircraft registered in the United States and actually engaged in foreign trade or trade between the United States and any of its possessions; or

"(2) for supplies (including equipment) or repair of (A) vessels of war of any foreign nation, or (B) foreign vessels employed in the fisheries or in the whaling business, or actually engaged in foreign trade or trade between the United States and any of its possessions, where such trade by foreign vessels is permitted; or

"(3) for supplies (including equipment), ground equipment, maintenance, or repair of aircraft registered in any foreign country and actually engaged in foreign trade or trade between the United States and any of its possessions, where trade by foreign aircraft is permitted. With respect to articles for ground equipment, the exemption hereunder shall apply only to duties and to taxes imposed upon or by reason of importation.

"(b) DRAWBACK.—Articles withdrawn from bonded warehouses, bonded manufacturing warehouses, continuous customs custody elsewhere than in a bonded warehouse, or from a foreign-trade zone, and articles of domestic manufacture or production, laden as supplies upon any such vessel or aircraft of the United States or laden as supplies (including equipment) upon, or used in the maintenance or repair of, any such foreign vessel or aircraft, shall be considered to be exported within the meaning of the drawback provisions of this Act."

(b) Section 317 (b) of the Tariff Act of 1930, as amended (U. S. C., 1946 edition, title 19, sec. 1317(b)), is amended to read as follows:

"(b) The shipment or delivery of any merchandise for use as supplies (including equipment) upon, or in the maintenance or repair of any vessel or aircraft described in subdivision (2) or (3) of section 309 (a) of this Act, or for use as ground equipment for any such aircraft, shall be deemed an exportation within the meaning of the customs and internal-revenue laws applicable to the exportation of such merchandise without the payment of duty or internal-revenue tax. With respect to merchandise for use as ground equipment, such shipment or delivery shall not be deemed an exportation within the meaning of the internal-revenue laws relating to taxes other than those imposed upon or by reason of importation."

(c) Section 3115 of the Revised Statutes, as amended (U. S. C., 1946 edition, title 19, sec. 258), is further amended by—

(1) striking out the comma at the end of paragraph (2) and inserting in lieu thereof "; or" and inserting after paragraph (2) the following new paragraph:

"(3) That such equipments, or parts thereof, or materials, or labor, were used as dunnage for cargo, or for the packing or shoring thereof, or in the erection of temporary bulkheads or other similar devices for the control of bulk cargo, or in the preparation (without permanent repair or alternation) of tanks for the carriage of liquid cargo;"; and

(2) striking out "such equipments" the last place it appears in such section and inserting in lieu thereof "such equipments or parts thereof or materials".

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Approved August 8, 1953.

H. R. 6402. PUBLIC LAW 274, EIGHTY-THIRD CONGRESS
[CHAPTER 488, FIRST SESSION]

An Act To provide for abatement of jeopardy assessments when jeopardy does not exist.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That (a) section 273 of the Internal Revenue Code (relating to the abatement of jeopardy assessments of income taxes) is hereby amended by adding at the end thereof the following new subsection:

(a) ABATEMENT IF JEOPARDY DOES NOT EXIST.—The Secretary may abate the jeopardy assessment if he finds that jeopardy does not exist. Such abatement may not be made after a decision of The Tax Court of the United States in respect of the deficiency has been rendered or, if no petition is filed with The Tax Court of the United States, after the expiration of the period for filing such petition. The period of limitation on the making of assessments and the beginning of distraint or a proceeding in court for collection, in respect of any deficiency, shall be determined as if the jeopardy assessment so abated had not been made, except that the running of such period shall in any event be suspended for the period from the date of such jeopardy assessment until the expiration of the tenth day after the day on which such jeopardy assessment is abated.

(b) Sections 872 and 1013 (relating to the abatement of jeopardy assessments of estate and gift taxes, respectively) are hereby amended by adding at the end of each of such sections the following new subsection:

(j) ABATEMENT IF JEOPARDY DOES NOT EXIST.—The Secretary may abate the jeopardy assessment if he finds that jeopardy does not exist. Such abatement may not be made after a decision of The Tax Court of the United States in respect of the deficiency has been rendered, or, if no petition is filed with The Tax Court of the United States, after the expiration of the period for filing such petition. The period of limitation on the making of assessments and the beginning of distraint or a proceeding in court for collection, in respect of any deficiency, shall be determined as if the jeopardy assessment so abated had not been made, except that the running of such period shall in any event be suspended for the period from the date of such jeopardy assessment until the expiration of the tenth day after the day on which such jeopardy assessment is abated.

(c) The amendments made by this Act shall be applicable to jeopardy assessments made or in existence on the date of enactment of this Act or which are thereafter made.

Approved August 14, 1953.

H. R. 4980. PUBLIC LAW 283, EIGHTY-THIRD CONGRESS
[CHAPTER 508, FIRST SESSION]

An Act To amend section 3250(1)(5) of the Internal Revenue Code to provide that a person entitled to drawback with respect to certain nonbeverage products may elect to receive such drawbacks on a monthly instead of a quarterly basis.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the last two sentences of section 3250(1)(5) of the Internal Revenue Code are hereby amended to read as follows: "Such drawback shall be due and payable quarterly upon filing of a proper claim with the Secretary; except that, where any person entitled to such drawback shall elect in writing to file monthly claims therefor, such drawback shall be due and pay-

able monthly upon filing of a proper claim with the Secretary: *Provided, however*, That the Secretary may require persons electing to file monthly drawback claims to file with him a bond or other security in such amount and with such conditions as he shall by regulations prescribe. Any such election may be revoked upon filing of notice thereof with the Secretary. No claim under this subsection shall be allowed unless filed with the Secretary within the three months next succeeding the quarter in which the distilled spirits covered by the claim were used as provided in this subsection."

SEC. 2. The amendment made by the first section of this Act shall apply only with respect to claims for drawback with respect to distilled spirits which, on or after the first day of the first quarter after the quarter in which this Act is enacted, are used in the manufacture or production of nonbeverage products.

Approved August 15, 1953.

H. R. 6426. PUBLIC LAW 287, EIGHTY-THIRD CONGRESS
[CHAPTER 512, FIRST SESSION]

An Act To amend the Internal Revenue Code to extend the time during which certain provisions relating to income and estate taxes shall apply, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That (a) SHORT TITLE.—This Act, divided into titles and sections according to the following table of contents, may be cited as the "Technical Changes Act of 1953":

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TITLE I—EXTENSION PROVISIONS

Sec. 101. Election as to recognition of gain in certain corporate liquidations.
Sec. 102. Extension of time to make election in respect of excessive depreciation allowed for periods before 1952.
Sec. 103. Extension of time for making election with respect to war-loss recoveries.
Sec. 104. Extension of period of abatement of income taxes of members of Armed Forces upon death.
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Sec. 106. Extension of period for exemption from additional estate tax of members of Armed Forces upon death.

TITLE II—MISCELLANEOUS

Sec. 201. Venue of actions for violations of Act of October 19, 1949.
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Sec. 207. Exclusion of certain transfers taking effect at death.
Sec. 208. Failure to relinquish a power in certain disability cases.
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Sec. 210. Marital deduction in certain cases where decedent died before April 3, 1948.
Sec. 211. Mitigation of effect of statute of limitations.

(b) ACT AMENDATORY OF INTERNAL REVENUE CODE.—Except as otherwise expressly provided, wherever in this Act an amendment or

repeal is expressed in terms of an amendment to or repeal of a chapter, subchapter, title, supplement, section, subsection, subdivision, paragraph, subparagraph, or clause, the reference shall be considered to be made to a provision of the Internal Revenue Code.

(c) MEANING OF TERMS USED.—Except as otherwise expressly provided, terms used in this Act shall have the same meaning as when used in the Internal Revenue Code:

TITLE I—EXTENSION PROVISIONS

SEC. 101. ELECTION AS TO RECOGNITION OF GAIN IN CERTAIN CORPORATE LIQUIDATIONS.

(a) AMENDMENT OF SECTION 112(b)(7).—Section 112(b)(7) (relating to recognition of gain in certain corporate liquidations) is hereby amended by striking out "1951 or 1952" in subparagraph (A)(ii) and inserting in lieu thereof "1951, 1952, or 1953".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply with respect to taxable years ending after December 31, 1952.

SEC. 102. EXTENSION OF TIME TO MAKE ELECTION IN RESPECT OF EXCESSIVE DEPRECIATION ALLOWED FOR PERIODS BEFORE 1952.

(a) AMENDMENT OF SECTION 113(d).—So much of section 113(d) (relating to election in respect of depreciation, etc., allowed before 1952) as follows the first sentence thereof is hereby amended to read as follows: "Such an election shall be made in such manner as the Secretary may by regulations prescribe and shall be irrevocable when made, except that an election made on or before December 31, 1952, may be revoked at any time before January 1, 1955. A revocation of an election shall be made in such manner as the Secretary may by regulations prescribe, and no election may be made by any person after he has so revoked an election. The election shall apply in respect of all property held by the person making the election at any time on or before December 31, 1952, and in respect of all periods since February 28, 1913, and before January 1, 1952, during which such person held such property or for which adjustments must be made under subsection (b)(2). An election or a revocation of an election by a transferor, donor, or grantor made after the date of the transfer, gift, or grant of property shall not affect the basis of such property in the hands of the transferee, donee, or grantee. No election may be made under this subsection after December 31, 1954."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall be effective as if included in the amendment made by section 2 of Public Law 539, Eighty-Second Congress, at the time of its enactment.

SEC. 103. EXTENSION OF TIME FOR MAKING ELECTION WITH RESPECT TO WAR-LOSS RECOVERIES.

Section 127(c)(5) (relating to election with respect to war-loss recoveries) is hereby amended by striking out "December 31, 1952" and inserting in lieu thereof "December 31, 1953".

SEC. 104. EXTENSION OF PERIOD OF ABATEMENT OF INCOME TAXES OF MEMBERS OF ARMED FORCES UPON DEATH.

Section 154 (relating to income taxes of members of Armed Forces on death) is hereby amended by striking out "January 1, 1954" and inserting in lieu thereof "January 1, 1955".

SEC. 105. EXTENSION OF TEMPORARY PROVISIONS RELATING TO LIFE INSURANCE COMPANIES.

(a) TAX FOR 1953.—Sections 201(a)(1) (relating to imposition of tax on life insurance companies), 203A (relating to 1951 and 1952 adjusted normal-tax net income of life insurance companies), and 433(a)(1)(H) (relating to excess profits net income of life insurance companies) are each hereby amended by striking out "1951 and 1952" wherever appearing therein and inserting in lieu thereof "1953".

(b) EFFECTIVE DATE.—The amendments made by subsection (a) shall apply only to taxable years beginning in 1953. The application of the amendment to section 201(f) (relating to disallowance of double deductions) made by section 336(c)(2) of the Revenue Act of 1951 is hereby extended to taxable years beginning after December 31, 1952.

SEC. 106. EXTENSION OF PERIOD FOR EXEMPTION FROM ADDITIONAL ESTATE TAX OF MEMBERS OF ARMED FORCES UPON DEATH.

Section 939(b) (relating to the tax treatment of estates of certain members of the Armed Forces) is hereby amended by striking out "JANUARY 1, 1954" and inserting in lieu thereof "JANUARY 1, 1955", and by striking out "January 1, 1954" and inserting in lieu thereof "January 1, 1955".

TITLE II—MISCELLANEOUS

SEC. 201. VENUE OF ACTIONS FOR VIOLATIONS OF ACT OF OCTOBER 19, 1949.

(a) AMENDMENT OF ACT.—Section 2 of the Act entitled "An Act to assist States in collecting sales and use taxes on cigarettes", approved October 19, 1949 (15 U. S. C., sec. 376), is hereby amended by striking out "forward to" and inserting in lieu thereof "file with".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply only in respect of memoranda or copies of invoices covering shipments made during the calendar month in which this Act is enacted and subsequent calendar months.

SEC. 202. DEDUCTION OF CERTAIN UNPAID EXPENSES AND INTEREST.

(a) AMENDMENT OF SECTION 24(c).—Paragraph (1) of section 24(c) (relating to disallowance of certain deductions for expenses incurred and interest accrued) is hereby amended to read as follows:

"(1) If within the period consisting of the taxable year of the taxpayer and two and one-half months after the close thereof (A) such expenses or interest are not paid, and (B) the amount thereof is not includible in the gross income of the person to whom the payment is to be made; and".

(b) EFFECTIVE DATE.—

(1) Except as otherwise provided in paragraph (2), the amendment made by subsection (a) shall apply only with respect to taxable years beginning after December 31, 1950.

(2) At the election of a taxpayer (hereinafter in this paragraph referred to as the "payor") made within one year after the date of the enactment of this Act, the amendment made by subsection (a) shall also apply with respect to such taxable years of the payor beginning after December 31, 1945, and before January 1, 1951, as are specified by the payor in making such election. Such election for any taxable year shall not be valid as to any amount unless, at or before the time when such election is filed—

(A) the person (hereinafter in this paragraph referred to as the "payee") to whom such amount was payable included such amount in gross income for his taxable year for which such amount was includible in gross income, or

(B) the payee files a written consent to the assessment and collection of any deficiency and interest resulting from the payee's failure to include such amount in gross income for such taxable year, or

(C) the payor pays an amount equal to the deficiency and interest which would be payable by the payee pursuant to subparagraph (B) if he filed such consent. (Any amount paid under this subparagraph shall be assessed, notwithstanding any law or rule of law to the contrary, as an addition to the tax of the payor for the year for which the election is filed.)

The periods of limitation provided in sections 275 and 276 of the Internal Revenue Code on the making of an assessment and the beginning of distraint or a proceeding in court for collection shall, with respect to any deficiency and interest thereon resulting from any consent filed pursuant to subparagraph (B), include one year immediately following the date such consent is

filed, and such assessment and collection may be made notwithstanding any provision of law or any rule of law which otherwise would prevent such assessment and collection. If an election by a payor should be filed for a taxable year of the payor for which allowance of credit or refund of an overpayment is barred (at the time of such filing) by any law or rule of law, any consent filed by the payee in respect of any amount which represents expenses incurred or interest accrued by the payor for such year shall be void. If a consent requires the inclusion in the gross income of the payee for any taxable year of an amount which was erroneously included in the gross income of the payee for another taxable year and, on the date the consent is filed, correction of the effect of the error is prevented by the operation of any provision of the internal-revenue laws other than section 3761 of the Internal Revenue Code (relating to compromises), then the effect of the error shall be corrected in accordance with section 3801 of the Internal Revenue Code as if the consent were a determination under such section 3801 in which there is adopted a position maintained by the Secretary of the Treasury. The Secretary of the Treasury shall prescribe such regulations as may be necessary to carry out the provisions of this paragraph.

SEC. 203. BASIS OF CERTAIN PROPERTY TRANSFERRED IN TRUST.

(a) AMENDMENT OF SECTION 113(a)(5).—The second sentence of section 113(a)(5) (relating to the basis of property transmitted at death) is hereby amended by inserting immediately after the word "revoke the trust" the following: "or to make any change in the enjoyment thereof through the exercise of a power to alter, amend, or terminate the trust".

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply (1) only in the case of property transferred by grantors dying after December 31, 1951, and (2) only with respect to taxable years ending after December 31, 1951.

SEC. 204. EARNED INCOME FROM SOURCES WITHOUT THE UNITED STATES.

(a) AMENDMENT OF SECTION 116(a)(2).—Section 116(a)(2) (relating to exclusion from gross income of earned income from sources without the United States) is hereby amended by adding at the end thereof the following new sentences:

"If the 18-month period includes the entire taxable year, the amount excluded under this paragraph for such taxable year shall not exceed $20,000. If the 18-month period does not include the entire taxable year, the amount excluded under this paragraph for such taxable year shall not exceed an amount which bears the same ratio to $20,000 as the number of days in the part of the taxable year within the 18-month period bears to the total number of days in such year."

(b) WITHHOLDING OF TAX ON WAGES OF CITIZENS OUTSIDE THE UNITED STATES.—So much of section 1621(a)(8) (relating to the definition of wages) as precedes subparagraph (B) thereof is hereby amended to read as follows:

"(8)(A) for services for an employer (other than the United States or any agency thereof) (i) performed by a citizen of the United States if, at the time of the payment of such remuneration, it is reasonable to believe that such remuneration will be excluded from gross income under section 116(a), or (ii) performed in a foreign country by such a citizen if, at the time of the payment of such remuneration, the employer is required by the law of any foreign country to withhold income tax upon such remuneration, or".

(c) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply with respect to taxable years ending after December 31, 1952, but only to amounts received after such date. In the case of any taxable year beginning in 1952 and ending in 1953 the exclusion of amounts received after December 31, 1952, shall not exceed an amount which is the same proportion of $20,000 as the number of days in such taxable year after December 31, 1952, is of 365 days. The amendments made by subsections (a) and (b) shall not affect the liability of any employer to deduct and withhold the tax imposed by section 1622 in the case of any remuneration paid before the first day of the first month beginning more than ten days after the date of the enactment of this Act.

SEC. 205. NET OPERATING LOSS CARRY-OVERS.

(a) AMENDMENT OF SECTION 122(b)(2).—

(1) Section 122(b)(2) (relating to net operating loss carry-over) is hereby amended by adding after subparagraphs (D) the following new subparagraphs:

"(E) Loss For Taxable Years of Corporations Beginning in 1947 and Ending in 1948.—If a corporation (other than a corporation which commenced business after December 31, 1945) has a net operating loss for a taxable year beginning in 1947 and ending in 1948, subparagraph (C) shall apply as if the taxable year began after December 31, 1947; except that the net operating loss carry-over for the third succeeding taxable year shall not exceed that amount which bears the same ratio to the net operating loss as the number of days in the taxable year after December 31, 1947, bears to the total number of days in the taxable year.

"(F) Loss in Case of Corporations Whose First Taxable Year Began in 1949 and Ended in 1950.—If the first taxable year of a corporation began in 1949 and ended in 1950, and if the corporation had a net operating loss for such first taxable year, there shall be a net operating loss carry-over for the fourth and fifth succeeding taxable years. The amount of such carry-over shall be determined in accordance with the first sentence of subparagraph (B); except that—

"(i) such carry-over for the fourth succeeding taxable year shall not exceed so much of such net operating loss as is allocable to 1950, and

"(ii) such carry-over for the fifth succeeding taxable year shall not exceed the amount by which the carry-over for the fourth succeeding taxable year (as limited by clause (i) of this sentence) exceeds the net income for the fourth succeeding taxable year computed as provided in clauses (i) and (ii) of the first sentence of subparagraph (B).

For the purposes of the preceding sentence, the portion of the net operating loss which is allocable to 1950 shall be an amount which bears the same ratio to such loss as the number of days in the taxable year after December 31, 1949, bears to the total number of days in the taxable year."

(2) Subparagraph (A) of section 122(b)(2) is hereby amended by striking out "subparagraph (D)," and inserting in lieu thereof "subparagraphs (D) and (E),".

(3) The amendment made by paragraph (2), and subparagraph (E) of section 122(b)(2) of the Internal Revenue Code as added by paragraph (1), shall apply with respect to taxable years ending after December 31, 1947. Subparagraph (F) of section 122 (b) (2) of the Internal Revenue Code as added by paragraph (1) shall apply with respect to taxable years ending after December 31, 1949.

(b) SUCCESSOR RAILROAD CORPORATIONS.—

(1) Subsection (c) of the first section of the Act of July 15, 1947 (61 Stat. 324), relating to allowance to successor railroad corporations of benefits of certain carry-overs of predecessor corporations, is hereby amended to read as follows:

"(c) For the purposes of this section, if the period, beginning on the first day of the taxable year of the predecessor corporation in which the acquisition occurred and ending on the last day of the taxable year of the successor corporation in which the acquisition occurred, is not more than twelve months, then—

"(1) if such net operating loss or unused excess profits credit was for a taxable year beginning before January 1, 1948, the number of succeeding taxable years to which such net operating loss or unused excess profits credit is a carry-over shall be three (instead of two, as respectively provided in section 122(b)(2)(A) and section 710(c)(3)(B) of such code); and

"(2) if such net operating loss was for a taxable year beginning after December 31, 1947, and before January 1, 1950, the number of succeeding

taxable years to which such net operating loss is a carry-over shall be four (instead of three, as provided in section 122(b)(2)(C) of such code);

and such regulations shall prescribe (as nearly as possible in the manner respectively prescribed in sections 122(b)(2) and 710(c)(3)(B) of such code with respect to a net operating loss or an unused excess profits credit, as the case may be, for such taxable year) the amount to be carried over to the last of such succeeding taxable years."

(2) The amendment made by paragraph (1) shall be effective as if included in such Act of July 15, 1947, at the time of its enactment.

SEC. 206. AMORTIZATION DEDUCTION FOR GRAIN STORAGE FACILITIES.

(a) ALLOWANCE OF DEDUCTION.—Supplement B of subchapter C of chapter 1 is hereby amended by inserting after section 124A the following new section:

"SEC. 124B. AMORTIZATION DEDUCTION FOR GRAIN STORAGE FACILITIES.

"(a) ALLOWANCE OF DEDUCTION.—

"(1) ORIGINAL OWNER.—Any person who constructs, reconstructs, or erects a grain storage facility (as defined in subsection (d)) shall, at his election, be entitled to a deduction with respect to the amortization of the adjusted basis (for determining gain) of such facility based on a period of sixty months. The sixty-month period shall begin as to any such facility, at the election of the taxpayer, with the month following the month in which the facility was completed, or with the succeeding taxable year.

"(2) SUBSEQUENT OWNERS.—Any person who acquires a grain storage facility from a taxpayer who—

"(A) elected under subsection (b) to take the amortization deduction provided by this subsection with respect to such facility, and

"(B) did not discontinue the amortization deduction pursuant to subsection (c).

shall, at his election, be entitled to a deduction with respect to the adjusted basis (determined under subsection (e)(2)) of such facility based on the period, if any, remaining (at the time of acquisition) in the sixty-month period elected under subsection (b) by the person who constructed, reconstructed, or erected such facility.

"(3) AMOUNT OF DEDUCTION.—The amortization deduction provided in paragraphs (1) and (2) shall be an amount, with respect to each month of the amortization period within the taxable year, equal to the adjusted basis of the facility at the end of such month, divided by the number of months (including the month for which the deduction is computed) remaining in the period. Such adjusted basis at the end of the month shall be computed without regard to the amortization deduction for such month. The amortization deduction above provided with respect to any month shall be in lieu of the deduction with respect to such facility for such month provided by section 23(l) (relating to exhaustion, wear and tear, and obsolescence).

"(b) ELECTION OF AMORTIZATION.—The election of the taxpayer under subsection (a)(1) to take the amortization deduction and to begin the sixty-month period with the month following the month in which the facility was completed shall be made only by a statement to that effect in the return for the taxable year in which the facility was completed. The election of the taxpayer under subsection (a)(1) to take the amortization deduction and to begin such period with the taxable year succeeding such year shall be made only by a statement to that effect in the return for such succeeding taxable year. The election of the taxpayer under subsection (a)(2) to take the amortization deduction shall be made only by a statement to that effect in the return for the taxable year in which the facility was acquired. Notwithstanding the preceding three sentences, the election of the taxpayer under subsection (a) (1) or (2) may be made, under such regulations as the Secretary may prescribe, before the time prescribed in the applicable sentence.

"(c) TERMINATION OF AMORTIZATION DEDUCTION.—A taxpayer which has elected under subsection (b) to take the amortization deduction provided in subsection (a) may, at any time after making such election, discontinue the amortization deduction with respect to the remainder of the amortization period, such discontinuance to begin as of the beginning of any month specified by the taxpayer

in a notice in writing filed with the Secretary before the beginning of such month. The deduction provided under section 23(l) shall be allowed, beginning with the first month as to which the amortization deduction is not applicable, and the taxpayer shall not be entitled to any further amortization deduction with respect to such facility.

"(d) DEFINITION OF GRAIN STORAGE FACILITY.—For the purposes of this section, the term 'grain storage facility' means—

"(1) any corn crib, grain bin, or grain elevator, or any similar structure suitable primarily for the storage of grain, which crib, bin, elevator, or structure is intended by the taxpayer at the time of his election to be used for the storage of grain produced by him (or, if the election is made by a partnership, produced by the members thereof); and

"(2) any public grain warehouse permanently equipped for receiving, elevating, conditioning, and loading out grain,

the construction, reconstruction, or erection of which was completed after December 31, 1952, and on or before December 31, 1956. If any structure described in clause (1) or (2) of the preceding sentence is altered or remodeled so as to increase its capacity for the storage of grain, or if any structure is converted, through alteration or remodeling, into a structure so described, and if such alteration or remodeling was completed after December 31, 1952, and on or before December 31, 1956, such alteration or remodeling shall be treated as the construction of a grain storage facility. The term 'grain storage facility' shall include only property of a character which is subject to the allowance for depreciation provided in section 23(l). The term 'grain storage facility' shall not include any facility any part of which is an emergency facility within the meaning of section 124A.

"(e) DETERMINATION OF ADJUSTED BASIS.—

"(1) ORIGINAL OWNERS.—For the purpose of subsection (a)(1)—

"(A) in determining the adjusted basis of any grain storage facility, the construction, reconstruction, or erection of which was begun before January 1, 1953, there shall be included only so much of the amount of the adjusted basis (computed without regard to this subsection) as is properly attributable to such construction, reconstruction, or erection after December 31, 1952, and

"(B) in determining the adjusted basis of any facility which is a grain storage facility within the meaning of the second sentence of subsection (d), there shall be included only so much of the amount otherwise included in such basis as is properly attributable to the alteration or remodeling.

If any existing grain storage facility as defined in the first sentence of subsection (d) is altered or remodeled as provided in the second sentence of subsection (d), the expenditures for such remodeling or alteration shall not be applied in adjustment of the basis of such existing facility but a separate basis shall be computed in respect of such facility as if the part altered or remodeled were a new and separate grain storage facility.

"(2) SUBSEQUENT OWNERS.—For the purpose of subsection (a)(2), the adjusted basis of any grain storage facility shall be whichever of the following amounts is the smaller: (A) The basis (unadjusted) of such facility for the purposes of this section in the hands of the transferor, donor, or grantor, adjusted as if such facility in the hands of the taxpayer had a substitute basis within the meaning of section 113(b)(2)(A), or (B) so much of the adjusted basis (for determining gain) of the facility in the hands of the taxpayer (as computed without regard to this subsection) as is properly attributable to construction, reconstruction, or erection after December 31, 1952.

"(f) DEPRECIATION DEDUCTION.—If the adjusted basis of the grain storage facility (computed without regard to subsection (e)) exceeds the adjusted basis computed under subsection (e), the deduction provided by section 23(l) shall, despite the provisions of subsection (a)(3) of this section, be allowed with respect to such grain storage facility as if the adjusted basis for the purpose of such deduction were an amount equal to the amount of such excess.

"(g) LIFE TENANT AND REMAINDERMAN.—In the case of property held by one person for life with remainder to another person, the amortization deduction provided in subsection (a) shall be computed as if the life tenant were the absolute owner of the property and shall be allowed to the life tenant."

(b) TECHNICAL AMENDMENTS.—

(1) Section 23(t) is hereby amended to read as follows:

"(t) AMORTIZATION DEDUCTION.—The deduction for amortization provided in sections 124, 124A, and 124B."

(2) Section 172 is hereby amended by striking out "of emergency facilities".

(3) Section 190 is hereby amended by inserting after "emergency facilities" the following: "or grain storage facilities".

(c) EFFECTIVE DATE.—The amendments made by subsections (a) and (b) shall apply only with respect to taxable years ending after the date of the enactment of this Act.

SEC. 207. EXCLUSION OF CERTAIN TRANSFERS TAKING EFFECT AT DEATH.

(a) DECEDENTS DYING AFTER FEBRUARY 10, 1939.—Paragraph (1) of section 811(c) (relating to the inclusion of certain interests in the decedent's gross estate) is hereby amended by inserting after subparagraph (C) the following:

"Subparagraph (B) shall not apply to a transfer made before March 4, 1931; nor shall subparagraph (B) apply to a transfer made after March 3, 1931, and before June 7, 1932, unless the property transferred would have been includible in the decedent's gross estate by reason of the amendatory language of the joint resolution of March 3, 1931 (46 Stat. 1516)."

(b) DECEDENTS DYING BEFORE FEBRUARY 11, 1939.—For the purposes of section 302(c) of the Revenue Act of 1926, as amended, an interest of a decedent shall not be included in his gross estate as intended to take effect in possession or enjoyment at or after his death unless it would have been includible as such a transfer under section 811(c)(2) of the Internal Revenue Code, as amended by section 7 of Public Law 378, Eighty-first Congress, approved October 25, 1949 (63 Stat. 891), had such section 811(c)(2), as so amended, applied to the estate of such decedent. No refund or credit of any overpayment resulting from the application of this subsection shall be allowed or made if prevented by the operation of the statute of limitations or by any other law or rule of law; except that if the determination of the Federal estate tax liability in respect of the estate of any decedent dying before February 11, 1939, was pending on January 17, 1949, in the Tax Court of the United States or in any other court of competent jurisdiction, or if a decision of the Tax Court of the United States or such other court determining such estate tax liability did not become final until on or after January 17, 1949, then refund or credit of any overpayment resulting from the application of this subsection may, nevertheless, be made or allowed if claim therefor is filed within one year from the date of the enactment of this Act, notwithstanding section 319(a) of the Revenue Act of 1926 or any other law or rule of law which would otherwise prevent the allowance of such refund or credit.

(c) INTEREST.—No interest shall be allowed or paid on any overpayment resulting from the application of this section with respect to any payment made before the date of the enactment of this Act.

(d) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply only with respect to estates of decedents dying after February 10, 1939. Subsection (b) shall apply only with respect to estates of decedents dying before February 11, 1939.

SEC. 208. FAILURE TO RELINQUISH A POWER IN CERTAIN DISABILITY CASES.

(a) AMENDMENT OF SECTION 811(d).—Section 811(d) (relating to revocable transfers) is hereby amended by inserting after paragraph (3) thereof the following new paragraph:

"(4) EFFECT OF DISABILITY IN CERTAIN CASES.—For the purposes of this subsection, in the case of a decedent who was (for a continuous period beginning not less than three months before December 31, 1947, and ending with his death) under a mental disability to relinquish a power, the term 'power' shall not include a power the relinquishment of which on or after January 1, 1940, and on or before December 31, 1947, would, by reason of section 1000(e), be deemed not to be a transfer of property for the purposes of chapter 4."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply only with respect to estates of decedents dying after December 31, 1950.

SEC. 209. REVERSIONARY INTERESTS IN CASE OF LIFE INSURANCE.

(a) DECEDENTS DYING AFTER JANUARY 10, 1941, AND BEFORE OCTOBER 22, 1942.—Effective with respect to estates of decedents dying after January 10, 1941, and before October 22, 1942, the proceeds of life insurance receivable by beneficiaries other than the executor shall not be included in the gross estate of a decedent under section 811(g) of the Internal Revenue Code unless such proceeds would have been includible under section 404 (c) of the Revenue Act of 1942 (as amended by section 503(a) of the Revenue Act of 1950) had such section 404(c), as so amended, applied to such estate.

(b) INTEREST.—No interest shall be allowed or paid on any overpayment resulting from the application of subsection (a) with respect to any payment made before the date of the enactment of this Act.

SEC. 210. MARITAL DEDUCTION IN CERTAIN CASES WHERE DECEDENT DIED BEFORE APRIL 3, 1948.

(a) IN GENERAL.—In the case of an interest in property passing by will from the decedent, if the surviving spouse is entitled for life to all the income from such property, payable annually or at more frequent intervals, with power in the surviving spouse to use and consume such portion of the property as the surviving spouse may need or desire for her (or his) comfortable support and maintenance, and with no power in any person other than the surviving spouse to appoint any part of such property, then—

(1) the interest so passing shall, for the purposes of subparagraph (A) of section 812(e)(1) of the Internal Revenue Code, be considered as passing to the surviving spouse; and

(2) no part of the interest so passing shall, for the purposes of subparagraph (B)(i) of section 812 (e)(1) of the Internal Revenue Code, be considered as passing to any person other than the surviving spouse.

Nothing in this subsection shall be construed to permit the same items to be twice deducted.

(b) ELECTION.—The provisions of subsection (a) shall apply only if the surviving spouse files an election under this section with the Secretary within one year after the date of the enactment of this Act under such regulations as the Secretary shall prescribe. If such election is so filed, the property subject to such power shall, notwithstanding any other provision of law, be considered for purposes of chapters 3 and 4 of the Internal Revenue Code as property as to which the surviving spouse had a general power of appointment exercisable by deed or will. If the surviving spouse has made an election pursuant to this section, the periods of limitation provided in chapters 3 and 4 of the Internal Revenue Code on the making of an assessment and the beginning of distraint or a proceeding in court for collection shall, with respect to any deficiency and interest thereon resulting from such election, include one year immediately following the date such election is filed, and such assessment and collection may be made notwithstanding any provision of law or any rule of law which otherwise would prevent such assessment and collection.

(c) INTEREST.—No interest shall be allowed or paid on any overpayment resulting from the application of this section.

(d) EFFECTIVE DATE.—This section shall apply only with respect to estates of decedents dying after December 31, 1947, and on or before the date of the enactment of the Revenue Act of 1948. If refund or credit of any overpayment resulting from the application of subsections (a) and (b) is prevented on the date of the enactment of this Act, or within one year from such date, by the operation of any law or rule of law (other than section 3760 of the Internal Revenue Code, relating to closing agreements, and other than section 3761 of such code, relating to compromises), refund or credit of such overpayment may, nevertheless, be made or allowed if claim therefor is filed within one year from the date of the enactment of this Act.

SEC. 211. MITIGATION OF EFFECT OF STATUTE OF LIMITATIONS.

(a) AMENDMENT OF SECTION 3801(b).—Section 3801(b) (relating to circumstances of adjustment) is hereby amended by inserting after paragraph (5) the following new paragraphs:

"(6) Disallows a deduction or credit which should have been allowed to, but was not alowed to, the taxpayer for another taxable year, or to a related taxpayer; but this paragraph shall apply only if (A) the determination became final on or after June 1, 1952, and (B) credit or refund of the overpayment attributable to the deduction or credit which should have been allowed to the taxpayer or related taxpayer was not barred, by any law or rule of law, at the time the taxpayer first maintained before the Secretary or the Tax Court of the United States, in writing, that he was entitled to such deduction or credit in the taxable year for which it is so disallowed; or

"(7) Requires the exclusion from gross income of an item which is includible in the gross income of the taxpayer for another taxable year or in the gross income of a related taxpayer; but this paragraph shall apply only if (A) the determination became final on or after June 1, 1952, and (B) assessment of deficiency under section 272(a) by the Secretary for such other taxable year or against such related taxpayer was not barred, by any law or rule of law, at the time the Secretary first maintained in a notice of deficiency sent pursuant to section 272(a) or before the Tax Court of the United States, that such item should be included in the gross income of the taxpayer for the taxable year to which the determination relates—".

(b) TECHNICAL AMENDMENTS.—

(1) Paragraph (5) of section 3801(b) is hereby amended by striking out "transaction—" and inserting in lieu thereof "transaction; or".

(2) The second sentence of section 3801(b) is hereby amended by striking out "Such" and inserting in lieu thereof "Except in cases described in paragraphs (6) and (7), such".

(c) EFFECTIVE DATE.—The amendments made by subsections (a) and (b) shall be effective as if included in the Internal Revenue Code at the time of its enactment. In any case in which the determination referred to in paragraph (6) or (7) of section 3801(b), as amended by subsection (a) of this section, became final before the date of the enactment of this Act, the one-year period described in section 3801(c) shall be extended to include the one-year period beginning with the date of the enactment of this Act.

Approved August 15, 1953.

Rev. Rul. 213

Digests of public laws enacted during the first session of the Eighty-third Congress which pertain to internal revenue matters.

The Internal Revenue Code has been amended by the following public laws enacted during the first session of the Eighty-third Congress:

Number of public law	*Date approved*	*Page No., this Bulletin*
125	July 16, 1953	473
196	Aug. 5, 1953	474
213	Aug. 7, 1953	475
219	Aug. 7, 1953	476
238	Aug. 8, 1953	479
240	Aug. 8, 1953	480
274	Aug 14, 1953	484
283	Aug. 15, 1953	484
287	Aug. 15, 1953	485

Following is a list of the Code sections which were amended or added by these public laws and a brief explanation of the amendment. The statements explaining the Code sections and the amendments are not intended as interpretations but are intended merely to indicate the general nature or effect of the provisions involved.

22(b)(13). *Exemption from tax of combat pay of members of the Armed Forces.*—Section 22(b)(13) exempts from income tax

the pay received, prior to January 1, 1954, by certain members of the Armed Forces while they are serving in a combat zone. Public Law 213 extends this exemption for an additional year to January 1, 1955.

24(c). *Deduction of unpaid expenses and interest.*—Section 24(c) prohibits the allowance of a deduction for interest and other expenses incurred during the taxable year of the taxpayer (payor) and payable to a closely related taxpayer (payee) who reports income on the cash receipts basis unless the expenses are paid during the payor's taxable year or within 2½ months thereafter or unless the payee constructively receives during the payor's taxable year the amounts to be paid. The constructive receipt rule is extended by Public Law 287 to cover the 2½-month period.

25(b)(3). *Definition of dependent.*—In defining those who may qualify as a dependent of a taxpayer, section 25(b)(3) provides that a legally adopted child of a person shall be considered a child of such person by blood. This rule is extended by Public Law 213 to a child for whom a petition for adoption was filed and denied because of mental incapacity of the surviving natural parent to agree to the adoption.

112(b)(7). *Recognition of gain in certain "1 month" complete corporate liquidations.*—Section 112(b)(7) grants partial relief to certain shareholders who receive distributions in 1951 and 1952 in complete liquidation of a corporation provided the liquidation occurs within a single calendar month. Public Law 287 extends this provision to 1953.

113(a)(5). *Basis of trust property transmitted at death.*—Section 113(a)(5) provides that the basis of property acquired by bequest, devise, or inheritance shall be the fair market value of such property at the time of such acquisition. Where property is transferred in trust with the grantor retaining the income from such property for his life with power to revoke the trust, the basis of the property to the person taking it under the terms of the trust is the same as if the property had passed under a will executed on the day of the grantor's death. The same treatment is extended by Public Law 287 to property acquired from a trust in which the grantor reserved a life estate and had the power to make any change in the enjoyment of the corpus of the trust through the power to alter, amend, or terminate the trust. Before this amendment, the basis of property transferred without consideration to a trust with those reservations was determined, after death of the grantor, by reference to the rules for gift property—that is, the basis for gain was the grantor's basis, and the basis for loss was the lower of the grantor's basis or the fair market value at the time of the transfer by the grantor.

113(d). *Election in respect of excessive depreciation (Virginian Hotel rule).*—Section 113(d) gave taxpayers until the close of 1952 to make an irrevocable election with respect to adjustments for excessive depreciation during the period March 1, 1913 through December 31, 1951. Public Law 287 extends

to December 31, 1954, the period for making the election, and provides that a taxpayer may, at any time before January 1, 1955, revoke an election that he made on or before December 31, 1952.

116(a)(2). *Earned income from sources outside the United States.*—This section provides that a citizen who during a period of 18 consecutive months spends at least 510 full days in a foreign country or countries may exclude from gross income the income he earns abroad during that period. There was no limitation on the amount that could be excluded from gross income under this provision; but the amendment made by Public Law 287 provides for a limitation of $20,000 for an entire taxable year.

122(b)(2). *Net operating loss carryovers for corporations.*—Before amendment of this section, there was a 2-year carryover period for taxable years beginning before 1948, a 3-year period for taxable years beginning in 1948 and 1949, and a 5-year period for taxable years beginning after December 31, 1949. Public Law 287 amends this section to provide in the case of certain corporations a 3-year carryover period for taxable years beginning in 1947 and ending in 1948 and a 5-year period for taxable years beginning in 1949 and ending in 1950. An amendment was also made to the act of July 15, 1947, to allow a 4-year carryover period for taxable years beginning in 1948 and 1949, in the case of certain successor railroad corporations.

124B. *Amortization deduction for grain storage facilities.*—Public Law 287 adds this new section to the Code to permit taxpayers to deduct over a period of 60 months the costs of construction or adaptation of grain storage facilities completed after December 31, 1952, and on or before December 31, 1956. Related technical amendments were made to sections 23(t), 172, and 190.

127(c)(5). *Election with respect to war-loss recoveries.*—The Revenue Act of 1951 added to section 127(c) the provision that a taxpayer may elect to compute his tax liability with respect to war-loss recoveries by measuring the tax benefits received from deducting the war losses in prior years. With respect to recoveries made during taxable years ending before October 21, 1951 (the date of enactment of the Revenue Act of 1951) the election must be made on or before December 31, 1952. Public Law 287 extends the time for making this election to December 31, 1953.

154. *Abatement of income taxes of members of the Armed Forces.*—In the case of a member of the Armed Forces who dies after June 24, 1950, and before January 1, 1954, while serving in a combat zone, section 154 provides that any unpaid income tax liability at date of death shall be abated. It further provides that any tax paid for the taxable year in which he dies and for prior taxable years ending after the first day he served in a combat zone after June 24, 1950, shall be credited or refunded. Public Law 287 extends these provisions to January 1, 1955.

201 (a) (1), (f)
203A
433(a)(1)(H). *Temporary provisions relating to life insurance companies.*—Public Law 287 extends to 1953 the temporary provisions for taxation of life insurance companies which have been applicable to 1951 and 1952. It also makes permanent the provision in section 201(f) that double deductions may not be allowed. Formerly, section 201(f) was applicable only to 1951 and 1952.
273. *Abatement of income tax jeopardy assessments.*—When the ultimate collection of a tax is in danger, an immediate jeopardy assessment may be made to get control of available assets of a taxpayer pending final determination of his liability, if any. No specific authority has existed to revoke such an assessment where it is subsequently found that there is no danger of losing the tax. Public Law 274 adds a new subsection (k) which specifically authorizes the abatement of income tax jeopardy assessments when it is determined that jeopardy does not exist.
430 (a), (c)
432(b). *Extension of excess-profits tax.*—The excess-profits tax was originally scheduled to expire on June 30, 1953. Public Law 125 extends the tax for an additional 6 months to December 31, 1953.
811(c). *Exemption of certain reserved-income transfers from estate tax.*—In the case of decedents dying on or after January 1, 1951, section 811(c)(1)(B) required the inclusion in the decedent's gross estate of all transfers made during the decedent's lifetime where he retained interests in the income from the transferred property. Public Law 287 amends section 811(c) to exempt from the estate tax all transfers of that type made prior to March 4, 1931, and all such transfers made between March 3, 1931, and June 7, 1932, which would not have been taxable under the provisions of the Joint Resolution of March 3, 1931.
811(d). *Relief from estate tax in certain disability cases.*—Section 811(d) requires the inclusion in the decedent's gross estate of any property which he transferred during his lifetime retaining a power to alter, amend, revoke, or terminate the enjoyment of the property by the beneficiary. Section 1000(e) permitted the release of such a power (provided it was one which only permitted the grantor to change the beneficial enjoyment of the property but not to revest it in himself) prior to December 31, 1947, without liability for gift tax. Public Law 287 amends section 811(d) to exempt from estate tax in the case of decedents dying after December 31, 1950, property subject to a power which could have been released free of gift tax under section 1000(e) provided the decedent was under a mental disability to relinquish the power for a period beginning at least 3 months prior to December 31, 1947, and ending with his death.
872. *Abatement of estate tax jeopardy assessments.*—Public Law 274 adds a new subsection (j) which specifically authorizes

the abatement of gift tax jeopardy assessments when it is determined that jeopardy does not exist.

939(b). *Exemption from additional estate tax of certain members of the Armed Forces.*—This section exempts from the additional estate tax the estates of certain members of the Armed Forces who die after June 24, 1950, and before January 1, 1954, as a result of serving in a combat zone. Public Law 287 extends this exemption so that the provisions are applicable to persons who die before January 1, 1955.

1013. *Abatement of gift tax jeopardy assessments.*—Public Law 274 adds a new subsection (j) which specifically authorizes the abatement of gift tax jeopardy assessments when it is determined that jeopardy does not exist.

1106. *Retirement of judges of The Tax Court of the United States.*—Public Law 219 adds to the Code a new section setting forth provisions with respect to the retirement of judges of The Tax Court of the United States.

1606, 1607. *Unemployment insurance coverage for certain merchant seamen.*—Public Law 196 amends these sections to permit unemployment insurance coverage under State unemployment compensation laws for seamen employed on certain merchant vessels operated by the United States.

1621(a)(1). *Exemption from withholding tax of combat pay of members of the Armed Forces.*—This section in effect exempts from withholding tax the combat pay of a member of the Armed Forces for services performed prior to January 1, 1954. Public Law 213 extends this exemption an additional year to January 1, 1955.

1621(a)(8). *Withholding of tax on wages of citizens outside the United States.*—Prior to amendment, section 1621(a)(8) excluded from withholding remuneration for services performed in a foreign country by a United States citizen if certain conditions were met. In some cases withholding was required with regard to remuneration for services which was excluded from gross income under section 116(a)(1) or (2) where the remuneration was for services performed outside the United States but not within a foreign country, for example, remuneration for services performed on the high seas. Public Law 287 amends section 1621(a)(8) to eliminate this condition and to make section 1621(a)(8) correspond more precisely with section 116(a).

2563. *Extension of certain narcotics provisions to the Trust Territories of the Pacific Islands.*—This section sets forth the territorial extent of certain narcotics provisions of the Code. Public Law 238 amends the section to extend these provisions to the Trust Territory of the Pacific Islands. Related technical amendments are made to sections 2554(h)(1), 2564, 2565, and 3228.

3228. *Definition of "narcotic drugs".*—Doubt has existed as to whether the narcotics provisions of the Code may be construed as being applicable to narcotic drugs produced synthetically. Public Law 240 adds to section 3228 a new subsection (g) to make it clear the term "narcotic drugs" includes drugs syn-

thetically produced. Related technical amendments are made to sections 2550(a), 2558(b), 2564(b), 2565, 3220, 3220(g), 3222(c)(1), 3228(e), and 3228(f). The term "narcotic drugs" was substituted for certain words wherever they appear in subchapter A of chapter 23 of the Code and part V of subchapter A of chapter 27 of the Code.

3250(1)(5). *Drawback on distilled spirits used for designated nonbeverage purposes.*—The drawback under this section of taxes on distilled spirits has previously been allowed only on a quarterly basis. Public Law 283 amends the section to provide that a taxpayer may elect to receive the refund on a monthly basis.

3801(b). *Mitigation of effect of the statute of limitations.*—Section 3801(b) has previously set forth five circumstances under which the effect of the statute of limitations may be mitigated to permit an adjustment in income tax cases. Adjustment under these five circumstances is dependent upon the maintenance of an inconsistent position by the Commissioner or the taxpayer. Public Law 287 adds two additional circumstances. An adjustment under either of these two circumstances is not dependent upon the maintenance of an inconsistent position.

Some other provisions enacted during the first session of the Eighty-third Congress which did not actually amend an Internal Revenue Code section but which have a direct bearing on internal revenue matters are as follows:

Section 207(b), Public Law 287, exempts from estate tax in the case of decedents dying before February 11, 1939, certain transfers previously taxable as transfers intended to take effect at or after death. However, refunds are allowable in such cases only if the cases are still open or became barred on or after January 17, 1949.

Section 209, Public Law 287, with reference to Code section 811(g), makes the 5-percent rule in the case of reversionary interests in life insurance applicable to decedents dying after January 10, 1941, rather than after October 21, 1942, as previously provided.

Section 210, Public Law 287, with reference to Code section 812(e)(1), provides a marital deduction, if elected by the surviving spouse, with respect to property passing by will from a decedent who died in 1948 but before April 3 of that year, if the surviving spouse is entitled to receive the income for life and has the power to use or consume the corpus for her (his) comfortable support.

Public Law 4, approved February 14, 1953, continues until June 30, 1954, the suspension of certain import taxes on copper.

Public Law 178, approved August 1, 1953, extends indefinitely the provision that Members of Congress may deduct for income tax purposes amounts which they expend for "living expenses" in Washington. The deduction may not exceed $3,000 in any taxable year.

Section 4, Public Law 212, entitled "Outer Continental Shelf Lands Act," approved August 7, 1953, extends the internal rev-

enue laws to all artificial islands and fixed structures which may be erected on the outer Continental Shelf for the exploitation therefrom of resources.

Public Law 221, approved August 7, 1953, continues until the close of June 30, 1954, the suspension of duties and import taxes on metal scrap.

Public Law 243 (Customs Simplification Act of 1953), approved August 8, 1953, amends certain administrative provisions of the Tariff Act of 1930. Certain of the provisions amended relate to exemptions from duties and internal revenue taxes.

Pertinent excerpts from Public Laws 178, 212, and 243, and the entire text of Public Law 221 are published on pages 473, 475, 481, and 478, this Bulletin. Public Law 4 was published in C. B. 1953-1, 529.

Rev. Rul. 226*

Publication of new income tax Regulations 118

Regulations 118 superseding Regulations 111 with respect to taxable years beginning after December 31, 1951, was published in the Federal Register on Saturday, September 26, 1953, as part 39 of title 26 of the Code of Federal Regulations.

The new regulations codify the existing provisions of Regulations 111 which are applicable to taxable years beginning after December 31, 1951, but do not contain provisions of Regulations 111 which have no application to taxable years beginning after that date. They do not affect the validity of elections or other actions taken pursuant to the provisions of Regulations 111.

The regulations as published in the Federal Register are a true copy of the official regulations and may be cited in the usual manner. (For example, sec. 39.22(a)-1, Regulations 118.) Copies of the Federal Register have been distributed to each regional commissioner and district director. Limited distribution has also been made in the National Office.

Official copies of Regulations 118 will be available in bound form from the Superintendent of Documents in approximately a month. These copies will contain an index and appendix and will be in the same format as is used by the Federal Register.

COMMISSIONER'S REORGANIZATION ORDER No. 14

Establishment of internal revenue regions and regional offices

SECTION 1. PURPOSE.

The purpose of this reorganization order is to implement the provisions of Treasury Department Order No. 150-26 by providing basic instructions for the orderly liquidation of former district commissioners' offices and establishment of internal revenue regions and regional offices.

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*Originally issued as IR-Circular No. 189, dated September 23, 1953.

SEC. 2. ORGANIZATION AND FUNCTIONS.

.01 Effective July 1, 1953, Treasury Department Order No. 150-26, copy attached, abolishes the offices of district commissioners of internal revenue and establishes in lieu thereof nine internal revenue regions, each of which comprises the jurisdictional area of a regional commissioner of internal revenue. Each internal revenue region is composed of several internal revenue districts, which term will hereafter be used to describe the districts established pursuant to section 3650 of the Code, each of which comprises the jurisdictional area of a district director of internal revenue.

.02 Treasury Department Order No. 150-26 has no effect on the activities or jurisdictional areas of the internal revenue districts, except for the transfer of Puerto Rico and the Virgin Islands of the United States to the District Director of Internal Revenue, Lower Manhattan. The district directors shall continue to exercise the authorities and perform the duties delegated and assigned to them before the effective date of such order, except with respect to functions performed by the Alcohol and Tobacco Tax Divisions which are being transferred by separate order to the Assistant Regional Commissioner, Alcohol and Tobacco Tax. It is anticipated that other functions will be placed in district directors July 1, 1953, or shortly thereafter. Each district director shall report and be responsible to the regional commissioner of the internal revenue region which encompasses his internal revenue district.

.03 The regional commissioners shall exercise the authorities and perform the duties delegated and assigned to the former district commissioners of internal revenue and in effect immediately prior to the effective date of this order, including the direction and coordination of the work of the district directors of internal revenue within such regions, and such other duties as may subsequently be assigned. Each regional commissioner shall report and be responsible to the Commissioner of Internal Revenue.

SEC. 3. DESIGNATION OF REGIONAL COMMISSIONERS.

Regional commissioners have been designated as follows:

Region	*Regional commissioner's office*	*Regional commissioner*
Atlanta	Atlanta Federal Savings Bldg.	Ellison C. Palmer
Boston	55 Tremont St.	Wilbur A. Gallahan
Chicago	17 North Dearborn St.	Ernest C. Wright
Cincinnati	Post Office Bldg.	George E. Neal
Dallas	Mercantile Commerce Bldg.	Alfred W. Fleming
New York City	90 Church St.	Clarence R. Krigbaum
Omaha	Dodge and 18th Sts.	Frank W. Lohn
Philadelphia	1700 Widener Bldg.	Edward C. Dougherty
San Francisco	Flood Bldg.	Morris A. Fremming

SEC. 4. LIQUIDATION OF DISTRICT COMMISSIONERS' OFFICES.

.01 Former district commissioners' offices located in Atlanta, Boston, Chicago, Dallas, New York City, and Philadelphia are transferred to the new regional commissioners' offices in their respective cities.

.02 Former district commissioners' offices located in Buffalo, Cleveland, Detroit, Los Angeles, Seattle, and St. Paul are each wholly contained within a new internal revenue region. The regional commissioners of the internal revenue regions in which such offices are located shall be responsible for the liquidation of these offices.

.03 Former district commissioners' offices located in Baltimore, Birmingham, Denver, St. Louis, and Louisville are having their internal revenue districts divided among two or more internal revenue regions. Responsibility for the liquidation of these offices shall be as follows:

Baltimore	—Regional Commissioner, Philadelphia
Birmingham	—Regional Commissioner, Atlanta
Denver	—Regional Commissioner, Omaha
St. Louis	—Regional Commissioner, Omaha
Louisville	—Regional Commissioner, Cincinnati

.04 Officers in charge are expected to take all possible steps leading to the orderly transfer or liquidation of their respective offices prior to July 1, 1953. In those cases where it is desirable for the liquidating officer to take over prior to July 1, 1953, because the officer in charge is being transferred to a new position, or for other reason, arrangements should be made between the officers concerned to that effect.

SEC. 5. UTILIZATION OF PERSONNEL, RECORDS, AND FACILITIES.

.01 The personnel, records, equipment, and other facilities of the former district commissioners' offices are transferred to the supervision of the regional commissioners responsible for the transfer or liquidation of such offices, as set forth in section 4 of this order, with the exception that former district commissioners' office personnel (such as Appellate personnel) administratively located in an internal revenue district transferred to a different regional commissioner are transferred, together with pertinent records and facilities, to the supervision of such regional commissioner.

.02 The Bureau's policy with respect to the personnel attached to the offices being liquidated is to utilize all qualified personnel in the Internal Revenue Service to the fullest extent possible. Lists of such employees available for transfer to other positions and locations will be furnished employing officers throughout the Bureau with instructions for preferential treatment in connection with all vacancies in the Internal Revenue Service. In those cases where personnel is found to be excess to the needs of the Bureau, all actions taken with respect to such personnel will be processed strictly in accordance with the reduction-in-force regulations of the Civil Service Commission and the Treasury Department.

.03 The general principle governing the transfer of records is that records pertaining to each individual internal revenue district will be transferred to the regional office encompassing such district, while records of a general nature will be transferred to the regional office to which the former district commissioner's office is transferred or which has liquidation authority over it.

.04 The disposition of space, supplies, equipment, and other facilities will be determined by the liquidation officer.

.05 Additional instructions covering the policies and procedures set forth in this section are being prepared for early issuance.

SEC. 6. TIMING OF LIQUIDATION.

It is expected that all major phases of the liquidation process will be completed by August 1, 1953, although it may be necessary to hold a few employees for an additional period of not more than 30 days. This liquidation goal does not apply to Appellate or Alcohol and

Tobacco Tax activities, concerning which special instructions will be issued.

SEC. 7. ESTABLISHMENT OF REGIONAL COMMISSIONERS' OFFICES.

The regional commissioners will move as rapidly as possible to establish their new offices and have them in operation by July 1, 1953. Instructions previously issued for the establishment of the former district commissioners' offices may be used as general guide lines for the establishment and staffing of such offices. Necessary modifications of these instructions will soon be issued.

SEC. 8. ADJUSTMENTS IN INSPECTION AND LEGAL SERVICES.

.01 The Inspection Service organization is being adjusted to change the title "chief inspector" to "regional inspector" and to provide one such regional inspector for each internal revenue region.

.02 It is understood that the organization of the Office of Chief Counsel also will be adjusted to change the title "district counsel" to "regional counsel", and to provide one such regional counsel for each internal revenue region.

.03 The effective date of these organizational adjustments will be announced later.

SEC. 9. EFFECT ON EXISTING DUTIES AND DIRECTIVES.

.01 Except as modified by this order, all employees shall continue to perform the duties they were authorized to perform immediately prior to the effective date of this order, and to comply with procedures in effect at that time, until otherwise provided.

.02 All directives, instructions, orders, certificates, regulations, rulings, delegations of authority, and other actions heretofore issued or taken, and in effect immediately prior to the effective date of this order, shall remain in full force and effect except as herein modified, until otherwise provided; provided that whenever any such document, delegation, or action applies to the incumbent of a position where title has been changed by, or by virtue of, this order it shall be deemed to apply to the incumbent of the position carrying the new counterpart title.

SEC. 10. EFFECTIVE DATE.

This order is effective July 1, 1953, concurrently with Treasury Department Order No. 150–26.

O. GORDON DELK,
Acting Commissioner.

June 19, 1953.

TREASURY DEPARTMENT ORDER No. 150-26

Bureau of Internal Revenue reorganization. Offices of regional commissioner and district director of internal revenue.

By virtue of the authority vested in me as Secretary of the Treasury, it is hereby ordered:

1. *Regional commissioner of internal revenue.*—Each office of district commissioner of internal revenue shall bear the operating title of "regional commissioner of internal revenue," identified by the name of the city in which the headquarters office is located.

2. *District director of internal revenue.*—The title of each office of director of internal revenue shall be changed to "district director of internal revenue," identified by the name of the city or subdivision thereof in which the headquarters office is located.

3. *Establishment of offices and boundaries of regional commissioner.*—

(*a*) *Atlanta.*—There is established an office of Regional Commissioner of Internal Revenue, Atlanta, which shall be comprised of the States of Alabama, Florida, Georgia, Mississippi, North Carolina, South Carolina, and Tennessee, and the Canal Zone. The headquarters office shall be in Atlanta, Ga.

(*b*) *Boston.*—There is established an office of Regional Commissioner of Internal Revenue, Boston, which shall be comprised of the States of Connecticut, Maine, Massachusetts, New Hampshire, Rhode Island, and Vermont. The headquarters office shall be in Boston, Mass.

(*c*) *Chicago.*—There is established an office of Regional Commissioner of Internal Revenue, Chicago, which shall be comprised of the States of Illinois, Michigan, and Wisconsin. The headquarters office shall be in Chicago, Ill.

(*d*) *Cincinnati.*—There is established an office of Regional Commissioner of Internal Revenue, Cincinnati, which shall be comprised of the States of Indiana, Kentucky, Ohio, Virginia, and West Virginia. The headquarters office shall be in Cincinnati, Ohio.

(*e*) *Dallas.*—There is established an office of Regional Commissioner of Internal Revenue, Dallas, which shall be comprised of the States of Arkansas, Louisiana, Oklahoma, New Mexico, and Texas. The headquarters office shall be in Dallas, Tex.

(*f*) *New York City.*—There is established an office of Regional Commissioner of Internal Revenue, New York City, which shall be comprised of the State of New York and Puerto Rico and Virgin Islands of the United States. The headquarters office shall be in New York, N. Y.

(*g*) *Omaha.*—There is established an office of Regional Commissioner of Internal Revenue, Omaha, which shall be comprised of the States of Colorado, Iowa, Kansas, Minnesota, Missouri, Nebraska, North Dakota, South Dakota, and Wyoming. The headquarters office shall be in Omaha, Nebr.

(*h*) *Philadelphia.*—There is established an office of Regional Commissioner of Internal Revenue, Philadelphia, which shall be comprised of the States of Delaware, Maryland, New Jersey, and Pennsylvania, and the District of Columbia. The headquarters office shall be in Philadelphia, Pa.

(*i*) *San Francisco.*—There is established an office of Regional Commissioner of Internal Revenue, San Francisco, which shall be comprised of the States of Arizona, California, Idaho, Montana, Nevada, Oregon, Utah, and Washington, and the Territories of Alaska and Hawaii. The headquarters office shall be in San Francisco, Calif.

4. *Abolition of certain offices of district commissioner.*—The offices of district commissioner of internal revenue established prior to the effective date of this order are abolished.

5. *Regional office in which office of district director included.*—The office of any district director of internal revenue included within the territory comprising the office of a regional commissioner of internal revenue shall be included within the office of such regional commissioner.

6. *Internal revenue districts.*—Each district established pursuant to section 3650 of the Internal Revenue Code shall be known as an internal revenue district and shall be identified by the name of the city or subdivision thereof in which the headquarters office of the district director of internal revenue is located.

7. *Puerto Rico and Virgin Islands of United States included in Internal Revenue District, Lower Manhattan.*—Puerto Rico and the Virgin Islands of the United States, now comprising a part of the Internal Revenue District, Baltimore, shall be and they are transferred to and made a part of the Internal Revenue District, Lower Manhattan.

8. *Inconsistent provision.*—Any provision of any order inconsistent with any provision of this order is modified to the extent of such inconsistency.

9. *Effective date.*—This order shall be effective July 1, 1953.

M. B. FOLSOM,
Acting Secretary of the Treasury.

June 15, 1953.

COMMISSIONER'S REORGANIZATION ORDER No. 15

General delegation of functions to regional commissioners and district directors of internal revenue.

Pursuant to the authority vested in me as Commissioner of Internal Revenue, it is hereby ordered:

1. *Regional commissioner.*—The functions of the regional commissioner of internal revenue with respect to the region in which his office is located shall, except as otherwise provided by any order or document effective on the same date as this order, consist of the functions vested in the district commissioner of internal revenue immediately prior to the effective date of this order.

2. *Assistant regional commissioners.*—(*a*) *Positions.*—There shall be in the office of the regional commissioner of internal revenue a position of assistant regional commissioner for each of the following functions:

Administration	Audit
Alcohol and Tobacco Tax	Collection
Appellate	Intelligence

(*b*) *Functions.*—The functions of the assistant regional commissioners shall, except as otherwise provided by any order or document effective on the same date as this order, consist of the functions vested in the assistant district commissioner for the same activities immediately prior to the effective date of this order.

3. *District directors.*—(*a*) *Functions.*—The functions of the district director of internal revenue with respect to the district in which his office is located shall, except as otherwise provided by any order or document effective on the same date as this order, consist of the func-

tions vested in directors of internal revenue immediately prior to the effective date of this order: *Provided*, That such functions shall not include those of the former head, Alcohol and Tobacco Tax Division, which functions have been vested in the Assistant Regional Commissioner, Alcohol and Tobacco Tax.

4. *Division heads.*—(*a*) *Positions.*—There shall be in the office of the district director a position of head of each of the following divisions:

Administration	Collection
Audit	Intelligence

(*b*) *Functions.*—The functions of each head of division shall, except as otherwise provided by any order or document effective on the same date as this order, consist of the functions vested in the head of the same division immediately prior to the effective date of this order.

5. *Assistant district director of internal revenue.*—There shall be in the office of each district director of internal revenue the position of assistant district director of internal revenue. In case of death, resignation, absence, or sickness of the district director, such assistant district director shall, without further authorization, perform the functions of the district director until otherwise provided. In the performance of such functions he shall be designated as acting district director of internal revenue.

6. *Authority to redelegate.*—Any function vested in a regional commissioner or district director of internal revenue may, within the framework of the organization described herein, be delegated by him to any subordinate under his supervision, except as otherwise directed.

7. *Continuation of functions.*—Except as otherwise directed, all officers and employees within any region shall continue to perform the functions they were authorized to perform immediately prior to the effective date of this order and to comply with procedures in effect at such time.

8. *Prior orders affected.*—(*a*) The following orders and any amendments thereof are revoked:

Commissioner's Reorganization Order No Chi-1, dated May 15, 1952.
Commissioner's Reorganization Order No. NYC-1, dated June 23, 1952.
Operations Reorganization Order No. 3, dated September 4, 1952.
Operations Reorganization Order No. Det-1, dated November 24, 1952.

(*b*) Any other order inconsistent with any provision of this order is modified to the extent of such inconsistency.

9. *Effective date.*—This order shall be effective July 1, 1953.

T. COLEMAN ANDREWS,
Commissioner.

July 1, 1953.

COMMISSIONER'S REORGANIZATION ORDER No. 17

Standard nomenclature for organizational units and principal officers.

Pursuant to the authority vested in me as Commissioner of Internal Revenue and in order to standardize terminology applicable to the Internal Revenue Service, it is directed:

1. The geographic organizations of the Internal Revenue Service are designated as National, Regional, and District.

2. The organizational components of the Internal Revenue Service and the titles of its principal officers are designated as follows, the designation of each component and the principal officer of such component being indicated on the same line:

Service	Commissioner
Office	Assistant commissioner
Region	Regional commissioner
District	District director
Division (National)	Director
Division (Region or district)	Chief
Branch	Chief
Section	Chief
Unit	Supervisor
Group	Supervisor

3. All existing delegations of authority to any officer or employee and all references to any organizational component affected by this order shall apply to the position or the organizational component as redesignated by this order.

4. This order shall be effective July 7, 1953.

T. COLEMAN ANDREWS,
Commissioner.

July 7, 1953.

COMMISSIONER'S REORGANIZATION ORDER No. 20

Delegation of authority to grant extensions of time for filing estate tax returns.

Pursuant to the authority vested in me as Commissioner of Internal Revenue, it is directed:

1. The authority to grant extensions of time to file estate tax returns, not to exceed 6 months from the due date, is delegated to the district directors of internal revenue to be exercised in accordance with applicable regulations and procedures.

2. This order shall become effective September 1, 1953.

O. GORDON DELK,
Acting Commissioner.

August 26, 1953.

COMMISSIONER'S REORGANIZATION ORDER No. 21

Delegation of authority to grant extension of time to pay income, excess profits, estate, and gift taxes.

Pursuant to the authority vested in me as Commissioner of Internal Revenue, it is directed that:

1. The authority to grant extensions of time to pay income, excess profits, estate, and gift taxes, including deficiencies, is hereby delegated to the district directors of internal revenue to be exercised in accordance with applicable regulations and procedures.

2. This order shall become effective September 1, 1953.

O. GORDON DELK,
Acting Commissioner.

August 26, 1953.

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COMMISSIONER'S REORGANIZATION ORDER No. 23

District directors authorized to require records to be kept showing liability to income tax.

Pursuant to the authority vested in me as Commissioner of Internal Revenue, district directors of internal revenue are hereby authorized to require any person, by notice served upon him, to keep such records as shall show whether or not such person is liable to the income tax under chapter 1 of the Internal Revenue Code, and the correct amount of income subject to tax.

T. COLEMAN ANDREWS,
Commissioner.

September 11, 1953.

COMMISSIONER'S REORGANIZATION ORDER No. 25

Delegation of authority to grant extensions of time for filing returns and paying certain excise taxes.

Pursuant to the authority vested in me as Commissioner of Internal Revenue, it is directed:

1. The authority to grant extensions of time to file returns and pay taxes collected with respect to telegram, telephone, radio, and cable facilities, and transportation of persons and property, pursuant to sections 3467(b), 3469(e), and 3475(d) of the Internal Revenue Code, respectively, and to make monthly deposits in payment of such taxes pursuant to Treasury Decision 6025 [p. 400, this Bulletin], approved July 3, 1953, is delegated to district directors of internal revenue to be exercised in accordance with applicable regulations and procedures.
2. This order shall be effective this date.

T. COLEMAN ANDREWS,
Commissioner.

September 29, 1953.

TECHNICAL CHANGES, ACT OF 1953

[House of Representatives Report No. 894, Eighty-third Congress, First Session]

[July 21, 1953]

Mr. Reed of New York, from the Committee on Ways and Means, submitted the following report [to accompany H. R. 6426]:

The Committee on Ways and Means, to whom was referred the bill (H. R. 6426) to amend the Internal Revenue Code to extend the time during which certain provisions relating to income and estate taxes shall apply, and for other purposes, having considered the same, report favorably thereon without amendment and recommend that the bill do pass.

I. GENERAL STATEMENT

H. R. 6426 contains 17 sections dealing with amendments to the Internal Revenue Code. Six of the sections extend the period during which certain provisions of the Code will apply. The other 11 sections relate to amendments to the Internal Revenue Code providing for removal of inequities in income and estate tax cases. Your committee believes that it is important to take care of these inequities ahead of the general revision bill which will be considered next year.

II. EXPLANATION OF THE BILL

A. Extension Provisions

Section 101. Election as to recognition of gain in certain corporate liquidations.

This section extends to 1953 the provisions of section 112(b)(7) of the Internal Revenue Code dealing with the nonrecognition of gain in certain corporate liquidations. This provision which applied to certain liquidations in a single calendar month in 1951 was extended by the Revenue Act of 1951 to such liquidations in 1952 and is further extended by this bill to such liquidations occurring in a single calendar month in 1953. Your committee believes that such an extension for 1 year is desirable to enable those who were unable to arrange for liquidation within the requisite period in 1951 or 1952 to have the benefits of this provision if they can complete such liquidations in a single calendar month in 1953.

Section 102. Extension of time for elections under Public Law 539 overruling Virginian Hotel case.

In Public Law 539, approved July 14, 1952, Congress overruled the decision of the Supreme Court in the Viriginian Hotel case. Under that decision a taxpayer who deducted depreciation for any year in excess of the amount allowable for such year was nevertheless required to reduce the basis of his property by the entire amount of depreciation allowed, even though he had received no tax benefit from claiming such excessive depreciation as a deduction. Under Public Law 539, the basis of the property was not required to be reduced by such excessive depreciation unless the taxpayer had received a tax benefit for taking a deduction for such excessive amount. The taxpayer was granted under the law an election (under such regulations as the Secretary prescribed) to apply this new treatment retroactively to the period since February 28, 1913, and before January 1, 1952, but no election could be made after December 31, 1952. The Treasury regulations under the law were not promulgated until December 30, 1952. Thus taxpayers were not given sufficient time to determine whether such an election would be beneficial to them. Your committee therefore deems it desirable to extend through December 31, 1954, the time within which an election may be made. Since Public Law 539 provides that an election once made is irrevocable, the bill, in order to provide uniform treatment, permits taxpayers to revoke within the extended period elections made prior to January 1, 1953.

Section 103. Extension of time for making election with respect to war loss recoveries.

Section 341 of the Revenue Act of 1951 sets forth a new method for treatment of war losses under section 127 of the Internal Revenue Code. It provides that at the election of the taxpayer (under such regulations as the Secretary may prescribe) the tax for the year in which the deduction for the war loss was taken is to be recomputed by reducing the deduction by the amount of the recovered property taken at its depreciated cost on the date of the loss or at its fair market value on the date of recovery, whichever is lower. The resulting increase in tax for the year of the loss, if any, is added to the tax for the year of recovery. The time for electing the benefit of this provision expired on December 31, 1952. Since the Treasury regulations interpreting this section of the law were not promulgated until December 30, 1952, taxpayers did not have sufficient time to determine whether it was advantageous to make such an election. The bill extends the period for making such an election through December 31, 1953.

Section 104. Extension of period of abatement of income taxes of deceased members of Armed Forces.

Section 154 of the Internal Revenue Code provides in the case of an individual who died after June 24, 1950, and prior to January 1, 1954, as a result of active service in a combat zone as a member of the Armed Forces, an abatement of income tax liability which was outstanding at the date of his death. It also provides a forgiveness of the tax with respect to the taxable year in which falls the date of his death or with respect to any prior taxable year ending on or after the first day he so served in a combat zone after June 24, 1950. Your committee bill extends the period to which this section is applicable for one additional year so as to include the calendar year 1954.

Section 105. Extension of temporary provisions relating to life insurance companies.

The present temporary provisions for the taxation of life insurance companies are extended for 1 year by this section of your committee's bill. Pending the results of studies being made by the staffs of the Treasury and the Joint Committee on Internal Revenue Taxation, your committee deems it advisable to continue for 1 year the provisions of the present law.

Section 106. Extension of period for exemption from additional estate tax of deceased members of Armed Forces.

Section 939(b) of the Internal Revenue Code exempts from the additional estate tax estates of decedents dying after June 24, 1950, and before January 1, 1954, while in active service as members of the Armed Forces of the United States, where such decedents were killed in action while serving in a combat zone or died from wounds, disease, or injury incurred while so serving in line of duty and by reason of a hazard to which they were subjected as an incident of such service. Your committee's bill extends the application of this section to January 1, 1955.

B. Miscellaneous

Section 201. Venue of action for violation of State cigarette tax laws.

The act of October 19, 1949, provided that persons, other than distributors, who sell or dispose of cigarettes in interstate commerce must forward to the tobacco tax administrators of States to which shipments are made monthly reports setting forth the names and addresses of the persons to whom shipments are made and the brand and quantity of cigarettes so shipped. Some courts have held that under the statute violations of the act are committed at the place from which the cigarettes are shipped, since the act only requires the shippers to forward their reports. The bill requires the actual filing of the reports with the State tobacco administrator. This would have the effect of assuring, in the event of an offense committed under the act, that the venue of the action would be in the district in which the State tobacco administrator has his office.

Section 202. Deduction of certain unpaid expenses and interest.

In the case of certain closely related taxpayers, such as a corporation and a shareholder owning more than 50 percent of the corporation's stock, section 24(c) of the Code operates to disallow deduction of certain expenses and interest if the following conditions are met:

(1) The amount is not paid within the taxable year or within 2½ months after the close thereof; and

(2) Under the recipient's method of accounting the amount is not, unless paid, includible in his income in the taxable year in which, or with which, the taxable year of the payor corporation ends.

This provision is intended to insure that transactions between such related taxpayers do not operate to shift items of income or deductions. A situation has been called to the attention of your committee, however, where section 24(c) may work an undue hardship. For example, a recipient on the cash basis may have an amount credited to his account and made available to him by the corporate payor within 2½ months after the close of the payor's taxable year so that the recipient must include it in income as an item constructively received in the taxable year so credited. If, however, the corporate taxpayer fails actually to pay over such amount within the period of 2½ months, the item will not be allowed to the corporation as a deduction. Your committee believes that such a case should not fall within the ban of section 24(c) and the bill so provides by an appropriate amendment of requirement (1) above.

The amendment is applicable to taxable years of the payor beginning after December 31, 1950, but under certain conditions, set forth to insure that payments will be properly accounted for taxwise with respect to both parties, the payor may elect to make this amendment applicable to taxable years beginning after December 31, 1945, and before January 1, 1951.

Section 203. Income tax basis of property transferred in trust.

Section 113(a)(5) of existing law contains a provision to the effect that where the grantor retains the income from property in trust for his life with power to revoke the trust, the basis of the property in the hands of the persons entitled to take the property under the terms of the trust instrument after the grantor's death shall, after such death, be the same as if the property had passed under a

will executed on the day of the grantor's death. This results in the basis of the property in the hands of the recipients being its fair market value at the date of the grantor's death or, at the election of the executor, the value 1 year from the date of death. Your committee believes that this same rule should apply to situations where the grantor with a reserved life estate has the power to make any change in the enjoyment of the corpus of the trust through the power to alter, amend, or terminate the trust. In both cases, the trust property is required to be included in the gross estate of the grantor for estate tax purposes. The amendment applies only to grantors dying after December 31, 1951, and only with respect to taxable years ending after December 31, 1951.

Section 204. Earned income from sources without the United States.

Your committee deems it advisable to repeal section 116(a)(2) of the Internal Revenue Code, effective as to amounts received after April 14, 1953. Section 116(a)(2) excludes from income in the case of a citizen of the United States income earned abroad if such citizen was present in a foreign country or countries for a period of 17 out of 18 consecutive months. While this paragraph was designed to encourage men with technical knowledge to go abroad in order to complete specific projects, it has been subject to a great deal of abuse. Some individuals with large earnings have seized upon the provision as an inducement to go abroad to perform services, which were customarily performed at home, for the primary purpose of avoiding the Federal income taxes. It has also been ascertained that in many cases Americans taking advantage of this provision do not pay any income tax even to the foreign country or countries in which the income is earned. This is because they are not in any particular foreign country long enough to establish a residence or because the foreign country in question does not impose any income tax. It is believed that the repeal should not be effective until April 15, 1953, so that taxpayers who went abroad will not be subject to a tax on their earnings received prior to notice that this provision would be eliminated. However, taxpayers were put on notice as to the possible repeal of section 116(a)(2) by the introduction of a repeal bill on April 14, 1953, by the chairman of the committee and by the publication of correspondence with the Secretary of the Treasury, which was published in the Congressional Record of that date, in which the Secretary of the Treasury expressed concern over the manner in which this paragraph was being utilized for tax-avoidance purposes and expressed the hope that legislative treatment would be given to this problem to prevent such abuses. The bill will not affect the liability of any employer to deduct and withhold the tax on such earnings in the case of remuneration paid before the first day of the first month beginning more than 10 days after the date of the enactment of this act.

Section 205. Net operating loss deductions.

Your committee has included provisions designed to eliminate disparities in the treatment of taxpayers in respect to the taxable years to which a net operating loss may be carried forward. Under these provisions the number of years to which a net operating loss may be carried forward by certain corporations reporting income on the basis of a fiscal year has been extended. Under the cutoff dates in existing law these corporations are limited in the use of their net operating losses. For example, under existing law, if a corporation has a taxable year beginning on December 1, 1947, a net operating loss developed in that year may only be carried forward to the 2 succeeding taxable years whereas if the taxable year had begun on January 1, 1948, such may be available to offset gains of the 3 succeeding taxable years.

Your committee has provided that in the case of a corporation, other than a corporation which commenced business after December 31, 1945, which has a net operating loss for a taxable year beginning in 1947 and ending in 1948 (so that the taxable year overlaps the critical dates) such a corporation may utilize such loss in the third succeeding taxable year. The amount of such carryover to the third year cannot exceed an amount which bears the same ratio to the net operating loss as the number of days in the loss year falling after December 31, 1947, is of the total number of days in the loss year.

In the case of a corporation the first taxable year of which began in 1949 and ended in 1950, a comparable extension is provided. Such corporations are put on a basis similar to that provided for corporations with net operating losses for taxable years beginning after 1949, that is, the net operating loss may be available for the 5 succeeding taxable years. However, your committee's amendment

subjects the amount of the carryover to the fourth and fifth succeeding taxable years to a general limitation to such part of the net operating loss as is properly allocable to 1950.

Your committee has also added a provision amending section 1 of the act of July 15, 1947 (61 Stat. 324). This act allowed a carryforward of the net operating loss of a predecessor railroad corporation to a successor railroad corporation. Since the reorganization may have caused a short taxable year of the predecessor and of the successor to fall within one 12-month period, such corporations would, in effect, be denied the full 2-year carryforward available to other corporations, the act allowed a carryover for 3 taxable years in such cases. Section 330(b) of the Revenue Act of 1951 added section 122(b)(2)(C) to the Code which provided, in the case of all corporations, for a 3-year carryforward of a net operating loss incurred for any taxable year beginning after December 31, 1947, and before January 1, 1950. Accordingly your committee's amendment would allow a successor railroad corporation a 4-year carryover in order to continue the prior treatment under the act of July 15, 1947.

Section 206. Amortization deduction for grain storage facilities.

A critieal shortage of facilities for storing grain has developed throughout the Nation during the past several years. This shortage has been felt particularly by producers of such grains as wheat and corn. In view of the situation which has arisen, your committee has felt impelled to provide an inducement for taxpayers to construct new grain storage facilities, to increase the capacity of those already in existence, or to adapt existing construction to the storage of grain.

Under existing law, a taxpayer undertaking such expenditures would be allowed to recover his costs only through a deduction for depreciation taken over the period of the useful life of such new construction or adaptation. Your committee has added section 124B to the Code to allow such costs in the case of construction or adaptation after December 31, 1952, and before January 1, 1957, to be deducted, at the taxpayer's election, over the period of 60 months beginning either with the month following the month in which the facility was completed, or with the succeeding taxable year. In the event that the shortage of facilities for storing grain remains in a critical state through 1956, your committee would consider it appropriate to extend the date within which a taxpayer may construct such facilities and receive the benefits of this provision. The deduction is available only with respect to taxable years ending after the date of the enactment of this act. In the case of new construction the deduction is only available with respect to so much of the cost as is attributable to construction after December 31, 1952, and in the case of the alteration or adaptation of existing buildings only such cost as is properly attributable thereto after such date may be so deducted.

This amortization deduction is in lieu of that allowed for depreciation, but a taxpayer is allowed to deduct ordinary depreciation for that part of his costs of construction which would not qualify under this section, for example, by reason of not having been incurred subsequent to December 31, 1952. A taxpayer may elect to discontinue his amortization deductions under this section as of the beginning of any month specified in a notice filed with the Secretary before the beginning of such month and may thereafter be allowed the depreciation deduction. In the case of property held by one person for life with remainder to another, the life tenant is allowed the deduction under this section as if he were the absolute owner. Special rules are provided to allow the benefits of this deduction to a person acquiring a grain storage facility to which this section is applicable. These rules are discussed in the technical part of this report relating to this provision.

This special amortization deduction is available to a farmer constructing a grain storage facility. The statute defines a grain storage facility as a corncrib, grain bin, or grain elevator, or any similar structure primarily suited for the storage of grain, which is intended by the taxpayer at the time of his election to be used for the storage of grain produced by him. The deduction is also available to any person who constructs any public grain warehouse permanently equipped for handling grain. Under the definition of a grain storage facility the special amortization deduction is not allowed to persons who store only grain purchased for consumption in their business. For example, persons engaged in the milling of flour who construct storage facilities for purchased grain used in such processing would not be allowed to deduct the cost of any facilities under this provision.

Section 207. Exclusion of certain transfers taking effect at death.

Your committee has amended the estate tax provisions of the Code relating to certain transfers of property with retention of the income for life by the transferor. In 1930 the Supreme Court held that property so transferred should not be included in the taxable estate of the transferor. *May* v. *Heiner* (281 U. S. 238). In response to this and related decisions, on March 3, 1931, Congress adopted a joint resolution providing that such transfers were includible (46 Stat. 1516), and the Revenue Act of 1932 substantially reenacted the provisions of this joint resolution. The joint resolution was interpreted in 1938 as being only prospective in its operation so as not to apply the transfers made prior to the date of its adoption. *Hassett* v. *Welch* (303 U. S. 303).

In the face of what had long been regarded as the settled interpretation of the then existing estate tax provisions relating to these pre-1931 transfers with retention of a life estate by the transferor, the Supreme Court in 1949 in effect overruled its two earlier decisions and held that a transfer of property in 1924, with income retained for life by the transferor, required that the transferred property be included in the taxable estate of the transferor who died in 1939. *Commissioner* v. *Church* (335 U. S. 632).

Following the Church decision the Technical Changes Act of 1949 (as amended) provided that, in the case of life estates retained in transfers made on or before March 3, 1931 (and in some cases before June 7, 1932), the property would not be included in the decedent's gross estate solely by reason of retention of the life estate if the decedent died after the enactment of the Code on February 10, 1939, and prior to January 1, 1951. As that act was passed by the Senate, it contained provisions which would have restored the estate tax law to what it was prior to the Church opinion, that is, pre-1931 transfers would not be included in the gross estate of the decedent merely by reason of the retention of a life estate, regardless of when the decedent died. This provision was limited in conference, however, in the manner described above.

Your committee now agrees that the effect of the Church decision should be eliminated in all cases to which it was applicable. Prior legislation has already restored the estate tax law to what it was before the Church decision in respect to all decedents dying after the enactment of the Code and prior to January 1, 1951. Your committee's provision accomplishes this same result in respect of decedents dying on or after January 1, 1951.

Your committee has also provided relief for certain decedents where the death occurred prior to February 11, 1939, and whose estates were burdened with estate tax by reason of transfers made before March 4, 1931, involving the retention of a life estate, the reservation of a minute reversionary interest, or both. Since property transferred in this manner would not be included in the gross estate if the decedent died after February 10, 1939 (and before 1951), your committee's amendment would achieve a similar exemption for estates of decedents dying prior thereto. However, your committee has not felt it necessary to open the statute of limitations to any great extent in cases of decedents dying prior to February 11, 1939. It is only in cases in litigation at the time of the Church decision where there would appear to be any undue hardship. In these cases a refund or credit resulting from this provision will be allowed if a claim is filed within 1 year from the date of enactment of this act.

Section 208. Failure to relinquish a power in certain disability cases.

Grantors of discretionary trusts created prior to January 1, 1939, who had retained certain powers which would result in the inclusion of the trust property in their gross estate for estate tax purposes were, under section 1000(e) of the Code, permitted to relinquish such powers on or after January 1, 1940, and on or before December 31, 1947, free of gift tax. Your committee believes that grantors who were unable to relinquish their discretionary powers within the above period because of a mental disability should not be penalized. It is therefore provided that there shall not be included in a decedent's estate property previously transferred in trust as to which he retained certain discretionary powers if such decedent for at least 3 months prior to December 31, 1947, and continuing to the date of his death was under a mental disability such that he could not have relinquished such powers free of gift tax pursuant to section 1000(e). The term "mental disability" is intended to encompass those cases in which the decedent during the requisite period prior to his death was, in fact, incapable because of his mental condition of relinquishing the power, whether or not he was legally declared mentally incompetent during all or any part of such period.

Section 209. Reversionary interests in case of life insurance.

Section 404(c) of the Revenue Act of 1942 (as amended by sec. 503(a) of the Revenue Act of 1950) provided in the case of decedents dying after the date of its enactment (October 21, 1942) that the proceeds of life insurance policies should not be included in the decedent's estate by reason of premiums paid by the decedent prior to January 10, 1941, if the decedent at no time after that date retained an incident of ownership in such policy. In determining whether the decedent had such an "incident of ownership" after January 10, 1941, there was to be taken into account only those reversionary interests exceeding 5 percent of the value of the policy and arising other than by operation of law. Your committee believes that similar treatment should be extended in the case of decedents dying after January 10, 1941, and before October 22, 1942. Such decedents will be deemed to have an incident of ownership in insurance policies by reason of a reversionary interest held after January 10, 1941, only if such reversionary interest exceeded 5 percent of the value of the policy and arose by the express terms of the policy or other instrument and not by operation of law.

Section 210. Marital deduction in certain cases where decedent died before April 3, 1948.

The provisions of this section relate to the marital deduction for estate tax purposes. The attention of your committee has been called to certain situations where a decedent died after December 31, 1947, but prior to the date of the enactment of the Revenue Act of 1948, which allowed a marital deduction for estate tax purposes. Consequently, while the act applied to such cases, estates of decedents dying within this short period from January 1, 1948, to the date of its enactment on April 2, 1948, were unable to secure the benefit of its provisions in some cases because the will of the decedent was not in accord with certain technical requirements of the act. If the decedent had been alive after the enactment of the Revenue Act of 1948, his will would undoubtedly have been rewritten to conform to the provisions of the act. Thus, under the act, property subject to a power of appointment in order to be taken into account for purposes of the marital deduction must meet the requirements of section 812(e)(1)(F) of the Internal Revenue Code. This section requires the interest in property passing from the decedent under a power of appointment to be in trust and the power to be unlimited and exercisable by the surviving spouse at all events. Cases have been called to the attention of your committee where the power granted to the surviving spouse was not in trust and was confined to a power in the surviving spouse to use and consume such portion of the property as the surviving spouse may need or desire for her (or his) comfortable support or maintenance. It is the opinion of your committee that in the case of a decedent dying after December 31, 1947, and prior to April 3, 1948, a power of this broad application should be considered as sufficient to permit the marital deduction of property subject to such power and the bill so provides. The section is only applicable if the surviving spouse files with the Secretary of the Treasury within 1 year after the date of the enactment of this act an election to take the benefits of the section. If such an election is made the property subject to such power shall be considered as property as to which the surviving spouse had a general power of appointment created on the date of the decedent's death, exercisable by deed or by will. Thus a relinquishment of such power by the surviving spouse during her lifetime will result in a taxable gift and if such power is not relinquished during the lifetime of the surviving spouse, the property subject to such power will be considered as part of the estate of such surviving spouse for estate tax purposes.

Section 211. Mitigation of effect of statute of limitations.

Section 3801 of the Code allows either the taxpayer or the Commissioner to correct an improper tax result in certain cases where such action would otherwise be prevented by the running of the statute of limitations. This is possible by reason of the allowance under that section of an additional period of time beyond the period of limitations which would ordinarily be applicable. One of the principles of the present statute is to preclude any adjustment unless the hardship results from the maintenance of an inconsistent position by either the taxpayer or the Commissioner.

The statute operates effectively in cases to which it is directed, but your committee realizes that tax inequities, the correction of which is prevented by the running of the period of limitations, may exist without regard to whether or not

the position maintained by either party is inconsistent. A taxpayer may be disallowed a deduction or credit to which he is entitled in another taxable year or to which a related taxpayer may be entitled. Similarly, the Commissioner may have included an item in income for a taxable year different from the year for which such item should have been included, or the Commissioner may have included the item in the income of a related taxpayer.

Under present law, the errors described may not be corrected if discovered after the expiration of the period of limitation in respect to the correct year of the taxpayer or of the proper taxpayer. Your committee's bill includes provisions amending section 3801 in order to open the statute of limitations in such cases. Where a taxpayer claims a deduction or credit for a taxable year which is later determined to be the incorrect taxable year, or which is determined properly to belong to a related taxpayer, the amendment would permit a proper adjustment. However, the taxpayer is entitled to the benefits of this provision only if a credit or refund of the overpayment attributable to the deduction or credit for the correct year or to the related taxpayer was not barred at the time the taxpayer formally asserted that he should have received such credit or refund in the year disallowed.

Similarly, the Commissioner would be allowed to make assessment of tax with respect to the proper taxable year, if at the time he formally asserted that an item was includible in income for a taxable year, later determined to be the incorrect year, he could have made a proper assessment of tax for the correct year. An opportunity to make a proper assessment would also be extended to the Commissioner under similar circumstances in the case of the related taxpayer.

The amendments added by your committee are applicable only where the determination relating to the disallowance of the deduction or credit, or the exclusion of the item from gross income, as the case may be, became final after June 30, 1952.

III. DETAILED DISCUSSION OF THE TECHNICAL PROVISIONS OF THE BILL

TITLE I—EXTENSION PROVISIONS

SECTION 101. ELECTION AS TO RECOGNITION OF GAIN IN CERTAIN CORPORATE LIQUIDATIONS

This section amends section 112(b)(7) of the Code (relating to election as to recognition of gain in certain corporate liquidations), which section is applicable under existing law only in cases in which the liquidation was pursuant to a plan adopted after December 31, 1950, and the transfer of all the property under the liquidation occurred within 1 calendar month in 1951 or 1952. The amendment made by this section extends section 112(b)(7) for an additional year and makes it applicable to cases in which the liquidation is pursuant to a plan adopted after December 31, 1950, and the transfer of all the property under the liquidation occurs within 1 calendar month in 1951, 1952, or 1953. The effect of the section is, in general, to postpone the recognition of that portion of a qualified electing shareholder's gain on the liquidation which would otherwise be recognized and which is attributable to appreciation in the value of certain corporate assets unrealized by the corporation at the time such assets are distributed in complete liquidation.

Since the only amendment made by your committee to section 112(b)(7) is the insertion of the date 1953 after the dates 1951 and 1952 where they now appear in subparagraph (A)(ii), the date August 15, 1950, is still applicable in subparagraphs (B), (E), and (F) of that section (relating to the definition of excluded corporations and relating to the recognition of gain to the shareholders from the receipt of money or of stock or securities acquired by the liquidating corporation after such date).

The amendment made by this section is applicable to taxable years ending after December 31, 1952.

SECTION 102. EXTENSION OF TIME TO MAKE ELECTION IN RESPECT OF EXCESSIVE DEPRECIATION ALLOWED FOR PERIODS BEFORE 1952

This section amends section 113(d) of the Code so as to extend through December 31, 1954, the period within which a person may make the election pro-

vided in section 113(d). This section also permits an election made on or before December 31, 1952, to be revoked on or before December 31, 1954.

Any election made after December 31, 1952, under section 113(d), as amended by this section, will be irrevocable on the date made and shall be made in such manner as the Secretary may by regulations prescribe. If an election made on or before December 31, 1952, is revoked after such date, no new election may be made.

Neither an election nor a revocation of an election by the transferor, donor, or grantor, shall affect the basis of property in the hands of the transferee, donee, or grantee if such election or revocation was made after the date of the transfer, gift, or grant of such property.

The election under section 113(d), as amended by this section shall apply in respect of all property held by the person making the election at any time on or before December 31, 1952.

SECTION 103. EXTENSION OF TIME FOR MAKING ELECTION WITH RESPECT TO WAR LOSS RECOVERIES

This section amends section 127(c)(5) of the Code (relating to elections with respect to war losses) to extend from December 31, 1952, to December 31, 1953, the period during which a taxpayer may make an election to have the provisions of section 127(c)(3) apply to war loss property which was recovered during a taxable year ending on or before October 20, 1951. No change is made with respect to elections relating to such property recovered during taxable years ending after October 20, 1951.

SECTION 104. EXTENSION OF PERIOD OF ABATEMENT OF INCOME TAXES OF MEMBERS OF ARMED FORCES UPON DEATH

This section amends section 154 of the Internal Revenue Code to continue for an additional year the abatement of income tax provided for members of the Armed Forces who die as the result of service in a combat zone.

Section 154 of the Code now provides that in the case of an individual who dies after June 24, 1950, and prior to January 1, 1954, while in active service as a member of the Armed Forces of the United States, if such death occurred while serving in a combat zone (as determined under sec. 22(b)(13) of the Code) or as a result of wounds, disease, or injury incurred while so serving, (1) the income tax imposed by chapter 1 of the Code shall not apply with respect to the taxable year in which he dies or with respect to any prior taxable year ending on or after the first day he so served in a combat zone after June 24, 1950, and (2) the income tax imposed by chapter 1 of the Code and under the corresponding title of each prior revenue law for taxable years preceding his years of service in a combat zone which is unpaid at the date of his death shall be forgiven. This section merely continues this provision until January 1, 1955.

SECTION 105. EXTENSION OF TEMPORARY PROVISIONS RELATING TO LIFE INSURANCE COMPANIES

This section would amend sections 201, 203A, and 433 of the Internal Revenue Code to provide that the method of taxing life insurance companies used in 1951 and 1952 shall be extended 1 more year to apply with respect to taxable years beginning in 1953.

The amendment to section 201 continues for taxable years beginning in 1953 the flat-rate tax of 3¾ percent on the first $200,000 and 6½ percent on amounts in excess of $200,000 of adjusted normal-tax net income (as defined in sec. 203A). The injunction in section 201(f) against construing sections 201, 202, 203, and 203A so as to permit a double deduction for the same items is continued for taxable years beginning after December 31, 1952.

The amendment to section 203A applies the definition of adjusted normal-tax net income contained therein to taxable years beginning in 1953.

The amendment to section 433(a)(1)(H) extends to 1953 taxable years the 87 percent reserve interest credit used in 1951 and 1952 in arriving at the normal tax net income of life insurance companies for purposes of computing excess-profits net income.

SECTION 106. EXTENSION OF PERIOD FOR EXEMPTION FROM ADDITIONAL ESTATE TAX OF MEMBERS OF ARMED FORCES UPON DEATH

This section amends section 939(b) of the Internal Revenue Code to continue for an additional year the existing exemption from the additional estate tax provided for members of the Armed Forces who die as the result of service in a combat zone.

Section 939(b) of existing law provides that the tax imposed by section 935 (the additional estate tax) shall not apply to the transfer of the net estate of a citizen or resident of the United States dying after June 24, 1950, and before January 1, 1954, while in active service as a member of the Armed Forces of the United States, if such decedent (1) was killed in action while serving in a combat zone, as determined under section 22(b)(13) or (2) died at any place as a result of wounds, disease or injury suffered, while serving in a combat zone (as determined under sec. 22(b)(13)) and while in line of duty, by reason of a hazard to which he was subjected as an incident of such service. This section merely continues the exemption until January 1, 1955.

TITLE II—MISCELLANEOUS

SECTION 201. VENUE OF ACTIONS FOR VIOLATIONS OF ACT OF OCTOBER 19, 1949

This section would amend section 2 of the act entitled "An act to assist States in collecting sales and use taxes on cigarettes," approved October 19, 1949.

Section 2 of that act provides that any person selling or disposing of cigarettes in interstate commerce whereby such cigarettes are shipped to other than a distributor licensed by or located in a State taxing the sale or use of cigarettes shall, not later than the 10th day of each month, forward to the tobacco tax administrator of the State into which the shipment is made, a memorandum or a copy of the invoice covering each shipment made during the previous month into such State. The amendment made by subsection (a) of this section would require that the memorandum or copy of invoice be filed with, rather than forwarded to, the tobacco tax administrator, so that actions for violations of the act may be brought in the judicial district where the tobacco tax administrator of the State involved is located.

Subsection (b) of this section provides that the amendment shall apply only in respect of memorandums or copies of invoices covering shipments made during the calendar month in which this act is enacted and subsequent calendar months.

SECTION 202. DEDUCTION OF CERTAIN UNPAID EXPENSES AND INTEREST

Under the present provisions of section 24(c) of the Code no deduction is allowed for interest or expenses (1) if not paid within the taxable year or within 2½ months after the close thereof; and (2) if, by reason of the method of accounting of the person to whom the payment is to be made, the amount thereof is not, unless paid, includible in the gross income of such person for the taxable year in which or with which the taxable year of the taxpayer ends; and (3) if, at the close of the taxable year of the taxpayer or at any time within 2½ months thereafter, both the taxpayer and the person to whom the payment is to be made are persons between whom losses would be disallowed under section 24(b) of the Code. In general, section 24(c) has been interpreted as requiring actual payment (cash or negotiable paper having a determinable market value) of the expense or interest not later than 2½ months after the close of the taxable year. This construction has resulted in the denial of deductions to taxpayers in some cases even though by application of the doctrine of constructive receipt the amount for which the deduction is claimed is required to be included in the gross income of the payee during the 2½ months after the close of the payor's taxable year.

Section 202 of this bill amends section 24(c)(1) of the Code to prevent the disallowance of a deduction for interest or expenses if the amount thereof is includible in the gross income of the payee within the taxable year of the payor or within the 2½ months following the close of such taxable year.

Paragraph (b)(1) of section 202 of this bill provides that subsection (a) shall be applicable to taxable years of the payor beginning after December 31, 1950.

Paragraph (b)(2) provides that, if the taxpayer (payor) so elects within 1 year after the date of the enactment of this act, subsection (a) shall also apply to such taxable years of the taxpayer which began after December 31, 1945, and before January 1, 1951, as are specified in the election. This election for any taxable year will not be valid unless at or before the time of filing such election, (A) the payee has included the amount deductible by the taxpayer in gross income for the taxable year in which it was includible, (B) the payee files a written consent to the assessment and collection of any deficiency and interest attributable to the noninclusion of such amount in gross income for such taxable year, or (C) the taxpayer pays an amount equal to the deficiency and interest which would be assessed if the payee had filed such consent.

The period of limitations provided in sections 275 and 276 of the Code on the making of an assessment and the beginning of distraint or a proceeding in court for collection shall, with respect to any deficiency and interest thereon resulting from the filing of the consent required in (B) above, include 1 year following the date such consent was filed if such period of limitations otherwise would expire before the end of such 1-year period. The assessment and collection may be made notwithstanding any provision of law or any rule of law which otherwise would prevent such assessment and collection.

If an election by a taxpayer is filed for a taxable year for which the allowance of a credit or refund of an overpayment is barred, at the time of filing the election, by any law or rule of law, then any consent filed by the payee pursuant to this subsection with respect to such year shall be void.

If the payee is required to include in gross income pursuant to his consent an amount which was erroneously included in his gross income for another taxable year and, on the date the consent is filed, proper adjustment for the other taxable year is prevented by a provision of the internal revenue laws other than section 3761 (relating to compromises), then the error shall be corrected in accordance with the provisions of section 3801 of the Code as if such consent were a determination under section 3801 of the Code in which there is adopted a position maintained by the Secretary of the Treasury.

SECTION 203. BASIS OF CERTAIN PROPERTY TRANSFERRED IN TRUST

Subsection (a) of section 203 of the bill amends section 113(a)(5) of the Code, relating to the basis of property transmitted at death, to extend the application of that section to property acquired under the terms of certain types of trust instruments.

If property is transferred in trust to pay the income for life to, or upon the order or direction of, the grantor with the right reserved to the grantor at all times prior to his death to revoke the trust, section 113(a)(5) of existing law provides that the basis of such property in the hands of persons entitled under the terms of the trust instrument to the property after the grantor's death shall, after such death, be the same as though the trust instrument had been a will executed by the grantor on the date of his death. .This section of the bill would provide the same rule in cases where the grantor (in addition to reserving rights in the income) under the terms of the trust instrument had reserved the right at all times prior to his death to make a change in the enjoyment thereof through the exercise of a power to alter, amend, or terminate the trust. This amendment, like the provisions of existing law, is intended to apply only to property which forms a part of the corpus of the trust at the time of the grantor's death.

Subsection (b) of section 203 of the bill provides that the amendment made by subsection (a) shall apply only in the case of property transferred by grantors dying after December 31, 1951, and only with respect to taxable years ending after December 31, 1951.

SECTION 204. EARNED INCOME FROM SOURCES WITHOUT THE UNITED STATES

Under present section 116(a)(2) a citizen of the United States may exclude from gross income all amounts received from sources without the United States which constitute earned income (as specifically defined) attributable to any period of 18 consecutive months during which the taxpayer is physically present in a foreign country or countries for a total of at least 510 full days. Amounts paid by the United States or any agency thereof do not come within the exclusion.

This section limits the exclusion from gross income provided by section 116(a)(2) of the Code to amounts received or accrued, depending upon the taxpayer's method of accounting, on or before April 14, 1953, provided such amounts otherwise meet the requirements of section 116(a)(2). Amounts received or accrued, depending upon the taxpayer's method of accounting, after April 14, 1953, may not be excluded under section 116(a)(2).

The amendment has no effect on the running of the 18-month period during which a taxpayer may qualify with respect to the exclusion of income received on or before April 14, 1953. Thus, a part of the 18-month qualifying period may occur after April 14, 1953.

The amendment made by this section provides with regard to an amount received after April 14, 1953, in the case of a taxpayer entitled to the benefits of section 107, that the computations under section 107 shall be made without regard to the exclusion provided by section 116(a)(2).

Subsection (b) amends section 1621(a)(8)(A) of the Code to provide that there will be no withholding on remuneration paid to an employee if it is reasonable to believe that such remuneration will be excluded from gross income under section 116(a) of the Code. Under present law, withholding is required with regard to remuneration for services which may be excluded from gross income under section 116(a)(1) or (2) in cases where the remuneration is for services performed outside the United States but not within a foreign country, for example, remuneration for services performed on the high seas.

Subsection (c) provides that the amendment to section 1621(a)(8)(A) shall not affect the liability of any employer to deduct and withhold tax imposed by section 1622 in the case of any remuneration paid before the first day of the first month beginning more than 10 days after the date of enactment.

SECTION 205. NET OPERATING LOSS CARRYOVERS

(a) Amendment of section 122(b)(2).

Section 122(b)(2) of the Internal Revenue Code provides, in general, that a net operating loss sustained in a taxable year beginning prior to January 1, 1948 (to the extent that it is not absorbed as a carryback), can be carried over to the 2 succeeding taxable years, and similarly that a net operating loss sustained in a taxable year beginning after December 31, 1947, and before January 1, 1950, can be carried over to the 3 succeeding taxable years. Subsection (a) of section 205 would amend section 122(b)(2) of the Code to provide that a corporation which has a net operating loss for a taxable year beginning in 1947 and ending in 1948 may likewise carry such loss forward to the 3 succeeding taxable years. The carryover to the third succeeding taxable year, however, shall not exceed that amount of the net operating loss which bears the same ratio to the loss as the number of days in the taxable year after December 31, 1947, bears to the total number of days in the taxable year. The amendment in effect would thus allow that portion of the loss attributable to 1948 to be carried over for 3 taxable years to the extent that it has not been absorbed by the income of prior and intervening years. The amendment has no application to a corporation which commenced business after December 31, 1945, since such a corporation, under the present provisions of section 122(b)(2)(D), may carry a net operating loss sustained in a taxable year beginning after December 31, 1946, and before January 1, 1948, forward to the 3 succeeding taxable years.

Section 122(b)(2)(B) of the Code provides that a net operating loss sustained in a taxable year beginning after December 31, 1949, may be carried over to the 5 succeeding taxable years. Subsection (a) of section 205 would also amend section 122 (b) (2) to provide that if the first taxable year of the corporation began in 1949 and ended in 1950 and if it sustained a net operating loss in that taxable year, so much of the net operating loss as is allocable to 1950 may be carried forward to the fourth and fifth succeeding taxable years. The amount of the net operating loss which is allocable to 1950 is determined by dividing the loss by the number of days in the taxable year and multiplying by the number of days of the taxable year which fell in 1950. The amount of the carryover is determined in accordance with the first sentence of section 122(b)(2)(B), which amount is the excess of the net operating loss over the sum of the net income for each of the intervening years computed with the limitations, additions, and exceptions in clauses (i) and (ii) of that sentence, except that the carryover to the fourth succeeding taxable year is limited to the amount of loss allocable to 1950,

and is limited for the fifth succeeding taxable year to the portion of the loss allocable to 1950 minus the amount of the loss absorbed by the fourth year.

(b) Successor railroad corporations.

Subsection (b) of section 205 amends section 1(c) of Public Law 189, Eightieth Congress. Public Law 189 allows the successors corporation in the case of certain reorganized railroads to have the benefit of the carryovers of the net operating losses and unused excess-profits credits of the predecessor corporation. At the time of the enactment of Public Law 189 all taxpayers were allowed a 2-year carryover of net operating losses under the provisions of section 122 of the Internal Revenue Code. Section 1(c) of Public Law 189 in effect provided that if the period beginning on the first day of the taxable year of the predecessor corporation in which the acquisition occurred and ending on the last day of the taxable year of the successor corporation in which the acquisition occurred was not more than 12 months, then the net operating loss or unused excess-profits credit would be carried over for 3 years instead of 2 years as in the case of all other corporations. This provision was inserted in the statute because the last taxable year of the predecessor corporation and the first taxable year of the successor corporation in such a case would be short taxable years and it was desired in effect to give the successor corporation, as in the case of other corporations, the benefit of the carryovers for a full 2-year period. Section 330(b) of the Revenue Act of 1951, however, added section 122(b)(2)(C) to the Code which provided that a net operating loss sustained in a taxable year beginning after December 31, 1947, and before January 1, 1950, could be carried forward for 3 taxable years by all taxpayers. Section 205(b) of this bill accordingly amends section 1(c) of Public Law 189 to provide a 4-year carryover of a net operating loss sustained in a taxable year beginning after December 31, 1947, and before January 1, 1950, in the case of such reorganized railroads. The amendment in effect will make the results under Public Law 189 conform to those obtained by all corporations under section 122(b)(2)(C) of the Code. The amendment is to be effective as if included in Public Law 189 at the time of its enactment.

SECTION 206. AMORTIZATION DEDUCTION FOR GRAIN STORAGE FACILITIES

Subsection (a) of this section adds new section 124B to the Code, providing an amortization deduction for grain storage facilities. Under section 124B(a) the taxpayer may elect to amortize the adjusted basis (for determining gain) of a grain storage facility over a period of 60 months. The amortization deduction is allowable to (1) the original owner of a grain storage facility, i. e., the person who constructs, reconstructs, or erects such facility, or (2) any subsequent owner who acquires such a facility from another person who had made a valid election to take the amortization deduction and had not discontinued such deduction under section 124B(c). The deduction is allowable to a subsequent owner only if the original owner and each intervening owner elects to claim the amortization deduction, and neither the original owner nor any intervening owner had discontinued the amortization deduction under section 124B(c) prior to his disposition of the facility.

In the case of the original owner who constructs, reconstructs, or erects a grain storage facility, the amortization period is a period of 60 months. He may elect to begin such period with respect to any grain storage facility either with the month following the month in which the facility was completed or with the beginning of the succeeding taxable year. In the case of a subsequent owner, the amortization period is the period, if any, remaining at the time of his acquisition in the 60-month period elected under section 124B(b) by the person who originally constructed, reconstructed, or erected the facility.

The amount of the amortization deduction under section 124B(a) is an amount with respect to each month of the amortization period within the taxable year equal to the adjusted basis of the facility at the end of such month divided by the number of months remaining in the period, including the month for which the deduction is to be computed. The adjusted basis of the facility at the end of any month is to be computed without regard to the amortization deduction for such month. The amortization deduction with respect to any month is in lieu of any deduction with respect to the facility for that month provided by section 23(l) of the Code, relating to the allowance for depreciation.

The original owner of a grain storage facility may elect to take the amortization deduction with respect to such facility and to begin the 60-month amortiza-

tion period either with the month following the month in which the facility was completed or with the beginning of the succeeding taxable year. In either event the election is to be made by a statement in the taxpayer's return for the taxable year involved to the effect that the taxpayer elects to take the amortization deduction with respect to the particular facility and to begin the 60-month period at the time designated in the statement. In the case of a subsequent owner the election to take the amortization deduction must be made by a statement to that effect in the return for the taxable year in which the facility was acquired by him. However, under regulations to be prescribed by the Secretary, either an original owner or a subsequent owner may make the election under section 124B(b) prior to the filing of the return.

Any taxpayer, whether the original owner or a subsequent owner of the grain storage facility who has elected under section 124B(b) to claim the amortization deduction with respect to such facility, may, at any time after making the election, discontinue the amortization deduction as to the remainder of the amortization period. Such discontinuance shall become effective as of the beginning of any month, during which the taxpayer holds the facility, which is specified by the taxpayer in a notice in writing filed with the Secretary before the beginning of such month. From the beginning of the month specified for the discontinuance of the amortization deduction the deduction allowable under section 23(l) of the Code shall be allowed, and neither the taxpayer nor any subsequent owner of the grain storage facility shall be entitled to any further amortization deduction with respect to such facility.

Section 124B(d) defines the term "grain storage facility" to mean—

(1) any corncrib, grain bin, or grain elevator, or any similar structure suitable primarily for the storage of grain, which crib, bin, elevator, or structure is intended by the taxpayer, at the time of his election to claim the amortization deduction, to be used for the storage of grain produced by him or, if the election is made by a partnership, by the members thereof, and

(2) any public grain warehouse permanently equipped for receiving, elevating, conditioning, and loading out grain.

The intent referred to in clause (1) above must be present at the time the election is made, whether the election is being made by the original owner or by the subsequent owner.

The definition contained in section 124B(d) does not include any facility unless the construction, reconstruction, or erection of such facility was completed after December 31, 1952, and on or before December 31, 1956. However, if any structure described in clause (1) or (2) above is altered or remodeled so as to increase its capacity for the storage of grain, or if an existing structure not described in clause (1) or (2) above is converted through alteration or remodeling into a structure so described, such alteration or remodeling is to be treated as the "construction" of a grain storage facility, provided such alteration or remodeling was completed after December 31, 1952, and on or before December 31, 1956. The term "grain storage facility" as used in section 124B does not include a facility any part of which constitutes an "emergency facility" within the meaning of section 124A. Nor does "grain storage facility" include any property which is not of a character which is subject to the allowance for depreciation provided in section 23(l). Thus, "grain storage facility" does not include the land on which a structure defined in clause (1) or (2) above is erected.

Section 124B(e) provides for the determination of the adjusted basis of a grain storage facility in the hands of a taxpayer for the purposes of section 124B(a). In determining the adjusted basis of any grain storage facility in the hands of the original owner where the construction, reconstruction, or erection of the facility was begun before January 1, 1953, there is to be included only so much of the amount of the adjusted basis computed without regard to subsection (e) as is properly attributable to construction, reconstruction, or erection after December 31, 1952. In the case of any alteration or remodeling of a structure which alteration or remodeling under section 124B(d) is treated as a construction of a grain storage facility, the adjusted basis of any such facility in the hands of the original owner is to be determined by including only that portion of the adjusted basis of the facility computed without regard to section 124B(e) as is properly attributable to such alteration or remodeling as was completed after December 31, 1952, and on or before December 31, 1956.

If any existing grain storage facility completed after December 31, 1952, is (prior to January 1, 1957) altered or remodeled so as to increase its capacity

for the storage of grain, such remodeling or alteration shall be considered a new and separate grain storage facility, and the expenditures for such remodeling or alteration shall not be applied in adjustment of the basis of the preexisting facility, but a separate basis shall be computed for such remodeling or alteration. Such remodeling or alteration shall also constitute a new and separate "grain storage facility" for the purpose of the election under subsection (b) of section 124B to take the amortization deduction and to begin the 60-month period.

Under the provisions of section 124B(e) the adjusted basis of a grain storage facility for the purpose of computing the amortization deduction may differ from what would otherwise constitute the adjusted basis of such facility, in that the adjusted basis for the purpose of section 124B(a) may be only a portion of the adjusted basis (for determining gain) of the grain storage facility computed for other purposes. Thus, the adjusted basis for the purpose of computing the amortization deduction will be only a portion of the adjusted basis computed under section 113(b) where only a portion of the basis (unadjusted) is attributable to construction, reconstruction, or erection after December 31, 1952. Also, in the case of any alteration or remodeling which is treated under section 124B(d) as the construction of a grain storage facility, the adjusted basis of the facility for the purpose of the amortization deduction will include only that portion of the adjusted basis of the facility, otherwise determined without regard to section 124B(e), as is properly attributable to such alteration or remodeling as was completed after December 31, 1952. In these cases, therefore, it is necessary to determine the unadjusted basis for the grain storage facility from which the adjusted basis for amortization purposes is derived. The adjusted basis of the grain storage facility for amortization purposes is the unadjusted basis for amortization purposes less the adjustment properly applicable thereto. Such adjustments are those specified in section 113(b) of the Code, except that no adjustments are to be taken into account which increase the adjusted basis of the grain storage facility for the purposes of the amortization deduction.

In the case of a subsequent owner of any grain storage facility the adjusted basis of such facility in his hands for the purpose of section 124B(a) shall be determined by including only the smaller of the following amounts: (1) The basis of such facility for the purposes of section 124B in the hands of the transferor, donor, or grantor, adjusted as if such facility in the hands of the taxpayer had a substituted basis within the meaning of section 113(b)(2)(A), or (2) so much of the adjusted basis (for determining gain) of the facility in the hands of the taxpayer, computed without regard to section 124B as is properly attributable to construction, reconstruction, or erection after December 31, 1952.

Likewise, in the case of a subsequent owner of a grain storage facility the adjusted basis of a facility for the purpose of computing the amortization deduction may differ from what would otherwise constitute the adjusted basis of such facility, in that the adjusted basis for the purpose of the amortization deduction may be determined by reference to the unadjusted basis for amortization purposes in the hands of the prior owner less the adjustments properly applicable to such prior owner.

The provisions of section 124B(e) may be illustrated by the following examples:

Example (1). On February 28, 1953, A completes the construction of a grain storage facility as defined in section 124B(d) at a cost of $2,000 for the land and $6,000 for the construction. Only $3,000 of the total cost of the facility is properly attributable to construction after December 31, 1952. A elects to claim the amortization deduction and to begin the 60-month period on March 1, 1953. Under section 124B(e) the adjusted basis of the facility for the purpose of section 124B(a) as of that date is only $3,000, the amount attributable to construction after December 31, 1952. In determining the adjusted basis of the facility as of any subsequent date for the purpose of computing the amortization deduction, the amortization deductions allowable in respect of the period prior to such date must, of course, be taken into account. See section 113(b) of the Code. Thus, the adjusted basis of the facility for the purpose of computing the amount of the amortization deduction allowable for the month of January, 1954, is $2,500 ($3,000 minus $500, the amortization deductions allowable prior to January 1, 1954).

Example (2). A began on January 1, 1953, and completed on June 30, 1953, the construction of a grain storage facility as defined in section 124B(d) at a cost of $5,000 for the land and $30,000 for the construction. A elects to claim

the amortization deduction and to begin the 60-month period on July 1, 1953. On May 1, 1954, A sells the grain storage facility to B for a price of $34,000 of which $6,000 is allocable to the land. B elects to claim the amortization deduction on the basis of the 50 months remaining in the amortization period. B, in determining the adjusted basis of the facility in his hands, must start with the unadjusted basis of the facility in the hands of A ($30,000) and adjust such basis under section 113(b)(1)(B) in respect of amortization claimed by A during his ownership of the facility ($5,000). Since this amount ($25,000) is smaller than the adjusted basis (for determining gain) of the facility in B's hands as of May 1, 1954 ($28,000, that is $34,000 less $6,000 allocable to land), the adjusted basis of the facility for the purpose of section 124B(a) in B's hands as of May 1, 1954, is $25,000. A, therefore, may include only $25,000 in determining the adjusted basis of the facility in his hands as of May 1, 1954, the date of the purchase. The amortization deductions claimed by B must, of course, be applied in reduction of such adjusted basis in determining the adjusted basis of the facility as of any subsequent date for the purpose of his amortization deduction under section 124B(a). The amount by which the purchase price paid by B and allocable to depreciable property ($28,000) exceeds the adjusted basis determined under section 124B(e) for such property ($25,000)—or $3,000—is treated as the adjusted basis (as of May 1, 1954) for the purpose of the depreciation deduction allowable under section 23(l).

As indicated in example (2) above, if the adjusted basis of any grain storage facility computed without regard to section 124B(e) exceeds the adjusted basis of such facility computed under section 124B(e), the deduction provided by section 23(l) shall, despite the provisions of section 124B(a)(3), be allowed with respect to the grain storage facility as if the adjusted basis for the purpose of the section 23(l) deduction were an amount equal to the amount of such excess.

In the case of property held by one person for life with remainder to another person, section 124B(g) provides that the amortization deduction shall be computed as if the life tenant were the absolute owner of the property and provides that such deduction shall be allowed to the life tenant.

Subsection (b) of this section makes certain technical amendments. Paragraph (1) amends section 23(t) of the Code to include the amortization deduction provided in section 124B. Paragraph (2) amends section 172 of the Code to strike out the phrase "of emergency facilities," and thus conforms this section to the amendment made in section 23(t). Paragraph (3) amends section 190 of the Code to provide the same treatment in the case of grain storage facilities owned by a partnership as in the case of emergency facilities of the partnership.

Under subsection (c) the amendments made by subsection (a) and (b) of this section shall apply only with respect to taxable years ending after the date of the enactment of the bill.

SECTION 207. EXCLUSION OF CERTAIN TRANSFERS TAKING EFFECT AT DEATH

Section 811(c)(1)(B) of the Internal Revenue Code provides for the inclusion in the decedent's gross estate for estate tax purposes of certain transfers in which the decedent retained the income interests for life. Under section 7(b) of Public Law 378, Eighty-first Congress, as amended by section 608 of the Revenue Act of 1951, transfers of this type made prior to March 4, 1931, or in some cases prior to June 7, 1932, are not includible under section 811(c)(1)(B) if the decedent died prior to January 1, 1951. Subsection (a) would amend section 811(c)(1) of the Code to exempt from sectin 811(c)(1)(B) transfers made prior to the dates indicated where the decedent died at any time after February 10, 1939.

In the case of *Commissioner* v. *Church* (335 U. S. 632) the Supreme Court held that a transfer in which the decedent retained the income interests until death is includible in the decedent's gross estate as a transfer intended to take effect in possession or enjoyment at or after death. However, section 811(c)(2) of the Code as added by section 7 of Public Law 378 (Eighty-first Cong.) provides that transfers made prior to October 8, 1949, are not subject to tax under section 811(c)(1)(C), applicable to transfers intended to take effect in possession or enjoyment at or after death (even though the decedent has reserved a life estate) unless the decedent has retained a reversionary interest in the transferred property arising by the express terms of the instrument of transfer and exceeding in value 5 percent of the value of the transferred property. Since section 811(c)(2)

is applicable only to estates of decedents dying after February 10, 1939, reserved income transfers made before March 4, 1931, may still be includible under section 811(c) in the estates of decedents dying on or before February 10, 1939, even though the value of the decedent's reversionary interest is less than 5 percent. Subsection (b) of this section of the bill would apply the limitations of section 811(c)(2) to the estate of a decedent dying before February 11, 1939.

Subsection (b) also provides a rule for cases in which the refund or credit of any overpayment resulting from the application of subsection (b) of this section is barred. The rule provides that if refund or credit resulting from the application of subsection (b) is prevented by the operation of the statute of limitiations or by any other law or rule of law and the determination of estate tax liability of the estate of any decedent dying before February 11, 1939, was pending on January 17, 1949, in the Tax Court or any court of competent jurisdiction, or the decision of any such court did not become final until on or after that date, then refund or credit may nevertheless be allowed if claim therefor is filed within 1 year from the date of enactment of this act. A refund is considered as resulting from the application of this subsection if its application removes an offsetting adjustment otherwise preventing a refund or credit.

SECTION 208. FAILURE TO RELINQUISH A POWER IN CERTAIN DISABILITY CASES

Under section 811(d) of the Internal Revenue Code there is required to be included in the gross estate for estate tax purposes certain property transferred in trust by the decedent during his lifetime where the decedent reserved the right to change the trust beneficiaries, but had no power to revest the trust property in himself. Section 208 of the bill would exempt from this particular provision certain trusts of this type where the decedent died after December 31, 1950, and was under a mental disability for a continuous period beginning not less than 3 months prior to December 31, 1947, and ending with his death.

In cases covered by the amendment made by this section, the decedent, if not under a mental disability, could have taken advantage of section 1000(e) of the Internal Revenue Code to release, free of gift tax, the power to change the trust beneficiaries. As a result of such a release the trust property would ordinarily not have been includible in his gross estate under the provisions of section 811(d) of the Code. This section places the grantor of such a trust in the same position for estate tax purposes as he would have been if he had been mentally able to release the described power, and had done so. This section would apply even though a guardian could have released the power for the decedent. The term "mental disability" as used in this amendment means mentally incompetent to make the release, whether or not there was a court adjudication of such incompetence.

SECTION 209. REVERSIONARY INTERESTS IN CASE OF LIFE INSURANCE

This section applies the rules contained in section 404(c) of the Revenue Act of 1942, as amended by section 503(a) of the Revenue Act of 1950, relating to reversionary interests in the case of life insurance, to estates of decedents dying after January 10, 1941, and before October 22, 1942.

Section 404 of the Revenue Act of 1942 generally revised the provisions governing the estate tax treatment of life insurance payable to beneficiaries other than the executor. Under the revised treatment one basis for subjecting such life insurance to estate tax is payment of premiums by the decedent. For this purpose section 404(c) provided that the portion of the proceeds of life insurance policies attributable to premiums paid by the decedent on or before January 10, 1941, shall be excluded if at no time after such date the decedent possessed an incident of ownership in the policies. For this purpose a reversionary interest was treated as an incident of ownership.

However, section 503(a) of the Revenue Act of 1950 amended section 404(c) of the Revenue Act of 1942 by providing that, for the purpose of determining whether the decedent possessed an incident of ownership after January 10, 1941, a reversionary interest was not an incident of ownership unless at some time after that date it exceeded in value 5 percent of the value of the policy and the reversionary interest arose by the express terms of the policy or other instrument and not by operation of law. The amendment made by section 503(a) of the

Revenue Act of 1950 was effective, however, only as to estates of decedents dying after October 21, 1942. This section applies the rules contained in section 404(c) of the Revenue Act of 1942, as amended by section 503(a) of the Revenue Act of 1950, to estates of decedents dying after January 10, 1941, and before October 22, 1942.

Subsection (b) provides that no interest shall be paid in respect of any overpayment resulting from the application of subsection (a) as to any payment made prior to the date of the enactment of this act.

SECTION 210. MARITAL DEDUCTION IN CERTAIN CASES WHERE DECEDENT DIED BEFORE APRIL 3, 1948

Subsection (a) of this section provides for the allowance of a marital deduction under section 812(e)(1)(A) of the Internal Revenue Code in a case where an interest in property passes by will from a decedent, if the surviving spouse is entitled for life to all the income from such property, payable annually or at more frequent intervals, with power in the surviving spouse to use and consume such portion of the property as the surviving spouse may need or desire for her (or his) comfortable support and maintenance, provided that there is no power in any person other than the surviving spouse to appoint any part of such property. This subsection would also apply in a case where the surviving spouse had greater powers than those described in subsection (a) if such greater powers include the specified powers. Under existing law, a marital deduction would not be allowable in a case of this type because of the operation of the terminable interest rule contained in section 812(e)(1)(B) of the Code. It is further provided that nothing in this subsection shall be construed to permit a double deduction for any property.

Under subsection (b), subsection (a) is to apply only if the surviving spouse so elects and in such case the property subject to the power is treated, for both gift and estate tax purposes, as property over which such spouse has a general power of appointment created on the date of the decedent's death and exercisable by deed or will. It is further provided that if the surviving spouse makes the election, the limitation provisions on the assessment and collection of any amount of gift or estate tax resulting from such election shall be extended to include 1 year from the date such election is filed.

Subsection (c) provides that this section shall apply only to estates of decedents dying after December 31, 1947, and on or before the date of the enactment of the Revenue Act of 1948.

SECTION 211. MITIGATION OF EFFECT OF STATUTE OF LIMITATIONS

Section 211 of the bill adds new paragraphs (6) and (7) to section 3801(b) of the Code, relating to circumstances of adjustment, and amends the second sentence of section 3801(b). Paragraph (6) permits an adjustment, when a deduction or credit is disallowed, of tax liability within the additional period of time provided by section 3801(c) in cases where (1) a related taxpayer was entitled to the deduction or credit or (2) the taxpayer was entitled to the deduction or credit for a different taxable year, if, at the time the deduction or credit was incorrectly claimed, credit or refund for the correct year or to the related taxpayer was not barred. Paragraph (7) provides similar rules where the Secretary included an income item in the incorrect taxable year or included an income item in the income of the wrong taxpayer of a related taxpayer group. The amendment to the second sentence of section 3801(b) excepts cases described in paragraphs (6) and (7) from the requirement that the adjustment be made only in cases where the other party has maintained an inconsistent position, since cases described in paragraphs (6) and (7) are not attributable to the maintenance of an inconsistent position by the other party to the dispute. The new paragraphs (6) and (7) apply only where the determination became final on or after July 1, 1952.

Subsection (c) of section 211 provides that in any case in which the determination became final before the enactment of this bill, the 1-year period in section 3801(c) for the making of the adjustment is extended to include the period of 1 year from the date of enactment of the bill.

AMENDING THE INTERNAL REVENUE CODE TO EXTEND THE TIME DURING WHICH CERTAIN PROVISIONS RELATING TO INCOME AND ESTATE TAXES SHALL APPLY

[Senate Report No. 685, Eighty-third Congress, First Session Calendar No. 682]

[July 28 (legislative day, July 27), 1953]

Mr. Millikin, from the Committee on Finance, submitted the following report [to accompany H. R. 6426]:

The Committee on Finance, to whom was referred the bill (H. R. 6426) to amend the Internal Revenue Code to extend the time during which certain provisions relating to income and estate taxes shall apply, and for other purposes, having considered the same, report favorably thereon with amendments and recommend that the bill as amended do pass.

The amendments are as follows:

Section 204(a) is amended by striking out lines 17 through 25, inclusive, on page 10 and lines 1 through 8, inclusive, on page 11 and inserting in lieu thereof the following:

(a) AMENDMENT OF SECTION 116(a)(2).—Section 116(a)(2) (relating to exclusion from gross income of earned income from sources without the United States) is hereby amended by adding at the end thereof the following new sentences: If the 18-month period includes the entire taxable year, the amount excluded under this paragraph for such taxable year shall not exceed $20,000. If the 18-month period does not include the entire taxable year, the amount excluded under this paragraph for such taxable year shall not exceed an amount which bears the same ratio to $20,000 as the number of days in the part of the taxable year within the 18-month period bears to the total number of days in such year.

Page 12, line 1, strike out "April 14, 1953" and insert:

December 31, 1952, but only to such amounts as are received on or after January 1, 1953.

Page 29, line 11, strike out "July" and insert in lieu thereof "June" and on page 30, line 1, strike out "July" and insert "June."

I. GENERAL STATEMENT

H. R. 6426 contains 17 sections dealing with amendments to the Internal Revenue Code. Six of the sections extend the period during which certain provisions of the Code will apply. The other 11 sections relate to amendments to the Internal Revenue Code providing for removal of inequities in income and estate tax cases. Your committee believes that it is important to take care of these inequities ahead of the general revision bill which will be considered next year.

II. EXPLANATION OF THE BILL

A. EXTENSION PROVISIONS

Section 101. Election as to recognition of gain in certain corporate liquidations.

This section extends to 1953 the provisions of section 112(b)(7) of the Internal Revenue Code dealing with the nonrecognition of gain in certain corporate liquidations. This provision which applied to certain liquidations in a single calendar month in 1951 was extended by the Revenue Act of 1951 to such liquidations in 1952 and is further extended by this bill to such liquidations occurring in a single calendar month in 1953. Your committee believes that such an extension for 1 year is desirable to enable those who were unable to arrange for liquidation within the requisite period in 1951 or 1952 to have the benefits of this provision if they can complete such liquidations in a single calendar month in 1953.

Section 102. Extension of time for elections under Public Law 539 overruling Virginian Hotel case.

In Public Law 539, approved July 14, 1952, Congress overruled the decision of the Supreme Court in the Virginian Hotel case. Under that decision a taxpayer who deducted depreciation for any year in excess of the amount allowable for

such year was nevertheless required to reduce the basis of his property by the entire amount of depreciation allowed, even though he had received no tax benefit from claiming such excessive depreciation as a deduction. Under Public Law 539, the basis of the property was not required to be reduced by such excessive depreciation unless the taxpayer had received a tax benefit for taking a deduction for such excessive amount. The taxpayer was granted under the law an election (under such regulations as the Secretary prescribed) to apply this new treatment retroactively to the period since February 28, 1913, and before January 1, 1952, but no election could be made after December 31, 1952. The Treasury regulations under the law were not promulgated until December 30, 1952. Thus taxpayers were not given sufficient time to determine whether such an election would be beneficial to them. Your committee therefore deems it desirable to extend through December 31, 1954, the time within which an election may be made. Since Public Law 539 provides that an election once made is irrevocable, the bill, in order to provide uniform treatment, permits taxpayers to revoke within the extended period elections made prior to January 1, 1953.

Section 103. Extension of time for making election with respect to war loss recoveries.

Section 341 of the Revenue Act of 1951 sets forth a new method for treatment of war losses under section 127 of the Internal Revenue Code. It provides that at the election of the taxpayer (under such regulations as the Secretary may prescribe) the tax for the year in which the deduction for the war loss was taken is to be recomputed by reducing the deduction by the amount of the recovered property taken at its depreciated cost on the date of the loss or at its fair market value on the date of recovery, whichever is lower. The resulting increase in tax for the year of the loss, if any, is added to the tax for the year of recovery. The time for electing the benefit of this provision expired on December 31, 1952. Since the Treasury regulations interpreting this section of the law were not promulgated until December 30, 1952, taxpayers did not have sufficient time to determine whether it was advantageous to make such an election. The bill extends the period for making such an election through December 31, 1953.

Section 104. Extension of period of abatement of income taxes of deceased members of Armed Forces.

Section 154 of the Internal Revenue Code provides in the case of an individual who died after June 24, 1950, and prior to January 1, 1954, as a result of active service in a combat zone as a member of the Armed Forces, an abatement of income tax liability which was outstanding at the date of his death. It also provides a forgiveness of the tax with respect to the taxable year in which falls the date of his death or with respect to any prior taxable year ending on or after the first day he so served in a combat zone after June 24, 1950. The bill extends the period to which this section is applicable for 1 additional year so as to include the calendar year 1954.

Section 105. Extension of temporary provisions relating to life insurance companies.

The present temporary provisions for the taxation of life insurance companies are extended for 1 year by this section of the bill. Pending the results of studies being made by the staffs of the Treasury and the Joint Committee on Internal Revenue Taxation, your committee deems it advisable to continue for 1 year the provisions of present law.

Section 106. Extension of period for exemption from additional estate tax of deceased members of Armed Forces.

Section 939(b) of the Internal Revenue Code exempts from the additional estate tax estates of decedents dying after June 24, 1950, and before January 1, 1954, while in active service as members of the Armed Forces of the United States, where such decedents were killed in action while serving in a combat zone or died from wounds, disease, or injury incurred while so serving in line of duty and by reason of a hazard to which they were subjected as an incident of such service. The bill extends the application of this section to January 1, 1955.

B. MISCELLANEOUS

Section 201. Venue of action for violation of State cigarette tax laws.

The act of October 19, 1949, provided that persons, other than distributors, who sell or dispose of cigarettes in interstate commerce must forward to the tobacco tax administrators of States to which shipments are made monthly reports setting forth the names and addresses of the persons to whom shipments are made and the brand and quanity of cigarettes so shipped. Some courts have held that under the statute violations of the act are committed at the place from which the cigarettes are shipped, since the act only requires the shippers to forward their reports. The bill requires the actual filing of the reports with the State tobacco administrator. This would have the effect of assuring, in the event of an offense committed under the act, that the venue of the action would be in the district in which the State tobacco administrator has his office.

Section 202. Deduction of certain unpaid expenses and interest

In the case of certain closely related taxpayers, such as a corporation and a shareholder owning more than 50 percent of the corporation's stock, section 24(c) of the Code operates to disallow deduction of certain expenses and interest if the following conditions are met:

(1) The amount is not paid within the taxable year or within 2½ months after the close thereof; and

(2) Under the recipient's method of accounting the amount is not, unless paid, includible in his income in the taxable year in which, or with which, the taxable year of the payor corporation ends.

This provision is intended to insure that transactions between such related taxpayers do not operate to shift items of income or deductions. A situation has been called to the attention of your committee, however, where section 24(c) may work an undue hardship. For example, a recipient on the cash basis may have an amount credited to his account and made available to him by the corporate payor within 2½ months after the close of the payor's taxable year so that the recipient must include it in income as an item constructively received in the taxable year so credited. If, however, the corporate taxpayer fails actually to pay over such amount within the period of 2½ months, the item will not be allowed to the corporation as a deduction. Your committee believes that such a case should not fall within the ban of section 24(c) and the bill so provides by an appropriate amendment of requirement (1) above.

The provision is applicable to taxable years of the payor beginning after December 31, 1950, but under certain conditions, set forth to insure that payments will be properly accounted for taxwise with respect to both parties, the payor may elect to make this amendment applicable to taxable years beginning after December 31, 1945, and before January 1, 1951.

Section 203. Income tax basis of property transferred in trust.

Section 113(a)(5) of existing law contains a provision to the effect that where the grantor retains the income from property in trust for his life with power to revoke the trust, the basis of the property in the hands of the persons entitled to take the property under the terms of the trust instrument after the grantor's death shall, after such death, be the same as if the property had passed under a will executed on the day of the grantor's death. This results in the basis of the property in the hands of the recipients being its fair market value at the date of the grantor's death or, at the election of the executor, the value 1 year from the date of death. Your committee believes that this same rule should apply to situations where the grantor with a reserved life estate has the power to make any change in the enjoyment of the corpus of the trust through the power to alter, amend, or terminate the trust. In both cases, the trust property is required to be included in the gross estate of the grantor for estate tax purposes. The amendment applies only to grantors dying after December 31, 1951, and only with respect to taxable years ending after December 31, 1951.

Section 204. Earned income from sources without the United States.

Your committee deems it advisable to amend section 116(a)(2) of the Internal Revenue Code, effective as to amounts received after December 31, 1952. Section 116(a)(2) excludes from income in the case of a citizen of the United States income earned abroad if such citizen was present in a foreign country or countries for a period of 17 out of 18 consecutive months. While this paragraph was designed to encourage men with technical knowledge to go abroad in order

to complete specific projects, it has been subject to a great deal of abuse. Some individuals with large earnings have seized upon the provision as an inducement to go abroad to perform services, which were customarily performed at home, for the primary purpose of avoiding the Federal income taxes. It has also been ascertained that in many cases Americans taking advantage of this provision do not pay any income tax even to the foreign country or countries in which the income is earned. This is because they are not in any particular foreign country long enough to establish a residence or because the foreign country in question does not impose any income tax. Under the House bill, section 116(a)(2) of the Internal Revenue Code is repealed effective as of April 15, 1953. Under your committee amendment, section 116(a)(2) is retained but is limited to $20,000 of earned income if the taxpayer is abroad for the full taxable year or to a portion thereof if the taxpayer is abroad for less than the full taxable year. While the committee amendment applies to taxable years ending after December 31, 1952, it will cover only such amounts as are received on or after January 1, 1953. Your committee believes that an outright repeal of section 116(a)(2) is not necessary to correct the reported abuses under existing law. There are many legitimate business arrangements which necessitate sending technical personnel abroad. A limitation on the amount of the earned income from foreign sources which is exempt will, in the opinion of your committee, be sufficient to correct the evils which have been brought to its attention. The bill will not affect the liability of any employer to deduct and withhold the tax on remuneration paid before the first day of the first month beginning more than 10 days after the date of the enactment of this bill. For the purpose of this provision, if an individual travels from one place in a foreign country to another place in the same country, or to a place in another foreign country and if such travel extends over a period of less than 24 hours and does not involve travel within the United States or any possession thereof, such individual shall not be deemed outside a foreign country during the period of such travel.

Section 205. Net operating loss deductions.

The bill includes provisions designed to eliminate disparities in the treatment of taxpayers in respect to the taxable years to which a net operating loss may be carried forward. Under these provisions the number of years to which a net operating loss may be carried forward by certain corporations reporting income on the basis of a fiscal year has been extended. Under the cutoff dates in existing law these corporations are limited in the use of their net operating losses. For example, under existing law, if a corporation has a taxable year beginning on December 1, 1947, a net operating loss developed in that year may only be carried forward to the 2 succeeding taxable years whereas if the taxable year had begun on January 1, 1948, such may be available to offset gains of the 3 succeeding taxable years.

It is provided that in the case of a corporation, other than a corporation which commenced business after December 31, 1945, which has a net operating loss for a taxable year beginning in 1947 and ending in 1948 (so that the taxable year overlaps the critical dates) such a corporation may utilize such loss in the third succeeding taxable year. The amount of such carryover to the third year cannot exceed an amount which bears the same ratio to the net operating loss as the number of days in the loss year falling after December 31, 1947, is of the total number of days in the loss year.

In the case of a corporation the first taxable year of which began in 1949 and ended in 1950, a comparable extension is provided. Such corporations are put on a basis similar to that provided for corporations with net operating losses for taxable years beginning after 1949, that is, the net operating loss may be available for the 5 succeeding taxable years. However, the bill subjects the amount of the carryover to the fourth and fifth succeeding taxable years to a general limitation to such part of the net operating loss as is properly allocable to 1950.

The bill adds a provision amending section 1 of the act of July 15, 1947 (61 Stat. 324). This act allowed a carryforward of the net operating loss of a predecessor railroad corporation to a successor railroad corporation. Since the reorganization may have caused a short taxable year of the predecessor and of the successor to fall within one 12-month period, such corporations would, in effect, be denied the full 2-year carryforward available to other corporations, the act allowed a carryover for 3 taxable years in such cases. Section 330(b) of the Revenue Act of 1951 added section 122(b)(2)(C) to the Code which provided, in the case of all corporations, for a 3-year carryforward of a net operating loss incurred for

any taxable year beginning after December 31, 1947, and before January 1, 1950. Accordingly the bill would allow a successor railroad corporation a 4-year carryover in order to continue the prior treatment under the act of July 15, 1947.

Section 206. Amortization deduction for grain storage facilities.

A critical shortage of facilities for storing grain has developed throughout the Nation during the past several years. This shortage has been felt particularly by producers of such grains as wheat and corn. In view of the situation which has arisen, it is believed necessary to provide an inducement for taxpayers to construct new grain storage facilities, to increase the capacity of those already in existence, or to adapt existing construction to the storage of grain.

Under existing law, a taxpayer undertaking such expenditures would be allowed to recover his costs only through a deduction for depreciation taken over the period of the useful life of such new construction or adaptation. The bill adds section 124B to the Code to allow such costs in the case of construction or adaptation after December 31, 1952, and before January 1, 1957, to be deducted, at the taxpayer's election, over the period of 60 months beginning either with the month following the month in which the facility was completed, or with the succeeding taxable year. In the event that the shortage of facilities for storing grain remains in a critical state through 1956, it would be appropriate to extend the date within which a taxpayer may construct such facilities and receive the benefits of this provision. The deduction is available only with respect to taxable years ending after the date of the enactment of this act. In the case of new construction the deduction is only available with respect to so much of the cost as is attributable to construction after December 31, 1952, and in the case of the alteration or adaptation of existing buildings only such cost as is properly attributable thereto after such date may be so deducted.

This amortization deduction is in lieu of that allowed for depreciation, but a taxpayer is allowed to deduct ordinary depreciation for that part of his costs of construction which would not qualify under this section, for example, by reason of not having been incurred subsequent to December 31, 1952. A taxpayer may elect to discontinue his amortization deductions under this section as of the beginning of any month specified in a notice filed with the Secretary before the beginning of such month and may thereafter be allowed the depreciation deduction. In the case of property held by one person for life with remainder to another, the life tenant is allowed the deduction under this section as if he were the absolute owner. Special rules are provided to allow the benefits of this deduction to a person acquiring a grain storage facility to which this section is applicable. These rules are discussed in the technical part of this report relating to this provision.

This special amortization deduction is available to a farmer constructing a grain storage facility. The statute defines a grain storage facility as a corncrib, grain bin, or grain elevator, or any similar structure primarily suited for the storage of grain, which is intended by the taxpayer at the time of his election to be used for the storage of grain produced by him. The deduction is also available to any person who constructs any public grain warehouse permanently equipped for handling grain. Under the definition of a grain storage facility the special amortization deduction is not allowed to persons who store only grain purchased for consumption in their business. For example, persons engaged in the milling of flour who construct storage facilities for purchased grain used in such processing would not be allowed to deduct the cost of any facilities under this provision.

Section 207. Exclusion of certain transfers taking effect at death.

The bill amends the estate tax provisions of the Code relating to certain transfers of property with retention of the income for life by the transferor. In 1930 the Supreme Court held that property so transferred should not be included in the taxable estate of the transferor. *May* v. *Heiner* (281 U. S. 238). In response to this and related decisions, on March 3, 1931, Congress adopted a joint resolution providing that such transfers were includible (46 Stat. 1516), and the Revenue Act of 1932 substantially reenacted the provisions of this joint resolution. The joint resolution was interpreted in 1938 as being only prospective in its operation so as not to apply the transfers made prior to the date of its adoption. *Hassett* v. *Welch* (303 U. S. 303).

In the face of what had long been regarded as the settled interpretation of the then existing estate tax provisions relating to these pre-1931 transfers with retention of a life estate by the transferor, the Supreme Court in 1949 in effect

overruled its two earlier decisions and held that a transfer of property in 1924, with income retained for life by the transferor, required that the transferred property be included in the taxable estate of the transferor who died in 1939. *Commissioner* v. *Church* (335 U. S. 632).

Following the Church decision the Technical Changes Act of 1949 (as amended) provided that, in the case of life estates retained in transfers made on or before March 3, 1931 (and in some cases before June 7, 1932), the property would not be included in the decedent's gross estate solely by reason of retention of the life estate if the decedent died after the enactment of the Code on February 10, 1939, and prior to January 1, 1951. As that act was passed by the Senate, it contained provisions which would have restored the estate tax law to what it was prior to the Church opinion, that is, pre-1931 transfers would not be included in the gross estate of the decedent merely by reason of the retention of a life estate, regardless of when the decedent died. This provision was limited in conference, however, in the manner described above.

It is believed that the effect of the Church decision should be eliminated in all cases to which it was applicable. Prior legislation has already restored the estate tax law to what it was before the Church decision in respect to all decedents dying after the enactment of the Code and prior to January 1, 1951. The provision in the bill accomplishes this same result in respect to decedents dying on or after January 1, 1951.

The bill also provides relief for certain decedents where the death occurred prior to February 11, 1939, and whose estates were burdened with estate tax by reason of transfers made before March 4, 1931, involving the retention of a life estate. the reservation of a minute reversionary interest, or both. Since property transferred in this manner would not be included in the gross estate if the decedent died after February 10, 1939 (and before 1951), the bill would achieve a similar exemption for estates of decedents dying prior thereto. However, it is not felt necessary to open the statute of limitations to any great extent in cases of decedents dying prior to February 11, 1939. It is only in cases in litigation at the time of the Church decision where there would appear to be any undue hardship. In these cases a refund or credit resulting from this provision will be allowed if a claim is filed within 1 year from the date of enactment of this act.

Section 208. Failure to relinquish a power in certain disability cases.

Grantors of discretionary trusts created prior to January 1, 1939, who had retained certain powers which would result in the inclusion of the trust property in their gross estate for estate tax purposes were, under section 1000(e) of the Code, permitted to relinquish such powers on or after January 1, 1940, and on or before December 31, 1947, free of gift tax. Grantors who were unable to relinquish their discretionary powers within the above period because of a mental disability should not be penalized. It is therefore provided that there shall not be included in a decedent's estate property previously transferred in trust as to which he retained certain discretionary powers if such decedent for at least 3 months prior to December 31, 1947, and continuing to the date of his death was under a mental disability such that he could not have relinquished such powers free of gift tax pursuant to section 1000(e). The term "mental disability" is intended to encompass those cases in which the decedent during the requisite period prior to his death was, in fact, incapable because of his mental condition of relinquishing the power. whether or not he was legally declared mentally incompetent during all or any part of such period.

Section 209. Reversionary interests in case of life insurance.

Section 404(c) of the Revenue Act of 1942 (as amended by sec. 503(a) of the Revenue Act of 1950) provided in the case of decedents dying after the date of its enactment (October 21, 1942) that the proceeds of life insurance policies should not be included in the decedent's estate by reason of premiums paid by the decedent prior to January 10, 1941, if the decedent at no time after that date retained an incident of ownership in such policy. In determining whether the decedent had such an "incident of ownership" after January 10, 1941, there was to be taken into account only those reversionary interests exceeding 5 percent of the value of the policy and arising other than by operation of law. It is believed that similar treatment should be extended in the case of decedents dying after January 10, 1941, and before October 22, 1942. Such decedents will be deemed to have an incident of ownership in insurance policies by reason of a reversionary interest held after January 10, 1941, only if such reversionary

interest exceeded 5 percent of the value of the policy and arose by the express terms of the policy or other instrument and not by operation of law.

Section 210. Marital deduction in certain cases where decedent died before April 3, 1948.

The provisions of this section relate to the marital deduction for estate tax purposes. Attention has been called to certain situations where a decedent died after December 31, 1947, but prior to the date of the enactment of the Revenue Act of 1948, which allowed a marital deduction for estate tax purposes. Consequently, while the act applied to such cases, estates of decedents dying within this short period from January 1, 1948, to the date of its enactment on April 2, 1948, were unable to secure the benefit of its provisions in some cases because the will of the decedent was not in accord with certain technical requirements of the act. If the decedent had been alive after the enactment of the Revenue Act of 1948, his will would undoubtedly have been rewritten to conform to the provisions of the act. Thus, under the act, property subject to a power of appointment in order to be taken into account for purposes of the marital deduction must meet the requirements of section 812(e)(1)(F) of the Internal Revenue Code. This section requires the interest in property passing from the decedent under a power of appointment to be in trust and the power to be unlimited and exercisable by the surviving spouse at all events. Cases have arisen where the power granted to the surviving spouse was not in trust and was confined to a power in the surviving spouse to use and consume such portion of the property as the surviving spouse may need or desire for her (or his) comfortable support or maintenance. In the case of a decedent dying after December 31, 1947, and prior to April 3, 1948, a power of this broad application should be considered as sufficient to permit the marital deduction of property subject to such power and the bill so provides. The section is only applicable if the surviving spouse files with the Secretary of the Treasury within 1 year after the date of the enactment of this act an election to take the benefits of the section. If such an election is made the property subject to such power shall be considered as property as to which the surviving spouse had a general power of appointment created on the date of the decedent's death, exercisable by deed or by will. Thus a relinquishment of such power by the surviving spouse during her lifetime will result in a taxable gift and if such power is not relinquished during the lifetime of the surviving spouse, the property subject to such power will be considered as part of the estate of such surviving spouse for estate tax purposes.

Section 211. Mitigation of effect of statute of limitations.

Section 3801 of the Code allows either the taxpayer or the Commissioner to correct an improper tax result in certain cases where such action would otherwise be prevented by the running of the statute of limitations. This is possible by reason of the allowance under that section of an additional period of time beyond the period of limitations which would ordinarily be applicable. One of the principles of the present statute is to preclude any adjustment unless the hardship results from the maintenance of an inconsistent position by either the taxpayer or the Commissioner.

The statute operates effectively in cases to which it is directed, but tax inequities, the correction of which is prevented by the running of the period of limitations, may exist without regard to whether or not the position maintained by either party is inconsistent. A taxpayer may be disallowed a deduction or credit to which he is entitled in another taxable year or to which a related taxpayer may be entitled. Similarly, the Commissioner may have included an item in income for a taxable year different from the year for which such item should have been included, or the Commissioner may have included the item in the income of a related taxpayer.

Under present law, the errors described may not be corrected if discovered after the expiration of the period of limitation in respect to the correct year of the taxpayer or of the proper taxpayer. The bill includes provisions amending section 3801 in order to open the statute of limitations in such cases. Where a taxpayer claims a deduction or credit for a taxable year which is later determined to be the incorrect taxable year, or which is determined properly to belong to a related taxpayer, the amendment would permit a proper adjustment. However, the taxpayer is entitled to the benefis of this provision only if a credit or refund of the overpayment attributable to the deduction or credit for the correct year or to the related taxpayer was not barred at the time the taxpayer formally asserted that he should have received such credit or refund in the year disallowed.

Similarly, the Commissioner would be allowed to make assessment of tax with respect to the proper taxable year, if at the time he formally asserted that an item was includible in income for a taxable year, lated determined to be the incorrect year, he could have made a proper assessment of tax for the correct year. An opportunity to make a proper assessment would also be extended to the Commissioner under similar circumstances in the case of the related taxpayer.

The provisions added by the bill apply only where the determination relating to the disallowance of the deduction or credit, or the exclusion of the items from gross income, as the case may be, became final after June 30, 1952. Under your committee's bill the provision will not apply if the determination became final prior to June 1, 1952.

In the opinion of the committee it is necessary to dispense with the requirements of subsection 4 of rule XXIX of the Standing Rules of the Senate to expedite the business of the Senate.

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